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An Antitrust Narcotic: How the Rule of Reason Is Lulling Vertical Enforcement to Sleep

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AN ANTITRUST NARCOTIC:
HOW THE RULE OF REASON IS LULLING VERTICAL ENFORCEMENT TO SLEEP

*Nicole McGuire**

Over time, the Supreme Court has adopted a laissez faire attitude toward antitrust enforcement, which now threatens to end vertical enforcement altogether. Since the inception of the Sherman Act, the Court has limited the application of Section 1 to only those contracts that endorse unreasonable restraints on trade. In doing so, the Court voiced a preference for using the defendant-friendly rule of reason over the strict per se standard when determining reasonableness. Then in 2007, the Court took the final step in relaxing vertical enforcement by mandating that courts evaluate all vertical restraints under the rule of reason. Regrettably, the rule of reason often amounts to per se nonliability in practice, thereby frustrating the very objectives that the Sherman Act was enacted to protect. This Article argues that the Court, through its leniency toward vertical enforcement and its failure to provide sufficient guidance about how to apply the rule of reason, has endorsed per se legality for all vertical restraints. It then proposes that in order to resume an optimal level of enforcement, the rule of reason should be replaced by a rebuttable presumption of illegality.

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"Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone." Judge Learned Hand[1]

I. INTRODUCTION

Promoting competition and implementing a free-market system are generally accepted in the United States as the best ways to allocate resources and eliminate economic waste.[2] The U.S. Supreme Court has even gone so far as to say that competition in the free market "provid[es] an environment conducive to the preservation of our democratic political and social institutions."[3] Simultaneously, the government has always been concerned with too much centralized economic power, monopolies in particular,[4] fearing that efficiency and consumer welfare are sacrificed when private businesses are allowed to operate, unregulated, in the free market.[5] To prevent excessive centralized power, the government has developed protections in the form of antitrust laws. The primary purpose of U.S. antitrust laws is to eliminate conduct that could prove detrimental to competition, consumers, and the free market.[6] However, effective antitrust laws must strike a balance between favoring a competitive,

1. United States v. Aluminum Co. of Am., 148 F.2d 416, 427 (2d Cir. 1945).

2. N. Pac. Ry. Co. v. United States, 356 U.S. 1, 4 (1958) ("[T]he unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress . . . ."); ROBERT PITOFSKY ET AL., TRADE REGULATION 2 (Robert C. Clark et al. eds., 6th ed. 2010).

3. *N. Pac. Ry.*, 356 U.S. at 4.

4. PITOFSKY ET AL., *supra* note 2, at 1; *see also* Christopher S. Kelly, Leegin Creative Leather Products, Inc. v. PSKS, Inc.*: The Final Blow to the Use of the Per Se Rules in Judging Vertical Restraints—Why the Court Got It Wrong*, 28 N. ILL. U. L. REV. 593, 595 (2008) ("By the late nineteenth century, . . . [i]t was feared that if economic power was concentrated in the hands of a select few, additional concentration of market power would naturally occur, and would result in trusts that would use their power to oppress individuals and injure the public.").

5. PITOFSKY ET AL., *supra* note 2, at 2.

6. *See* Nat'l Soc'y of Prof'l Eng'rs v. United States, 435 U.S. 679, 695 (1978) (quoting Standard Oil Co. v. Fed. Trade Comm'n, 340 U.S. 231, 248 (1951)) ("The Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services. 'The heart of our national economic policy long has been faith in the value of competition.'").

free market economy and eliminating the excessive power that such an economy has the potential to generate.

When Congress created antitrust enforcement by passing Section 1 of the Sherman Act, it recognized the importance of maintaining this balance by stating that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal."[7] The Supreme Court has since limited the scope of the Sherman Act by declaring that Section 1 should not be interpreted so broadly as to apply to all contracts, but instead should apply to only those that impose *unreasonable* restraints on trade.[8] In light of this interpretation, the Court has repeatedly stated that courts should favor the "rule of reason" when determining the reasonableness, and thereby the legality, of a restraint.[9] The rule of reason enables the fact-finder to consider all of the circumstances surrounding a restraint, including its procompetitive justifications.[10] In this way, the standard is supposed to assist the fact-finder in deciding whether a particular restraint is in fact unreasonable in violation of Section 1.[11]

Particularly, the Court has emphasized the use of the rule of reason in cases where the adverse economic impact of a specific restraint is not obvious because the rule allows courts to scrutinize that impact to determine whether the restraint actually stifles competition.[12] The Court departs from the rule of reason approach in favor of a per se standard only when it faces a class of restraints that has the tendency to always, or almost always, decrease competition or output.[13] The per se standard requires no investigation into the nature and impact of a restraint; instead the restraint is declared illegal at the outset.[14]

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7. 15 U.S.C. § 1 (2006).

8. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 885 (2007) (quoting State Oil Co. v. Khan, 522 U.S. 3, 10 (1997)).

9. *Id.* at 885–86.

10. Maurice E. Stucke, *Does the Rule of Reason Violate the Rule of Law?*, 42 U.C. DAVIS L. REV. 1375, 1379 (2009).

11. *Id.*

12. *See Leegin*, 551 U.S. at 885–86.

13. *Id.* at 886 (quoting Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 723 (1988)).

14. Mark A. Lemley & Christopher R. Leslie, *Categorical Analysis in Antitrust Jurisprudence*, 93 IOWA L. REV. 1207, 1214 (2008); Stucke, *supra* note 10, at 1378–79; *see also infra* Part II.C.1 (discussing the mechanics of the per se rule).

Nevertheless, even after it declared a particular class of restraints to be per se illegal, the Court has maintained that it reserves the freedom to change the appropriate standard to the rule of reason in any subsequent decision where economic and practical realities justify the switch.[15] The Court has demonstrated its freedom to change the standard of analysis throughout the evolution of antitrust enforcement in what has been referred to as a "pattern of reflexive condemnations."[16] Whenever a state-of-the-art business practice emerges, and its competitive impact is not yet understood, courts immediately assume that the practice is contrary to competitive ideals and condemn it as per se illegal. Then, when the underlying efficiency explanations prove to be adequate justifications for the practice, courts ditch the per se standard in favor of the rule of reason.[17] The impact of this pattern is a tendency toward false positives—findings of illegal conduct when there has been no actual harm to competition.[18] Only after extensive economic analysis of the procompetitive justifications is the practice eventually evaluated according to the rule of reason.[19]

Despite this self-proclaimed grant of power to change the standard of analysis, the Court has never identified a standard other than the per se rule and the rule of reason.[20] There is, of course, the "quick look" rule of reason, which shifts the initial burden of proof from the plaintiff, who no longer has to define the proper market, to the defendant, who must demonstrate the procompetitive benefits of the restraint.[21] However, the quick-look approach has been criticized as a pared down version of the rule of reason, offering no novelty or clarity to the analysis.[22] In fact, courts often choose to defer to a full

15. *Leegin*, 551 U.S. at 899–900; *see also* State Oil Co. v. Khan, 522 U.S. 3, 20–21 (1997) (quoting Payne v. Tennessee, 501 U.S. 808, 828 (1991)) (internal quotation marks omitted) (stating that stare decisis "is not an inexorable command" and that when "the theoretical underpinnings of [earlier] decisions are called into serious question" because of changes in economic circumstances and increased experience evaluating the relevant circumstances, the Court should reconsider "its decisions construing the Sherman Act").

16. Joshua D. Wright, *Antitrust, Economics and Innovation in the Obama Administration*, GCP: THE ANTITRUST CHRON., Nov. 2009, at 2, *available at* http://www.techpolicyinstitute.org/files/wright-nov09.pdf.

17. *Id.*

18. *Id.*

19. *Id.*

20. *See* Stucke, *supra* note 10, at 1408–09.

21. *Id.* at 1410.

22. *See id.* at 1411–15.

rule of reason analysis instead of utilizing the quick-look approach.[23] In essence, the quick-look approach is no longer a distinct standard but rather has become a shortcut for a full rule of reason analysis.[24]

Inexorably, the Supreme Court has not entertained a new standard of analysis or elaborated on how to accurately apply the rule of reason; instead it has flip-flopped between the per se standard and the rule of reason.[25] Unfortunately, this approach does nothing to resolve the problems imposed by the standards as they currently exist, and it has only increased uncertainty in the law.[26] By continuously failing to clarify the rule of reason or to implement a new, clearer standard, the Court seems to be hoping that the lower courts will miraculously generate an accurate and workable standard from the vague rule of reason it created.[27] This is particularly unsettling because the rule of reason is often criticized for being, in application, "little more than a euphemism for nonliability."[28] Nonliability can frustrate antitrust objectives because as enforcement wanes, businesses are permitted to act, unchecked, in their own self-interest.[29] As a result, competition is likely to suffer and, inevitably, consumers are forced to pay higher prices.[30]

This Article argues that the Supreme Court is dangerously close to rendering vertical restraints legal per se. This approach to per se legality is largely due to the Supreme Court's mandate in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*,[31]which required courts to apply the rule of reason in all vertical-restraint cases but provided no clear guidance about how to apply the rule. Three factors contribute to vertical restraints' succumbing to per se legality: (1)

23. *Id.* at 1413–15.

24. Lemley & Leslie, *supra* note 14, at 1219. Indeed, the quick look rule of reason never quite caught on in the context of vertical restraints and has since lost its traction as a favorable standard for other types of restraints as well. Stucke, *supra* note 10, at 1413.

25. *See* Stucke, *supra* note 10, at 1408–09.

26. Jordan A. Dresnick & Thomas A. Tucker Ronzetti, *Vertical Price Agreements in the Wake of* Leegin v. PSKS*: Where Do We Stand Now?*, 64 U. MIAMI L. REV. 229, 249–50 (2009) (explaining how the Court's failure to elaborate on the proper application of the rule of reason in *Leegin* will lead to uncertainty in the lower court's application of the rule).

27. Stucke, *supra* note 10, at 1490.

28. Richard A. Posner, *The Rule of Reason and the Economic Approach: Reflections on the* Sylvania *Decision*, 45 U. CHI. L. REV. 1, 14 (1977).

29. Pamela Jones Harbour, *Vertical Restraints: Federal and State Enforcement of Vertical Issues*, ALI-ABA COURSE OF STUDY: PRODUCT DISTRIBUTION AND MARKETING, Mar. 17–19, 2005, at 3–4, *available at* http://www.ftc.gov/speeches/harbour/050329vertical.pdf.

30. *Id.*

31. 551 U.S. 877 (2007).

when courts apply *Leegin* in conjunction with *Bell Atlantic Corp. v. Twombly*,[32] plaintiffs are rarely able to survive the pleading stages; (2) courts are reluctant to acknowledge when vertical restraints are being used as a guise for horizontal conduct unless the horizontal collusion is obvious; and (3) the lower courts are not able to perform reliable economic analyses of vertical restraints using the rule of reason under the current *modus operandi*. This Article contends that because these factors rarely have led the lower courts to find that a plaintiff has successfully alleged a violation of Section 1, these factors have, in effect, caused vertical restraints to come closer to per se legality than ever.

Ultimately, this Article proposes adopting a rebuttable-presumption-of-illegality standard for evaluating all vertical restraints on trade. This standard would garner more success for plaintiffs while preserving the Court's desire to consider the economic justifications for imposing restraints. While courts might consider this to be a dramatic shift from the current standard, the Court's shift to the rule of reason has spurred the desertion of vertical enforcement. Thus, in order to prevent a de facto standard of per se legality, the Court must take action by articulating a comprehensible standard for evaluating whether a vertical restraint constitutes an antitrust violation.

Part II of this Article identifies the need for vertical enforcement, defines the different types of vertical restraints, explains the differences between the per se and rule of reason standards, and tracks the Court's enforcement of vertical restraints from their per se origins through the adoption of the rule of reason. Part III evaluates how the lower courts are currently handling vertical-restraint cases under the rule of reason and explores whether, as a result, vertical restraints have been rendered legal per se. Part IV then proposes that the Court consider replacing the rule of reason approach with a rebuttable-presumption-of-illegality standard to evaluate whether an alleged violation constitutes an unreasonable restraint on competition. Finally, Part V concludes that the Supreme Court has gone too far by declaring that all vertical restraints be subject to the rule of reason—thereby causing vertical enforcement

32. 550 U.S. 544 (2007) (raising the pleading standard for a plaintiff alleging an antitrust violation); *see infra* Part III.A.

levels to become suboptimal—and that to correct this misstep the Court must institute a new standard.

II. BACKGROUND

For purposes of determining their legality under Section 1 of the Sherman Act, restraints on trade are categorized as either vertical or horizontal.[33] Vertical restraints arise when an entity in the chain of distribution, typically a manufacturer, imposes restrictions on an entity at a different level within the chain, usually a retailer.[34] Horizontal restraints, on the other hand, arise when an entity enters into an agreement with a competitor at the same level of the distribution chain to eliminate competition.[35] Vertical restraints are generally considered less threatening to antitrust ideals than horizontal restraints because they do not eliminate competition in the same way horizontal restraints do.[36] Horizontal restraints are more likely than vertical restraints to eliminate *interbrand* competition[37]—competition between sellers offering similar but distinct products under different brand names.[38] Vertical restraints, on the other hand, more commonly reduce *intrabrand* competition[39]—competition between entities promoting the same brand of a certain product.[40] While the elimination of intrabrand competition may be less disconcerting than the elimination of interbrand competition, intrabrand competition is not completely innocuous, and for this reason, the current level of vertical enforcement is troubling.

33. Lemley & Leslie, *supra* note 14, at 1219.

34. *Id.* This Article will discuss both price and nonprice vertical restraints. *See infra* Part II.B.

35. Lemley & Leslie, *supra* note 14, at 1219.

36. *Leegin Creative Leather Prods., Inc.,* 551 U.S. at 888 (citing to Arizona v. Maricopa Cnty. Med. Soc'y, 457 U.S. 332, 348 n.18 (1982) ("[H]orizontal restraints are generally less defensible than vertical restraints."); Lemley & Leslie, *supra* note 14, at 1219; *see also infra* notes 150–153 and accompanying text (stating that one of the Court's main reasons for overturning the per se standard in *Leegin* was the difference between the procompetitive justifications for the two types of restraints).

37. *See* NCAA v. Bd. of Regents, 468 U.S. 85, 104–07 (1984) (explaining that a decrease in horizontal competitors was one anticompetitive consequence of a horizontal agreement).

38. Dresnick & Tucker Ronzetti, *supra* note 26, at 264.

39. Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 54 (1977).

40. Dresnick & Tucker Ronzetti, *supra* note 26, at 264 n.369.

A. Conflicting Interests and the Need for Vertical Enforcement

Vertical antitrust enforcement is thought to be essential for encouraging competition and protecting consumers because consumers' best interests usually do not coincide with the interests of those imposing the restraints.[41] The Supreme Court has advised that the antitrust laws should be interpreted in a way that protects interbrand competition more than intrabrand competition, and, as a result, restraints impacting interbrand competition should be more carefully scrutinized.[42] Nonetheless, eliminating intrabrand competition elicits antitrust concerns because it is questionable whether businesses can act as an effective surrogate for consumers' best interests—frequently, eliminating intrabrand competition leads to higher prices for consumers.[43]

Vertical restraints are most utilized by manufacturers.[44] Often, manufacturers decide to develop a chain of distribution, "a network of independent intermediate distributors and retail outlets," rather than to sell products directly to the end consumer.[45] This distribution chain is made up of numerous entities, each seeking to maximize profits.[46] Once a manufacturer sells a good, whether to a dealer or directly to a consumer, it has collected all the profit possible from that particular sale.[47] As a result, a manufacturer may want to act in its own self-interest and choose to limit the degree and nature of intrabrand competition—competition between its dealers—by imposing vertical restraints.[48] Vertical restraints make it possible for manufacturers to control the market after the initial sale of the good.[49] In other words, vertical restraints enable a manufacturer to ensure that its dealers will act in accordance with the manufacturer's best interest.[50] Other common reasons for imposing vertical restraints include stimulating interbrand competition, increasing the

41. *Id.* at 238.
42. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 890 (2007).
43. PITOFSKY ET AL., *supra* note 2, at 608.
44. *See id.*
45. *Id.* at 606.
46. Harbour, *supra* note 29, at 3–4.
47. *Id.*
48. PITOFSKY ET AL., *supra* note 2, at 606.
49. *See id.*
50. *Id.* at 606–07.

availability of customer services, and facilitating entry into the market for new competitors.[51]

Regrettably, despite their appeal to manufacturers, vertical restraints can threaten competition and thus raise antitrust concerns for other entities in the chain of distribution, particularly consumers.[52] Vertical restraints not only force consumers to pay higher prices for the same goods and services without receiving any additional benefits,[53] but they also limit dealers' profit margins because dealers no longer have the power to set their own prices. In addition, oftentimes vertical restraints facilitate cartel formation and market-power abuse, leading to higher prices for consumers.[54] This is often a result of conflicting interests.[55] Manufacturers prefer a decrease in intrabrand competition and an increase in interbrand competition, and vertical restraints enable manufacturers to realize this penchant. Unfortunately, consumers' best interests are not aligned with this preference, as an increase in both intrabrand and interbrand competition is most beneficial to consumers.[56]

Consumer benefit is calculated relative to the number of options available when purchasing a good, and the availability of options is proportional to the quantity of intrabrand and interbrand competition.[57] When the Court chose to subject all vertical restraints to the rule of reason in *Leegin*, it relied both on the appraisal that interbrand competition is more valuable to the free market than intrabrand competition and on the belief that vertical restraints,

51. Jessica L. Taralson, Note, *What Would Sherman Do? Overturning the Per Se Illegality of Minimum Vertical Price Restraints Under the Sherman Act in* Leegin Creative Leather Products, Inc. v. PSKS, Inc. *Was Not as Reasonable as It Seemed*, 31 HAMLINE L. REV. 549, 568–69 (2008); *see also* Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 55 (1977) ("[N]ew manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer. Established manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products. Service and repair are vital for many products . . . . The availability and quality of such services affect a manufacturer's goodwill and the competitiveness of his product. Because of market imperfections . . . these services might not be provided by retailers in a purely competitive situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did.").

