
PROCOMPETITIVE JUSTIFICATIONS IN ANTITRUST LAW

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ABSTRACT

The rule of reason has come to dominate modern antitrust law. Rule-of-reason analysis takes into account both harmful and beneficial effects of defendants' conduct. For decades, what qualifies as "harmful" has been the subject of intense judicial and academic debate. But what counts as "beneficial"? Despite its fundamental importance to the antitrust enterprise, this has remained a surprisingly open question. The relevant case law contains a tangle of competing approaches and seemingly irreconcilable opinions.

This article provides answers and clarity. It identifies the "market failure" approach to procompetitive-justification analysis as both doctrinally correct and economically optimal. Under this approach, restraints of trade may be justified if—but only if—they alleviate a market failure, thereby increasing consumer welfare. The leading alternative standards, "competitive process" and "type of effect", find some support in precedent but are at odds with the bulk of modern authority. Moreover, error-cost analysis indicates that these alternatives produce excessive uncertainty and systematically skewed outcomes.

While the market-failure approach is appropriate, it is not always—and perhaps not often—deployed as well as it might be. In response, this article delineates the proper rule-of-reason framework. This expanded mode of analysis can, in practice, facilitate rule-of-reason decisionmaking. Used correctly, the suggested framework prompts more transparent and rigorous analyses that will minimize errors and maximize consumer welfare.

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I. INTRODUCTION

The rule of reason has come to dominate antitrust law.¹ Over the past several decades, courts have systematically retreated from bright-line rules condemning various categories of marketplace conduct as *per se* illegal.² The rule of reason, a more searching mode of analysis, takes into account both harmful and beneficial effects of defendants' conduct.³ For decades, what qualifies as “harmful” has been the subject of intense judicial and scholarly debate.⁴ But what counts as “beneficial”?

Analyzing beneficial effects, or, in modern parlance, “procompetitive justifications”, is a vital cornerstone of modern antitrust jurisprudence. But it is also a topic that remains—in light of its centrality to the antitrust enterprise—rather shockingly underexplored. As a leading text observes, “what constitutes an offsetting benefit to competition” remains “[a] question left open.”⁵ An examination of the relevant case law reveals competing approaches that, at times, have produced seemingly irreconcilable results. The resulting confusion is such that different scholars can view the very same U.S. Supreme Court decision as both a “conundrum”⁶ and the Court’s “most elucidating”⁷ opinion on the subject.

¹ PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION* ¶ 1500 (2017) (“Ever since [the U.S. Supreme Court’s 1911 *Standard Oil* decision], antitrust law has been governed by the ‘rule of reason.’”). Analysts tend to use the term “rule of reason” to describe Sherman Act § 1 proceedings, though the structural framework is somewhat similar to merger and monopoly analyses. The present discussion generally confines itself to Sherman Act § 1, but the implications offer value in merger and monopolization contexts as well. *See generally* Andrew I. Gavil, *Moving Beyond Caricature and Characterization: The Modern Rule of Reason in Practice*, 85 S. CAL. L. REV. 733, 735 (2012) (describing modern antitrust as “a collection of ‘rules of reason’ that cut across [statutes] and serve as a set of unifying first principles of antitrust law”).

² *See, e.g.*, Gavil, *supra* note 1, at 734 (“The rule of reason has evolved considerably . . . , largely due to the Court’s . . . march away from *per se* rules and undemanding burdens of proof.”).

³ *See, e.g.*, Rebecca Haw Allensworth, *The Commensurability Myth in Antitrust*, 69 VAND. L. REV. 1, 5 n.7 (2016) (“The Rule of Reason . . . [is] a standard that balances pro- with anticompetitive effects”). *But see* Michael A. Carrier, *The Real Rule of Reason: Bridging the Disconnect*, 1999 B.Y.U. L. REV. 1265 (finding that actual balancing is quite rare); D. Daniel Sokol, *The Transformation of Vertical Restraints: Per Se Illegality, the Rule of Reason, and Per Se Legality*, 79 ANTITRUST L.J. 1003, 1008 (2014) (arguing that some types of vertical restraints, including maximum resale price maintenance and territorial restrictions, have effectively become *per se* legal).

⁴ Neither Congress nor the U.S. Supreme Court have clearly articulated the goal(s) of antitrust law. *See, e.g.*, Roger D. Blair & D. Daniel Sokol, *The Rule of Reason and the Goals of Antitrust: An Economic Approach*, 89 ANTITRUST L.J. 471, 473 (2012). That said, the modern consensus—which the present analysis joins—is that antitrust should seek to maximize the economic conception of consumer welfare, though some argue instead for a total-welfare standard. *See, e.g., id.*

⁵ LAWRENCE A. SULLIVAN ET AL., *THE LAW OF ANTITRUST: AN INTEGRATED HANDBOOK* § 5.3f, at 223 (3d ed. 2016).

⁶ SULLIVAN ET AL., *supra* note 4, § 5.3f, at 223.

⁷ Gregory J. Werden, *Antitrust’s Rule of Reason: Only Competition Matters*, 79 ANTITRUST L.J. 713, 732 (2014).

Meanwhile, modern antitrust defendants have continued to proffer an ever-expanding plethora of justifications for their conduct. In recent years, defendants have attempted to avoid liability by arguing variously that their restraints of trade created a “healthier market” by facilitating the launch of an online ebook platform,⁸ preserved “amateurism” and promoted “competitive balance” in college sports,⁹ promoted the “health and welfare” of horses,¹⁰ helped pay for “uniforms and newly painted trucks”,¹¹ integrated college academics and athletic programs,¹² responded to an “inherently anticompetitive” government-agency action,¹³ increased access to the Ivy League for financially needy students,¹⁴ promoted student-body diversity,¹⁵ preserved a “differentiated business model” that entailed charging high prices to customers,¹⁶ protected one group of hospital patients from having to subsidize another,¹⁷ enhanced the defendant’s “market penetration”,¹⁸ helped to limit conflicts of interest among employees,¹⁹ ensured the “undivided loyalty” of National Football League team owners,²⁰ helped to fund cemeteries’ task of resetting grave memorials that “have settled or shifted”, and many more. In the face of this onslaught, and without clear guidance, judicial decisionmaking has yielded, at best, mixed results.

This Article provides clarity and answers to the “open questions” posed by procompetitive justifications. It begins, in Part II, by identifying and describing the three primary competing approaches to justification analysis. Under the “market failure” approach, a valid justification is present if—and only if—the challenged restraint alleviates a market failure.²¹ Alternatively, the “competitive process”

⁸ *United States v. Apple*, 952 F. Supp. 2d 638, 707 (S.D.N.Y. 2013), *aff’d*, 787 F.3d 131 (2015) (“Censuring Apple for entering a tumultuous new market, in Apple’s view, will have a ‘chilling and confounding . . . effect not only on commerce but specifically on content markets throughout this country. . . . It is not entirely clear to what Apple is alluding, however, when it describes its procompetitive behavior and creation of healthy competition.”).

⁹ *O’Bannon v. NCAA*, 802 F.3d 1049, 1058 (9th Cir. 2015).

¹⁰ *JES Props., Inc. v. USA Equestrian, Inc.*, No. 802-CV-1585 T24MAP, 2005 WL 1126665 (M.D. Fla. May 9, 2005)

¹¹ *New York v. Anheuser-Busch, Inc.*, 811 F. Supp. 848 (E.D.N.Y. 1993).

¹² 802 F.3d at 1058.

¹³ *United States v. N.D. Hosp. Ass’n*, 640 F. Supp. 1028 (D.N.D. 1986).

¹⁴ *United States v. Brown Univ.*, 5 F.3d 658, 674 (3d Cir. 1993).

¹⁵ *Id.*

¹⁶ *United States v. Am. Express Co.*, 88 F. Supp. 3d 143, 224 (E.D.N.Y. 2015), *rev’d*, 838 F.3d 179 (2d Cir. 2016).

¹⁷ 640 F. Supp. at 1038.

¹⁸ *Graphic Products Distribs., Inc. v. Itek Corp.* 717 F.2d 1560 (11th Cir. 1983).

¹⁹ *Pluekhahn v. Farmers Ins. Exch.*, 749 F.2d 241, 243 (5th Cir. 1985).

²⁰ *N. Am. Soccer League v. NFL*, 670 F.2d 1249 (2d Cir. 1982)

²¹ See *infra* Part II.B (detailing the doctrinal support for the market-failure approach). This Article is not the first to argue that alleviating a market failure should qualify as a valid procompetitive justification. See Alan J. Meese, *In Praise of All or Nothing Dichotomous Categories: Why Antitrust Law Should Reject the Quick Look*, 104 GEO. L.J. 835, 849–50 (2016) (arguing that “technological efficiencies or overcoming a market failure” can trigger rule-of-reason analysis); Marina Lao, *Discrediting Accreditation?: Antitrust and Legal Education*, 79 WASH. U. L.Q. 1035, 1983 (2001) (arguing that accreditation decisions may be justified by virtue of curing certain market failures, specifically information asymmetries and externalities); Peter J. Hammer, *Antitrust Beyond Competition: Market Failures, Total Welfare, and the Challenge of Intramarket Second-Best Tradeoffs*,

approach attempts to condemn restraints that harm (and bless restraints that benefit) “competition” itself or the so-called “competitive process”.²² Lastly, the “type of effect” approach appears to offer a shortcut: simply identify the effects of the challenged restraint, then ascertain whether they align with a pre-approved typology of virtuous marketplace effects (e.g., higher output, lower prices, etc.).²³

Part III conducts a doctrinal analysis of these competing approaches. It reveals that, after a brief initial period of confusion, the U.S. Supreme Court offered early support for the market-failure approach.²⁴ That early guidance was subsequently abandoned, however, as antitrust entered its Inhospitability Era.²⁵ During that time, courts employing—or at least attempting to employ—the competitive-process approach were quite suspicious of all agreements that varied from simple one-off spot contracts. That suspicion translated into *per se* condemnation of many such restraints, eliminating the need for analysis of actual marketplace effects. Indeed, as Part III reveals, the overriding concern was not consequentialist at all. Rather, it centered around a vaguely defined bundle of rights: the “right” of traders to be “free” from exclusive-territory restrictions,²⁶ group boycotts,²⁷ and the like, as well as a more general (though equally ill-defined) “freedom of action”.²⁸

With the dawn of the Modern Era, however, the Court’s jurisprudence returned to a fundamentally consequentialist mode of analysis. Actual marketplace effects, both good and ill, returned to prominence. The framework nearly universally adopted was—and is—that of contemporary economics, which draws upon (inter alia) price theory and transaction-cost economics. Through this lens, competitive effects are assessed vis-à-vis the conceptions of welfare, efficiency, and inefficiency, i.e., market

98 MICH. L. REV. 849 (2000) (arguing that restraints are sometimes justified as “intramarket second-best tradeoffs”); Thomas L. Greaney, *Quality of Care and Market Failure Defenses in Antitrust Health Care Litigation*, 21 CONN. L. REV. 605 (1989) (arguing that market failures may sometimes justify restraints in health-care markets). This Article expands upon past commentary by more clearly identifying and explaining the alternative approaches to procompetitive-justification analysis, making an explicitly doctrinal case for the market-failure approach, and incorporating the Neo-Chicagoan error-cost framework into a normative, consequentialist argument in favor of the market-failure approach. On error-cost analysis and antitrust, see generally Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1 (1984).

²² See *infra* Part II.B (describing the competitive-process approach).

²³ See *infra* Part II.C (describing the type-of-effect approach).

²⁴ See *infra* Part III.A.

²⁵ See *infra* Part III.B.

²⁶ *E.g.*, *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 611 (1972) (“[T]he Sherman Act gives to each Topco member and to each prospective member the right to ascertain for itself whether or not competition with other supermarket chains is more desirable than competition in the sale of Topco brand products.”).

²⁷ *E.g.*, *Fashion Originators Guild of Am. v. FTC*, 312 U.S. 457, 465 (1941) (“[A]mong the many respects in which the Guild’s plan runs contrary to the policy of the Sherman Act are these: it narrows the outlets to which garment and textile manufacturers can sell and the sources from which retailers can buy . . . [and] subjects all retailers and manufacturers who decline to comply with the Guild’s program to an organized boycott . . .”).

²⁸ *E.g.*, *id.* (“[T]he Guild’s plan . . . takes away the freedom of action of members by requiring each to reveal to the Guild the intimate details of their individual affairs . . .”).

failure. Thus, as Part III explains, the Court has adopted the market-failure approach to justification analysis.²⁹ Lower courts and enforcers have, at times, attempted to use the type-of-effect approach as a crude heuristic. But it is best understood as simply that: a shortcut method of market-failure analysis. Viewed through this lens, cases using the type-of-effect approach do not undercut the precedential basis for the market-failure approach. If anything, they reinforce it.

Having demonstrated the doctrinal superiority of the market-failure approach, Part III concludes by considering the ramifications for non-welfare-related justifications.³⁰ It identifies multiple judicial rule-of-reason analyses that incorrectly took into account such justifications, and demonstrates that these decisions represent both bad law and bad policy.

Part IV undertakes an error-cost analysis of the three competing approaches. It finds that, on efficiency and welfare grounds, the market-failure approach is superior to the alternatives. The competitive-process approach that characterized the Inhospitability Era tends to produce excessive false positives—and, in any event, is so “wonderfully ill-defined”³¹ that it offers little to no guidance to courts, enforcers, and private parties.³² The type-of-effect approach, on the other hand, likely produces excessive false positives and negatives. Certain restraints can efficiently alleviate a market failure while producing effects not typically included on pre-approved typologies of procompetitive virtues—e.g., restraints that reduce negative externalities or marketplace deception, thereby lowering output.³³ The type-of-effect approach would incorrectly condemn such restraints. At the same time, courts employing this shorthand method often fail to scrutinize defendants’ proffered justifications with the appropriate degree of skepticism, resulting in false negatives.³⁴ And, again, this alternative creates unwarranted confusion and a lack of clarity. The type-of-effect approach offers no guidance as to novel types of effects. Thus, courts using it have repeatedly been forced to resolve essentially unanswerable questions: Is increasing student-body diversity “procompetitive”?³⁵ Promoting the “health and welfare” of horses?³⁶ Paying for “uniforms and newly painted trucks”?³⁷

By way of contrast, the market-failure approach is shown to minimize errors. Used properly, it can yield fewer false positives than the competitive-process approach, and fewer false positives and negatives than the type-of-effect approach.³⁸

²⁹ See *infra* Part III.C (describing Modern Era jurisprudence and noting Nat’l Soc’y of Prof’l Engineers v. United States, 435 U.S. 679, 684 (1978), as aberrational).

³⁰ See *infra* Part III.D.

³¹ Hammer, *supra* note 5, at 850 n.3.

³² See *infra* Part IV.A.

³³ See *infra* notes ___ and accompanying text.

³⁴ See *infra* notes ___ and accompanying text (describing courts’ tendency to credit baseless claims of “preventing free-riding”).

³⁵ United States v. Brown Univ., 5 F.3d 658 (3d Cir. 1997).

³⁶ JES Props., Inc. v. USA Equestrian, Inc., No. 802-CV-1585 T24MAP, 2005 WL 1126665 (M.D. Fla. May 9, 2005)

³⁷ New York v. Anheuser-Busch, Inc., 811 F. Supp. 848 (E.D.N.Y. 1993).

³⁸ See *infra* Part IV.C.

It also offers relatively clear, useful guidance for courts, enforcers, private parties, and other analysts and stakeholders. Moreover, the market-failure approach has the beneficial side effect of reorienting antitrust away from an unhealthy obsession with output (and price), and toward achieving its consensus goal of promoting consumer welfare.³⁹

Building on these insights, Part V offers an expanded rule-of-reason framework. The appropriate rule-of-reason analysis requires that the defendant explicitly identify a specific market failure and demonstrate that the relevant market actually suffered from (or would have suffered from) that failure absent the challenged restraint.⁴⁰ Part V also recommends a recent opinion *par excellence* in which the court conducted a rigorous justification analysis, in line with the recommendations contained herein.⁴¹ The outcome of the case illustrates how the expanded framework can be used in practice to reduce errors and filter out baseless justifications. Part VI briefly concludes.

