ANTITRUST LAW: POLICY AND PRACTICE

Fourth Edition

2013 Supplement

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p. 139, before "Notes on Miscellaneous Conduct Issues," insert:

Trinko was applied to "price squeezes" in *Pacific Bell Telephone Co. v. Linkline Communications, Inc.*, 555 U.S. 438 (2009)

p. 207, before concluding note, insert:

PACIFIC BELL TELEPHONE CO. v. LINKLINE COMMUNICATIONS, INC.

Supreme Court of the United States
555 U.S. 438 (2009)

CHIEF JUSTICE ROBERTS delivered the opinion of the Court.

The plaintiffs in this case . . . allege that a competitor subjected them to a "price squeeze" in violation of § 2 of the Sherman Act. They assert that such a claim can arise when a vertically integrated firm sells inputs at wholesale and also sells finished goods or services at retail. If that firm has power in the wholesale market, it can simultaneously raise the wholesale price of inputs and cut the retail price of the finished good. This will have the effect of "squeezing" the profit margins of any competitors in the retail market. Those firms will have to pay more for the inputs they need; at the same time, they will have to cut their retail prices to match the other firm's prices. The question before us is whether such a price-squeeze claim may be brought under § 2 of the Sherman Act when the defendant is under no antitrust obligation to sell the inputs to the plaintiff in the first place. We hold that no such claim may be brought.

I

This case involves the market for digital subscriber line (DSL) service, which is a method of connecting to the Internet at high speeds over telephone lines. AT&T owns much of the infrastructure and facilities needed to provide DSL service in California. In particular, AT&T controls most of what is known as the "last mile"—the lines that connect homes and businesses to the telephone network. Competing DSL providers must generally obtain access to AT&T's facilities in order to serve their customers.

Until recently, the Federal Communications Commission (FCC) required incumbent phone companies such as AT&T to sell transmission service to independent DSL providers, under the theory that this would spur competition. In 2005, the Commission largely abandoned this forced-sharing requirement in light of the emergence of a competitive market beyond DSL for high-speed Internet service; DSL now faces robust competition from cable companies and wireless and satellite services. As a condition for a recent merger, however, AT&T remains bound by the mandatory interconnection requirements, and is obligated to provide wholesale "DSL transport" service to independent firms at a price no greater than the retail price of AT&T's DSL service.

The plaintiffs are four independent Internet service providers (ISPs) that compete with AT&T in the retail DSL market. Plaintiffs . . . lease DSL transport service from AT&T pursuant to the merger conditions described above. AT&T thus participates in the DSL market at both the wholesale and retail levels . . . .

In July 2003, the plaintiffs brought suit in District Court, alleging that AT&T violated § 2 of the Sherman Act by monopolizing the DSL market in California. The complaint alleges that AT&T refused to deal with the plaintiffs, denied the plaintiffs access to essential facilities, and engaged in a "price squeeze." Specifically, plaintiffs contend that AT&T squeezed their profit margins by setting a high wholesale price for DSL transport and a low retail price for DSL Internet service. This maneuver allegedly "exclude[d] and unreasonably impede[d] competition," thus allowing AT&T to "preserve and maintain its monopoly control of DSL access to the Internet."

In *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 410 (2004), we held that a firm with no antitrust duty to deal with its rivals at all is under no obligation to provide those rivals with a "sufficient" level of service. Shortly after we issued that decision, AT&T moved for judgment on the pleadings, arguing that the plaintiffs' claims in this case were foreclosed by *Trinko.* The District Court held that AT&T had no antitrust duty to deal with the plaintiffs, but it denied the motion to dismiss with respect to the price-squeeze claims. The court acknowledged that AT&T's argument "has a certain logic to it," but held that *Trinko* "simply does not involve price-squeeze claims." . . .

At the District Court's request, plaintiffs then filed an amended complaint providing greater detail about their price-squeeze claims. AT&T again moved to dismiss, arguing that price-squeeze claims could only proceed if they met the two established requirements for predatory pricing: below-cost retail pricing and a "'dangerous probability'" that the defendant will recoup any lost profits. See *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222-224 (1993). The District Court did not reach the issue whether *all* price-squeeze claims must meet the *Brooke Group* requirements, because it concluded that the amended complaint, "generously construed," satisfied those criteria. The court also certified its earlier order for interlocutory appeal on the question whether "*Trinko* bars price squeeze claims where the parties are compelled to deal under the federal communications laws."

On interlocutory appeal, the Court of Appeals for the Ninth Circuit affirmed the District Court's denial of AT&T's motion for judgment on the pleadings on the price-squeeze claims. The court emphasized that "*Trinko* did not involve a price squeezing theory." Because "a price squeeze theory formed part of the fabric of traditional antitrust law prior to *Trinko*," the Court of Appeals concluded that "those claims should remain viable notwithstanding either the telecommunications statutes or *Trinko.*" . . .

Judge Gould dissented . . . . Judge Gould would have allowed the plaintiffs to amend their complaint if they could, in good faith, raise predatory pricing claims meeting the *Brooke Group* requirements.

We granted certiorari to resolve a conflict over whether a plaintiff can bring price-squeeze claims under § 2 of the Sherman Act when the defendant has no antitrust duty to deal with the plaintiff. We reverse.

II

This case has assumed an unusual posture. The plaintiffs now assert that they agree with Judge Gould's dissenting position that price-squeeze claims must meet the *Brooke Group* requirements for predatory pricing. They ask us to vacate the decision below in their favor and remand with instructions that they be given leave to amend their complaint to allege a *Brooke Group* claim. . . .

We do not think this case is moot. First, the parties continue to seek different relief. . . .

Second, it is not clear that the plaintiffs have unequivocally abandoned their price-squeeze claims.

. . . [P]rudential concerns favor our answering the question presented. . . .

III

A

. . . .

As a general rule, businesses are free to choose the parties with whom they will deal, as well as the prices, terms, and conditions of that dealing. See *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919). But there are rare instances in which a dominant firm may incur antitrust liability for purely unilateral conduct. For example, we have ruled that firms may not charge "predatory" prices—below-cost prices that drive rivals out of the market and allow the monopolist to raise its prices later and recoup its losses. *Brooke Group*, 509 U.S. at 222-224. Here, however, the complaint at issue does not contain allegations meeting those requirements.

There are also limited circumstances in which a firm's unilateral refusal to deal with its rivals can give rise to antitrust liability. See *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 608-611 (1985). Here, however the District Court held that AT&T had no such antitrust duty to deal with its competitors, and this holding was not challenged on appeal.[2]

The challenge here focuses on retail prices—where there is no predatory pricing—and the terms of dealing—where there is no duty to deal. Plaintiffs' price-squeeze claims challenge a different type of unilateral conduct in which a firm "squeezes" the profit margins of its competitors. This requires the defendant to be operating in two markets, a wholesale ("upstream") market and a retail ("downstream") market. A firm with market power in the upstream market can squeeze its downstream competitors by raising the wholesale price of inputs while cutting its own retail prices. This will raise competitors' costs (because they will have to pay more for their inputs) and lower their revenues (because they will have to match the dominant firm's low retail price). Price-squeeze plaintiffs assert that defendants must leave them a "fair" or "adequate" margin between the wholesale price and the retail price. In this case, we consider whether a plaintiff can state a price-squeeze claim when the defendant has no obligation under the antitrust laws to deal with the plaintiff at wholesale.

[2] The Court of Appeals assumed that any duty to deal arose only from FCC regulations, and the question on which we granted certiorari made the same assumption. Even aside from the District Court's reasoning, it seems quite unlikely that AT&T would have an antitrust duty to deal with the plaintiffs. Such a duty requires a showing of monopoly power, but—as the FCC has recognized—the market for high-speed Internet service is now quite competitive; DSL providers face stiff competition from cable companies and wireless and satellite providers.

B

1. A straightforward application of our recent decision in *Trinko* forecloses any challenge to AT&T's *wholesale* prices. In *Trinko*, Verizon was required by statute to lease its network elements to competing firms at wholesale rates. The plaintiff—a customer of one of Verizon's rivals—asserted that Verizon denied its competitors access to interconnection support services, making it difficult for those competitors to fill their customers' orders. The complaint alleged that this conduct in the upstream market violated § 2 of the Sherman Act by impeding the ability of independent carriers to compete in the downstream market for local telephone service.

We held that the plaintiff's claims were not actionable under § 2. Given that Verizon had no antitrust duty to deal with its rivals at all, we concluded that "Verizon's alleged insufficient assistance in the provision of service to rivals" did not violate the Sherman Act. *Trinko* thus makes clear that if a firm has no antitrust duty to deal with its competitors at wholesale, it certainly has no duty to deal under terms and conditions that the rivals find commercially advantageous.

In this case, as in *Trinko*, the defendant has no antitrust duty to deal with its rivals at wholesale; any such duty arises only from FCC regulations, not from the Sherman Act. There is no meaningful distinction between the "insufficient assistance" claims we rejected in *Trinko* and the plaintiffs' price-squeeze claims in the instant case. The *Trinko* plaintiffs challenged the quality of Verizon's interconnection service, while this case involves a challenge to AT&T's pricing structure. But for antitrust purposes, there is no reason to distinguish between price and nonprice components of a transaction. See, *e.g.*, *American Telephone & Telegraph Co. v. Central Office Telephone, Inc*., 524 U.S. 214, 223 (1998) ("Any claim for excessive rates can be couched as a claim for inadequate services and vice versa"). The nub of the complaint in both *Trinko* and this case is identical—the plaintiffs alleged that the defendants (upstream monopolists) abused their power in the wholesale market to prevent rival firms from competing effectively in the retail market. *Trinko* holds that such claims are not cognizable under the Sherman Act in the absence of an antitrust duty to deal.

The District Court and the Court of Appeals did not regard *Trinko* as controlling because that case did not directly address price-squeeze claims. This is technically true, but the reasoning of *Trinko* applies with equal force to price-squeeze claims. AT&T could have squeezed its competitors' profits just as effectively by providing poor-quality interconnection service to the plaintiffs, as Verizon allegedly did in *Trinko.* But a firm with no duty to deal in the wholesale market has no obligation to deal under terms and conditions favorable to its competitors. If AT&T had simply stopped providing DSL transport service to the plaintiffs, it would not have run afoul of the Sherman Act. Under these circumstances, AT&T was not required to offer this service at the wholesale prices the plaintiffs would have preferred.

2. The other component of a price-squeeze claim is the assertion that the defendant's *retail* prices are "too low." Here too plaintiffs' claims find no support in our existing antitrust doctrine.

"[C]utting prices in order to increase business often is the very essence of competition." *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986). In cases seeking to impose antitrust liability for prices that are too low, mistaken inferences are "especially costly, because they chill the very conduct the antitrust laws are designed to protect." Ibid.; see also *Brooke Group*, 509 U.S., at 226 . . . . To avoid chilling aggressive price

competition, we have carefully limited the circumstances under which plaintiffs can state a Sherman Act claim by alleging that prices are too low. Specifically, to prevail on a predatory pricing claim, a plaintiff must demonstrate that: (1) "the prices complained of are below an appropriate measure of its rival's costs"; and (2) there is a "dangerous probability" that the defendant will be able to recoup its "investment" in below-cost prices. Brooke Group, supra, at 222-224. . . .

In the complaint at issue in this interlocutory appeal, there is no allegation that AT&T's conduct met either of the *Brooke Group* requirements. Recognizing a price-squeeze claim where the defendant's retail price remains above cost would invite the precise harm we sought to avoid in *Brooke Group*: Firms might raise their retail prices or refrain from aggressive price competition to avoid potential antitrust liability. . . .

3. Plaintiffs' price-squeeze claim, looking to the relation between retail and wholesale prices, is thus nothing more than an amalgamation of a meritless claim at the retail level and a meritless claim at the wholesale level. If there is no duty to deal at the wholesale level and no predatory pricing at the retail level, then a firm is certainly not required to price *both* of these services in a manner that preserves its rivals' profit margins. [3]

C

1. Institutional concerns also counsel against recognition of such claims. We have repeatedly emphasized the importance of clear rules in antitrust law. Courts are ill suited "to act as central planners, identifying the proper price, quantity, and other terms of dealing." *Trinko*, 540 U.S., at 408. "'No court should impose a duty to deal that it cannot explain or adequately and reasonably supervise. The problem should be deemed irremedia[ble] by antitrust law when compulsory access requires the court to assume the day-to-day controls characteristic of a regulatory agency.'" Id., at 415 (quoting Areeda, Essential Facilities: An Epithet in Need of Limiting Principles, 58 Antitrust L. J. 841, 853 *(1989)*) . . . .

It is difficult enough for courts to identify and remedy an alleged anticompetitive practice at one level, such as predatory pricing in retail markets or a violation of the duty-to-deal doctrine at the wholesale level. . . . Recognizing price-squeeze claims would require courts simultaneously to police both the wholesale and retail prices to ensure that rival firms are not being squeezed. And courts would be aiming at a moving target, since it is the *interaction* between these two prices that may result in a squeeze.

Perhaps most troubling, firms that seek to avoid price-squeeze liability will have no safe harbor for their pricing practices. See *Town of Concord*, *supra*, at 22 (antitrust rules "must be clear enough for lawyers to explain them to clients"). . . .

The most commonly articulated standard for price squeezes is that the defendant must leave its rivals a "fair" or "adequate" margin between the wholesale price and the retail price. See

[3] Like the Court of Appeals, amici argue that price-squeeze claims have been recognized by Circuit Courts for many years, beginning with Judge Hand's opinion in *United States v. Aluminum Co. of America*, 148 F.2d 416 (CA2 1945) (*Alcoa*). In that case, the Government alleged that Alcoa was using its monopoly power in the upstream aluminum ingot market to squeeze the profits of downstream aluminum sheet fabricators. The court concluded: "That it was unlawful to set the price of 'sheet' so low and hold the price of ingot so high, seems to us unquestionable, provided, as we have held, that on this record the price of ingot must be regarded as higher than a 'fair price.'" Given developments in economic theory and antitrust jurisprudence since *Alcoa*, we find our recent decisions in *Trinko* and *Brooke Group* more pertinent to the question before us.

Town of Concord, *supra*, at 23-25; *Alcoa*, 148 F.2d 416, 437-438 (CA2 1945). One of our colleagues has highlighted the flaws of this test in Socratic fashion:

> "[H]ow is a judge or jury to determine a 'fair price?' Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition 'would have set' were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price 'gap?' Must it be large enough for all independent competing firms to make a 'living profit,' no matter how inefficient they may be? . . . And how should the court respond when costs or demands change over time, as they inevitably will?" *Town of Concord*, *supra*, at 25.

Some amici respond to these concerns by proposing a "transfer price test" for identifying an unlawful price squeeze: A price squeeze should be presumed if the upstream monopolist could not have made a profit by selling at its retail rates if it purchased inputs at its own wholesale rates. Whether or not that test is administrable, it lacks any grounding in our antitrust jurisprudence. An upstream monopolist with no duty to deal is free to charge whatever wholesale price it would like; antitrust law does not forbid lawfully obtained monopolies from charging monopoly prices. . . . Similarly, the Sherman Act does not forbid—indeed, it *encourages*—aggressive price competition at the retail level, as long as the prices being charged are not predatory. *Brooke Group*, 509 U.S., at 223-224. If both the wholesale price and the retail price are independently lawful, there is no basis for imposing antitrust liability simply because a vertically integrated firm's wholesale price happens to be greater than or equal to its retail price.

