THE NEO-BRANDEISIAN APPROACH TO VERTICAL MERGERS – A ZIPLINE TO OBLIVION?

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THE NEO-BRANDEISIAN APPROACH TO VERTICAL MERGERS – A ZIPLINE TO OBLIVION?

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In a major policy switch, federal antitrust agencies recently announced increased hostility to vertical mergers. Stated reasons include skepticism of their benefits and of remedies traditionally used to control their competitive risks. Based on the long enforcement history involving vertical mergers, the agencies' concerns are materially overstated. Since February 2022, agency litigation threats led to voluntary termination of several deals, but the agencies lost both of the other cases that were tried. While subject to further appeal, the meticulous reasoning of each seems persuasive. When mergers do not involve competitors and the parties offer plausible business justifications, it takes sophisticated analysis, strong factual support and effective advocacy to explain to an objective decision maker why they pose antitrust concerns sufficient to justify prohibition. The agencies should consider the lessons of their recent defeats. Any new vertical merger policy should be based on a balanced, thorough and realistic assessment of the key relevant considerations: the competitive risks of vertical transactions, their potential competitive benefits, and the availability of limited conduct remedies to address the second-order competitive issues present in some transactions.

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I. INTRODUCTION

Neo-Brandeisians now have full control of both federal antitrust agencies, with strong support from Congressional Democrats, the President, and an amen corner of NGO's (among others). Almost halfway through the Biden Administration, it is now obvious that agency leadership regards vertical integration with far greater and more consistent hostility than any administration in living memory. The agencies' recent hot pursuit of vertical cases has become a significant element of the Neo-Brandeisian mutiny against the broader antitrust consensus that has prevailed in the half-century since *General Dynamics,*[2] *Sylvania*[3] *and Brunswick.*[4] President Biden acknowledges that the U.S. has become "the wealthiest, most innovative nation in history,"[5] yet he has denounced the longstanding antitrust consensus as an "experiment" that "failed," blaming it on "people like Robert Bork."[6]

Without seeking public input (and, at least in the FTC's case, apparently without consulting its own professional staff) on September 23, 2021 the agencies summarily rescinded their joint Vertical Merger Guidelines issued in June, 2020.[7] The FTC also withdrew the associated Commentary on Vertical Merger Enforcement that it had published in December, 2020. As a part of their effort to rewrite the current Horizontal Merger Guidelines (announced January 18, 2022), the agencies signaled their intent to revisit vertical merger analysis as well. If the official speeches and recent merger challenges are any indication, the entire effort seems like a zipline to oblivion. Assuming that the critical substance of Clayton Act Section 7 (last amended in 1950) will apply for the foreseeable future, the agencies should carefully reflect on the potential consequences of their present course.

They might wish to acknowledge why merger enforcement shifted in the 1970's, from heavy reliance on a simplistic (and flawed) structure/conduct/performance paradigm and invocation of vague political themes (e.g. "fairness," protection of small businesses in spite of economic cost) to case-by-case analysis based on sound theoretical and empirically-supported economics as provided in recent versions of the merger guidelines. Extensive scholarly analysis and years of open debate regarding merger enforcement had exposed serious weaknesses in the pre-*General Dynamics* approach. The agencies would do well to ensure that future merger guidelines adopt an economically sound and fact-based approach with regard to vertical transactions, keeping agency policy within hailing distance of well-regarded precedents and mainstream understandings.[8]

The Vertical Guidelines and Commentary attempted to distill lessons learned from years of previous analysis and enforcement experience, as explained by courts, scholars of law and economics, enforcers, practitioners and others in the antitrust community. It has long been recognized that there are few simple objective tests that allow confident predictions of the competitive effects of vertical transactions. Traditional reliance on key market structure variables – concentration, barriers to entry, product differentiation, transaction characteristics and the like – can be of some help with regard to horizontal transactions, where loss of direct competition is a central concern. But these guideposts may not be especially useful for vertical transactions. Such transactions do not reduce the number of direct competitors, so more sophisticated theorizing is required about how vertical deals can inhibit competition.

