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# Antitrust Policy and Horizontal Collusion in the 21st Century

by William E. Kovacic,  
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## Introduction

For most of this century, at least since the enshrinement of the per se rule against horizontal price fixing in *United States v. Socony-Vacuum Co.*,<sup>1</sup> detecting and punishing concerted horizontal price and output restraints have formed the core of antitrust enforcement in the United States. The Department of Justice (“DOJ”) and the Federal Trade Commission (“FTC”) aggressively prosecute bid-rigging, price-fixing, and market allocation schemes.<sup>2</sup> In fact, commentators generally regard the enforcement of stringent rules against such agreements as antitrust’s most important positive contribution to the American economy.<sup>3</sup>

Three troubling phenomena attend current efforts to attack collusion and will beset future enforcement programs. One is substantial conceptual uncertainty and doctrinal confusion about how to distinguish between lawful unilateral conduct and illegal collective behavior. The definition and proof of concerted action are much litigated issues in horizontal restraints cases under Section 1 of the Sherman Act,<sup>4</sup> yet neither courts nor commentators have developed a satisfactory calculus for determining whether, without direct proof of agreement, the plaintiff has established that the defendants conspired to restrain trade.<sup>5</sup>

A second disturbing phenomenon is the apparent persistence of a significant level of covert collaboration by rivals to set prices or other vital terms of trade. For some time, business managers have known that horizontal price-fixing is illegal and punishable by severe civil and

criminal sanctions.<sup>6</sup> The per se rule against horizontal output restraints is clear, well-known, and stringently applied to violators, yet the DOJ still convenes numerous grand juries to probe price-fixing. Reports about the DOJ’s criminal inquiry into price-fixing in the food additives industry – which yielded the payment by Archer Daniels Midland of a record fine of \$100 million<sup>7</sup> – lead one to ask how many episodes of collusion go undetected?

The third phenomenon is the recognition and use of techniques for coordinating business conduct that courts are unlikely to label as “price fixing” or even characterize as concerted action. The modern economic literature has identified how firms can coordinate conduct by means that avoid an express exchange of assurances or employ tactics – such as subtle forms of signalling – that are less likely to attract an antitrust challenge.<sup>8</sup> Enforcement of the Sherman Act has inspired firms to adopt tactics that achieve roughly the same results as a conventional agreement with their rivals while operating outside Section 1’s ban on concerted action.

This Article offers a strategy for addressing these phenomena and guiding antitrust’s future treatment of horizontal collusion. The strategy has four elements. The first is to reformulate the doctrine governing the proof of agreement where the plaintiff lacks direct testimony or documents proving concerted action and, instead, relies entirely on circumstantial evidence that the defendants conspired to fix prices or restrict output.

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Such an approach would rest heavily on modern economic understandings of what cartel participants must do to coordinate their behavior.

The second element seeks to generate a larger volume of direct evidence of conspiracy. This Article proposes the use of bounties to encourage employees of cartel participants to inform government enforcement officials about episodes of collusion. A bountyhunting mechanism would help identify covert agreements and, by increasing the likelihood of detection, would discourage direct exchanges of assurances. This mechanism would also force cartel members to rely more upon less direct means for coordination which may be harder to use successfully.

The third element is to frustrate the formation and operation of cartels by altering government policies that facilitate effective collusion. Moreover, an adjustment to the processes by which public entities purchase goods and services is strongly recommended. With striking frequency, government purchasing bodies are the victims of collusive schemes to rig bids. This Article further advocates the abandonment of procurement practices that make the government more vulnerable to successful collusion by helping cartel members achieve consensus, detect cheating, and punish defectors.

The fourth element is institutional. The Article suggests that the FTC play a greater role in identifying conduct that indirectly facilitates the

coordination of pricing and output decisions without significant offsetting of competitive benefits. The FTC could perform this function by conducting hearings or economic studies. Such inquiries might suggest the appropriateness of proscribing specific conduct by issuing enforcement guidelines, initiating cases, or adopting administrative rules.

#### **I. Doctrine governing the use of circumstantial evidence to prove an illegal Section 1 agreement**

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Antitrust litigants devote much effort to determining whether the conduct in question stemmed from an agreement and, therefore, implicates Section 1's ban against collective trade restraints. A law whose reach hinges on the existence of an agreement requires courts to decide what conduct constitutes an agreement and how such an agreement may be proven in a trial.<sup>9</sup>

#### **A. Four forms of coordination**

Antitrust disputes under Section 1 of the Sherman Act present four types of coordination. In the first group of matters, the defendants expressly exchange assurances that they will follow a common course of action, and the fact of collective action emerges through documents or testimony from participants to the challenged

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arrangement. When detected by government enforcement officials, episodes of such behavior rarely result in fully litigated trials. Instead, they usually are concluded through plea agreements, civil consent orders, or damage settlements.<sup>10</sup>

Many cases present harder analytical and evidentiary issues. In a second group of matters, defendants covertly exchange express assurances, but there is no direct evidence showing that the defendants assured one another that they would act in concert. Here, the plaintiff relies on circumstantial proof to demonstrate the probability that the observed behavior resulted from a covert exchange of assurances.