2. Amici assert that there are circumstances in which price squeezes may harm competition. For example, they assert that price squeezes may raise entry barriers that fortify the upstream monopolist's position; they also contend that price squeezes may impair nonprice competition and innovation in the downstream market by driving independent firms out of business.

The problem, however, is that amici have not identified any independent competitive harm caused by price squeezes above and beyond the harm that would result from a duty-to-deal violation at the wholesale level or predatory pricing at the retail level. See 3A P. Areeda & H. Hovenkamp, Antitrust Law ¶ 767c, p 126 (2d ed. 2002) ("[I]t is difficult to see any *competitive* significance [of a price squeeze] apart from the consequences of vertical integration itself"). To the extent a monopolist violates one of these doctrines, the plaintiffs have a remedy under existing law. We do not need to endorse a new theory of liability to prevent such harm.

IV

Lastly, as mentioned above, plaintiffs have asked us for leave to amend their complaint to bring a *Brooke Group* predatory pricing claim. We need not decide whether leave to amend should be granted. Our grant of certiorari was limited to the question whether price-squeeze claims are cognizable in the absence of an antitrust duty to deal. The Court of Appeals addressed only AT&T's motion for judgment on the pleadings on the plaintiffs' *original* complaint. For the reasons stated, we hold that the price-squeeze claims set forth in that complaint are not cognizable under the Sherman Act. . . .

* * *

The judgment of the Court of Appeals is reversed, and the case is remanded for further proceedings consistent with this opinion. . . .

JUSTICE BREYER with whom JUSTICE STEVENS, JUSTICE SOUTER, and JUSTICE GINSBURG join, concurring in the judgment.

I would accept respondents' concession that the Ninth Circuit majority's "price squeeze" holding is wrong, I would vacate the Circuit's decision, and I would remand the case in order to allow the District Court to determine whether respondents may proceed with their "predatory pricing" claim as set forth in Judge Gould's dissenting Ninth Circuit opinion.

A "price squeeze" claim finds its natural home in a Sherman Act § 2 monopolization case where the Government as plaintiff seeks to show that a defendant's monopoly power rests, not upon "skill, foresight and industry," *United States v. Aluminum Co. of America*, 148 F.2d 416, 430 (CA2 1945) (*Alcoa*), but upon exclusionary conduct, *United States v. Grinnell Corp*., 384 U.S. 563, 576 (1966). As this Court pointed out in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), the "'means of illicit exclusion, like the means of legitimate competition, are myriad.'" Id., at 414 (quoting *United States v. Microsoft Corp*., 253 F.3d 34, 58 (CADC 2001) (en banc) (*per curiam*)). They may involve a "course of dealing" that, even if profitable, indicates a "willingness to forsake short-term profits to achieve an anticompetitive end." Trinko, supra, at 409. See, *e.g.*, *Aspen Skiing Co. v. Aspen Highlands Skiing Corp*., 472 U.S. 585, 610-611 (1985); Complaint in *United States* v. *International Business Machines Corp.*, Civil Action No. 69 Civ. 200 (SDNY, filed Jan. 17, 1969), ¶ 20(c) . . . . And, as Judge Hand wrote many years ago, a "price squeeze" may fall within that latter category. Alcoa, supra, at 437-438. As a matter of logic, it may be that a particular price squeeze can only be exclusionary if a refusal by the monopolist to sell to the "squeezed customer" would also be exclusionary. But a court, faced with a price squeeze rather than a refusal to deal, is unlikely to find the latter (hypothetical) question any easier to answer than the former.

I would try neither to answer these hypothetical questions here nor to foreshadow their answer. We have before us a regulated firm. During the time covered by the complaint, petitioners were required to provide wholesale digital subscriber line (DSL) transport service as a common carrier, charging "just and reasonable" rates that were not "unreasonabl[y] discriminat[ory]." 47 U.S.C. §§ 201(b), 202(a) (2000 ed.). And, in my view, a purchaser from a regulated firm (which, if a natural monopolist, is lawfully such) cannot win an antitrust case simply by showing that it is "squeezed" between the regulated firm's wholesale price (to the plaintiff) and its retail price (to customers for whose business both firms compete). When a regulatory structure exists to deter and remedy anticompetitive harm, the costs of antitrust enforcement are likely to be greater than the benefits. See *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 26-29 (CA1 1990). Cf. 3 P. Areeda & D. Turner, Antitrust Law ¶¶ 834-836, pp 344-355 (1978) (whether a particular course of conduct counts as "exclusionary" for antitrust purposes depends upon a host of factors, including, for example, the market position of the defendant, the nature of the market, and the nature of the defendant's conduct).

. . . .

Respondents now seek to show only that the defendant engaged in predatory pricing, within the terms of this Court's decision in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). The District Court can determine whether there is anything in the procedural history of this case that bars respondents from asserting their predatory pricing claim. And if not, it can decide the merits of that claim. As I said, I would remand the case so that it can do so.

Notes and Questions

(1) To what extent does Justice Breyer, with Justices Stevens, Souter, and Ginsburg, disagree with the other five Justices? Which group has the better of the disagreement?

(2) Should the Court have simply summarily reversed, citing *Trinko*? Why or why not?

(3) Is the result of this case to allow a monopolist in an upstream market to monopolize all downstream markets as well? Or will that possibility be policed by the doctrine of the "antitrust duty to deal"? (Consider "day skiing" and "destination skiing" in *Aspen Skiing*.) Try to put into your own words the concept of an "antitrust duty to deal."

(4) Back in 1945 (*Alcoa*) a "price squeeze" seemed like a wrong that should be prevented. In 2009 it did not. What changed?

On pages 419 and 420, delete notes (7) and (8).

On page 420, insert:

AMERICAN NEEDLE, INC. v. NATIONAL FOOTBALL LEAGUE

Supreme Court of the United States
560 U.S. 183 (2010)

JUSTICE STEVENS delivered the opinion of the Court.

"Every contract, combination in the form of a trust or otherwise, or, conspiracy, in restraint of trade" is made illegal by § 1 of the Sherman Act. The question whether an arrangement is a contract, combination, or conspiracy is different from and antecedent to the question whether it unreasonably restrains trade. This case raises that antecedent question about the business of the 32 teams in the National Football League (NFL) and a corporate entity that they formed to manage their intellectual property. We conclude that the NFL's licensing activities constitute concerted action that is not categorically beyond the coverage of § 1. The legality of that concerted action must be judged under the Rule of Reason.

Originally organized in 1920, the NFL is an unincorporated association that now includes 32 separately owned professional football teams.[1] Each team has its own name, colors, and logo, and owns related intellectual property. Like each of the other teams in the league, the New Orleans Saints and the Indianapolis Colts, for example, have their own distinctive names, colors, and marks that are well known to millions of sports fans.

Prior to 1963, the teams made their own arrangements for licensing their intellectual property and marketing trademarked items such as caps and jerseys. In 1963, the teams formed National Football League Properties (NFLP) to develop, license, and market their intellectual property. Most, but not all, of the substantial revenues generated by NFLP have either been given to charity or shared equally among the teams. However, the teams are able to and have at times sought to withdraw from this arrangement.

Between 1963 and 2000, NFLP granted nonexclusive licenses to a number of vendors, permitting them to manufacture and sell apparel bearing team insignias. Petitioner, American Needle, Inc., was one of those licensees. In December 2000, the teams voted to authorize NFLP to grant exclusive licenses, and NFLP granted Reebok International Ltd. an exclusive 10-year license to manufacture and sell trademarked headwear for all 32 teams. It thereafter declined to renew American Needle's nonexclusive license.

American Needle filed this action in the Northern District of Illinois, alleging that the agreements between the NFL, its teams, NFLP, and Reebok violated §§ 1 and 2 of the Sherman Act. In their answer to the complaint, the defendants averred that the teams, NFL, and NFLP were incapable of conspiring within the meaning of § 1 "because they are a single economic enterprise, at least with respect to the conduct challenged." After limited discovery, the District Court granted summary judgment . . . *American Needle, Inc.* v. *New Orleans La. Saints*, 496 F. Supp. 2d 941, 943 (2007). The court concluded "that in that facet of their operations they have so integrated their operations that they should be deemed a single entity rather than joint ventures cooperating for a common purpose."

The Court of Appeals for the Seventh Circuit affirmed. The panel observed that "in some contexts, a league seems more aptly described as a single entity immune from antitrust scrutiny, while in others a league appears to be a joint venture between independently owned teams that is subject to review under § 1." Relying on Circuit precedent, the court limited its inquiry to the particular conduct at issue, licensing of teams' intellectual property. The panel agreed with petitioner that "when making a single-entity determination, courts must examine whether the conduct in question deprives the marketplace of the independent sources of economic control that competition assumes." The court, however, discounted the significance of potential competition among the teams regarding the use of their intellectual property because the teams "can function only as one source of economic power when collectively producing NFL football." The court noted that football itself can only be carried out jointly. ("Asserting that a single

[1] The NFL was founded in Canton, Ohio as the "American Professional Football Association." . . . It took its current name in 1922. Forty-one franchises failed in the first forty-one years of the League's existence.

football team could produce a football game . . . is a Zen riddle: Who wins when a football team plays itself"). Moreover, "NFL teams share a vital economic interest in collectively promoting NFL football . . . [to] compet[e] with other forms of entertainment." "It thus follows," the court found, "that only one source of economic power controls the promotion of NFL football," and "it makes little sense to assert that each individual team has the authority, if not the responsibility, to promote the jointly produced NFL football." Recognizing that NFL teams have "license[d] their intellectual property collectively" since 1963, the court held that § 1 did not apply.

II

As the case comes to us, we have only a narrow issue to decide: whether the NFL respondents are capable of engaging in a "contract, combination . . . , or conspiracy" as defined by § 1 of the Sherman Act, or, as we have sometimes phrased it, whether the alleged activity by the NFL respondents "must be viewed as that of a single enterprise for purposes of § 1." *Copperweld Corp.* v. *Independence Tube Corp.*, 467 U.S. 752, 771 (1984).

Taken literally, the applicability of § 1 to "every contract, combination . . . or conspiracy" could be understood to cover every conceivable agreement, whether it be a group of competing firms fixing prices or a single firm's chief executive telling her subordinate how to price their company's product. But even though, "read literally," § 1 would address "the entire body of private contract," that is not what the statute means. . . . See also *Texaco Inc.* v. *Dagher*, 547 U.S. 1, 5 (2006) ("This Court has not taken a literal approach to this language"); cf. *Board of Trade of Chicago* v. *United States*, 246 U.S. 231, 238 (1918) (reasoning that the term "restraint of trade" in § 1 cannot possibly refer to any restraint on competition because "[e]very agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence"). Not every instance of cooperation between two people is a potential "contract, combination . . . , or conspiracy, in restraint of trade."

. . . .

. . . [U]nlike independent action, "[c]oncerted activity inherently is fraught with anticompetitive risk" insofar as it "deprives the marketplace of independent centers of decisionmaking that competition assumes and demands." Id., at 768-769. And because concerted action is discrete and distinct, a limit on such activity leaves untouched a vast amount of business conduct. As a result, there is less risk of deterring a firm's necessary conduct; courts need only examine discrete agreements; and such conduct may be remedied simply through prohibition. . . . Concerted activity is thus "judged more sternly than unilateral activity under § 2," *Copperweld*, 467 U.S., at 768. For these reasons, § 1 prohibits any concerted action "in restraint of trade or commerce," even if the action does not "threate[n] monopolization," Ibid. And therefore, an arrangement must embody concerted action in order to be a "contract, combination . . . or conspiracy" under § 1.

III

We have long held that concerted action under § 1 does not turn simply on whether the parties involved are legally distinct entities. Instead, we have eschewed such formalistic distinctions in favor of a functional consideration of how the parties involved in the alleged anticompetitive conduct actually operate.

As a result, we have repeatedly found instances in which members of a legally single entity violated § 1 when the entity was controlled by a group of competitors and served, in essence, as a vehicle for ongoing concerted activity. In *United States* v. *Sealy, Inc.*, 388 U.S. 350 (1967), for example, a group of mattress manufacturers operated and controlled Sealy, Inc., a company that licensed the Sealy trademark to the manufacturers, and dictated that each operate within a specific geographic area. Id., at 352-353. The Government alleged that the licensees and Sealy were conspiring in violation of § 1, and we agreed. Id., at 352-354. We explained that "[w]e seek the central substance of the situation" and therefore "we are moved by the identity of the persons who act, rather than the label of their hats." Id., at 353. We thus held that Sealy was not a "separate entity, but . . . an instrumentality of the individual manufacturers." Id., at 356. In similar circumstances, we have found other formally distinct business organizations covered by § 1. . . . We have similarly looked past the form of a legally "single entity" when competitors were part of professional organizations or trade groups.

Conversely, there is not necessarily concerted action simply because more than one legally distinct entity is involved. Although, under a now-defunct doctrine known as the "intraenterprise conspiracy doctrine," we once treated cooperation between legally separate entities as necessarily covered by § 1, we now embark on a more functional analysis.

The roots of this functional analysis can be found in the very decision that established the intraenterprise conspiracy doctrine. In *United States* v. *Yellow Cab Co.*, 332 U.S. 218 (1947), we observed that "corporate interrelationships . . . are not determinitive of the applicability of the Sherman Act" because the Act "is aimed at substance rather than form." Id., at 227. We nonetheless held that cooperation between legally separate entities was necessarily covered by § 1 because an unreasonable restraint of trade "may result as readily from a conspiracy among those who are affiliated or integrated under common ownership as from a conspiracy among those who are otherwise independent." Ibid.*;* see also *Kiefer-Stewart Co.* v. *Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211, 215 (1951).

. . . .

We finally reexamined the intraenterprise conspiracy doctrine in *Copperweld Corp.* v. *Independence Tube Corp.*, 467 U.S. 752 (1984), and concluded that it was inconsistent with the "'basic distinction between concerted and independent action.'" Id., at 767. Considering it "perfectly plain that an internal agreement to implement a single, unitary firm's policies does not raise the antitrust dangers that § 1 was designed to police," id., at 769, we held that a parent corporation and its wholly owned subsidiary "are incapable of conspiring with each other for purposes of § 1 of the Sherman Act," id., at 777. We explained that although a parent corporation and its wholly owned subsidiary are "separate" for the purposes of incorporation or formal title, they are controlled by a single center of decisionmaking and they control a single aggregation of

economic power. Joint conduct by two such entities does not "depriv[e] the marketplace of independent centers of decisionmaking," id., at 769, and as a result, an agreement between them does not constitute a "contract, combination . . . or conspiracy" for the purposes of § 1.