II. PROCOMPETITIVE JUSTIFICATIONS: COMPETING APPROACHES

Despite their prominent role in antitrust enforcement, procompetitive justifications have remained a surprisingly underexplored and often poorly understood concept. There is general consensus as to the structure of modern rule-of-reason analyses, within which procompetitive justifications (or the lack thereof) come into play at two distinct stages.⁴² But what, exactly, constitutes a valid justification remains an “open question”.⁴³

As an initial, and uncontroversial, matter, not all restraints of trade are condemned by antitrust law. The leading treatise rightly points out that “[i]t is obviously not the purpose of the antitrust laws to condemn collaborations producing socially desirable results.”⁴⁴ At a high level, the task of antitrust tribunals and enforcers is to sort anticompetitive (“unreasonable”) restraints from procompetitive or neutral (“reasonable”) restraints.⁴⁵ Only the former are to be condemned under the antitrust laws.

³⁹ *Id.*

⁴⁰ *See infra* Part V.A.

⁴¹ *See infra* Part V.B (discussing *United States v. Am. Express Co.*, 88 F. Supp. 3d 143 (E.D.N.Y. 2015), *rev'd on other grounds*, 838 F.3d 179 (2d Cir. 2016)). To the extent it is relevant, the author represented the United States in this matter. The discussion herein does not draw upon or reveal any confidential information, and the positions taken represent solely those of the author and not those of the United States.

⁴² That said, even here there is some disagreement—the Supreme Court, for example, has suggested that the analytical framework does not rise even to the level of a “spectrum”. *Calif. Dental Ass'n v. FTC*, 526 U.S. 756, 780 (1999).

⁴³ SULLIVAN ET AL., *supra* note 4.

⁴⁴ AREEDA & HOVENKAMP, *supra* note 1, at ¶ 1504.

⁴⁵ *See, e.g.*, Gavil, *supra* note 1, at 735 (“The various frameworks of the new rules of reason are all animated by a common purpose: to differentiate anticompetitive from efficient conduct.”).

Procompetitive justifications play a two-fold role in such analyses.⁴⁶ First, courts confronting claims under Sherman Act § 1 must decide whether to apply the *per se* illegality rule or the more lenient rule of reason. Courts, enforcers, and commentators often invoke a categorical approach to answering this question, one based on the type of conduct at issue.⁴⁷ Thus, for example, one often encounters statements to the effect that “price fixing is *per se* illegal.”⁴⁸ But that is not always true. In *BMI*, for example, the U.S. Supreme Court applied the rule of reason to a joint-licensing arrangement that involved horizontal price fixing because of the agreement’s obvious beneficial effects.⁴⁹ Other courts have similarly applied the rule of reason to categories of conduct often spoken of as being *per se* illegal.⁵⁰

BMI readily illustrates the first function played by procompetitive justifications: if a restraint of trade has facially plausible procompetitive attributes, it generally falls under the rule of reason. This is so even if the restraint also falls into a category of conduct that is commonly treated as *per se* illegal.⁵¹ At this stage, the procompetitive-justifications inquiry serves as a filter. Courts take an initial glance⁵² at a restraint, ascertain its plausible competitive effects, and accordingly treat it under either the more extensive, effects-based rule-of-reason analysis (what the leading treatise calls “full-scale rule-of-reason”⁵³) or the *per se* illegality rule (which does not require plaintiffs to prove market power or harmful effects).⁵⁴ This initial glance can be usefully thought of as the “zero-step”⁵⁵ of analysis.

⁴⁶ For ease of discussion, this Article refers only to *per se* treatment and the full-scale rule of reason. According to the U.S. Supreme Court, however, “our categories of analysis of anticompetitive effect are less fixed than terms like ‘*per se*,’ ‘quick look,’ and ‘rule of reason.’”

⁴⁷ This was so particularly during the Inhospitability Era. See, e.g., Gavil, *supra* note 1, at 736 (“[T]he[] modern rule[] of reason also tend[s] to rely far less on the traditional approach of ‘categorization’ followed by condemnation or exoneration. For at least fifty years, from *United States v. Trenton Potteries Co.* to *Sylvania*, the Supreme Court developed a sorting framework that separated antitrust cases into categories based on the nature of the conduct and two distinct rules: *per se* and rule of reason.”). That said, this approach still manifests with some frequency today. See *infra* notes 32–34 and accompanying text.

⁴⁸ See, e.g., *Identifying Sherman Act Violations*, U.S. ATTORNEYS’ MANUAL, U.S. DOJ, <https://www.justice.gov/usam/antitrust-resource-manual-8-identifying-sherman-act-violations>.

⁴⁹ See also *Nat’l Bancard Corp. v. Visa U.S.A., Inc.*, 779 F.2d 592 (11th Cir. 1986) (upholding a uniform interchange fee set by an association of credit-card-issuing banks); *O’Bannon v. NCAA*, 802 F.3d 1049 (9th Cir. 2015) (applying the rule of reason to horizontal price fixing).

⁵⁰ See, e.g., *Polk Bros., Inc. v. Forest City Enters., Inc.*, 776 F.2d 185 (7th Cir. 1985) (horizontal product-market allocation); *United States v. Kemp & Assocs., Inc.*, No. 2:16-CF-403DS (D. Utah June 22, 2017) (horizontal customer allocation).

⁵¹ See, e.g., sources cited *supra* notes ____.

⁵² One hesitates to use the term “quick look”, given its unique connotations in the antitrust arena. See AREEDA & HOVENKAMP, *supra* note 1, at ¶ 1508 (“This treatise has generally avoided using the term ‘quick look’ unless quoting from decisions, because it suggests a tripartite division [“rule of reason”, “quick look”, and “*per se*”] that does not account for the full range of variations that the cases display.”).

⁵³ AREEDA & HOVENKAMP, *supra* note 1, at ¶ 1504.

⁵⁴ Thus, even the nominal *per se* rule allows consideration of legitimate justifications that, if found, trigger a full-scale rule of reason inquiry. *Id.* at 1504e.

⁵⁵ See Matthew G. Sipe, “The Sherman Act and Avoiding Void-for-Vagueness”, at 25 (May 16, 2017), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2968933.

The second function played by procompetitive justifications (or lack thereof) comes into play if the restraint receives full-scale rule-of-reason analysis, and the plaintiff successfully makes out its *prima facie* case. In such cases, procompetitive justifications may arise as a responsive defense. The decisional framework underlying the full-scale rule of reason involves burden-shifting.⁵⁶ In a given case, the plaintiff first bears the burden of alleging and proving that the challenged conduct “is of a type reasonably calculated to have”,⁵⁷ or actually has,⁵⁸ anticompetitive effects. Should the plaintiff do so, the burden of production⁵⁹ shifts to the defendant, which must identify a procompetitive justification for its restraint.⁶⁰

The following discussion identifies and describes the three leading alternative approaches to analyzing defendants’ procompetitive justifications. Each approach has been used, to varying degrees and with varying degrees of success, by antitrust courts and enforcers.

A. Market Failure

As we shall see in Parts III and IV, the market-failure approach is both doctrinally correct and produces superior outcomes with lower attendant error costs relative to the competitive-process or type-of-effect approaches. To set the groundwork for that normative analysis, a brief primer on the workings and underlying economics of the market-failure approach follows.

A market failure occurs when a market produces outcomes that are less efficient than they might be.⁶¹ As employed in antitrust law and economics, “efficiency” generally refers to “Kaldor-Hicks” efficiency. A change is Kaldor-Hicks efficient if those made better off thereby could compensate (out of their gains) any left worse off.⁶² “Better” and “worse” in this context relate to “welfare”, a sometimes-frustratingly vague signifier properly synonymous with the price-theoretic concept of “surplus”.⁶³ “Surplus” refers to the difference between what a buyer (or seller) would

⁵⁶ See, e.g., *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001) (employing a burden-shifting analysis under both Sherman Act § 1 and § 2, identifying balancing as the final step of analysis).

⁵⁷ AREEDA & HOVENKAMP, *supra* note 1, at ¶ 1504b.

⁵⁸ *FTC v. Ind. Fed’n of Dentists*, 476 U.S. 447, 457 (1986); *United States v. Microsoft Corp.*, 253 F.3d 34, 58–59 (D.C. Cir. 2001).

⁵⁹ See, e.g., Meese, *supra* note 31, at 108.

⁶⁰ Despite some doctrinal confusion, most authorities agree that if the defendant establishes a procompetitive justification, the next stage entails examining whether less-restrictive means were available. C. Scott Hemphill, *Less Restrictive Alternatives in Antitrust Law*, 116 COLUM. L. REV. 927, 938 n. 49 (2015) (collecting cases). Absent such an alternative, the majority view is that courts will balance the anticompetitive effects against the procompetitive effects. E.g., 253 F.3d 34, 58–59; Carrier, *supra* note 2.

⁶¹ See generally, e.g., Francis M. Bator, *The Anatomy of Market Failure*, 72 Q.J. ECON. 351, 351 (1958) (“What is it we mean by ‘market failure’? Typically, . . . we mean the failure of a more or less idealized system of price-market institutions to sustain ‘desirable’ activities or to estop ‘undesirable’ activities.”).

⁶² E.g., HERBERT HOVENKAMP, *FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE* § 2.3, at 101 (5th ed. 2016).

⁶³ *Id.* at 891–95 (discussing consumer surplus and its relationship to total welfare).

have been willing to pay (or accept) and what that buyer actually paid (or accepted).⁶⁴ Because analyzing all the interactions in an economy (“general equilibrium analysis”) is not practical, antitrust economics instead usually employs “partial equilibrium” analysis.⁶⁵ This methodology entails defining and analyzing a single market (the “relevant market”⁶⁶) in isolation, holding constant competitive conditions in all other markets.⁶⁷

Sometimes, restraints of trade imposed by private market participants can improve the relevant market’s performance, yielding more efficient outcomes.⁶⁸ The “market failure” approach, which permeates the U.S. Supreme Court’s Modern Era antitrust jurisprudence,⁶⁹ recognizes that such restraints may accordingly be justified.

An academic debate lingers on over which market participants’ surplus is relevant to antitrust analysis. Proponents of a total- or social-welfare standard contend that both producer and consumer surplus are relevant, whereas consumer-welfare advocates focus solely on consumer surplus.⁷⁰ In practice, courts seem to prefer a consumer-welfare standard,⁷¹ suggesting that only restraints of trade that increase consumer surplus are potentially justified. Put another way, while courts often speak of the benefits of “efficiency”, they do not appear to use that term in a strict Kaldor-Hicksian sense. If a restraint increases a monopolist’s surplus but decreases consumer surplus, it will likely be condemned—even if the monopolist’s gain from the restraint is so large that it could have hypothetically compensated consumers’ losses. Thus, judicial references to “efficiency” are best understood vis-à-vis a market’s impact, beneficial or detrimental, on consumer welfare. Where a market fails to maximize consumer welfare as well as it otherwise might, it is—in the argot of antitrust courts—not “efficient”.

This concept is cornerstone of the “market-failure” approach. Where a restraint of trade alleviates a market failure, it is “efficient” (in the unique, consumer-

⁶⁴ *Id.*

⁶⁵ See, e.g., Hammer, *supra* note 5, at 853–56.

⁶⁶ “Relevant market” is a term of art in antitrust, the legal significance of which is, in a given case, somewhat murky. In some cases—for example, those involving hardcore horizontal price-fixing without any plausible procompetitive justifications—plaintiffs are not required to prove that the defendants possessed market power, which in turn usually requires first defining a “relevant market”. See, e.g., Louis Kaplow, *Why (Ever) Define Markets?*, 124 HARV. L. REV. 437, 438–39 (2010) (noting that market definition plays a “roughly similar” role in competition-law regimes outside the United States). But in many—perhaps most—antitrust cases, market definition plays a pivotal role. See *id.* at 439 (citing *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 469 n.15 (1992) (“Because market power is often inferred from market share, market definition generally determines the result of the case.”)).

⁶⁷ *Id.* at 856.

⁶⁸ See, e.g., *id.*

⁶⁹ See *infra* Part III.B.

⁷⁰ See, e.g., Jonathan B. Baker & Steven C. Salop, *Antitrust, Competition Policy, and Inequality*, 104 GEO. L.J. ONLINE 1, 15 (2015).

⁷¹ See, e.g., Herbert Hovenkamp, *Implementing Antitrust’s Welfare Goals*, 81 FORDHAM L. REV. 2471, 2476 (2013).

focused sense in which modern antitrust courts use the term) and therefore potentially justified. But how are courts and enforcers to identify market failures?

Modern antitrust law draws from partial-equilibrium price theory,⁷² transaction-cost economics,⁷³ game theory,⁷⁴ and even (as we shall see) behavioral economics.⁷⁵ It offers, in other words, something for everyone to criticize.

The use of price theory's idealized⁷⁶ "perfect competition" model is no exception, having drawn rather intense criticism for its supposed lack of descriptive accuracy and blindness to certain types of market failure, as well as the procompetitive potential of nonstandard contracts.⁷⁷ That said, the perfect-competition model offers some value in the present context: it can help to identify some common sources of market failure and to explain some of the relevant case law.⁷⁸

Perfect competition is a partial-equilibrium model: it is meant to be used to analyze a single market in isolation, rather than the economy as a whole.⁷⁹ How closely a given market approximates a state of perfect competition depends on several conditions.⁸⁰ Deviations from at least some of these conditions tend to decrease the relevant market's efficiency. Most relevant for present purposes are the conditions of perfect information,⁸¹ zero transaction costs,⁸² lack of externalities,⁸³ and rational behavior by market participants.⁸⁴ In addition, though less commonly recognized, for a market to function efficiently it is also necessary that individual interests align with group interests.⁸⁵

The presence of transaction costs, for example, can make a given exchange unprofitable for sellers and/or buyers. Rational actors would not enter into such an

⁷² *E.g.*, Alan J. Meese, *Price Theory, Competition, and the Rule of Reason*, 2003 U. ILL. L. REV. 77, 120.

⁷³ *E.g.*, Oliver E. Williamson, *The Economics of Antitrust: Transaction Cost Considerations*, 122 U. PA. L. REV. 1439 (1974).

⁷⁴ *E.g.*, *Petruzzi's IGA Supremarkets, Inc. v. Darling-Delaware Co.*, 998 F.2d 1224, 1233 (3d Cir. 1993) ("Game theory teaches us that a cartel cannot survive absent some enforcement mechanism because otherwise the incentives to cheat are too great.").

⁷⁵ *See infra* Part __; *see also* Elizabeth M. Bailey, *Behavioral Economics and U.S. Antitrust Policy*, 47 REV. IND. ORG. 355 (2015).

⁷⁶ Or, as Meese wryly puts it, "antiseptic". Meese, *supra* note 31, at 120.

⁷⁷ Alan J. Meese, *Market Failure and Non-Standard Contracting: How the Ghost of Perfect Competition Still Haunts Antitrust*, 1 J. COMPETITION L. & ECON. 21, 22 (2005).

⁷⁸ *Cf.* ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 60 (1993) ("[A]ntitrust must use the model [of perfect competition] and its implications as a guide to reasoning about actual markets . . .").

⁷⁹ *See* Hammer, *supra* note 5, at 855–56.

⁸⁰ *See generally* FRANK H. KNIGHT, *RISK, UNCERTAINTY, AND PROFIT* 51–93 (1921) (listing requisite conditions for perfect competition).

⁸¹ Meese, *supra* note 31, at 116.

⁸² *Id.* at 116–17.

⁸³ Herbert Hovenkamp, *Antitrust Policy After Chicago*, 84 MICH. L. REV. 213, 244 (1985).

⁸⁴ *E.g.*, John M. Newman, *The Myth of Free*, 86 GEO. WASH. L. REV. (forthcoming, 2017).

⁸⁵ Maurice E. Stucke, *Is Competition Always Good?*, 1 J. ANTITRUST ENFORCEMENT 162, 179 (2013).

exchange, even where it would, absent transaction costs, make both parties better off.⁸⁶ Consequently, where significant (but reducible) transaction costs are present in a given market, that market does not produce efficient results.⁸⁷ Certain restraints of trade can reduce transaction costs, facilitating mutually beneficial exchanges and increasing efficiency.⁸⁸ The market-failure approach recognizes such restraints as (at least potentially) justified.⁸⁹

It bears emphasizing that not all of the conditions requisite for perfect competition necessarily promote efficiency. Perfect competition, for example, assumes rising average total costs.⁹⁰ Such markets will tend to feature many small sellers. But in a market where average cost declines throughout some relevant range of output, production is subject to economies of scale. In markets with scale economies, the presence of many sellers—each with a higher-than-necessary cost structure—is likely inefficient.⁹¹ A restraint of trade that “alleviates” market concentration caused by economies of scale does not necessarily increase, and may very well decrease, efficiency. As a result, the market-failure approach would not, at least *ipso facto*, recognize such restraints as justified.