In a third group of cases, the parties use indirect means to design and adopt a collective plan of action. Finding an agreement depends on the plaintiff's ability to specify the tactics that serve as surrogates for a direct exchange of assurances and to show that such tactics enabled the defendants to formulate and execute a common strategy.

In a fourth set of matters, firms coordinate their behavior simply by observing and anticipating the moves of their rivals. In some industry settings, such conduct may yield competitive effects that mimic those of an express cartel agreement. As the hazards of using an express exchange of assurances to coordinate behavior with rivals have increased, firms may rely more upon signalling and other tactics that are less likely to elicit a government inquiry (or, more remotely, criminal prosecution) and may help achieve some of the same results.

Horizontal restraints cases have featured continuing efforts to create a vocabulary that describes the continuum of evidence that plaintiffs have offered to establish concerted action. At

one end of the continuum is proof of direct evidence of an exchange of assurances, often consisting of documents or testimony recounting how the participant formed a plan of action. At the other end is unadorned proof of patterns of parallel behavior – proof that the industry defendants have pursued (simultaneously or sequentially) similar business strategies over time.<sup>11</sup>

Courts often distinguish between express and tacit agreements. These terms acknowledge differences in the types of proof used to prove concerted action. Cases speaking of express agreements usually involve direct proof that the defendants exchanged assurances that they will act in concert – such as a document embodying a collective commitment to pursue a course of conduct or testimony by which a conspirator describes how the group reached consensus. Direct documentary or testimonial evidence typically stands atop the hierarchy of proof because it gives the court greater confidence that the defendants acted in concert.

In cases that speak of tacit collusion, the plaintiff usually uses circumstantial evidence to prove an agreement. The tacit collusion label acknowledges that the proof is inferior to direct documentary or testimonial evidence of an agreement. Many cases that use this terminology find liability. The crucial policy issue in such matters is how to define the quantum of proof that will support an inference that the defendants exchanged assurances.

In some cases, courts seem to use the terms express and tacit as synonyms for collective and unilateral. In saying that behavior constitutes a tacit conspiracy, a court may be saying that, though the conduct is suspicious, the plaintiff has not introduced enough proof to permit an inference of collective action. Courts using the ter-

minology in this way ordinarily decline to find liability.

## B. Basic framework of Sherman Act agreement jurisprudence

Modern judicial efforts to define the elements of a Section 1 agreement originated in four Supreme Court decisions beginning with *Interstate Circuit, Inc. v. United States*<sup>12</sup> in 1939 and ending with *Theatre Enterprises, Inc. v. Paramount Film Distributing Corp.*<sup>13</sup> in 1954. In sustaining the conviction of movie exhibitors for fixing the prices to be charged for first-run films, the *Interstate Circuit* Court defined the concerted action requirement in these terms:

While the District Court's finding of an agreement of the distributors among themselves is supported by the evidence, we think that in the circumstances of this case such agreement for the imposition of the restrictions upon subsequent-run exhibitors was not a prerequisite to an unlawful conspiracy. It was enough that, knowing that concerted action was contemplated or invited, the distributors gave their adherence to the scheme and participated in it.<sup>14</sup>

The Court explained that "[a]cceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act."<sup>15</sup>

Seven years later, in *American Tobacco Co. v. United States*,<sup>16</sup> the Court addressed the agreement issue in reviewing conspiracy to monop-

olize charges under Section 2 of the Sherman Act. The Court stated that "[n]o formal agreement is necessary to constitute an unlawful conspiracy."<sup>17</sup> The Court explained that a finding of conspiracy is justified "[w]here the circumstances are such as to warrant a jury in finding that the conspirators had a unity of purpose or a common design and understanding, or a meeting of minds in an unlawful arrangement."<sup>18</sup>

In 1948 in *United States v. Paramount Pictures, Inc.*,<sup>19</sup> the Court reiterated *Interstate Circuit's* agreement formula. In considering Section 1 and Section 2 conspiracy claims, the Court said "[i]t is not necessary to find an express agreement in order to find a conspiracy. It is enough that a concert of action is contemplated and that the defendants conformed to the arrangement."<sup>20</sup>

The formative period of agreement decisions ended in 1954 in *Theatre Enterprises*. There the Court said "[c]ircumstantial evidence of consciously parallel behavior may have made heavy inroads into the traditional judicial attitude toward conspiracy; but 'conscious parallelism' has not read conspiracy out of the Sherman Act entirely."<sup>21</sup>

As a group, the four cases established three conceptual points of reference. First, courts would characterize as concerted action interfirm coordination realized by means other than a direct exchange of assurances. Second, courts would allow agreements to be inferred by circumstantial proof suggesting that the challenged conduct more likely than not resulted from concerted action. Third, courts would not find an agreement where the plaintiff showed only that the defendants recognized their interdependence and simply mimicked their rivals' pricing moves.