52. Harbour, *supra* note 29, at 3–4.

53. *Id.* at 3.

54. Taralson, *supra* note 51, at 569.

55. *See* Harbour, *supra* note 29, at 7.

56. *See id.*

57. *See id.*

specifically minimum resale-price maintenance,[58] promote interbrand competition by encouraging manufacturers to compete for customers on more than just lower prices.[59] Attractive storefronts and customer service, for example, become more important to product differentiation when prices are stabilized.[60]

When it valued interbrand above intrabrand competition, the Court suggested that manufacturers would effectively act as fiduciaries for consumers when it imposed vertical restraints on its retailers.[61] But this inevitably begs the question of whether manufacturers' interests truly align with those of consumers.[62] Justice Breyer is skeptical.[63] In his dissent in *Leegin*, he recognized the potential for anticompetitive consequences to materialize as intrabrand competition dwindles.[64] Justice Breyer was apprehensive of minimum resale-price maintenance because it can incentivize dealers to charge higher prices, can fail to respond to changes in demand, and can sacrifice efficiency and innovation.[65] He was also worried that minimum resale-price maintenance would trigger horizontal conspiracies because tacit collusion among manufacturers is more likely to occur when pricing behavior is easily monitored.[66] In *Leegin*, the majority dismissed the argument that consumers were harmed by the higher prices resulting from minimum resale-price maintenance.[67] Instead, it assumed that all dealers would be induced to compete by offering additional customer service and that all consumers were willing to sacrifice lower price for increased

58. Minimum resale price maintenance is the practice where manufacturers set the lowest price at which its retailers are permitted to charge consumers for a product. *See infra* note 74 and accompanying text.

59. Dresnick & Tucker Ronzetti, *supra* note 26, at 238 & n.91 (citing Brief for Petitioner at 19–20, Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007) (No. 06-480), 2007 WL 160780, at *19–20).

60. *See id.* at 238–39 (explaining that vertical price restraints force retailers "to compete on more than mere price" by offering extra incentives like "customer service and an attractive presentation").

61. *See id.* at 238 & n.87 (explaining how increased interbrand competition ultimately benefits consumers); *see also* PITOFSKY ET AL., *supra* note 2, at 608 (suggesting that manufacturers could be thought of as surrogates for consumers' interests).

62. PITOFSKY ET AL., *supra* note 2, at 608.

63. *See Leegin*, 551 U.S. at 915 (Breyer, J., dissenting) ("[R]esale price maintenance can cause harms with some regularity—and certainly when dealers are the driving force.").

64. *Id.* at 910–11.

65. *Id.*

66. *Id.* at 911.

67. *Id.* at 895–96 (majority opinion).

service.[68] In doing so, the majority failed to acknowledge that these suppositions are not always true. The end result is that, regardless of what complimentary services dealers offer to compensate for higher prices, when a manufacturer demands that its retailers engage in minimum price fixing, consumers pay the price—literally.[69]

Regrettably, the majority in *Leegin* may have gravely underestimated the importance of intrabrand competition, and market realities demonstrate that the relationship between interbrand and intrabrand competition is, at the very least, more complex than the majority acknowledged.[70] The bottom line is that while eliminating interbrand competition may be more damaging to competition, consumers benefit most when both interbrand *and* intrabrand competition are exhibited in the market.[71]

B. Price vs. Nonprice: Breaking Down Vertical Restraints

Vertical restraints can be classified into two basic categories: price restraints and nonprice restraints.[72] Price and nonprice restraints, although seemingly distinct, are often difficult to differentiate for categorization purposes because they "generally occur under similar circumstances and have an almost identical economic impact."[73] Usually, vertical price restraints take the form of price-fixing agreements, also known as resale-price maintenance, and they surface when a seller sets a specific price—a price ceiling

68. *See id.* at 891 ("If the consumer can then buy the product from a retailer that discounts because it has not spent capital providing services or developing a quality reputation, the high-service retailer will lose sales to the discounter, forcing it to cut back its services to a level lower than consumers would otherwise prefer. Minimum resale price maintenance alleviates the problem because it prevents the discounter from undercutting the service provider.").

69. Note, *Leegin's Unexplored "Change in Circumstance": The Internet and Resale Price Maintenance*, 121 HARV. L. REV. 1600, 1605 (2008) [hereinafter *Change in Circumstance*] (quoting Robert Pitofsky, *In Defense of Discounters: The No-Frills Case for a* Per Se *Rule Against Vertical Price Fixing*, 71 GEO. L.J. 1487, 1488 (1983)) (internal quotation marks omitted) ("[T]he one point that emerges clearly in any debate concerning the *per se* rule is that minimum vertical price agreements lead to higher, and usually uniform, resale prices.").

70. *See infra* notes 321–337 and accompanying text.

71. *See* Harbour, *supra* note 29, at 7.

72. *See* Lemley & Leslie, *supra* note 14, at 1224.

73. Taralson, *supra* note 51, at 568; *see also* Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 727–28 (1988) (discussing the possibility of using vertical nonprice restraints to set prices).

(maximum resale price maintenance) or a price floor (minimum resale price maintenance)—at which a buyer may resell the good.[74]

Nonprice vertical restraints include a much broader array of restraints, including customer and territorial restrictions, channel of distribution restraints, exclusive dealing or distributor agreements, and tying arrangements.[75] Customer and territorial restraints occur when a supplier or manufacturer mandates that a distributor may not sell outside of an assigned geographic territory or a particular demographic of customers.[76] For instance, in order to eliminate competition among its retailers, a gasoline supplier may set different territorial boundaries for each retailer outside of which each is prohibited from selling gasoline to consumers. A channel-of-distribution restraint results when a supplier or manufacturer requires a distributor to sell solely within a designated "channel of distribution."[77] Any means by which a good reaches a consumer is considered a channel of distribution; this includes all intermediate entities in the chain of distribution and even extends to situations in which entities decide to utilize the Internet.[78] For example, a manufacturer of expensive designer watches may want to protect the brand's high-end reputation by prohibiting distributors from selling the watches in wholesale stores or over the Internet. Exclusive dealing arrangements arise when a buyer agrees to buy products or

74. LAWRENCE FULLERTON ET AL., GETTING THE DEAL THROUGH: VERTICAL AGREEMENTS: THE REGULATION OF DISTRIBUTION PRACTICES IN 34 JURISDICTIONS WORLDWIDE 210 (Stephen Kinsella ed., 2008).

75. *Id.* A tying arrangement exists when a seller agrees to sell a product to a buyer, but only if the buyer also purchases another product from the seller. *Id.* While this Article is limited to enforcement under Section 1, it should be noted that tying arrangements can also be evaluated under section 3 of the Clayton Act, which has a quasi per se analysis. *See* Daniel E. Lazaroff, *Reflections on* Eastman Kodak Co. v. Image Technical Services, Inc.*: Continued Confusion Regarding Tying Arrangements and Antitrust Jurisprudence*, 69 WASH. L. REV. 101, 106 (1994). Although beyond the scope of this Article, it is interesting that courts are increasingly considering the business justifications for tying arrangements, which shows a preference for a rule of reason type analysis. FULLERTON ET AL., *supra* note 74, at 212. For a more comprehensive discussion and history of antitrust enforcement of tying arrangements, see PITOFSKY ET AL., *supra* note 2, at 859; *United States v. Loew's Incorporated*, 371 U.S. 38, 44–47 (1962); *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2, 9–18 (1984); *Eastman Kodak Company v. Image Technical Services., Inc.*, 504 U.S. 451, 461–62 (1992); *Illinois Tool Works, Inc. v. Independent Ink, Inc.*, 547 U.S. 28, 33–43 (2006).

76. *See* FULLERTON ET AL., *supra* note 74, at 210.

77. *Id.*

78. *See Distribution Channel Definition*, THE FREE DICTIONARY, http://www.thefreedictionary.com/distribution+channel (last visited Apr. 12, 2012) (defining distribution channel as "a way of selling a company's product either directly or via distributors").

services exclusively from one seller for a specific period of time.[79] Similarly, exclusive distributorship arrangements arise when a manufacturer agrees that a distributor will have the sole right to sell products or goods in a certain geographic area.[80]

C. Standards for Analysis: Per Se and Rule of Reason

As a consequence of the Supreme Court's effort to limit the scope of the Sherman Act to prohibit only those restraints which unreasonably restrain competition, the Supreme Court has developed two primary standards of analysis: the per se standard and the rule of reason.[81]

1. The Per Se Standard

The Court has consistently held that the per se standard applies to agreements that "because of their pernicious effect on competition and lack of any redeeming virtue" yield an irrebuttable presumption of unreasonableness.[82] In effect, a court presumes, without conducting an economic analysis or considering procompetitive defenses, that certain conduct is unreasonable and, therefore, illegal per se.[83] Implicit in a per se designation is the presumption that any underlying business reasons for imposing a restraint will always be less significant than the restraint's detriment to competition and, therefore, need not be considered by the court.[84] The finality of a per se classification is severe, in that once a restraint is found to fall into a class of restraints subject to the per se standard, it is automatically declared to be illegal.[85] The impact of this classification on the outcome of litigation is unmistakable—once a plaintiff proves that

79. *See* FULLERTON ET AL., *supra* note 74, at 210.

80. *Id.*

81. Lemley & Leslie, *supra* note 14, at 1212.

82. N. Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958); *see also* Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 723 (1988) ("We have said that per se rules are appropriate only for 'conduct that is manifestly anticompetitive,' that is, conduct 'that would always or almost always tend to restrict competition and decrease output.'" (citations omitted)).

83. Lemley & Leslie, *supra* note 14, at 1213–14; *see also* Stucke, *supra* note 10, at 1379 ("Under the per se rule, once a plaintiff proves an agreement among competitors to engage in the prohibited conduct, the plaintiff wins.").

84. *See* Lemley & Leslie, *supra* note 14, at 1213–14.

85. *Id.*

competitors agreed to engage in conduct that is illegal per se, the plaintiff wins.[86]

2. The Rule of Reason

In contrast to the per se standard, the rule of reason is a flexible standard that requires the fact-finder to consider all of the circumstances in each case to determine whether the conduct is an unreasonable restraint on competition.[87] Legality, under the rule of reason, is a question of whether the restraint "merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition."[88] To answer that question, the court must consider several factors, including the facts surrounding the type of business in which the restraint applies, the business's economic condition before and after the restraint became effective, the nature of the restraint, and the restraint's actual or probable economic impact.[89] In addition, the court should take into account the "history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, [and] the purpose or end sought to be attained . . . ."[90] After evaluating all of these considerations, the court then determines what the net competitive effect of the restraint is by balancing the procompetitive justifications against the anticompetitive implications.[91]

Another difference between the standards is that the rule of reason imposes a heightened burden on plaintiffs.[92] Under both standards, the plaintiff must first prove the existence of an agreement among competitors.[93] In rule of reason cases, however, the plaintiff must then affirmatively prove that the restraint unreasonably restricts competition.[94] That is, the court will not assume unreasonableness, as

86. Stucke, *supra* note 10, at 1379.

87. Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 49 (1977).

88. Bd. of Trade of City of Chi. v. United States, 246 U.S. 231, 238 (1918).

89. *Id.*

90. *Id.* While good intentions cannot save unreasonable restraints on trade, knowledge of intent can help the court to interpret the circumstances and predict economic consequences. *Id.*

91. *See id.*

92. *See, e.g.*, Richard Liebeskind & Joseph R. Tiffany, *Two Years After Leegin, Questions Remain on Lawfulness of Resale Price Maintenance*, July 31, 2009, at 2, *available at* http://www.pillsburylaw.com/siteFiles/Publications/053986E13BCE687E8E0CA54E89372048.pdf ("*Leegin*'s reasonableness requirement makes the already heightened *Twombly* standard even more rigorous in RPM cases.").

93. Stucke, *supra* note 10, at 1385.

94. *See id.* at 1385.

it does in the context of a per se analysis.[95] Rather, the plaintiff must demonstrate an actual or potential anticompetitive impact in the market and generally must also show that the defendant possesses market power.[96] If the plaintiff satisfies this initial burden of proof, the defendant can then provide procompetitive justifications for imposing the restraint.[97] If the defendant is able to do so, the plaintiff once again shoulders the burden of proving that that the restraint is not reasonably necessary.[98] If the plaintiff is able to prove this, the court will then consider whether the anticompetitive effects of the restraint outweigh the procompetitive justifications.[99] Only if the court finds that the procompetitive benefits do not outweigh the anticompetitive injuries can the plaintiff prevail.[100]

D. Vertical Restraint Case Law: A Pattern of Reflexive Condemnations?

At the outset of antitrust enforcement, the Court could not identify any procompetitive justifications for imposing vertical restraints, and thus, in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*,[101] the Court deemed them to be illegal per se. However, this pronouncement has not endured. About fifty years after *Dr. Miles*, the Court began to reconsider its blanket condemnation of vertical restraints. In *Continental T. V., Inc. v. GTE Sylvania Inc.*,[102] the Court declared that all vertical nonprice restraints would be subject to the rule of reason.[103] Then in *Leegin*, the Court overturned nearly one hundred years of precedent when it changed the appropriate standard for evaluating minimum resale price fixing from the per se rule to rule of reason, thereby subjecting all vertical restraints to a

95. *See id.*
96. *In re* Ins. Brokerage Antitrust Litig., 618 F.3d 300, 315–16 (3d Cir. 2010).
97. Stucke, *supra* note 10, at 1385.
98. *Id.* at 1385–86.
99. *Id.* at 1386. During this stage, the court may consider less restrictive alternatives to the restraint, but the existence of such alternatives does not automatically designate a restraint as anticompetitive, and, in the same way, the absence of such an alternative does not excuse the restraint as procompetitive. *See* White Motor Co. v. United States, 372 U.S. 253, 271–72 (1963) (explaining that less restrictive alternatives are one of many considerations for determining competitive impact).
100. *See* Stucke, *supra* note 10, at 1386.
101. 220 U.S. 373, 399–409 (1911).
102. 433 U.S. 36 (1977).
103. *Id.* at 44–45, 59.

rule of reason analysis.[104] The Court stated that "[i]t would make no sense to create out of the single term 'restraint of trade' a chronologically schizoid statute, in which a 'rule of reason' evolves with new circumstances and new wisdom, but a line of *per se* illegality remains forever fixed where it was."[105] The Court then declared that when Congress left the interpretation of the scope of the Sherman Act to the courts, it also granted the courts the power to decide if that scope must "evolve to meet the dynamics of present economic conditions."[106] Through the use of this power, the Supreme Court has created a "pattern of reflexive condemnations" in vertical enforcement,[107] and it is clear that the Court still reserves the power to alter the standard whenever changing economic realities necessitate a change in the future.

1. Vertical Nonprice Restraints

Initially, the Supreme Court refused to extend the per se standard to vertical nonprice restraints, as demonstrated in *White Motor Co. v. United States*.[108] The Court recognized that this case was the first time that it was evaluating a vertical territorial restriction and, as such, stated that "[w]e need to know more than we do about the actual impact of these arrangements on competition to decide whether they . . . should be classified as *per se* violations of the Sherman Act."[109] The Court wanted to discern more information about the economic and business reasons for imposing the geographic restrictions and their actual impact on competition before condemning them as illegal per se.[110]

Not long after that decision, the Court disregarded the hesitation it demonstrated in *White*, declaring all vertical nonprice restraints illegal per se in *United States v. Arnold, Schwinn & Co.*[111] Instead of considering the economic effects of the territorial restraints that Schwinn imposed on its retailers, the Court relied on property law theories to justify the switch to the per se standard.[112] The Court

104. *See* Leegin Creative Prods. Inc. v. PSKS Inc., 551 U.S. 877, 907 (2007).
105. *Id.* at 900 (quoting Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 732 (1988)).
106. *Id.* at 899.
107. *See* Wright, *supra* note 16, at 2.
108. 372 U.S. 253, 255–57 (1963).
109. *Id.* at 263.
110. *See id.*
111. 388 U.S. 365, 382 (1967).
112. *Id.* at 374–78.

stated that once a manufacturer "parts with dominion over his product or transfers risk of loss to another, he may not reverse control over its destiny or the conditions of its resale."[113] The Court then reasoned that a manufacturer attempting to control future sales of a product after the title passed to a purchaser would have no other motive but to eliminate competition.[114] In the Court's opinion, this was enough to validate a per se condemnation.[115]

However, the *Schwinn* ruling was short lived. Just ten years later, the Court reconsidered the per se classification for all vertical nonprice restraints in *Sylvania*.[116] In an effort to reinvigorate its dwindling market share, Sylvania had undertaken a new marketing strategy and, as part of its strategy, eliminated its distributors from the retail chain and instead sold directly to franchised retailers.[117] Sylvania then imposed limitations on the franchisors by limiting them to selling Sylvania products only from their specific franchised location while maintaining the ability to increase or decrease retailers as it deemed appropriate.[118] The Court was concerned about applying a per se rule to the limitations in Sylvania's franchise agreements because it wanted to know more about the actual impact of the arrangements on competition before proclaiming that they were unjustified and only had a "pernicious effect on competition."[119]

The Court pointed out that, although it is possible for vertical restrictions to reduce intrabrand competition, the restrictions generally prompt an increase of interbrand competition because manufacturers often use the restrictions to become more competitive with each other.[120] It was this potential increase in interbrand competition that the Court accepted as a reasonable justification for restraining competition. In fact, the Court explained that due to market imperfections, specifically the "free rider"[121] problem,

113. *Id.* at 379.
114. *Id.* at 379–81.
115. *Id.* at 382.
116. Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977).
117. *Id.* at 38.
118. *Id.*
119. *Id.* at 50 (quoting N. Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958)).
120. *Id.* at 54–55.
121. The free-rider problem arises when consumers utilize the services that a full-price retailer offers but ultimately purchase a good from a discount retailer who offers lower prices but no services. *Change in Circumstance*, *supra* note 69, at 1615. For a more complete discussion of free riding, see *infra* Part III.C.1.

