1985

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Notes

Characterizing Horizontal Market-Division Agreements Under the Ancillary Restraints Doctrine

INTRODUCTION

Since the 1960's, marketing arrangements in many businesses have become more complex as firms seek to distribute their products in conjunction with national advertising and promotional campaigns. Typically, manufacturers or retailers will allocate territories in order to facilitate the efficient distribution of their products. If not properly implemented, such an arrangement, referred to as a market-division agreement, may be an illegal restraint of trade under section 1 of the Sherman Act.

1. The increased sophistication of marketing techniques has caused tension vis-à-vis the antitrust laws. As Philip Kotler has noted, "some students of business regulation go so far as to charge that judges and the Federal Trade Commission have remade the law into a body of rules of which a large portion impair competition. But, by and large, regulations are needed to keep businessmen fearful about overstepping the line in trying to neutralize competition through marketing arrangements." See P. Kotler, Marketing Management 39 (1976).

2. For example, a group of small manufacturers might want to adopt a common trademark in order to obtain the kind of public visibility that a large manufacturer is able to achieve on its own. Each manufacturer, however, may hesitate to commit its own resources to advertising the trademark in the hope that others will do so, thus enabling it to be able to take advantage of the others' advertising. If enough of the manufacturers resort to this practice, the purpose of the common trademark will be defeated. This problem can be overcome by allocating territories to each manufacturer and forbidding it to sell under the trademark outside of its territory. See R. Posner, Antitrust Law 225-26 (1974).


Every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal. . . .

See generally Letwin, Law and Economic Policy in America: The Evolution of the Sherman Antitrust Act ch. 3 (1965) for a worthwhile discussion of the legal and political background of the Sherman Act; Bork, Legislative Intent and the Policy of the Sherman Act, 6 J. Law & Econ. 7 (1966). Professor Bork has argued from a close reading of the legislative history that the Act was intended to forbid anticompetitive behavior strictly in the economic sense. See Bork, The Rule of Reason and the Per Se Concept: Price Fixing and Market-Division (Part I), 74 Yale L.J. 775 (1965); Bork, The Rule of Reason and the Per Se Concept: Price Fixing and Market-Division (Part II), 75 Yale L.J. 375 (1966).
Under antitrust law, courts determine the legality of challenged market-division agreements by initially characterizing the restraint as one that is either per se illegal\(^4\) or alternatively, as a restraint that will be judged under the rule of reason.\(^5\) Since a per se proscription finds illegality on the face of the agreement without further examination, the initial label which courts attach to a market-division agreement is crucial.\(^6\) Currently, the legality of challenged market-division agreements dividing markets between a manufacturer and its retailers is determined under a rule of reason analysis.\(^7\) Agreements dividing markets among competing firms,

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4. A plaintiff may also establish a per se case for other illegal conduct, *see, e.g.*, Klor's v. Broadway-Hale Stores, 359 U.S. 207, 212 (1959) (group boycotts and refusals to deal: electrical appliance retailer and manufacturers' of appliances agreement to boycott retailer's competitor held to be per se illegal); Northern Pac. Ry. Co. v. United States, 356 U.S. 1, 8 (1958) (tying agreements: railroad which sold land only upon the condition that purchasing companies ship over the seller's raillines held illegal per se); United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 158 (1940) (price-fixing: spot purchases by oil company which tended to stabilize the price of "distress gasoline" found to be illegal per se); Dr. Miles Medical Co. v. John D. Park & Sons Co., 320 U.S. 373, 379 (1911) (resale price maintenance: price restriction required of retailers by the manufacturer of patent medicines held per se illegal); *see also infra* notes 46-49 and accompanying text.

5. Market-division agreements which are not believed to have an inherently pernicious effect on competition are judged for their reasonableness by assessing their purpose and effect on the market. *See Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 59 (1977)* (market-division agreement implemented by a television set manufacturer among hand-picked retailers held to be a restraint to be assessed under the rule of reason). The rule of reason has also been applied to market perfecting arrangements, *see Maple Flooring Mfrs. Ass'n v. United States, 268 U.S. 563, 586 (1925)* (shared data disseminated between members of a trade association made available to buyers and sellers found reasonable under the rule of reason). *But see American Column & Lumber Co. v. United States, 257 U.S. 377, 411-12 (1921)* (members of trade association who shared specific prices charged to identified customers in closed transactions found to be in violation of the Sherman Act); *Broadcast Music, Inc. v. Columbia Broadcasting Sys., Inc., 441 U.S. 1, 24 (1979)* (blanket licensing to buyers of copyrighted musical compositions held to be a restraint to be judged under the rule of reason).

6. It is crucial that a market-division agreement be characterized as a restraint of trade to be analyzed under the rule of reason if the agreement is to survive at all. Although the per se rule contains a degree of arbitrariness, it reflects the view that the gains from the rule outweigh the losses and that significant administrative advantages will result. *See United States v. Container Corp. of Am. 393 U.S. 333, 341 (1969)* (Marshall, J., dissenting) (exchange of price information between building material sellers held illegal per se).

7. This type of agreement is referred to as a vertical agreement. A vertical agreement links two markets in the same chain of manufacture or distribution, usually through the linkage of two firms that can stand in the relationship of supplier and customer. *See United States v. Arnold, Schwinn & Co., 388 U.S. 365, 388 (1967)* (bicycle manufacturer restrictions on resale for its resellers and distributors held to be illegal per se). A market-division agreement implemented by a manufacturer upon its resellers is an example of a vertical agreement. The Supreme Court has held that vertical market-division agreements are to be tested under the rule of reason. *See Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 57 (1977).*
however, are relegated to the illegal per se category.\(^8\)

Economic analysis recognizes that competing firms may divide markets for procompetitive as well as anticompetitive purposes.\(^9\) The most common procompetitive purpose underlying the implementation of a market-division agreement is the elimination of "free-riding"\(^10\) among retailers who might otherwise take advantage of advertising and promotional efforts paid for by other retailers.\(^11\) The per se rule which is currently applied to agreements among competing firms that are motivated by such procompetitive reasons, however, restricts potential economic benefit from increased competition among the agreeing firms.\(^12\)

An alternative apparatus exists which courts can utilize to assess the legality of market-division agreements implemented by competing firms. The ancillary restraints doctrine\(^13\) presents a standard test by which potentially procompetitive agreements are elevated from the illegal per se category to a rule of reason analy-

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8. A market-division agreement implemented by competing firms or firms in the same line of business is horizontal. See, e.g., United States v. Penn-Olin Chem. Co., 378 U.S. 158, 163 (1964) (joint venture between two chemical companies engaged in the same line of business termed horizontal). A horizontal market-division involves only one market level. For example, four firms that manufacture identical widgets and consequently agree to divide the market in which they sell their widgets would be participating in a horizontal market-division agreement. Similarly, if the four firms agreed to fix the price for their widgets, they would be participating in a horizontal price-fixing agreement. Both agreements have identical consequences: prices move upward because output has been restricted. See E. GELLHORN, ANTITRUST LAW AND ECONOMICS 188-89 (1981).

The Supreme Court in United States v. Topco Assoc., Inc., 405 U.S. 596, 608 (1972), relegated horizontal market-division agreements to the illegal per se category.

9. See infra notes 33-35 and accompanying text.

10. Professor Robert Bork has categorized the five most obvious ways in which market-division is capable of enhancing the efficiency of business transactions. By far, the most common market-division is aimed at the elimination of the free-rider problem. This note necessarily will confine itself to that problem.

