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Assume that Defendant is a monopolist at the upstream level; that it produces a product at the downstream level; and that it also sells the upstream input to downstream competitors. Under certain circumstances, Defendant can, by reducing its downstream prices or by increasing its upstream prices, eliminate downstream competitors' margins and "squeeze" the downstream competitor out of the downstream market. That much is uncontroversial. Much more controversial is whether such conduct should be subject to scrutiny under the antitrust laws.

In Europe, the answer is yes. Under Article 82, if Defendant's combination of upstream and downstream prices eliminates margins for an equally efficient downstream competitor, the price squeeze may constitute an abuse of dominance.[1] But in the United States—as the Supreme Court recently ruled in *Pacific Bell Tel. Co. v. linkLine Communications, Inc.*[2]—the answer is no.[3] Where a defendant "has no obligation under the antitrust laws to deal with the plaintiff at wholesale," the defendant likewise has no duty to "leave . . . a 'fair' or 'adequate' margin between the wholesale price and the retail price."[4]

The Supreme Court's ruling is not uncontroversial: while academic commentary has been skeptical about price-squeeze claims,[5] the Federal Trade Commission has supported price-squeeze theory as a basis for liability.[6] Furthermore, the case for recognition of price-squeeze liability seems intuitive. By limiting price-squeeze liability to instances where a defendant reduces the margin between its upstream and

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[1] *See*, *e.g.*, Case T-271/03, Deutsche Telekom AG v. Commission of the European Communities, 2008 ECJ Eur-Lex LEXIS 634.

[2] 129 S. Ct. 1109 (2009).

[3] The Supreme Court effectively rejected a series of opinions from the lower courts recognizing price squeeze as a basis for liability under Section 2. *See* 129 S. Ct. at 1120 n.3 ; *see also*, *e.g.*, City of Anaheim v. Southern California Edison Co., 955 F.2d 1373 (9th Cir. 1992); Bonjorno v. Kaiser Aluminum & Chem. Corp., 752 F.2d 802 (3d Cir. 1984); City of Kirkwood v. Union Elec. Co., 671 F.2d 1173 (8th Cir. 1982); City of Mishawaka v. American Elec. Power Co., 616 F.2d 976 (7th Cir. 1980); United States v. Aluminum Co. of Am., 148 F.2d 416 (2d Cir. 1945).

[4] 129 S. Ct. at 1118; *see id.* at 1120.

[5] *See* PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 767 (3d ed. 2008); Dennis W. Carlton, *Should "Price Squeeze" Be a Recognized Form of Anticompetitive Conduct*, 4 J. COMPETITION L. & ECON. 271 (2008); Herbert J. Hovenkamp & Erik N. Hovenkamp, *The Viability of Antitrust Price Squeeze Claims*, Univ. of Iowa Legal Studies Research Paper No. 08-33 (July 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1156974; J. Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4 J. COMPETITION L. & ECON. 279 (2008).

[6] *See* Statement of the Federal Trade Commission at 3-4, Re: Petition for a Writ of Certiorari in Pacific Tel. Co. [sic] d/b/a AT&T California v. linkLine Communications, Inc., No. 07-512 (U.S. May 2008).

downstream prices to less than its own incremental cost of producing the downstream product, a defendant is held liable only for elimination of at least equally-efficient downstream competitors. All things being equal, it is generally better to have multiple competitors rather than just one at a given level of production, because competitive rivalry often spurs innovation and non-price competition.[7] And the downstream competitor may eventually challenge the upstream monopoly. Such a rule would seem to avoid penalizing a defendant who can demonstrate that the price squeeze is a result of the defendant's superior efficiency as a downstream producer.

Indeed, the Supreme Court did not deny that elimination of downstream rivals through a price squeeze has potential to cause the type of harm to competition that is of concern to the antitrust laws.[8] Nevertheless, the Court found that such considerations were outweighed by concerns about the negative impact of a rule subjecting price squeezes to antitrust scrutiny. The Court's analysis reflects more general concerns about rules governing unilateral conduct; concerns that appear to have gained much greater traction in the United States than they have, at least so far, in Europe. Those concerns fall under three general headings.