Many mechanisms have been proposed as potential sources of competitive restraint from vertical transactions – facilitation of cartel activity (e.g. by improving access to information required to monitor and enforce cartel agreements), regulatory evasion, or price discrimination (where such discrimination is likely anticompetitive). Antitrust literature is rich with existence theorems regarding conditions in which vertical

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2 *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974).

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

4 *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977).

5 @POTUS, Sept. 27, 2022.

6 White House, Remarks by President Biden At Signing of An Executive Order Promoting Competition in the American Economy, July 9, 2021, available at https://www.whitehouse.gov/briefing-room/speeches-remarks/2021/07/09/remarks-by-president-biden-at-signing-of-an-executive-order-promoting-competition-in-the-american-economy/. For this purpose, "people like Robert Bork" would include former Supreme Court Justices Ruth Bader Ginsburg and Stephen Breyer, as well as Donald Turner (Lyndon Johnson's first AAG for antitrust) among many other respected antitrust experts and agency officials (economists and lawyers) of both political parties who for many years have supported the use of sound, fact-based economic analysis in antitrust enforcement.

7 https://www.ftc.gov/news-events/news/press-releases/2021/09/federal-trade-commission-withdraws-vertical-merger-guidelines-commentary.

8 The most recent plenary Supreme Court decision on the analysis of the competitive effects of mergers as required by Section 7 goes all the way back to *General Dynamics, supra* note 2, and *United States v. Marine Bancorporation, Inc.*, 418 U.S. 602 (1974). A substantial lower-court jurisprudence, exemplified by *United States v. Baker Hughes, Inc.*, 908 F.2d 981 (D.C. Cir. 1990) (opinion by Thomas, J. joined by Ginsburg, J.), tethers merger analysis to the fundamentals of post-*General Dynamics* Supreme Court antitrust decisions.

transactions might restrict competition, but there are few shortcuts available to determine their realism and accuracy in specific cases. Antitrust enforcers and courts are condemned to muddle through, forced to engage in fact-based case-by-case analysis in order to reach outcomes that make sense in vertical cases.

Brown Shoe[9] – an early Supreme Court case that applied the current version of Clayton Act Section 7 to a transaction with both horizontal and vertical aspects – focused on "foreclosure" in the elementary sense of limits that might be set by a vertically integrated firm on sales/purchases to/from a competing downstream/upstream firm. *Brown Shoe* clearly stated, however, that mere foreclosure (unless at one or the other extreme of *de minimis* or monopoly levels) is not determinative in evaluating future competitive effects of vertical transactions.[10] In closely related substantive areas involving this same type of potential foreclosure – requirements contracts, exclusive dealing – a rule of reason is applied and the *competitive effect* of a substantial foreclosure (as distinct from mere loss of opportunity to transact) is the key consideration.[11] Nevertheless, *Brown Shoe* condemned a transaction involving minimal foreclosure, with no sinister element other than the possibility that in the relevant sector, "a cumulative series of vertical mergers . . . if left unchecked, will be likely 'substantially to lessen competition.'" [12] By so doing, it suggested a strong presumption against vertical combinations, since many industries might be susceptible to such a development. How would parties to a vertical transaction rebut government speculation that a future "unchecked" vertical merger trend "will be likely substantially to lessen competition"?

Aside from doubts that such fortune telling could or should satisfy the government's statutory burden to prove a sufficient likelihood of substantial anticompetitive effect, the idea of a presumption against vertical transactions seems especially questionable in light of the settled principle that anticompetitive use of vertical control can be challenged at the time of suit (even decades after the vertical acquisition that produced such control, without regard to any statute of limitations).[13] This should render it unnecessary for courts to speculate about future competitive conduct at the time of acquisition if there is concern regarding future anticompetitive foreclosure.

As mentioned above, it is well recognized that trying to specify objective circumstances in which vertical transactions create unacceptable anticompetitive risks is a treacherous area because there are few reliable quantitative landmarks, a bewildering variety of speculative theories of harm, and mixed historical evidence regarding the effects of vertical transactions. In rescinding the Vertical Guidelines and Commentary, the agencies have abandoned the prior approach based on claims that the Guidelines and Commentary are imperfect, without offering any alternative analysis. In various statements on the subject, the mutineers reject consideration of efficiencies, or heavily discount their existence and/or magnitude. They downplay or ignore that over the long course of U.S. industrial history problematic vertical transactions are rare compared to problematic horizontal transactions, and they question the reality and significance of "elimination of double marginalization," ignoring other obvious rationales for vertical acquisitions (discussed below) even where double marginalization may not be significant.