The other four procompetitive market-division agreements that Bork has categorized intend to: (1) optimize local sales efforts by eliminating the size of the market; (2) encourage exchanges of information; (3) minimize the cost of providing post-sale service and minimize the risk of customer dissatisfaction; (4) prevent overlapping use of a service whose cost is shared. See R. BORK, THE ANTITRUST PARADOX 430-31 (1979).


12. The finality of the per se rule precludes defendants from presenting justification arguments which might otherwise demonstrate the procompetitive effects of their agreement. By the same token, the finality and predictability of the per se rule has eliminated hundreds of anticompetitive agreements and no doubt others have been made less effective. See generally R. Bork, Ancillary Restraints and the Sherman Act, 15 Antitrust L.J. 211 (1959).

sis. The doctrine distinguishes between "naked" and "ancillary" restraints and applies per se illegality to a naked market-division agreement whose sole purpose is the elimination of competition. An agreement which is ancillary to a lawful purpose, on the other hand, is analyzed under the rule of reason regardless of whether it has been implemented by competing firms.

In General Leaseways, Inc. v. National Truck Leasing Association, the Seventh Circuit employed this doctrine to assess the legality of a market-division agreement implemented by a group of truck lessors. Application of the ancillary restraints doctrine enabled the court to characterize the agreement as a naked restraint based upon the lack of increased efficiency and competition resulting from the agreement. After determining that the market-division was a naked restraint of trade, the Seventh Circuit relegated the agreement to the per se category.

This note will briefly describe the economic structure of market-division agreements and their relationship to the elimination of free-riding. It will then examine the development of the characterization rules currently utilized by courts to categorize market-division agreements. The ancillary restraints doctrine will then be

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14. See infra note 95.
15. A "naked" restraint of trade is an agreement in which the parties have no significant dealing other than the elimination of competition. For example, if two widget manufacturers enter into an agreement to lower the output of their respectively similar products in order to raise prices, the resulting trade restraint is intended to eliminate competition. It has no lawful business purpose. See Addyston Pipe, 85 F. at 281-82. For a more detailed discussion of the mechanics of a naked restraint of trade see infra notes 97-98 and accompanying text.
16. An "ancillary" restraint of trade is an agreement which is subordinate and collateral to a separate, lawful business purpose. For example, if four widget manufacturers enter into an agreement to divide territories in which they send sales representatives because their particular market is too small to repay the efforts of two sellers of a single brand, the restraint is an ancillary one because it is subordinate to the lawful purpose of increasing widget sales in markets which might otherwise go untapped altogether. See Addyston Pipe, 85 F. at 282. For a more detailed description of the mechanics of an ancillary restraint see infra note 97.
17. The ancillary restraints doctrine, for example, would elevate an ancillary market-division agreement among competing firms to the rule of reason category, see, e.g., General Leaseways, Inc. v. National Truck Leasing Ass'n, 744 F.2d 588, 592 (7th Cir. 1984). Under current law, however, the agreement is illegal per se. See, e.g., United States v. Topco Assoc., Inc., 405 U.S. 596, 608 (1972). As a characterization device, the ancillary restraints doctrine preserves the per se and the rule of reason categories. The doctrine's fundamental criterion for characterizing market-division agreements is not their vertical or horizontal nature, but their capacity for contributing to efficiency. See R. Bork, supra note 10, at 30.
18. 744 F.2d 588 (7th Cir. 1984).
19. Id. at 595.
20. Id.
introduced and discussed. Finally, the General Leaseways opinion will be analyzed and the efficacy of the ancillary restraints doctrine as applied thereto will be discussed.

BACKGROUND

The Nature of Market-Division Agreements

The most direct manner in which competing firms can reap monopoly profits is by agreeing to fix the price of a similar or identical product which the firms sell. Firms may reap monopoly profits not only by implementing direct price-fixing agreements, however, but also indirectly by agreeing to eliminate competition by dividing markets. A market-division agreement which is implemented by a manufacturer among its resellers is termed a vertical market-division. Alternatively, an agreement implemented among the retailers themselves is termed a horizontal market-

21. "Monopoly profit" is the excess of total revenue over total costs which a firm that holds a monopoly will receive by being a sole producer or, alternatively, a producer that colludes with others to fix prices or allocate an exclusive territory. In a perfectly competitive industry, for example, all the producing firms will set output at a level where their marginal revenue equals marginal cost, with "cost" in the economic sense including a reasonable return on invested capital. The monopolist, be it a multi-national giant with no competitors, or a small firm with an exclusive market, can raise its price and lower its output in order to reap excess marginal revenue. The excess is monopoly profit. See R. Bork, supra note 10, at 90-104; R. Posner, supra note 11, at 5-14.

22. See, e.g., United States v. Trenton Potteries Co., 273 U.S. 392 (1927) (direct price fixing plan among competitors in the plumbing industry held to be per se unlawful); United States v. Joint Traffic Ass'n, 171 U.S. 505, 569 (1898) (agreement among competitors to set schedule rates for railroad service held to be per se illegal direct price-fixing).

The courts have held a variety of direct price-fixing arrangements to be per se unlawful. Among such per se unlawful arrangements are conspiracies to submit collusive, non-competitive rigged bids. See, e.g., United States v. Portsmouth Paving Corp., 694 F.2d 312, 317 (4th Cir. 1982); United States v. Koppers Corp., 652 F.2d 290, 297 (2d Cir.), cert. denied, 454 U.S. 1083 (1981); United States v. Brighton Bldg. & Maintenance Co., 598 F.2d 1101, 1106 (7th Cir. 1979); United States v. Flom, 558 F.2d 1179, 1183 (5th Cir. 1977); United States v. Champion Int'l Corp., 557 F.2d 1270 (9th Cir. 1977), cert. denied, 434 U.S. 938 (1978); Las Vegas Merchant Plumbers Ass'n v. United States, 210 F.2d 732, 748-49 (9th Cir.), cert. denied, 348 U.S. 817-8 (1954).

In certain circumstances, agreements among competitors to engage in cooperative price advertising have been held to be illegal direct price-fixing agreements. See, e.g., United States v. Serta Assoc., 296 F. Supp. 1121, 1125-26 (N.D. Ill. 1968), aff'd mem., 393 U.S. 534 (1969) (cooperative advertising program used by horizontal competitors conditioning dealer participation on all advertising containing suggested retail prices held to be direct price-fixing); United States v. Pittsburgh Area Pontiac Dealers, Inc., 1978-2 Trade Cas. (CCH) ¶62,233 (W.D. Pa. 1978) (consent decree terminating litigation charging dealers with advertising as a group and listing prices for dealer models).

23. Timken Roller Bearing Co. v. United States, 341 U.S. 593, 598 (1951) (agreement among American, French, and British corporations to allocate international trade territories held illegal as part of an aggregate of trade restraints).

24. See supra note 7.
Firms may divide markets geographically, technically or functionally by classes of customers. By eliminating competitors, the firm becomes a monopolist in the market it has been allocated. The firm can raise prices, or it may withdraw supplies from the market, thus indirectly raising the price of its product. Consequently, consumers pay higher prices than that would be set by competition.