First, the Supreme Court's 2004 *Trinko* decision[9] emphasized the importance of preserving incentives for all competitors—including those with substantial market power—to invest and innovate. This concern goes well beyond Judge Hand's famous dictum—that "[t]he successful competitor, having been urged to compete, must not be turned upon when he wins."[10] The *Trinko* Court explained that the ability to exploit a monopoly—to charge monopoly prices—is "an important element of the free-market system."[11] More generally, the Court expressed skepticism about imposition of duties under the antitrust laws—such as affirmative duties to deal—that would require a monopolist to assist competitors. "Compelling such firms to share the source of their advantage may lessen the incentive for the monopolist, the rival, or both to invest in . . . economically beneficial facilities."[12] Investment in innovation is risky, and much of the incentive for such investment comes from the ability to earn high profits when the innovation succeeds. If rivals can piggy-back on innovative success, the incentive to innovate will be undercut.[13]

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[7] It is now understood, however, that the intuition that a monopolist can earn a greater monopoly profit by gaining a monopoly at two levels of production rather than at a single level is often mistaken—under many circumstances, there is only one "monopoly profit" to be earned, and the monopolist's interest is to maximize efficiency at each level of production, often by promoting competition among consumers of the monopoly input.

[8] *See* 129 S. Ct. at 1122.

[9] Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004).

[10] United States v. Aluminum Co. of Am., 148 F.2d 416 (2d Cir. 1945).

[11] *Trinko*, 540 U.S. at 407.

[12] *Id.* at 407-08.

[13] *See also* AT&T Corp. v. Iowa Utils. Bd., 525 U.S. 366, 429 (1999) (Breyer, J., concurring in part and dissenting in part) ("It is in the *un* shared, not in the shared, portions of the enterprise that meaningful competition would likely emerge.").

This concern is directly implicated by price-squeeze doctrine.[14] To deem a downstream producer "equally efficient" because it can match the defendant's incremental cost of production at the downstream level ignores the fact that the downstream producer is dependent on the provision of the upstream input by the defendant. Considered from a static point of view, it may seem that recognition of price-squeeze claims promises enhanced competition because it will tend to preserve rivalry at the downstream level. But considered from a dynamic point of view, a competitor-protection duty may significantly diminish the incentive of upstream competitors to invest.

There is something to be said on the other side: Price-squeeze claims are likely to arise only in circumstances where a monopolist either chose to deal voluntarily or where it was required to deal by regulation. In either case, one might think that the existence of a price squeeze would at least justify a demand for a pro-competitive explanation. In the case of voluntary dealing, if a price squeeze was treated as tantamount to a constructive refusal to deal, it might be compared to the termination of voluntary dealing that was one of the factors that led to Section 2 liability in *Aspen Skiing*,[15] a case that the Supreme Court was careful not to over-rule in *Trinko*. And in the case of dealing compelled by regulation, imposition of a price squeeze might be a way to evade regulation; imposition of price-squeeze liability thus provides "back up" for regulation that is not achieving its desired ends.

Neither suggestion is satisfactory. If a monopolist becomes responsible for the welfare of downstream rivals when it chooses to deal voluntarily, it is much less likely to deal in the first place.[16] Recognition of price-squeeze liability thus deters socially desirable voluntary dealing. And the Court in *Trinko* (and in its earlier decision in the *Discon*[17] case) has made clear that enforcement of regulatory duties to deal is a job for regulators, not antitrust courts, reflecting the fact that affirmative regulatory duties often go well beyond the generally negative duties imposed under Section 2.[18] Furthermore, the current Supreme Court has treated the existence of regulation as a reason to scale back on antitrust liability—not to expand it—both because civil antitrust rules are less flexible than regulatory remedies and because the risk of over-deterrence associated with antitrust rules is greater (reflecting the *in terrorem* effect of class action litigation, treble damages, and attorneys' fees).[19]

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[14] The Court found that "[a] straightforward application of our recent decision in *Trinko* forecloses any challenge to AT&T's *wholesale* prices." 129 S. Ct. at 1119.