IV

As *Copperweld* exemplifies, "substance, not form, should determine whether a[n] . . . entity is capable of conspiring under § 1." 467 U.S., at 773, n. 21. This inquiry is sometimes described as asking whether the alleged conspirators are a single entity. That is perhaps a misdescription, however, because the question is not whether the defendant is a legally single entity or has a single name; nor is the question whether the parties involved "seem" like one firm or multiple firms in any metaphysical sense. The key is whether the alleged "contract, combination . . . , or conspiracy" is concerted action—that is, whether it joins together separate decisionmakers. The relevant inquiry, therefore, is whether there is a "contract, combination . . . or conspiracy" amongst "separate economic actors pursuing separate economic interests," id., at 769, such that the agreement "deprives the marketplace of independent centers of decisionmaking," ibid., and therefore of "diversity of entrepreneurial interests," *Fraser* v. *Major League Soccer, L. L. C.*, 284 F.3d 47, 57 (CA1 2002) (Boudin, C. J.), and thus of actual or potential competition, see *Freeman* v. *San Diego Ass'n of Realtors*, 322 F.3d 1133, 1148-1149 (CA9 2003) (Kozinski, J.); *Rothery Storage & Van Co.* v. *Atlas Van Lines, Inc.*, 792 F.2d 210, 214-215, 253 U.S. App. D.C. 142 (CADC 1986) (Bork, J.); see also Areeda & Hovenkamp ¶1462b, at 193-194 (noting that the "central evil addressed by Sherman Act § 1" is the "elimin[ation of] competition that would otherwise exist").

Thus, while the president and a vice president of a firm could (and regularly do) act in combination, their joint action generally is not the sort of "combination" that § 1 is intended to cover. Such agreements might be described as "really unilateral behavior flowing from decisions of a single enterprise." *Copperweld*, 467 U.S., at 767. Nor, for this reason, does § 1 cover "internally coordinated conduct of a corporation and one of its unincorporated divisions," id., at 770, because "[a] division within a corporate structure pursues the common interests of the whole," ibid., and therefore "coordination between a corporation and its division does not represent a sudden joining of two independent sources of economic power previously pursuing separate interests," id., at 770-771. Nor, for the same reasons, is "the coordinated activity of a parent and its wholly owned subsidiary" covered. See id., at 771. They "have a complete unity of interest" and thus "[w]ith or without a formal 'agreement,' the subsidiary acts for the benefit of the parent, its sole shareholder." Ibid.

. . . .

V

The NFL teams do not possess either the unitary decisionmaking quality or the single aggregation of economic power characteristic of independent action. Each of the teams is a

substantial, independently owned, and independently managed business. "[T]heir general corporate actions are guided or determined" by "separate corporate consciousnesses," and "[t]heir objectives are" not "common." *Copperweld*, 467 U.S., at 771; see also *North American Soccer League* v. *NFL*, 670 F.2d 1249, 1252 (CA2 1982) (discussing ways that "the financial performance of each team, while related to that of the others, does not . . . necessarily rise and fall with that of the others"). The teams compete with one another, not only on the playing field, but to attract fans, for gate receipts and for contracts with managerial and playing personnel. See *Brown* v. *Pro Football, Inc.*, 518 U.S. 231, 249 (1996); *Sullivan* v. *NFL*, 34 F.3d 1091, 1098 (CA1 1994); *Mid-South Grizzlies* v. *NFL*, 720 F.2d 772, 787 (CA3 1983); cf. *NCAA*, 468 U.S., at 99.

Directly relevant to this case, the teams compete in the market for intellectual property. To a firm making hats, the Saints and the Colts are two potentially competing suppliers of valuable trademarks. When each NFL team licenses its intellectual property, it is not pursuing the "common interests of the whole" league but is instead pursuing interests of each "corporation itself," *Copperweld*, 467 U.S., at 770; teams are acting as "separate economic actors pursuing separate economic interests," and each team therefore is a potential "independent cente[r] of decisionmaking," id., at 769. Decisions by NFL teams to license their separately owned trademarks collectively and to only one vendor are decisions that "depriv[e] the marketplace of independent centers of decisionmaking," ibid., and therefore of actual or potential competition. See *NCAA*, 468 U.S., at 109, n. 39 (observing a possible § 1 violation if two separately owned companies sold their separate products through a "single selling agent"); cf. Areeda & Hovenkamp ¶1478a, at 318 ("Obviously, the most significant competitive threats arise when joint venture participants are actual or potential competitors").

In defense, respondents argue that by forming NFLP, they have formed a single entity, akin to a merger, and market their NFL brands through a single outlet. But it is not dispositive that the teams have organized and own a legally separate entity that centralizes the management of their intellectual property. An ongoing § 1 violation cannot evade § 1 scrutiny simply by giving the ongoing violation a name and label. "Perhaps every agreement and combination in restraint of trade could be so labeled." *Timken Roller Bearing Co.* v. *United States*, 341 U.S. 593, 598 (1951).

The NFL respondents may be similar in some sense to a single enterprise that owns several pieces of intellectual property and licenses them jointly, but they are not similar in the relevant functional sense. Although NFL teams have common interests such as promoting the NFL brand, they are still separate, profit-maximizing entities, and their interests in licensing team trademarks are not necessarily aligned. . . . Common interests in the NFL brand "*partially* unit[e] the economic interests of the parent firms," Brodley, Joint Ventures and Antitrust Policy, 95 Harv. L. Rev. 1521, 1526 (1982) (emphasis added), but the teams still have distinct, potentially competing interests.

It may be, as respondents argue, that NFLP "has served as the 'single driver" of the teams' "promotional vehicle," "'pursu[ing] the common interests of the whole.'" Brief for NFL Respondents 28 (quoting *Copperweld*, 467 U.S., at 770-771; brackets in original). But illegal restraints often are in the common interests of the parties to the restraint, at the expense of those who are not parties. It is true, as respondents describe, that they have for some time marketed

their trademarks jointly. But a history of concerted activity does not immunize conduct from § 1 scrutiny. "Absence of actual competition may simply be a manifestation of the anticompetitive agreement itself." *Freeman*, 322 F.3d at 1149.

Respondents argue that nonetheless, as the Court of Appeals held, they constitute a single entity because without their cooperation, there would be no NFL football. It is true that "the clubs that make up a professional sports league are not completely independent economic competitors, as they depend upon a degree of cooperation for economic survival." *Brown*, 518 U.S., at 248. But the Court of Appeals' reasoning is unpersuasive.

> The justification for cooperation is not relevant to whether that cooperation is concerted or independent action. A "contract, combination . . . or conspiracy," § 1, that is necessary or useful to a joint venture is still a "contract, combination . . . or conspiracy" if it "deprives the marketplace of independent centers of decisionmaking," *Copperweld*, 467 U.S., at 769. See *NCAA*, 468 U.S., at 113. ("[J]oint ventures have no immunity from antitrust laws"). Any joint venture involves multiple sources of economic power cooperating to produce a product. And for many such ventures, the participation of others is necessary. But that does not mean that necessity of cooperation transforms concerted action into independent action; a nut and a bolt can only operate together, but an agreement between nut and bolt manufacturers is still subject to § 1 analysis. Nor does it mean that once a group of firms agree to produce a joint product, cooperation amongst those firms must be treated as independent conduct. The mere fact that the teams operate jointly in some sense does not mean that they are immune.[7]

The question whether NFLP decisions can constitute concerted activity covered by § 1 is closer than whether decisions made directly by the 32 teams are covered by § 1. This is so both because NFLP is a separate corporation with its own management and because the record indicates that most of the revenues generated by NFLP are shared by the teams on an equal basis. Nevertheless we think it clear that for the same reasons the 32 teams' conduct is covered by § 1, NFLP's actions also are subject to § 1, at least with regards to its marketing of property owned by the separate teams. NFLP's licensing decisions are made by the 32 potential competitors, and each of them actually owns its share of the jointly managed assets. Cf. *Sealy*, 388 U.S., at 352-354. Apart from their agreement to cooperate in exploiting those assets, including their decisions as the NFLP, there would be nothing to prevent each of the teams from making its own market decisions relating to purchases of apparel and headwear, to the sale of such items, and to the granting of licenses to use its trademarks.

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[7] In any event, it simply is not apparent that the alleged conduct was necessary at all. Although two teams are needed to play a football game, not all aspects of elaborate interleague cooperation are necessary to produce a game. Moreover, even if leaguewide agreements are necessary to produce football, it does not follow that concerted activity in marketing intellectual property is necessary to produce football.

The Court of Appeals carved out a zone of antitrust immunity for conduct arguably related to league operations by reasoning that coordinated team trademark sales are necessary to produce "NFL football," a single NFL brand that competes against other forms of entertainment. But defining the product as "NFL football" puts the cart before the horse: Of course the NFL produces NFL football; but that does not mean that cooperation amongst NFL teams is immune from § 1 scrutiny. Members of any cartel could insist that their cooperation is necessary to produce the "cartel product" and compete with other products.

We generally treat agreements within a single firm as independent action on the presumption that the components of the firm will act to maximize the firm's profits. But in rare cases, that presumption does not hold. Agreements made within a firm can constitute concerted action covered by § 1 when the parties to the agreement act on interests separate from those of the firm itself, and the intrafirm agreements may simply be a formalistic shell for ongoing concerted action. See, *e.g.*, *Topco Associates, Inc.*, 405 U.S., at 609; *Sealy*, 388 U.S., at 352-354.

For that reason, decisions by the NFLP regarding the teams' separately owned intellectual property constitute concerted action. Thirty-two teams operating independently through the vehicle of the NFLP are not like the components of a single firm that act to maximize the firm's profits. The teams remain separately controlled, potential competitors with economic interests that are distinct from NFLP's financial well-being. . . . Unlike typical decisions by corporate shareholders, NFLP licensing decisions effectively require the assent of more than a mere majority of shareholders. And each team's decision reflects not only an interest in NFLP's profits but also an interest in the team's individual profits. . . . The 32 teams capture individual economic benefits separate and apart from NFLP profits as a result of the decisions they make for the NFLP. NFLP's decisions thus affect each team's profits from licensing its own intellectual property. "Although the business interests of" the teams "will *often* coincide with those of the" NFLP "as an entity in itself, that commonality of interest exists in every cartel." *Los Angeles Memorial Coliseum Comm'n* v. *NFL*, 726 F.2d 1381, 1389 (CA9 1984) (emphasis added). In making the relevant licensing decisions, NFLP is therefore "an instrumentality" of the teams. *Sealy*, 388 U.S., at 352-354; see also *Topco Associates, Inc.*, 405 U.S., at 609.

If the fact that potential competitors shared in profits or losses from a venture meant that the venture was immune from § 1, then any cartel "could evade the antitrust law simply by creating a 'joint venture' to serve as the exclusive seller of their competing products." *Major League Baseball Properties, Inc.* v. *Salvino, Inc.*, 542 F.3d 290, 335 (CA2 2008) (Sotomayor, J., concurring in judgment). "So long as no agreement," other than one made by the cartelists sitting on the board of the joint venture, "explicitly listed the prices to be charged, the companies could act as monopolies through the 'joint venture.'" Ibid. (Indeed, a joint venture with a single management structure is generally a better way to operate a cartel because it decreases the risks of a party to an illegal agreement defecting from that agreement). However, competitors "cannot simply get around" antitrust liability by acting "through a third-party intermediary or 'joint venture'." *Id.*, at 336.[9]

VI

[9] For the purposes of resolving this case, there is no need to pass upon the Government's position that entities are incapable of conspiring under § 1 if they "have effectively merged the relevant aspect of their operations, thereby eliminating actual and potential competition . . . in that operational sphere" and "the challenged restraint [does] not significantly affect actual or potential competition . . . outside their merged operations." Brief for United States as *Amicus Curiae* 17. The Government urges that the choices "to offer only a blanket license" and "to have only a single headwear licensee" might not constitute concerted action under its test. *Id.*, at 32. However, because the teams still own their own trademarks and are free to market those trademarks as they see fit, even those two choices were agreements amongst potential competitors and would constitute concerted action under the Government's own standard. At any point, the teams could decide to license their own trademarks. It is significant, moreover, that the teams here control NFLP. The two choices that the Government might treat as independent action, although nominally made by NFLP, are for all functional purposes choices made by the 32 entities with potentially competing interests.

Football teams that need to cooperate are not trapped by antitrust law. "[T]he special characteristics of this industry may provide a justification" for many kinds of agreements. *Brown*, 518 U.S., at 252 (STEVENS, J., dissenting). The fact that NFL teams share an interest in making the entire league successful and profitable, and that they must cooperate in the production and scheduling of games, provides a perfectly sensible justification for making a host of collective decisions. But the conduct at issue in this case is still concerted activity under the Sherman Act that is subject to § 1 analysis.

When "restraints on competition are essential if the product is to be available at all," *per se* rules of illegality are inapplicable, and instead the restraint must be judged according to the flexible Rule of Reason. *NCAA*, 468 U.S., at 101; see id., at 117 ("Our decision not to apply a per se rule to this case rests in large part on our recognition that a certain degree of cooperation is necessary if the type of competition that petitioner and its member institutions seek to market is to be preserved"); see also *Dagher*, 547 U.S., at 6. In such instances, the agreement is likely to survive the Rule of Reason. See *Broadcast Music, Inc.* v. *Columbia Broadcasting System, Inc.*, 441 U.S. 1, 23 (1979) ("Joint ventures and other cooperative arrangements are also not usually unlawful . . . where the agreement . . . is necessary to market the product at all"). And depending upon the concerted activity in question, the Rule of Reason may not require a detailed analysis; it "can sometimes be applied in the twinkling of an eye." *NCAA*, 468 U.S., at 109, n. 39.

Other features of the NFL may also save agreements amongst the teams. We have recognized, for example, "that the interest in maintaining a competitive balance" among "athletic teams is legitimate and important," *NCAA*, 468 U.S., at 117. While that same interest applies to the teams in the NFL, it does not justify treating them as a single entity for § 1 purposes when it comes to the marketing of the teams' individually owned intellectual property. It is, however, unquestionably an interest that may well justify a variety of collective decisions made by the teams. What role it properly plays in applying the Rule of Reason to the allegations in this case is a matter to be considered on remand.

* * *

Accordingly, the judgment of the Court of Appeals is reversed, and the case is remanded for further proceedings consistent with this opinion.

Notes and Questions

(1) Is *American Needle*'s functional approach consistent with *Copperweld*? Do both cases simply emphasize substance over form, with the substance analysis cutting the opposite way in *American Needle*?

(2) Justice Stevens dissented in *Copperweld*, arguing that reliance on the rule of reason would be appropriate for discerning which intra-enterprise conspiracies enhance efficiency and

should be permitted and which do not and should be prohibited. Has he markedly changed his position in *American Needle*?

(3) It is interesting to note that both parties sought certiorari after the Seventh Circuit's decision, which, as described in Part I of the Supreme Court's opinion, held that Section 1 did not apply to the NFL clubs' licensing of their intellectual property. Why would the NFL have sought further review?

