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A MICRO-MICROECONOMIC APPROACH TO ANTITRUST LAW: GAMES MANAGERS PLAY

Harry S. Gerla*

Classical microeconomic theory (sometimes known as Chicago School Economics) has become the dominant tool for contemporary antitrust analysis.¹ In the academic realm, no instructor could in good conscience ignore the antitrust views of the Chicago School.² Classical microeconomics has also gained great influence among antitrust courts.³ Indeed, judicial acceptance of the Chicago School's version of antitrust law and economics may have reached a new high-water mark with the Supreme Court's recent decision in *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*⁴

In *Matsushita*, American electronic manufacturers claimed that their Japanese rivals conspired to take over the American consumer electronics market by agreeing to maintain artificially high prices in the Japanese home market while maintaining predatorily low prices in

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1. See, e.g., Gerhart, *The Supreme Court and Antitrust Analysis: The (Near) Triumph of the Chicago School*, 1982 SUP. CT. REV. 319; Sullivan, *The Economic Jurisprudence of the Burger Court's Antitrust Policy: The First Thirteen Years*, 58 NOTRE DAME L. REV. 1 (1982); Markovits, *The Burger Court and Antitrust Analysis*, in THE BURGER COURT 182 (V. Blasi ed. 1983).

The terms "microeconomics," "classical microeconomics," and "Chicago School Economics" are used interchangeably throughout this article. As far as antitrust law and policy are concerned, the two primary articles of faith of Chicago School Economics are (1) that overall wealth maximization (regardless of distributional consequences) should be the sole goal of the antitrust laws, and (2) classical microeconomics, also known as price theory, is the only useful tool for determining if wealth is being maximized. See Hovenkamp, *Antitrust Policy After Chicago*, 84 MICH. L. REV. 213, 226 (1985). For a more extended exposition of the Chicago School's view, see R. BORK, *THE ANTITRUST PARADOX* (1978); and Posner, *The Chicago School of Antitrust Analysis*, 127 U. PA. L. REV. 925 (1979).

2. Gellhorn & Robinson, *The Role of Economic Analysis in Legal Education*, 33 J. LEGAL ED. 247, 255 (1983).

3. See, e.g., *Continental T.V. v. GTE Sylvania, Inc.*, 433 U.S. 36, 55-56 (1977); *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 221-22 (D.C. Cir. 1986), *cert. denied*, 107 S. Ct. 880 (1987); *Business Elec. Corp. v. Sharp Elec. Corp.*, 780 F.2d 1212, 1221-22 (5th Cir. 1986) (Jones, J., concurring), *cert. granted*, 107 S. Ct. 3182 (1987); *Will v. Comprehensive Accounting Corp.*, 776 F.2d 665, 671 (7th Cir. 1985), *cert. denied*, 475 U.S. 1129 (1986).

4. 475 U.S. 574 (1986), *rev'd*. In re Japanese Elec. Prods. Antitrust Litig., 723 F.2d 238 (3d Cir. 1983), *aff'd*. *Zenith Radio Corp. v. Matsushita Elec. Indus. Co.*, 513 F. Supp. 1100 (E.D. Pa. 1981).

the American market.⁵ The Supreme Court reversed the United States Court of Appeals for the Third Circuit and upheld the district court's summary judgment decision in favor of the defendants.⁶ What is significant about the majority opinion in *Matsushita* is that it utilized the abstract principles of classical microeconomics to conclude that the plaintiffs' claim in the case was implausible and thus subject to dismissal on motion for summary judgment.⁷ In doing so, the Court ignored plaintiffs' evidence that defendants had initiated a predatory pricing conspiracy: "[E]xpert opinion evidence of below-cost pricing has little probative value in comparison with the economic factors . . . that suggest that such conduct is irrational."⁸

Thus, in *Matsushita* the Court adopted the essential reasoning of modern microeconomics. This reasoning begins with the assumptions that firms have as their prime goal the maximization of profits and that they will act rationally in pursuit of that goal.⁹ According to some Chicago School economists, predatory pricing is not a rational method of maximizing profits.¹⁰ The inexorable conclusion under this view is that the real-life firms in *Matsushita* did not engage in predatory pricing.

The central weakness of both classical microeconomic theory in general and the analytical approach employed by the majority opinion in *Matsushita* in particular is that both overlook an obvious point. Firms cannot act on their own. The actions of firms are the actions of the human beings who act as their managers.¹¹ The prime objective of these managers is the advancement of their careers. The styles and methods of contemporary American management often lead to a conflict between the steps necessary (or perceived as necessary) to advance a manager's career and the steps needed to ensure the long-run success of the manager's employer.¹² In the face of such a conflict, it would take a saint to pick the latter course, and saints are in as short supply

5. 475 U.S. at 577-78.