Subsequent Supreme Court decisions have tried to capture these principles in a new formula.

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In 1984, in addressing resale price maintenance conspiracy allegations in *Monsanto Co. v. Spray-Rite Service Corp.*,<sup>22</sup> the Court observed:

The correct standard is that there must be evidence that tends to exclude the possibility of independent action by the [parties]. That is, there must be direct or circumstantial evidence that reasonably tends to prove that [the parties] had a conscious commitment to a common scheme designed to achieve an unlawful objective.<sup>23</sup>

Neither the *Monsanto* standard nor its predecessor formulas provides a useful basis for identifying concerted action. These tests show that the concept of agreement encompasses more than a direct exchange of assurances, yet they offer no operational means for determining when the defendants have engaged in something more than consciously parallel conduct.

Under the *Monsanto* formula, one could deem interdependent conscious parallelism as a “conscious commitment to a common scheme.” Each firm in a tight oligopoly knows that the effect of its acts depends on the reactions of its rivals. All producers perceive that price increases will stick only if all firms raise prices. Realizing their interdependence, each firm decides, without consulting its rivals, to match competitor price increases. Repeated efforts to match rivals’ price moves arguably indicate the firm’s conscious commitment to achieve higher prices. The sole interfirm communication consists of each firm’s observation of its rivals’ price changes. By calibrating its own moves to conform with the decisions of its rivals, each firm can be said to have “consciously committed” itself to participate in a “common scheme.”

### C. Plaintiff’s burden of proof

Plaintiffs in Section 1 cases bear the burden of establishing the fact of an agreement. The “conscious commitment to a common scheme” can be shown with direct or circumstantial evidence.<sup>24</sup> As elaborated in later decisions, *Monsanto*’s articulation of the burden of proof has considerable importance where the defendant moves for summary judgment on conspiracy issues.

The fear that mistaken inferences from ambiguous evidence might deter procompetitive or benign conduct led the Supreme Court in *Matsushita Electrical Industrial Co. v. Zenith Radio Corp.*<sup>25</sup> to extend and apply *Monsanto*’s conspiracy standards to horizontal agreements. Where the plaintiff relies on circumstantial evidence to establish concerted action, *Matsushita* stated that “antitrust law limits the range of permissible inferences from ambiguous evidence in a Section 1 case” and emphasized that “conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy.”<sup>26</sup>

Quoting *Monsanto*, the *Matsushita* Court then specified the plaintiff’s burden of proof when the defendant seeks summary judgment or a directed verdict against claims when circumstantial evidence alone is introduced to establish collective action:

To survive a motion for summary judgment or for a directed verdict, a plaintiff seeking damages for a violation of Section 1 must present evidence that ‘tends to exclude the possibility’ that the alleged conspirators acted independently . . . [Plaintiffs] in this case, in other words, must show that the

inference of conspiracy is reasonable in light of the competing inferences of independent action or collusive action that could not have harmed [plaintiffs].<sup>27</sup>

As in *Monsanto*, the Court in *Matsushita* sought to reduce error costs associated with excessively broad application of liability standards.<sup>28</sup> In *Matsushita*, Japanese suppliers of electronics equipment allegedly conspired to price below cost in the United States, drive American firms from the market, and later raise prices to monopoly levels. In such a case, the Court emphasized that mistaken inferences of conspiracy could injure consumers by deterring firms from offering low prices.<sup>29</sup>

#### **D. Interdependence and the role of plus factors**

In markets characterized by interdependence, each firm realizes that the effect of its actions depends upon the response of its rivals.<sup>30</sup> In highly concentrated markets, the recognition of interdependence can lead firms to coordinate their conduct simply by observing and reacting to their competitors' moves. In some instances, such oligopolistic coordination yields parallel behavior (e.g., parallel price movements) that approaches the results that one might associate with a traditional agreement to set prices, output levels, or other conditions of trade.

The line that distinguishes tacit agreements (which are subject to Section 1 scrutiny) from mere tacit coordination stemming from oligopolistic interdependence (which eludes Section 1's reach) is indistinct. The size of the safe harbor recognized by *Theatre Enterprises*<sup>31</sup> depends on what conduct courts regard as the "ex-

tra ingredient of centralized orchestration of policy which will carry parallel action over the line into the forbidden zone of implied contract and combination."<sup>32</sup> Courts enjoy broad discretion to establish the reach of Section 1 by defining this "extra ingredient" broadly or narrowly.

Courts have relied on operational criteria known as "plus factors" to determine whether a pattern of parallel conduct results from an agreement. The chief "plus factors" have included:

- The existence of a rational motive for defendants to act in concert.
- Actions contrary to each defendant's self-interest unless pursued as part of a collective plan.
- Phenomena that can be explained rationally only as the result of concerted action, such as submitting uniform sealed bids where the uniformity could not result from common cost factors.
- The defendant's participation in past collusion-related offenses.
- Evidence that the defendants had the opportunity to communicate or actually did so.
- The use of facilitating devices such as delivered pricing or most favored nation clauses.
- Industry characteristics (product homogeneity, frequent transactions, readily observed price adjustments, high entry barriers, and high concentration) that are conducive to successful coordination.
- Industry performance data, such as extraordinary profits, that suggest successful coordination.
- The absence of a plausible, legitimate

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business rationale for suspicious conduct (such as certain communications with rivals), or the presentation of contrived rationales for certain conduct.