(4) The Department of Justice and the FTC participated jointly as amicus and relied on *Dagher* to propose a standard which would exempt from Section 1 scrutiny collaborative conduct where there had been an "effective merger" of some operations with no anticompetitive spillover effects outside the area of thee effective merged operations. In footnote 9 the Court notes that it is not necessary for it to consider the Government's position, given its resolution of the case. How does the Government's proposed standard differ from the Court's?

(5) Does it seem surprising that the Court cites *Texaco v. Dagher* only twice in passing for (1) the proposition that the Supreme Court has not taken a literal approach to applying the language of Section 1 and (2) in support of the application of the rule of reason? Is it because the joint venture in *Dagher* was more "functionally integrated" than the NFL? Do not Shell and Texaco, the two parties to the joint venture in *Dagher*, compete outside of the joint venture, just as do the teams of the NFL outside of the licensing agreement? What explains the different outcomes in the two cases? If *American Needle* stands for the proposition that entities can't fundamentally compete and still avoid Section 1 scrutiny, how does the joint venture in *Dagher* differ?

(6) Was the agreement between the NFL teams and the NFLP simply a joint marketing agreement among independent competitors? Were there any facts about the NFLP and its relationship to and with the NFL and its constituent teams that the Supreme Court considered to be outcome determinative?

(7) The *American Needle* Court points to the rule of reason as the appropriate vehicle for determining whether the joint licensing agreement violates Section 1. Is that surprising? Who is likely to win on remand? Is it likely that a per se price fixing case could be made from the NFLP's exclusive licensing agreement? In *Major League Baseball Properties, Inc. v. Salvino, Inc.*, 542 F.3d 290 (2d Cir. 2008), the Second Circuit applied the rule of reason to a challenge the exclusive licensing agreement that Major League Baseball teams had entered into with Major League Baseball Properties (MLBP) for the marketing of their trademarks. It found that the under the quick look rule of reason, that the claimant had failed to show any competitive injury. In what amounted to dicta, the court stated that the exclusive agreement could not amount to price fixing among the clubs because the teams shared profits equally. Judge (now Justice) Sotomayor disagreed in a concurring opinion, noting that the effect of the agreement was to eliminate price competition for trademark licenses among all the clubs. *Id.* at 334-35. Does this argue for application of the per se rule in *American Needle*?

(8) After *American Needle*, if law firm partners agree to raise their billing rate, is that an agreement for purposes of Section 1?

On page 560, insert before notes and questions:

Press Release, Federal Trade Commission & U.S. Department of Justice, FTC and U.S. Department of Justice Issue Revised Horizontal Merger Guidelines (Aug. 19, 2010), http://www.justice.gov/atr/public/press_releases/2010/261642.htm.

For Release: 08/19/2010

Federal Trade Commission and U.S. Department of Justice Issue Revised Horizontal Merger Guidelines

2010 Guidelines More Accurately Represent Agencies' Merger Review Process

The Federal Trade Commission and Department of Justice issued today revised Horizontal Merger Guidelines that outline how the federal antitrust agencies evaluate the likely competitive impact of mergers and whether those mergers comply with U.S. antitrust law. These changes mark the first major revision of the merger guidelines in 18 years, and will give businesses a better understanding of how the agencies evaluate proposed mergers.

A primary goal of the 2010 guidelines is to help the agencies identify and challenge competitively harmful mergers while avoiding unnecessary interference with mergers that either are competitively beneficial or likely will have no competitive impact on the marketplace. To accomplish this, the guidelines detail the techniques and main types of evidence the agencies typically use to predict whether horizontal mergers may substantially lessen competition.

The revised merger guidelines derive from the agencies' collective experience in assessing thousands of transactions focusing on the types of evidence the department and the FTC use to decide whether a merger of competitors may harm competition. Many of the proposed refinements and changes reflect issues previously identified in the "Commentary on the Horizontal Merger Guidelines," which the agencies jointly issued in 2006. In crafting the revisions, the agencies considered a wide range of opinions gathered through a series of joint public workshops, as well as hundreds of public comments submitted by attorneys, academics, economists, consumer groups and businesses.

"Because of the hard work of all involved at both agencies, private parties and judges will be better equipped to understand how the agencies evaluate deals. That improvement in clarity and predictability will benefit everyone," said FTC Chairman Jon Leibowitz. "We thank Christine Varney and her team at DOJ for their terrific work on this initiative, demonstrating once again how effectively and collegially the two agencies work together."

"The revised guidelines better reflect the agencies' actual practices," said Christine Varney, Assistant Attorney General in charge of the Department of Justice's Antitrust Division. "The guidelines provide more clarity and transparency, and will provide businesses with an even

greater understanding of how we review transactions. This has been a successful process due to the commitment of the talented staff from both agencies and the excellent working relationship with the FTC led by Jon Leibowitz."

The agencies jointly announced the project in September 2009, followed by a series of workshops over the course of the winter. The FTC issued proposed revisions for public comment on April 20, 2010. All of the written comments are posted on the FTC's website at http://www.ftc.gov/os/comments/hmgrevisedguides/index.shtm.

The 2010 guidelines are different from the 1992 guidelines in several important ways. The guidelines:

- Clarify that merger analysis does not use a single methodology, but is a fact-specific process through which the agencies use a variety of tools to analyze the evidence to determine whether a merger may substantially lessen competition.
- Introduce a new section on "Evidence of Adverse Competitive Effects." This section discusses several categories and sources of evidence that the agencies, in their experience, have found informative in predicting the likely competitive effects of mergers.
- Explain that market definition is not an end itself or a necessary starting point of merger analysis, and market concentration is a tool that is useful to the extent it illuminates the merger's likely competitive effects.
- Provide an updated explanation of the hypothetical monopolist test used to define relevant antitrust markets and how the agencies implement that test in practice.
- Update the concentration thresholds that determine whether a transaction warrants further scrutiny by the agencies.
- Provide an expanded discussion of how the agencies evaluate unilateral competitive effects, including effects on innovation.
- Provide an updated section on coordinated effects. The guidelines clarify that coordinated effects, like unilateral effects, include conduct not otherwise condemned by the antitrust laws.
- Provide a simplified discussion of how the agencies evaluate whether entry into the relevant market is so easy that a merger is not likely to enhance market power.
- Add new sections on powerful buyers, mergers between competing buyers, and partial acquisitions.

The 2010 guidelines are available on the FTC's website at http://www.ftc.gov/os/2010/08/100819hmg.pdf and the Department of Justice's website at http://www.justice.gov/atr/public/guidelines/hmg-2010.html.

The Horizontal Merger Guidelines, which were first adopted in 1968, and revised in 1992, serve as an outline of the main analytical techniques, practices and enforcement policies the FTC and the Department of Justice use to evaluate mergers and acquisitions involving actual or potential competitors under federal antitrust laws.

The guidelines issued today take into account the legal and economic developments since the 1992 guidelines were issued. They are not intended to represent a change in the direction of merger review policy, but to offer more clarity on the merger review process to better assist the business community and, in particular, parties to mergers and acquisitions.

The Bank Merger Competitive Review guidelines, which the federal banking agencies and the Department of Justice developed in 1995 to facilitate the competitive review of bank mergers, remain unchanged. The Bank Merger Competitive Review guidelines can be found at http://www.justice.gov/atr/public/premerger.htm.

The FTC vote approving the 2010 guidelines was 5-0. Chairman Leibowitz issued a separate written statement outlining some of the ways the guidelines have been improved. Commissioner J. Thomas Rosch issued a separate concurring statement praising the guidelines for considering "competitive effects first, and market definition second, thereby making clear that while . . . the market must be defined at some point in the process, ultimately merger analysis must rest on the competitive effects of a transaction." Commissioner Rosch, nevertheless, noted concerns that the guidelines place too much emphasis on economic evidence including margins and prices, and insufficient attention to empirical evidence and non-price competitive effects.

The FTC's Bureau of Competition works with the Bureau of Economics to investigate alleged anticompetitive business practices and, when appropriate, recommends that the Commission take law enforcement action. To inform the Bureau about particular business practices, call 202-326-3300, send an e-mail to antitrust@ftc.gov, or write to the Office of Policy and Coordination, Room 394, Bureau of Competition, Federal Trade Commission, 600 Pennsylvania Ave, N.W., Washington, DC 20580. To learn more about the Bureau of Competition, read "Competition Counts" at http://www.ftc.gov/competitioncounts.

The full text of the new guidelines can be found at:

http://www.ftc.gov/os/2010/08/100819hmg.pdf or
http://www.justice.gov/atr/public/guidelines/hmg-2010.html

and should replace pages App. C-1 through App. C-28 of Appendix C in the casebook.

On page 598, insert before note on hospital mergers:

Note on *United States v. H & R Block, Inc.*

In *United States v. H & R Block, Inc.*, 831 F. Supp. 2d 27 (D.D.C. 2011) a district court considered the proposed merger of two digital do-it-yourself tax preparation products (DDIY), H & R Block (HRB) and TaxACT. The industry leader, Intuit, accounted for 62.2% of DDIY returns with HRB second at 15.6% and TaxACT third at 12.8%. The government argued that the "combination would result in an effective duopoly between HRB and Intuit in the DDIY market,

in which the nearest competitor will have an approximately 3 percent market share, and most other competitors will have less than a 1 percent share."

In enjoining the merger the court frequently referred to the Merger Guidelines, both in defining the relevant market and assessing competitive impact. The defendants vigorously asserted that the relevant market should include all tax preparation methods which would be comprised of DDIY, "pen-and-paper" (tax return preparation by hand or with free forms from the IRS website), and "assisted" return preparation (hiring of an accountant or specialist at a retail tax store). In its analysis, the court relied on the SSNIP from the guidelines:

> Thus, the question here is whether it would be hypothetically useful to have a monopoly over all DDIY tax preparation products because the monopolist could then profitably raise prices for those products by five percent or more; or whether, to the contrary, there would be no reason to monopolize all DDIY tax preparation products because substitution and price competition with other methods of tax preparation would restrain any potential DDIY monopolist from profitably raising prices. In other words, would enough DDIY users switch to the assisted or pen-and-paper methods of tax preparation in response to a five-to-ten percent increase in DDIY prices to make such a price increase unprofitable?

While the defendants argued that they were trying to capture both assisted and pen-and-paper tax return consumers, the court noted that significant price disparities existed and found that "none of the major DDIY competitors sets their prices based on consideration of assisted prices." Similarly, it concluded that, applying the SSNIP test, "pen-and-paper preparation is unlikely to provide a meaningful restraint for DDIY products. . . ." The court even went so far to state that "[t]he government well illustrated the overly broad nature of defendants' proposed relevant market by posing to the defendants' expert the hypothetical question of whether 'sitting at home and drinking chicken soup [would be] part of the market for [manufactured] cold remedies.'"

The court also considered the government expert's "critical loss" analysis as part of its relevant market determination. The critical loss test "attempts to calculate 'the largest amount of sales that a monopolist can lose before a price increase becomes unprofitable.'" The Merger Guidelines recognize it as a method for implementing the SSNIP test, § 4.1.3, and courts have recognized it as a standard methodology to study potential relevant markets, *see, e.g.*, *FTC v. CCC Holdings Inc.*, 605 F. Supp. 2d 26, 40 n.16 (D.D.C. 2009). The government expert in *H & R Block* concluded that the critical loss using the DDIY market for a 10% price increase would be 16.7%. That is, a 10% price in DDIY would be profitable if the resulting lost sales did not surpass 16.7%. The court concluded, however, that while the critical loss analysis was helpful in ascertaining the relevant market, it could not rely on it alone because it could be used to confirm multiple relevant markets within the tax preparation industry.

After concluding based on all the evidence that the relevant market was DDIY products, the court noted that the pre-merger HHI was 4,291 with a HHI increase of about 400, both of which raised a presumption of anticompetitive effects. The court noted that the Supreme Court had adopted a "totality-of-the-circumstances" approach and that reliance on the HHI did not

guarantee a government injunction. It went on, however, to reference the guidelines in dismissing defendants' rebuttal arguments and finding the likelihood of both coordinated effects ("As the Merger Guidelines explain, coordinated interaction involves a range of conduct, including unspoken understandings about *how* firms compete or refrain from competing.") and unilateral effects. Similarly, the court found that the defendants had not shown that their claimed efficiency gains were merger specific, as required by the guidelines.

Is the government's chicken soup analogy apt? Is there a discernible difference between tax preparation services and available cold remedies? For example, one does not have to seek a cold remedy, but one does have to pay taxes. Certainly all tax preparation services compete in that each tax preparation consumer must choose a method of tax preparation. Why then did the court carve out DDIY as the relevant market?

On page 600, replace the "Note on European Community Merger Law" with the following:

Articles 101 and 102 of the Treaty on the Functioning of the European Union (formerly Articles 81 and 82, then Articles 85 and 86, of the Treaty establishing the European Community) are the basis of EU competition law, including the law regarding mergers. Although Article 101 prohibits agreements that distort competition and Article 102 forbids one or more dominant firms from abusing their market position, these articles include no express provision relating to mergers. *Treaty on the Functioning of the European Union*, O.J. (C 115) 47 (2008); *Treaty Establishing the European Community*, O.J. (C 224) 1 (1992).

Initially, mergers attracted little attention because member states viewed mergers as a convenient and effective method of integrating the Community's economies and markets. When the European Commission did finally bring merger enforcement actions, relying on the general language of Articles 85 and 86 proved problematic and somewhat analogous to U.S. merger law under the Sherman Act prior to passage of the Clayton Act. *See* Sergio Baches Opi, *Merger Control in the United States and the European Union: How Should the United States' Experience Influence the Enforcement of the Council Merger Regulation?* 6 J. Transnat'l L. & Pol'y 223, 232-33 (1997).

In the first EC merger action, *Continental Can Co. v. European Commission*, 6/72, 1973 E.C.R. 215, 219-220, the Commission brought an action under Article 86 when a U.S. can company acquired 86% of the shares of the largest German producer of packaging and metal closures, who in turn purchased 91% of the shares of a leading manufacturer of packaging materials in Benelux. The European Court of Justice ruled that the acquisitions, although not expressly prohibited by the article, could fall within Article 86 because its list of abuses was not intended to be exhaustive. The decision sparked a long, sporadic debate over whether the Commission should adopt an explicit merger control regulation.

Agreement was eventually reached on a regulation and a new era in European antitrust law began on September 21, 1990 when EEC Regulation 4064/89 ("the Merger Regulation") went into effect. The Merger Regulation applied to mergers and acquisitions, called "concentrations," which satisfied certain threshold tests. Once the threshold levels were met, the parties to the transaction were required to file notification forms with the European Commission

(in a manner similar to that that required by the Hart-Scott-Rodino Act in the United States) and undergo review by the Commission of the transaction's affect on competition. The legal standard under which mergers were assessed asked whether the merger "create[d] or strengthen[ed] a dominant position as a result of which effective competition would be significantly impeded." This was a two-part test, requiring both dominance and a significant impeding of competition.