25. See supra note 8.

26. See, e.g., Addyston Pipe, 175 U.S. at 240-41 (combination among pipe manufacturers to allocate business found illegal); Topco, 405 U.S. at 608 (agreement among supermarket chains to allocate territories for private label merchandise held per se unlawful).

27. See, e.g., Ron Tonkin Gran Turismo, Inc. v. Fiat Distrib., Inc., 637 F.2d 1376, 1382-83 (9th Cir. 1981), (agreement among auto import dealers to allocate big ticket sports cars); cert. denied, 454 U.S. 831 (1982); Eiberger v. Sony Corp. of Am., 622 F.2d 1068, 1072 (2d Cir. 1980) (agreement to allocate dictation machines according to technical sophistication); Arizona v. American Petrofina, Inc., 1974-2 Trade Cas. (CCH) ¶75,398 (N.D. Cal. 1974) (agreement to classify petroleum refiners by level of gasoline refined).

28. See, e.g., United States v. Koppers Co., 652 F.2d 290, 296-97 (2d Cir. 1981) (customer allocation per se unlawful); cert. denied, 454 U.S. 1083 (1982); United States v. Cadillac Overall Supply Co., 568 F.2d 1078, 1087-90 (5th Cir.) (customer allocation conspiracy wherein competitors agreed not to solicit others' accounts and balanced among themselves those accounts that changed held per se illegal), cert. denied, 437 U.S. 903 (1978); United States v. Penn. Refuse Removal Ass'n, 357 F.2d 806 (3d Cir.) (agreement between refuse pick-up customers to allocate roll-off and industrial customers held per se illegal), cert. denied, 384 U.S. 961 (1966); United States v. Laundries Corp., 291 F.2d 563, 575-76 (2d Cir. 1961) (agreement among laundry companies dividing factory processes for clothing items held per se unlawful).

29. A "monopolist" in the traditional sense is the only producer of its product and faces no outside competition. After a market-division agreement is implemented, the same state of affairs results: the market-division monopolist is the only producer or seller in its territory and it faces no competition. See E. Gellhorn, supra note 8, at 181-82.

30. In an industry with a large number of sellers, each relatively small, an individual firm will not assume that market prices can be affected by its own output decision. Each firm will take costs and prices as given and will set output at a level maximizing returns at given prices. This model, generally known as the competitive model, encourages independent, competitive conduct. Under the competitive model, forces and materials are efficiently allocated among the various lines of industry.

A monopolist, on the other hand, because its output is the output of the industry, recognizes that as it increases output, the prices it can charge will decrease. The monopolist therefore adjusts output and price to maximize return. Consequently, output for the industry will be lower and profits higher than if the industry functioned competitively.

Market-division generally occurs in an industry where there are a substantial, though not an exceedingly large number of firms. The industry may function competitively, but if the firms agree upon a cooperative market-division policy they can lower industry output much as a monopolies would. See L. Sullivan, Handbook of Antitrust §61 (1981).

31. Decreased output harms consumers by artificially driving the price of the product upward. Senator John Sherman, the prime mover of the legislation which bears his name, made clear the objective to be served by the antitrust laws. The bill declares illegal two classes of "arrangements, contracts, agreements, trusts, or combinations: (1) those...
Economic analysis recognizes, however, that market-division agreements can also enhance competition when they are employed to make productive activity more efficient. The most commonly implemented procompetitive market-division agreement is aimed at the elimination of the free-rider problem. For example, the competitive efficiency of a firm that retails Steinway pianos may be impaired by the presence of a free-riding Steinway dealer located nearby. If Steinway dealer A provides an elaborate showroom, demonstrations, and other services that consumers demand, it must cover the costs incurred by raising the price of its pianos. Steinway dealer B, a free-rider, rather than provide any services, can suggest to its customers that they first utilize dealer A's services to select the piano they want and return to dealer B for the purchase. Dealer B can offer lower prices than dealer A because it does not incur the expenses that dealer A incurs in providing services. Faced with dealer B's lower priced competition, dealer A may eventually stop providing services and Steinway piano sales may decrease.

A geographical market-division agreement allocating exclusive territories to Steinway piano retailers will solve the free-rider problem by eliminating intrabrand competition. With intrabrand competition removed, interbrand competition with, for instance

made with a view, or which tend, to prevent full and free competition, and (2) those designed, or which tend to advance cost to the consumer. . . . " For a detailed and interesting discussion of the policies behind the Sherman Act see Bork, Legislative Intent and the Policy of the Sherman Act, 9 J. LAW AND ECON. 7 (1966).

32. See supra note 10.

33. The common occurrence of the free-rider elimination agreement has found its way to the Supreme Court as well. The two main cases which address procompetitive market-division are Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977) and United States v. Topco Assoc., Inc., 405 U.S. 596 (1972). Both of these cases are free-rider elimination cases.

34. The Steinway retailers example concerns firms in the same line of business. Alternatively, competing firms can implement a market-division agreement to eliminate free-riding if they all offer one product in common but compete with each other nonetheless. For example, if several small grocery chains form an association to distribute private-label products in order to compete with A & P and Safeway's lower priced brands, they might be inclined to implement a market-division agreement to eliminate free-riding if advertising costs are not shared. In this case, there is decreased intrabrand competition vis-à-vis the private label products. Interbrand competition with other grocery chains may be enhanced.


37. "Interbrand competition is the competition among the manufacturers or resellers of the same generic product," pianos in this example. "The degree of intrabrand compe-
Baldwin piano retailers, may be enhanced because Steinway retailers are assured that their prices will not be undercut by other Steinway dealers. The assurance of an exclusive territory encourages Steinway dealers to increase advertising and sales efforts, carry larger inventories, and provide higher quality maintenance and repair service which attracts prospective piano buyers.

In the Steinway piano example, a market-division agreement may be implemented by the piano manufacturer among its retailers or, alternatively, by an agreement implemented among the Steinway retailers themselves. Either market-division agreement, whether implemented by vertical or horizontal structure, would be aimed at eliminating the free-rider problem and can be procompetitive. Many courts rely exclusively upon the structure by which the agreement is implemented to determine the legality of the agreement. Consequently, horizontal market-division agreements have been generally found to be illegal per se while vertical agreements have been judged under a rule of reason standard.

Professor Posner has noted that the availability of these services may increase a consumer's desire to deal with firms that offer them, especially if the firms sell high-priced products like pianos or automobiles. See R. Posner, supra note 11, at 148-50.

The fundamental difference between the structure of horizontal and vertical market-division lies with the parties who are imposing the restraint. A horizontal market-division is imposed by firms at the same market-level. Economic analysis suggests that it is as likely that horizontal market-division is imposed to restrict output as it is to increase business efficiency. A vertical market-division, on the other hand, is imposed by a manufacturer on its resellers. Economic analysis suggests that vertical market-division is generally implemented to increase business efficiency because the manufacturer desires to encourage rather than restrict competition for its own benefit. Horizontal market division agreements, however, can also be implemented to increase competition. See R. Posner, supra note 11, at 149-50.

See, e.g., New Home Appliance Center, Inc. v. Thompson, 250 F.2d 881, 885 (10th Cir. 1957) (any horizontal agreement among local competitors, or with manufacturers, which has the purpose or effect of apportioning territories is illegal per se); Pfotzer v. Aqua Sys. Inc., 162 F.2d 779 (2d Cir. 1947) (it is immaterial to the illegality of horizontal territorial limitation that the agreement does not set up impenetrable boundaries); United States v. Imperial Chem. Indus., Ltd., 100 F. Supp. 504 (S.D.N.Y. 1951) (the fact that defendants do not dominate industry involved is immaterial to illegality of agreement establishing horizontal territorial limitations).