Two basic problems have attended judicial efforts to identify and evaluate plus factors. First, courts have failed to establish an analytical framework that explains why specific plus factors have stronger or weaker evidentiary value or presents a hierarchy of such factors. Antitrust agreement decisions rarely rank plus factors according to their probative merit or specify the minimum critical mass of plus factors that must be established to sustain an inference that conduct resulted from concerted acts rather than from conscious parallelism. Nor do courts devote much effort to evaluating the economic significance of each factor. The lack of a meaningful analytical framework makes judgments about the resolution of future cases problematic and gives an impressionistic quality to judicial decision making in agreement-related disputes.

The failure in modern cases to provide a hierarchy of plus factors and explain the competitive significance of each might be attributed to one of the less discussed but more important Supreme Court decisions of the 1960s. In *Continental Ore Co. v. Union Carbide & Carbon Corp.*,<sup>33</sup> the Court stated that “plaintiffs should be given the full benefit of their proof without tightly compartmentalizing the various factual components and wiping the slate clean after scrutiny of each.”<sup>34</sup> For lower court judges, this passage can be read to dispense with the need for a careful assessment of the importance of each element of proof and to encourage the practice of dropping difficult conceptual issues into the lap of the jury.

The variation in judicial analysis of plus factors suggests that the outcome in many agreement cases depends upon the court’s unarticulated intuition about the likely cause of observed parallel behavior. Judges appear to vary in their acceptance of the proposition in *Theatre Enterprises* that conscious parallelism does not always bespeak concerted behavior. Judges who regard pricing uniformity as a sign of collaboration will give lip service to *Theatre Enterprises* but will expand the range and reduce the quantum of conduct that, when added to parallel behavior, can support a finding of agreement. On the other hand, judges who see parallelism as a desirable, natural manifestation of rivalry are likely to display a greater reluctance to give effect to asserted plus factors and will be more sympathetic to the defendants’ explanations about why such plus factors implicate conduct that is either procompetitive or essentially benign.

The second problem results from the development of new arguments, rooted in the modern economics literature dealing with repeated games, that market performance associated with collusive schemes can result from interdependent, consciously parallel conduct in some industry settings. Firms in a number of industry settings may be able to achieve collusive outcomes without resorting to conduct that might be characterized as an agreement.<sup>35</sup> Under *Matsushita*, defendants might argue successfully that observed parallelism is as consistent with what agreement doctrine has recognized as independent action — namely, the recognition and response to interdependence — as with an inference of collusive behavior. Moreover, under *Matsushita*’s implausibility test, firms could assert that it makes no economic sense for them to



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use tactics that violate Section 1 of the Sherman Act when the recognition of interdependence can yield the same market results. Where the recognition of interdependence alone accounts for the market outcome, the difficulties in identifying and prescribing avoidable conduct are likely to preclude effective antitrust intervention.

**E. Proposed approach for establishing an agreement based on circumstantial evidence**

The refinement of federal merger enforcement policy in the past fifteen years has placed increasing reliance on economic theories that illuminate the conditions in which consolidation is likely to have net anticompetitive effects. Among other features, the DOJ/FTC 1992 Horizontal Merger Guidelines<sup>36</sup> specify how a transaction might increase the abilities of firms to coordinate their activity. The economic understanding of the process by which firms cooperate successfully guides the analysis of coordinated anticompetitive effects.

A similar, economically-oriented reformulation of agreement jurisprudence in circumstantial evidence cases would focus on the three prerequisites to successful cooperation by rivals:

- The reaching of a consensus on pricing, output, or other terms of trade;
- The detection of deviations from the agreement; and
- The punishment of firms that cheat.

A reformulated standard in circumstantial evidence cases would be organized to focus on the fulfillment of these conditions. Where the evidence of collaboration is wholly circumstantial, the plaintiff's prima facie case would consist of

introducing proof that demonstrates how the defendants achieve consensus, detect defection from the agreed course of action, and sanction cheaters. To survive a motion for summary judgment or a motion to dismiss, the plaintiff would need to provide a plausible explanation for how defendants have executed all three tasks. The defendants could rebut this prima facie case by advancing benign or procompetitive rationales for specific challenged acts, or by demonstrating that the observed market outcomes more likely than not resulted from the recognition of interdependence alone.