A new EC Merger Regulation, Council Regulation No. 139/2004, came into force on May 1, 2004, resulting in a number of changes. For present purposes, the most significant of those changes was in the governing substantive standard, which now states that "[a] concentration which would significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared incompatible with the common market." Art. 2(3). Although this standard continues to include a reference to dominance, it no longer makes it a *sine qua non* of illegality. The regulation goes further and specifies factors that the Commission, in making the competition assessment, must take into account:

(a) the need to maintain and develop effective competition within the common market in view of, among other things, the structure of all the markets concerned and the actual or potential competition from undertakings located either within or outwith the Community;
(b) the market position of the undertakings concerned and their economic and financial power, the alternatives available to suppliers and users, their access to supplies or markets, any legal or other barriers to entry, supply and demand trends for the relevant goods and services, the interests of the intermediate and ultimate consumers, and the development of technical and economic progress provided that it is to consumers' advantage and does not form an obstacle to competition.

Like the U.S. enforcement agencies, the EC has issued guidelines regarding its treatment of mergers. *See* Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, O.J. (C 31) 5 (2004); Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, O.J. (C 265) 6 (2008).

Generally speaking, the standards applied by the EC are similar to those applied in the U.S., though there are some differences. *See generally* John J. Parisi, *A Simple Guide to the EC Merger Regulation of 2004*, The Antitrust Source 1 (January 2005). Although the EC is often thought to be more strict in its merger decisions, the comparison is in fact not clearly one-sided. *See* François Lévêque, *Merger Control: More Stringent in Europe than in the United States?* (November 2007), available at http://www.cerna.ensmp.fr/Documents/FL-MergerEUvsUS.pdf. An essential point, though, is that the EC applies the law to "all concentrations with a Community dimension," which includes not only mergers internal to the EC but also many transactions that involve merging parties from countries outside Europe. Indeed, in recent years the Commission has become increasingly involved in multinational mergers, resulting in significant conflict with U.S. enforcement agencies and U.S. companies, which, if doing business in Europe, must gain European Commission authorization in addition to U.S. approval for its acquisitions.

In 1997 the Boeing Company, the world's largest commercial jet aircraft manufacturer with a 64% market share, acquired the McDonnell Douglas Corporation, a smaller but important competitor. In July, 1997, the FTC approved the merger, despite the fact that it would increase Boeing's market share to over 70%. Although the FTC did not classify the Douglas Aircraft Company (DAC), the commercial aircraft division of McDonnell Douglas, as a failing company, it determined that the merger would not decrease competition in the commercial aircraft market because DAC was no longer an effective entrant in the market.

The European Community expressed shock that the FTC had approved the merger and accused it of protecting a "national champion" and ignoring its own standards for merger review. The EC undertook its own review and approved the merger only on condition that Boeing relinquish its recent 20 year exclusive supply contracts with American, Delta, and Continental Airlines, who were the first, third, and fourth largest operators of DAC aircraft. Boeing was forced to accept the condition, after being unable to persuade the Commission that the exclusive supply agreements were unrelated to the merger. *See* Commission of the European Communities, *The Commission Clears the Merger Between Boeing and McDonnell Douglas Under Certain Conditions and Obligations*, 1997 O.J. (L 336-8/12/1997) 16.

Members of Congress in turn accused the EC of exceeding its jurisdictional authority and attempting to protect and gain an unfair advantage for Airbus Industries, a European government aircraft manufacturing consortium. H.R. Res. 191, 105th Cong. (1997), 143 Cong. Rec. 5550 (1997); S. Res. 108, 105th Cong. (1997), 143 Cong. Rec. 7609 (1997). The EC, however, stated that it had taken into account U.S. concerns "to the extent consistent with EU law, and limited the scope of its action to the civil [as opposed to military] side of the operation." *See generally* Roberto, *The Boeing/McDonnell Douglas Merger Review: A Serious Stretch of European Competition Powers*, 24 Brook. J. Int'l L. 593 (1998).

In part, the EC opposed the Boeing/McDonnell Douglas merger because of concern of possible "portfolio effects" or "range effects" emanating from the acquisition. The terms refer to the potential of a dominant firm extending its market power into a complementary product market. For example, purchasers often prefer buying a full line of complementary products from a single seller, rather than selecting each product from different suppliers who do not offer a full product line. Thus, if, through an acquisition, a company with market power extends its complementary product lines, it may in theory enable the company to foreclose market access to firms that do not offer a full line. According to the Commission, Boeing's large fleet in service coupled with increasing its types of available commercial aircraft through the acquisition of McDonnell-Douglas "can be a key factor which may often determine decisions of airlines on fleet planning or acquisitions."

Portfolio effects played a major role in the Commission's 2001 decision to block the $43 million acquisition of Honeywell by conglomerate General Electric, which is the largest maker of jet engines. Honeywell manufactures industrial automation and control systems (avionics) for the aerospace industry. The U.S. Department of Justice Antitrust Division indicated it would not oppose the merger on the minor condition that the merged entity sell off its helicopter engine business. The European Commission, however, blocked the takeover because of its concern that the combining of Honeywell's avionics and GE's dominant position in jet engines might lead to

dominance of the aerospace supply markets. The Commission was concerned, among other issues, that GE would be able to offer low price "bundles" of aircraft engines and avionics to which single or narrow-line competitors could not compete. *See General Electric/Honeywell Case* COMP/M.2220, Commission Decision of July 3, 2001.

The decision, which was the Commission's first block of a merger involving two U.S. companies, heightened trade enmity between the European Union and the United States. It also signaled a marked divergence in antitrust policy, since the Antitrust Division was persuaded that the merged firm would benefit customers by offering lower prices and better products and by inducing rivals to respond with better quality and lower prices. In other words, the Commission appears more concerned with competitors and less with consumers than does the United States.

The parties appealed to the European Court of First Instance, which took more than four years to render its decision. It did so in late 2005, *see General Electric Co. v. Commission*, Case T-210/99 (Dec. 14, 2005), upholding the Commission's rejection of the merger but on a much narrower basis. The Court was troubled by certain horizontal aspects of the merger, such as the regional jet engine market, the corporate jet engine market, and the market for small marine gas turbines. It held, however, that the Commission had failed to adequately establish any "conglomerate effects" or advantages based on the merged company's bundling of products or services and offering customers better deals than the competition.

The *General Electric* decision was the latest of several in which the Court of First Instance overturned or criticized Commission merger findings. *See Tetra Laval BV v. Commission*, Cases T-5/02 and T-80/02 (Oct. 25, 2002); *Schneider Electric SA v. Commission*, Cases T-310/01 and T-77/02 (Oct. 22, 2002); *Airtours plc v. Commission*, Case No. T-342/99 (June 6, 2002). These decisions, at least in part, may be the harbinger of change, as the EC's "regulatory zeal" seems to be waning. By the middle of the current decade it had approved a number of large mergers, including Oracle's takeover of PeopleSoft Inc., Proctor & Gamble's $53 billion acquisition of Gillette Co., and Johnson & Johnson's $25.4 billion purchase of Guidant Corp., a medical device maker. Further, GE itself had received EC approval on 13 acquisitions since the Honeywell ruling in 2001. *See* M. Jacoby, *Court Backs EU on Blocked GE Deal — But Future Acquisitions Might Be More Difficult To Reject Based on Ruling*, Wall Street Journal, Dec. 15, 2005, at A3.

On page 729, delete note (5), renumber note (6) to (5), and add the following note (6):

(6) Independent of federal antitrust law, a number of states continue to view resale price maintenance as illegal per se under their own antitrust laws or other state laws. Indeed, in 2009 Maryland amended its antitrust law to make resale price maintenance illegal. Maryland Antitrust Act, Md. Code Ann. Com. Law § 11-204(b). And there have been several bills introduced in Congress to the same effect, though those bills have not progressed far in the legislative process.

Two recent cases, in California and New York, illustrate the importance of state law in this area. In February 2010, the California Attorney General brought suit in California state court

alleging that DermaQuest, a maker of cosmetics, committed a per se violation of California's antitrust law, the Cartwright Act, by entering into RPM agreements with distributors. DermaQuest entered into a consent judgment, agreeing to disavow the agreements, refrain from RPM in the future, and pay a civil penalty and investigative costs. antitrust statute by entering into agreements with sellers. *See* 98 Antitrust & Trade Reg. Rep. (BNA) 316 (3/12/10).

In the New York case, the attorney general filed a petition in March 2010 alleging resale price maintenance by Tempur-Pedic International, Inc., a maker of mattresses. The petition did not assert claims under the Sherman Act or under New York's own antitrust statute, the Donnelly Act, but instead under New York General Business Code § 369-a, which provides that "[a]ny contract provision that purports to restrain a vendee of a commodity from reselling such commodity at less than the price stipulated by the vendor or producer shall not be enforceable or actionable at law." This statute appears to establish a per se rule, but it is less clear whether its provision that RPM is "unenforceable" gives rise to an independent action against the seller. The case is pending. *See* 98 Antitrust & Trade Reg. Rep. (BNA) 464 (4/16/10). The New York courts held in the *Tempur-Pedic* litigation that resale pricing policy was not illegal price-fixing or fraudulent conduct and did not constitute an unenforceable price-fixing contract. *People ex rel. State v. Tempur-Pedic Int'l, Inc.*, 916 N.Y.S.2d 900 (2011) (granting defendant's motion to dismiss), *order aff'd, People v. Tempur-Pedic Int'l, Inc.*, 944 N.Y.S.2d 518 (N.Y. 2012).

On p. 765, insert the following note:

Note on *Brantley v. NBC Universal, Inc.*

A recent case from the Ninth Circuit raises interesting questions about how tying affects competition. The plaintiffs in *Brantley v. NBC Universal, Inc.*, 675 F.3d 1192 (9th Cir. 2012), were a class of cable and satellite television subscribers, and the defendants were programmers that produced television programming and distributors that delivered that programming over their cable and satellite systems. With respect to the tying allegations, the programmers produced both "'must-have' channels with high demand and a large number of viewers" and "less desirable, low-demand channels with low viewership," and they provided the channels only in packages. As a result, the plaintiffs alleged, "distributors can offer consumers only prepackaged tiers of cable channels which consist of each programmer's entire offering of channels." The court said that "[i]n essence, plaintiffs seek to compel programmers and distributors of television programming to sell each cable channel separately, thereby permitting plaintiffs to purchase only those channels that they wish to purchase, rather than paying for multi-channel packages, as occurs under current market practice."

The central problem with the plaintiffs' case, in the court's view, was that they did not allege that any providers of programming were foreclosed from the market. The plaintiffs initially made such an allegation but then abandoned it, as the court emphasized: "The [amended] complaint does not allege that Programmers' practice of selling 'must-have' and low-demand channels in packages excludes other sellers of low-demand channels from the market, or that this practice raises barriers to entry into the programming market." This, the court said,

distinguished the case from *United States v. Loew's, Inc.*, 371 U.S. 38 (1962), where it said the somewhat similar block-booking requirement did cause such foreclosure. Therefore, the court concluded that "the mere allegations that Programmers have chosen to limit the ability of Distributors to offer Programmers' channels for sale individually does not state a cognizable injury to competition."

The court also relied on the Supreme Court's statement in *Jefferson Parish* that "when a purchaser is 'forced' to buy a product he would not have otherwise bought even from another seller in the tied product market, there can be no adverse impact on competition because no portion of the market which would otherwise have been available to other sellers has been foreclosed." That is, at least if we imagine that cable and satellite capacity is unlimited, as the court presumably was doing, forcing distributors to carry unwanted channels would not prevent them from carrying other channels as well. It might not even raise prices, because, as the Federal Circuit said in a patent case, "[i]t is entirely rational for a patentee who has a patent that is essential to particular technology, as well as other patents that are not essential, to charge what the market will bear for the essential patent and to offer the others for free." *U.S. Philips Corp. v. International Trade Comm'n*, 424 F.3d 1179, 1191 (Fed. Cir. 2005). Analogously, perhaps the programmers could charge the full price for the "must-have" channels and provide the others for free.

However, the court acknowledged, following *Leegin*, that given the widespread use of the package deals by programmers, "[w]e cannot rule out the possibility that competition could be injured or reduced due to a widely applied practice that harms consumers." It said, though, that "the plaintiffs here have not alleged in their complaint how competition (rather than consumers) is injured by the widespread practice of packaging low- and high-demand channels." (If the court is suggesting here that consumers were in fact injured, but not by any harm to competition, it does not make clear what *other* mechanism might have caused that consumer injury.) The plaintiffs' problem, therefore, might have arisen not so much from the law as from the absence of appropriate factual allegations. As so often in tying cases, one wonders why the defendants would insist on a particular package arrangement if it had no competitive effect, and if there was a procompetitive effect from the programmers' packaging, it was not made clear in the case.

Considering possible factual allegations, one might ask whether it is true that the requirement of distribution of a large number of low-demand channels makes it less likely that a distributor would be interested in independent programming. Although the plaintiffs abandoned this claim, it seems likely that there would be diminishing returns to a distributor from including additional channels as the number of channels increases. It also seems plausible that a programmer's ability to require that a channel be carried by a distributor would lessen the programmer's investment in the quality of that channel. Perhaps, though, any such effect would be outweighed by the desire to attract viewers, not just distributors.

In light of the plaintiffs' ultimate approach, these questions were not explored in the case. It is worth contemplating, though, what evidence would have been sufficient to establish these effects, or even obtain discovery regarding them, given that the case was dismissed for failure to state a claim. As the court said, quoting *Twombly*, the "complaint does not allege facts that 'raise a reasonable expectation that discovery will reveal evidence of' injury to competition." What

facts could the plaintiffs have alleged that would have enabled them to overcome the *Twombly* hurdle? And if such facts were difficult to come by, why did the plaintiffs not bring a per se tying claim?

On page 1024, following the notes on *Omni*, insert:

FEDERAL TRADE COMMISSION v. PHOEBE PUTNEY HEALTH SYSTEM, INC.

Supreme Court of the United States
133 S. Ct. 1003 (2013)

JUSTICE SOTOMAYOR delivered the opinion of the [unanimous] Court.

Under this Court's state-action immunity doctrine, when a local governmental entity acts pursuant to a clearly articulated and affirmatively expressed state policy to displace competition, it is exempt from scrutiny under the federal antitrust laws. In this case, we must decide whether a Georgia law that creates special-purpose public entities called hospital authorities and gives those entities general corporate powers, including the power to acquire hospitals, clearly articulates and affirmatively expresses a state policy to permit acquisitions that substantially lessen competition. Because Georgia's grant of general corporate powers to hospital authorities does not include permission to use those powers anticompetitively, we hold that the clear-articulation test is not satisfied and state-action immunity does not apply.

I

A

In 1941, the State of Georgia amended its Constitution to allow political subdivisions to provide health care services. The State concurrently enacted the Hospital Authorities Law (Law) "to provide a mechanism for the operation and maintenance of needed health care facilities in the several counties and municipalities of th[e] state." . . . As amended, the Law authorizes each county and municipality, and certain combinations of counties or municipalities, to create "a public body corporate and politic" called a "hospital authority." Hospital authorities are governed by 5- to 9-member boards that are appointed by the governing body of the county or municipality in their area of operation.

