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Refining the *Matsushita* Standard and the Role Economics Can Play

*James Langenfeld and James Morsch**

The conference that generated the papers in this journal brought together a diverse group of academics, lawyers, and economists to celebrate and reflect on the twentieth anniversary of the Supreme Court's storied decision in *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*¹ From our perspective as the conference's moderators, two themes emerged: (1) the continued uncertainty surrounding the proper standard for evaluating evidence in a horizontal conspiracy case where the evidence of collusion is circumstantial and the market at issue oligopolistic, and (2) the crucial but limited role economists can and should play in such cases. In this short article, we briefly analyze each of these issues. We conclude that evidence of back-and-forth communications between alleged conspirators should be at least one "plus factor" used in evaluating an alleged conspiracy, and that economic analysis can provide important evidence on whether the alleged conspiracy is likely to have existed.

REFINING THE *MATSUSHITA* STANDARD

In the twenty years since the Court's decision in *Matsushita*, many courts have attempted to articulate the type of evidence needed at the summary judgment stage in an antitrust conspiracy case where no direct evidence of a collusive agreement exists. These so-called "plus factors" have generated considerable controversy but, more importantly, they are generally viewed as in need of further refinement. Professor Bill Page's substantial and thoughtful article recommends such a refinement, suggesting that courts require proof of communication between alleged conspirators in a case where there is no explicit evidence of an agreement. In general, the conference received his suggestion as an

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1. 475 U.S. 574 (1986).

interesting and innovative way to help separate illegal collusion from legal unilateral parallel actions in a concentrated industry (the “oligopoly problem”). It is, after all, difficult to imagine a successful coordination of rivals without some type of communication back and forth between the participants or, failing that, some history of collusion in the industry at issue. Even economists who have argued that proper economic analysis can provide useful evidence on the existence of an agreement have conceded the need for communications to be a part of the analysis.²

Practitioners’ reactions to Professor Page’s proposal to add competitor communications as an additional plus factor on summary judgment, not surprisingly, are likely to depend on the clients they normally represent in these types of cases. Mark McLaughlin, a defense lawyer, embraces the notion as a way of helping trial courts weed out cases that may be thick with mountains of evidence—but the quality of that evidence on the question of conspiracy is weak.³ Michael Freed, a preeminent plaintiffs’ antitrust lawyer, believes that adding a communication requirement would unfairly raise the bar and make it more difficult for many plaintiffs to survive summary judgment.⁴ What both of these commentators implicitly acknowledge is that clearer standards on summary judgment in Sherman section 1 cases are indeed needed, but that care should be taken to insure that good cases get to the jury and inherently implausible ones should be weeded out on summary judgment.

The trouble with establishing a clear standard, as we all know from practical experience, is that much of the world operates based on nonverbal communication and “an agreement” can be reached in a variety of ways. How do we make sense of the somewhat ambiguous legal definition? Perhaps the best way to view communications between competitors is as a threshold issue for the ability to conspire. Communications among competitors, even absent explicit evidence of an agreement not to compete, can enhance the ability of competitors to reach an agreement and to monitor whether firms are complying with any agreement. That is, communications offer rivals opportunities to

2. See Gregory Werden, *Economic Evidence on the Existence of Collusion: Reconciling Antitrust Law with Oligopoly Theory*, 71 ANTITRUST L.J. 719, 780 (2004) (“The existence of an agreement should not be inferred absent some evidence of communications of some kind among the defendants.”).