The most important threshold element of proof in this framework would consist of evidence showing how the defendants communicate their intentions and confirm their commitment to a proposed course of action. Perhaps the most probative proof of the mechanism for achieving consensus would consist of evidence demonstrating that a pattern of extensive communication among the defendants preceded a complex, parallel adjustment in behavior that could not readily be explained as the product of the defendants independent efforts to identify and adhere to focal points for organizing their conduct. The existence of a means for detecting cheating might be revealed by establishing a pattern of bilateral exchanges of pricing information among competitors or exchanges of data through trade associations. Such conduct might serve the purpose of identifying defections from the consensus price.

**II. Bounty hunting as a means for generating direct evidence of conspiracy**

Over the past twenty years, federal enforcement officials have pursued a number of initiatives to increase their ability to obtain direct evi-

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dence of collusion. The DOJ has resorted more frequently to investigation techniques such as wire-tapping and electronic surveillance and has broadened cooperation with other law enforcement entities and government bureaus. The DOJ also has experimented with expanded leniency and immunity programs that provide incentives for cartel participants to inform the government about episodes of collusion. Collectively, these steps have increased the likelihood that efforts by competitors to coordinate their behavior through a direct exchange of assurances would be detected, prosecuted, and penalized.

Many of these information-gathering mechanisms seek to obtain the assistance of cartel insiders. Cooperation by insiders — such as the disgruntled employee, or the cartel participant who feels betrayed by other cartel members — is a key ingredient to many successful efforts to unmask covert coordination among rivals. Efforts to entice insiders to provide information on the cartel recognizes the benefits of decentralized monitoring in enforcing antitrust commands. Decentralized monitoring schemes seek to exploit the superior access of insiders, vis-a-vis external observers such as government investigators, to information bearing upon the commission of violations of the law.

To date, antitrust enforcement has enlisted informers chiefly by offering leniency or immunity to offenders, or simply by relying on voluntary disclosures by nonculpable individuals (such as sales managers who are upset by what they

perceive to be unethical conduct). Beyond these information-gathering techniques, the antitrust system does not enlist the assistance of informers. For example, antitrust doctrine generally denies standing to employees who allege that their employers have engaged in conduct that restricts competition in product markets in which the employers sell their goods or services.<sup>37</sup>

One approach to uncovering and deterring covert coordination schemes is to give company insiders more robust incentives to provide infor-

mation to enforcement agencies. Experimentation with a bountyhunting mechanism modeled loosely on the Civil False Claims Act would serve this purpose.<sup>38</sup> Although the Civil False Claims Act bountyhunting scheme has a number of serious flaws, it properly recog-

nizes the power of decentralized monitoring to uncover violations of the law that otherwise would pass undetected or would be detected without the assistance of insiders only at a comparatively higher cost.

An antitrust bounty-hunting mechanism would pay informers a percentage of amounts ultimately recovered by the government where the informer's cooperation contributes significantly to the identification and successful prosecution of a collusion offense. Such a bounty scheme would have the following procedural elements:

- The informer's data would be presented in writing to the DOJ.
- The amount of the informer's bounty

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— ranging up to as much as 25 percent of all recovered fines and civil penalties — would be set ex post in a court hearing and would be adjusted downward where the informer has helped organize or execute the scheme.

- Informers would be protected by anti-retaliation safeguards.
- Informers could be represented by counsel, who would be entitled to the payment of reasonable attorneys fees and costs for assisting the informer.
- Defendant organizations could pursue counterclaims for contribution against informers for their participation in illegal collusion.

Experimentation with such a mechanism might run for ten years and would sunset unless reauthorized by Congress. A ten-year trial would provide a suitable time to assess the efficacy of the informing system in eliciting useful information about covert cartels. Its anticipated benefit would be to generate a larger body of direct evidence of unlawful cooperation and, thus, to avoid reliance on more problematic circumstantial proof.

### **III. Promoting entry and otherwise destabilizing coordination: the case of public procurement policy**

Bid-rigging schemes in federal, state, and local procurement programs account for a strikingly large percentage of DOJ antitrust grand jury proceedings. From 1988 through 1992, for example, approximately 40 percent of all DOJ criminal indictments challenged collusive schemes targeted at public procurement bodies.<sup>39</sup> Public purchasing authorities seem unusually

vulnerable to successful collusion. In an impressive number of instances, the challenged cartels have lasted ten years or more.

One important element of anti-collusion policy is to avoid creating conditions that facilitate successful coordination. To a large degree, government procurement policy assists firms in devising and implementing cartels. Two features of procurement policy stand out. The first consists of domestic content or local content purchasing requirements that narrow the field of potential bidders. Domestic preference commands such as the Buy American Act<sup>40</sup> stymie the destabilizing influence of entry as a discipline on cartel coordination.