Under the Law, a hospital authority "exercise[s] public and essential governmental functions" and is delegated "all the powers necessary or convenient to carry out and effectuate" the Law's purposes. Giving more content to that general delegation, the Law enumerates 27 powers conferred upon hospital authorities, including the power "[t]o acquire by purchase, lease, or otherwise and to operate projects," which are defined to include hospitals and other public health facilities; "[t]o construct, reconstruct, improve, alter, and repair projects;" "[t]o lease . . . for operation by others any project" provided certain conditions are satisfied; and "[t]o establish rates and charges for the services and use of the facilities of the authority." Hospital authorities may not operate or construct any project for profit, and accordingly they must set rates so as only to cover operating expenses and create reasonable reserves.

B

In the same year that the Law was adopted, the city of Albany and Dougherty County established the Hospital Authority of Albany-Dougherty County (Authority) and the Authority promptly acquired Phoebe Putney Memorial Hospital (Memorial), which has been in operation in Albany since 1911. In 1990, the Authority restructured its operations by forming two private nonprofit corporations to manage Memorial: Phoebe Putney Health System, Inc. (PPHS), and its subsidiary, Phoebe Putney Memorial Hospital, Inc. (PPMH). The Authority leased Memorial to PPMH for $1 per year for 40 years. Under the lease, PPMH has exclusive authority over the operation of Memorial, including the ability to set rates for services. . . . PPMH is subject to lease conditions that require provision of care to the indigent sick and limit its rate of return.

Memorial is one of two hospitals in Dougherty County. The second, Palmyra Medical Center (Palmyra), was established in Albany in 1971 and is located just two miles from Memorial. . . . Together, Memorial and Palmyra account for 86 percent of the market for acute-care hospital services provided to commercial health care plans and their customers in the six counties surrounding Albany. . . .

In 2010, PPHS began discussions with HCA [which owned Palmyra] about acquiring Palmyra. Following negotiations, PPHS presented the Authority with a plan under which the Authority would purchase Palmyra with PPHS controlled funds and then lease Palmyra to a PPHS subsidiary for $1 per year under the Memorial lease agreement. The Authority unanimously approved the transaction.

The Federal Trade Commission (FTC) shortly thereafter issued an administrative complaint alleging that the proposed purchase-and-lease transaction would create a virtual monopoly and would substantially reduce competition in the market for acute-care hospital services, in violation of § 5 of the Federal Trade Commission Act and §7 of the Clayton Act. The FTC, along with the State of Georgia,[51] subsequently filed suit against the Authority, HCA, Palmyra, PPHS, PPMH, and the new PPHS subsidiary created to manage Palmyra (collectively respondents), seeking to enjoin the transaction pending administrative proceedings.

The United States District Court for the Middle District of Georgia denied the request for a preliminary injunction and granted respondents' motion to dismiss. The District Court held that respondents are immune from antitrust liability under the state-action doctrine.

The United States Court of Appeals for the Eleventh Circuit affirmed. As an initial matter, the court "agree[d] with the [FTC] that, on the facts alleged, the joint operation of Memorial and Palmyra would substantially lessen competition or tend to create, if not create, a monopoly." But the court concluded that the transaction was immune from antitrust liability. The Court of Appeals explained that as a local governmental entity, the Authority was entitled to state-action immunity if the challenged anticompetitive conduct was a "'foreseeable result'" of Georgia's legislation. According to the court, anticompetitive conduct is foreseeable if it could have been "'reasonably anticipated'" by the state legislature; it is not necessary, the court reasoned, for an anticompetitive effect to " be 'one that ordinarily occurs, routinely occurs, or is inherently likely to occur as a result of the empowering legislation.'" (quoting FTC v. Hospital Bd. of Directors of Lee Cty., 38 F.3d

[1] Georgia did not join the notice of appeal filed by the FTC and is no longer a party in the case.

1184, 1188, 1190-1191 (CA11 1994)). Applying that standard, the Court of Appeals concluded that the Law contemplated the anticompetitive conduct challenged by the FTC. The court noted the "impressive breadth" of the powers given to hospital authorities, which include traditional powers of private corporations and a few additional capabilities, such as the power to exercise eminent domain. More specifically, the court reasoned that the Georgia Legislature must have anticipated that the grant of power to hospital authorities to acquire and lease projects would produce anticompetitive effects because "[f]oreseeably, acquisitions could consolidate ownership of competing hospitals, eliminating competition between them."

. . . .

We granted certiorari on two questions: whether the Georgia Legislature, through the powers it vested in hospital authorities, clearly articulated and affirmatively expressed a state policy to displace competition in the market for hospital services; and if so, whether state-action immunity is nonetheless inapplicable as a result of the Authority's minimal participation in negotiating the terms of the sale of Palymra and the Authority's limited supervision of the two hospitals' operations. Concluding that the answer to the first question is "no," we reverse without reaching the second question.

II

In Parker v. Brown , 317 U.S. 341 (1943), this Court held that because "nothing in the language of the Sherman Act or in its history" suggested that Congress intended to restrict the sovereign capacity of the States to regulate their economies, the Act should not be read to bar States from imposing market restraints "as an act of government." Following Parker, we have held that under certain circumstances, immunity from the federal antitrust laws may extend to nonstate actors carrying out the State's regulatory program.

But given the fundamental national values of free enterprise and economic competition that are embodied in the federal antitrust laws, "state-action immunity is disfavored, much as are repeals by implication." Consistent with this preference, we recognize state-action immunity only when it is clear that the challenged anticompetitive conduct is undertaken pursuant to a regulatory scheme that "is the State's own." Accordingly, "[c]loser analysis is required when the activity at issue is not directly that of" the State itself, but rather "is carried out by others pursuant to state authorization." When determining whether the anticompetitive acts of private parties are entitled to immunity, we employ a two-part test, requiring first that "the challenged restraint . . . be one clearly articulated and affirmatively expressed as state policy," and second that "the policy . . . be actively supervised by the State." *California Regtail Liquor Dealers Assn. v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980) (internal quotation marks omitted).

This case involves allegedly anticompetitive conduct undertaken by a substate governmental entity. Because municipalities and other political subdivisions are not themselves sovereign, state-action immunity under Parker does not apply to them directly. At the same time, however, substate governmental entities do receive immunity from antitrust scrutiny when they act "pursuant to state policy to displace competition with regulation or monopoly public service."[64] . . .

[4] An *amicus curiae* contends that we should recognize and apply a "market participant" exception to state-action immunity because Georgia's hospital authorities engage in proprietary activities. Brief for National

As with private parties, immunity will only attach to the activities of local governmental entities if they are undertaken pursuant to a "clearly articulated and affirmatively expressed" state policy to displace competition. *Community Communications Co. v. Boulder*, 455 U.S. 40, 52 (1982). But unlike private parties, such entities are not subject to the "active state supervision requirement" because they have less of an incentive to pursue their own self-interest under the guise of implementing state policies. *Hallie v. Eau Claire,* 470 U.S. 34, 46-47 (1985).

"[T]o pass the 'clear articulation' test," a state legislature need not "expressly state in a statute or its legislative history that the legislature intends for the delegated action to have anticompetitive effects." Id., at 43. Rather, we explained in *Hallie* that state-action immunity applies if the anticompetitive effect was the "foreseeable result" of what the State authorized. We applied that principle in *Omni*, where we concluded that the clear articulation test was satisfied because the suppression of competition in the billboard market was the foreseeable result of a state statute authorizing municipalities to adopt zoning ordinances regulating the construction of buildings and other structures.

III

A

Applying the clear-articulation test to the Law before us, we conclude that respondents' claim for state-action immunity fails because there is no evidence the State affirmatively contemplated that hospital authorities would displace competition by consolidating hospital ownership. The acquisition and leasing powers exercised by the Authority in the challenged transaction, which were the principal powers relied upon by the Court of Appeals in finding state-action immunity, mirror general powers routinely conferred by state law upon private corporations. Other powers possessed by hospital authorities that the Court of Appeals characterized as having "impressive breadth" also fit this pattern, including the ability to make and execute contracts, to set rates for services, to sue and be sued, to borrow money, and the residual authority to exercise any or all powers possessed by private corporations.

Our case law makes clear that state-law authority to act is insufficient to establish state-action immunity; the substate governmental entity must also show that it has been delegated authority to act or regulate anticompetitively. In *Boulder*, we held that Colorado's Home Rule Amendment allowing municipalities to govern local affairs did not satisfy the clear-articulation test. There was no doubt in that case that the city had authority as a matter of state law to pass an ordinance imposing a moratorium on a cable provider's expansion of service. But we rejected the proposition that "the general grant of power to enact ordinances necessarily implies state authorization to enact specific anticompetitive ordinances" because such an approach "would wholly eviscerate the concepts of 'clear articulation and affirmative expression' that our precedents require." *Id.*, at 56. We explained that when a State's position "is one of mere neutrality respecting the municipal actions challenged as anticompetitive," the State cannot be said to have "'contemplated'" those anticompetitive actions. *Id.*, at 55.

Federation of Independent Business 6-24; see also *Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.s. 365, 374-75, 379 (1991) (leaving open the possibility of a market participant exception). Because this argument was not raised by the parties or passed on by the lower courts, we do not consider it.

The principle articulated in *Boulder* controls this case. Grants of general corporate power that allow substate governmental entities to participate in a competitive marketplace should be, can be, and typically are used in ways that raise no federal antitrust concerns. As a result, a State that has delegated such general powers "can hardly be said to have 'contemplated'" that they will be used anticompetitively. Ibid. See also 1A P. Areeda & H. Hovenkamp, Antitrust Law P225a, p. 131 (3d ed. 2006) (hereinafter Areeda & Hovenkamp) ("When a state grants power to an inferior entity, it presumably grants the power to do the thing contemplated, but not to do so anticompetitively"). Thus, while the Law does allow the Authority to acquire hospitals, it does not clearly articulate and affirmatively express a state policy empowering the Authority to make acquisitions of existing hospitals that will substantially lessen competition.

B

In concluding otherwise, and specifically in reasoning that the Georgia Legislature "must have anticipated" that acquisitions by hospital authorities "would produce anticompetitive effects," the Court of Appeals applied the concept of "foreseeability" from our clear-articulation test too loosely.

In *Hallie*, we recognized that it would "embod[y] an unrealistic view of how legislatures work and of how statutes are written" to require state legislatures to explicitly authorize specific anticompetitive effects before state-action immunity could apply. "No legislature," we explained, "can be expected to catalog all of the anticipated effects" of a statute delegating authority to a sub-state governmental entity. Instead, we have approached the clear-articulation inquiry more practically, but without diluting the ultimate requirement that the State must have affirmatively contemplated the displacement of competition such that the challenged anticompetitive effects can be attributed to the "state itself." *Parker*, 317 U.S., at 352. Thus, we have concluded that a state policy to displace federal antitrust law was sufficiently expressed where the displacement of competition was the inherent, logical, or ordinary result of the exercise of authority delegated by the state legislature. In that scenario, the State must have foreseen and implicitly endorsed the anticompetitive effects as consistent with its policy goals.

For example, in *Hallie*, Wisconsin statutory law regulating the municipal provision of sewage services expressly permitted cities to limit their service to surrounding unincorporated areas. See 471 U.S., at 41. While unincorporated towns alleged that the city's exercise of that power constituted an unlawful tying arrangement, an unlawful refusal to deal, and an abuse of monopoly power, we had no trouble concluding that these alleged anticompetitive effects were affirmatively contemplated by the State because it was "clear" that they "logically would result" from the grant of authority. *Id.*, at 42. As described by the Wisconsin Supreme Court, the state legislature "'viewed annexation by the city of a surrounding unincorporated area as a reasonable quid pro quo that a city could require before extending sewer services to the area.'" Id. , at 44-45, n. 8, (quoting Hallie v. Chippewa Falls , 105 Wis. 2d 533, 540-541, 314 N. W. 2d 321, 325 (1982)). Without immunity, federal antitrust law could have undermined that arrangement and taken completely off the table the policy option that the State clearly intended for cities to have.

Similarly, in *Omni*, where the respondents alleged that the city had used its zoning power to protect an incumbent billboard provider against competition, we found that the clear-articulation test was easily satisfied even though the state statutes delegating zoning authority to the city did not explicitly permit the suppression of competition. We explained that "[t]he very

purpose of zoning regulation is to displace unfettered business freedom in a manner that regularly has the effect of preventing normal acts of competition" and that a zoning ordinance regulating the size, location, and spacing of billboards "necessarily protects existing billboards against some competition from newcomers." 499 U.S., at 373. Other cases in which we have found a "clear articulation" of the State's intent to displace competition without an explicit statement have also involved authorizations to act or regulate in ways that were inherently anti-competitive.[77]

By contrast, "simple permission to play in a market" does not "foreseeably entail permission to roughhouse in that market unlawfully." Kay Elec. Cooperative v. Newkirk , 647 F.3d 1039, 1043 (CA10 2011). When a State grants some entity general power to act, whether it is a private corporation or a public entity like the Authority, it does so against the backdrop of federal antitrust law. Of course, both private parties and local governmental entities conceivably may transgress antitrust requirements by exercising their general powers in anticompetitive ways. But a reasonable legislature's ability to anticipate that (potentially undesirable) possibility falls well short of clearly articulating an affirmative state policy to displace competition with a regulatory alternative.

Believing that this case falls within the scope of the foreseeability standard applied in *Hallie* and *Omni*, the Court of Appeals stated that "[i]t defies imagination to suppose the [state] legislature could have believed that every geographic market in Georgia was so replete with hospitals that authorizing acquisitions by the authorities could have no serious anticompetitive consequences." Respondents echo this argument, noting that each of Georgia's 159 counties covers a small geographical area and that most of them are sparsely populated . . . .

Even accepting, arguendo, the premise that facts about a market could make the anticompetitive use of general corporate powers "foreseeable," we reject the Court of Appeals' and respondents' conclusion because only a relatively small subset of the conduct permitted as a matter of state law by Ga. Code Ann. §31-7-75(4) has the potential to negatively affect competition. Contrary to the Court of Appeals' and respondents' characterization, §31-7-75(4) is not principally concerned with hospital authorities' ability to acquire multiple hospitals and consolidate their operations. Section 31-7-75(4) allows authorities to acquire "projects," which includes not only "hospitals," but also "health care facilities, dormitories, office buildings, clinics, housing accommodations, nursing homes, rehabilitation centers, extended care facilities, and other public health facilities." Narrowing our focus to the market for hospital services, the power to acquire hospitals still does not ordinarily produce anticompetitive effects. Section 31-7-75(4) was, after all, the source of power for newly formed hospital authorities to acquire a hospital in the first instance . . . .