In sum, the market-failure approach to procompetitive-justification analysis recognizes that restraints of trade can sometimes improve the functioning of markets. Where a restraint alleviates a market failure, thereby increasing that market’s efficiency, it is potentially justified. As Part III will demonstrate, this approach fits comfortably within the consensus framework for rule-of-reason analysis and antitrust law at large. It also produces more accurate decisions, with lower attendant error costs, than either of the two alternatives discussed below.

B. Competitive Process

The competitive-process approach purports to distinguish between pro- and anticompetitive restraints via their effects not on welfare or efficiency, but on

⁸⁶ Meese usefully distinguishes between “technological” transaction costs, defined as “bargaining and information costs that generally precede a transaction”, and “non-technological transaction costs”, which “postdate relationship-specific investments that enhance product differentiation.” Alan J. Meese, *Reframing Antitrust in Light of Scientific Revolution: Accounting for Transaction Costs in Rule of Reason Analysis*, 62 HASTINGS L.J. 457, 459 (2010). This Article would recognize both types as cognizable causes of structural market failures.

⁸⁷ See generally 2 KENNETH J. ARROW, GENERAL EQUILIBRIUM 134 (1983) (“[T]ransaction costs, which in general impede and in particular cases completely block the formation of markets.”).

⁸⁸ See, e.g., Oliver E. Williamson, *Economies as an Antitrust Defense Revisited*, 125 U. PA. L. REV. 699, 723–26 (1977) (merger context).

⁸⁹ See, e.g., *BMI v. CBS, Inc.*, 441 U.S. 1 (1979).

⁹⁰ E.g., Eugene V. Rostow, *The New Sherman Act: A Positive Instrument of Progress*, 14 U. CHI. L. REV. 575–76 (1947).

⁹¹ See, e.g., Alan J. Meese, *Debunking the Purchaser Welfare Account of Section 2 of the Sherman Act: How Harvard Brought Us a Total Welfare Standard and Why We Should Keep It*, 85 N.Y.U. L. REV. 659, 693 (2010) (“Adherents to ‘workable competition’ . . . recognize[ed] that certain departures from perfect competition could actually generate more benefits than harms, despite resulting market power. The classic example was economies of scale . . .”).

“competition itself”, i.e., on the “competitive process”. But although this approach has been deployed by the U.S. Supreme Court to condemn a variety of restraints, it remains a cipher. Terms like “competition” and “competitive process” are “wonderfully ill-defined”.⁹² The literature contains scholarly arguments to the effect that the “competitive process” is the sole appropriate metric for analysis⁹³—but these arguments appear to neglect answering the fundamental question of what, exactly, comprises this “competitive process”.

Whatever the competitive process may be, it (apparently) can be harmed. Under the competitive-process approach, a plaintiff carries its initial burden by showing that the challenged restraint is harmful to competition. Presumably, the burden then shifts to the defendant to demonstrate some offsetting benefit. If it is unclear what constitutes harm to the competitive process, it is even less clear what constitutes a benefit thereto. But presumably, if such a benefit can be discerned, the restraint at issue may avoid liability.

A permissible reading of the relevant case law suggests that the overriding concern does not lie with marketplace effects—immediately placing this approach at loggerheads with the rest of antitrust law.⁹⁴ Instead, according to this understanding, the competitive-process approach derives from a group of rather vaguely defined rights. These appear to include, but are not limited to, the right of a “single merchant” to compel a “group of powerful businessmen” to supply him with “the goods he needs to compete effectively”,⁹⁵ the “right” of traders to be “free” from various nonstandard contractual provisions,⁹⁶ a more general right of “freedom of action”,⁹⁷ etc.

Given the lack of clarity in the area, one is left free (or, less charitably, forced) to speculate as to the source and exact nature of these rights. Perhaps they derive from a *Lochnerian* freedom of contract. Certain of the Supreme Court’s early antitrust decisions—which happen to lie squarely in the heart of the *Lochner* Era—do speak of antitrust-related “rights”. Thus, for example, the Court in 1914 identified a single

⁹² Hammer, *supra* note 5, at 850 n.3.

⁹³ Werden, *supra* note ___.

⁹⁴ See, e.g., Daniel A. Crane, “*The Magna Carta of Free Enterprise*” *Really?*, 99 IOWA L. REV. BULL. 17, 23 (2013) (“Antitrust is . . . best understood as a consequentialist body of law designed to maximize economic efficiency and consumer welfare.”).

⁹⁵ *Klor’s, Inc. v. Broadway–Hale Stores, Inc.*, 359 U.S. 207 (1959) (applying the *per se* illegality rule to a thinly alleged “conspiracy” among multinational electronics manufacturers to refuse to deal with an independent retailer).

⁹⁶ These include exclusive-territory restrictions, e.g., *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 611 (1972) (“[T]he Sherman Act gives to each Topco member and to each prospective member the right to ascertain for itself whether or not competition with other supermarket chains is more desirable than competition in the sale of Topco brand products.”); group boycotts, e.g., *Fashion Originators Guild of Am. v. FTC*, 312 U.S. 457, 465 (1941) (“[A]mong the many respects in which the Guild’s plan runs contrary to the policy of the Sherman Act are these: it narrows the outlets to which garment and textile manufacturers can sell and the sources from which retailers can buy . . . [and] subjects all retailers and manufacturers who decline to comply with the Guild’s program to an organized boycott . . .”); etc.

⁹⁷ E.g., *id.* (“[T]he Guild’s plan . . . takes away the freedom of action of members by requiring each to reveal to the Guild the intimate details of their individual affairs . . .”).

retailer’s “unquestioned right to stop dealing with a wholesaler for reasons sufficient to himself.”⁹⁸ But by 1945, after the end of the *Lochner* Era,⁹⁹ the Court was retreating from that hardline stance, referring to it as “true” only “in a very general sense”¹⁰⁰ and calling into question the continuing validity of such rights.

Whatever their source, these rights have the practical effect of rendering many contractual arrangements invalid under the antitrust laws. Perhaps unsurprisingly, the competitive-process approach rarely, if ever, identifies any procompetitive justifications. During the Inhospitability Era, when this approach was *en vogue*, nearly every restraint was treated as harmful to the “competitive process”,¹⁰¹ usually under the strict rule of *per se* illegality. Not much more than simple, one-off contracts escaped liability.

C. Type of Effect

Some courts, enforcers, and scholars instead attempt justification analysis using a typology of pre-approved marketplace effects. The inquiry comprises two steps. First, the analyst must identify a checklist of effects that constitute valid procompetitive justifications. The typical list approves of restraints that “reduce cost, increase output or improve product quality, service, or innovation.”¹⁰² Second, the analyst simply ascertains whether the relevant restraint’s marketplace effect is on that list.

Under the type-of-effect approach, a restraint that increases output, lowers price, etc., is justified (“reasonable”) regardless of the reason it causes that effect. A restraint that decreases output, increases price, etc., is unjustified (“unreasonable”), again regardless of why it does so.

In *Law v. NCAA*, for example, the Tenth Circuit employed this approach to analyze an NCAA-imposed cap on coaches’ salaries.¹⁰³ After noting the obvious

⁹⁸ *Eastern States Retail Lumber Dealers’ Ass’n v. United States*, 234 U.S. 600 (1914).

⁹⁹ *See West Coast Hotel Co. v. Parrish*, 300 U.S. 379 (1937) (overturning *Adkins v. Children’s Hosp.*, 261 U.S. 525 (1923)).

¹⁰⁰ *Assoc. Press v. United States*, 326 U.S. 1, 15 (1945). At least arguably, the Court subsequently lurched back toward this attitude. *See, e.g., Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984) (“A manufacturer of course generally has a right to deal, or refuse to deal, with whomever it likes, as long as it does so independently.”); *see also Verizon Commc’ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 408 (“[A]s a general matter, the Sherman Act does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.” (quoting *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919) (internal quotation marks omitted) (alteration in original))). But even these cases refer only to a “general” right, rather than the “unquestioned” right identified in *Eastern States Retail Lumber Dealers’ Ass’n v. United States*, 234 U.S.

¹⁰¹ *See, e.g., Werden, supra* note 96, at 729 (“*Northern Pacific* began an era during which the Supreme Court saw a ‘pernicious effect’ in every restraint it examined.”).

¹⁰² *McWane, Inc. v. F.T.C.*, 783 F.3d 814, 841 (11th Cir. 2015) (quoting approvingly the FTC’s decision in *In re McWane, Inc.*, 2014 WL 556261 (Jan. 30, 2014) (internal quotation marks omitted)).

¹⁰³ 134 F.3d 1010 (10th Cir. 1998).

anticompetitive effects of the cap, the court first set forth its checklist of valid procompetitive effects: “increasing output, creating operating efficiencies, making a new product available, enhancing product or service quality, and widening consumer choice”.¹⁰⁴ The court also identified “mere profitability or cost savings” as types of effects that are *not* included in the list.¹⁰⁵ Since the NCAA’s proffered justification—“cost containment”—was not on the “valid” list, and was in fact on the “invalid” list, the court rejected it.¹⁰⁶

A more extreme version of the type-of-effect approach focuses solely on output effects. Under this view, conduct that increases output is always justified. Conduct that decreases output is always unjustified and unreasonable. The following passage, from Bork’s seminal work, sums up this approach: “The task of antitrust is to identify and prohibit those forms of behavior whose net effect is output restricting and hence detrimental.”¹⁰⁷ This “output-only” form of the type-of-effect approach effectively collapses the entire rule-of-reason inquiry into an output analysis.¹⁰⁸

Those who use and advocate for the type-of-effect approach generally appear to agree that maximizing some form of welfare—not maximizing output *per se*—is the overarching goal of antitrust.¹⁰⁹ Thus, this approach may (perhaps somewhat charitably) be understood as heuristic in nature. If, for example, it is true that conduct that increases in output virtually always increase consumer welfare, then output effects arguably can be used as a shortcut to facilitate efficient judicial decisionmaking.

In practice, however, courts appear to require more guidance than the extreme-form, output-only approach offers. Actual output effects are often difficult, if not impossible, to assess in a given case.¹¹⁰ Conduct that increases output does not always increase—and may, in fact, decrease—consumer welfare.¹¹¹ And antitrust courts are often confronted with claims involving effects on other aspects of competition: a given case may hinge instead on quality, product variety, etc.¹¹² Thus, the normative discussion that follows will focus on the type-of-effect approach as it is actually employed, rather than the extreme-form espoused by Bork.

¹⁰⁴ *Id.* at 1023.

¹⁰⁵ *Id.* (“[M]ere profitability or cost savings have not qualified as a defense under the antitrust laws.”).

¹⁰⁶ *Id.*

¹⁰⁷ BORK, *supra* note __, at 122.

¹⁰⁸ *See, e.g.*, HERBERT HOVENKAMP ET AL., IP AND ANTITRUST: AN ANALYSIS OF ANTITRUST PRINCIPLES APPLIED TO INTELLECTUAL PROPERTY LAW § 7.03[A] (3d ed. 2017) (“Fundamentally, the rule of reason considers whether a restraint is output increasing or output decreasing.”).

¹⁰⁹ *See, e.g.*, BORK, *supra* note __ (arguing for a total-welfare standard, which Bork referred to as “consumer welfare”).

¹¹⁰ [[Cite]]

¹¹¹ *See infra* notes __ and accompanying text (identifying several instances of increased output resulting from inefficiencies); Mark R. Patterson, *Coercion, Deception, and Other Demand-Increasing Practices in Antitrust Law*, 66 ANTITRUST L.J. 1, 5–6 (1997) (“[C]oercion and deception can also increase demand and output, yet may injure consumers.”).

¹¹² *E.g.* Allensworth, *supra* note __.

III. DOCTRINAL BASIS FOR THE MARKET-FAILURE APPROACH

Antitrust doctrine generally supports the view that a procompetitive justification is cognizable if—but only if—it mitigates a market failure. On its face, Sherman Act § 1 condemns “[e]very . . . restraint of trade.”¹¹³ That phrase invoked a well-established common-law doctrine disfavoring contractual non-compete provisions.¹¹⁴ Initially, all such provisions were held to be against public policy and therefore invalid.¹¹⁵ But, recognizing their potential to facilitate welfare-enhancing investments and transactions, courts relaxed the doctrine to prohibit only “unreasonable” agreements not to compete. Under this standard, such agreements were “reasonable” (and therefore enforceable) so long as they were no broader than necessary to “protect the legitimate commercial interests of the party seeking protection.”¹¹⁶ This consequentialist mode of analysis provided a groundwork upon which nascent antitrust laws would build.

After some early uncertainty,¹¹⁷ the U.S. Supreme Court quickly concluded that Sherman Act § 1 similarly condemns only *unreasonable* restraints of trade.¹¹⁸ Since all contracts “restrain trade” to some degree, a literal reading of the statute would have been untenable.¹¹⁹ In its seminal *Standard Oil* opinion in 1911, the Court pronounced that “the standard of reason which had been applied at the common law . . . was intended to be the measure used” in applying the Sherman Act.¹²⁰ Thus, antitrust courts’ primary task under Sherman Act § 1 became deciding which agreements “in restraint of trade” are unreasonable, and which are reasonable.

A. Early Support

Seven years after *Standard Oil* was decided, in *Chicago Board of Trade* (“*CBOT*”), Justice Brandeis set forth the classic formulation of the rule of reason: “The history of the restraint, the *evil* believed to exist, the reason for adopting the particular *remedy*, the purpose or end sought to be attained, all are relevant facts.”¹²¹ Though

¹¹³ 15 U.S.C. § 1.

¹¹⁴ *Cf.* *United States v. Trans-Missouri Freight Ass’n*, 166 U.S. 290 (1897) (construing the Sherman Act’s prohibition of “restraints of trade”, recognizing that “[c]ontracts in restraint of trade have been known and spoken of for hundreds of years both in England and in this country”).

¹¹⁵ *See, e.g.*, *United States v. Standard Oil*, 225 U.S. 1, 51 (1911).

¹¹⁶ *See, e.g.*, David Cabrelli & Louise Floyd, *New Light Through Old Windows: Restraint of Trade in English, Scottish, and Australian Employment Laws*, 26 INT’L J. COMP. LABOUR L. 167, 168 (2010).

¹¹⁷ *United States v. Trans-Missouri Freight Ass’n*, 166 U.S. 290, 327 (1897) (rejecting argument that Sherman Act § 1 “does not mean what the language used therein plainly imports, but that it only means to declare illegal any such contract which is in *unreasonable* restraint of trade”).

¹¹⁸ *United States v. Joint Traffic Ass’n*, 171 U.S. 505 (1898).

¹¹⁹ *Id.* (“To suppose . . . that the effect of the decision in the *Trans-Missouri* case is to render illegal most business contracts . . . , however indispensable and necessary they may be . . . is to make a most violent assumption, and one not called for or justified by the decision mentioned, or by any other decision of this court.”).

¹²⁰ *Standard Oil Co. v. United States*, 221 U.S. 1, 60 (1911).

¹²¹ *Chi. Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918) (emphasis added).

not-infrequently criticized as overbroad,¹²² Brandeis’s articulation highlights a useful point: left “unrestrained” in a literal sense, markets may fail to produce optimal results, i.e., cause “evil”. Thus, what looks like a restraint of trade may, in fact, be a “remedy” for such undesirable results.¹²³

Though Brandeis wrote at a time before the modern economic concept of market failure had crystallized,¹²⁴ his opinion for the majority in *CBOT* invoked its underlying tenets. The challenged conduct—a rule freezing the price of grain during after-hours trading—was unquestionably a “restraint” of trade, specifically price competition. Yet the *CBOT* Court was hospitable to a number of the defendant’s procompetitive justifications because, as Brandeis put it, the restraint “helped to improve market conditions.”¹²⁵ Importantly, those justifications were not purely effects-based, i.e., not simple claims that the rule increased output, lowered price, etc. Rather, they contemplated (if a bit clumsily) correcting market failures by, e.g., correcting information asymmetries.¹²⁶

Around the same time, a district court decided *United States v. American Can Co.*, a case that has since attracted substantial attention.¹²⁷ (The Supreme Court refused to hear the Government’s appeal, arguably tacitly blessing the lower court’s decision.) The record was voluminous, stretching to over 8,700 printed pages.¹²⁸ Among the many instances of conduct challenged under Sherman Act §§ 1 and 2 was the defendant’s acquisitions of multiple rival manufacturers.¹²⁹ The court, however, declined to condemn these acquisitions. By allowing it to achieve sufficient size, the defendant’s conduct allowed it to invest in innovative quality-control measures,¹³⁰

¹²² See, e.g., Edward D. Cavanagh, *The Rule of Reason Re-examined*, 67 BUS. LAW. 435, 435 (2012) (“From the beginning, federal courts have been troubled by the open-ended nature of the Brandeis formulation of the Rule of Reason . . .”).