6. 475 U.S. at 576-77.

7. 475 U.S. at 588-95.

8. 475 U.S. at 594 n.19.

9. See, e.g., Flynn, *Appendix: Definitions and Assumptions of Economic Analysis*, 12 Sw. U. L. REV. 361, 369-70 (1981); Hovenkamp, *supra* note 1, at 228.

10. E.g., R. BORK, *supra* note 1, at 149-55; Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263, 264-65 (1981); McGee, *Predatory Pricing Revisited*, 23 J.L. & ECON. 289, 294-300 (1980). The Court in *Matsushita* relied on these authorities to conclude that the plaintiffs' claim of a predatory pricing scheme was implausible as a matter of law. 475 U.S. at 588-90.

11. See M. GREEN & J. BERRY, *THE CHALLENGE OF HIDDEN PROFITS: REDUCING CORPORATE BUREAUCRACY AND WASTE* 13-14 (1985).

12. See Part I *infra*.

among management as they are among the rest of humanity. Classical microeconomic theory, with its operative assumption of rational, profit-maximizing firms, ignores this messy reality. As a consequence, predictions of the effects of antitrust laws and policies derived from classical microeconomic theory are often simply wrong.¹³

If we are to gain an accurate perspective on the impact of antitrust laws and policies on the behavior of firms in the real world, we must adopt a micro-microeconomic approach which focuses not on how rational, profit-maximizing firms will theoretically behave, but upon how late twentieth-century American managers and executives actually behave. This article attempts to begin that task.

Part I of this article examines the justifications for focusing on individual managers rather than profit-maximizing firms as the key actors in antitrust law. Part II looks at contemporary management mores and practices and develops some generalized "rules of the game" for how managers advance their careers in present-day American firms. Finally, Part III applies the rules to predict how managers might well guide their firms in three scenarios vital to modern antitrust law: entry into new markets, exclusion of competitors, and collusion among competitors.¹⁴

I. WHY MANAGERS AND NOT FIRMS?

In classical microeconomic theory, managers are pictured as virtual automatons, generally behaving in a manner consistent with the long-run profit-maximization of their firms.¹⁵ While some managers

13. *Matsushita* itself may be the best example of a case in which the simplifying assumptions of classical microeconomics led to erroneous conclusions in antitrust law. In reaching its conclusion that the defendants in *Matsushita* could not possibly have entered into a predatory-pricing conspiracy, the majority completely ignored what we know about business psychology in general, and Japanese business psychology and sociology in particular. For a devastating critique of *Matsushita* along these lines see Crew, *Matsushita v. Zenith: The Chicago School Teaches the Supreme Court a Dubious Lesson*, ANTITRUST, Fall 1986, at 11.

14. The scenarios discussed in this article are the ones in which a micro-microeconomic approach focusing on managers as the key actors will likely have the most utility for antitrust law. This does not mean that such an approach will not prove helpful in other areas of antitrust law. For example, classical microeconomics suggests that firms impose vertical restraints because these provide the most efficient means for distributing wares. H. HOVENKAMP, *ECONOMICS AND FEDERAL ANTITRUST LAW* 252 (1985). Close examination of the actual restraints from a micro-microeconomic perspective may show that in fact the restraints are imposed for the convenience of the managers rather than for the benefit of their employers.

In a recent article, Professor Hovenkamp challenges those who believe that firms do not act as rational profit-maximizers to demonstrate how that fact is relevant to contemporary antitrust law. See Hovenkamp, *supra* note 1, at 228 n.77. Responding to his challenge is one goal of the discussion in Part III.

15. See, e.g., F. SCHERER, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* 29 (2d ed. 1980); Henderson, *Product Liability and the Passage of Time: The Imprisonment of Corporate Rationality*, 58 N.Y.U. L. REV. 765, 769 (1983); Hovenkamp, *supra* note 1, at

undoubtedly behave in such a manner, most persons familiar with the real world of firms recognize that managers tend to pursue policies which do not maximize their firms' profits.¹⁶ Managers pursue nonmaximizing policies for two reasons. First, there is a gap between what managers perceive as the best methods for maximizing their firms' long-term profitability and the policies which in fact will accomplish that objective. Often the techniques, shibboleths, and styles of modern "scientific" management, which many managers fervently believe to be the path to success for their firms, lead to decreased profitability for the company. Firms engage in nonmaximizing behavior, not necessarily because of some nefarious conflict of interest on the part of their management, but because the managers erroneously believe that their management practices will lead to long-run profitability for the firm.