[15] Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985).

[16] *See* Olympia Equip. Leasing Co. v. Western Union Tel. Co., 797 F.2d 370 (7th Cir. 1986). Lawyers who counsel clients with significant market power will be familiar with this concern.

[17] NYNEX Corp. v. Discon, Inc., 525 U.S. 128 (1998).

[18] *Trinko*, 540 U.S. at 415-16 (distinguishing between the regulatory goal of "*eliminat[ing] . . . monopolies*" and Section 2's goal of "prevent[ing] *unlawful monopolization*") (internal quotation marks omitted; emphasis in original).

[19] The four concurring Justices in *linkLine* would have treated the existence of regulation as a decisive reason to reject price-squeeze liability in the case. *See* 129 S. Ct. at 1124 (Breyer, J.) ("When a regulatory structure exists to deter and remedy anti-competitive harm, the costs of antitrust enforcement are likely to be greater than the benefits.").

Second, in crafting antitrust rules, the Supreme Court has been sensitive to institutional limitations on generalist courts. In rejecting the refusal-to-deal claims at issue in that case, *Trinko* held that antitrust laws avoid imposition of duties that would "require[] antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill suited"—or that would "require continuing supervision of a highly detailed decree."[20] While it may be relatively straightforward to articulate a particular economic test in theory—think of the famous "rule of reason" test, which is said to require weighing of competitive harms and benefits—it can be extremely difficult if not impossible for a court (and jury) to administer the test reliably.

The Court found that this concern is strongly implicated by any price-squeeze inquiry.[21] Assume for the sake of argument that an economically appropriate test for unlawful price squeeze is that the margin between the defendant's upstream and downstream prices is less than the monopolist's incremental cost of production.[22] Measuring such prices—which change over time and which may be embedded within bundles of multiple products—and costs is extremely difficult. Recognizing the difficulty, some have suggested that the issue can be dealt with by imposing price-squeeze liability only when upstream prices actually exceed downstream prices. But such a rule ignores the problem that it is not downstream *prices* that matter; it is downstream *revenues*—in many markets, a producer may have multiple sources of revenue: think of subscription revenues and advertising. That upstream *prices* exceed downstream prices may not be at all surprising. Furthermore, the rule is unprincipled: Whether the upstream price is a penny more or a penny less than the downstream price is unlikely to make any substantive difference.

Third, courts have begun to give greater recognition to the need to craft legal rules that are clear, administrable, and that are sensitive to the risk of over-deterrence.[23] One of the key insights of the "Harvard School" of antitrust analysis is that, in evaluating potential antitrust rules, courts should consider the impact of those rules on business conduct that may never be the subject of litigation.[24] That concern underlies the Supreme Court's holding in *Brooke Group*[25] that above-cost prices are *per se* lawful under

[20] *Trinko*, 540 U.S. at 408, 414-15.

[21] *See* 129 S. Ct. at 1120-22.

[22] *See* John Vickers, *Abuse of Market Power*, 115 Econ. J., F244, F251 (2005).

[23] *See*, *e.g.*, Schor v. Abbott Labs., 457 F.3d 608 (7th Cir. 2006) (Easterbrook, J.), *cert. denied*, 127 S. Ct. 1257 (2007).

[24] One of the best articulations of this concern is in then-Judge Breyer's opinion in Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 234 (1st Cir. 1983). He wrote: "while technical economic discussion helps to inform antitrust laws, those laws cannot precisely replicate the economists' (sometimes conflicting) views. For, unlike economics, law is an administrative system the effects of which depend upon the content of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients. Rules that seek to embody every economic complexity and qualification may well, through the vagaries of administration, prove counter-productive, undercutting the very economic ends they seek to serve." *See also* Town of Concord v. Boston Edison Co., 915 F.2d 17, 22 (1st Cir. 1990) (legal rules should be "designed with the knowledge that firms ultimately act, not in precise conformity with the literal language of complex rules, but in reach to what they see as the likely outcome of court proceedings").