¹²³ Werden, *supra* note __, at 728 (“Brandeis invited only the justification that a restraint makes the market work better.”).

¹²⁴ See HOVENKAMP, *supra* note __, at § 2.1, at 71.

¹²⁵ *Id.* at 240 (emphasis added).

¹²⁶ *Id.* (“Before [the restraint’s] adoption, bids were made privately. Men had to buy and sell without adequate knowledge of actual market conditions. This was disadvantageous to all concerned, but particularly so to country dealers and farmers.”).

¹²⁷ A recent Westlaw “Citing References” search yielded seventy citations by secondary sources and nine citations in judicial decisions, including the district-court decisions in *Du Pont* (cellophane) and *Alcoa*.

¹²⁸ *United States v. Am. Can Co.*, 234 F. 1019 (D. Md. 1916).

¹²⁹ *Id.* at 887-89. More than a decade before the court’s decision, the defendant had engaged in a serial-acquisition that the court found to be anticompetitive. *Id.* at 881 (“It is clear an attempt was made both to restrain and monopolize the interstate trade in tin cans. Trade was restrained.”). This finding was likely correct; as the court pointed out, the defendant shuttered many of the plants immediately after acquiring them. *Id.* at 876-77. But the court declined to grant the Government’s requested structural remedy, since “defendant for a number of years past has done nothing of the sort.” *Id.* at 902.

¹³⁰ *Id.* at 894 (“Defendant makes good cans. . . . The defendant has usually at its command a wider range of expert capacity in dealing with the problems which may arise . . .”).

undertake substantial research-and-development efforts aimed at improving existing technology,¹³¹ and offer buyers a stable source of supply.¹³²

The court was particularly satisfied with the last of these virtues. “Consumers of cans,” the opinion explained, “[became] practically certain of being able to get what cans they wanted when and as they wanted them.”¹³³ And, as the court emphasized, it was the defendant’s “having great facilities” that allowed this certainty.¹³⁴ Because the defendant had used its power “on the whole, rather for weal than for woe,” the court declined to order its dissolution.¹³⁵

American Can is notable in multiple respects. First is the court’s prescient focus on consumer welfare as the touchstone for analysis.¹³⁶ This focus, it goes nearly without saying, buttresses the doctrinal case for the market-failure approach. Second is the sophistication of the court’s economic analysis. In recognizing that acquisitions can sometimes facilitate innovation competition, the court anticipated the position taken by the influential U.S. DOJ/FTC *Horizontal Merger Guidelines* published nearly a century later.¹³⁷ Additionally, the court appeared to recognize the importance of transaction costs—a textbook cause of market failure. Offering buyers a stable source of supply can eliminate their need to negotiate with a new seller in the event of, for example, a single-factory accident—a virtue emphasized by the *American Can* court¹³⁸—thereby reducing transaction costs and improving consumer welfare. These virtues—what a modern court would call “procompetitive justifications”—led the court to look favorably on the challenged conduct.

B. The Inhospitability Era

Beginning approximately with *Northern Pacific* in 1958,¹³⁹ the Court entered its “Inhospitability Era”,¹⁴⁰ a period characterized by plaintiff-friendly rulemaking.¹⁴¹ During this Era, the Court condemned outright many restraints that have subsequently

¹³¹ *Id.* at 895 (“The defendant claims, with much reason, to have been the first of the can makers systematically and scientifically to study canners’ problems, with a view to discovering the causes of damage to and deterioration in canned goods.”).

¹³² *Id.* at 895 (“From the [buyer]’s standpoint, the most important respect in which the condition of the industry has . . . changed for the better, has been the practically universal [advent] of the agreement to supply all cans needed by a packer during a particular season . . .”).

¹³³ *Id.* at 897.

¹³⁴ *Id.*

¹³⁵ *Id.* at 902.

¹³⁶ To be sure, the court framed the underlying goal of the Sherman Act in terms of protecting small businesses. But Congress’s chosen means of achieving that goal were, in the court’s view, more modest. *Id.* at 901.

¹³⁷ U.S. DOJ & FTC, HORIZONTAL MERGER GUIDELINES § 11 (2010).

¹³⁸ *Id.* at 896 (“The defendant has many shops, most of its competitors but one. The probability of its delivery of cans being altogether prevented by a factory accident is therefore almost negligible.”).

¹³⁹ *N. Pac. R. Co. v. United States*, 356 U.S. 1 (1958).

¹⁴⁰ Meese, *supra* note 51, at 146.

¹⁴¹ *See generally* HOVENKAMP, *supra* note __, § 2.1, at 82 (“1960’s antitrust policy . . . was openly hostile toward innovation and large scale development, and a zealous protector of the right of small business to operate independently.”).

been treated with much less suspicion. Few, if any, virtues could insulate a restraint from antitrust liability.¹⁴² The *Northern Pacific* Court, for example, unanimously condemned tying arrangements as *per se* illegal.¹⁴³ *Albrecht v. Herald Co.*, decided in 1968, imposed a similar *per se* ban on vertical maximum-resale-price agreements.¹⁴⁴ In 1972, the *Topco* majority applied the *per se* rule to market-division agreements,¹⁴⁵ despite fairly substantial evidence suggesting that the particular challenged agreement was not harmful.¹⁴⁶

Many Inhospitality Era decisions appear primarily concerned with protecting the “competition” or the “competitive process”, rather than consumer welfare.¹⁴⁷ The *Northern Pacific* Court, for example, was troubled by tying arrangements’ “pernicious effect on competition”.¹⁴⁸ The *Albrecht* Court preferred *per se* condemnation of vertical maximum-resale-price agreements due to concerns that such “schemes” disrupt “the forces of the competitive market.”¹⁴⁹ The *Topco* majority flatly rejected the defendant’s proffered justifications, reasoning that antitrust tribunals are unable “to weigh, in any meaningful sense, destruction of competition in one sector of the economy against promotion of competition in another sector.”¹⁵⁰

Inhospitality Era decisions never defined, exactly, what comprises “competition” or the “competitive process”. Instead, these opinions explained themselves by reference to an equally ill-defined bundle of “rights” and “freedoms”. The *Northern Pacific* Court, for example, fretted over the loss of landowners’ “freedom to deal with competing carriers”.¹⁵¹ The *Albrecht* majority was concerned that vertical maximum-resale-price agreements “cripple the freedom of traders.”¹⁵² The *Topco* majority stated that the antitrust laws protect “our fundamental personal freedoms,”¹⁵³ and that “guaranteed each and every business, no matter how small, is

¹⁴² Though this Article focuses on restraints of trade, merger case law during this time exhibited analogous hostility to “efficiencies” defenses. *See, e.g.*, *United States v. Procter & Gamble Co.*, 386 U.S. 568, 580 (1967) (“Congress was aware that some mergers which lessen competition may also result in economies but it struck the balance in favor of protecting competition.”). Subsequent courts have hewed closer to this precedent than to analogous restraints-of-trade precedent. *See, e.g.*, *United States v. Aetna, Inc.*, No. 16-1494, 2017 WL 325189, *70 (D.D.C. Jan. 23, 2017) (requiring “proof of extraordinary efficiencies” to justify a presumptively anticompetitive merger). This is perhaps unsurprising: mergers (unlike restraints of trade) necessarily eliminate a marketplace participant.

¹⁴³ 356 U.S. at 8.

¹⁴⁴ *Albrecht v. Herald Co.*, 390 U.S. 145, 152 (1968).

¹⁴⁵ *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972).

¹⁴⁶ Alan J. Meese, *Competition and Market Failure in the Antitrust Jurisprudence of Justice Stevens*, 74 *FORDHAM L. REV.* 1775, 1782 n.56 (2006).

¹⁴⁷ *See* Werden, *supra* note 79, at 757.

¹⁴⁸ 356 U.S. at 5. That said, the Court also foreshadowed the Modern Era by emphasizing the centrality of efficiency to antitrust law: “[The Sherman Act] rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources” *Id.* at 4.

¹⁴⁹ *Albrecht v. Herald Co.*, 390 U.S. 145, 152 (1968).

¹⁵⁰ *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972).

¹⁵¹ 356 U.S. at 7.

¹⁵² *Albrecht v. Herald Co.*, 390 U.S. 145, 152 (1968).

¹⁵³ 405 U.S. at 610.

the freedom to compete—to assert with vigor, imagination, devotion, and ingenuity whatever economic muscle it can muster.”¹⁵⁴

But these decisions were subsequently relegated (for the most part¹⁵⁵) to the dustbin of history. The Court explicitly overruled many of them,¹⁵⁶ and has substantially eroded others.¹⁵⁷ The Inhospitality Era met its end less than twenty years after *Northern Pacific* marked its birth.

C. The Modern Era

By 1977, the economic conceptions of market failure and efficiency had gained considerable clarity. In *GTE Sylvania*, often heralded as marking the beginning of the “Modern Era” of antitrust,¹⁵⁸ the Court reversed its earlier *per se* prohibition of vertical exclusive-territory restraints. At a high level, the rationale for treating such restraints with less suspicion was their likelihood of creating “efficiencies”.¹⁵⁹ More specifically, the majority reasoned such restraints can alleviate “*market imperfections* such as the so-called ‘free rider’ effect.”¹⁶⁰ Thus, the Court ushered in the Modern Era of antitrust by explicitly invoking the market-failure approach to justification analysis. Free-riding—which can cause welfare-reducing underproduction—results from the presence of externalities, a common cause of market failure.¹⁶¹ It bears emphasizing that the Court’s focus was not on whether the restraint created a particular type of marketplace effect, such as higher output or lower prices.¹⁶² Rather, the Court held that restraints may be justified where they alleviate market failures.

One year later, the Court issued a puzzling opinion best understood as a leftover from the Inhospitality Era. *Professional Engineers* involved a trade association rule prohibiting members from submitting price bids to potential customers.¹⁶³ The association attempted to justify its rule by arguing that without the

¹⁵⁴ *Id.*

¹⁵⁵ *Topco* has not been explicitly overruled, though some lower courts have blatantly disregarded it. *See, e.g., Polk Bros., Inc. v. Forest City Enters., Inc.*, 776 F.2d 185 (7th Cir. 1985); E. THOMAS SULLIVAN & JEFFREY L. HARRISON, UNDERSTANDING ANTITRUST AND ITS ECONOMIC IMPLICATIONS § 4.14 (5th ed. 2009) (“The question arises whether [such cases] are reconcilable with *Topco* or whether they are mere examples of judicial activism by lower federal court judges.”).

¹⁵⁶ *See, e.g., Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 58 (1977) (overruling the *per se* rule for vertical exclusive-territory restrictions announced in *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967)).

¹⁵⁷ *Compare, e.g., Jefferson Parish Hosp. Dist. v. Hyde*, 466 U.S. 2 (1984) (requiring a finding of market power before condemning tying arrangements), with *Northern Pacific*, 356 U.S. 1 (1958) (rejecting a requirement of “monopoly power” and requiring only “sufficient economic power”).

¹⁵⁸ *See, e.g., Lindsey M. Edwards & Joshua D. Wright, The Death of Antitrust Safe Harbors: Causes and Consequences*, 23 GEO. MASON L. REV. 1205, 1205 (2016).

¹⁵⁹ *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 54 (1977).

¹⁶⁰ *Id.* at 55 (emphasis added).

¹⁶¹ *See, e.g., MASSIMO MOTTA, COMPETITION POLICY: THEORY AND PRACTICE* 314–16 (2004).

¹⁶² It was the concurring opinion that appeared more focused on the restraint’s “output-enhancing possibilities,” rather than its efficiency-enhancing possibilities. *Id.* at 70 (White, J., concurring in the judgment).

¹⁶³ *Nat’l Soc’y of Prof’l Engineers v. United States*, 435 U.S. 679, 684 (1978).

rule, the market would produce suboptimally low-quality engineering services.¹⁶⁴ Although not often recognized as such, this was a market-failure-based justification¹⁶⁵ (albeit one with questionable substantive merits).

In sweeping language, however, Justice Stevens condemned the proffered justification as “nothing less than a frontal assault on the basic policy of the Sherman Act.”¹⁶⁶ Stevens castigated the association for arguing that competition itself was “bad”.¹⁶⁷ That was, of course, precisely what the association was arguing: that the challenged restraint alleviated the relevant market’s tendency to produce “bad” outcomes. The problem with this argument, according to Stevens, was that “the statutory policy precludes inquiry into the question whether competition is good or bad.”¹⁶⁸ *Professional Engineers* thus appears to have employed the retrograde competitive-process approach,¹⁶⁹ which leaves little room for defendants to proffer justifications.

The following year (1979), the Court issued *BMI*, and with it signaled a clear return to the Modern Era’s market-failure approach to justification analysis. At issue was a joint copyright-licensing agreement that involved horizontal price-fixing.¹⁷⁰ Eight justices—and the U.S. Justice Department as *amicus*—agreed that even a horizontal price-fixing agreement should receive rule-of-reason treatment when it alleviated a market failure.¹⁷¹ Only Justice Stevens dissented.¹⁷² Unrestrained, the relevant market exhibited prohibitive transaction costs: “the impracticability of negotiating individual licenses for each composition.”¹⁷³ The restraint eliminated such transaction costs, which are a textbook source of market failure.¹⁷⁴

Some subsequent authorities instead describe *BMI* as hinging on the output increase caused by the restraint.¹⁷⁵ Under this view, *BMI* exemplifies the type-of-

¹⁶⁴ See, e.g., Brief for Petitioner, 435 U.S. 679, at *54 (“NSPE contends . . . that . . . the submission of a bid . . . before the problem can possibly be comprehended or an adequate approach to it proposed limits the amount and quality of analysis ultimately applied to the problem . . .”).

¹⁶⁵ At least in part, see *infra* notes __ and accompanying text.

¹⁶⁶ 435 U.S. at 695.

¹⁶⁷ *Id.*

¹⁶⁸ *Id.* Despite its peculiar reasoning, the *Professional Engineers* majority likely reached the correct substantive outcome. There were likely alternative restraints available to the association that would have been much less restrictive, yet still offered similar benefits. And, as demonstrated below, Stevens’s hostility was most likely a misdirected response to the particular *type* of market failure allegedly corrected by the restraint.

¹⁶⁹ At the very least, Stevens *invoked* that approach. See Meese, *supra* note 31, at __ (arguing that the *Professional Engineers* Court actually applied a market-failure approach).

¹⁷⁰ *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1 (1979).

¹⁷¹ *Id.* at 15 (“[T]he United States disagrees with the Court of Appeals in this case, and urges that the blanket licenses . . . are not *per se* violations of the Sherman Act.”).

¹⁷² *Id.* at 25.

¹⁷³ 441 U.S. at 15 (quoting Memo. for United States as Amicus Curiae on Pet. for Cert., *K-91, Inc. v. Gershwyn Publ’g Corp.*, 88 S. Ct. 761 (1968) (internal quotation marks omitted)).

¹⁷⁴ See *supra* notes __ and accompanying text.

¹⁷⁵ See, e.g., *SCFC ILC, Inc. v. Visa USA, Inc.*, 36 F.3d 958, 964 (10th Cir. 1994).

effect approach critiqued *infra*.¹⁷⁶ But the Court mentioned “output” only in passing, and not strictly in connection with procompetitive justifications,¹⁷⁷ whereas it placed great weight on the fact that “a bulk license of some type is . . . necessary to achieve the[] efficiencies.”¹⁷⁸ In other words, the reduction of transaction costs (which had previously caused a market failure)—not the resulting output increase *per se*—dictated rule-of-reason treatment.