restrictions may sometimes be necessary to preserve service quality and distribution efficiency.[122] The Court clarified that a "departure from the rule of reason standard must be based upon demonstrable economic effect rather than . . . upon formalistic line drawing."[123] It then held that, due to the procompetitive justifications, the rule of reason was the appropriate test for all vertical nonprice restraints.[124]

2. Vertical Price Restraints

In 1911, *Dr. Miles* first brought antitrust enforcement of vertical price fixing to the Court's attention.[125] In *Dr. Miles*, the Court deemed vertical price fixing illegal per se because it could find no difference between vertical and horizontal price fixing.[126] Dr. Miles Medical Company was a drug manufacturer that sought to impose a minimum resale price on its distributors and all other subsequent purchasers in the chain of distribution.[127] At issue was whether the manufacturer could impose such restrictions.[128] In reaching its decision, the Court ignored the economic impact of the restrictions and instead relied on the property concept of restraints on alienation.[129] The Court explained that once a purchaser has secured full ownership of a product, the purchaser shall be free from restrictions on any future uses.[130]

The Court also found that the agreement among the manufacturer, the wholesalers, and the retailers to set retail prices was an obvious restraint on trade because it stifled competition.[131] The Court stated that the manufacturer had created "a system of interlocking restrictions" through which it attempted to control not only the prices set by its agents but also the prices set by all dealers in all industry-wide sales.[132] The Court clarified that while reasonable restraints of trade are allowed, vertical price fixing was not reasonable because, like horizontal price fixing, there were no

122. *Sylvania*, 433 U.S. at 54–56.
123. *Id.* at 58–59.
124. *Id.*
125. *See* Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373, 408 (1911).
126. *See id.* at 407–08.
127. *Id.* at 394.
128. *Id.* at 395.
129. *Id.* at 404–05.
130. *Id.*
131. *Id.* at 400.
132. *Id.* at 399.

procompetitive benefits.[133] The Court determined that the only possible motivation for invoking such restrictions was a desire to set prices and eliminate price competition.[134] As a result, the Court classified vertical price fixing within the same category as horizontal price fixing agreements and declared it to be illegal per se.[135]

More than eighty-five years after *Dr. Miles*, the Court began the shift to the rule of reason in *State Oil Co. v. Khan*[136] when it reevaluated the suitability of the per se standard for analyzing maximum price fixing.[137] Barkat Khan had entered into an agreement to lease and operate a gas station owned by State Oil and purchase its gasoline supply from State Oil.[138] The agreement required that if Khan decided to sell gasoline at a price higher than State Oil's suggested retail price, he would rebate the excess profits to State Oil.[139] By imposing this restriction, State Oil had likely established a maximum resale price[140]—a per se violation of the Sherman Act according to *Dr. Miles*.[141] However, instead of invoking stare decisis, the Court determined that maximum resale price fixing could be distinguished from minimum resale price fixing because the former does not encourage higher prices, and thus it does not harm competition and consumers.[142] The Court then held that the rule of reason should apply to maximum resale price fixing.[143]

Then, just ten years later, the Court completed the transition to the rule of reason in *Leegin* when it once again decided to "temper, limit, or overrule once strict prohibitions on vertical restraints."[144] The Court took the last step in relaxing vertical enforcement by holding that the per se standard should no longer apply to minimum resale price maintenance.[145] Leegin sold belts and other women's fashion accessories under the name "Brighton" to over five thousand retailers, primarily independent boutiques and specialty stores, one of

133. *Id.* at 407.
134. *Id.*
135. *Id.* at 408.
136. 522 U.S. 3 (1997).
137. *Id.* at 7.
138. *Id.* at 7–8.
139. *Id.* at 8.
140. *Id.* at 9.
141. *See* Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373, 408 (1911).
142. *State Oil Co.*, 522 U.S. at 15.
143. *Id.* at 22.
144. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 901 (2007).
145. *Id.* at 907.

which was PSKS.[146] Leegin had a policy of refusing to deal with any retailer who would not comply with its minimum suggested retail prices.[147] When Leegin discovered that PSKS had been cutting prices by 20 percent across the entire line, it requested that PSKS comply with the suggested price, but PSKS refused.[148]

On appeal before the Court, Leegin did not deny the existence of the agreement fixing minimum resale prices but instead argued that the rule of reason was the appropriate standard for determining whether its policy was in violation of the Sherman Act.[149] In the years following *Dr. Miles*, the Court had continued to worry that vertical agreements produced the same anticompetitive effects as horizontal agreements and, as such, had declined to switch to the rule of reason.[150] However, in *Leegin*, the Court recognized that the more recent case law no longer treated vertical and horizontal conduct as analogous and found the property concepts applied in *Dr. Miles* were outdated.[151] As a result, the Court reconsidered the economic impacts of the two classes of restraints.[152] In the end, the Court agreed with Leegin that vertical price fixing, unlike horizontal price fixing, could have procompetitive justifications, including an increase of interbrand competition, a decrease in the prevalence of free riders, and an increased facilitation for new market entrants.[153]

In reaching its decision, the Court noted that, although higher prices were a potential consequence, they were not sufficient to hold minimum resale price fixing to a per se standard without an additional showing of anticompetitive conduct.[154] Instead, the Court stressed that the purpose of the antitrust laws is to promote interbrand competition, not to protect consumers from high prices.[155] Despite this proclamation, the Court assured the parties that the "rule of reason [was] designed and used to eliminate anticompetitive transactions from the market."[156] It also warned the lower courts to

146. *Id.* at 882.
147. *Id.* at 883.
148. *Id.* at 884.
149. *Id.* at 884–85.
150. *Id.* at 887–89.
151. *Id.*
152. *Id.* at 889.
153. *Id.* at 890–92.
154. *Id.* at 895.
155. *Id.* at 895–96.
156. *Id.* at 898.

be diligent in eliminating the anticompetitive uses of vertical price restraints from the market, particularly when policing entities with dominant market power that could be disguising a cartel with vertical price fixing.[157]

III. DOWN FOR THE COUNT: VERTICAL RESTRAINTS ARE LEGAL PER SE UNDER THE RULE OF REASON

In spite of its admission in *Leegin* that anticompetitive impacts could outweigh the procompetitive effects of vertical restraints, the Court tasked the lower courts with devising their own rules and fabricating their own litigation structures to guarantee that the rule of reason would eliminate anticompetitive restraints from the market.[158] Consequently, after *Leegin*, there was a great deal of uncertainty as to how the lower courts would interpret the Court's strategy for an effective rule of reason analysis.[159] Since *Sylvania* and *Leegin*, federal courts[160] have employed the rule of reason in vertical price and nonprice restraint cases, and while courts seem to be heeding the advice of the Supreme Court—to develop their own methods for performing a rule of reason analysis—plaintiffs seeking vertical enforcement have experienced very limited success.[161] This should not come as a surprise to many, as one of the primary criticisms of the rule of reason is that enforcement levels become suboptimal because plaintiffs have difficulty overcoming the high burden of proof.[162] Under the rule of reason, plaintiffs must first satisfy their initial burden of proof by sufficiently alleging the existence of an

157. *Id.* at 897–98.

158. *Id.* at 898–99.

159. Dresnick & Tucker Ronzetti, *supra* note 26, at 249–50.

160. The scope of this Article is limited to federal courts, but it is worth noting that although many states chose to harmonize their antitrust laws with federal antitrust laws, *Leegin* is not binding precedent on the states. Michael A. Lindsay, *State Resale Price Maintenance Laws After* Leegin, ANTITRUST SOURCE, Oct. 2009, at 1, *available at* http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Oct09_Lindsay10_23f.authcheckdam.pdf. After *Leegin*, it was unclear how the states would deal with vertical restraint enforcement. *Id.* Some state courts rejected the per se standard and at least one state had even taken measures to proclaim its outright rejection of *Leegin*. *Id.* at 2. Less than two years after *Leegin*, Maryland passed legislation declaring that minimum resale price fixing was unlawful per se. *Id.* at 2. For a more detailed discussion of state antitrust enforcement after *Leegin*, see *id.* at 1–7, and Lindsay, *Overview of State RPM*, ANTITRUST SOURCE, Dec. 2010, *available at* http://www.americanbar.org/content/dam/aba/publications/antitrust_law/source_lindsay_chart.authcheckdam.pdf.

161. Dresnick & Tucker Ronzetti, *supra* note 26, at 257–65.

162. *See Change in Circumstance*, *supra* note 69, at 1620.

agreement that unreasonably restrains competition and must then prove that the restraint's anticompetitive harms outweigh any procompetitive justifications.[163] Satisfying the second burden has become particularly challenging in light of courts' willingness to accept the facile procompetitive justifications that a restraint promotes interbrand competition or counteracts the free-rider problem.[164] The suboptimal enforcement existing under the rule of reason leads many skeptics to declare that, in application, the rule of reason operates as a de facto rule of legality.[165]

In *Sylvania* and *Leegin*, the Supreme Court endorsed a rule of reason approach and never expressly sanctioned a per se legality standard.[166] However, notwithstanding the Court's intention, there is substantial data and literature supporting the idea that the rule of reason defaults to a rule of per se legality.[167] For example, then-Judge Ginsburg of the U.S. Court of Appeals for the District of Columbia Circuit conducted a survey of the outcome of all vertical nonprice restraint cases following the Court's decision in *Sylvania*.[168] She found that from 1977 until 1991, federal district courts considered forty-five cases alleging an antitrust violation, and, of those, plaintiffs lost forty-one.[169] This exposes that, following the Court's decision to subject nonprice restraints to the rule of reason, less than 10 percent of plaintiffs won cases alleging an antitrust violation.[170] Moreover, there also is evidence that maximum vertical price fixing has suffered a similar fate by becoming "de facto legal" since the Court's decision to subject the practice to the rule of reason in *Khan*.[171] Perhaps most revealing, one study demonstrates that in the decade from 1999 and 2009, plaintiffs lost 221 out of all 222

163. Stucke, *supra* note 10, at 1385.

164. *See* William Kolasky, *Review of* How the Chicago School Overshot the Mark, 5 COMPETITION POL'Y INT'L 173, 177 (2009) (noting that scholars recently identified this trend).

165. *See, e.g.*, Marina Lao, *Resale Price Maintenance: The Internet Phenomenon and Free Rider Issues*, 55 ANTITRUST BULL. 473, 507 (2010) (referencing criticisms by Judge Richard Posner and Judge Douglas Ginsburg); Kelly, *supra* note 4, at 635–40.

166. Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977); Lao, *supra* note 165, at 507.

167. *See* Lao, *supra* note 165, at 507–10.

168. *Id.* at 508.

169. *Id.*

170. *Id.*

171. *Id.* (citing Daniel A. Crane, *Chicago, Post-Chicago, and Neo-Chicago*, 76 U. CHI. L. REV. 1911, 1912 (2009)).

cases subject to the rule of reason that reached final judgment.[172] That is, plaintiffs lost more than 99 percent of cases under the rule of reason in a ten-year period.[173]

The extreme scarcity of successful claims under the rule of reason raises a red flag, and while these studies alone are not determinative, they certainly suggest that the rule of reason standard has resulted in per se legality.[174] The mounting concern for plaintiffs who are unable to win under the rule of reason is further evidenced by reflexive actions taken by Congress and state governments following the *Leegin* decision, including a Senate bill proposal that would overturn *Leegin*[175] and many state laws proclaiming that vertical price fixing remained illegal per se.[176] The Senate bill, proposed less than four months after *Leegin*, disparaged *Leegin* outright and explicitly disclosed that the bill's purpose was to overturn the Court's decision and return vertical minimum price fixing to a per se standard.[177] The bill, since renamed the Discount Pricing Consumer Protection Act, has been a highly controversial topic in Congressional hearings and has not yet been passed.[178] Contributing further to this unrest is the contention that the Court has exceeded its congressional grant of authority by forgoing the original intention of the Sherman Act and choosing, instead, to favor its own ideologies.[179] The argument is not that policy concessions should

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172. *Id.* (citing Michael A. Carrier, *The Rule of Reason: An Empirical Update for the 21st Century*, 16 GEO. MASON L. REV. 827, 829 (2009)). It is fair to point out that at least some cases settle before final judgment; therefore, plaintiffs may have a higher likelihood of prevailing under the rule of reason than these studies reveal. Stucke, *supra* note 10, at 1424.

173. *Id.*

174. *Id.*

175. *See* Kelly, *supra* note 4, at 643.

176. *See supra* note 160 and accompanying text.

177. Kelly, *supra* note 4, at 643.

178. Ariana E. Gillies, Note, *Not with a Bang, But a Whimper: Congress's Proposal to Overturn the Supreme Court's* Leegin *Decision with the Discount Pricing Consumer Protection Act of 2009*, 18 VILL. SPORTS & ENT. L.J. 645, 646 (2011). A version of the bill died in committee in 2009; in 2011, Senator Herbert Kohl and Representative Henry Johnson sponsored new versions of the bill, neither of which has been passed into law. *Discount Pricing Consumer Protection Act of 2009*, GOVTRACK, http://www.govtrack.us/congress/bills/111/hr3190 (last visited Oct. 30, 2012); *Discount Pricing Consumer Protection Act of 2011*, GOVTRACK, http://www.govtrack.us/congress/bills/112/hr3406 (last visited Oct. 30, 2012); *Discount Pricing Consumer Protection Act*, GOVTRACK, http://www.govtrack.us/congress/bills/112/s75 (last visited Oct. 30, 2012).

179. Stucke, *supra* note 10, at 1480–81.

never be made, but that the legislature—not the courts—should be responsible for making that assessment.[180]

Although the Supreme Court might have intended the rule of reason to be a flexible replacement for the per se rule, it erred by continuing to ignore the infirmities associated with conducting a rule of reason analysis. The Court failed to articulate a clear standard of analysis in *Sylvania* and then neglected to do so again in *Leegin*. This lack of guidance is particularly unsettling because the Court said that the lower courts' ineffectiveness in conducting an accurate economic analysis was a primary factor contributing to its decision in *Leegin* to switch to the rule of reason.[181] Yet, despite the Court's acknowledgement that the lower courts were not familiar enough with the competitive effects of vertical restraints to validate a per se rule, the Court somehow had confidence that the lower courts were familiar enough to develop their own standards for conducting a rule of reason analysis.[182]

As one commentator pointed out, "[t]he Court's shift from per se rules would be an unsurprising reflection of the Court's increased confidence in its or the lower courts' capacity to adjudicate complex economic issues . . . ."[183] However, this is not the case with antitrust analysis—the Court has actually become more skeptical of the judiciary's competence to issue consistent and accurate rulings in recent years.[184]

Lower courts' inability to evaluate the impact of economic changes, which include difficulty allocating the proper weight to policy considerations, may be the biggest concern for plaintiffs, but additional obstacles have contributed to plaintiffs' limited success in recent vertical-restraint cases. Such difficulties include an increased burden at the pleading stage in the wake of *Leegin* and *Twombly*,[185] and the issue of how the lower courts identify the horizontal effects of vertical agreements—except in cases exhibiting clear proof of

180. *Id.*

181. Liebeskind & Tiffany, *supra* note 92, at 2.

182. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 898–99 (2007).

183. Stucke, *supra* note 10, at 1408.

184. *Id.* at 1408–09 (citing Credit Suisse Secs. (USA) LLC v. Billing, 551 U.S. 264, 281–82 (2007); Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570 (2007); Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 414–15 (2004)).

185. *See* Liebeskind & Tiffany, *supra* note 92, at 2 ("*Leegin*'s reasonableness requirement makes the already heightened *Twombly* standard even more rigorous . . . .").

horizontal collusion.[186] When viewed in the aggregate, these issues bolster the concerns that the lower courts are applying a rule of reason analysis that fails to protect the market from anticompetitive conduct, and thereby results in a de facto declaration of per se legality for vertical restraints.

A. Leegin *and* Twombly*: Sounding the Death Knell for Vertical Restraint Liability*

When a pleading standard is too high, it becomes nearly impossible for a plaintiff to survive a motion to dismiss for failure to state a claim.[187] In vertical-restraint cases, this heightened pleading standard essentially operates as a presumption of legality. *Twombly* increased the burden on plaintiffs in the pleading stages of antitrust cases by requiring them to disclose enough factual information to demonstrate that the defendant's conduct was plausible and not just possible.[188] On its own, *Twombly* does not seem to create an impenetrable standard for pleading, but when combined with *Leegin*, it might.

1. Plausible Pleadings as Required by *Twombly*

In *Twombly*, consumers brought a putative class action against numerous major telecommunications providers, alleging that the providers violated Section 1 of the Sherman Act.[189] In their complaint, the consumers did not provide proof of a tacit unlawful agreement between the providers but instead pointed to the providers' parallel conduct to prove an agreement existed.[190] The Supreme Court dismissed the complaint because the plaintiffs had not "nudged their claims across the line from conceivable to plausible."[191] The Court explained that to survive a motion to dismiss, plaintiffs must plead not just a "short and plain statement of

186. *See infra* Part III.B.

187. Arthur R. Miller, *From* Conley *to* Twombly *to* Iqbal*: A Double Play on the Federal Rules of Civil Procedure*, 60 DUKE L.J. 1, 67–68 (2010) (discussing a high dismissal rate after *Twombly*).

188. *Twombly*, 550 U.S. at 570.

189. *Id.* at 550.

190. *Id.* at 564.