The response of many American firms to foreign competition provides an excellent example of how management style can cause firms to act differently from the manner predicted by the profit-maximization hypothesis. Numerous sectors of the American economy are suffering from an onslaught of foreign competition.¹⁷ An increasing number of commentators have focused on management inadequacies as the culprit in the decline of American competitiveness. Critics of American management have pointed out that prevalent practices such as overemphasizing quantitative measures of performance, treating labor as simply a factor of production rather than a human resource, and focusing on short-run profit-maximization to the exclusion of long-run concerns have hurt the ability of United States firms to compete against their European and Far-Eastern rivals.¹⁸ The managers who utilize these practices are not attempting to injure their own firms. The managers are in fact attempting to assist their firms by using orthodox "modern" management techniques. Nonetheless, the practices are dysfunctional in the face of present-day foreign competition. If the managers of firms were the profit-maximizing automatons postulated by classical microeconomists, American firms would not

228; Kaplow, *Extension of Monopoly Power Through Leverage*, 85 COLUM. L. REV. 515, 547-48 (1985).

16. *E.g.*, W. BAUMOL, BUSINESS BEHAVIOR, VALUE AND GROWTH 45-52 (1967); P. DRUCKER, TOWARD THE NEXT ECONOMICS AND OTHER ESSAYS 14 (1981); M. GREEN & J. BERRY, *supra* note 11, at 13-14.

17. *See, e.g.*, W. ABERNATHY, K. CLARK & A. KANTROW, INDUSTRIAL RENAISSANCE 9-14 (1983); R. REICH, THE NEXT AMERICAN FRONTIER 117-27 (1983); L. THUROW, THE ZERO-SUM SOLUTION 47-52 (1985).

18. *E.g.*, R. HAYES & S. WHEELWRIGHT, RESTORING OUR COMPETITIVE EDGE 7-19 (1984); P. PASCARELLA, THE NEW ACHIEVERS 157-72 (1984); R. REICH, *supra* note 17, at 140-45, 157-72; L. THUROW, *supra* note 17, at 144-57.

overly rely on quantitative measures, treat labor as a mere commodity, or focus only on the short run. The widespread persistence of these practices among American managers indicates that, contrary to the Chicago School model, one cannot simply assume that firms and their managers will act as rational profit-maximizers. The styles and techniques which prevail among individual managers can and do lead firms to take paths radically different from those predicted by the profit-maximization hypothesis.

The second reason why managers pursue policies which do not maximize the long-term profitability of their firms is that the interests of the managers diverge from the interests of the firms or their shareholders. The seminal source for the concept of a split between ownership and management interest is, of course, Berle and Means's pioneering work in the late 1920s and early 1930s.¹⁹ Classical microeconomists have expended a great deal of effort in attempting to discredit the Berle and Means thesis that modern corporations are controlled by managers furthering their personal interests rather than the shareholders' interests.²⁰ Nonetheless, the track record of contemporary American management provides strong anecdotal support for the notion that managers will often be faced with choices between actions which promote their careers and actions which promote the long-range viability of their firms, and when faced with such a choice, will pick the former.

Two areas of modern management behavior provide particularly apt examples. The first is simple corporate waste and inefficiency.²¹ Waste and inefficiency are inimical to the financial health of both the corporation and its shareholders. In the make-believe world of classical microeconomics, rational managers would not engage in wasteful or inefficient practices except perhaps by mistake, and those who make mistakes too frequently would be swiftly eliminated by an efficient and unforgiving market.²² In the real world, however, managers fre-

19. A. BERLE & G. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932).

20. See, e.g., *Corporations and Private Property*, 26 J.L. & ECON. 235 (1983). For modern defenses of the Berle & Means thesis, see A. BERLE & G. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* xxix-xxxi, 358-59 (rev. ed. 1967); R. LARNER, *MANAGEMENT CONTROL AND THE LARGE CORPORATION* 9-24 (1970).

21. The term "waste" refers to what Green and Berry call "avoidable waste" — waste caused by "decisions that [managers] know, or should know, will cost more than they yield." M. GREEN & J. BERRY, *supra* note 11, at 13. This is similar to the concept of X-inefficiency developed by economist Harvey Leibenstein. Professor Leibenstein defines X-inefficiency as "all types of inefficiencies resulting from the complete or partial lack of motivation to use economic opportunities as effectively as they might be used." Leibenstein, *Microeconomics and X-efficiency Theory: If There Is No Crisis, There Ought To Be*, in *THE CRISIS IN ECONOMIC THEORY* 97, 98 (D. Bell & I. Kristol eds. 1981).