The second feature is a series of procedural controls that are designed to increase the integrity of the procurement process but whose main effect is often likely to be the promotion of effective seller coordination. A major example is the process for opening bids in a sealed bid procurement. Bids ordinarily are unsealed in a public setting and are displayed for all offerors to observe.<sup>41</sup> This procedure enables cartel participants to determine whether their co-conspirators abided by the terms of their agreement to rotate bids or otherwise suppress rivalry. An obvious reform would be to permit inspection of bids by a guardian internal to the purchasing organization, such as an inspector general. This simple measure would complicate the detection of cheating by cartel members and still ensure that the winning offeror has been identified correctly.<sup>42</sup>

Amid considerable current interest in reinventing public institutions, a broad-based effort to identify public policies that reinforce collusion would be appropriate. The public procurement mechanism is a single important illustration. A fuller assessment of the causes of episodes of collusion prosecuted by the DOJ and the FTC is

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likely to reveal other respects in which public policies facilitate collusion by discouraging destabilizing entry and increasing the likelihood that deviations from cartel arrangements will be detected and punished. It would not be surprising if one found that the federal antitrust agencies often are in the position of attempting to correct behavior that stems from perverse incentives supplied by flawed public policies.

#### **IV. The role of the Federal Trade Commission**

Section 5 of the FTC Act prohibits “unfair methods of competition”<sup>43</sup> and has been interpreted to prohibit conduct that violates Section 1 of the Sherman Act. Courts also have concluded that the FTC can use Section 5 to challenge conduct that infringes the “spirit or policy” of the Sherman Act or constitutes an incipient violation of the Sherman Act.<sup>44</sup> While the existence of a “contract, combination . . . or conspiracy”<sup>45</sup> in restraint of trade must be established to prove a Section 1 violation, no such proof is necessary to establish a Section 5 violation. For this reason, Section 5 has been a continuing source of attraction to the FTC and commentators as a means of attacking facilitating practices and forms of interfirm coordination that may defy characterization as an agreement for Sherman Act purposes.

Over the years, the Commission has used several approaches to apply Section 5 against facilitating practices. Many of the Commission’s earlier cases (where the FTC enjoyed the greatest success) used Section 5 to attack agreements, either express or tacit, by competitors to implement and use facilitating practices. For example, most of the Commission’s challenges to industrywide use of basing point pricing systems and similarly delivered pricing methods have

invoked such theories.<sup>46</sup> In these cases, the conduct arguably was equally susceptible to legal challenge under Section 1 of the Sherman Act, and reliance on Section 5 was not critical to successful prosecution of the complaint.

In some agreement cases, the FTC has combined conspiracy counts with a separate allegation that the practice violates Section 5 even if undertaken as a unilateral act, with no agreement or conspiracy. Although a number of cases find a violation on such a theory, they rely significantly on the finding of an agreement.<sup>47</sup> The Commission and judicial opinions in these cases are generally unsatisfying. Beyond offering broad generalizations about the FTC’s expansive authority under Section 5, the opinions imprecisely delineate either the liability standard being applied or the type and amount of evidence needed to establish a violation.

Finally, there are a handful of cases in which the Commission has challenged a practice that allegedly fixes prices or reduces competition without attempting to show any agreement. While these cases offer the greatest potential for carving out a unique role for Section 5 in the facilitating practices area, they pose the greatest analytical challenges, and the Commission’s efforts thus far have yielded unimpressive results. To date, the only success the Commission can claim in this area is a somewhat grudging acknowledgment from reviewing courts that such a violation may be theoretically possible. Courts uniformly have declined to find liability on the evidence advanced by the Commission.<sup>48</sup>

Despite limited success in this area, the FTC remains perhaps the best vehicle for articulating standards designed to discourage anticompetitive coordination among competitors. Rather than rely exclusively or even chiefly on litigation to provide guidance, the Commission might de-

velop enforcement guidelines or use rulemaking to delineate standards of conduct.<sup>49</sup> The basis for the use of such tools might be the type of comprehensive hearings that the Commission used in 1995 to lay the foundation for new approaches to dealing with issues associated with the emergence of global markets and innovation in antitrust analysis.<sup>50</sup> A comparable exploration of collusion would be appropriate as a foundation for reformulating policies controlling agreements among competitors.

## Conclusion

Collusion is a vital concern of competition policy, yet the antitrust system has achieved only modest success in devising a satisfactory definition for the concept of concerted action and creating a suitable methodology for establishing the existence of an agreement in litigation. This ar-

ticle has suggested several approaches for improving the treatment of collusion issues in the next century. The first is to apply a more meaningful and economically rigorous approach to evaluating plus factors that are used to determine when defendants have engaged in something more than consciously parallel activity and can properly be deemed to have acted in concert. A second approach is to experiment with new techniques for generating a larger volume of "direct" evidence of illegal agreements, including the use of bounties as incentives for the revelation of information by insiders to collusive schemes. A third approach is to alter government policies – such as various features of public procurement policy – that facilitate effective collusion. A fourth approach is for the FTC to assume a larger role, through hearings, guidelines, and rulemaking, in delineating conduct standards.

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## E N D N O T E S

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<sup>1</sup> 310 U.S. 150 (1940).