See Topco, 405 U.S. at 608.

Characterizing Market-Division Agreements: The Rule of Reason and the Per Se Rule

Courts determine the legality of challenged trade restraints by initially characterizing the restraint as one that is either per se illegal or, alternatively, as a restraint that will be judged under the rule of reason. A market-division is illegal per se if it is found to be inherently anticompetitive. To establish a per se case, the plaintiff need only prove that the anticompetitive behavior occurred, there being no other elements to the offense and no allowable defenses. The per se rule thus finds anticompetitive behavior illegal as a matter of law and terminates further analysis.

A restraint of trade that is not characterized as a per se offense is analyzed under the rule of reason. The rule of reason permits

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45. See supra notes 4-5.
46. The rule had its genesis in United States v. Trans-Missouri Freight Ass'n, 166 U.S. 290 (1897), in which the Court found the defendants guilty of price fixing yet did not remand the case for trial. In the most recent pronouncement regarding the per se rule, the Supreme Court noted that "per se rules are invoked when surrounding circumstances make the likelihood of anticompetitive conduct so great as to render unjustified further examination of the challenged conduct." National Collegiate Athletic Ass'n v. Board of Regents of the Univ. of Okla., 104 S. Ct 2948, 2962 (1984). Thus, the courts look to the Supreme Court's directives as to which restraints are to be relegated to the per se category.
47. See infra notes 51-52.
48. In National Collegiate Athletic Ass'n v. Board of Regents of the Univ. of Okla., 104 S. Ct. 2948, 2962 (1984) the Supreme Court noted that per se rules should not be invoked until considerable judicial experience with the restraint has shown it to be inherently anticompetitive. See also Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 104 S. Ct. 1551 (hospital's exclusive arrangement with anesthesiologist firm held not sufficiently anticompetitive to justify application of the per se rule). But see Arizona v. Maricopa County Medical Soc'y, 457 U.S. 332, 350-51 (1982) (maximum fee arrangement for medical care held per se illegal).
49. United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 221-23 (1940). Justice Thurgood Marshall has suggested this rationale behind the per se rule:
   Per se rules contain a degree of arbitrariness. They are justified on the assumption that the gains from the rule will far outweigh the losses and that significant administrative advantages will result. In other words, the potential competitive harm plus the administrative costs of determining in what particular situations the practice may be harmful must far outweigh the benefits that may result. If the potential benefits in the aggregate are outweighed to this degree, then they are simply not worth identifying in individual cases.
50. In United States v. Trenton Potteries Co., 273 U.S. 392 (1927), the Court noted that a price-fixing and market-division agreement among manufacturers of vitreous pottery was so clearly anticompetitive that such "agreements which create such potential power may well be held to be in themselves unreasonable or unlawful restraints, without the necessity of minute inquiry whether a particular price is reasonable or unreasonable." Id. at 397.
51. The rule of reason has its roots in the fact that if section 1 of the Sherman Act
courts to decide whether the market-division is significantly and unreasonably anticompetitive in purpose and effect before it is adjudged to be lawful or unlawful.\textsuperscript{52} Under the rule of reason, the defendants may come forward with justifications in order to explain their apparent deviation from the operations of a free market.\textsuperscript{53} Thus, if a market-division agreement is to survive at all, it must initially be characterized as a restraint to be judged under the rule of reason.\textsuperscript{54}

Judicial analysis under the rule of reason is currently accorded only to vertical market-division agreements.\textsuperscript{55} Horizontal market-division agreements are currently characterized as illegal per se.\textsuperscript{56} The disparity in treatment was laid down in two Supreme Court decisions: \textit{Continental T.V., Inc. v. GTE Sylvania, Inc.}\textsuperscript{57} and \textit{United States v. Topco Associates, Inc.}\textsuperscript{58} The \textit{Sylvania} decision held that to be read literally it would bar any commercial contract which touches upon trade or business. "Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence." Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918). Therefore, a literal interpretation of the statute could render illegal any contract "in the whole field of human activity . . . if in restraint of trade. . . ." Standard Oil Co. v. United States, 221 U.S. 1, 60 (1911).

Consequently, the statute has been interpreted to prohibit only undue restraints of trade. \textit{Id.} An undue restraint of trade is one which may suppress or even destroy competition, as opposed to a restraint which regulates and thereby promotes competition. Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918).

52. Justice Brandies spelled out the factors to be determined under a rule of reason analysis:

The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition. . . . To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable.

Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918).

53. See L. SULLIVAN, supra note 30, at 227-29.

54. National Collegiate Athletic Ass'n v. Board of Regents of the Univ. of Okla., 104 S. Ct. 2948, 2957 (1984). Much of the confusion which surrounds the characterization of market-division agreements stems from the initial analysis that the court must make at the outset of the case. The court's initial decision characterizing the restraint is crucial to the outcome of the case. Placing a restraint in the rule of reason category, however, is not indicative of its per se lawfulness. The rule of reason accords the defendants an opportunity to justify their apparent deviation from the free market. See generally L. SULLIVAN, supra note 30, at §§ 70-72.

55. Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977). The Court stated that applying per se illegality to vertical market-division agreements was to be "abandoned in favor of a return to the rule of reason." \textit{Id.} at 57.

56. Topco, 405 U.S. 596 (1972). The Court stated that "[t]he district court failed to make any determination as to whether there were per se horizontal territorial restraints in this case and simply applied the rule of reason in reaching its conclusions. . . . In so doing, the district court erred." \textit{Id.} at 608.


58. 405 U.S. 596 (1972).
that challenged vertical market-division agreements are to be analyzed for their reasonableness under the rule of reason. The Topco decision, on the other hand, relegated horizontal market-division agreements to the illegal per se category.

The Topco Decision: Horizontal Market-Division and the Per Se Rule

The Topco case involved a horizontal market-division agreement that designated territories in which small grocers could sell private-label products. Twenty-five small and medium-sized supermarket chains had formed an association, Topco Associates, which promulgated the private-label program across thirty-three states. Topco acted as a purchasing agent for its members, developed specifications for private-label products, and performed other tasks which gave members efficiencies attainable only by much larger chains.

Topco promulgated a rule which provided that members could sell Topco-brand products only in designated territories. The restraint promulgated by Topco had a plausible connection with efficiency although it was implemented by competing firms.

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59. Sylvania, 433 U.S. at 57.
60. Topco, 405 U.S. at 608.
61. A "private-label" is a less expensive alternative to products distributed by such national canners as Libby's and Green Giant. Topco, 405 U.S. at 599, n.3.
62. Topco Associates was founded in the 1940's by a group of small grocery chains. The Association was a corporation in which all the members owned the common stock in equal distributions. Id. at 598-99.
63. The Court's opinion recognized the efficiencies of the private label program: "It is obvious that by using private-label products a chain can achieve significant cost economies in purchasing, transportation, warehousing, promotion, and advertising. These economies may afford the chain opportunities for offering private-label products at lower prices than other brand name products." Id. at 599, n.3.
64. Article IX, sec. 2, of Topco's bylaws established three categories of territorial licenses that members could secure from the Association:
   (a) Exclusive: An exclusive territory is one in which the member is licensed to sell all products bearing specified trademarks of the Association, to the exclusion of all others.
   (b) Non-exclusive: A non-exclusive territory is one in which the member is licensed to sell all products bearing specified products of the Association, but not to the exclusion of others who may also be licensed to sell products bearing the same trademarks of the Association in the same territory.
   (c) Coextensive: A coextensive territory is one in which two (2) or more members are licensed to sell all products bearing specified trademarks of the Association to the exclusion of all other[s].