In 1984, the Supreme Court again employed the market-failure approach to justification analysis. *NCAA v. Board of Regents* involved an arrangement between undergraduate universities to jointly license the right to televise amateur-athletic sporting events.¹⁷⁹ Because such agreements can be “efficient”, the majority opinion—written by none other than Justice Stevens—found *per se* treatment to be inappropriate, even where the relevant restriction was a rather blatant output-reduction scheme.¹⁸⁰

The majority at times did use the terms “efficiency” and “increase[d] output” roughly interchangeably,¹⁸¹ suggesting (at least arguably) that it was instead employing the type-of-effect approach. This is, however, not the best reading of *Board of Regents*. Some early Modern Era analysts, Bork in particular, often appeared to conflate efficiency and higher output, but the modern consensus is that higher output is not always an efficient outcome.¹⁸² A variety of inefficient conditions and strategies (external costs, coercion, overconsumption, deception, etc.) can increase output.¹⁸³ Thus, the *Board of Regents* Court’s emphasis on output effects can most helpfully be understood not as endorsing Bork’s extreme-form type-of-effect analysis, but as a response to the particular restraint at issue: an agreement to restrict output.

In 1997, *State Oil Co. v. Khan* overturned the decades-old rule prohibiting vertical restraints setting maximum retail prices as illegal *per se*.¹⁸⁴ That rule traced its roots to *Albrecht*,¹⁸⁵ an opinion the *Khan* Court characterized as “grounded in the fear that maximum price fixing by suppliers could interfere with dealer freedom.”¹⁸⁶ Ironically, as the *Khan* Court pointed out, the ban on vertical maximum price fixing had prompted many suppliers to vertically integrate, thereby “eliminating the very

¹⁷⁶ See *infra* Part IV.B (demonstrating that the type-of-effect approach yields excessive error costs).

¹⁷⁷ 441 U.S. at 20 (framing the zero-step of analysis as a question of whether “the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output . . . , or instead one designed to ‘increase economic efficiency’” (quoting *U.S. Gypsum Co.*, 438 U.S. at 441 n.16)).

¹⁷⁸ *Id.* at 21.

¹⁷⁹ *NCAA v. Bd. of Regents of Oklahoma*, 468 U.S. 85 (1984).

¹⁸⁰ *Id.* at 103. The Court ultimately rejected the NCAA’s proffered justifications—calling them “efficiency justification[s]”, *id.* at 114–15—as being factually and legally unsupported.

¹⁸¹ *Id.* at 114.

¹⁸² See, e.g., Patterson, *supra* note __.

¹⁸³ See *infra* notes __ and accompanying text.

¹⁸⁴ 522 U.S. 3 (1997).

¹⁸⁵ *Albrecht v. Herald Co.*, 390 U.S. 145 (1968).

¹⁸⁶ 522 U.S. at 17.

independent trader for whom *Albrecht* professed solicitude.”¹⁸⁷ Justice O’Connor, writing for a unanimous majority, identified the following procompetitive justification for vertical maximum price fixing: “A supplier might . . . fix a maximum resale price in order to prevent his dealers from exploiting a monopoly position.”¹⁸⁸ Monopoly power (like transaction costs and externalities) is a textbook cause of market failure.¹⁸⁹ By overruling *Albrecht* and disapproving of its normative basis, *Khan* rather emphatically rejected the competitive-process approach. And by focusing on the restraint’s alleviation of a market failure, rather than its effect on output, *Khan* continued the Modern Era’s embrace of the market-failure approach.

The Supreme Court’s most recent in-depth justification analysis appeared in its 2007 *Leegin* decision.¹⁹⁰ The *Leegin* Court again employed the language of market failure and efficiency, this time to strike down a longstanding rule that vertical minimum-resale-price restraints were *per se* illegal. Because such restraints may often be the “most efficient way”¹⁹¹ to lower certain transaction costs,¹⁹² can decrease information asymmetries,¹⁹³ and prevent free-riding from “forcing [firms] to cut back [their] services to a level lower than consumers would otherwise prefer,”¹⁹⁴ the Court rejected *per se* illegality in favor of the rule of reason .

In sum, nearly a century of U.S. Supreme Court antitrust precedent counsels in favor of the market-failure approach to justification analysis. Against this backdrop, the relatively brief Inhospitality Era appears to be a historical aberration. And had *Professional Engineers* been issued just a few years earlier, it would today most likely be viewed as simply another relic of that bygone age. It is only by historical accident that *Professional Engineers* falls within what has become viewed as the Modern Era of antitrust, an accident that has perhaps caused it to attract more than its share of scholarly attention.

In hindsight, it seems Justice Stevens was wrong to flatly condemn all justifications that hinge on unrestrained competition producing “bad” outcomes. The vast majority of precedent—other than that issued during the earlier Inhospitality Era—holds that alleviating a market failure is an acceptable procompetitive justification. The defendants in *CBOT*, *GTE Sylvania*, *BMI*, *Board of Regents*, *Khan*, and *Leegin* all successfully argued that unrestrained competition was producing “bad” outcomes. In fact, *Professional Engineers* was at least arguably overruled by multiple

¹⁸⁷ *Id.* (quoting 8 PHILLIP AREEDA, ANTITRUST LAW ¶ 1635 (1989)).

¹⁸⁸ *Id.* at 16 (quoting *Khan & Assocs., Inc. v. State Oil Co.*, 93 F.3d 1358 (7th Cir. 1996) (internal quotation marks omitted)).

¹⁸⁹ RICHARD G. LIPSEY & COLIN HARBURY, FIRST PRINCIPLES OF MICROECONOMICS 169 (2d ed. 1992) (“[T]here is clearly a case to be made against monopoly on grounds of market failure . . .”).

¹⁹⁰ *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007).

¹⁹¹ *Id.* at 892.

¹⁹² *Id.* (“It may be difficult and inefficient for a manufacturer to make and enforce a contract with a retailer specifying the different services the retailer must perform.”).

¹⁹³ *Id.* at 891 (observing that resale-price maintenance may incentivize new entry by inducing firms to “make the kind of investment of capital and labor that is often required in the distribution of products *unknown to the consumer*” (internal quotation marks omitted) (emphasis added)).

¹⁹⁴ *Id.*

Modern Era decisions, including the majority opinion in *Board of Regents*—which Stevens himself penned.¹⁹⁵

D. Ramifications for Non-Welfare Justifications

Antitrust defendants occasionally proffer non-welfare-related explanations for their conduct. As we have seen, however, the bulk of authority indicates that only alleviating a market failure—and thereby increasing welfare—can give rise to a valid justification. It follows that, under Modern Era jurisprudence, non-welfare explanations should not be evaluated under the rule of reason, i.e., they should not come into play either at the zero-step or during a full-scale inquiry. This Subpart contends that instead, as a matter of both antitrust doctrine and policy, such explanations are to be considered only at the very outset of judicial decision-making. Thus, the scattered lower-court decisions attempting to weigh non-welfare explanations during rule-of-reason analyses were incorrect.

As an initial linguistic matter, this Article consciously uses the signifier “non-welfare” to refer to justifications unrelated to the economic conceptions of welfare and market failure. Elsewhere, such justifications are occasionally discussed under the appellation “non-economic”.¹⁹⁶ But, in a broad sense, “economic” as a modifier could apply to every possible justification—Merriam-Webster, for example, defines “economic” as “of, relating to, or based on the production, distribution, and consumption of goods and services”.¹⁹⁷ Moreover, modern economics as a discipline encompasses an exceedingly broad variety of subject matters.¹⁹⁸ As the scope of the discipline grows, the “economic/non-economic” dichotomy becomes increasingly unhelpful.¹⁹⁹ Consequently, the present discussion dispenses with the term “non-economic”, in favor of the more descriptive “non-welfare”.

The antitrust enterprise does immunize truly non-welfare-motivated conduct from liability. But this immunity is bestowed by labeling such conduct “noncommercial” at the very outset of a given case. Conduct that is deemed

¹⁹⁵ *NCAA v. Bd. of Regents of Oklahoma*, 468 U.S. 85 (1984).

¹⁹⁶ See, e.g., Julie L. Seitz, Comment, *Consideration of Noneconomic Procompetitive Justifications in the MIT Antitrust Case*, 44 EMORY L.J. 395 (1995); see also Robert Pitofsky, *The Political Content of Antitrust*, 127 U. PA. L. REV. 1051, 1051 (1979) (“The issue among most serious people has never been whether non-economic considerations should outweigh significant long-term economies of scale, but rather whether they had any role to play at all . . .”).

¹⁹⁷ MERRIAM-WEBSTER, *Economic*, <https://www.merriam-webster.com/dictionary/economic>.

¹⁹⁸ See, e.g., Herbert A. Simon, *Altruism and Economics*, 83 AM. ECON. REV. 156 (1993).

¹⁹⁹ In fact, the term was likely unhelpful from the beginning. Modern economics stakes out incredibly broad territory—the American Economic Association, for example, defines “economics” as “the study of scarcity, the study of how people use resources, or the study of decision-making.” AEA, *What Is Economics? Understanding the Discipline*, <https://www.aeaweb.org/resources/students/what-is-economics> (last visited June 22, 2017). With such an all-encompassing definition in place, one might well ask whether any aspect of human interaction could properly be considered “noneconomic”. For an admirably broad early definition, see LIONEL ROBBINS, AN ESSAY ON THE NATURE AND SIGNIFICANCE OF ECONOMIC SCIENCE 4 (1932) (“The definition of Economics which would probably command most adherents . . . is that which relates it to the study of the causes of material welfare.”).

noncommercial falls outside the ambit of the Sherman Act, which by its terms applies only to “trade” or “commerce”.²⁰⁰ Thus, for example, the Eighth Circuit in *Missouri v. NOW*²⁰¹ declined to apply antitrust law to a boycott organized by the National Organization for Women (“NOW”). NOW refused to hold conventions in states that had not ratified the proposed Equal Rights Amendment to the U.S. Constitution.²⁰² Recognizing the boycott’s “social” and “political” purpose, the court deemed the challenged restraint entirely beyond the scope of the Sherman Act.²⁰³ This decision was reached before the zero-stage of analysis (deciding between the rule of reason and the *per se* rule), before initiating a rule-of-reason analysis, and certainly before proceeding to the procompetitive-justification stage of rule-of-reason analysis. On somewhat analogous facts (a politically motivated boycott), the U.S. Supreme Court has expressed similar sentiments.²⁰⁴

But lower courts have occasionally attempted to weigh non-welfare justifications as part of a full-scale rule-of-reason analysis. *JES Properties, Inc. v. USA Equestrian, Inc.*²⁰⁵ provides one rather striking example. The case involved horse-show competitions that were organized by a national governing body whose members owned the horses that competed.²⁰⁶ The governing body issued a rule—subsequently challenged as an anticompetitive restraint of trade—granting “officially recognized” status to shows scheduled on the same date only when such shows were to take place more than 250 miles apart.²⁰⁷ The district court located a valid procompetitive justification in the fact that the restraint “promote[d] the *health and welfare of the horses*.”²⁰⁸ It goes nearly without saying that the health of horses is unrelated to consumer welfare and the economic conception of market failure.²⁰⁹

²⁰⁰ See 15 U.S.C. § 1 (2012) (prohibiting restraints “of trade or commerce”); *id.* § 2 (banning monopolization or attempted monopolization of “any part of . . . trade or commerce”); see also John M. Newman, *Antitrust in Zero-Price Markets: Foundations*, 164 U. PA. L. REV. 149, 159–60 (2015) (analyzing whether zero-price products constitute “trade or commerce” under the Sherman Act).

²⁰¹ *Missouri v. Nat’l Org. for Women, Inc.*, 620 F.2d 1301 (8th Cir. 1980).

²⁰² *Id.* at 1302–03.

²⁰³ See *id.* at 1311–12; see also *id.* at 1319 (“We hold today that the Sherman Act does not cover NOW’s boycott activities . . .”).

²⁰⁴ See *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886, 914 (1982) (“[T]he purpose of petitioners’ campaign was not to destroy legitimate competition. Petitioners sought to vindicate rights of equality and of freedom that lie at the heart of the Fourteenth Amendment itself.”).

²⁰⁵ *JES Properties, Inc. v. USA Equestrian, Inc.*, 2005 WL 1126665, No. 802CV1585T24MAP (M.D. Fla. May 9, 2005).

²⁰⁶ *Id.* at *2.

²⁰⁷ *Id.* at *2 & n.3.

²⁰⁸ *Id.* at *17.

²⁰⁹ One could argue that an externality is at play, but it is, at best, not the sort of externality contemplated by antitrust law and economics. See, e.g., JEAN TIROLE, *THE THEORY OF INDUSTRIAL ORGANIZATION* 7 n.18 (1988) (“An externality arises when the consumption of a good by a consumer directly affects the welfare of another consumer, or when a firm’s production affects other economic agents.” (emphasis added)). The nature of those affected is the key distinction. Antitrust law can properly recognize (e.g.) investments in promotional materials as creating an externality because such investment directly affects other economic agents. By way of contrast, an owner’s behavior may detrimentally affect her horse’s health, but that “cost” is not imposed as an “externality” in the antitrust sense of the term, even though a layperson might (perhaps understandably) view such harm as an externalized cost.

Similarly, in *Brown University*, the Third Circuit appeared hospitable to a non-welfare justification.²¹⁰ At issue was an agreement among a group of Ivy League colleges to award financial aid only on the basis of need, and to ensure that aid offers would be comparable across colleges.²¹¹ In its defense, MIT (the only college that proceeded to trial) argued that the restraint facilitated access to education for financially disadvantaged students. The court credited this justification, in a decision that attracted substantial criticism.²¹² MIT’s argument—though perhaps noble—was unrelated to an economic market failure. To be sure, the court attempted to dress this justification in the structural language of “consumer choice”.²¹³ But the restraint did not create a new product, thereby increasing “consumer choice” as that term is used in the antitrust context.²¹⁴

Most recently, in *NCAA v. O’Bannon*, the Ninth Circuit waffled between treating a justification under the rubric of market failure or through a non-welfare lens—but appeared ready to credit the justification either way.²¹⁵ There, the challenged restraint was an NCAA rule prohibiting member schools from compensating student-athletes for the use of their names, images, and likenesses.²¹⁶ The court affirmed the district court’s holding that, by preserving “amateurism”, the rule could procompetitively increase consumer (i.e., viewer) demand.²¹⁷

It is possible to view this holding as an application of the market-failure approach. The relevant market failure may have arisen because of divergence between individual and group interests, such that a given course of action may be rational for an individual group member but, when undertaken by the entire group, leaves all group members worse off. Specifically, an individual school may be incentivized to pay its own athletes in order to produce a winning team. Other schools could then be incentivized to follow suit, even if the resulting shift away from an amateur model would be to reduce overall demand for the product,²¹⁸ inefficiently reducing consumer welfare.

²¹⁰ *United States v. Brown Univ.*, 5 F.3d 658 (3d Cir. 1997).

²¹¹ *Id.* at 662.

²¹² *See, e.g., Seitz, supra* note 178, at 427 (“Allowing courts to consider social, noneconomic justifications injects an unacceptable level of politics and personal opinion into antitrust analysis.”).

²¹³ 5 F.3d, at 675. The Third Circuit cited *NCAA v. Board of Regents of Oklahoma* for the proposition that consumer choice can be a valid procompetitive justification.

²¹⁴ *NCAA*, upon which the Third Circuit relied, was addressing a market (amateur collegiate sports) in which some horizontal restraints were necessary in order for the product to be offered at all. *NCAA v. Bd. of Regents of Oklahoma*, 468 U.S. 85, 101 (1984). Thus, some restraints—though not the particular restraint at issue in that case—did increase consumer choice.

²¹⁵ *O’Bannon v. NCAA*, 802 F.3d 1049 (9th Cir. 2015).

²¹⁶ *Id.* at 1052.

²¹⁷ *Id.* at 1059.

²¹⁸ *See generally* Stucke, *supra* note 41, at 25 (describing various examples of divergence between individual and group interests).

But the Ninth Circuit in *O'Bannon* also came quite close to blessing amateurism *per se*, as if amateurism carries intrinsic benefits unrelated to efficiency.²¹⁹ The court fretted that “the district court ignored that not paying student–athletes is *precisely what makes them amateurs*”²²⁰ and that paying players any amount would remove all “basis for returning to a rule of amateurism”, transforming college football into “minor league” football.²²¹ But the court did not explain why—in terms of consumer welfare—that state of affairs would be undesirable.