191. *Id.* at 570.

the claim" but enough factual allegations "to raise a right to relief above the speculative level."[192]

In reaching its decision, the Court warned plaintiffs of the danger of pleading only ambiguous parallel or interdependent conduct, stating that such conduct could just as easily be consistent with a conspiracy as it could with a "wide swath of rational and competitive business strategy unilaterally prompted by common perceptions of the market."[193] In an effort to prevent superfluous litigation, the Court required plaintiffs to provide in the pleadings a stronger showing of a violation.[194] While the plaintiffs in *Twombly* alleged a horizontal conspiracy among competitors, and not a vertical agreement, *Twombly* set the bar for the level of particularity required of pleadings in all antitrust cases.[195] Typically, there is no need to circumstantially prove the existence of concerted action in vertical-restraint cases because an agreement is usually clear; however, *Twombly* affects vertical-restraint cases by requiring plaintiffs to provide enough factual assertions of anticompetitive conduct in their complaints to allege an unreasonable restraint on trade that would entitle them to relief.[196]

2. An Insurmountable Standard? A Plaintiff's Plight in the Wake of *Leegin* and *Twombly*

By requiring more than mere allegations of anticompetitive conduct, *Twombly* forced plaintiffs to think twice before filing a complaint.[197] *Leegin* then added an additional burden for plaintiffs to garner antitrust enforcement in vertical-restraint cases.[198] After *Leegin*, plaintiffs had to successfully plead not only the existence of an agreement restraining competition but also the unreasonableness of the restraint.[199] Many courts have since gone as far as requiring plaintiffs to show that the restraint does not merely have the potential

192. *Id.* at 555.
193. PITOFSKY ET AL., *supra* note 2, at 497; *see Twombly*, 550 U.S. at 554.
194. *Twombly*, 550 U.S. at 558–59.
195. *See id.* at 555–56.
196. *See id.*
197. PITOFSKY ET AL., *supra* note 2, at 499.
198. Dresnick & Tucker Ronzetti, *supra* note 26, at 250.
199. *See* Liebeskind & Tiffany, *supra* note 92, at 2 (stating that in resale-price-maintenance cases, plaintiffs must allege facts that plausibly suggest that an agreement exists and that is unreasonable).

to harm competition but that it does in fact harm competition.[200] This additional element requires plaintiffs to sufficiently establish the relevant market and the anticompetitive impact of a restraint.[201] The lower courts have consistently emphasized that plaintiffs must satisfy this increased burden at the pleading stage.[202]

Prior to *Leegin*, plaintiffs often would describe only general allegations of anticompetitive conduct in their pleadings because defendants typically concealed such conduct, making it difficult to prove the allegations prior to discovery.[203] As a result, plaintiffs relied heavily on discovery to produce proof of antitrust violations.[204] However, this is no longer a viable strategy in the wake of *Leegin* and *Twombly*.[205]

Leegin's subsequent case history is particularly interesting.[206] After the Supreme Court reversed and remanded, the district court granted Leegin's 12(b)(6) motion to dismiss, and PSKS subsequently appealed to the Fifth Circuit.[207] Citing *Twombly*, the Fifth Circuit stated that in order to survive the pleading stages, the plaintiffs must describe "sufficient factual matter" and not mere "labels and conclusions."[208] The Fifth Circuit also explained that, in antitrust cases, this rule requires plaintiffs to demonstrate that the defendant's conduct actually harmed competition.[209] The court then clarified that, according to *Leegin*, higher prices alone do not sufficiently identify an unreasonable restraint on competition.[210] Instead, the court pointed out that when pleading resale-price-maintenance claims, plaintiffs must "plausibly define the relevant product and geographic

200. *See, e.g.*, Brantley v. NBC Universal, Inc., 675 F.3d 1192 (9th Cir. 2012); PSKS, Inc. v. Leegin Creative Leather Prods., Inc., 615 F.3d 412 (5th Cir. 2010); Jacobs v. Tempur-Pedic Int'l, Inc., 626 F.3d 1327 (11th Cir. 2010); Spahr v. Leegin Creative Leather Prods., Inc., No. 2:07-CV-187, 2008 WL 3914461 (E.D. Tenn. Aug. 20, 2008). According to lower courts, potential to harm competition is not sufficient unless a defendant also possesses market power, and some courts have even stated that actual harm to consumers, such as higher prices, is insufficient to overcome the procompetitive benefits as well. *See Jacobs*, 626 F.3d at 1339–40.

201. Liebeskind & Tiffany, *supra* note 92, at 2.

202. *Id.*

203. *Id.*

204. *Id.*

205. *Id.*

206. *See* PSKS, Inc. v. Leegin Creative Leather Prods., Inc., 615 F.3d 412 (2010).

207. *Id.* at 414.

208. *Id.* at 417 (internal quotations omitted).

209. *Id.*

210. *Id.*

markets"[211] and then "plausibly allege the defendant's market power [in those markets]."[212] After laying out the standards for defining a relevant market, the Fifth Circuit determined that PSKS failed to adequately define the relevant product market.[213] As a result, the court held that PSKS's claim could not survive the motion to dismiss because the complaint failed to sufficiently plead that Leegin possessed market power and did not allege any other injury to competition.[214]

Similarly, in a different case against Leegin, the United States District Court for the Eastern District of Tennessee had to evaluate whether a 12(b)(6) motion to dismiss was appropriate in light of *Leegin* and *Twombly*.[215] The facts of the case and the vertical price-fixing agreement were the same as those laid out in *Leegin*, except the plaintiff, Spahr, was a different retailer.[216] The court dismissed Spahr's definition of the relevant product market because reasonable substitute products for the Brighton brand were available.[217] The court also found that Spahr's evidence that the agreement led to higher prices was inadequate to demonstrate sufficient anticompetitive harm.[218] Ultimately, the court decided that Spahr had not appropriately pleaded a cause of action against Leegin.[219]

This trend has gained traction in other jurisdictions as well.[220] In *Jacobs v. Tempur-Pedic International, Inc.*,[221] the Eleventh Circuit applied a two-step analysis when evaluating whether the plaintiff's pleadings were sufficient.[222] In his complaint, the plaintiff alleged the existence of an anticompetitive price-fixing agreement between a mattress manufacturer and its distributor.[223] According to the court, the first step of the analysis calls for a determination of "whether the

211. *Id.* at 417.
212. *Id.* at 419.
213. *Id.* at 419–20.
214. *Id.*
215. *See* Spahr v. Leegin Creative Leather Prods., Inc., No. 2:07-CV-187, 2008 WL 3914461, at *1 (E.D. Tenn Aug. 20, 2008).
216. *Id.* at *2–3.
217. *Id.* at *11.
218. *Id.* at *11–12.
219. *Id.* at *16.
220. *See, e.g.*, Brantley v. NBC Universal, Inc., 675 F.3d 1192 (9th Cir. 2012); Jacobs v. Tempur-Pedic Int'l, Inc., 626 F.3d 1327 (11th Cir. 2010).
221. 626 F.3d 1327 (11th Cir. 2010).
222. *Id.* at 1333 (citing Ashcroft v. Iqbal, 556 U.S. 662, 679 (2009)).
223. *Id.* at 1331–33.

complaint's averments are more than bare legal conclusions," and the second step involves "examin[ing] the complaint for a sufficient quantum of allegations to plausibly suggest" that a vertical agreement to restrain trade existed and violated the Sherman Act.[224]

The court found that the pleadings satisfied the first step of the process but did not adequately identify the relevant market and, therefore, could not satisfy the second step.[225] Jacobs defined the relevant market as "visco-elastic foam mattresses" in the complaint but did not provide any factual economic data about the consumer demand for these mattresses.[226] The Eleventh Circuit acknowledged that a subset of a larger market can be identified as the relevant market, but only when there is a separate consumer demand for the product, and this demand must be pleaded in accordance with *Twombly*.[227] The court then noted that even if Jacobs had properly defined the relevant market, the complaint still would not have satisfied *Twombly* because it failed to provide more than "bald statement[s]" alleging anticompetitive harm and market power.[228]

Then in 2011, the Ninth Circuit jumped on board with this trend in *Brantley v. NBC Universal, Inc.*, when it held that merely pleading general harm to consumers, namely higher prices, was insufficient to survive a motion to dismiss.[229] Instead, the Ninth Circuit required the plaintiffs to point to a specific injury to competition.[230] In *Brantley*, a class of plaintiffs asked the Ninth Circuit to reverse the district court's 12(b)(6) dismissal for failure to state a valid claim.[231] The plaintiffs, a class of television subscribers, alleged that television programmers and distributors had violated Section 1 of the Sherman Act by bundling channels and effectively compelling consumers into purchasing multi-channel packages.[232] The Ninth Circuit stated that plaintiffs "may not substitute allegations of injury to the claimants

224. *Id.* at 1333.
225. *Id.* at 1333, 1336.
226. *Id.* at 1338.
227. *Id.* at 1337–38.
228. *Id.* at 1339–40.
229. 675 F.3d 1192, 1098–99 (9th Cir. 2012). The Ninth Circuit first decided *Brantley* in June 2011 but later withdrew the opinion and issued the superseding opinion cited in this Article. *Brantley v. NBC Universal, Inc.*, 649 F.3d 1078, 1081 (9th Cir. 2011) *opinion withdrawn,* 661 F.3d 1199 (9th Cir. 2011) and *superseded,* 675 F.3d 1192 (9th Cir. 2012).
230. *Id.*
231. *Id.* at 1195–96.
232. *Id.*

for allegations of injury to competition."[233] The court then found that the television subscribers had not claimed a sufficient injury to competition by merely pointing out that the bundles hurt consumers through reducing choice and increasing prices.[234] Although the court acknowledged that an industry-wide practice is more likely to be anticompetitive and should therefore be scrutinized more carefully, it refused to delve any deeper because the subscribers had not adequately explained in their pleadings how this widespread practice harmed competition.[235]

However, a few cases have proven that sufficiently pleading a vertical-restraint violation is possible.[236] For instance, in *Babyage.com, Inc. v. Toys 'R' Us, Inc.*,[237] the plaintiffs survived a motion to dismiss after alleging an anticompetitive price-fixing agreement.[238] There, Toys 'R' Us entered into agreements with product manufacturers to ensure that the manufacturers would impose minimum resale-price restraints on their retailers in order to prevent smaller retailers from undercutting Toys 'R' Us's prices.[239] In denying the motion to dismiss, the court stated that plaintiffs had pleaded their claim—by defining the relevant market, identifying concerted action, proving the anticompetitive nature of the action, and establishing a causal nexus—with enough "heft" to satisfy *Twombly*.[240] However, following the court's denial of the motion to dismiss, the parties settled the case, and the court never determined Toys 'R' Us's liability under the rule of reason.[241]

233. *Id.* at 1200.
234. *Id.* at 1201–02.
235. *Id.* at 1203–03.
236. *E.g.*, Babyage.com, Inc. v. Toys "R" Us, Inc., 558 F. Supp. 2d 575 (E.D. Pa. 2008).
237. *Id.*
238. *Id.* at 580–84.
239. *Id.* at 579.
240. *Id.* at 579–84.
241. Amaris Elliott-Engel, *$35 Million Settlement Approved in Baby Products Antitrust Class Action*, PITTSBURG POST-GAZETTE (Jan. 16, 2012, 12:00 AM), http://www.post-gazette.com/pg/12016/1203332-499.stm. This demonstrates a common trend that, even when plaintiffs have stated an antitrust injury sufficient to survive a motion to dismiss, they often settle to avoid the expense of continued litigation and uncertainty under the rule of reason. Heather M. Cooper, *What a 'Babies "R" Us' Class Action Lawsuit Can Teach Us About Successful Distribution Strategies for the Current Legal and Economic Climate*, ANTITRUST L. BLOG (Sept. 3, 2009), http://www.antitrustlawblog.com/2009/09/articles/what-a-babies-r-us-class-action-lawsuit-can-teach-us-about-successful-distribution-strategies-for-the-current-legal-and-economic-climate/. The concern with this trend is that plaintiffs are not being adequately compensated for the damage that vertical restraints inflict. *Id.*

In sum, the subsequent history of *Leegin* and the *Spahr*, *Jacobs*, and *Brantley* line of cases demonstrate the difficulty that plaintiffs currently encounter at the pleading stage in the wake of *Twombly* and *Leegin*. In most of these cases, the plaintiffs were not able to overcome the initial burden of proof, and, unfortunately, this is becoming the norm for plaintiffs attempting to allege an antitrust violation under the rule of reason. *Babyage* proves that, while difficult, plaintiffs can successfully plead an unreasonable restriction on competition under the rule of reason. However, even when plaintiffs survive a motion to dismiss, they often enter into settlement agreements, as seen in *Babyage*, because both parties recognize the costs and risks associated with undertaking a full rule of reason analysis at trial.[242] In either case, empirical evidence seems to suggest that, under the rule of reason, nearly all plaintiffs lose on motions to dismiss because they have not sufficiently pleaded an antitrust injury.[243] Given this, it is arguable that a heightened pleading standard has contributed to the per se legality of vertical restraints.[244]

B. Pleading Vertical Agreement and Horizontal Collusion: Not a Plaintiff's Saving Grace

The Supreme Court's earliest decisions concerning vertical price fixing reflected the belief that such restraints enabled manufacturers and retailers to conspire with each other or, in other words, to engage in horizontal price fixing.[245] One of the most prominent criticisms of evaluating vertical restraints under the rule of reason is that vertical restraints, specifically price restraints, increase horizontal collusion among competitors and can lead to more stabilized cartels among dealers and manufacturers.[246] A few antitrust scholars even contend that the distinction between horizontal and vertical conduct is nonsensical.[247] They argue that the relevant inquiry should not be whether one entity "imposed" a restriction on another entity but

242. Stucke, *supra* note 10, at 1424.
243. *Id.* at 1423.
244. *See* Liebeskind & Tiffany, *supra* note 92, at 2.
245. *See Change in Circumstance*, *supra* note 69, at 1602; *see, e.g.*, Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).
246. PITOFSKY ET AL., *supra* note 2, at 607.
247. *See* Lemley & Leslie, *supra* note 14, at 1238–39.

rather whether the restriction operates in an anticompetitive manner.[248]

Parties often implement horizontal and vertical restraints, specifically price fixing, with the same goals in mind—to increase profits and reduce competition.[249] Therefore the existence of one type of restraint can promulgate the existence of the other.[250] Horizontal price fixing results from vertical price fixing because manufacturers lose their incentive to undercut each other's prices as vertical price fixing stabilizes prices across the market.[251] If an industry-wide standard for resale pricing exists, manufacturers will prefer to maintain the status quo in order to continue taking advantage of higher profit margins.[252] Engaging in price competition by lowering prices no longer drives up a manufacturer's sales volume; instead, it only causes that manufacturer's profits to suffer.[253] This is because when price maintenance agreements regulate what price retailers may charge, retailers can no longer pass any reduction in a manufacturer's wholesale price along to consumers.[254] Therefore, in markets rife with resale price maintenance, the only beneficiaries of undercutting are retailers, and competition at the manufacturer level suffers as a result.[255] The capacity for vertical restraints to disguise horizontal collusion creates a conspicuous hazard that per se illegal conduct is going undetected.

1. Horizontal vs. Vertical: The Significance of Categorization

Before the Court overruled *Dr. Miles* and *Schwinn*, the horizontal ramifications of vertical restrictions were immaterial to the standard of analysis because both horizontal and vertical restraints were considered illegal per se. However, once the Court changed the standard for vertical restraints to the rule of reason, discerning what type of conduct was at issue became essential to

248. *Id.*
249. Taralson, *supra* note 51, at 581–82.
250. *Id.*
251. *See Change in Circumstance*, *supra* note 69, at 1605.
252. Kelly, *supra* note 4, at 627.
253. *Change in Circumstance*, *supra* note 69, at 1605.
254. Robert Pitofsky, *In Defense of Discounters: The No-Frills Case for a* Per Se *Rule Against Vertical Price Fixing*, 71 GEO. L.J. 1487, 1490–91 (1983).
255. *See id.*

determining legality.[256] This can be directly attributed to the weight that characterizing a restraint as horizontal or vertical has on the outcome of a case—plaintiffs win under the per se rule and almost always lose under the rule of reason.[257] Accordingly, plaintiffs attempt to trigger a per se standard by fitting the restraint into a "forbidden box," and meanwhile defendants work to keep it out of such a box and subject to a more lenient rule of reason analysis.[258] Inevitably, categorization has become the primary concern of litigants, thereby making it imperative for courts to ensure that vertical restraints are not used as a pretense to conceal an innately unlawful horizontal conspiracy.[259]

However, determining when vertical agreements buttress horizontal collusion is no easy feat.[260] In *Sylvania*, the Court recognized that, at times, courts may struggle to distinguish between horizontal and vertical restraints.[261] The pleading requirements set forth in *Twombly* require that plaintiffs clearly allege the existence of a horizontal agreement before a court can consider applying the per se rule.[262] Therefore, alleging horizontal conspiracy is especially difficult in cases where there is merely concerted action but no explicit agreement.[263] In particular, vertical price maintenance is extremely challenging to prove due to the ease with which competitors are able to enter into an unspoken agreement by just monitoring each other's prices.[264]

Therefore, because characterizing a restraint as horizontal or vertical proves to be outcome determinative, plaintiffs have more incentive to classify restraints as horizontal whenever possible to take advantage of the per se analysis.[265]And although plaintiffs have typically had very little success overcoming motions to dismiss after *Twombly*, they have been triumphant when they prove that a

256. *See* Lemley & Leslie, *supra* note 14, at 1232–33.
257. *See id.*
258. *Id.*
259. *See id.*
260. *See* Kelly, *supra* note 4, at 627.
261. Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 58 n.28 (1977).
262. Bell Atl. Corp. v. Twombly, 550 U.S. 544, 548–49, 556–57 (2007); *id.* at 571–72 (Stevens, J., dissenting).
263. *See* Kelly, *supra* note 4, at 627.
264. *Id.*
265. *See* Comment, *Vertical Agreement as a Horizontal Restraint:* Centuro, Inc. v. United Cabinet Corp., 128 U. PA. L. REV. 622, 644–45 n.138 (1980).

horizontal conspiracy was disguised by vertical conduct.[266] For example, plaintiffs win when they can prove that vertical price fixing was the result of a horizontal agreement to fix prices.[267]

2. Pleading Horizontal Collusion Pays Off

Not long after *Leegin*, the Fifth Circuit clarified in *Tunica Web Advertising v. Tunica Casino Operators Ass'n.* that a vertical refusal to deal would be per se illegal if it resulted from a horizontal agreement among competitors.[268] In *Tunica*, an Internet-advertising agency held the rights to the domain address tunica.com.[269] The agency proposed to all of the casinos in Tunica County, Mississippi, that they could lease the rights to the address for $2,500 per month, meaning that when web browsers clicked on tunica.com, they would be redirected to the Tunica County Tourism Commission's website, which featured information about each of the casinos.[270] The casinos declined unanimously.[271] The Fifth Circuit explained that the industry-wide refusal to agree to the proposal was not a sufficient violation.[272] However, when the casinos subsequently entered into a "gentleman's agreement" refusing to deal with the agency for the purpose of rendering tunica.com worthless, the court found that the casinos had crossed from vertical conduct into a horizontal agreement to boycott.[273] The court then remanded the case with instructions that the district court reconsider whether the rule of reason was the appropriate standard for evaluating this type of horizontal group boycott.[274] In doing so, the court stressed that *Leegin* required the per se rule only when "courts can predict with confidence that it would be invalidated in all or almost all instances under the rule of reason."[275]

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266. Peter Sullivan & Craig Linder, *Vertical Restraints*, *in* 48TH ANNUAL ADVANCED ANTITRUST SEMINAR: DISTRIBUTION & MARKETING VOLUME ONE 45, 69–70 (2009).