Topco, 405 U.S. at 601-02.
65. See supra note 63.

After remand, the District Court entered a judgment enjoining the use of agreements limiting the territories in which members could sell Topco products. The decree permit-
Intrabrand competition among Topco members was diminished, but interbrand competition with such national supermarket chains as A & P, Safeway, and Kroger was enhanced. The proposed justification for the practice was that the effective promotion of the private-label products was feasible only if the chains asked to incur the expense of the promotions also reaped the benefits. The Supreme Court rejected Topco's free-rider elimination argument, reasoning that the "restraint in this case is a horizontal one, and therefore a per se violation of section 1."\

In fashioning a per se proscription for horizontal market-division agreements, the Supreme Court noted that courts are ill-equipped to examine difficult economic problems. The Court reasoned that an agreement between competitors to allocate territories in order to minimize competition was a "classic example of a per se violation of section 1." The Topco Court thus surmised that most or all horizontal market-division agreements were anticompetitive and therefore should be per se illegal. In its decision to characterize all horizontal market-division agreements as per se illegal, however, the Court also placed potentially procompetitive agreements under the per se shroud.

The government appealed, contending that allowing the permissive clauses of the decree to become effective was tantamount to permitting a continuation of the exclusive territory arrangement struck down by the Court one year earlier. Despite the government's argument, the Supreme Court affirmed the decree by an evenly divided vote. United States v. Topco Associates, Inc., 414 U.S. 801 (1973).

66. See supra notes 41-43 and accompanying text.
67. Topco presents a perfect example of a horizontal market-division implemented to eliminate free-riding in the interest of promoting a common trademark.
68. Topco, 405 U.S. at 608.
69. Id. at 609.
70. Id. at 608. The Court was relying heavily on the fact that the illegal per se proscription had been vigorously applied to horizontal price-fixing agreements. It was the clear probability that such practice was anticompetitive that made it a classic example of a per se violation. Economists had recognized, however, that horizontal market-division agreements could be implemented for procompetitive as well as anticompetitive purposes. The Topco court believed that the salutary effect of the per se rule outweighed elevating all market-division to the per se category. Id. at 609.
71. Id. at 609.
72. Topco, 405 U.S. at 608. Topco was criticized by economists and commentators, most notably Professor Robert Bork, who noted that the Court had misperceived the task which had been laid before it. See R. BORK, supra note 10, at 274-79. Topco had been
Five years after the *Topco* decision, the Supreme Court was required to characterize a vertical market-division agreement in *Continental T.V., Inc. v. GTE Sylvania, Inc.* The *Sylvania* decision: A Rule of Reason Analysis for Vertical Market-Division

Sylvania, a major television manufacturer with a declining share of the market, abandoned its policy of saturation distribution and moved to a smaller group of franchised retailers. Sylvania's new plan contemplated an advertising and promotion blitz and allocated territories to franchisees in order to eliminate free-riding.

The market-division in *Sylvania* was similar in character to the agreement in *Topco* and was also intended to eliminate free-riding. It was classified as a vertical restraint, however, because the

preceeded by an earlier, though quite similar case, United States v. Sealy, Inc., 388 U.S. 350 (1967). In *Sealy*, the Court had faced characterizing an agreement which contained both price-fixing and market-division elements aimed at eliminating free-riding. The *Sealy* Court found the aggregate of restraints to be illegal per se probably because the price-fixing elements of the case poisoned the market-division. *Sealy*, 388 U.S. at 357.

In *Sealy*, however, the Court had given an example of a market-division agreement which was in many respects similar to the agreement which was struck down in *Topco*. *Id.* at 357. The faint pangs of reform in *Sealy* were erased, however, when the Court in *Topco* noted that "to the extent that *Sealy* casts doubt on whether horizontal territorial limitations, unaccompanied by price-fixing, are per se violations of the Sherman Act, we remove that doubt today." *Topco*, 405 U.S. at 609 n.9 (1972).


74. *Sylvania*, 433 U.S. at 38 (1977). "Saturation distribution" occurs when a manufacturer sells its product to independent or company-owned distributors who in turn resell the product to a large and diverse group of retailers.

75. *Id.*

76. Before 1962, Sylvania, a manufacturer of color television sets, sold to wholesalers who resold to a large and diverse group of retailers. In an effort to avert a decline in its market share to 1 or 2 percent, Sylvania adopted the franchise system in which it sold to a smaller number of retailers. Although Sylvania retained discretion to add franchises to any market, the intent and effect of the system clearly were to decrease rivalry among sellers of Sylvania products. Whether because the system induced greater dealer effort or for other reasons, Sylvania's share of the national market rose to 5 percent by 1965. *Id.* at 38.

77. The franchise agreement that Sylvania implemented did not grant exclusive territories to franchisees. Sylvania reserved the right to grant new franchises in areas near other franchises depending upon sales volume and other factors. See supra note 64.
manufacturer was party to the agreement.\textsuperscript{78} The Ninth Circuit reversed the district court's per se ruling and reasoned that the court erred by refusing to hear Sylvania's justification arguments.\textsuperscript{79} On appeal, the Supreme Court affirmed the Ninth Circuit and held that vertical market-division agreements would be tested under the rule of reason.\textsuperscript{80}

In \textit{Sylvania}, the Supreme Court explicitly recognized that manufacturers have an economic interest in maintaining intrabrand competition at a level consistent with the efficient distribution of their products.\textsuperscript{81} The Court further reasoned that the procompetitive benefits that could result from increased interbrand competition justified applying the rule of reason to vertical agreements.\textsuperscript{82} The Court held, however, that only vertical market-division agreements would be tested under the rule of reason despite the recognition that "[t]here may be occasional problems in differentiating vertical restrictions from horizontal restrictions originating in agreements among retailers."\textsuperscript{83}

After \textit{Sylvania}, challenged vertical market-division agreements were elevated to a rule of reason analysis.\textsuperscript{84} Horizontal market-division presented a different dilemma to the Court because such