Decisions validating, and attempting to weigh, non-welfare justifications during rule-of-reason analyses represent bad law and bad policy. Doctrinally, they represent an unwarranted deviation from established precedent.²²² As the foregoing demonstrates, only those restraints that alleviate an economic market failure are cognizable as procompetitive justifications.²²³ Proper rule-of-reason analysis therefore does not recognize non-welfare justifications—which, by their nature, do not alleviate a market failure—as valid. In fact, as most readers have likely already concluded, the name is something of a misnomer: as part of a rule-of-reason analysis, these “justifications” are anything but.²²⁴

Modern antitrust law’s approach to non-welfare justifications represents a balanced compromise. On the one hand, the antitrust enterprise seeks to further its consensus goal of promoting consumer welfare. On the other, it should not do so *ad infinitum*—there are other societal goals than these,²²⁵ and a single-minded pursuit of economic welfare may have the perverse effect of leaving society worse off. Antitrust doctrinally recognizes the need for balance by immunizing truly non-welfare-motivated, or “noncommercial”, conduct, as did the *Missouri v. NOW* court.²²⁶ Extending that comity to the second-to-last step of a full-scale rule-of-reason analysis would upset that careful balance.

Crediting non-welfare justifications during rule-of-reason analyses creates awkward, and essentially intractable, commensurability problems. Cases that proceed to the procompetitive-justifications stage can already present difficult trade-offs: how, for example, should a court balance quality improvements against price increases?²²⁷ But if such cases are difficult, adding social and moral considerations to the mix would make them nigh impossible. How is a generalist court supposed to weigh improved horse welfare against an increase in the price of tickets to horse-show competitions?

²¹⁹ In this way, the Ninth Circuit’s opinion echoed Justice White’s dissent in *NCAA v. Board of Regents of Oklahoma*, which argued in favor of recognizing “noneconomic values like the promotion of amateurism.” 468 U.S. 85, 134 (White, J., dissenting).

²²⁰ 802 F.3d, at 1076.

²²¹ *Id.* at 1078–79.

²²² See generally AREEDA & HOVENKAMP, *supra* note 1, at ¶ 262 (summarizing cases holding that noncommercial activities are immune from antitrust liability).

²²³ See *supra* notes ___ and accompanying text.

²²⁴ Hence the scare quotes in the title of this Subpart.

²²⁵ Cf. STEPHEN KING, *THE GUNSLINGER* (2003) (“Go then, there are other worlds than these.”).

²²⁶ *Missouri v. Nat’l Org. for Women, Inc.*, 620 F.2d 1301 (8th Cir. 1980).

²²⁷ Allensworth, *supra* note ___.

How does increasing access to prestigious colleges for financially disadvantaged students stack up against higher tuition prices to other students? What is the value of “amateurism” as a virtue unto itself, and how does it compare to lower wages for student–athletes? These questions are alien to antitrust law and economics.

Such policy questions are better answered by the legislative branch. Indeed, that is exactly what Congress did in response to the Justice Department lawsuit underlying *Brown University*. In 1992, the same year the Third Circuit’s decision was issued, Congress enacted an antitrust exemption for the specific conduct at issue in that case.²²⁸ The exemption has subsequently been extended repeatedly, demonstrating that Congress is capable of intervening if and when necessary.²²⁹

IV. ERROR-COST ANALYSIS

The modern antitrust enterprise is concerned with the social costs of erroneous decisions.²³⁰ Failures to condemn anticompetitive behavior (false negatives) reduce welfare, as do decisions that condemn procompetitive behavior (false positives). All else equal, the optimal approach to procompetitive-justification analysis is the one that most effectively minimizes such error costs. As the following discussion demonstrates, the market-failure approach does so.

A. Competitive Process: Excessive False Positives

As noted above, during the Inhospitality Era (and in *Professional Engineers*), the U.S. Supreme Court did appear to employ a competitive-process approach to justification analysis. In addition to those anachronistic decisions, the Court’s more modern rule-of-reason jurisprudence occasionally refers to restraints’ “impact on competition”²³¹ and “the competitive process.”²³² Scholar–enforcer Gregory Werden locates in such references and in the rhetoric of *Professional Engineers* a “single-minded focus on the competitive process.”²³³ Under this view, because “Congress has established a legislative policy favoring competition,”²³⁴ defendants cannot justify restraining the competitive process by pointing to failures of that same competitive

²²⁸ See 154 CONG. REC. 22,817 (2008) (statement of Rep. Smith) (“This exemption originated because Congress disagreed with a suit brought by the Department of Justice against nine colleges for their efforts to use common criteria to assess each student’s financial need.”).

²²⁹ *JES Properties* likewise reached its ultimate conclusion via legislative action, though somewhat more indirectly. On appeal, the Eleventh Circuit affirmed the district court’s holding that the defendants were granted implied antitrust immunity by the Ted Stevens Olympic and Amateur Sports Act. *JES Props., Inc. v. USA Equestrian, Inc.*, 458 F.3d 1224 (11th Cir. 2006).

²³⁰ See Easterbrook, *supra* note __.

²³¹ *FTC v. Ind. Fed’n of Dentists*, 476 U.S. 447, 458 (1986) (“[T]he test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition.”).

²³² *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128, 135 (1998).

²³³ Werden, *supra* note __, at 732–37.

²³⁴ *Hammer*, *supra* note 5, at 854–55. Hammer does not subscribe to this view, but merely observes its existence.

process. On this point, Werden deems *Professional Engineers* “one of the Court’s most elucidating” rule-of-reason decisions.²³⁵

But without more clarity, the competitive-process approach offers too little guidance to courts. As a result, it carries substantial risk of producing incorrect decisions, in the form of both false negatives and false positives. Although the Court not infrequently lauds the virtues of “competition” and the “competitive process” even during the Modern Era, it has never explained what those terms actually mean. Werden likewise argues for the competitive-process approach without ever seeming to clearly define “competitive process”.²³⁶ It remains unclear exactly why certain restraints (but not others) harm the competitive process or are justified.²³⁷ Even Werden observes that restraints are sometimes justified where “they make the market *work better*.”²³⁸ But what does “better” mean in this context? If “better” means simply “more efficient”,²³⁹ then it is unclear what value the competitive-process approach might add. Elsewhere, Werden posits that “a defendant cannot justify a restraint on the basis that it promotes social or consumer welfare in any way other than through promoting competition”²⁴⁰—but then observes that “[n]evertheless, a restraint likely would be permitted if the factfinder determined it was necessary to public health or safety.”²⁴¹ Why would this be so, if there were not some value at play other than the “competitive process” (or, at the very least, some other chosen means for promoting that value)?

Perhaps “competition” in this context means a state of atomistic rivalry in the spot market, to be pursued as an end unto itself²⁴² or in order to vindicate the vaguely defined grouping of rights discussed above.²⁴³ During the Court’s Inhospitality Era,

²³⁵ Werden, *supra* note 96, at 732.

²³⁶ The clearest definition this author could locate is as follows: “[R]ules designed to ensure the control of economic power that is incompatible with the social and political values of a just community, the integrity of individualism in that community, and the ideal of equality of economic opportunity. . . . [This approach] is often identified by the concept of a ‘competitive process’ and derives its meaning from a multiplicity of social sciences including history, economics, philosophy, political science, and sociology.” John J. Flynn, 35 N.Y.L. SCH. L. REV. 893, 897 (1990). While arguably an apt description of the Sherman Act’s overarching goals, it is difficult to ascertain how this approach would guide justification analysis in a given case.

²³⁷ Indeed, as Hammer observes, “[c]ompetition is a wonderfully ill-defined term.” *Id.* at 850 n.3.

²³⁸ Werden, *supra* note 96, at 754 (emphasis added).

²³⁹ There is some suggestion of this—Werden concludes that because “vertical restraints hold the promise of increasing a firm’s efficiency and enabling it to compete more effectively, . . . they normally do not harm the competitive process.” *Id.* at 750 (internal quotation marks omitted).

²⁴⁰ *Id.* at 753.

²⁴¹ *Id.* at 753 n.258.

²⁴² See, e.g., Alan J. Meese, *In Praise of All or Nothing Dichotomous Categories: Why Antitrust Law Should Reject the Quick Look*, 104 GEO. L.J. 835, 836 (2016) (“During antitrust’s ‘inhospitality era,’ courts declared . . . agreements unlawful per se, drawing upon economic theory hostile to various contracts that, although not naked, thwarted atomistic competition by restraining the conduct of trading partners.”), Alan J. Meese, *Robert Bork’s Forgotten Role in the Transaction Cost Revolution*, 79 ANTITRUST L.J. 953, 954 (2014) (describing the “inhospitality tradition of antitrust: an instinctive hostility to business conduct other than moment-by-moment rivalry in the spot market” (internal quotation marks omitted)).

²⁴³ See *supra* notes ___ and accompanying text.

nearly every restraint was treated as harmful to the “competitive process”,²⁴⁴ suggesting that not much more than simple, one-off contracts could escape liability. This approach to decisionmaking produces excessive false positives—courts using it will systematically condemn beneficial restraints. In fact, the entire agenda of the Chicago School of antitrust can largely be distilled into one objective: to critique the rules crafted during the Inhospitality Era on the grounds that they excessively condemned welfare-enhancing conduct.²⁴⁵ That objective was, of course, largely achieved. A variety of restraints that reduce “competition-as-atomistic-rivalry”, even horizontal price-fixing²⁴⁶ or market-allocation²⁴⁷ agreements, can potentially pass muster under modern antitrust law.

Thus, the competitive-process approach is either so ill-defined as to be effectively devoid of content, or it produces results so one-sided that the Court abandoned it after a brief dalliance. If the former, then the competitive-process approach will very likely yield a great deal of both false positives and negatives, randomly distributed. If the latter, it will yield—and, during the Inhospitality Era, did yield²⁴⁸—close to zero false negatives but an inordinate amount of false positives, skewing the field systematically in favor of plaintiffs. Either way, this approach fails to perform its supposed task of sorting legal (“reasonable”) from illegal (“unreasonable”) conduct, a task that is among the most time-honored elements of antitrust analysis.

The ironclad rule that restraints of trade are sometimes justified (i.e., are “reasonable”) depends on the often-implicit assumption that unrestrained markets sometimes fail to function well. A “restraint of trade” can be justified only if “trade” would produce worse outcomes without the restraint, a point even competitive-process advocates at times seem to recognize.²⁴⁹ Stevens, then, had it precisely backwards in *Professional Engineers*. The Sherman Act’s underlying policy does not preclude, but rather *mandates*, inquiry into “whether competition is good or bad” in a given market. That inquiry lies at the very heart of the rule of reason. It is Stevens’ failure to

²⁴⁴ See, e.g., Werden, *supra* note 96, at 729 (“*Northern Pacific* began an era during which the Supreme Court saw a ‘pernicious effect’ in every restraint it examined.”).

²⁴⁵ See, e.g., BORK, *supra* note __, at 7 (“Certain of its doctrines preserve competition, while others suppress it, resulting in a policy at war with itself.”).

²⁴⁶ *Broadcast Music, Inc. v. CBS*, 441 U.S. 1 (1979); Christopher Leslie, Comment, *Achieving Efficiency Through Collusion: A Market Failure Defense to Horizontal Price-Fixing*, 81 CAL. L. REV. 243, 263 (1993) (calling the joint license in *BMI* “the essence of price-fixing”); see also *O’Bannon v. NCAA*, 802 F.3d 1049 (9th Cir. 2015) (recognizing some procompetitive justifications for a horizontal agreement to fix prices paid by universities for the right to student-athletes’ names, images, and likenesses).

²⁴⁷ See *Polk Bros., Inc. v. Forest City Enters., Inc.*, 776 F.2d 185 (7th Cir. 1985) (product-market allocation); cf. *United States v. Kemp & Assocs., Inc.*, Case No. 2:16-CF-403DS (D. Utah June 22, 2017) (holding that the rule of reason applied to an alleged customer-allocation scheme that the Government had sought to prosecute criminally).

²⁴⁸ E.g., Meese, *supra* note 51, at 146.

²⁴⁹ Werden, *supra* note 96, at 754 (recognizing that restraints are sometimes justified where “they make the market *work better*” (emphasis added)).

recognize this fundamental point that makes *Professional Engineers* an aberrational “conundrum”,²⁵⁰ rather than the Court’s “most elucidating”²⁵¹ rule-of-reason opinion.

Even assuming *arguendo* that Congress intended some ill-defined conception of “competition” to serve as the overarching goal of the antitrust laws, the decision rules for promoting that goal may—and, in fact, must—nonetheless comprise something other than competition itself. Some standard is needed in order to distinguish between reasonable and unreasonable restraints. The “wonderfully ill-defined”²⁵² competitive-process approach fails to do so. Instead, it leaves courts either without sufficient guidance (imposing haphazard error costs), or prone to excessive false positives (imposing unwarranted, systematic error costs on defendants and, by extension, society at large).

B. Type of Effect: False Negatives, False Positives, and Unfocused Analyses

The type-of-effect approach fares no better. In addition to being out-of-step doctrinally, it yields incorrect outcomes in at least three ways. The first yields excessive false positives. The second produces excessive false negatives. The third creates confusion, which tends to increase the likelihood of both types of error.

First, the type-of-effect approach will cause analysts to mistakenly reject justifications that should be recognized as valid, causing false-positive errors. Some justifications can be welfare-enhancing and efficient, yet nonetheless cause a type of effect that is not included on the usual checklists.

A given restraint may, for example, alleviate a behavioral market failure caused by irrational overconsumption, thereby reducing output of the relevant product. Suppose that an organization made up of higher-educational institutions is tasked with overseeing its members’ accreditation status. Suppose further that member schools face mandatory public disclosure of all information relevant to prospective students’ cost-benefit analyses (tuition, employment rates, debt load, and the like). Nonetheless, a subset of students irrationally choose to attend a subpar institution that offers little hope of employment in exchange for a six-figure price tag.²⁵³ Eventually, the accrediting organization strips the subpar school of its accreditation, effectively foreclosing that competitor from the market. This conduct, which could be viewed as

²⁵⁰ SULLIVAN ET AL., *supra* note 4, § 5.3f, at 223.

²⁵¹ Werden, *supra* note 96, at 732.

²⁵² Hammer, *supra* note 5, at 850 n.3.

²⁵³ Some argue that (some) law schools fit this description. See, e.g., Michael Simkovic & Frank McIntyre, *The Economic Value of a Law Degree* 1 (Harv. L. Sch. Ctr. on the Legal Profession, Research Paper No. 2013-6, 2013), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2250585 (“Legal academics and journalists have marshaled statistics purporting to show that enrolling in law school is irrational.”). Behavioral-economics research on consumers’ intertemporal irrationality could offer a ready explanation for such behavior. Ted O’Donoghue & Matthew Rabin, *Doing It Now or Later*, 89 AM. ECON. REV. 103, 103 (1999).

a horizontal agreement in restraint of trade, would likely reduce output of the relevant product. Such conduct could invite—indeed, has invited—antitrust litigation.²⁵⁴

Or take, for example, the U.S. chemical industry’s “Responsible Care” initiative.²⁵⁵ Under this initiative, members of a trade association agree to, *inter alia*, reduce environmental pollution,²⁵⁶ an externality that causes market failure.²⁵⁷ Such efforts almost certainly decrease output, yet they are not condemned—in fact, the U.S. government actively encourages them.²⁵⁸

An analyst employing the type-of-effect approach would likely condemn the restraints in both cases. Both restraints lower output, a prototypical “anticompetitive effect”.²⁵⁹ But, in light of the doctrinal analysis above, both restraints should be validated: they alleviate market failures, increasing welfare.²⁶⁰ The first alleviates a market failure resulting from irrational behavior; the second alleviates a market failure resulting from externalized costs. As to such restraints, the type-of-effect approach would likely produce excessive false positives, thereby harming those whom the antitrust laws are supposed to protect.

Second, the type-of-effect approach may lead courts to credit justifications that should be rejected, causing false-negative errors. By inviting an over-simplified version of justification analysis, the type-of-effect approach can cause courts to skip over crucial steps and wrongly credit sham justifications. In *SCFC ILC, Inc. v. Visa*, for example, the Tenth Circuit incorrectly credited a defendant’s proffered “free riding” justification.²⁶¹ Visa USA, then a horizontal association of banks that issued credit cards, excluded Sears (which issued the competing Discover card) from issuing Visa credit cards.²⁶² The Tenth Circuit’s opinion carries throughout the hallmarks of the type-of-effect approach: it described *BMI*, for example, as crediting “the efficiency justification of increasing . . . aggregate output.”²⁶³

²⁵⁴ *Cf., e.g.*, *Mass. Sch. of Law v. ABA*, 846 F. Supp. 374 (E.D. Pa. 1994) (dismissing in part a complaint by an unaccredited law school against the American Bar Association [“ABA”], the primary accreditation body for U.S. law schools, alleging that several ABA accreditation standards were anticompetitive). On this topic generally, see Lao, *supra* note 5.