IV

A

Taking a somewhat different approach than the Court of Appeals, respondents . . . contend that hospital authorities are granted unique powers and responsibilities to fulfill the State's

[7] See *Southern Motor Carriers rate Conference, Inc. v. United States* (finding that a state commission's decision to encourage collective ratemaking by common carriers was entitled to state-action immunity where the legislature had left "[t]he details of the inherently anticompetitive rate-setting process . . . to the agency's discretion); . . . .

objective of providing all residents with access to adequate and affordable health and hospital care. Respondents argue that in view of hospital authorities' statutory objective, their specific attributes, and the regulatory context in which they operate, it was foreseeable that authorities facing capacity constraints would decide they could best serve their communities' needs by acquiring an existing local hospital rather than incur the additional expense and regulatory burden of expanding a facility or constructing a new one. In support of this argument, respondents observe that hospital authorities are simultaneously empowered to act in ways private entities cannot while also being subject to significant regulatory constraints. On the power side, as the Court of Appeals noted, hospital authorities may acquire through eminent domain property that is "essential to the [authority's] purposes." On the restraint side, hospital authorities are managed by a publicly accountable board, they must operate on a nonprofit basis, and they may only lease a project for others to operate after determining that doing so will promote the community's public health needs and that the lessee will not receive more than a reasonable rate of return on its investment. Moreover, hospital authorities operate within a broader regulatory context in which Georgia requires any party seeking to establish or significantly expand certain medical facilities, including hospitals, to obtain a certificate of need from state regulators.

We have no doubt that Georgia's hospital authorities differ materially from private corporations that offer hospital services. But nothing in the Law or any other provision of Georgia law clearly articulates a state policy to allow authorities to exercise their general corporate powers, including their acquisition power, without regard to negative effects on competition. The state legislature's objective of improving access to affordable health care does not logically suggest that the State intended that hospital authorities pursue that end through mergers that create monopolies. . . .

We recognize that Georgia, particularly through its certificate of need requirement, does limit competition in the market for hospital services in some respects. But regulation of an industry, and even the authorization of discrete forms of anticompetitive conduct pursuant to a regulatory structure, does not establish that the State has affirmatively contemplated other forms of anticompetitive conduct that are only tangentially related. . . .

B

Finally, respondents contend that to the extent there is any doubt about whether the clear articulation test is satisfied in this context, federal courts should err on the side of recognizing immunity to avoid improper interference with state policy choices. But we do not find the Law ambiguous . . . . More fundamentally, respondents' suggestion is inconsistent with the principle that "state-action immunity is disfavored." *Ticor Title*, 504 U.S., at 636. *Parker* and its progeny are premised on an understanding that respect for the States' coordinate role in government counsels against reading the federal antitrust laws to restrict the States' sovereign capacity to regulate their economies and provide services to their citizens. But federalism and state sovereignty are poorly served by a rule of construction that would allow "essential national policies" embodied in the antitrust laws to be displaced by state delegations of authority "intended to achieve more limited ends." 504 U.S., at 636. As an amici brief filed by 20 States in support of the FTC contends, loose application of the clear-articulation test would attach significant unintended consequences to States' frequent delegations of corporate authority to local bodies, effectively requiring States to disclaim any intent to displace competition to avoid inadvertently authorizing anticompetitive

conduct. Brief for State of Illinois et al. as Amici Curiae 12-17 . . . . We decline to set such a trap for unwary state legislatures.

* * *

We hold that Georgia has not clearly articulated and affirmatively expressed a policy to allow hospital authorities to make acquisitions that substantially lessen competition. . . .

Notes and Questions

(1) Should the Court have entered a simple order summarily reversing and remanding for failure to follow Supreme Court precedent? Does the opinion change anything?

(2) Variation on the theme: Will this opinion result in anything more than states generating a little extra legislative history when statutes such as Georgia's are enacted? (And would a mention in the legislative history be enough?) Note that the states, unlike the federal government, often do not keep records of legislative history.

(3) Imagine state authorization to license a trade or profession. Are denials and revocations of licenses automatically exempt, or not?

(4) Does *Phoebe Putney* suggest that the current Court is hostile to exemptions?

(5) Any guess as to why Georgia would have joined the FTC in challenging the acquisition, then not joined in the appeal?

On pp. 1155-67, replace *Schering-Plough* and the subsequent notes with the following case:

FEDERAL TRADE COMMISSION v. ACTAVIS, INC.

Supreme Court of the United States
133 S. Ct. 2223 (2013)

JUSTICE BREYER delivered the opinion of the Court.

Company A sues Company B for patent infringement. The two companies settle under terms that require (1) Company B, the claimed infringer, not to produce the patented product until the patent's term expires, and (2) Company A, the patentee, to pay B many millions of dollars. Because the settlement requires the patentee to pay the alleged infringer, rather than the other way around, this kind of settlement agreement is often called a "reverse payment" settlement agreement. And the basic question here is whether such an agreement can sometimes unreasonably diminish competition in violation of the antitrust laws. Cf. *Palmer v. BRG of Ga., Inc.*, 498 U.S. 46 (1990) (*per curiam*) (invalidating agreement not to compete).

In this case, the Eleventh Circuit dismissed a Federal Trade Commission (FTC) complaint claiming that a particular reverse payment settlement agreement violated the antitrust laws. In doing so, the Circuit stated that a reverse payment settlement agreement generally is "immune from antitrust attack so long as its anticompetitive effects fall within the scope of the exclusionary potential of the patent." *FTC v. Watson Pharmaceuticals, Inc*., 677 F.3d 1298, 1312 (2012). And since the alleged infringer's promise not to enter the patentee's market expired before the patent's term ended, the Circuit found the agreement legal and dismissed the FTC complaint. In our view, however, reverse payment settlements such as the agreement alleged in the complaint before us can sometimes violate the antitrust laws. We consequently hold that the Eleventh Circuit should have allowed the FTC's lawsuit to proceed.

I

A

Apparently most if not all reverse payment settlement agreements arise in the context of pharmaceutical drug regulation, and specifically in the context of suits brought under statutory provisions allowing a generic drug manufacturer (seeking speedy marketing approval) to challenge the validity of a patent owned by an already-approved brand-name drug owner. See 12 P. Areeda & H. Hovenkamp, Antitrust Law ¶ 2046, p. 338 (3d ed. 2012) (hereinafter Areeda); We consequently describe four key features of the relevant drug-regulatory framework established by the Drug Price Competition and Patent Term Restoration Act of 1984, 98 Stat. 1585, as amended. That Act is commonly known as the Hatch–Waxman Act.

First, a drug manufacturer, wishing to market a new prescription drug, must submit a New Drug Application to the federal Food and Drug Administration (FDA) and undergo a long, comprehensive, and costly testing process, after which, if successful, the manufacturer will receive marketing approval from the FDA. See 21 U.S.C. § 355(b)(1) (requiring, among other things, "full reports of investigations" into safety and effectiveness; "a full list of the articles used as components"; and a "full description" of how the drug is manufactured, processed, and packed).

Second, once the FDA has approved a brand-name drug for marketing, a manufacturer of a generic drug can obtain similar marketing approval through use of abbreviated procedures. The Hatch–Waxman Act permits a generic manufacturer to file an Abbreviated New Drug Application specifying that the generic has the "same active ingredients as," and is "biologically equivalent" to, the already-approved brand-name drug. *Caraco Pharmaceutical Laboratories, Ltd. v. Novo Nordisk A/S*, 566 U.S. ——, —— (2012) (citing 21 U.S.C. §§ 355(j)(2)(A)(ii), (iv)). In this way the generic manufacturer can obtain approval while avoiding the "costly and time-consuming studies" needed to obtain approval "for a pioneer drug." See *Eli Lilly & Co. v. Medtronic, Inc.*, 496 U.S. 661, 676 (1990). . . .

Third, the Hatch–Waxman Act sets forth special procedures for identifying, and resolving, related patent disputes. It requires the pioneer brand-name manufacturer to list in its New Drug Application the "number and the expiration date" of any relevant patent. See 21 U.S.C. § 355(b)(1). And it requires the generic manufacturer in its Abbreviated New Drug Application to "assure the FDA" that the generic "will not infringe" the brand-name's patents. See *Caraco, supra*, at ——, 132 S.Ct., at 1676.

The generic can provide this assurance in one of several ways. See 21 U.S.C. § 355(j)(2)(A)(vii). It can certify that the brand-name manufacturer has not listed any relevant patents. It can certify that any relevant patents have expired. It can request approval to market beginning when any still-in-force patents expire. Or, it can certify that any listed, relevant patent "is invalid or will not be infringed by the manufacture, use, or sale" of the drug described in the Abbreviated New Drug Application. See § 355(j)(2)(A)(vii)(IV). Taking this last-mentioned route (called the "paragraph IV" route), automatically counts as patent infringement, see 35 U.S.C. § 271(e)(2)(A) (2006 ed., Supp. V), and often "means provoking litigation." *Caraco, supra,* at ——. If the brand-name patentee brings an infringement suit within 45 days, the FDA then must withhold approving the generic, usually for a 30–month period, while the parties litigate patent validity (or infringement) in court. If the courts decide the matter within that period, the FDA follows that determination; if they do not, the FDA may go forward and give approval to market the generic product. See 21 U.S.C. § 355(j)(5)(B)(iii).

Fourth, Hatch–Waxman provides a special incentive for a generic to be the first to file an Abbreviated New Drug Application taking the paragraph IV route. That applicant will enjoy a period of 180 days of exclusivity (from the first commercial marketing of its drug). See § 355(j)(5)(B)(iv) (establishing exclusivity period). During that period of exclusivity no other generic can compete with the brand-name drug. If the first-to-file generic manufacturer can overcome any patent obstacle and bring the generic to market, this 180–day period of exclusivity can prove valuable, possibly "worth several hundred million dollars." Hemphill, Paying for Delay: Pharmaceutical Patent Settlement as a Regulatory Design Problem, 81 N.Y.U. L.Rev. 1553, 1579 (2006). . . . The 180–day exclusivity period, however, can belong only to the first generic to file. Should that first-to-file generic forfeit the exclusivity right in one of the ways specified by statute, no other generic can obtain it. See § 355(j)(5)(D).

B

1

In 1999, Solvay Pharmaceuticals, a respondent here, filed a New Drug Application for a brand-name drug called AndroGel. The FDA approved the application in 2000. In 2003, Solvay obtained a relevant patent and disclosed that fact to the FDA, as Hatch–Waxman requires.

Later the same year another respondent, Actavis, Inc. (then known as Watson Pharmaceuticals), filed an Abbreviated New Drug Application for a generic drug modeled after AndroGel. Subsequently, Paddock Laboratories, also a respondent, separately filed an Abbreviated New Drug Application for its own generic product. Both Actavis and Paddock certified under paragraph IV that Solvay's listed patent was invalid and their drugs did not infringe it.

Solvay initiated paragraph IV patent litigation against Actavis and Paddock. Thirty months later the FDA approved Actavis' first-to-file generic product, but, in 2006, the patent-litigation parties all settled. Under the terms of the settlement Actavis agreed that it would not bring its generic to market until August 31, 2015, 65 months before Solvay's patent expired (unless someone else marketed a generic sooner). Actavis also agreed to promote AndroGel to urologists. The other generic manufacturers made roughly similar promises. And Solvay agreed to pay millions of dollars to each generic—$12 million in total to Paddock; $60 million in total to Par; and an estimated $19–$30 million annually, for nine years, to Actavis. The companies

described these payments as compensation for other services the generics promised to perform, but the FTC contends the other services had little value. According to the FTC the true point of the payments was to compensate the generics for agreeing not to compete against AndroGel until 2015.

2

On January 29, 2009, the FTC filed this lawsuit against all the settling parties . . . . The FTC's complaint (as since amended) alleged that respondents violated § 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, by unlawfully agreeing "to share in Solvay's monopoly profits, abandon their patent challenges, and refrain from launching their low-cost generic products to compete with AndroGel for nine years." App. 29, Complaint ¶ 5. The District Court held that these allegations did not set forth an antitrust law violation. It accordingly dismissed the FTC's complaint. The FTC appealed.

The Court of Appeals for the Eleventh Circuit affirmed the District Court. It wrote that "absent sham litigation or fraud in obtaining the patent, a reverse payment settlement is immune from antitrust attack so long as its anticompetitive effects fall within the scope of the exclusionary potential of the patent." 677 F.3d, at 1312. The court recognized that "antitrust laws typically prohibit agreements where one company pays a potential competitor not to enter the market." *Id.*, at 1307 (citing *Valley Drug Co. v. Geneva Pharmaceuticals, Inc.*, 344 F.3d 1294, 1304 (C.A.11 2003)). See also *Palmer*, 498 U.S., at 50 (agreement to divide territorial markets held "unlawful on its face"). But, the court found that "reverse payment settlements of patent litigation presen[t] atypical cases because one of the parties owns a patent." 677 F.3d, at 1307 (internal quotation marks and second alteration omitted). Patent holders have a "lawful right to exclude others from the market," *ibid.* (internal quotation marks omitted); thus a patent "conveys the right to cripple competition." *Id.*, at 1310 (internal quotation marks omitted). The court recognized that, if the parties to this sort of case do not settle, a court might declare the patent invalid. But, in light of the public policy favoring settlement of disputes (among other considerations) it held that the courts could not require the parties to continue to litigate in order to avoid antitrust liability.

The FTC sought certiorari. Because different courts have reached different conclusions about the application of the antitrust laws to Hatch–Waxman–related patent settlements, we granted the FTC's petition. Compare, *e.g.*, *id.*, at 1312 (case below) (settlements generally "immune from antitrust attack"); *In re Ciprofloxacin Hydrochloride Antitrust Litigation*, 544 F.3d 1323, 1332–1337 (C.A.Fed.2008) (similar); *In re Tamoxifen Citrate Antitrust Litigation*, 466 F.3d 187, 212–213 (C.A.2 2006) (similar), with *In re K–Dur Antitrust Litigation*, 686 F.3d 197, 214–218 (C.A.3 2012) (settlements presumptively unlawful).

II

A

Solvay's patent, if valid and infringed, might have permitted it to charge drug prices sufficient to recoup the reverse settlement payments it agreed to make to its potential generic competitors. And we are willing to take this fact as evidence that the agreement's "anticompetitive effects fall within the scope of the exclusionary potential of the patent." 677

F.3d, at 1312. But we do not agree that that fact, or characterization, can immunize the agreement from antitrust attack.

For one thing, to refer, as the Circuit referred, simply to what the holder of a valid patent could do does not by itself answer the antitrust question. The patent here may or may not be valid, and may or may not be infringed. "[A] *valid* patent excludes all except its owner from the use of the protected process or product," *United States v. Line Material Co.,* 333 U.S. 287, 308 (1948) (emphasis added). And that exclusion may permit the patent owner to charge a higher-than-competitive price for the patented product. But an *invalidated* patent carries with it no such right. And even a valid patent confers no right to exclude products or processes that do not actually infringe. The paragraph IV litigation in this case put the patent's validity at issue, as well as its actual preclusive scope. The parties' settlement ended that litigation. The FTC alleges that in substance, the plaintiff agreed to pay the defendants many millions of dollars to stay out of its market, even though the defendants did not have any claim that the plaintiff was liable to them for damages. That form of settlement is unusual. And, for reasons discussed in Part II–B, *infra,* there is reason for concern that settlements taking this form tend to have significant adverse effects on competition.

Given these factors, it would be incongruous to determine antitrust legality by measuring the settlement's anticompetitive effects solely against patent law policy, rather than by measuring them against procompetitive antitrust policies as well. And indeed, contrary to the Circuit's view that the only pertinent question is whether "the settlement agreement ... fall[s] within" the legitimate "scope" of the patent's "exclusionary potential," 677 F.3d, at 1309, 1312, this Court has indicated that patent and antitrust policies are both relevant in determining the "scope of the patent monopoly"—and consequently antitrust law immunity—that is conferred by a patent.