The long history of antitrust enforcement suggests resources should be focused on horizontal rather than vertical transactions. It is easy to identify major horizontal combinations that occurred during the Second Industrial Revolution – before there were any effective legal constraints on such conduct – whose anticompetitive effects demonstrated the danger of competitor combinations. Formation of the Standard Oil Company, the American Tobacco Company, the Sugar Trust, and the Whiskey Trust, for example, were important developments whose impact inspired support for efforts to enact and enforce the Sherman Act. Standard Oil and American Tobacco were dissolved as a result of groundbreaking antitrust prosecutions in the early 20th Century Progressive Era. Some question whether these prosecutions were helpful on balance, but the present mainstream view, based on a century of debate, seems to be that these cases appropriately terminated mergers to monopoly and/or cartel arrangements – unvarnished anticompetitive conduct. This seems true even for *Standard Oil* – a case that did not receive a persuasive rationale until 1996.[14] Although now so obvious that one rarely stops to consider it, the clarity of the prohibition on merger to monopoly has essentially extinguished any realistic possibility that under normal conditions, well-advised business enterprises operating subject to U.S. antitrust jurisdiction would attempt it.

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9 *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962).

10 *Id.* at 329.

11 *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2 (1984); Tampa Electric Co. v. Nashville Coal Co., 365 U. S. 320 (1961).

12 *Id.* at 334. It bears pointing out that shoe manufacturing fled the United States at about this time, with mid-20th Century industry employment of around 250,000 declining drastically. At the same time the Antitrust Division aggressively prosecuted the leading shoe machinery supplier, United Shoe Machinery Corp. of Beverly, Massachusetts, ultimately leading to Supreme Court-mandated dissolution of the firm. 98-99% of shoes sold in the U.S. are now imported.

13 *United States v. E. I. du Pont de Nemours Co.*, 353 U.S. 586 (1957) (automotive finishes). The wisdom of this rule has been questioned, but *Brown Shoe* was decided only five years after *du Pont.*

14 Elizabeth Granitz & Benjamin Klein, Monopolization by "Raising Rivals' Costs": The Standard Oil Case, 39 J.L. & Econ. 1 (1996) (demonstrating that the key anticompetitive behavior consisted of Standard Oil's agreement to allocate petroleum shipments in accord with railroad cartel agreements, in return for railroad imposition of exclusionary rates and other terms of service on Standard Oil's competitors).

By contrast, infrequent antitrust prosecutions resulting in break-ups aimed at vertical integration have not proven especially effective in improving competition in the affected markets. The *Paramount Decrees*[15], which sliced the motion picture industry into separate tranches including film production, distribution and exhibition; the *Meatpackers Decree*,[16] separating meatpacking from other lines of business (including, *inter alia*, stockyards, transportation and communication services and facilities associated with livestock markets, and meat retailing); and the *Network Decrees*,[17] requiring television networks to allocate production of a specified portion of their programming inputs to unaffiliated suppliers, have produced questionable competitive benefits, if any. Even for vertical cases that result in major industry restructuring, it is difficult to discern whether competition was ultimately enhanced.[18]

The recent shift in the agencies' approach to vertical mergers was anticipated in at least one key respect during the Trump Administration. Soon after his investiture as AAG for Antitrust in 2017, Makan Delrahim – who otherwise generally maintained merger enforcement and other antitrust policies within the prevailing post-*General Dynamics* mainstream – chose a high-profile setting in which to declare strong antipathy to the use of conduct restrictions as a form of antitrust remedy, calling specific attention to vertical transactions.[19] This back-footed the antitrust bar, given the long-standing and common practice of settling vertical cases by having parties submit to conduct limitations addressing any narrow competitive concerns.