<sup>2</sup> See *Report of the ABA Antitrust Law Section Task Force on the Antitrust Division of the U.S. Department of Justice*, reprinted in 58 ANTITRUST L.J. 747, 763-65 (1989); Joseph W. McAnney, *The Justice Department's Crusade Against Price-Fixing: Initiative or Reaction?*, 36 ANTITRUST BULL. 521, 523-25 (1991). The number of criminal price-fixing cases initiated by the DOJ from 1980 through 1990 exceeded the total number of such matters in the previous 90 years of experience under the Sherman Act. See also James F. Rill, *60 Minutes with James F. Rill, Assistant Attorney General, Antitrust Division, U.S. Department of Justice*, 59 ANTITRUST L.J. 45 (1990); Charles R. Rule, *60 Minutes with Charles R. Rule, Assistant Attorney General, Antitrust Division*, 57 ANTITRUST L.J. 257 (1988).

<sup>3</sup> See, e.g., ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 263 (1978) (praising the per se ban against horizontal price-fixing and market divisions and concluding that "[i]ts contributions to consumer welfare over the decades have been enormous"). Such approval is not univer-

sal. Noteworthy critiques of antitrust's per se prohibition against certain horizontal output restrictions include Almarin Phillips, *Market Structure, Organization and Performance: An Essay on Price Fixing and Combinations in Restraint of Trade* (1962); George Bittlingmayer, *Price-Fixing and the Addyston Pipe Case*, 5 RES. IN L. & ECON. 57 (1983); Harold Demsetz, *How Many Cheers for Antitrust's 100 Years?*, 30 ECON. INQUIRY 207 (1992).

<sup>4</sup> 15 U.S.C. § 1 (1994).

<sup>5</sup> See Peter C. Carstensen, *Commentary: Reflections on Hay, Clark, and the Relationship of Economic Analysis and Policy to Rules of Antitrust Law*, 1983 WISC. L. REV. 953, 962 (observing that commentators have yet to provide "a clear standard to separate unlawful collusion from permissible interdependency" and concluding that "[t]he courts have sought, with a similar lack of success, to find legal criteria to determine the existence of an unlawful combination"); William E. Kovacic, *The Identification and Proof of Horizontal Agreements Under the Antitrust Laws*, 38 ANTITRUST BULL. 5, 24-25, 35-37 (1993).