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\item \textsuperscript{78} \textit{Sylvania}, 433 U.S. at 38. In contrast to the horizontal agreement in \textit{Topco}, the agreement in Sylvania was a vertical arrangement since two levels of the market, the manufacturer and its resellers, were linked by the agreement to divide markets.
\item \textsuperscript{79} GTE Sylvania, Inc. v. Continental TV., Inc., 537 F.2d 980, 1004 (9th Cir.), aff'd, 433 U.S. 36 (1977).
\item \textsuperscript{80} \textit{Sylvania}, 433 U.S. at 59. The \textit{Sylvania} decision was the last decision in a trilogy of opinions in which the Supreme Court addressed the legality of vertical market-division. In White Motor Co. v. United States, 372 U.S. 253, 264 (1963), the Court reversed and remanded for trial a case where the district court had accepted the Justice Department's contention that vertical market-division was illegal per se. The Court said that "we know too little of the actual impact of vertical territorial restrictions" to decide the legality or illegality on the bare record of a summary judgment for the government. \textit{Id.} at 261.
\item Four years later, the majority of the Supreme Court, distinguishing \textit{White Motor}, held that vertical market-division was per se illegal in United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967). The Court stated that "under the Sherman Act, it is unreasonable without more for a manufacturer to seek to restrict and confine areas . . . in which an article may be traded after the manufacturer has parted with dominion over it." \textit{Id.} at 379.
\item Changing direction again in \textit{Sylvania}, the Supreme Court rejected the per se illegality rule of \textit{Schwinn}, stating that "we conclude that the appropriate decision is to return to the rule of reason that governed vertical restrictions prior to \textit{Schwinn}." \textit{Sylvania}, 433 U.S. at 59.
\item \textsuperscript{81} \textit{Sylvania}, 433 U.S. at 56.
\item \textsuperscript{82} \textit{Id.} at 54.
\item \textsuperscript{83} \textit{Id.} at 58, n.28; see also supra note 41.
\item The Court left the door slightly ajar for applying per se illegality to particular applications of vertical market-division. \textit{Sylvania}, 433 U.S. at 58.
\end{itemize}
agreements can be implemented for anticompetitive as well as procompetitive purposes.\textsuperscript{85} Under the \textit{Topco} rationale,\textsuperscript{86} all horizontal market-division agreements are placed in the per se category.

The horizontal/vertical dichotomy created by \textit{Topco} and \textit{Sylnia} has posed problems for courts faced with the task of assessing the legality of procompetitive market-division agreements implemented in horizontal structures.\textsuperscript{87} In fact, judicial reluctance in attaching a per se proscription to procompetitive horizontal agreements is evidenced by a trend among courts to place horizontal agreements in the vertical category in order to avoid the \textit{Topco} rule.\textsuperscript{88} A more useful guide for modern courts faced with assessing the legality of procompetitive horizontal market-division agreements is provided by the ancillary restraints doctrine.\textsuperscript{89}

\section*{DISCUSSION

\textit{Ancillary Restraints and Market-Division Agreements}}

The ancillary restraints doctrine elevates a restraint with procompetitive attributes to a rule of reason analysis notwithstanding the structure in which the restraint is implemented.\textsuperscript{90} The doctrine can be applied to price-fixing,\textsuperscript{91} and tying arrangements\textsuperscript{92} as

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\item [\textsuperscript{85}] Although there are no statistics available, horizontal market-division agreements can pose a threat to competition because they present either a combination or a conspiracy between competing firms or firms in the same line of business. The potential for abuse is apparent. That all horizontal market-division agreements have a pernicious effect on competition, however, has been shown to be a fallacy. \textit{See} R. \textit{Bork}, \textit{supra} note 10, at 430-31.
\item [\textsuperscript{86}] Professor Sullivan has noted that many courts have tested horizontal market-division agreements under the rule of reason where the court was presented with something less than a "flat out" naked agreement. \textit{See} L. \textit{Sullivan}, \textit{supra} note 30, at § 81.
\item [\textsuperscript{87}] \textit{See e.g.}, Ohio-Sealy Mattress Mfg. Co. v. Sealy, Inc., 585 F.2d 821, 827 (7th Cir. 1978) (national mattress licensors' agreement presented ambiguity to court over whether restraint was horizontal or vertical); Dougherty v. Continental Oil Co., 579 F.2d 954, 959 (5th Cir. 1978) (market-division implemented by Conoco had both horizontal and vertical attributes); Ohio-Sealy Mattress Mfg. Co. v. Duncan, 486 F. Supp. 1047, 1060 (S.D. Ohio 1980) (restructuring of corporate entity rendered vertical rather than horizontal market-division); West Texas Util. Co. v. Texas Elec. Serv., 470 F. Supp. 798, 830-31 (N.D. Tex. 1979) (market-division among public utility presented ambiguity between horizontal and vertical market-division).
\item [\textsuperscript{88}] \textit{See supra} notes 86-87.
\item [\textsuperscript{89}] \textit{See supra} notes 13-17 and accompanying text.
\item [\textsuperscript{90}] \textit{See infra} notes 99-105 and accompanying text.
\item [\textsuperscript{91}] Joint ventures sometimes include agreements under which two competitors specifically agree to fix prices. For example, an agreement between two competitors in a joint venture to submit a joint bid to build a subway system will necessarily contain price-fixing elements. Although competition between the two contractors is eradicated, interbrand competition with other contractors submitting subway bids is enhanced. The
well as market-division agreements. The doctrine was introduced nearly ninety years ago in the Sixth Circuit opinion of United States v. Addyston Pipe & Steel Co.

Addyston Pipe involved a section 1 action against six manufacturers who had agreed to fix prices and allocate selling territories for cast-iron pipe. In deciding how the agreement would be characterized, the court of appeals accorded restraints which were ancillary, those that were subordinate and collateral to another legitimate purpose, to a rule of reason analysis. The court then held that naked restraints, those that did nothing more than eliminate competition, would be placed in the illegal per se category.

The difference between an ancillary and a naked market-division is best illustrated by returning to the Steinway piano retailers example. An agreement among the Steinway retailers allocating selling territories in order to facilitate a promotional effort consti-
tutes a horizontal market-division aimed at the elimination of free-riding.\textsuperscript{99} The agreement is also ancillary to the joint promotional effort because the promotion is a lawful activity intended to achieve maximum interbrand competition.\textsuperscript{100} \textit{Addyston Pipe}'s ancillary restraints doctrine would test the legality of the agreement under a rule of reason analysis.\textsuperscript{101} Under the \textit{Topco} rule, however, the market-division would be illegal per se.\textsuperscript{102} Alternatively, the Steinway retailers may agree to allocate territories solely to reap monopoly profits.\textsuperscript{103} Under \textit{Addyston Pipe}, such an agreement is a non-ancillary, naked restraint and therefore would be relegated to the per se category.\textsuperscript{104}

The ancillary restraints doctrine was frequently applied by courts immediately following its formulation in \textit{Addyston Pipe}.\textsuperscript{105} Application of the doctrine declined as horizontal and vertical structure gradually became the tool courts employed to characterize market-division agreements.\textsuperscript{106} In \textit{General Leaseways, Inc. v. National Truck Leasing Association},\textsuperscript{107} however, the Seventh Cir-

\textsuperscript{99}. See supra notes 34-36 and accompanying text.

\textsuperscript{100}. \textit{Addyston Pipe} suggested that it was fairly simple to determine whether the restraint was ancillary or naked because the purpose of the main transaction "suggests the measure of protection needed, and furnishes a sufficient standard by which the validity of the restraint may be judicially determined." 85 F. 271 at 282.

\textsuperscript{101}. See supra notes 51-52 and accompanying text.

\textsuperscript{102}. See supra notes 46-49 and accompanying text.

\textsuperscript{103}. See supra note 21.

\textsuperscript{104}. The ancillary restraints doctrine, unlike the per se rule, places risk in having a naked restraint judged under the rule of reason. Although the likelihood of a naked market-division surviving a rule of reason analysis is low, this may be better than to proscribe potentially procompetitive market-division agreements under the per se rule. The per se rule, however, is preserved for naked horizontal agreements. See Bork, \textit{Ancillary Restraints and the Sherman Act}, 15 ANTITRUST L.J. 211, 217 (1959).