267. *Id.*

268. 496 F.3d 403, 406–08, 411–15 (5th Cir. 2007).

269. *Id.* at 406.

270. *Id.* at 407.

271. *Id.*

272. *Id.* at 410.

273. *See id.* at 410–11, 414.

274. *Id.* at 414–15.

275. *Id.* at 414 (quoting Leegin Creative Leather Prods. v. PSKS, Inc., 551 U.S. 877, 886–87 (2007)) (internal quotation marks omitted).

Shortly after the Supreme Court decided *Leegin*, a district court in the Eastern District of Wisconsin applied the per se rule to a statute that encouraged both vertical and horizontal agreement in *Lotus Business Group, LLC v. Flying J Inc.*[276] In *Flying J*, a gasoline retailer alleged that a competitor had violated a Wisconsin statute requiring gasoline retailers to increase their resale price by at least 9.18 percent.[277] The competitor asserted as an affirmative defense that the enforcement of the statute violated the Supremacy Clause by establishing price fixing in contravention of the Sherman Act.[278] The court agreed that the statute constituted an antitrust violation and subjected it to per se analysis.[279] Following *Leegin*, the district court reconsidered the statute under the rule of reason, but it upheld its application of the per se rule, finding that the statute created horizontal price fixing by setting an industry-wide standard.[280] The court declared that it would still evaluate horizontal cartels as per se violations even when vertical price fixing was also involved.[281] Furthermore, the court said that the statute would be unlawful regardless of whether it was evaluated under the per se standard or the rule of reason because it constituted a vertical price-fixing agreement intended to facilitate a horizontal cartel.[282] The court also contrasted this situation with one in which only a few manufacturers, without market power, implement the practice, concluding that vertical price fixing deserves more careful scrutiny when many competing manufacturers adopt the practice or when there is a strong showing of market power.[283]

Similarly, the Fourth Circuit confirmed in *TFWS, Inc. v. Franchot* that horizontal price fixing would remain distinguishable from vertical price fixing and would continue to be illegal per se.[284] Following *Leegin*, the state of Maryland asked the Fourth Circuit to reevaluate whether it was appropriate to apply the per se rule to its liquor and wine price-setting regulations.[285] Maryland claimed that in

276. 532 F. Supp. 2d 1011, 1029 (E.D. Wis. 2007).
277. *Id.* at 1012.
278. *Id.* at 1012–13.
279. *Id.* at 1012, 1017–18.
280. *Id.* at 1028–29.
281. *Id.* at 1028.
282. *Id.*
283. *Id.* at 1027.
284. 572 F.3d 186, 192 (4th Cir. 2009).
285. *Id.* at 188.

Leegin the Supreme Court declared that all resale price maintenance would be subject to rule of reason analysis.[286] The Fourth Circuit refused to accept this argument because the Court considered only vertical restraints in *Leegin* and not horizontal price fixing like that being implemented by Maryland.[287] In reaffirming its earlier decision to apply the per se rule, the Fourth Circuit interpreted *Leegin* as confirming the importance of using the per se standard when evaluating horizontal agreements restricting competition.[288]

These cases indicate the willingness of courts to apply the per se rule when plaintiffs successfully establish that there is a horizontal agreement in effect. Thus, at least some courts seem capable of distinguishing between horizontal collusion and agreements among entities within the chain of distribution. However, not all courts are on the same page, and plaintiffs continue to struggle to meet the burden of proving horizontal conspiracy in cases where there is evidence of both horizontal and vertical agreements.

3. Not an Absolute: Courts Are Reluctant to Classify Restraints as Horizontal

Despite the success plaintiffs have had when they are able to establish that defendants' vertical restraints are actually horizontal in nature, the courts are reluctant to make such characterizations by merely implying that vertical restraints have horizontal repercussions.[289] In *Leegin*, the Supreme Court reminded the lower courts that horizontal behavior must be distinguished from vertical behavior and must continue to be evaluated under the per se standard.[290] This warning seems to be carrying some weight in the lower courts.[291] Lower courts have ensured that when there is evidence of a horizontal agreement among competitors to fix prices or eliminate competition, a per se standard is still appropriate.[292] However, some courts have refused to extend the per se exception to

286. *See id.* at 191.
287. *Id.* at 191–92.
288. *Id.*
289. Sullivan & Linder, *supra* note 266, at 71.
290. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 893 (2007).
291. *See, e.g.*, Toledo Mack Sales & Serv., Inc. v. Mack Trucks, Inc., 530 F.3d 204 (3d Cir. 2008); Spahr v. Leegin Creative Leather Prods., Inc., No. 2:07-CV-187, 2008 WL 3914461 (E.D. Tenn. Aug. 20, 2008).
292. *See Mack*, 530 F.3d at 225; *Spahr*, 2008 WL 3914461, at *4–6.

vertical restraints unless an explicit horizontal agreement exists.[293] This poses a problem for plaintiffs because oftentimes horizontal agreements are unspoken.[294] Additionally, courts sometimes choose to ignore certain horizontal relationships.[295] For instance, a horizontal aspect emerges in the relationship between a manufacturer and its retailers when the manufacturer chooses to sell its products directly to consumers and through independent retailers, but courts often find that this relationship does not warrant a per se approach.[296] Moreover, at least one court has refused to use the per se rule even when a manufacturer imposes vertical restraint for the sole purpose of strengthening illegal horizontal cartels.[297]

In deciding to dismiss *Spahr v. Leegin Creative Leather Products, Inc.*, the Eastern District of Tennessee rejected Spahr's assertion that the per se rule should apply because Leegin, as a distributor of its own products, had engaged in horizontal price fixing.[298] Spahr's argument was that because Leegin was a retailer of its own products, it should be viewed as a horizontal competitor to its independent retailers and thereby as a participant in a horizontal conspiracy to fix prices.[299] Citing the Sixth Circuit case *International Logistics Group, Ltd. v. Chrysler Corp.*,[300] the court stated that businesses operating under a dual-distribution system[301] do not open themselves up to horizontal liability when imposing restraints on independent distributors.[302] The court found that no horizontal scheme existed because antitrust laws do not prohibit businesses from selling their own products while simultaneously utilizing independent retailers, and Spahr had demonstrated no other evidence

293. *Mack*, 530 F.3d at 220–21; *Spahr*, 2008 WL 3914461, at *3–4.
294. *See* Kelly, *supra* note 4, at 627.
295. *See* Lemley & Leslie, *supra* note 14, at 1235–36.
296. *Id.* at 1236.
297. *Spahr*, 2008 WL 3914461, at *4.
298. *Id.* at *4, *15.
299. *Id.* at *5.
300. 884 F.2d 904 (6th Cir.1989).
301. In other words, a manufacture simultaneously distributes its own products to consumers directly and through other independent distributors. *Spahr*, 2008 WL 3914461, at *6 (stating that a dual distributor is a manufacturer who "operates a branch of dealership on the same market level as one or more of its customers" (citation omitted)).
302. *Id.*

of horizontal collusion.[303] Consequently, the court applied the rule of reason.[304]

Likewise, the Third Circuit found the rule of reason was the appropriate standard in *Toledo Mack Sales & Services, Inc. v. Mack Trucks, Inc.*,[305] despite recognizing the likelihood that a truck manufacturer's sole purpose for entering into agreements with its dealers was to support an agreement among the dealers not to compete.[306] One of Mack's dealers refused to comply with the terms of the agreement that limited the dealer to distributing trucks inside an assigned geographic territory.[307] The dealer alleged that the only reason Mack implemented the territorial restrictions was to support an agreement between its dealers to fix prices by agreeing not to compete with one another.[308] The Third Circuit explained that it would evaluate the agreement among the dealers according to the per se rule because the agreement involved collusion among horizontal competitors to set prices,[309] but it also explained that the agreements between Mack and its dealers would be subject to the rule of reason.[310] The Third Circuit, citing *Leegin*, stated that "the rule of reason analysis applies [to vertical agreements] even when . . . the plaintiff alleges that the purpose of the vertical agreement between a manufacturer and its dealers is to support illegal horizontal agreements between multiple dealers."[311]

As shown in the case law above, although the *Leegin* Court rejected the per se rule for all vertical restraints, plaintiffs have identified an approach that allows them to utilize the rule by proving that a vertical restraint is merely a pretext for a horizontal agreement.[312] This technique has offered some success to plaintiffs alleging that vertical restraints constitute antitrust violations. Nonetheless, this has not saved vertical restraints from per se legality because courts are reluctant, as seen in *Spahr* and *Mack*, to overextend this exception to all situations that exhibit both vertical

303. *Id.* at *7.
304. *Id.* at *7–8.
305. 530 F.3d 204, 225 (3d Cir. 2008).
306. *Id.* at 218–19.
307. *Id.* at 209–10.
308. *Id.* at 218–19.
309. *Id.* at 221.
310. *Id.* at 225.
311. *Id.*
312. Sullivan & Linder, *supra* note 266, at 70.

and horizontal undercurrents unless there is unambiguous evidence of horizontal conspiracy. In effect, this has limited the number of situations in which pleading horizontal conspiracy is a viable strategy for plaintiffs, and as vertical enforcement continues its decline into per se legality under the rule of reason, serious implications arise if illegal horizontal conduct is masquerading as vertical conduct.

C. Hitting the Wall: Plaintiffs' Difficulty Overcoming Economic Analyses

For the few plaintiffs fortunate enough to survive the pleading stages of an antitrust claim, the challenge is far from over. In order to win an antitrust claim under the rule of reason, the plaintiff must first convince the court that the anticompetitive consequences of the restraint outweigh the procompetitive benefits.[313] When determining whether the plaintiff has met this burden the court must undertake an in-depth economic analysis of the restraint, the relevant market, and the industry as a whole.[314] A constantly evolving economic market and ever-changing business realities complicate economic analyses.[315] Courts cannot employ a bright-line rule because the economy is so dynamic that the impact of a restriction can vary immensely within a particular market over time.[316]

The fact that the strength of antitrust enforcement has fluctuated with the political climate of the time further complicates the precision of courts' economic analyses.[317] Much to the dismay of antitrust scholars, political biases have, over time, led courts to become less suspicious of vertical restraints' anticompetitive effects.[318] This decrease in skepticism, in conjunction with the

313. Stucke, *supra* note 10, at 1385–86.

314. *Id.*

315. *See Change in Circumstance*, *supra* note 69, at 1600–10 (discussing the impact that the advent of the internet has had on doing business).

316. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 905 (2007). The Court explained that it is important that "our antitrust doctrines 'evolve with new circumstances and new wisdom.'" *Id.* (citation omitted).

317. *See* PITOFSKY ET AL., *supra* note 2, at 2.

318. *See Leegin Creative Leather Prods., Inc.*, 551 U.S. at 877; *see also* Saami Zain, Quanta *Leap or Much Ado About Nothing? An Analysis on the Effect of* Quanta v. LG Electronics, 20 ALB. L.J. SCI. & TECH. 67, 115 (2010) ("In recent times, however, courts and commentators have grown less suspicious of vertical restraints, and specifically, whether they are likely to be anticompetitive.").

Supreme Court's concern for producing too many false positives,[319] prompted the Court to switch from per se illegality to the rule of reason in *Sylvania* and *Leegin*.[320] But recently, skepticism has surfaced as to whether courts are able to properly weigh the competitive impact of vertical restraints under the rule of reason. If, in practice, the courts never find that anticompetitive effects outweigh procompetitive justifications, a real concern arises that courts are not conducting proper economic analyses.

1. Operating on Uncertainty: Can Courts Properly Evaluate Economic Impact?

The courts' ability to conduct an accurate economic analysis and correctly predict how business practices will influence competition is essential to effective antitrust enforcement.[321] In *Leegin*, the Supreme Court acknowledged that the lower courts did not have adequate experience weighing the procompetitive and anticompetitive impacts of resale price maintenance.[322] In fact, the Court implied that this was one of its primary reasons for overturning the per se standard and implementing the rule of reason instead.[323] In order to conduct an effective economic analysis, courts must possess "the ability to understand, apply, and explain microeconomics and industrial organization theory . . . to . . . specific real-world situation[s]."[324] Unfortunately, courts typically are not equipped with the skills needed to identify the actual economic impact, and the nature of the adversarial system only complicates matters more so.[325]

319. A false positive occurs when a court finds conduct that does not actually harm competition to be anticompetitive. False positives typically arise as the result of over enforcement and per se rules. *See* Wright, *supra* note 16, at 3 n.10 (stating that an example of a false positive would be when a firm is falsely accused of an antitrust violation); *see also* Harbour, *supra* note 29, at 15 (referring to false positives as "Type I" errors).

320. Stucke, *supra* note 10, at 1407–08.

321. Abbott B. Lipsky, Jr., *Improving Competitive Analysis*, 16 GEO. MASON L. REV. 805, 805–06 (2009).

322. *See* Leegin Creative Leather Prods., Inc., 551 U.S. at 894–98.

323. *See id.*

324. Lipsky, *supra* note 321, at 806.

325. *Id.* ("[J]udges are almost never appointed based on their credentials as microeconomists."); *see also* Stucke, *supra* note 10, at 1440 ("Weighing a particular restraint's competitive benefits and harms, however, is often beyond the litigants', [and] the judiciary's . . . capacity.").

a. Complications in appraising the value of a restraint's procompetitive justifications

Over time, courts have accumulated limited experience in performing accurate economic and competitive analyses but have not fully developed the ability to understand real-world markets or predict future competitive effects.[326] Indeed, as one antitrust scholar noted:

> Economists, much less judicial fact-finders, are ill-equipped to quantify the value of different forms of competition, such as inter- and intrabrand competition, static versus dynamic efficiency, and a restraint's impact on that competition. Even if such weighing were feasible, no consensus exists on the relative weights for each factor. In certain industries, society may seek to promote innovation (dynamic efficiency) more than lower prices (static efficiency). Moreover, the weighing ignores the distributional effects of the challenged restraint . . . [because] the fact-finder does not consider whether one group bears the brunt of anticompetitive effects over time.[327]

Partly, this inexperience can be attributed to the fact that earlier antitrust cases rarely required such an in-depth economic analysis as is presently required.[328] Further, courts have dismissed many cases for failure to state a claim before they have actually performed an economic analysis, and in the few cases that survive motions to dismiss, the parties often settle before the court conducts its analysis.[329] Additionally, courts have not explicated which policy considerations should trump others when weighing a restraint's effects on competition.[330]

If courts are overvaluing the procompetitive benefits and undervaluing the anticompetitive harms of vertical restraints, there is a real concern that they are not balancing the competitive impacts accurately. In particular, courts may be giving too much weight to arguments that vertical restraints are permissible because they have

326. Lipsky, *supra* note 321, at 806.
327. Stucke, *supra* note 10, at 1442.
328. Lipsky, *supra* note 321, at 805–06.
329. *Id.* at 805; *see* discussion *supra* Part III.A.
330. *See* Stucke, *supra* note 10, at 1441.

the potential to promote interbrand competition and combat free riders.[331] If these justifications are not as persuasive as the Court has deemed, the rule of reason is groundlessly excusing anticompetitive restraints.

i. Undervaluing the benefit of intrabrand competition

Traditionally, economists have neglected to investigate the competitive significance of intrabrand competition.[332] The Supreme Court has openly proclaimed that promoting interbrand, and not intrabrand, competition is the "primary concern of antitrust law."[333] The result seems to be that courts have chosen to overlook the consequences that arise from limiting intrabrand competition based on the assumption that the increase in interbrand competition is more desirable.[334] But this apathy toward intrabrand competition may be misguided, and eliminating intrabrand competition may not be as benign as economists have conventionally believed.[335]

Intrabrand competition encourages entities at the same level of distribution to compete for sales margins and market shares, which eventually leads to lower prices for consumers.[336] This is not to say that the need for intrabrand competition will always negate an increase in interbrand competition, but it is certainly a consideration that courts need to delve into more deeply than they have in the superficial investigations they have conducted in the past.[337] A blanket statement that interbrand competition outweighs intrabrand competition is dangerous because it distracts courts from evaluating the actual market impact of intrabrand competition.

331. *See* Harbour, *supra* note 29, at 11–14 (explaining how the Chicago School's views often undervalue or ignore the anticompetitive effects of eliminating intrabrand competition); Lao, *supra* note 165, at 512 (questioning the extent of the free-rider problem).

332. *See* Harbour, *supra* note 29, at 10–11.

333. *See* Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 724 (1988) (citing Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 52 n.19 (1977)).

334. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 895–96 (2007); *Bus. Elecs. Corp.*, 485 U.S. at 724–25; *Cont'l T. V., Inc.*, 433 U.S. at 51–52 & 52 n.19.

335. Harbour, *supra* note 29, at 13–14.

336. *Id.* at 4–5, 12.