²⁵⁵ AM. CHEM. COUNCIL, *Responsible Care*, <https://responsiblecare.americanchemistry.com/>; *see also* Keith Brouhle et al., “The Use of Voluntary Approaches for Environmental Policymaking in the U.S.”, Nat’l Ctr. for Env’tl Econ., Working Paper # 04-05 (2004), https://www.epa.gov/sites/production/files/2014-12/documents/the_use_of_voluntary_approaches_for_environmental_policymaking.pdf.

²⁵⁶ AM. CHEM. COUNCIL, *supra* note 303.

²⁵⁷ *See, e.g.*, Boris N. Mamlyuk, *Analyzing the Polluter Pays Principle Through Law and Economics*, 18 SE. ENVTL. L.J. 39 (2010).

²⁵⁸ Brouhle et al., *supra* note 303.

²⁵⁹ *See* BORK, *supra* note __, at 122 (“The task of antitrust is to identify and prohibit those forms of behavior whose net effect is output restricting . . .”).

²⁶⁰ *See supra* Part __.

²⁶¹ *SCFC ILC, Inc. v. Visa USA, Inc.*, 36 F.3d 958 (10th Cir. 1994).

²⁶² Visa also excluded bank issuers that issued American Express cards. *Id.* at 961.

²⁶³ *Id.* at 964.

And it was the type-of-effect approach that ultimately led the *SCFC* court to wrongly credit Visa’s argument that its restraint prevented Sears from “free riding”. It was entirely unclear how the restraint could have done so—or even upon what, exactly, Sears could have taken a free ride.²⁶⁴ The court simply accepted Visa’s invocation of “preventing free riding” as a sort of shibboleth.²⁶⁵ Following the type-of-effect approach, the court reasoned as follows: (1) “concern[] about free-riding” is one of the type of effects that justify anticompetitive restraints; (2) Visa argued that its restraint prevented free riding; (3) as a result, the restraint was justified. A few years later, the government sued to enjoin Visa’s exclusionary restraint. In a more rigorous decision that was upheld by the Second Circuit, the district court rejected Visa’s proffered justification,²⁶⁶ reinforcing the conclusion that the *SCFC* was incorrectly decided.

Similarly, in *Brown University*, the court wrongly credited a justification based on the type of effect alleged—“higher quality”—where it was unclear why an unrestrained market would have failed to optimize quality.²⁶⁷ The Third Circuit credited the defense that the challenged restraint improved product quality by promoting diversity. Adopting the simplistic type-of-effect approach, the court reasoned simply that “higher quality” was a “procompetitive virtue” and blessed the restraint accordingly.²⁶⁸ But what was the market failure? And why was the restraint needed? If students behave rationally, they are presumably willing to pay higher prices in exchange for a higher-quality product, thereby covering any additional costs of increasing diversity.²⁶⁹ Alternatively, if students irrationally prefer a suboptimal education, a horizontal restraint is not needed to correct that irrationality. Unless the Ivy League schools were operating on shoestring budgets that reflected hyper-efficient business models (an unlikely proposition²⁷⁰), an individual school could simply reallocate internal funds toward increasing diversity.²⁷¹

Third, the type-of-effect approach can introduce unnecessary confusion into antitrust doctrine, increasing the likelihood of both types of error. If assembling a proper checklist of “procompetitive benefits” is the starting point, cases like *Professional Engineers* become difficult—if not impossible—to synthesize. Indeed,

²⁶⁴ AREEDA & HOVENKAMP, *supra* note 1, at ¶ 2223b & nn. 3–4.

²⁶⁵ See generally Oliver E. Williamson, *Why Law, Economics, and Organization?*, 1 ANN. REV. L. & SOC. SCI. 369, 383 (2005) (“Finally, unspecific free-rider claims are too often used as a shibboleth.”).

²⁶⁶ *United States v. Visa USA*, 63 F. Supp. 2d 322 (S.D.N.Y. 2001), *aff’d*, 344 F.3d 229 (2d Cir. 2003).

²⁶⁷ *United States v. Brown Univ.*, 5 F.3d 658 (3d Cir. 1997).

²⁶⁸ *Id.* at 674.

²⁶⁹ To be clear, this discussion is not meant to suggest that diversity does not actually improve education quality, a position that is descriptively (and, in the author’s view, morally) untenable. See, e.g., Katherine W. Phillips, *How Diversity Makes Us Smarter*, SCI. AM., <https://www.scientificamerican.com/article/how-diversity-makes-us-smarter/>.

²⁷⁰ See Carlson & Shepherd, *supra* note 330.

²⁷¹ One could imagine a “death spiral” argument in response, but the defendant did not prove anything of the sort—as the court noted, “MIT has vast resources” including an “operating budget of \$1.1 billion and an endowment of \$1.5 billion”. 5 F.3d at 661. The endowment has since grown to \$14.8 billion. MIT NEWS, *MIT Releases Endowment Figures for 2017* (Sept. 8, 2017), <http://news.mit.edu/2017/endowment-figures-2017-0908>.

some analysts present the case as a “conundrum”.²⁷² On one hand, the Court seemed to suggest that “enhanced public safety and increased quality . . . [a]re not the sort of virtues courts should consider.”²⁷³ On the other, however, such claims—particularly those involving higher quality—have repeatedly met with approval from subsequent courts. The Supreme Court itself extolled higher quality as a virtue in *Leegin*.²⁷⁴ Since different market-failure correctives can push output, quality, etc. in different directions, the type-of-effects approach creates unnecessary—indeed, intractable—confusion over which types are valid.

This mischief can be seen at play in *Law v. NCAA*, discussed above.²⁷⁵ The Tenth Circuit’s checklist of valid justifications included “creating operating efficiencies.”²⁷⁶ Yet the same opinion also identified “cost savings” as a categorically *invalid* justification.²⁷⁷ One wonders: what are “operating efficiencies” if not a type of “cost savings”? Other courts have used the terms interchangeably.²⁷⁸ And guidelines jointly issued by the DOJ and FTC explicitly contemplate “cost savings” as a *valid* justification.²⁷⁹ What is a court to make of this mess? Is “cost savings” on the valid checklist? The invalid blacklist? Both?

To further illustrate the confusion caused by this approach, consider the nearly nonsensical analysis in *New York v. Anheuser-Busch*, a case involving exclusive territorial restrictions imposed by a large liquor manufacturer on its wholesalers.²⁸⁰ By way of justification, the manufacturer identified several types of “procompetitive effects”, including increased wholesaler investments in “cosmetics”.²⁸¹ The plaintiff argued in response that cosmetic features like “uniforms and newly painted trucks are not procompetitive.”²⁸² But precedent offered no guidance as to whether those were, in fact, a valid type of “procompetitive effect”. As a result, the court was left to conjecture (citing no authority) that “given a choice people buy a clean or smartly dressed or groomed product ahead of one that presents a dirty or disheveled

²⁷² SULLIVAN ET AL., *supra* note 4, § 5.3f, at 223.

²⁷³ Meese, *supra* note 83, at 1788 (“Simply put, the supposed benefits of the restriction on price competition—enhanced public safety and increased quality—were not the sort of virtues courts should consider when conducting a rule of reason analysis.”); *see also* SULLIVAN ET AL., *supra* note 4, § 5.3f, at 223 (associating *Professional Engineers* with the proposition that “public health and welfare cannot be counted as independent benefit categories.”). Later in the same article, Meese urges a reading that aligns with the present one: “[W]hen read properly, *Professional Engineers* allows defendants to escape per se condemnation by adducing a plausible argument that, absent the restriction, one or more departures from the assumptions of perfect competition would lead unbridled rivalry to produce a market failure.” *Id.* at 1790–91.

²⁷⁴ *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 891–92 (2007).

²⁷⁵ *See supra* notes ___ and accompanying text.

²⁷⁶ 134 F.3d 1010, 1023 (10th Cir. 1998).

²⁷⁷ *Id.* (“[M]ere profitability or cost savings have not qualified as a defense under the antitrust laws.”).

²⁷⁸ *E.g.*, *United States v. LTV Corp.*, No. 84-884, 1984 WL 21973, at *10 (D.D.C. Aug. 2, 1984).

²⁷⁹ U.S. DOJ & FTC, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE 20, 21, 80, 97, 123, 134 (1996).

²⁸⁰ *New York v. Anheuser-Busch, Inc.*, 811 F. Supp. 848 (E.D.N.Y. 1993).

²⁸¹ *Id.* at 876.

²⁸² *Id.*

appearance.”²⁸³ While that observation may generally be accurate, it was a non sequitur: it gave no explanation of why the unrestrained market would have failed to optimize product quality or how the restraint could have alleviated such a failure. Nonetheless, the justification was held to be valid.²⁸⁴ Such unfocused “analysis” speaks for itself. An antitrust enterprise concerned with minimizing error costs cannot use the type-of-effect approach as the linchpin of justification analysis.

C. The Market-Failure Approach Minimizes Errors

In addition to the doctrinal superiority of the market-failure approach, it also offers consequentialist advantages over other approaches. The modern antitrust enterprise generally seeks to minimize error costs.²⁸⁵ An explicitly market-failure-based approach is best-suited to do so. It is more likely to avoid false positives than the competitive-process approach, and more likely to prevent false negatives than the type-of-effect approach.

As to the former, one need look no further than the Supreme Court’s Modern Era jurisprudence to find the market-failure approach being used to correctly reject challenges to beneficial restraints. The competitive-process approach may well have condemned the joint license in *BMI*, for example—which, after all, involved horizontal price-fixing. At least assuming that the goal of antitrust relates to promoting consumer welfare, such a decision would have constituted an obvious false positive. The *BMI* Court’s market-failure approach avoided that undesirable outcome.

As to the latter, consider again *SCFC*. That court could have avoided its erroneous decision by employing the more rigorous market-failure approach. “Free riding” occurs due to a particular type of market failure: the presence of positive externalities.²⁸⁶ With that in mind, the court first should have pointedly asked whether Visa’s business model created positive externalities upon which Sears could have taken a free ride. Since that does not appear to have been the case, the inquiry could (and should) have ended at this point.²⁸⁷

²⁸³ *Id.* at 877.

²⁸⁴ *Id.* The court need not have reached this result, since it also found that the defendant lacked market power. See *Carrier*, *supra* note 2, at 1276.

²⁸⁵ See generally Easterbrook, *supra* note 5. For a trenchant critique of error-cost analysis as currently employed by the antitrust orthodoxy, see Jonathan B. Baker, *Taking the Error Out of “Error Cost” Analysis: What’s Wrong with Antitrust’s Right*, 80 ANTITRUST L.J. 1 (2015).

²⁸⁶ See, e.g., Tyler Cowen, *Public Goods and Externalities*, CONCISE ENCYCLOPEDIA OF ECONOMICS, <http://www.econlib.org/library/Enc1/PublicGoodsandExternalities.html> (“[T]he free-rider problem and positive externalities are two sides of the same coin.”).

²⁸⁷ Some courts and scholars suggest that free riding on point-of-sale services occurs rarely in practice. See, e.g., *Graphic Prods. Distr., Inc. v. Itek Corp.*, 717 F.2d 1560, 1576 (11th Cir. 1983); William S. Stewart & Barry S. Roberts, *Viability of the Antitrust Per Se Illegality Rule: Schwinn Down, How Many to Go?*, 58 WASH. U. L.Q. 727, 756 (1980) (“Frequently point-of-sale services are unnecessary and the ‘free-rider’ problem does not actually exist.”).

The *Anheuser-Busch* analysis could similarly have been improved. There, the supposed procompetitive justifications invoked free-rider problems.²⁸⁸ Wholesalers allegedly needed exclusive territories to prevent rivals from free-riding on their investments.²⁸⁹ But do wholesalers' investments in fresh paint for their delivery trucks create any positive externalities upon which rivals could take a free ride? Of course not. By the time a delivery truck arrives, the purchasing decision has already been made. Unlike (for example) a storefront retailer's investment in a knowledgeable sales staff, fresh paint for delivery trucks does not create any potential externalities. There was no free ride to be had. By prompting such questions, the market-failure approach could have prevented the *Anheuser-Busch* court from crediting a sham justification.²⁹⁰

U.S. courts, as core institutional members of a deep-seated liberal tradition, tend naturally to be skeptical of claims that markets do not work.²⁹¹ By focusing the justification inquiry on whether the challenged restraint actually alleviated a failure of the relevant market, the market-failure approach is likely to prompt a more searching analysis. The relatively simple type-of-effect approach, on the other hand, carries danger as well as allure: it may entice courts into crediting hollow arguments that simply recite a "correct" effect.

In addition to these means of minimizing systematic error costs, the market-failure approach also offers greater clarity vis-à-vis the "conundrum" described above.²⁹² Cases like *Professional Engineers* are more helpfully understood as reactions to the type of market failure involved, rather than the type of effect alleged.²⁹³ More specifically, it was likely hostility to the concept of "behavioral market failure," and not to claims of increased quality or public safety, that motivated Stevens's biting rhetoric in *Professional Engineers*.²⁹⁴ Regardless, the proper question is not—contrary to the framing employed by some scholars—whether "higher quality" *per se* is procompetitive. That inquiry leads nowhere; authority can be found to support either proposition. Instead, the proper question is whether the challenged restraint alleviated a market failure.

Moreover, the market-failure approach refocuses antitrust on its *raison d'être*: consumer welfare. The type-of-effect approach, in particular, has yielded—and was perhaps born out of—an unhealthy obsession with output.²⁹⁵ While output effects can

²⁸⁸ 811 F. Supp., at 855–56.

²⁸⁹ *Id.*

²⁹⁰ See *infra* notes ___ and accompanying text.

²⁹¹ See, e.g., Frank H. Easterbrook, *Workable Antitrust Policy*, 84 MICH. L. REV. 1696, 1701 (1986) (advocating an antitrust program that is "profoundly . . . skeptical of the ability of courts to make things better even with the best data").

²⁹² See SULLIVAN ET AL., *supra* note 4, § 5.3f, at 223..

²⁹³ See John M. Newman, "Rationalizing Procompetitive Justifications" (unpublished manuscript, on file with author) (arguing that *Professional Engineers* was, at least in part, a reaction to the defendant's claim that its restraint was necessary to prevent consumers from irrationally purchasing shoddy services).

²⁹⁴ See *id.*

²⁹⁵ BORK, *supra* note ___, at 122 ("The task of antitrust is to identify and prohibit those forms of behavior whose net effect is output restricting and hence detrimental."); cf. Barak Y. Orbach, *The Antitrust*

be useful as a diagnostic tool, they are not, nor should they be, the entirety of antitrust analysis. Externalities,²⁹⁶ overconsumption,²⁹⁷ deception,²⁹⁸ coercion²⁹⁹—all can increase output, yet decrease efficiency and harm consumer welfare. A challenged restraint that forbids deception may, for example, decrease consumption and output of a shoddy product. Such restraints should not be condemned under the antitrust laws based on their output effects alone.³⁰⁰

V. EXPANDED RULE-OF-REASON FRAMEWORK

Refocusing the procompetitive-justifications inquiry on market failure brings to light important questions that should be incorporated into the modern rule-of-reason framework. The basic framework, though exceedingly defendant-friendly in practice,³⁰¹ does offer an appealing structure for analysis. As currently implemented, however, it often lacks sufficient rigor at the procompetitive-justifications stage.

A. Theory: Situating the Market-Failure Approach

As an initial matter, it is not enough to ask—as too many courts have—simply whether the defendant has offered some procompetitive justification for its conduct. That question, standing alone, is overly broad and has yielded doctrinal confusion and unfocused decision-making.³⁰² Such an approach unnecessarily yields false negatives. Anticompetitive conduct goes unremedied where courts treat empty claims of, for example, “preventing free-riding” as a shibboleth indicating pro-consumer behavior.³⁰³

Parties cannot simply claim, without more, that the market was subject to “some” failure. Identification of a specific failure is required. Thus, for example, a defendant can point to the presence of transaction costs as the starting point for a valid procompetitive justification.³⁰⁴ Furthermore, lest the inquiry accidentally devolve into a type-of-effect analysis, defendants must demonstrate with specificity the *particular* transaction costs that—absent the restraint—yielded a market failure. A vague claim

Consumer Welfare Paradox, 7 J. COMPETITION L. & ECON. 133, 153 (2010) (“[A]ntitrust laws appear to welcome low prices regardless of the actual impact on consumer welfare.”).