3. T. Mark McLaughlin, *Comments on Professor Page’s Discussion of Matsushita*, 38 LOY. U. CHI. L.J. 467 (2007).

4. Michael J. Freed, *Comments on Professor Page’s Discussion of Matsushita: Plaintiffs’ Perspective*, 38 LOY. U. CHI. L.J. 461 (2007).

develop collusive strategies and reduce the risk of competitors cheating on any agreement, and so can facilitate keeping prices above the level that would occur even in an oligopolistic market (where independently acting competitors take into account the actions by other firms). Accordingly, absent at least some evidence of such communications, plaintiffs probably should be required to offer a legitimate explanation about how the alleged conspiracy operated based on other relevant facts in order to survive summary judgment. Such an analysis could be offered through an economist, industry officials, or relevant documents, and might include evidence of past collusion or perhaps evidence of indirect communications through third parties who share the alleged competitors' goal of maximizing industry profits.⁵

THE ROLE ECONOMICS CAN PLAY

The conference also focused on whether economic analysis has much to contribute for “plus factors” in evaluating a conspiracy lacking direct evidence of an agreement. Economics has established certain conditions that are in general necessary for a conspiracy to operate successfully. Typically, a conspiracy not to compete involves parallel action, such as price increases occurring at similar times or firms not expanding sales into other firms' territories or customers. However, these conditions can also occur where there is competition, so by themselves they would not be considered sufficient to show a conspiracy. Also, in general, conspiracies are more likely to be possible with fewer competitors, such as in an oligopoly.⁶ In an oligopoly, however, economics teaches us that firms are likely to anticipate the actions of their competitors in determining their strategies, such as pricing and where to try to sell their products, even absent an agreement to fix prices or not to compete.⁷

For example, assume that firms A and B each dominate different regions of the United States. They may conspire not to expand into each other's territories, and thus can charge supracompetitive prices in each territory. Alternatively, firm A may unilaterally decide not to

5. For example, there might be extensive communications through investment firms that follow an industry, who could also gain from higher profits driven by a conspiracy. Judge Richard Posner has suggested a variety of other factors that might be included as relevant for inferring an agreement. See RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* ch. 4 (1976); RICHARD A. POSNER, *ANTITRUST LAW* ch. 3 (2d ed. 2001).

6. See, e.g., George J. Stigler, *A Theory of Oligopoly*, 72 J. POL. ECON. 44 (1964).

7. For a discussion that highlights the difficulties economics encounter in evaluating conspiracies in an oligopoly setting, see MICHAEL D. WHINSTON, *LECTURES ON ANTITRUST ECONOMICS* 20 (2006).

expand into the territory dominated by firm B without any agreement. Why? Firm A may anticipate that firm B would retaliate by expanding into firm A's territory—and visa versa. As this example illustrates, in oligopoly markets where collusion is most likely, it can be particularly difficult to separate collusion from nonconspiratorial actions.

Lawyers and courts often turn to economists hoping they can provide some clarity on the question of whether courts should infer a conspiratorial agreement from conduct alone where competitors are expected to take their rivals' action into consideration. Given the Court's decision in *Matsushita*, it is clear that economics can be helpful in answering whether it would be economically rational for the market players to conspire, and the Court dismissed the case on summary judgment when it found the answer to be no.⁸ The question is whether economic analysis can be used not only as a "minus factor" as in *Matsushita*, but also as a "plus factor" in determining whether a conspiracy actually existed.

There seems to be a broad consensus supporting Dan Shulman's⁹ and the Sedona Working Group's¹⁰ conclusion that economic testimony can be helpful in answering some basic questions that go to "plus factors" beyond parallel behavior. One area of plus factors is showing that certain thresholds for the economic plausibility of a conspiracy exist. For example, is the market sufficiently concentrated that it could plausibly meet the necessary conditions for a successful conspiracy and thus make "economic sense"? The second area focuses on whether there is evidence of firm behavior that would be profitable with a conspiracy, but not profitable without conspiracy.¹¹ This area goes beyond the "necessary" into what might be considered "sufficient" evidence (or at least an independent plus factor) for surviving summary judgment. The typical example here would be showing that a price increase by a firm would not be profitable unless the other firms followed, the other firms had a strong profit incentive and ability to keep prices lower, but all of the other firms nevertheless immediately followed the price increase. Another example might be where firms in a market had strong profit incentives to expand sales into other territories,

8. 475 U.S. at 587.