337. *See id.* at 11.

ii. Overestimating the prevalence of free riding

Likewise, procompetitive justifications that vertical restraints fight free riders may be as blindly glorified as the importance of interbrand competition.[338] When purchasing goods, consumers often value, and are prepared to pay more for, services such as in-store salespersons, live dealer demonstrations, and attractive storefronts.[339] Therefore, manufacturers usually desire that their retailers provide those additional services to customers during the sale of their products, and, in turn, their retailers charge consumers higher prices.[340] Free riding occurs when, after using one retailer's services, consumers ultimately purchase the product at a lower price from another retailer who does not provide those services.[341] For example, a consumer may go to an expensive retail store offering live demonstrations to research a product but then go to a discount warehouse to purchase it. In this example, the warehouse would be "free riding" on the services provided by the retail store. Free riding is a problem because it eliminates retailers' incentive to offer the services altogether.[342] In the end, consumers and manufacturers suffer because retailers cease to offer the services or discontinue the sale of the product.[343]

Proponents of vertical price fixing are adamant that it decreases the prevalence of free riding.[344] Resale price fixing ensures that a discount retailer—the free rider—does not undercut the price of a retailer selling the same product and offering additional services, thereby eliminating the motivation for consumers to buy the product from the discount retailer.[345] However, many economists oppose this argument, and there is virtually no empirical evidence demonstrating that free riding is as rampant as the supporters of vertical price fixing claim.[346] In fact, free riding may materialize only in the sale of expensive or complex products—products that require some sort of

338. Lao, *supra* note 165, at 478–79.
339. *Change in Circumstance*, *supra* note 69, at 1606–07.
340. PITOFSKY ET AL., *supra* note 2, at 608–09.
341. *See, e.g.*, *Change in Circumstance*, *supra* note 69, at 1614–15.
342. *Id.* at 1607.
343. *See id.*
344. *See id.* at 1606.
345. *See, e.g.*, *id.* at 1607.
346. Lao, *supra* note 165, at 478–79 (citing to, among others, antitrust scholars Robert Pitofsky, Kevin Arquit, and Stanley Ornstein).

interaction with a salesperson.[347] Yet there are a multitude of everyday products that do not require services of any sort and, as such, are not susceptible to free riding but remain subject to price maintenance nonetheless.[348] If economists cannot agree about the extent of free riding or whether it is actually a legitimate reason for restraining trade, how can we expect the courts to make a judgment call about its impact?

b. Battling experts, high costs, and other deficiencies of the adversarial system

To complicate matters even more, the lower courts have been exposed to economic analysis only in the context of adversarial proceedings.[349] During litigation, parties present customers and documents that support their position with respect to the challenged restraint.[350] Furthermore, "motivated advocates," including lawyers and experts, assert economic theories supporting their position with "towering confidence," often forgoing unbiased reflection and impartial explanations.[351]

When courts are asked to determine a restraint's impact on competition, they typically turn to "neoclassical economic theories," which are based upon the assumption that "profit-maximizing market participants pursue their economic self-interest with perfect knowledge and willpower."[352] Unfortunately, actual behavior rarely coincides with theoretical behavior.[353] Individuals do not have a "perfect knowledge" of economics, and no single definition of perfect competition exists because it varies so greatly across different product markets.[354] Because of the disparity among economists, the trials result in a "battle of the experts,"[355] as the parties retain experts to demonstrate the so-called actual impact of the challenged

347. *Id.* at 479 (giving examples of advanced audio and video equipment as a complex products).

348. *Id.* at 479–80 (describing products that do not require services but remain subject to price fixing to include "boxed candy, pet foods, jeans, vitamins, shampoo, [etc]").

349. *See* Lipsky, *supra* note 321, at 806.

350. Stucke, *supra* note 10, at 1427.

351. Lipsky, *supra* note 321, at 806.

352. Stucke, *supra* note 10, at 1426.

353. *Id.* at 1426–27.

354. *Id.*

355. Kelly, *supra* note 4, at 640.

restraint.[356] However, this approach carries some serious infirmities. First, these experts rarely have practical work experience in the industry at issue and thus base their testimonies not on actual business realities but on theoretical economics.[357] Furthermore, the court is then asked to evaluate each party's skewed position based on only its basic and limited understanding of economics to determine which theory it believes is more likely to be accurate.[358]

Of course, the trial judge can mitigate the potential for error by scrutinizing an expert's testimony before it is presented to ensure that it has a reliable foundation and is relevant to the economic analysis.[359] However, "judges are almost never appointed based on their credentials as microeconomists" and their understanding of valid economic theories is limited.[360] Additionally, judges are often able to dictate the outcome of a case being decided under the rule of reason by relying on their subjective biases.[361] Granting judges the ability to foreclose or insist upon the admittance of expert testimony only augments their tendency to "jealously guard their prerogative[s]" by allowing them to decide what theories will be entertained at trial.[362] In this way, judges may exclude from consideration any testimony that would be contrary to their interests.[363] Thus, judges may not be able to adequately fulfill their role as gatekeepers in antitrust cases.

Another obstacle that plaintiffs commonly encounter with the judicial system is the high cost of litigation.[364] The Supreme Court has acknowledged that antitrust cases are particularly protracted and expensive, especially when the rule of reason applies.[365] This is

356. Stucke, *supra* note 10, at 1427.

357. *Id.*

358. Kelly, *supra* note 4, at 640; Stucke, *supra* note 10, at 1427.

359. Daubert v. Merrell Dow Pharm., Inc., 509 U.S. 579, 597 (1993).

360. Lipsky, *supra* note 321, at 806.

361. *See supra* Part III.C.3.

362. John E. Lopatka & William H. Page, *Economic Authority and the Limits of Expertise in Antitrust Cases*, 90 CORNELL L. REV. 617, 621 (2005).

363. *Id.*

364. Kelly, *supra* note 4, at 636.

365. *See* Stucke, *supra* note 10, at 1461–62 (citing to Bell Atl. Corp. v. Twombly, 550 U.S. 544, 558–59 (2007); Nw. Wholesale Stationers v. Pac. Stationery & Printing Co., 472 U.S. 284, 289 (1985); Arizona v. Maricopa Cnty. Med. Soc'y, 457 U.S. 332, 343 (1982)); *see also* Kelly, *supra* note 4, at 636 (explaining that because discovery and other pre-trial costs are extremely expensive in rule of reason cases, plaintiffs are often prompted to forgo filing a suit altogether or to settle early on).

directly attributable to the fact-intensive nature of the economic analysis required by the rule of reason.[366] The high cost of litigation causes some anxiety because, as one scholar noted, "if it is too costly to vindicate one's legal rights, the law is majestic in theory, but impractical in reality."[367] Consequently, plaintiffs will think twice about pursuing a suit when they perceive that the costs will outweigh the benefits, causing an already wavering level of enforcement to plummet even further.[368]

2. Picking and Choosing: The Court Recognizes Change, but Ignores Reality

Since the Sherman Act's inception in 1890, business practices have changed, perhaps most significantly due to the emergence of the Internet and discount wholesaler chains.[369] While the Court in *Leegin* did not directly address why courts could not perform an adequate competitive analysis, the underlying theme was that because the economic realities have changed dramatically over the last century, the anticompetitive harm was no longer as apparent as it once had been.[370] The Court, however, neglected to consider how these constantly evolving economic and business dynamics might only further confuse courts about how to conduct an accurate economic analysis. It is thus necessary to understand how these changes impact business before evaluating their effects on courts' economic analyses.

a. Emergence of the Internet

There is no doubt that the Internet has changed the way that people do business. Businesses have increasingly relied on the Internet to conduct day-to-day operations, including advertising, customer services, sales transactions, and communications.[371] Between 2002 and 2007, Internet sales increased by over 23 percent each year while total retail sales increased by only 5 percent each

366. Stucke, *supra* note 10, at 1462.
367. *Id.* at 1460.
368. *See id.*
369. *See Change in Circumstance*, *supra* note 69, at 1600–01.
370. *See id.*
371. *See* U.S. CENSUS BUREAU, E-STATS: E-COMMERCE 2009 1 (2011), *available at* http://www.census.gov/econ/estats/2009/2009reportfinal.pdf.

year.[372] The Internet is particularly appealing to consumers because they are no longer constrained to shopping during store hours or to purchasing from retailers within their geographic locations.[373] As a result, they have greater access to more shopping options than ever before.[374] Accordingly, consumers have more opportunities to obtain lower prices or purchase unusual goods.[375]

Nevertheless, the Internet has become one of the most troublesome issues for businesses seeking to impose vertical restrictions today.[376] Specifically, the Internet poses new and worrisome challenges to manufacturers due to the ease with which consumers can access pricing information for competing goods.[377] Internet retailers are more often thought to free ride on brick-and-mortar retailers because they have lower overhead costs, offer lower prices, and generally do not offer the same services that brick-and-mortar stores do.[378] As a result, the accessibility provided by the Internet is a major reason why vertical price fixing has become a more desirable business practice for manufacturers in recent years.[379]

While price is not consumers' sole concern when making purchases—picking trustworthy retailers has proven to be an important consideration—Internet shoppers are particularly price aware.[380] Due to the availability of product information online, consumers have changed their shopping habits.[381] Today, consumers often research products on the Internet before purchasing them from a retail store.[382] As a result, retail storefronts and customer service have become less important to consumers' decisions to purchase.[383] Unfortunately for rivaling retailers, Internet accessibility enables users to compare prices among retailers more easily, which has the

372. Lao, *supra* note 165, at 483.
373. *Id.* at 485–86.
374. *See id.*
375. *Id.* at 485. The lack of geographic restraints is particularly beneficial to "consumers living in communities without sufficient population to support a robust local retail market" and "buyers with less common needs." *Id.*
376. *Change in Circumstance*, *supra* note 69, at 1601.
377. *Id.*
378. Lao, *supra* note 165, at 482.
379. *See Change in Circumstance*, *supra* note 69, at 1601.
380. *Id.* at 1613–14.
381. *Id.*
382. Lao, *supra* note 165, at 493.
383. *Change in Circumstance*, *supra* note 69, at 1614.

potential to harm competition in numerous ways.[384] First, it can cause an increase in free riders.[385] Second, it can improve the ability of retail cartel participants to monitor other cartel participants[386] because price cutting becomes more obvious.[387] Finally, it increases the strength of horizontal relationships when manufacturers decide to sell online instead of solely through retailers.[388]

The ease of comparing prices directly correlates to the prevalence of free riding.[389] The Internet encourages free riding because consumers who desire a high level of customer service can merely visit the brick-and-mortar store before returning home to locate the lowest price among online retailers.[390] Consumers are no longer geographically constrained and can easily peruse numerous retailers for the best deal without the hassle of driving from store to store.[391] However, the belief that the Internet encourages free riding on brick-and-mortar retailers is controversial—and recent studies have yielded results indicating that free riding is occurring in the opposite direction more frequently.[392] Due to the volume of information accessible via the Internet, consumers may research a product over the Internet before travelling to the brick-and-mortar

384. *See id.* at 1612.

385. *Id.* at 1612, 1615; *see* Lao, *supra* note 165, at 482.

386. "Cartels are associations of firms that restrict output or set prices. They may divide markets geographically, allocate customers, rig bids at auctions, or restrict nonprice terms. They have often been formed with the participation or support of state actors." MARGARET C. LEVENSTEIN & VALERIE Y. SUSLOW, THE NEW PALGRAVE DICTIONARY OF ECONOMICS ONLINE (Steven N. Durlauf & Lawrence E. Blume eds., 2d ed. 2008).

387. *Change in Circumstance*, *supra* note 69, at 1612, 1617–18.

388. *Id.* at 1612, 1618–19.

389. *Id.* at 1615.

390. *Id.*

391. Lao, *supra* note 165, at 488–89.

392. *Id.* at 476. However, some economists believe that even if brick-and-mortar stores do free ride on Internet retailers, the cost of free riding is more detrimental to brick-and-mortar retailers than to online retailers. *See Change in Circumstance*, *supra* note 69, at 1615–16 (explaining that Internet retailers have fixed costs while brick-and-mortar stores' costs are variable and depend on the cost of employing sales associates and the investment of maintaining a physical storefront). This is because consumers are always forced to pay full price at brick-and-mortar stores regardless of whether the consumer desires the services or benefits from the services. *See The Discount Pricing Consumer Protection Act: Do We Need to Restore the Ban on Vertical Price Fixing?: Hearing Before the Subcomm. on Antirust, Competition Policy And Consumer Rights of the S. Comm. on the Judiciary,* 111th Cong. 141 (2010) [hereinafter *Hearings*] (statement of James Wilson, Chairman, Antitrust Section of the Am. Bar Ass'n) (explaining that "while some services may benefit consumers as well as manufacturers, other services provide little or no benefit to consumers even though resale price maintenance can be expected to elevate the price that some consumers pay").

store to purchase it.[393] Research also indicates that free riding can be synergistic—simultaneously benefitting both brick-and-mortar and Internet retailers—in that as internet shoppers utilize the services of a brick-and-mortar store, they create an appearance of a more crowded store, which increases other shoppers' desires to purchase a product from that store and drives up the total sales of the store.[394]

Another concern with Internet accessibility is that the Internet encourages an increase in manufacturer and retail cartels.[395] An essential feature of successful cartels is the ability to detect when parties are not in compliance with the agreement.[396] Because prices are so readily available on the Internet, manufacturers and retailers can monitor price cutting behavior almost effortlessly, thereby increasing their ability to overesee retail and manufacturer cartels.[397] A final concern is that the Internet encourages retail cartels to form as manufacturers vertically integrate themselves into the chain of distribution.[398] Selling products via the Internet requires much fewer capital and upkeep costs, and, therefore, manufacturers may find establishing an Internet retail front to be a valuable business tactic.[399] Once a manufacturer decides to sell through its own website, it can engage in price fixing behavior with its retailers much more easily by preventing them from making Internet sales or by requiring them to sell at its set price.[400]

It is obvious that the Internet has changed the way people do business, but how it has affected competition is unclear. Therefore, how the courts should evaluate the impact the Internet has had on vertical restraints in an economic analysis is not intuitive. The Supreme Court could have addressed how the Internet might influence an economic analysis in *Leegin*, but instead it chose to leave this question unanswered—ensuring that the courts remain ill-equipped to weigh economic impacts.

393. Lao, *supra* note 165, at 490–91.
394. *Id.* at 476.
395. *Change in Circumstance*, *supra* note 69, at 1617.
396. *Id.*
397. *Id.*
398. *Id.* at 1618.
399. *See* Lao, *supra* note 165, at 482; *Change in Circumstance*, *supra* note 69, at 1611–12.
400. *Change in Circumstance*, *supra* note 69, at 1618.

b. Discount retailers' dominance

In recent decades, the retail industry has been significantly altered by the emergence of discount retailing and by the significant rise in the prominence of discount retail chains,[401] such as Wal-Mart, Target, and Costco.[402] Since the first discount store was established in the 1950s, discount retailers have grown substantially and now dominate the retail market.[403] The public has been extremely skeptical of the impact of these chains, and exactly how these discount retailers have impacted the economy and competition is uncertain.[404] Studies demonstrate that when a chain store enters the market, it renders roughly 50 percent of the single-firm discount stores unprofitable.[405] However, due to modeling difficulties, few empirical studies have been able to establish the precise impact of dominant retail chains.[406]

401. A discount retailer can be defined as "a departmentalized retail establishment that makes use of self-service techniques to sell a large variety of hard goods and soft goods at uniquely low margins." Panle Jia, *What Happens When Wal-Mart Comes to Town: An Empirical Analysis of the Discount Retailing Industry*, 76 ECONOMETRICA 1263, 1264 (2008).

402. *Id.*

403. *See id.* at 1263–64; *see also Company Dossier: Costco Wholesale Corporation*, LEXISNEXIS, http://0-www.lexisnexis.com.linus.lmu.edu/hottopics/lnacademic/?shr=t&sfi=AC02NBCmpDosSrch (last visited Nov. 13, 2011) (stating that Costco is the largest wholesale-club operator in the United States); *Company Dossier: Target Corporation*, LEXISNEXIS, http://0-www.lexisnexis.com.linus.lmu.edu/hottopics/lnacademic/?shr=t&sfi=AC02NBCmpDosSrch (last visited Nov. 13, 2011) (stating that Target is the United States's second-top discount retail chain); *Company Dossier: Wal-Mart Stores Inc.*, LEXISNEXIS, http://0-www.lexisnexis.com.linus.lmu.edu/hottopics/lnacademic/?shr=t&sfi=AC02NBCmpDosSrch (last visited Nov. 13, 2011) (stating that Wal-Mart is the world's top retailer).

404. *See* Jia, *supra* note 401, at 1264–65.

405. *See id.* at 1266. This can be attributed to a decline in customer demand for the higher priced product. Raymond Deneckere et al., *Demand Uncertainty, Inventories, and Resale Price Maintenance*, 11 Q. J. ECON. 885, 911 (1996). Discounters are able to charge lower prices because they are less likely to be stuck with unsold merchandise. *Id.* As retailers lose customers to discount retailers, they are forced to increase their markups, which inevitably leads to even more unsold merchandise and basically destroys customer demand for the marked-up products. *Id.*

406. Jia, *supra* note 401, at 1265. "'[A] mathematical model is a description of a process or a prediction about the end result of a process, expressed as an equation' or set of equations." Matthew W. Swinehart, *Remedying Daubert's Inadequacy in Evaluating the Admissibility of Scientific Models Used in Environmental-Tort Litigation*, 86 TEX. L. REV. 1281, 1284 (2008) (quoting ORRIN H. PILKEY & LINDA PILKEY-JARVIS, USELESS ARITHMETIC: WHY ENVIRONMENTAL SCIENTISTS CAN'T PREDICT THE FUTURE 24 (2007)). When there are too many variables in an equation, it becomes impossible to get an answer; therefore, if economists want to quantify economic impact through algorithms, they often have to make assumptions that cause certain variables to remain constant. *Id.* at 1288–93. However, these assumptions usually do not reflect real market conditions, and as a result, they can yield erroneous, sometimes even useless, numerical results. *Id.* The term "modeling difficulties" refers to these inaccuracies. *Id.*

If economists cannot pinpoint the impact that these retail chains are having on businesses, courts certainly are not better suited to making that determination. Yet, once again, the Supreme Court overlooked this problem, refused to identify how it might influence courts' analyses under the rule of reason, and left lower courts to find their own solutions.[407] Furthermore, because the Court realized that the lowers courts would likely be confused when evaluating the impact of retail chains, it cannot use its ignorance as an excuse for its failure to provide a framework for incorporating that impact into an economic analysis. In fact, during oral argument in *Leegin*, Justice Scalia acknowledged that discount retailers could be concerned with suffering from the economic implications of switching from per se illegality to the rule of reason.[408] However, Justice Scalia quickly, and perhaps misguidedly, dismissed this as a nonissue because, in his own words, if the discount retailers had a real gripe, "they would have been here."[409]

The Supreme Court was clearly correct when it said that both the economy and the way people conduct business have evolved since the Sherman Act's inception in 1890. However, when the Court defaulted to the rule of reason without providing additional guidance about how to conduct an appropriate economic analysis in light of these changes, it made a costly error—one that vertical-restraint plaintiffs are still paying for.