. . . .

Thus, contrary to the dissent's suggestion, there is nothing novel about our approach. What *does* appear novel are the dissent's suggestions that a patent holder may simply "pa[y] a competitor to respect its patent" and quit its patent invalidity or noninfringement claim without any antitrust scrutiny whatever, *post,* at 2228, and that "such settlements ... are a well-known feature of intellectual property litigation," *post,* at 2243. Closer examination casts doubt on these claims. The dissent does not identify any patent statute that it understands to grant such a right to a patentee, whether expressly or by fair implication. It would be difficult to reconcile the proposed right with the patent-related policy of eliminating unwarranted patent grants so the public will not "continually be required to pay tribute to would-be monopolists without need or justification." *Lear, Inc. v. Adkins*, 395 U.S. 653, 670 (1969). And the authorities cited for this proposition (none from this Court, and none an antitrust case) are not on point. Some of them say that when Company A sues Company B for patent infringement and demands, say, $100 million in damages, it is not uncommon for B (the defendant) to pay A (the plaintiff) some amount less than the full demand as part of the settlement—$40 million, for example. See Schildkraut, Patent–Splitting Settlements and the Reverse Payment Fallacy, 71 Antitrust L.J. 1033, 1046 (2004) (suggesting that this hypothetical settlement includes "an implicit net payment" from A to B of $60 million—*i.e.*, the amount of the settlement discount). The cited authorities also indicate that if B has a counterclaim for damages against A, the original infringement plaintiff, A might end up paying B to settle B's counterclaim. Insofar as the dissent urges that settlements taking

these commonplace forms have not been thought for that reason alone subject to antitrust liability, we agree, and do not intend to alter that understanding. But the dissent appears also to suggest that reverse payment settlements—*e.g.*, in which A, the plaintiff, pays money to defendant B purely so B will give up the patent fight—should be viewed for antitrust purposes in the same light as these familiar settlement forms. We cannot agree. In the traditional examples cited above, a party with a claim (or counterclaim) for damages receives a sum equal to or less than the value of its claim. In reverse payment settlements, in contrast, a party with no claim for damages (something that is usually true of a paragraph IV litigation defendant) walks away with money simply so it will stay away from the patentee's market. That, we think, is something quite different.

Finally, the Hatch–Waxman Act itself does not embody a statutory policy that supports the Eleventh Circuit's view. Rather, the general procompetitive thrust of the statute, its specific provisions facilitating challenges to a patent's validity, see Part I–A, *supra*, and its later-added provisions requiring parties to a patent dispute triggered by a paragraph IV filing to report settlement terms to the FTC and the Antitrust Division of the Department of Justice, all suggest the contrary. See §§ 1112–1113, 117 Stat. 2461–2462. . . .

B

The Eleventh Circuit's conclusion finds some degree of support in a general legal policy favoring the settlement of disputes. The Circuit's related underlying practical concern consists of its fear that antitrust scrutiny of a reverse payment agreement would require the parties to litigate the validity of the patent in order to demonstrate what would have happened to competition in the absence of the settlement. Any such litigation will prove time consuming, complex, and expensive. The antitrust game, the Circuit may believe, would not be worth that litigation candle.

We recognize the value of settlements and the patent litigation problem. But we nonetheless conclude that this patent-related factor should not determine the result here. Rather, five sets of considerations lead us to conclude that the FTC should have been given the opportunity to prove its antitrust claim.

First, the specific restraint at issue has the "potential for genuine adverse effects on competition." *Indiana Federation of Dentists*, 476 U.S., at 460–461 (citing 7 Areeda ¶ 1511, at 429 (1986)). The payment in effect amounts to a purchase by the patentee of the exclusive right to sell its product, a right it already claims but would lose if the patent litigation were to continue and the patent were held invalid or not infringed by the generic product. Suppose, for example, that the exclusive right to sell produces $50 million in supracompetitive profits per year for the patentee. And suppose further that the patent has 10 more years to run. Continued litigation, if it results in patent invalidation or a finding of noninfringement, could cost the patentee $500 million in lost revenues, a sum that then would flow in large part to consumers in the form of lower prices.

We concede that settlement on terms permitting the patent challenger to enter the market before the patent expires would also bring about competition, again to the consumer's benefit. But settlement on the terms said by the FTC to be at issue here—payment in return for staying out of the market—simply keeps prices at patentee-set levels, potentially producing the full

patent-related $500 million monopoly return while dividing that return between the challenged patentee and the patent challenger. The patentee and the challenger gain; the consumer loses. Indeed, there are indications that patentees sometimes pay a generic challenger a sum even larger than what the generic would gain in profits if it won the paragraph IV litigation and entered the market. . . .

But, one might ask, as a practical matter would the parties be able to enter into such an anticompetitive agreement? Would not a high reverse payment signal to other potential challengers that the patentee lacks confidence in its patent, thereby provoking additional challenges, perhaps too many for the patentee to "buy off?" Two special features of Hatch–Waxman mean that the answer to this question is "not necessarily so." First, under Hatch–Waxman only the first challenger gains the special advantage of 180 days of an exclusive right to sell a generic version of the brand-name product. . . . Subsequent challengers cannot secure that exclusivity period, and thus stand to win significantly less than the first if they bring a successful paragraph IV challenge. . . . Second, a generic that files a paragraph IV after learning that the first filer has settled will (if sued by the brand-name) have to wait out a stay period of (roughly) 30 months before the FDA may approve its application, just as the first filer did. See 21 U.S.C. § 355(j)(5)(B)(iii). These features together mean that a reverse payment settlement with the first filer (or, as in this case, *all* of the initial filers) "removes from consideration the most motivated challenger, and the one closest to introducing competition." Hemphill, *supra*, at 1586. . . .

Second, these anticompetitive consequences will at least sometimes prove unjustified. As the FTC admits, offsetting or redeeming virtues are sometimes present. The reverse payment, for example, may amount to no more than a rough approximation of the litigation expenses saved through the settlement. That payment may reflect compensation for other services that the generic has promised to perform—such as distributing the patented item or helping to develop a market for that item. There may be other justifications. Where a reverse payment reflects traditional settlement considerations, such as avoided litigation costs or fair value for services, there is not the same concern that a patentee is using its monopoly profits to avoid the risk of patent invalidation or a finding of noninfringement. In such cases, the parties may have provided for a reverse payment without having sought or brought about the anticompetitive consequences we mentioned above. But that possibility does not justify dismissing the FTC's complaint. An antitrust defendant may show in the antitrust proceeding that legitimate justifications are present, thereby explaining the presence of the challenged term and showing the lawfulness of that term under the rule of reason.

Third, where a reverse payment threatens to work unjustified anticompetitive harm, the patentee likely possesses the power to bring that harm about in practice. At least, the "size of the payment from a branded drug manufacturer to a prospective generic is itself a strong indicator of power"—namely, the power to charge prices higher than the competitive level. 12 Areeda, ¶ 2046, at 351. An important patent itself helps to assure such power. . . .

Fourth, an antitrust action is likely to prove more feasible administratively than the Eleventh Circuit believed. The Circuit's holding does avoid the need to litigate the patent's validity (and also, any question of infringement). But to do so, it throws the baby out with the bath water, and there is no need to take that drastic step. That is because it is normally not

necessary to litigate patent validity to answer the antitrust question (unless, perhaps, to determine whether the patent litigation is a sham) An unexplained large reverse payment itself would normally suggest that the patentee has serious doubts about the patent's survival. And that fact, in turn, suggests that the payment's objective is to maintain supracompetitive prices to be shared among the patentee and the challenger rather than face what might have been a competitive market—the very anticompetitive consequence that underlies the claim of antitrust unlawfulness. The owner of a particularly valuable patent might contend, of course, that even a small risk of invalidity justifies a large payment. But, be that as it may, the payment (if otherwise unexplained) likely seeks to prevent the risk of competition. And, as we have said, that consequence constitutes the relevant anticompetitive harm. In a word, the size of the unexplained reverse payment can provide a workable surrogate for a patent's weakness, all without forcing a court to conduct a detailed exploration of the validity of the patent itself. 12 Areeda ¶ 2046, at 350–352.

Fifth, the fact that a large, unjustified reverse payment risks antitrust liability does not prevent litigating parties from settling their lawsuit. They may, as in other industries, settle in other ways, for example, by allowing the generic manufacturer to enter the patentee's market prior to the patent's expiration, without the patentee paying the challenger to stay out prior to that point. Although the parties may have reasons to prefer settlements that include reverse payments, the relevant antitrust question is: What are those reasons? If the basic reason is a desire to maintain and to share patent-generated monopoly profits, then, in the absence of some other justification, the antitrust laws are likely to forbid the arrangement.

In sum, a reverse payment, where large and unjustified, can bring with it the risk of significant anticompetitive effects; one who makes such a payment may be unable to explain and to justify it; such a firm or individual may well possess market power derived from the patent; a court, by examining the size of the payment, may well be able to assess its likely anticompetitive effects along with its potential justifications without litigating the validity of the patent; and parties may well find ways to settle patent disputes without the use of reverse payments. In our view, these considerations, taken together, outweigh the single strong consideration—the desirability of settlements—that led the Eleventh Circuit to provide near-automatic antitrust immunity to reverse payment settlements.

III

The FTC urges us to hold that reverse payment settlement agreements are presumptively unlawful and that courts reviewing such agreements should proceed via a "quick look" approach, rather than applying a "rule of reason." See *California Dental*, 526 U.S., at 775, n. 12 ("Quick-look analysis in effect" shifts to "a defendant the burden to show empirical evidence of procompetitive effects"). We decline to do so. In *California Dental*, we held (unanimously) that abandonment of the "rule of reason" in favor of presumptive rules (or a "quick-look" approach) is appropriate only where "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets." 526 U.S., at 770; *id.*, at 781 (Breyer, J., concurring in part and dissenting in part). We do not believe that reverse payment settlements, in the context we here discuss, meet this criterion.

That is because the likelihood of a reverse payment bringing about anticompetitive effects depends upon its size, its scale in relation to the payor's anticipated future litigation costs, its independence from other services for which it might represent payment, and the lack of any other convincing justification. The existence and degree of any anticompetitive consequence may also vary as among industries. These complexities lead us to conclude that the FTC must prove its case as in other rule-of-reason cases.

To say this is not to require the courts to insist, contrary to what we have said, that the Commission need litigate the patent's validity, empirically demonstrate the virtues or vices of the patent system, present every possible supporting fact or refute every possible pro-defense theory. As a leading antitrust scholar has pointed out, " '[t]here is always something of a sliding scale in appraising reasonableness,'" and as such "'the quality of proof required should vary with the circumstances.' " *California Dental, supra,* at 780 (quoting with approval 7 Areeda ¶ 1507, at 402 (1986)).

As in other areas of law, trial courts can structure antitrust litigation so as to avoid, on the one hand, the use of antitrust theories too abbreviated to permit proper analysis, and, on the other, consideration of every possible fact or theory irrespective of the minimal light it may shed on the basic question—that of the presence of significant unjustified anticompetitive consequences. See 7 *id.,* ¶ 1508c, at 438–440. We therefore leave to the lower courts the structuring of the present rule-of-reason antitrust litigation. We reverse the judgment of the Eleventh Circuit. And we remand the case for further proceedings consistent with this opinion.

It is so ordered.

JUSTICE ALITO took no part in the consideration or decision of the case. CHIEF JUSTICE ROBERTS filed a dissenting opinion, in which JUSTICE SCALIA and JUSTICE THOMAS joined.

Notes and Questions

(1) In an omitted portion of the majority's opinion and in Chief Justice Roberts's dissent, the justices debated the significance of several prior Supreme Court decisions in which antitrust analysis was applied in the presence of patents. In the most analogous of those cases, *United States v. Singer Manufacturing Co.*, 374 U.S. 174 (1963), the government brought an antitrust challenge to a settlement of a patent interference proceeding (a proceeding to determine the rights of multiple parties claiming patents on a single invention), arguing that there was a possibility that the interference proceeding could have resulted in invalidation or narrowing of both parties' claims. The Court condemned the agreement and Justice White offered the following comments in concurrence:

> In itself the desire to secure broad claims in a patent may well be unexceptionable —when when purely unilateral action is involved. And the settlement of an interference in which the only interests at stake are those of the adversaries, as in the case of a dispute over relative priority only and where possible invalidity, because of known prior art, is not involved, may well be consistent with the general policy favoring settlement of litigation. But the present case involves a less innocuous setting. Singer and Gegauf

> agreed to settle an interference, at least in part, to prevent an open fight over validity. There is a public interest here, which the parties have subordinated to their private ends—the public interest in granting patent monopolies only when the progress of the useful arts and of science will be furthered because as the consideration for its grant the public is given a novel and useful invention. When there is no novelty and the public parts with the monopoly grant for no return, the public has been imposed upon and the patent clause subverted.

Id. at 199-200 (White, J., concurring). See Mark R. Patterson, *Leveraging Information about Patents: Settlements, Portfolios, and Holdups*, 50 HOUS. L. REV. 483 (2012).

(2) Chief Justice Roberts's dissenting opinion followed the position adopted by several lower courts: Since the settlement allowed for entry before expiration of the patent (here five years before) and since settlements in general are favored, there was no basis for finding a violation. In dissent, Roberts claims that "[i]f [the patentee's] actions are within the scope of the patent, they are not subject to antitrust scrutiny, with two exceptions concededly not applicable here: (1) when the parties settle sham litigation, cf. *Professional Real Estate Investors, Inc. v. Columbia Pictures Industries, Inc.*, 508 U.S. 49, 60–61 (1993); and (2) when the litigation involves a patent obtained through fraud on the Patent and Trademark Office. *Walker Process Equipment*, 382 U.S. 172, 177 (1965)." This claim echoes a similar statement by the Federal Circuit in *In re Independent Service Organizations Antitrust Litigation (CSU, L.L.C. v. Xerox Corp.)*, 203 F.3d 1322, 1327 (Fed. Cir. 2000). Unlike the Federal Circuit's statement in *Xerox*, though, and contrary to the claim of Chief Justice Roberts, the Supreme Court has never held that antitrust limits on patent enforcement are limited to those two types of conduct. In that sense, at least, the majority seems more accurate in saying that "[w]hether a particular restraint lies 'beyond the limits of the patent monopoly' is a *conclusion* that flows from [antitrust] analysis" (emphasis in original).

(3) On the other hand, does the majority provide sufficient guidance for courts to determine how antitrust analysis should be applied? Is its observation that in a reverse-payment agreement the "form of settlement is unusual" helpful? Are you convinced that it is not necessary to evaluate patent validity because "[a]n unexplained large reverse payment itself would normally suggest that the patentee has serious doubts about the patent's survival"?

(4) Are there other circumstances in which an agreement among parties to eliminate uncertainty could constitute an antitrust violation? Is uncertainty procompetitive or anticompetitive?