9. Daniel R. Shulman, *Matsushita and the Role of Economists with Regard to Proof of Conspiracy*, 38 LOY. U. CHI. L.J. 497 (2007).

10. THE SEDONA CONFERENCE, WORKING GROUP ON THE ROLE OF ECONOMICS IN ANTITRUST, THE SEDONA CONFERENCE COMMENTARY ON THE ROLE OF ECONOMICS IN ANTITRUST LAW (Feb. 2006), available at <http://www.thosedonaconference.org>.

11. See Werden, *supra* note 2, at 767.

even considering the potential for any likely unilateral retaliation, but did not expand.

Economic analysis, however, can only do so much. As Dr. Salinger's paper highlights, "When economists testify on subjects where the economics is inherently inconclusive, there is a real risk that it will get out of hand."¹² As discussed above, economics teaches that it is difficult to infer a conspiracy only from market information of parallel conduct in an oligopoly setting,¹³ and it is probably improper for an economist to testify as to the existence of a conspiratorial agreement. David Marx takes this argument further.¹⁴ To paraphrase his article, (1) economists sometimes go too far and testify to conclusions that are within the province of the jury, (2) dueling economists tend to cancel each other out at trial, and (3) forcing the jury to listen to dueling economists may actually take the focus away from the central legal issue at trial, i.e., did the defendants really agree to fix prices, allocate customers, or reduce output. However, even considering the example provided by David Marx, it does not appear that his criticism relates to economic analysis and reasoning, but to the use of expert economists when there are other ways to present that evidence to the jury.

There is little disagreement that economists should not testify in areas beyond their expertise, and economists and economic analyses by themselves cannot prove the defendants charged with wrongdoing explicitly agreed to collude. However, economists (or at least economic analyses) can provide evidence on the plausibility of conspiracy, and whether the actions of the firms in the market are consistent or inconsistent with an alleged conspiracy.

CONCLUSION

As in any conspiracy case, proof of illicit conduct is an inherently fact-driven inquiry. Cases with theories of conspiracy that do not make economic sense, lack any evidence of past collusion, or do not show some communications probably should be disposed of on summary judgment. The remainder should go to the jury as long as sufficient "plus factors" can be shown, and economic analysis can provide some of those "plus factors."

12. Michael A. Salinger, *The Legacy of Matsushita: The Role of Economics in Antitrust Litigation*, 38 LOY. U. CHI. L.J. 475 (2007).

13. WHINSTON, *supra* note 7, at 20.

14. David Marx, Jr., *The "Proper"—And By That I Mean Limited—Role for Economists in Price-Fixing Litigation*, 38 LOY. U. CHI. L.J. 491 (2007).

Against this background, we believe that the prospect that the Supreme Court may impose *Matsushita*'s standards on plaintiffs at the pleading stage should be troubling for lawyers and economists alike.¹⁵ Plaintiffs are unlikely to possess substantial economic or other evidence useful for evaluating the plausibility of a conspiracy prior to discovery, except perhaps where there is evidence of past collusion. Shifting the burden typically imposed at summary judgment to the pleading phase, therefore, would likely discourage potentially meritorious cases or reward plaintiffs' lawyers who are willing to plead "plus factors" without a substantial basis in fact. If courts were to add communications among the defendants as another "plus factor" (as we and Professor Page recommend) and require that it be shown at the pleadings stage, then plaintiffs' burden would be substantially greater because such communications rarely are available to plaintiffs absent discovery into the defendants' records.

15. As we are writing this article, the U.S. Supreme Court is in the process of deciding whether plaintiffs should be required at the pleading stage to set forth their plus factor evidence. See *Twombly v. Bell Atlantic Corp.*, 425 F.3d 99 (2d Cir. 2005), *cert. granted*, 126 S. Ct. 2965 (No. 05-1126).