3. It All Comes Down to Politics: Subjective Bias as the Deciding Factor

Washington defines antitrust policy in two ways: the first is by interpreting and providing guidance on the laws made by the Department of Justice (DOJ) and the Federal Trade Commission (FTC), and the second is by enforcing cases filed by the DOJ and

407. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007).

408. Stucke, *supra* note 10, at 1459.

409. *Id.* (quoting Transcript of Oral Argument, Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007) (No. 06-480), 2007 WL 967030, at *31–32). Scalia noted that discount retailers—the Wal-Marts and the Targets—did not file amicus briefs and claimed that if they were really concerned about losing profits they would have petitioned as amici. *Id.* This comment raises an additional concern in that Justice Scalia seems to be encouraging rent seeking in future cases by stating that if businesses decline to petition the Court when their profitability is at issue in a case, they are essentially disclaiming any adverse economic impact. *Id.* at 1457–60 (discussing concerns of an increase in rent seeking behavior under the rule of reason).

FTC.[410] In addition, because the president appoints DOJ prosecutors and FTC commissioners,[411] a change in presidential administration can greatly influence antitrust enforcement, which is usually clear from the cases that the different administrations bring—or fail to bring.[412] This strong political influence creates a concern that an administration may not implement the laws faithfully because it has too much discretion to decide what conduct will be prohibited or permitted.[413] Thus, an administration's failure to enforce certain restraints can contribute to a standard of per se legality.

Different administrations have used antitrust enforcement to promote their own political objectives since the Reagan administration, when enforcement politics began to infiltrate enforcement schemes.[414] Before Reagan took office, the Republican Party predominantly endorsed antitrust enforcement, as reflected by the continuity with which the Republican and Democratic administrations had previously enforced the antitrust laws.[415] During the Reagan administration, however, the Republican Party departed from "overbearing regulation," and antitrust enforcement waned.[416] Under Reagan, the government actively pursued actions to eliminate predatory competitive pricing and price gouging but never prosecuted any vertical restraint or monopoly cases.[417] The Republican Party has maintained the laissez-faire attitude it adopted during the Reagan administration through the Bush Administration until today and, at times, has even been accused of abandoning antitrust enforcement altogether given its lax enforcement policies.[418]

When George W. Bush took office, he promised to enforce antitrust laws as forcefully as the Clinton administration had.[419] This

410. *See* Stephen Labaton, *Obama Takes Tougher Antitrust Line*, N.Y. TIMES (May 11, 2009), http://www.nytimes.com/2009/05/12/business/economy/12antitrust.html?pagewanted=all.

411. *About the Office*, DEP'T OF JUSTICE, http://www.justice.gov/ag/about-oag.html (last visited Nov. 12, 2011); *Commissioners*, FED. TRADE COMM'N, http://www.ftc.gov/commissioners/index.shtml (last visited Nov. 12, 2011).

412. *See* Stucke, *supra* note 10, at 1448–50.

413. *Id.* at 1450–51.

414. *Id.* at 1448–51.

415. *Id.* at 1450 n.324, 1451 n.326.

416. *See id.* at 1450 n.324.

417. *Id.* at 1452. The sole exception was a monopoly case against AT&T, which the Reagan administration settled in 1982. *Id.*; *see* United States v. Am. Tel. & Tel. Co., 552 F. Supp. 131 (D.D.C. 1982).

418. *Id.* at 1452–54 & n.337.

419. *Id.* at 1452–53.

proclamation, however, proved to be a sham.[420] Contrary to President Bush's assertion, merger enforcement declined by over 50 percent, and the DOJ did not prosecute a single monopoly case against a dominant firm during his administration.[421] This caused great dissatisfaction among the "press, antitrust scholars, politicians, and practitioners."[422] One antitrust scholar even commented that the Bush Administration's guidelines for enforcement were a "brief for defendants."[423] As previously noted, this statement has proven to be somewhat accurate as defendants rarely, if ever, lost antitrust cases judged according to the rule of reason during the Bush Administration.[424] Furthermore, it was under President Bush's administration that the Court took the final step in relaxing vertical enforcement by extending the rule of reason to vertical price fixing.[425] When antitrust enforcement seriously favors defendants, inadvertently defaulting to per se legality becomes a real concern.

Now with President Obama at the helm, antitrust enforcement agencies seem to be taking a tougher stance on anticompetitive practices. The discrepancy between the different political agendas of the Bush and Obama administrations and its impact on antitrust enforcement may be most apparent in the actions taken by the DOJ when Obama took office. In 2008, at the end of the Bush Administration, the DOJ issued guidelines on how to enforce predatory conduct by dominant firms.[426] The guidelines memorialized the Bush Administration's approach to enforcement[427] and were condemned by the FTC as "a blueprint for radically weakened enforcement."[428] Then, only a few months after the DOJ

420. *Id.* at 1453.

421. Senator Barack Obama, Statement of Senator Barack Obama for the American Antitrust Institute (Sept. 27, 2007), *available at* http://www.antitrustinstitute.org/files/aai-%20Presidential %20campaign%20-%20Obama%209-07_092720071759.pdf; *see also* Labaton, *supra* note 410 ("During the Bush Administration, the Justice Department did not file a single case against a dominant firm for violating the antimonopoly law.").

422. Stucke, *supra* note 10, at 1453–54 & n.337–40.

423. Labaton, *supra* note 410 (quoting Herbert Hovenkamp).

424. Lao, *supra* note 165, at 508. See *supra* note 172 and accompanying text.

425. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007) (subjecting all vertical restraints to a rule of reason analysis).

426. Steven Pearlstein, *Antitrust Challenges for the Obama Administration*, WASH. POST (May 17, 2009), http://www.washingtonpost.com/wp-dyn/content/article/2009/05/15/AR2009051502920.html.

427. Labaton, *supra* note 410 (quoting an unnamed FTC commissioner).

428. *Id.*

implemented the guidelines, the Obama administration took over the executive branch, and the DOJ rescinded those very guidelines.[429]

Currently, the Obama administration has maintained the level of enforcement that the Bush Administration claimed it would pursue.[430] The resurgence of enforcement under Obama is based on the belief that the Bush Administration disregarded the ultimate goals of antitrust law by implementing a policy that "effectively straightjacket[ed]" antitrust enforcement agencies and courts trying to rectify antitrust injuries, thereby allowing all but the "most bold and predatory conduct" to go unregulated.[431] The Obama administration has voiced a particular concern with this approach in light of the recent economic downturn and the importance of vigorously enforcing antitrust laws during economic crises.[432] Up to this point, Obama's administration has demonstrated an attitude geared toward revamping vertical enforcement as well.[433] It has voiced its support for legislation aimed at overturning *Leegin* and reverting to the per se treatment of minimum vertical price fixing.[434] While the extent to which the change in the presidential administration will strengthen vertical enforcement is still unclear, Obama has indicated a commitment to a more rigorous approach than that taken under President Bush, which may help to save vertical price fixing from per se legality.[435]

However, the executive branch is not the only branch of government that makes decisions based upon its political platforms, and thus plaintiffs should remain wary when seeking private enforcement.[436] Courts, including the Supreme Court, are not isolated from partisanship: Supreme Court justices are appointed by the executive branch and generally support their party's political platforms during their tenure.[437] Increasingly, business lobbyists are

429. Pearlstein, *supra* note 426.

430. Labaton, *supra* note 410 (discussing how Obama's "new enforcement policy reverses the Bush administration's approach").

431. *Id.* (quoting Christine Varney, former Assistant Attorney General for the Antitrust Division of the Department of Justice).

432. *Id.*

433. Quentin R. Wittrock & Jeremy L. Johnson, *Can Franchisors Control Franchisee Prices?*, 28 FRANCHISE L.J. 199, 243 (2009).

434. *Id.*

435. *See id.* at 243–44.

436. *See* Stucke, *supra* note 10, at 1456.

437. *See id.* at 1457 n.356.

becoming less concerned with changing legislation, choosing instead to turn their efforts toward influencing the courts.[438] In addition, vague standards, like the rule of reason, allow judges to introduce their personal ideological and political beliefs into antitrust analyses.[439]

A survey of Supreme Court justices' voting decisions between 1937 and 2006 revealed that Republican-appointed justices consistently voted more conservatively than Democratic-nominated justices.[440] This trend shows no sign of changing, as more-recent appointees have demonstrated an even greater propensity for voting according to their political ideologies.[441] At the conclusion of the 2007–2008 term, one commentator noticed that the Supreme Court followed the example set during recent terms and "once again sided in most cases with employers over employees, with big businesses over consumers, and with the government over individuals."[442] Then in 2010 another commentator noted that, in the previous six years, the Supreme Court had "become critical (or even somewhat hostile) to antitrust, having decided [only] eight antitrust cases—all having the effect of [further] weakening antitrust enforcement."[443] While this deterioration of antitrust enforcement is disquieting for plaintiffs, even more alarming is the fact that the Supreme Court heard eighteen antitrust cases during the sixteen years between 1993 and 2009 and did not rule for the plaintiff in a single one.[444]

As demonstrated above, the executive branch has the ability to dictate the level of antitrust enforcement through appointments to the FTC, DOJ, and judiciary, and therefore, an administration's political platforms can have serious repercussions on plaintiffs' chances of prevailing under the antitrust laws.[445] Thus, de facto per se legality of vertical restraints seems more likely to occur under a Republican administration, like President Bush's, than a Democratic

438. *Id.* at 1457.
439. *Id.* at 1456.
440. *Id.* at 1457 n.356.
441. *Id.*
442. *Id.* at 1458 (quoting Andrew Cohen, *Not Your Father's Court: Andrew Cohen Reviews the Decisions and Looks at Trends from the Past Supreme Court Term*, CBS NEWS (July 2, 2008), http://www.cbsnews.com/stories/2008/07/02/opinion/courtwatch/main4227922.shtml.
443. Zain, *supra* note 318, at 115. *Leegin* was one of these cases. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2006).
444. Stucke, *supra* note 10, at 1458.
445. *See supra* notes 410–444 and accompanying text.

administration, like Obama's. Unfortunately, although it seems plaintiffs can take some solace in the Obama administration's resolution to reinvigorate antitrust enforcement, the courts have yet to entirely adopt this sentiment, and thus, per se legality remains a concern.

Collectively, the Supreme Court's failure to articulate a clearer standard by which to conduct a competitive analysis, its ignorance of the constantly evolving economic and political climates, and the inherent deficiencies of the adversarial system have caused courts to consistently yield unpredictable results when applying the rule of reason.[446] At least once, the Court itself recognized the high likelihood that the rule of reason would produce inconsistent results:

> [A]ntitrust plaintiffs may bring lawsuits throughout the Nation in dozens of different courts with different nonexpert judges and different nonexpert juries. In light of the nuanced nature of the evidentiary evaluations necessary to separate the permissible from the impermissible, it will prove difficult for those many different courts to reach consistent results. And, given the fact-related nature of many such evaluations, it will also prove difficult to assure that the different courts evaluate similar fact patterns consistently. The result is an unusually high risk that different courts will evaluate similar factual circumstances differently.[447]

And the outcome of an economic analysis is not the only inconsistency under the rule of reason: courts differ as to how many steps exist for establishing liability, how encompassing those steps are, and which litigant shoulders the burden of proving them.[448] Additionally, some courts require plaintiffs to definitively identify the relevant market early on, while others bypass this requirement if

446. *Change in Circumstance*, *supra* note 69, at 1620.

447. Credit Suisse Sec. (USA) LLC v. Billing, 551 U.S. 264, 281–82 (2007); Stucke, *supra* note 10, at 1423.

448. Stucke, *supra* note 10, at 1432*; see also* Kelly, *supra* note 4, at 637 ("[I]t is not perfectly clear what criteria the court must use to judge a practice under the rule [of] reason, how each criterion should be judged, or how much weight to give each criterion considered."); *id.* at 637 n.331 (explaining that different requirements for demonstrating market power exist among the federal circuit courts); *see, e.g.*, FTC v. Ind. Fed'n of Dentists, 476 U.S. 447 (1986); NCAA v. Bd. of Regents, 468 U.S. 85 (1984); Levine v. Cent. Fla. Med. Affiliates, Inc., 72 F.3d 1538 (11th Cir. 1996); Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210 (D.C. Cir. 1986); Muenster Butane, Inc. v. Stewart Co., 651 F.2d 292, 298 (5th Cir. 1981).

the plaintiff can prove an actual harm to competition.[449] Obviously, inconsistencies in the law pose significant concerns for businesses and plaintiffs alike in that it is very difficult to determine antitrust liability prior to litigation.[450] As former President Woodrow Wilson once explained, "Nothing hampers business like uncertainty."[451]

Because the economy is not stagnant, the Court deferred to the rule of reason, believing it to be a standard flexible enough to account for economic changes.[452] But when the Court neglected to explain how to perform an objective economic analysis, it failed to gauge the harm that allowing lower courts to incorporate their subjective biases into analyses would have on enforcement levels. Thus, while the Court may have intended the rule of reason to protect competitive ideals by reacting reflexively to economic progress, it has inadvertently created a standard that does not react to anticompetitive practices at all—per se legality.

IV. THE COURT HAS HIT THE SNOOZE BUTTON FOR LONG ENOUGH: IT IS TIME TO AWAKEN VERTICAL ENFORCEMENT

By upholding the rule of reason for vertical enforcement, the Court refuses to acknowledge the probability that vertical restraints tend to injure competition, whether it be by eliminating intrabrand competition or by leading to horizontal collusion. In doing so, the Court also ignores its own proclamation in *Leegin*—that the lower courts are ill-equipped to sufficiently perform an economic analysis. Why, then, did the Court endorse a standard that not only requires but also relies entirely upon an economic analysis?

As courts become progressively more reluctant to find that the anticompetitive effects of a restraint outweigh the procompetitive benefits, plaintiffs' successes will continue to dwindle.[453] Accordingly, it may only be a matter of time before plaintiffs recognize that the cost of litigating vertical restraint cases is not

449. Stucke, *supra* note 10, at 1432–33; *see also* Kelly, *supra* note 4, at 637 (explaining that there is a legal division about whether plaintiffs should be required to demonstrate a defendant's market power).

450. Stucke, *supra* note 10, 1422–23.

451. *Id.* at 1396 (quoting Woodrow Wilson, U.S. President, Address to Joint Session of Congress on Trusts & Monopolies (Jan. 20, 1914), (transcript available at http://www.presidency.ucsb.edu/ws/?pid=65374).

452. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 907 (2007).

453. *See supra* Part III.C.1.a.

worth the risk, thus prompting vertical enforcement to completely succumb to a de facto rule of per se legality.[454] To avoid this fate, the Supreme Court must reevaluate the rule of reason's construction and provide a more definitive standard for analyzing vertical restraints. This is not to say that the Court should return to a rule of per se illegality. Rather, the Court should evaluate the problems that both the rule of reason and the per se standards have exposed and, instead, endorse a new standard that would avoid those same infirmities and allow vertical enforcement to resume an optimum level.

After accounting for the infirmities of the current standard of analysis, the Supreme Court should invoke a rebuttable presumption of per se illegality for all vertical restraints. Inherent in this standard would be a rebuttable presumption of market power as well. This standard forsakes the traditional approach to categorization and instead refocuses the courts' attention on the effect of a restraint.[455] While some may be skeptical of the impact that this standard will have on precedent, evoking this new standard does not render all of the antitrust precedent worthless. Rather, it merely recalibrates the weight that courts should give to such precedent—categorization will be used as a tool in performing an economic analysis instead of being used to determine if an analysis is necessary.

A rebuttable presumption would still require that a plaintiff sufficiently plead the existence of an agreement restraining competition, but once this initial burden is satisfied, the complaint would carry the assumption that the restraint is unreasonable.[456] A defendant would then be able to refute the plaintiff's allegation of an antitrust violation by proffering evidence that procompetitive justifications excuse the restraint before a court decides if the practice is anticompetitive.[457] At this stage of analysis, courts would be free to consider the categorical analysis that currently exists: restraints which have long been recognized as procompetitive should require the defendant to produce less evidence of reasonableness, while those more controversial restraints should be evaluated based upon their actual effect and not an arbitrary designation.[458] In doing

454. *See supra* notes 359–363 and accompanying text.

455. *See* Kelly, *supra* note 4, at 644–45.

456. *See* Lao, *supra* note 165, at 511.

457. Kelly, *supra* note 4, at 644–45.

458. *See* Lemley & Leslie, *supra* note 14, at 1269 (explaining that categories can be helpful to an economic analysis but should not be dispositive of the outcome).

so, courts should assign less deference to practices that rouse horizontal sentiments, such as price fixing, dual distribution, or those that strengthen cartels, but should consider practices that have long been viewed as beneficial to competition, such as vertical nonprice restraints, more leniently.[459] The upshot is that although categories may still factor into a court's analysis, the emphasis on categorization will have shifted from being the utmost priority to being one of many factors a court can utilize to predict the actual economic impact of the restraint.