[25] Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224 (1993).

Section 2. The point is not that above-cost prices can never eliminate competitors and lead to consumer harm—they can. Rather, it is that subjecting above-cost prices to antitrust scrutiny will discourage price cutting and therefore harm consumers in countless cases that would never find their way to court. Antitrust analysts have recognized that subjecting conduct to potential liability—even if the circumstances under which liability will be imposed seem sensibly circumscribed—will deter conduct that is lawful and desirable. And this is true even if the rate of actual false positives is low, because the costs of litigation may themselves be a substantial deterrent.[26]

Even if one was persuaded that the existence of a price squeeze might harm consumers in certain circumstances, the risk of deterrence of pro-competitive conduct is great.[27] There is no dispute that the mere existence of circumstances where the margin between a defendant's upstream and downstream prices discomfits a downstream rival often reflects the integrated defendant's desirable efficiencies or pro-competitive responses to demand conditions. If all such squeezes are subject to scrutiny, a potential defendant will know that a reduction in the margin between upstream and downstream prices may lead to litigation, with guaranteed expense and no guarantee of a correct outcome.

The conduct that is likely to be deterred, furthermore, brings both immediate consumer benefit and long-term efficiency. First, recognition of price-squeeze claims exerts pressure on a vertically-integrated monopolist to keep its downstream retail prices high. Even if superior efficiency was a justification for a price squeeze, it would always be difficult for an adjudicator to distinguish a price squeeze resulting from such efficiency from a price squeeze resulting from supposedly excessive wholesale prices. Second, subjecting a wholesale monopolist to potential liability for a price squeeze would deter efficient vertical integration and socially desirable, voluntary dealing. A monopolist might offer an upstream product, used by another firm to produce a downstream product. If the monopolist begins to produce the downstream product itself, it might well face the prospect of price-squeeze litigation brought by the current downstream producer. Such a possibility might either deter the monopolist from entering the downstream market (even in cases where it would be more efficient than existing rivals) or deter the monopolist from selling to downstream producers in the first place.

The foregoing concerns are prominent in the *linkLine* decision, where the Court "emphasized the importance of clear rules in antitrust law."[28] As the Court recognized, the focus of the price-squeeze theory—which is on the margin between upstream and

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[26] *See generally* David S. Evans & A. Jorge Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. CHI. L. REV. 73, 81 (2005).

[27] *See* 129 S. Ct. at 1120 ("In cases seeking to impose antitrust liability for prices that are too low, mistaken inferences are 'especially costly, because they chill the very conduct the antitrust laws are designed to protect.'") (quoting Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 594 (1986)).

[28] 129 S. Ct. at 1120-21.

downstream prices and the impact on competitors—is all wrong. If the existence of a price squeeze is of competitive significance, it is only in circumstances where the defendant has a duty to deal under the antitrust laws, and where the price squeeze constitutes a constructive refusal to deal.[29] But such cases are much better dealt with under the law governing refusals to deal, which is both narrow in scope and (at least under the test that the Court suggested in *Trinko*) relatively administrable.[30]

[29] *See* EINER ELHAUGE & DAMIEN GERADIN, GLOBAL ANTITRUST LAW AND ECONOMICS 458 (2007).

[30] *See* 129 S. Ct. at 1122 (noting that there is no "independent competitive harm caused by price squeeze above and beyond the harm that would result from a duty-to-deal violation at the wholesale level or predatory pricing at the wholesale level"). For example, there would be no good argument for imposition of price-squeeze liability in a circumstance where a defendant continued to make a given input available to all buyers (for use in multiple downstream products) but reduced the price of one downstream product below the incremental cost of production. Imposition of liability in such a case would not only discourage voluntary dealings with the producers of the particular downstream product at issue, but would also discourage voluntary dealing with producers of *other* downstream products. *See* Carlton, *supra* n.5 at 276-77.