\textsuperscript{105}. See, e.g., United States v. Chesapeake & Ohio Fuel Co., 105 F. 93, 103 (6th Cir. 1900) (agreement to divide markets and restrict the output of coal found to be a naked restraint of trade); Lowry v. Tile & Mantel Ass'n of Calif., 98 F. 817, 824 (9th Cir. 1899) (agreement to raise the price of fireplace fixtures found to be a non-ancillary, naked restraint); Cravens v. Carter-Crume Co., 92 F. 479, 485-86 (6th Cir. 1899) (agreement to limit the production of wooden dishes found to be an non-ancillary restraint of trade).

\textsuperscript{106}. Professor Bork has referred to the \textit{Addyston Pipe} decision as the "high water-mark of rational antitrust doctrine." See R. BORK, supra note 10, at 29-30. The doctrine has had a faint rebirth in the last few years. See, e.g., Los Angeles Memorial Coliseum Comm'n v. National Football League, 726 F.2d 1381, 1395-98 (9th Cir. 1984) (NFL's rule requiring three-fourths of member teams to approve a team's moving into another team's league held to be non-ancillary restraint of trade); Lektro-Vend Corp. v. Vendo Co., 660 F.2d 255, 265-66 (7th Cir. 1981) (noncompetition covenants that were ancillary to legitimate acquisition by plaintiff held to be reasonable restraints of trade).

\textsuperscript{107}. 744 F.2d 588 (7th Cir. 1984).
cuit revived the ancillary restraints doctrine in order to characterize a horizontal market-division agreement.

General Leaseways, Inc. v. National Truck Leasing Association

Factual Background

The plaintiff, General Leaseways, was engaged in leasing trucks to businesses on a full-service basis. Full-service leases provided that General Leaseways was responsible for maintaining and repairing the trucks if they broke down. Many of the leases provided for "over-the-road" service, which meant that the lessee could drive the truck anywhere in the United States.

General Leaseways was a member of the National Truck Leasing Association which administered among its approximately 130 members a reciprocal service arrangement which enabled each member to lease trucks on a full-service, over-the-road basis. The Association's rules required each member to repair other members' leased trucks. The price that members charged each other for the repair service was not fixed, but it was substantially lower than the price charged non-members.

The Association disseminated trade information to members, and also administered a joint fuel purchasing program. Members shared a trademark, "NationaLease," but neither the Association nor its members advertised or promoted the trademark extensively. Each member operated under an Association franchise agreement that designated the particular location at which a member could do business as a National franchisee. Franchises were spaced at least 10 to 20 miles apart so that they could not compete for the same customers. In addition, the Association forbade its members to affiliate with any other full-service truck leasing firm.

General Leaseway defied the location and non-affiliation restrictions and was expelled from the Association for its infractions.

108. Id. at 589.
109. Id.
110. Id.
111. Id.
112. Id.
113. Id.
114. Id.
115. Id. at 590.
116. Id.
117. Id.
118. Id.
119. Id.
It brought suit under section 1 of the Sherman Act and alleged that the market-division agreement promulgated by the Association was an unlawful restraint of trade.\textsuperscript{120} The district court entered an injunction ordering the Association not to expel General Leaseways.\textsuperscript{121} The Association appealed and the Seventh Circuit was required to consider, among other things, the "bounds of permissible cooperation among competitors under section 1 of the Sherman Act."\textsuperscript{122}

The Seventh Circuit Opinion

The court of appeals upheld the decision of the district court and found that the Association had most likely promulgated a naked horizontal market-division agreement intended solely to decrease competition among Association members.\textsuperscript{123} The Seventh Circuit noted that the geographical division of markets among the Association's members did not appear to be ancillary to the reciprocal provision of repair service or any other lawful activity.\textsuperscript{124} The court of appeals thus concluded that the market-division was more likely than not a per se violation of section 1 of the Sherman Act.\textsuperscript{125}

The Seventh Circuit initially noted that, until \textit{Sylvania}, where firms in the same line of business agreed not to enter each other's territories they violated section 1 even if they could show that their market-division agreement yielded benefits greater than the cost of diminished competition.\textsuperscript{126} The court reasoned that the \textit{Sylvania} decision, although itself a case which addressed the legality of vertical market-division, cast doubt over the continued blanket application of the per se rule established for horizontal market-division agreements in \textit{Topco}.\textsuperscript{127}

\textsuperscript{120} \textit{Id.}
\textsuperscript{121} \textit{Id.}
\textsuperscript{122} \textit{Id.} The Seventh Circuit was required to consider the likelihood that the plaintiff would prevail on the merits in its decision to affirm or reverse the grant of the preliminary injunction. Although the record before the court was necessarily limited, the facts were such that the court could confidently apply the ancillary restraints doctrine. \textit{See id.} at 595.
\textsuperscript{123} \textit{Id.}
\textsuperscript{124} \textit{See supra} notes 96-97 and accompanying text. The Association argued that the lawful and legitimate purpose of providing reciprocal repair services at less than exorbitant prices justified its territory and non-affiliation restrictions. In effect, that such restraint were "ancillary" to a lawful main purpose. \textit{Id.} at 592-93.
\textsuperscript{125} \textit{General Leaseways}, 744 F.2d at 595.
\textsuperscript{126} \textit{Id.} at 591.
\textsuperscript{127} The Seventh Circuit did not address or resolve that tension, however, because the Association failed to make a plausible free-rider argument. \textit{Id.} at 593.
The Seventh Circuit next rejected the proposition that the Association’s territorial restriction was a reasonable measure intended to eliminate a free-rider effect by which multi-franchised members like General Leaseways could exploit the underpricing of reciprocal repair service. The court reasoned that lawful market-division agreements were tolerated to enable firms to safely disseminate information such as advertising and promotions. The court noted that whereas virtually nobody will pay to consume advertising or promotions, Association members charged each other for reciprocal repairs. Moreover, the court noted that as a member of the Association added franchises, it put itself in a position to expect more service calls as well as to demand more service from others.

The Seventh Circuit next examined the market-division agreement under the rationale laid down in Addyston Pipe. The court noted that although some degree of cooperation among Association members was necessary for providing reciprocal services, the connection between the restraint and the Association’s cooperation needs which would raise the restraint from merely naked to an ancillary one was missing because no plausible reason had been suggested why Association members were forbidden to compete with each other. The court thus determined that the Association’s market-division agreement was not ancillary to the reciprocal repair arrangement nor any other lawful business purpose and was most likely a per se violation of the Sherman Act.

Finally, the Seventh Circuit considered whether the preliminary injunction could be upheld if the case were decided under the rule of reason, noting that its initial per se condemnation could be incorrect. In its examination of purpose and effect, the court noted that evidence had been presented which demonstrated that where there were few truck leasing firms, prices for leases were

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128. *Id.* at 592. The court noted that this argument was “terribly speculative.” *Id.*
129. *Id.* at 592-93.
130. *Id.*
131. *Id.* at 592.
132. *Id.* at 595.
133. *Id.*
134. *Id.*
135. *Id.* at 596; see also supra note 52. The Seventh Circuit was following the example of the Tenth Circuit in Athletic National Collegiate Ass’n v. Board of Regents of the Univ. of Okla., 707 F.2d 1147, 1157 (10th Cir. 1983), *aff’d*, 104 S. Ct. 2948 (1984).
136. In economic terms, this indicated that the Association and its members had the market power to affect prices. *General Leaseways*, 744 F.2d at 596.
higher. The court reasoned that this evidence suggested a weakness of competition which tended to show that the Association had enough market power to restrain competition. Accordingly, the court found that under the rule of reason, the market-division agreement was more likely than not an unlawful restraint of trade.