- <sup>6</sup> Since 1974, Sherman Act violations have been punishable as felonies. On several occasions in the past twenty years, Congress has strengthened the scheme of penalties and thus increased the likelihood that violators will be punished severely. See ERNEST GELLHORN & WILLIAM E. KOVACIC, *ANTITRUST LAW AND ECONOMICS IN A NUTSHELL* 451-52 (4th ed. 1994).
- <sup>7</sup> See *Grain Processor to Pay \$100 Million to Resolve Price Fixing Case*, TRADE REG. REPORTS (CCH), Issue No. 443, at 1 (Oct. 16, 1996); see also Scott Kilman, *Ajinomoto Pleads Guilty to Conspiring With ADM, Others to Fix Lysine Price*, WALL ST. J., Nov. 15, 1996, at A4 (reporting that another participant in the food additives price-fixing arrangement has agreed to pay a fine of \$10 million to settle the government's criminal charges).
- <sup>8</sup> See Jonathan B. Baker, *Two Sherman Act Section 1 Dilemmas: Parallel Pricing, the Oligopoly Problem, and Contemporary Economic Theory*, 38 ANTITRUST BULL. 143 (1993).
- <sup>9</sup> The discussion in this section is derived in part from Kovacic, *supra* note 5.
- <sup>10</sup> LOUIS B. SCHWARTZ, JOHN J. FLYNN & HARRY FIRST, *FREE ENTERPRISE AND ECONOMIC ORGANIZATION: ANTITRUST* 438 (6th ed. 1983).
- <sup>11</sup> Agreements also might be classified by how strongly the alleged conspirators commit themselves to a common scheme. The evidence of agreement may reveal unqualified support for a course of action, a receptive attitude falling short of outright approval, or an expression of interest that reserves freedom to act as one likes. See VI PHILLIP AREEDA, *ANTITRUST LAW* 63-65 (1986).
- <sup>12</sup> 306 U.S. 208 (1939).
- <sup>13</sup> 346 U.S. 537 (1954).
- <sup>14</sup> 306 U.S. at 226.
- <sup>15</sup> *Id.* at 227.
- <sup>16</sup> 328 U.S. 781 (1946).
- <sup>17</sup> *Id.* at 809.
- <sup>18</sup> *Id.* at 810.
- <sup>19</sup> 334 U.S. 131 (1948).
- <sup>20</sup> *Id.* at 142.
- <sup>21</sup> 346 U.S. at 541.
- <sup>22</sup> 465 U.S. 752 (1984).
- <sup>23</sup> *Id.* at 768.
- <sup>24</sup> See *ES Dev., Inc. v. RWM Enters.*, 939 F.2d 547, 554 (8th Cir. 1991) (“[A]n antitrust plaintiff may prove the existence of a combination or conspiracy by providing either direct or circumstantial evidence sufficient to ‘warrant a . . . finding that the conspirators had a unity of purpose or common design and understanding, or a meeting of the minds in an unlawful arrangement.’” (quoting *American Tobacco Co. v. United States*, 328 U.S. 781, 810 (1946))), *cert. denied*, 502 U.S. 1097 (1992).
- <sup>25</sup> 475 U.S. 574 (1986).
- <sup>26</sup> *Id.* at 588.
- <sup>27</sup> *Id.*
- <sup>28</sup> *Monsanto* emphasized the dangers of discouraging legitimate discussions between producers and their dealers. 465 U.S. at 763-64.
- <sup>29</sup> 475 U.S. at 593. *Matsushita*'s policy rationale may have less significance for horizontal conspiracy cases that do not involve claims of collective below-cost pricing. Horizontal agreements to raise prices or cut output pose greater competitive dangers than the concerted low pricing challenged in *Matsushita* and therefore might be subject to more liberal standards of proof.
- <sup>30</sup> See F.M. SCHERER & DAVID ROSS, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* 199 (3d ed. 1990).
- <sup>31</sup> 346 U.S. 537 (1954).
- <sup>32</sup> SCHWARTZ ET AL., *supra* note 10, at 439.
- <sup>33</sup> 370 U.S. 690 (1962).
- <sup>34</sup> *Id.* at 699. The Court added that “the duty of the jury was to look at the whole picture and not merely at the individual figures in it.” *Id.* (citing *American Tobacco Co.*, 147 F.2d at 106.)
- <sup>35</sup> See Baker, *supra* note 8 for the formative treatment of this point.
- <sup>36</sup> The 1992 Horizontal Merger Guidelines are reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104.
- <sup>37</sup> See, e.g., *Apperson v. Fleet Carrier Corp.*, 879 F.2d 1344, 1352 (6th Cir. 1989) (denying standing to employees who challenged their employer's alleged antitrust violations observing that employees could have been economic beneficiaries of the conduct), *cert. denied*, 495 U.S. 947 (1989).
- <sup>38</sup> 31 U.S.C. §§ 3729-31 (1994); see also William E. Kovacic, *Whistleblower Bounty Lawsuits as Monitoring Devices in Government Contracting*, 29 LOYOLA L.A. L. REV. 1799 (1996) (discussing False Claims Act bounty mechanism).
- <sup>39</sup> To compute this number, I treated multiple indictments arising from the same prosecution as one enforcement event.
- <sup>40</sup> 41 U.S.C. §§ 10a-10d (1994).
- <sup>41</sup> See Federal Acquisition Regulations, 48 C.F.R. § 14.401 (1996) (specifying procedures for the opening of sealed bids).
- <sup>42</sup> The bid opening process is hardly the only cartel-reinforcing feature of the public procurement process. For example, the government's structuring of bids for infant formula apparently played a central role in generating the price increases that motivated the FTC's prosecution of infant formula producers. See *American Home Prods.*, 5 Trade Reg. Rep. (CCH) ¶ 23,209 (FTC 1992).
- <sup>43</sup> 15 U.S.C. § 45(a)(1) (1994).
- <sup>44</sup> See Neil W. Averitt, *The Meaning of “Unfair Methods of Competition” in Section 5 of the Federal Trade Commission Act*, 21 B.C. L. REV. 227, 243 (1980).
- <sup>45</sup> 15 U.S.C. § 1 (1998).

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<sup>46</sup> See *e.g.*, *FTC v. Cement Instit.*, 333 U.S. 683, 720-21 (1948).

<sup>47</sup> See *e.g.*, *FTC v. Motion Picture Advertising Serv.*, 344 U.S. 392, 394-95 (1953).

<sup>48</sup> See *E.I. Du Pont de Nemours & Co. v. FTC*, 729 F.2d 128, 139 (2d Cir. 1984); *Boise Cascade Corp. v. FTC*, 637 F.2d 573, 581 (9th Cir. 1980).

<sup>49</sup> See *Baker*, *supra* note 8. See generally *DuPont*, 729 F.2d at

139 (dicta regarding the “FTC’s duty to define conditions under which price uniformity conduct would be “unfair” absent an agreement.”)

<sup>50</sup> See I Federal Trade Commission, *Anticipating the 21st Century: Competition Policy in the New High Tech, Global Marketplace*, 1996 WL 293773 (F.T.C.) Guide/Report (May 1996) (FTC staff report on results of FTC hearings).

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**A N T I T R U S T      L A W**  
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**N E W      M I L L E N N I U M**

**AN EXAMINATION OF LEADING ISSUES IN ANTITRUST  
ENFORCEMENT POLICY FOR THE APPROACHING AGE**

*The Honorable Hubert L. Will Conference*

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# **THE PROPER GOALS OF ANTITRUST: WHEN PUBLIC AND PRIVATE INTERESTS COLLIDE**

*The antitrust laws were designed to protect the free enterprise system in an age where there were few regulatory barriers and requirements. Today, we live in a world brimming with government regulation. This gap between 19th century theory and 20th century reality has generated ongoing debate over the interpretation of the antitrust laws themselves.*

## **Introduction:**

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