The practice has long been based on the accepted realities that (1) competitive concerns with vertical deals have been rare (since as defined they do not involve the elimination of direct competition, and correction for Type II error in a vertical context is in principle available at time of suit, at least where foreclosure is a main concern) and (2) experience powerfully suggests that conduct remedies – although challenging to implement, especially where continuing enforcement is required – can be justified if relatively limited decree provisions seem likely to limit any risks while preserving the substantial benefits characteristically associated with vertical transactions. By strongly asserting an aversion to conduct remedies, AAG Delrahim was setting up a major change in enforcement policy toward vertical transactions. Perhaps not widely anticipated at the time, the potential combination of antipathy to conduct remedies with a Neo-Brandeisian emphasis on competitive risks of vertical transactions coupled with rejection of recognized procompetitive aspects of such combinations might imply frequent or even per se opposition to such transactions.

AAG Delrahim's shift anticipated an Antitrust Division challenge to AT&T's acquisition of Time Warner. The Division's request for injunction was rejected by a district judge with significant recent experience in a similar matter: in 2011 the judge had approved an antitrust consent decree permitting NBC Universal (entertainment supplier) to combine with Comcast (entertainment distributor), subject to conduct relief. The remedy followed a classic anti-foreclosure remedy model, establishing mechanisms to resolve disputes arising from a potential future denial of

15 There have been numerous antitrust challenges to alleged horizontal and vertical competitive practices of the motion picture industry. Following Supreme Court affirmance of a district court decision condemning a variety of such practices, *United States v. Paramount Pictures, Inc.*, 334 U.S. 131 (1948), the defendant firms entered into consent decrees that imposed numerous restrictions on their vertical scope (in addition to conduct restrictions). Efforts to modify or vacate these decrees have extended almost to the present day, with the decrees finally scheduled to terminate, pursuant to court order, only two months prior to this writing. *United States v. Paramount Pictures, Inc.*, Order in Case 1:19-mc-00544-AT (S.D.N.Y. Aug. 7, 2020) (decrees terminated subject to a two-year "sunset period" for certain prohibitions). Although the decrees still have their supporters, evidence that the vertical limitations had any positive competitive impact is mixed at best.

16 The *Meatpackers Decree* has a long and complex history originating with complaints about industry practices that predate the Sherman Act. A government antitrust complaint impending in 1919 (based on a report on the industry compiled by the FTC at Presidential Wilson's request) was settled with entry of an industry-wide consent decree in 1920, followed by enactment of closely related regulatory legislation in 1921 (Packers and Stockyards Act). More than a half-century of court proceedings involving interpretation of and proposed modifications to the Decree followed. See e.g. *United States v. Armour & Co.*, 402 U.S. 673 (1971). The Decree was terminated on joint motion of the parties in 1982, *United States v. Swift & Co.*, 1982-1 Trade Cas. (CCH) 64,464 (N.D. Ill. 1981), although regulation of and continuing antitrust action against the industry remains ongoing.

17 These decrees were entered in 1978-1981 in settlement of Antitrust Division litigation against the three major broadcasting networks, essentially regulating certain forms of integration and contractual relationships with suppliers of broadcast content. Similar to the relationship between the *Meatpackers Decree* and the Packers and Stockyards Act, there was a parallel scheme of Federal Communications Commission regulation of broadcasters governing much of the same subject matter addressed in the decrees. The *Network Decrees* were substantially modified in 1993. *United States v. National Broadcasting Co., Inc.* (Case No. CV74-3601-R); United States v. American Broadcasting Companies, Inc. (Case No. CV74-3600-R); *United States v. CBS, Inc.* (Case No. CV74-3599-R) (C.D. Cal., November 10, 1993).

18 Arguably the break-up of the former Bell System by consent decree after years of litigation can be placed in a category of non-horizontal divestitures that ultimately led to significant procompetitive results. This case also involved important parallel developments in telecommunications regulation at both federal and state levels (e.g. FCC administration of a scheme of "access tariffs" governing the rates, terms and conditions upon which competing long-distance telecommunications carriers would obtain interconnections to local telephone systems). The persistence of major unresolved issues following the divestiture and during the administration of the decree eventually elicited Congressional intervention through the Telecommunications Act of 1996, pursuant to which the decree court was required to vacate the antitrust remedy.