ANALYSIS

The current approach utilized by most courts to assess the legality of market-division agreements begins with an initial identification of the structure by which the agreement has been implemented. Once the structure has been identified, vertical agreements are elevated to the rule of reason under Sylvania while horizontal agreements are placed in the per se category under Topco. A horizontal market-division agreement with procompetitive attributes, however, creates a tension between Sylvania and Topco. Courts have traditionally resolved the tension in two ways: by applying Topco's per se proscription or by classifying the market-division as a vertical restraint.

This method of resolving the issue has proven inadequate, especially when a procompetitive horizontal agreement is automatically placed in the per se category under the rigid Topco rule. Further, a reclassification of structure has caused many courts to strain in order to elevate a procompetitive horizontal market-division agreement to a rule of reason analysis.

The Seventh Circuit recognized in General Leaseways that

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137. General Leaseways, 744 F.2d at 596.
138. Id.
139. Id.
140. See supra note 42.
141. See supra notes 7-8 and accompanying text.
142. See supra notes 84-86 and accompanying text.
143. In West Texas Util. Co. v. Texas Elec. Serv., 470 F. Supp. 798, 831 (N.D. Texas 1979), the district court applied the per se rule to a boycott and market-division arrangement although the court noted that as to the procompetitive effects of the arrangement it was "difficult . . . to determine which pigeonhole the facts in this case belong." Id. at 831.
144. See supra notes 86-87 and accompanying text.
145. After Sylvania, courts determine the legality of vertical restraints under the rule of reason while horizontal restraints are held to be per se illegal. 433 U.S. 36 at 59. Thus, the ancillary restraints doctrine is of particular utility in elevating a procompetitive horizontal market-division agreement out of the per se category and into a rule of reason analysis. In fact, the doctrine is of particular utility for all restraints now relegated to the per se category. See supra note 4; see also R. BORK, supra note 10, at 30.
146. See supra notes 86-87 and accompanying text.
neither device is adequate. As a result, the court employed Addyston Pipe's ancillary restraint doctrine which elevates potentially procompetitive arrangements to the rule of reason category.

Although the Seventh Circuit properly endorsed the utilization of the ancillary restraints doctrine, the court correctly applied the per se rule to the horizontal market-division agreement because the agreement was not ancillary, but rather was naked in that it restricted competition and indirectly raised prices.

Application of the ancillary restraints doctrine supersedes the Topco rule presently used by most courts to assess the legality of horizontal market-division agreements. Although a horizontal market-division is more likely to be the focal point of an anticompetitive restraint than a vertical market-division, the ancillary restraints doctrine requires more than a simple identification of structure before per se condemnation is rendered. Application of the ancillary restraints doctrine may thus save a procompetitive horizontal market-division agreement which might otherwise be placed in the per se category under the rigid Topco test.

Further, the ancillary restraints doctrine eliminates the need to reclassify a procompetitive horizontal market-division as a vertical one in order to avoid the Topco rule. The doctrine correctly supposes that a horizontal market-division agreement should ultimately stand or fall on the basis of its procompetitive or anticompetitive attributes. The doctrine's fundamental criterion for lifting a horizontal market-division out of the category of per se illegality is neither its explicitness nor its implicitness, nor its horizontal or vertical nature, but its capacity for contributing to efficiency.

147. General Leaseways, 744 F.2d at 594.
148. The doctrine's fundamental criterion for lifting a horizontal market division out of the per se category is neither its explicitness nor its implicitness, nor its horizontal or vertical nature, but its capacity for contributing to efficiency. See Addyston Pipe, 85 F. at 283.
149. The ancillary restraints doctrine does not alter the substantive aspects of the rule of reason or the per se rule. See supra notes 96-97.
150. The doctrine "supersedes" the Topco rule in the sense that it does not cut short analysis after an agreement is shown to be ancillary to a lawful purpose. See R. Bork, supra note 10, at 267.
151. See supra note 41.
152. See supra note 148.
153. See supra note 87.
154. The increased consumer welfare which may result from a procompetitive market-division agreement may justify determining its legality under the rule of reason. The efficiency and welfare which may result will justify the court's time and effort. See R. Bork, supra note 10, at 29-30.
It is still necessary under the ancillary restraints doctrine for courts to distinguish between vertical and horizontal structure in order to apply the per se rule to a naked horizontal market-division agreement. The *Topco* court recognized that the per se rule provides predictability for business people and their counsel.  

Application of the per se rule has eliminated many anticompetitive market-division agreements and no doubt thousands of others have never been launched because of the overhanging threat of the rule.

The Seventh Circuit recognized in *General Leaseways* that testing the lawfulness of all horizontal market-division agreement under the rule of reason would eradicate the predictability of the per se rule and would take up considerable judicial time and effort.  

The ancillary restraints doctrine preserves the integrity of the per se rule for naked market-division agreements. Judicial time and effort is well-spent analyzing potentially procompetitive, ancillary agreements under the rule of reason.

As the increasing complexity of marketing arrangements brings challenges under the Sherman Act, such arrangements should stand or fall on the basis of their anticompetitive or procompetitive effect. The Seventh Circuit's application of the ancillary restraints doctrine in *General Leaseways* signals a change in the tenor of section 1 jurisprudence and a recognition of the ability of a horizontal market-division to contribute to productive efficiency. A rebirth

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157. *See Bork, The Rule of Reason and the Per Se Concept* (Part II), 75 YALE L.J. 373, 384-87 (1966). Bork argues that the salutary effects of the per se rule justify its use in antitrust law. He further argues that the ancillary restraints doctrine provides courts with the best device for applying a rule of reason analysis to potentially procompetitive agreements while retaining the vitality of the per se rule for naked restraints.

158. The Seventh Circuit noted that "the per se rule would collapse if every claim of economies from restricting competition, however implausible, could be used to move a horizontal agreement not to compete from the per se to the rule of reason category." *General Leaseways*, 744 F.2d 18.

159. *See supra* note 97.

160. *See supra* note 96.

161. *See supra* notes 32-35 and accompanying text.
of the ancillary restraints doctrine may soon cast doubt over the continued application of the Topco rule. The fate of the Topco decision will ultimately be determined if and when the Supreme Court sanctions and adopts the ancillary restraints doctrine.

CONCLUSION

The utility of the market-division agreement as a tool that firms can use to increase business efficiency should not be undermined by a misapplication of the antitrust laws. Since economic analysis has shown that firms in the same line of business may implement market-division agreements for procompetitive purposes, the legality of such agreements, if shown to be ancillary to a lawful purpose, should be tested under the rule of reason. The per se rule is preserved for naked horizontal market-division agreements.

The ancillary restraints doctrine presents a standard which elevates potentially procompetitive agreements to a rule of reason analysis. In General Leaseways, the Seventh Circuit took a step in the right direction by applying the ancillary restraints doctrine. Antitrust jurisprudence will become more rational as it allows economic efficiency to guide its judgment of challenged market-division agreements. The outcome of General Leaseways illustrates that the Seventh Circuit is moving in the right direction.

JEFFREY J. JARMUTH