²⁹⁶ See *supra* notes __ and accompanying text.

²⁹⁷ See *e.g.*, John M. Newman, *Copyright Freeconomics*, 66 VAND. L. REV. 1409, 1446 (2013) (discussing overconsumption and hoarding behaviors in the context of “free” digital-media products).

²⁹⁸ Patterson, *supra* note __.

²⁹⁹ *Id.*

³⁰⁰ *Cf.*, *e.g.*, *id.* (identifying cases condemning deceptive conduct as violative of the antitrust laws).

³⁰¹ Michael A. Carrier, *The Rule of Reason: An Empirical Update for the 21st Century*, 16 GEO. MASON L. REV. 827, 830 (2009) (observing that, during the decade stretching from 1999 to 2009, defendants won 221 of 222 rule-of-reason cases, a 99.5% win rate).

³⁰² Perhaps as a result, it gave rise to the oversimplified and misdirected type-of-effect approach discussed above. See *supra* Part __.

³⁰³ See, *e.g.*, Hovenkamp, *supra* note 200 (“For challenges to horizontal restraints, the need to control free riding is an often asserted but greatly overused defense.”).

³⁰⁴ See, *e.g.*, *BMI v. CBS, Inc.*, 441 U.S. 1 (1979).

of “transaction costs” alone is not enough. Cases like *BMI* are illustrative: the defendant did not merely claim a “market failure” or even “transaction costs”; instead, it persuasively demonstrated that the vast number of sellers and buyers in the market meant the costs of transacting were prohibitively high relative to the value of the rights at issue.³⁰⁵

Instead, the proper initial inquiry is whether the defendant has sufficiently alleged or proven (depending on the stage of litigation) that the relevant market was failing or would have failed³⁰⁶ absent the restraint. Framing the question in this way is, of course, more appropriate to the task at hand.³⁰⁷ It also has the salutary side effect of helping courts and enforcers to view claimed procompetitive justifications with a degree of suspicion more appropriate in a liberal society that assumes markets usually work.³⁰⁸ Moreover, it will help analysts avoid the essentially intractable commensurability problems presented by non-welfare justifications.³⁰⁹ Conduct that is truly noncommercial should not be subject to rule-of-reason analysis, as it falls outside the scope of the antitrust laws.³¹⁰ If a defendant offers plausible explanations for its conduct that are unrelated to an economic welfare, analysts should decide whether its conduct was, in fact, noncommercial and therefore immune from antitrust liability. If a defendant’s explanations are welfare-related, but there is no suggestion of actual market failure, the justifications can be rejected without further inquiry.

The next question involves the connection between the identified market failure and the challenged restraint: does the restraint actually alleviate the failure? Evidence of intent may be relevant, but the focus is on effect.³¹¹ Though the defendant need not show that the restraint entirely cured the relevant market failure, some alleviation is required.

It is sometimes said that, if a defendant “asserts” a procompetitive justification, the burden shifts back to the plaintiff to “rebut that claim”.³¹² This is misleading at best. Merely “asserting” a justification is, of course, not enough—just as a plaintiff’s mere “assertion” of an anticompetitive effect is not enough.³¹³

³⁰⁵ Brief for Petitioners at 23, *id.* (“[T]he transaction costs in obtaining rights to individual songs are prohibitively high in relation to the value of the rights.”).

³⁰⁶ *Cf.* Brief of Respondent at 26, *FTC v. Ind. Fed’n of Dentists*, 476 U.S. 446 (1985) (“Hopefully, a body count will not be required before health care concerns are considered in a proper rule of reason analysis.”).

³⁰⁷ *See supra* Part III.C (outlining the doctrinal case for market failure as the sole touchstone for rule-of-reason analysis).

³⁰⁸ *See supra* notes __ and accompanying text.

³⁰⁹ *See supra* Part III.D (discussing non-welfare justifications).

³¹⁰ *See supra* notes __ and accompanying text (summarizing authorities suggesting that noncommercial activity is generally immune from antitrust liability).

³¹¹ *AREEDA & HOVENKAMP, supra* note 1, at ¶ 1506.

³¹² *Cf., e.g., United States v. Microsoft Corp.*, 253 F.3d 34, 59 (D.C. Cir. 2001) (Sherman Act § 2).

³¹³ *See, e.g., Hovenkamp, supra* note 200, at 25 (“[T]he defendant has the burden of proving a justification for its restraint.”); *Carrier, supra* note 2, at 1268 (“If the plaintiff can demonstrate an anticompetitive effect, the burden shifts to the defendant to demonstrate a legitimate procompetitive justification for the restraint.”); *cf. also, e.g., 253 F.3d* at 58–59 (“[T]he plaintiff, on whom the burden

Moreover, the use of the term “rebut” in this context is unhelpful. To be sure, a procompetitive justification can be “rebutted” in some sense: by the existence of a less-restrictive alternative (“LRA”).³¹⁴ (In some jurisdictions, plaintiffs must proffer an LRA in response to a defendant’s successfully demonstrating a justification; in others, defendants must prove that no LRA was available.³¹⁵) But the term “rebut” is vague enough to permit an incorrect understanding, namely, that a defendant satisfies its initial burden by simply claiming *some* justification for its restraint. Under this mistaken view, the burden then shifts back to the plaintiff to prove that the restraint does not actually alleviate a market failure—no matter how vacuous the defendant’s claim might be. A rule of reason structured in such a one-sided manner would undoubtedly entail substantial error costs. Instead, it is incumbent on a defendant to prove that its restraint *actually* alleviated a market failure.

As we have seen, valid procompetitive justifications often entail increasing, but sometimes decreasing, demand for (and output of) the relevant product.³¹⁶ Claimed justifications that decrease demand/output of the defendant’s own product are particularly suspect, for self-apparent reasons. That being said, such justifications are more likely—though certainly not always³¹⁷—valid where the defendant is a nonprofit entity,³¹⁸ or where the defendants comprise a majority of nonprofit entities.³¹⁹

of proof of course rests . . . must demonstrate that the monopolist’s conduct indeed has the requisite anticompetitive effect.”);

³¹⁴ For thoughtful discussions of the LRA inquiry, see HERBERT HOVENKAMP ET AL., *IP AND ANTITRUST: AN ANALYSIS OF ANTITRUST PRINCIPLES APPLIED TO INTELLECTUAL PROPERTY LAW* § 30.03(B) (3d ed.) (2017) (arguing that neither party should bear alone the burden of proving a LRA, but instead that plaintiffs may proffer an LRA and that defendants are allowed to show that the proffered LRA “will not work or is in fact not less restrictive”); Hemphill, *supra* note 54 (arguing that courts should not insist on “dominant” LRAs, i.e., LRAs that are as effective as the challenged restraint at alleviating the relevant market failure).

³¹⁵ Hemphill, *supra* note 54, at 979–80 & n. 257 (citing cases).

³¹⁶ See *supra* notes __ and accompanying text.

³¹⁷ See, e.g., *United States v. N.D. Hosp. Assoc.*, 640 F. Supp. 1028 (D.N.D. 1986) (striking down a horizontal agreement among nonprofit, charitable institutions).

³¹⁸ As to nonprofits, the general consensus view appears to echo by Judge Posner’s observation in *Hospital Corporation of America*, affirming the FTC’s decision to block a hospital merger: “The adoption of the nonprofit form does not change human nature” *Hosp. Corp. of Am. v. FTC*, 807 F.2d 1381, 1390 (7th Cir. 1986). Such institutions are still, by and large, presumed to be rational and profit-maximizing. *Cf. id.* at 1390–91; *United States v. N.D. Hosp. Assoc.*, 640 F. Supp. 1028 (D.N.D. 1986) (striking down a horizontal agreement among nonprofit, charitable institutions). *But see* *FTC v. Butterworth Health Corp.*, 946 F. Supp. 1285, 1296–97 (1996) (relying, in the context of an FTC challenge to a proposed hospital merger, on the nonprofit status—and attendant nonstandard incentives—of both merging parties to conclude that harm to competition was unlikely).

³¹⁹ *Cf. N.C. St. Bd. of Dental Examiners v. FTC*, 135 S. Ct. 1101 (2015) (holding that a state licensing board comprising a majority of active market participants did not receive state-action immunity from antitrust liability).

With these principles in mind, the proper rule-of-reason inquiry is structured as follows:

1. First, the plaintiff must adequately allege or prove either an actual anticompetitive effect or a “potential” or “likely” anticompetitive effect (which requires demonstrating market power).
2. Second, if the plaintiff does so, the defendant must adequately demonstrate a procompetitive justification.
 - a. This requires first identifying the specific market failure and adequately showing that the relevant market is, in fact, subject to such a failure.
 - b. Next, the defendant must show that the challenged restraint actually alleviates the relevant market failure. If that entails lowering output of the defendant’s own product, the court should view the proffered justification with particular suspicion. Nonprofit status may ameliorate that suspicion to some degree, but is not dispositive.
3. Third, the plaintiff may proffer—though it need not prove—the availability of an LRA. If the plaintiff does so, the defendant must respond by showing that that proposal either will not work or is not actually less restrictive. (Alternatively, in some jurisdictions, the defendant must prove that no LRA was available.)
4. Fourth, the court will, if necessary, balance the anticompetitive effects of the challenged restraint against its beneficial alleviation of a market failure.

By making explicit the multiple steps required by the market-failure approach, this expanded framework can assist courts in minimizing errors. It will also have the beneficial side effect of introducing greater transparency and clarity into judicial decision-making, a particularly important and noble goal in what is effectively a common-law discipline.³²⁰

B. Practice: Increasing Rigor, Improving Outcomes

The expanded rule-of-reason framework identified above can facilitate rigorous judicial decisionmaking, thereby minimizing error costs and maximizing

³²⁰ See, e.g., AREEDA & HOVENKAMP, *supra* note 1, at ¶ 1500 (“By exposing their reasoning, judges and commentators are subjected to others’ critical analyses, which in turn can lead to better understanding for the future.”).

consumer welfare. But it is one thing to suggest, as did Part IV,³²¹ that the market-failure approach could do so in theory. A skeptic might well ask whether it can do so in practice.

At least one modern court has engaged in an exemplary, expanded rule-of-reason analysis of the type contemplated herein. In *United States v. American Express Co.*³²² the district court was presented with two proffered justifications, both relating to the “free rider” concept that has misled other courts on multiple occasions.³²³ Neither justification was, on its face, an obvious candidate for rejection—but both justifications were, in fact, baseless. Employing a rigorous market-failure approach, the *American Express* district court reached the correct decision on both counts and rejected the defendant’s proffered justifications.³²⁴

At issue were a credit-card network’s contractual restraints that prevented merchant customers from, among other things, communicating (truthful) information about costs to their clientele.³²⁵ The first justification proffered by American Express was that its merchant restraints were necessary to preserve its “differentiated” business model, which depended on extracting high fees from its merchant customers.³²⁶ The court described at length American Express’s various complex arguments in favor of this justification, noting that they were “perhaps intuitively appealing.”³²⁷ But, as the court pointed out, “assuming American Express actually offers premium value to its merchants, the market will tolerate . . . a premium price for its network services.”³²⁸

In short, despite American Express’s substantial efforts to inject factual and legal complexity into the litigation, it simply failed to identify a market failure. Its arguments, boiled down to their essence, were—as the district court recognized—similar to the NCAA’s argument in *Board of Regents* that restricting televised-game coverage was necessary to protect live-game attendance.³²⁹ As the U.S. Supreme Court recognized in *Board of Regents*, a defendant cannot escape liability by arguing that its product is “insufficiently attractive to consumers” and therefore needs to be insulated from competition.³³⁰ Declining sales of an unattractive product does not represent a market failure that can be procompetitively alleviated by a restraint of trade. In fact, the opposite is true: a restraint that artificially props up demand for an

³²¹ See Part IV, *supra* (demonstrating that the market-failure approach minimizes error costs relative to other leading approaches).

³²² 88 F. Supp. 3d 143 (E.D.N.Y. 2015), *rev’d on other grounds*, 838 F.3d 179 (2d Cir. 2016).

³²³ See, e.g., sources cited *supra* note ____.

³²⁴ 88 F. Supp. at ____.

³²⁵ *Id.* at 165.

³²⁶ *Id.* at 225. The relevant market(s), however defined, in which credit-card networks operate appear to be less than perfectly competitive by a wide margin. See, e.g., Rory Van Loo, *Making Innovation More Competitive: The Case of Fintech*, 65 UCLA L. REV. (forthcoming 2017) (manuscript at 14–15) (drawing on natural experiments to argue that credit-card markets exhibit “insufficient competition”).

³²⁷ *Id.* at 227.

³²⁸ *Id.* at 233.

³²⁹ *Id.* at 228 (citing *NCAA v. Bd. of Regents of Univ. of Okla.*, 468 U.S. 86, 116–17 (1984)).

³³⁰ 468 U.S. at 117 (“[P]etitioner forwards a justification that is inconsistent with the basic policy of the Sherman Act.”).

unattractive product is *ipso facto* anticompetitive—it *causes* a market failure.³³¹ In other words, American Express was essentially arguing the Government’s case rather than its own. Because American Express failed even to identify a relevant market failure, let alone demonstrate that the relevant market was subject to that failure, the court’s analysis ended at this point.³³² The first proffered justification was properly rejected.

As modern antitrust defendants are wont to do, American Express also claimed its merchant restraints were necessary to prevent free-riding.³³³ Here, the district court began by identifying the particular market failure the defendant had asserted (a free-rider problem) and offering a sophisticated explanation of how free riding can cause a market failure “even in purely competitive markets.”³³⁴ Next, the court analyzed whether the relevant market was, in fact, subject to such a failure—in this case, whether American Express’s business strategy actually created some positive externality that merchants could have taken advantage of without paying. American Express claimed to be concerned about merchants free riding on its “useful advertising products” and “other market intelligence products”.³³⁵ But because American Express could have—and, in fact, sometimes did—charge merchants for these services, there was no such externality.³³⁶ Where the ride is not free, there is no free-rider market failure. As a result, the district court rejected the second proffered justification.³³⁷

Other courts would do well to follow this lead.³³⁸ The flexibility offered by the modern rule of reason is generally viewed as beneficial. But flexibility without guidance is chaos. By injecting much-needed rigor into rule-of-reason analyses, this framework focuses decision-making, yields more transparent opinions,³³⁹ minimizes error costs,³⁴⁰ and promotes consumer welfare. As a matter of doctrine, it both reflects and rationalizes existing precedent in this crucial area of antitrust law.

³³¹ In particular, the allocative inefficiency of such an arrangement is readily apparent, though a reduction of dynamic efficiency is also possible (and perhaps likely).

³³² 88 F. Supp. 3d.

³³³ *Id.* at 225.

³³⁴ *Id.* at 235.

³³⁵ *Id.*

³³⁶ *Id.* at 236 (“Where, as here, payment is possible, free-riding is not a problem because the ride is not free.” (quoting *Chi. Prof'l Sports Ltd. Partnership v. NBA*, 961 F.2d 667, 675 (7th Cir. 1992) (Easterbrook, J.) (internal quotation marks omitted)).

³³⁷ *Id.* at 235–36.

³³⁸ The *SCFC* court, for example, which was similarly confronted by free-rider claims in the context of credit-card markets, would likely have recognized the defendant’s justification as a sham had it used the more rigorous mode of analysis advocated herein. *See supra* notes ___ and accompanying text (demonstrating that the *SCFC* decision employed an over-simplified justification analysis and wrongly credited the defendant’s free-rider claim).

³³⁹ *See AREEDA & HOVENKAMP, supra* note ___.

³⁴⁰ *See supra* Part IV, demonstrating that the market-failure approach minimizes error costs relative to the other leading

VI. CONCLUSION

Understanding procompetitive justifications is a vital task for a modern antitrust enterprise that has come to be dominated by the rule of reason. By explicitly associating justifications with the economic conception of market failure, antitrust law can increase coherency, as well as reduce the social costs of erroneous decisions. And by implementing the more rigorous and thorough analytical framework identified herein, courts and enforcers can refocus on achieving the consensus goal of modern antitrust law: maximizing consumer welfare.