19 Assistant Attorney General Makan Delrahim Delivers Keynote Address at American Bar Association's Antitrust Fall Forum (November 16, 2017). https://www.justice.gov/opa/speech/assistant-attorney-general-makan-delrahim-delivers-keynote-address-american-bar

> "At the beginning of the last administration, the Division entered into several behavioral consent decrees to resolve vertical mergers it determined to be illegal, such as those in *Comcast/NBCU, Google/ITA, and LiveNation/TicketMaster.* Several observers took issue with this regulatory approach to antitrust enforcement . . ..
>
> "I agree with that skepticism. . .."

distribution competitors' access to content (actual or constructive) provided by the combined firm. So far as public sources disclose, however, only a single material dispute occurred during the decree's seven-year initial period. Arguably this may have been among the reasons why the Antitrust Division did not request extension of the *NBC Universal/Comcast* decree, even though the litigation against *AT&T/Time Warner* was pending. Reportedly the Division did wag a finger at *NBC Universal/Comcast*, stating its intent to maintain a watching brief on future conduct, presumably to inspire some degree of continuing constraint on the firm.[20]

In June 2018 the same judge who had approved and then presided over implementation of the *NBC Universal/Comcast* decree rejected the Division's request to enjoin *AT&T/Time Warner*. The D.C. Circuit affirmed in February 2019, and the Division then abandoned the case. The sky failed to fall as the Division had predicted, however, and only two years later AT&T, newly focused on the suddenly white-hot world of content-streaming, announced a spin-off of its recently acquired affiliate.

The Neo-Brandeisians are apparently undeterred by either the demonstrated judicial skepticism of the Division's recent apostasy regarding conduct remedies, or by the Division's loss in the challenge against *AT&T/Time Warner*. The Neo-Brandeisians have effectively discouraged a number of significant vertical transactions submitted for HSR review (*Nvidia/ARM, Lockheed Martin/Aerojet Rocketdyne*), but they are now 0 and 2 on litigated vertical cases (the FTC administrative complaint against *Illumina/Grail* and the Antitrust Division complaint against *UnitedHealth Group/Change Healthcare*), although the game is far from over: one decision by an FTC ALJ has been appealed to the full Commission by staff, and the other, a district court decision, remains subject to appeal by the Division. I limit the discussion to the *Illumina/Grail* case, but the district court decision in the *UnitedHealth Group/Change Healthcare* matter is worth reading since, like the ALJ Initial Decision in *Illumina/Grail*, it systematically and effectively explains why the government complaint does not justify any finding of illegality.

The FTC case challenges an acquisition by Illumina, the leader in what is called "Next-Generation Sequencing" ("NGS") – a system for deciphering human genetic code. Illumina's technology is reported to have increased the speed and reduced the cost of genetic sequencing by multiple orders of magnitude, opening up many new approaches to the fight against various diseases, specifically including cancer, the second-leading cause of death in the U.S. Illumina proposed to reacquire an entity it had partially spun off to pursue research on early cancer detection technologies enabled by Illumina's NGS. The spin-off, "Grail" (as in the Holy Grail of early cancer detection), fulfilled its sponsor's expectations by developing a prototype test that might detect with a single blood draw as many as 50 forms of cancer, most of which have no other viable early detection protocol (and which therefore are not diagnosed until treatment is less likely to succeed). The field of play is referred to as MCED – multi-cancer early detection. But there are no FDA-approved products as of yet and therefore no "market."

Grail then faced the realty of conducting a costly and complex multiyear campaign to persuade the FDA to grant necessary approvals, to obtain commercially critical assurances that services and treatments based on the technology would be reimbursable (by health insurers including Medicare/Medicaid, *inter alia*) and to produce, distribute and market all required elements of any MCED offering. Although Grail was considering an IPO to finance these major long-term efforts, Illumina (still a minority owner in Grail) proposed a recombination instead, which Grail accepted. The FTC attacked the transaction, claiming that Illumina would thereby gain the incentive and ability to deprive potential future competitors (at the Grail level) of equal access to Illumina's NGS offerings.