An additional feature of the new standard is a presumption of that a manufacturer possesses market power. Market power is often an important consideration in determining whether a practice is anticompetitive.[460] However, courts do not agree about how to apply or whether to even consider market power in an economic analysis of vertical restraints.[461] The reality is that if a manufacturer has enough influence to demand that its retailers consent to a price fixing agreement, it must possess market power.[462] Otherwise, the retailers would refuse to comply.[463]

A. Categorization: What Dreams Are Made of or a Complete Nightmare?

Many scholars agree that the antitrust laws are outdated and demand an overhaul, which would consist of abandoning passé categorizations and assumptions and increasing reliance on empirical evidence to develop a standard that is more relevant to the state of the current economy.[464] Particularly, scholars have argued that the once rigid categories of analysis have been manipulated to the extent that they fail to depict the current economic realities, and they worry that "[b]lind reliance on the categories of yesteryear unnecessarily complicates antitrust litigation, creates inaccurate results, and creates perverse incentives for American businesses."[465]

459. *See id.*
460. *See* Taralson, *supra* note 51, at 588–89.
461. *See supra* notes 448–449 and accompanying text.
462. Taralson, *supra* note 51, at 589.
463. *See id.*
464. *E.g.*, Lemley & Leslie, *supra* note 14, at 1270; Kelly, *supra* note 4, at 646–47; *see, e.g.*, Stucke, *supra* note 10, at 1490.
465. Lemley & Leslie, *supra* note 14, at 1270.

Further frustrating the current enforcement scheme is the weight given to classifying restraints as horizontal or vertical, as price or nonprice, and as illegal per se or subject to the rule of reason.[466] Because categorization is often dispositive, plaintiffs always prefer per se treatment while defendants argue that the rule of reason is appropriate.[467] One of the intrinsic problems with this categorical characterization is that the courts, not the legislature, created the categories and did so by manipulating "case-specific standards en masse into categorical rules."[468] Unfortunately, the economic effect of a restraint will vary under the different circumstances of every case, and often, one type of restraint will, in reality, result in the economic impact equivalent to a different type of restraint.[469] Yet, the courts do not consider the economic impact before selecting the appropriate category,[470] and courts are reluctant to reclassify vertical restraints as horizontal even when they operationally result in the same economic impacts as horizontal collusion.[471] For example, courts judge vertical price fixing according to the rule of reason even if it tacitly leads to horizontal price fixing.[472]

If the Court would take note of this breakdown, it would recognize the inherent flaws of the antitrust standards as they exist today and would find the emphasis on categorical classification to be counterproductive. Due to the variance in the economic impact of restraints across markets, it is imprudent to create blanket categories and strictly adhere to them.[473] The Court claims that it recognizes the danger of basing antitrust analysis on "formalistic line drawing," but nevertheless, that is precisely what it has done by creating and emphasizing categorical distinctions.[474] Effectively, because classifying a restraint into a per se category is usually outcome

466. *See id.* at 1211.

467. *See id.* at 1219.

468. *Id.* at 1211.

469. *See, e.g.*, LOUIS ALTMAN & MALLA POLLOCK, CALLMAN ON UNFAIR COMPETITION, TRADEMARKS, AND MONOPOLIES § 4:20 (4th ed. 2007) ("[T]here are vertical agreements that may have the same effect as a horizontal agreement.").

470. *See* Lemley & Leslie, *supra* note 14, at 1225.

471. *Id.* at 1235–39 (explaining how dual distributorships do not fit into either category of analysis due to their horizontal and vertical nature, yet courts still insist on classifying them and judging them accordingly before considering their impact).

472. *Supra* Part III.B.3.

473. *See* Lemley & Leslie, *supra* note 14, at 1211–12.

474. *Id.* at 1237 (quoting Robert Zwirb, *Dual Distribution and Antitrust Law*, 21 LOY L.A. L. REV. 1273, 1284 (1998)).

determinative, the current enforcement scheme is faulty because it inherently emphasizes the importance of classifying a restraint before considering its actual economic impact. Without a doubt, courts frequently devote more time to categorizing a restraint than to determining its economic impact.[475]

While completely eliminating the per se rule and rule of reason would be the most straightforward way to eliminate the problems posed by categorical analysis, the Court is highly unlikely to consider doing so given its current makeup. Most likely, the Court would fear that it would essentially render all of our antitrust precedent useless. Therefore, Congress may need to acknowledge the problems inherent in the current enforcement scheme and take matters into its own hands by passing a bill that changes the standard. Given the unrest in Congress following *Leegin*'s eradication of all per se illegal vertical restraints and the Court's long-standing tradition of outlawing only those restraints that unreasonably restrict competition, a rebuttable presumption of illegality would be a reasonable solution for the waning vertical enforcement. A Congressional bill proposing this solution would certainly be an easier sell to legislators than the bills currently urging a return to per se illegality. Furthermore, as mentioned previously, this approach will not erase all of our antitrust precedent; it will merely recalibrate the influence it will have on the outcome of a case.

B. Caffeine for the Court: How a Rebuttable Presumption of Illegality Will Reenergize Vertical Enforcement

The primary deficiency of the per se rule was that it yielded too many false positives.[476] Even when procompetitive benefits resulted from a vertical restraint on trade, the per se rule did not allow defendants to offer any of them as justifications for imposing the restraint.[477] As a result, the Supreme Court has repeatedly voiced its concern that the per se approach is inconsistent with its interpretation

475. *See id.* at 1211.
476. *See id.* at 1260.
477. *See id.*

of the Sherman Act as prohibiting only unreasonable restraints.[478] Similarly, the rule of reason is not flawless. As discussed previously, the major drawbacks of the rule of reason are that it imposes an extremely high burden on plaintiffs, promotes inconsistencies, and allows courts to incorporate their own biases into their analyses.[479] Collectively, these deficiencies create an even bigger problem for enforcement by preventing plaintiffs from prevailing under the rule of reason and, in so doing, creating a rule of per se legality. By employing a rebuttable presumption of illegality, courts will be able to resume an optimal level of vertical enforcement. A rebuttable presumption of illegality will remedy four primary problems that the current enforcement approach has exposed—accuracy, predictability, objectivity, and applicability.

1. Increasing the Accuracy of Rulings

First, a standard should yield accuracy so as to minimize indications of anticompetitive behavior.[480] Unfortunately, the current enforcement scheme incentivizes plaintiffs and defendants to argue for and create false positives and false negatives respectively.[481] The problem with false positives is that restraints that actually promote competition and consumer welfare are deemed to be illegal outright due to their categorization.[482] The result of underenforcement has been criticized as leading to too few condemnations because conduct harmful to competition and consumers too often goes undetected.[483] The concern with too many false negatives under the rule of reason is exacerbated by the fact that it has proven to operate as a de facto pronouncement of per se legality on more than one occasion.[484] Plaintiffs and defendants alike should be in a position to win antitrust cases, and, as such, the economic impact should be outcome determinative, not the categorization of the restraint.[485] Accuracy will reduce false indicators and encourage an optimal level of

478. *See, e.g.*, Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007); Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 58–59 (1977).

479. *See supra* notes 92–100, 359–363, 446–447 and accompanying text.

480. *See* Lemley & Leslie, *supra* note 14, at 1260–61.

481. *Id.*

482. *Id.*

483. *Id.* at 1261.

484. Lao, *supra* note 165, at 507–08.

485. Lemley & Leslie, *supra* note 14, at 1265.

enforcement—when a standard is accurate, courts can correctly identify which restraints are adequately justified, and thus reasonable, instead of judging a restraint based on its categorization.[486]

Under the rebuttable-presumption approach, accuracy would increase and courts could easily avoid false positives and negatives. Unlike the per se standard, the rebuttable-presumption standard allows the courts to consider the procompetitive justifications. Additionally, in contrast to the rule of reason, it does not impose an unfair burden on plaintiffs in the pleading stages—no longer would plaintiffs be required to plead an unreasonable restraint on trade or the defendant's market power in their complaints. Perhaps most importantly, it eliminates the possibility of miscategorization from the outset. Courts would no longer have to agonize over categorization before the economic analysis stage, and, even at that point, the court would not be limited to putting the restraint in one category. Instead, it would be free to consider multiple classifications based on the circumstances of the case.

2. Improving Predictability for Litigants

It is important that litigants are able to predict what test will be applied during litigation.[487] Uncertainty is unsavory to defendants and plaintiffs alike.[488] Businesses need to be able to predict their antitrust liability before imposing a restraint, and plaintiffs should be able to gauge the likelihood of success before filing a complaint.[489] In order for a standard to be predictable, it must be both consistent and transparent.

Inconsistency poses a problem because litigants should be able to anticipate with some degree of certainty how the courts will regard any given restraint. Currently, this is not possible because, due to the Court's broad grant of discretion in *Leegin*, different courts are giving contradictory treatment to the same or similar restraints.[490] Although the Court has prided itself on the flexibility of the

486. *See id.* at 1260–61.
487. Stucke, *supra* note 10, at 1422–23.
488. *See id.* at 1422.
489. *See id.* at 1432–33.
490. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 882 (2007).

categorical standards, the Court's ability to shift those categories on a whim has led to widespread bewilderment for litigants attempting to predict how the Court will rule.[491] Moreover, as mentioned previously, the Court can capriciously change the appropriate category of a given restraint.[492] If truth be told, the only thing courts have been seemingly consistent about in recent times is finding no antitrust violations in vertical-restraint cases.

It is also essential that the new standard be transparent so that litigants are able to fully understand how the courts will apply it.[493] Because of the Court's grant of discretionary authority in *Leegin*, courts are inconsistent in their application of the rule of reason.[494] *Leegin* allows courts to develop their own methods for determining whether a restraint is reasonable—with the only guiding principle being that the procompetitive benefits must outweigh the anticompetitive harms.[495] The Court has not opined as to the role that market power should play or the credence that courts should give to advantageous and adverse economic impacts.[496] This causes serious concern for litigants because they are not sure what approach to take when drafting their pleadings.[497]

Under a rebuttable-presumption standard, consistency and transparency will improve because businesses and plaintiffs will know which standard courts will apply, and they will be able to plan accordingly. All litigants will be on notice that, once the pleading burden is satisfied, the presumptions of unreasonableness and market power will be imposed and each party will be granted the opportunity to argue the merits of the case. Still, even under this approach, consistency and transparency may continue to be a concern because the courts will still be required to perform an economic analysis after the defendant offers procompetitive justifications. Under the current approach, however, courts do not seem to be making any headway toward consistency or transparency; thus, the rebuttable-presumption standard is at least a step in the right direction. Since plaintiffs are consistently losing under the rule of

491. Lemley & Leslie, *supra* note 14, at 1262–63.
492. *Id.*
493. *See* Stucke, *supra* note 10, at 1432–33.
494. *See id.*
495. *See id.* at 1385–86.
496. *See id.* at 1432–33 & nn.245–48.
497. *See id.*

reason, a rebuttable presumption of illegality certainly offers to improve those odds by giving plaintiffs more opportunity to argue the economic impact of the restraint as opposed to its categorical designation.

3. Forcing Courts to Be More Objective

A third concern is objectivity. An effective standard should require objectivity so that a court's ability to incorporate its subjective biases is as limited as possible.[498] Political biases and personal agendas inevitably make their way into a court's analysis when it applies vague standards.[499] This is demonstrated by the Court's arbitrary creation of categorical analysis based on haphazard distinctions.[500] Instead of focusing on the economic effect of a restraint, courts are able to favor parties and dictate outcomes by arbitrarily lumping restraints into whichever category will yield the desired result.[501]

Objectivity would improve under the proposed standard because a presumption of unreasonableness would eliminate a court's power to inject a subjective opinion of what is reasonable from the outset of litigation. Of course, defendants will still have the opportunity to rebut the presumption of unreasonableness, but courts will lose their power to favor one litigant over another by subjectively selecting the "appropriate" mode of analysis in the pleading stage. Although personal and political biases may still influence a court's ultimate holding to a certain degree—particularly during the economic analysis—at least the parties will have an opportunity to change the court's opinion before dismissal through oral arguments.

4. Ensuring Applicability Across the Gamut of Vertical Restraints

Finally, applicability is another important concern in that the standard should be universally applicable to all restraints.[502] As they exist now, the categories of analysis have become nonsensical, and

498. *See id.* at 1480.
499. *Id.* at 1456.
500. *See* Lemley & Leslie, *supra* note 14, at 1262–63.
501. *See id.* at 1262.
502. Stucke, *supra* note 10, at 1420–21.

they are no longer indicative of economic realities.[503] Even the Supreme Court has recognized the difficulty that courts face when determining whether some restraints are vertical or horizontal, price or nonprice.[504] Over time, the once strict categories have become muddled, and there is no longer a "bright line" that distinguishes whether restraints are subject to the per se rule or the rule of reason.[505] Applicability eliminates the need to immediately categorize restraints, thereby removing the opportunity for miscategorization.

A rebuttable presumption will certainly achieve an improvement in applicability, for not only will it subject all vertical restraints to the same category of analysis, but it will also eliminate the impact of illogical distinctions regarding what constitutes vertical and horizontal conduct. No longer will courts have to arbitrarily distinguish between the types of conduct at hand before delineating their economic effects. Dual distribution and price fixing could be evaluated by their impact on the market rather than the method used to implement them. Applicability cannot get much simpler than this: all vertical restraints will be considered unreasonable unless otherwise proven. While the depth of the economic analysis may vary based on the restraint at hand, both parties will know the test that will be applied.

Skeptics may attempt to argue that the rebuttable presumption will increase the cost and frequency of litigation for defendants, which would eventually be reflected in higher prices for consumers.[506] While noteworthy, this problem could be mitigated by a rule that required the plaintiff to pay for the defendant's court costs and attorney's fees when the defendant succeeds in demonstrating that the procompetitive benefits justify a restraint.[507] Further, if a new standard is put in place, anticompetitive practices—which often yield higher prices—should decrease, and the impact on consumer prices resulting from increased litigation costs and decreased anticompetitive practices would balance each other out. In that way, consumer prices should, at the worst, maintain the status quo.

503. Lemley & Leslie, *supra* note 14, at 1252.
504. *E.g.*, Cont'l T. V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 58 n.28 (1977).
505. *See* Lemley & Leslie, *supra* note 14, at 1262–63.
506. *See* Kelly, *supra* note 4, at 644–45.
507. *Id.* at 645.

Studies have shown that in practice, the rule of reason operates as a default rule of legality for vertical nonprice restraints and maximum price fixing.[508] The passage of *Leegin* indicates that maximum vertical pricing will suffer a similar fate. As vertical enforcement is rendered obsolete through the application of the rule of reason, serious questions arise as to whether the Court has lost sight of the original intentions of the Sherman Act. All things considered, the rebuttable-presumption approach strikes a fair balance between granting plaintiffs a fair opportunity to prevail while giving defendants a chance to show that the restraint is reasonable by proving that the procompetitive benefits outweigh the anticompetitive effects.[509]

V. CONCLUSION

The Supreme Court has consistently stood by its proclamation that the adoption of the rule of reason is consistent with the its interpretation of Section 1 of the Sherman Act as prohibiting only *unreasonable* restraints on trade.[510] However, the Court's assertion that the rule of reason is the appropriate standard for evaluating the reasonableness of all vertical restraints is doing a disservice to antitrust enforcement. Weak antitrust enforcement can become a serious concern, for businesses and consumers in particular, and under the rule of reason, weakened vertical enforcement has become a reality. Unfortunately, using the rule of reason to determine the reasonableness of a restraint operationally results in per se legality. Indeed, enforcement levels of vertical nonprice and maximum price restraints following *Sylvania* and *Khan* confirm that a shift toward the rule of reason has eviscerated regulation.

Lately, the Court has certainly not exercised any reasonable restraint of its own in advancing the deregulation of competition by extending the rule of reason. Before *Leegin*, the Court had only subjected vertical nonprice and maximum price restraints to the rule of reason and had continued to hold minimum vertical price fixing as subject to per se illegality. However, in *Leegin*, the Court could no longer resist the urge to finally subject all vertical restraints to the

508. *See supra* notes 167–173 and accompanying text.
509. Lao, *supra* note 165, at 511.
510. *Hearings*, *supra* note 392 (statement of James Wilson, Chairman, Antitrust Section of the American Bar Association).

rule of reason. The repercussions on vertical enforcement since *Leegin* have been significant. First, the Court endorsed a heightened pleading standard for plaintiffs by increasing the pleading burden on plaintiffs in both *Twombly* and *Leegin*. Second, the Court's warning that vertical restraints continue to be subjected to the rule of reason regardless of their horizontal impacts caused the lower courts to become reluctant to distinguish horizontal conduct without palpable evidence. Finally, the Court's failure to provide enough guidance about how to conduct an economic analysis using the rule of reason created a standard under which it is almost impossible for plaintiffs to win any vertical restraint cases. As a consequence, all vertical restraints—if they are not there already—are now startlingly close to per se legality.

Throughout the history of antitrust enforcement, the Court has been flexible when the circumstances demand that it overturn per se rules, but now it insists that the only alternative to per se illegality is the rule of reason.[511] The Supreme Court justices themselves have recognized the deficiencies of the rule of reason they created, but they choose to sit idly by, crossing their fingers and hoping that the lower courts will somehow convert the rule of reason into a workable standard.[512] The time has come for the Court to reconsider whether applying the rule of reason when evaluating vertical restraints is consistent with the ultimate goals of the antitrust laws. An unbiased reflection will reveal that it is not.

As demonstrated in this Article, the Court has become less concerned with protecting consumer welfare and competition in recent years, choosing to favor defendants, competitors, big businesses, and their own political platforms instead. In effect, they have lulled vertical enforcement to sleep. To remedy this misstep, the Court needs to provide the lower courts with a new, more clearly defined standard by which to evaluate reasonableness, and if the Court is unwilling, then Congress must do so. Instituting a rebuttable presumption of illegality promises to buttress the original aim of the antitrust laws and reinvigorate enforcement while simultaneously honoring the Supreme Court's tradition of prohibiting only unreasonable restraints.

511. Stucke, *supra* note 10, at 1490.
512. *Id.*