The FTC's *Illumina* complaint has far-reaching negative implications for competition and innovation. The substance of FTC's approach powerfully suggests *per se* illegality for downstream vertical integration by firms with superior technology or other competitive advantages. The key allegation seems to be that a post-merger *Illumina/Grail* will control access to its unique NGS technology by any later-emergent MCED competitors and is likely to exclude or limit them by denial of access or imposition of unfavorable transaction terms for its system and its enabling technology. The key objections to this story start with the fact that any firm should be permitted to control its own proprietary technology (if it has any) by choosing the parties with whom it will deal, and by setting prices and other terms and conditions for transactions with customers, licensees and other similarly situated parties. These are inherent and indispensable features of being a distinct business entity in a market system that *encourages* the development of unique advantages (a/k/a, competition on the merits, superior skill, foresight and industry, etc.).

Perhaps Illumina has stumbled into a narrow and unique sector with characteristics that justify regulation, but Congress should make any such judgment and establish an appropriate regulatory framework. Possession of superior technology is not an antitrust problem in any event, and antitrust institutions (law enforcement agencies and courts) are poorly equipped to set terms and conditions for compelled dealings, particularly when Congress has not identified either the key tradeoffs or the required regulatory mechanisms. As Justice Brandeis put it in dissent to a 1918 decision creating judicial protection for uncopyrighted news content:

20 Dawn C. Chmielewski, "DOJ Notifies Comcast It Will Continue to Keep an Eye on The Company — Report," Deadline (Aug. 30, 2018); https://deadline.com/2018/08/doj-comcast-scrutiny-continue-post-consent-decree-nbcu-1202455013/.

"Courts are ill-equipped to make the investigations which should precede a determination of the limitations which should be set upon any property right in news or of the circumstances under which news gathered by a private agency should be deemed affected with a public interest. Courts would be powerless to prescribe the detailed regulations essential to full enjoyment of the rights conferred or to introduce the machinery required for enforcement of such regulations."[21]

Although Illumina's advantages are not based primarily on copyright, the institutional objections to judicial implementation and management of the terms and conditions upon which Illumina would be required to provide its system to independent parties are identical. Courts are not equipped to identify industries and firms that are candidates for regulation and then impose and administer specific regulatory requirements that they deem appropriate; the fundamental judgments regarding the need for regulation are legislative questions for Congress, as are related questions regarding the design and implementation of appropriate instrumentalities for administration of any regulatory scheme.

Since Illumina could choose to license an independent Grail only, and thereby exclude competitors at that level, how does a combination change competition at either level (NGS or products and services relying on NGS)? Is the Commission suggesting that a firm with superior competitive abilities selling to multiple downstream outlets should be forced to provide different prices and terms than in the case where the firm has integrated downstream? And even if lower prices/more favorable terms were to result, what is the antitrust injury involved in the parties' election to integrate?

The Commission's approach seems to echo earlier cases such as *Otter Tail*[22] where the government's antitrust theory would require courts to force the superior firm to provide access on specified prices and terms to customers (as determined by the Federal Power Commission, in *Otter Tail*), but without identifiable competitive benefit at either level of commerce. In *Otter Tail* the problem was that both upstream (wholesale production and transmission of electricity) and downstream (retail distribution of electricity) levels were destined to be monopolies (due to federal regulation upstream and state regulation downstream) under any foreseeable outcome. In this case nothing will change the fact that Illumina controls technology that is essential to the full market development of Grail or any MCED competitor relying on Illumina's NGS.

Another fundamental point that the Commission might have considered is that there is no accepted formula that can predict relationships among structure, competition and innovation. On what basis, therefore, does the Commission assert that vertical integration by a firm like Illumina is likely to suppress innovation? Given the broad and longstanding recognition that the majority of long-run economic growth is attributable to technical improvements, scholars have focused on the structure/competition/innovation relationship, but research and debate are inconclusive. In any event, there is no widely accepted understanding that an innovator is more likely to succeed if it utilizes only independent routes to market, as distinct from relying on resources internal to the firm (i.e. a combined Illumina-Grail). Illumina might also pursue hybrid approaches following acquisition of Grail, encouraging other independent licensees of its NGS technology to pursue other applications. One can imagine outcomes involving reliance on downstream and complimentary resources that are internal, external, or a combination of both, but it is difficult to imagine why an antitrust agency would have a better assessment of the possibilities than the party that developed the technology, considering that the innovator has powerful incentives to promote widespread downstream utilization of its technology.

The Neo-Brandeisian views underlying the *Illumina/Grail* complaint minimize other antitrust policy considerations relevant to vertical integration. As suggested above, the agencies question efficiencies of vertical integration and specifically view elimination of double marginalization as exaggerated. Elimination of double marginalization, however, may not be determinative because there are other economic aspects of vertical integration that need not even relate to double marginalization. Every enterprise, without exception, must select the range of its activities: should a steel producer also mine its inputs, and/or fabricate products (in addition to raw steel)? There are clear objective elements to the make-buy decision: a classic example (used by George Stigler to discuss fundamental scope-of-the-firm issues going back to Adam Smith[23]) is the combination of steel production with steel product fabrication. Steel ingot made by a non-integrated producer will have to be reheated to allow end-product fabrication, whereas the integrated producer can avoid the expense and burden of facilities, operations and energy for reheating. Even if both steel production and fabrication were perfectly competitive (i.e. no EDM) there would be a cost minimization rationale for integration between the two stages. There may be transactional/administrative advantages to integration as well.

There are myriad similar considerations – related to every stage and every element of productive activity – that might influence the firm's choice of functional scope, even apart from EDM. Transactional structure and relative monitoring and enforcement costs as between

21 *International News Service v. Associated Press*, 248 U.S. 215, 267 (1918) (dissent of Justice Brandeis). This federal common-law approach, more characteristic at the time, was nullified along with other federal common-law doctrines by *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938). Concern with the judiciary's lack of capacity to fashion and administer decrees (without legislative authorization) imposing regulatory obligations on firms with unique competitive resources remains a major theme of modern antitrust cases. *Verizon Communications, Inc. v. Trinko, LLP*, 540 U.S. 398 (2004).

22 Otter Tail Power Co. v. United States, 410 U.S. 366 (1973).

23 George J. Stigler, The Division of Labor is Limited by the Extent of the Market, 59 J. Pol. Econ. 185 (1951).

market versus internal transactions may also be influential. To suggest that there must be serious antitrust review for every instance in which the firm seeks to acquire rather than "grow" a new function organically would burden vast numbers of transactions when only a tiny handful are ultimately likely to be considered problematic. The enormous diversity of the relevant considerations and the great number and complexity of the business issues surrounding the decision to "make or buy" mean that any antitrust threat to the exercise of business judgment regarding this fundamental issue may lead to the classic "chilling effect" – having to balance every business decision against the risk of provoking investigation or challenge by government agencies or by private attorneys general. The lack of any convenient analytical short-cut by which the agencies could second-guess business judgments on these questions strongly suggests that agency efforts to conduct an economy-wide dragnet to review run-of-mill vertical transactions would constitute extreme overkill.

The mutineers' doubts about efficiency and EDM in vertical transactions echo previous arguments challenging the competitive merits of vertical agreements in an earlier era. Among many procompetitive rationales cited for vertical agreements is prevention of free riding – encouraging downstream entities to make output-enhancing investments by steering rewards to those who actually invest. Opponents of vertical agreements sometimes attacked the validity of this rationale as if the merits of having a rule-of-reason approach depended on whether such a rationale applied in every case.

This was and remains a flawed approach to vertical restraints. Since vertical agreements only rarely implicate competitive concerns directly, it is doubtful that extensive review, investigation and/or legal challenge of the general run of such agreements could be justified as an appropriate use of enforcement resources. Just as with vertical acquisitions, there may well be circumstances in which competitive concern is justified. But without a realistic picture of the frequency and significance of such instances, enforcement policy is unguided. If efficiencies don't exist or are never enough to justify vertical integration, and if behavioral remedies are always pointless or guaranteed to be ineffective, we may as well build an enforcement machine without an off switch – a solution appropriate only for hard-core cartel behavior. That is no way to make antitrust policy for run-of-mill vertical acquisitions.

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