22. F. SCHERER, *supra* note 15, at 38.

quently engage in wasteful and inefficient behavior.²³ Economist Harvey Leibenstein estimates that between twenty and forty percent of the net national economic product is wasted through what he terms "X-inefficiency" and that waste by firms is the major source of this loss.²⁴

In the world of the corporation, much of the inefficiency can be traced to managers' attempts to pursue their own goals rather than to maximize their firms' profitability (or, to be more accurate, to minimize their firms' costs). Professor Leibenstein recounts an illustrative anecdote. During the 1920s, future historian Eleanor Dulles was working in a hairnet factory when she devised a worker-incentive system under which workers would be rewarded with a thirty to forty percent increase in wages for a fifty percent increase in productivity.²⁵ The system was a success, and several of the best workers began earning significantly increased wages while the factory's productivity and profitability surged. The rational, profit-maximizing manager, of course, would have been delighted with the new system. In actuality, the manager of the plant (who was not the owner of the company) discouraged worker participation in the plan and eventually wrecked the system because he did not want the better workers "thinking they are good . . . [and getting] above themselves."²⁶ The incentive system was clearly in the best interests of the owners of the firm. However, it was not maintained because the plant manager placed his own interest in status and perceived authority over the interests of the firm.

The second prevailing pattern which tends to confirm the thesis that the interests of managers diverge from those of their employers is the behavior of management in modern corporate takeover battles.²⁷

23. See, e.g., M. GREEN & J. BERRY, *supra* note 11. The existence of vast waste and inefficiency should come as no surprise. As Professor Scherer has noted, "[a]nyone with the remotest knowledge of real-world organizations must recognize that something resembling X-inefficiency exists." F. SCHERER, *supra* note 15, at 464. Economist Shlomo Maital puts the matter even more bluntly: "Readers with experience in the business world may be bemused that economists even question the existence of X-inefficiency. An entire branch of psychology, organizational behavior, is built on the assumption that X-inefficiency . . . is alive and well." S. MAITAL, *MINDS, MARKETS, AND MONEY* 112 (1982). For a summary of rigorous empirical research on the existence of X-inefficiencies, see H. LEIBENSTEIN, *BEYOND ECONOMIC MAN* 34-44 (1976).

24. Leibenstein, *supra* note 21, at 108.

25. *Id.* at 97.

26. *Id.*

27. Ironically, the Chicago School has been vigorous in pointing out how managers can act contrary to shareholder interests during takeover fights. To quote Judge Easterbrook, "[m]any managers . . . want to be secure in their jobs; the Chicago School generally supports free competition in the market for corporate control, even though this terrifies managers." Easterbrook, *Workable Antitrust Policy*, 84 MICH. L. REV. 1696, 1706 n.25 (1986). For a thorough survey and evaluation of the empirical studies on the adverse impact of management antitakeover techniques on shareholder interests, see Easterbrook & Jarrell, *Do Targets Gain from Defeating Tender Offers?*, 59 N.Y.U. L. REV. 277 (1984). For a succinct summary of the various types of antitakeover tactics utilized by management, see R. CLARK, *CORPORATE LAW* 571-77 (1986).

When managers utilize tactics such as "scorched-earth policies" (selling profitable divisions at below-market prices to make their companies less attractive to corporate raiders), purchasing divisions simply to raise antitrust problems for potential suitors, or paying "greenmail" to corporate raiders,²⁸ they can hardly be said to be acting in their firm's best interest. The use of such tactics supports the view that management is more interested in maintaining short-run job tenure than in running an efficient firm that will be viable in the long run.

The ease with which modern managers place their own interests above those of their corporations should come as no surprise. Many of the mechanisms which economists argued would prevent such a development not only have proven to be ineffective, but have actually encouraged managers to place their personal interests above those of their employers. The ineffectiveness of shareholders and boards of directors in supervising management has been discussed by many commentators.²⁹ The ultimate discipline for management, the Darwinian marketplace, may weed out firms whose managers look too much to their own goals, but the pressure exerted by that marketplace may be diminished by factors such as noncompetitive markets and sloth by rivals' managements.³⁰ Managers can fail to operate at top efficiency or to maximize the long-run profits of their firm without necessarily leading the firm to destruction.³¹ Even if management's actions end in the destruction of the firm, the managers may not necessarily have to face the consequences of their decisions.

One of the characteristics of contemporary American firms is the

28. R. CLARK, *supra* note 27, at 571-77. For a more detailed discussion of the deleterious effect on shareholder interests of paying "greenmail," see Dann & DeAngelo, *Standstill Agreements, Privately Negotiated Stock Repurchases, and the Market for Corporate Control*, 11 J. FIN. ECON. 275 (1983).

29. *E.g.*, E. HERMAN, CORPORATE CONTROL, CORPORATE POWER 30-48 (1981); M. MACE, DIRECTORS: MYTH AND REALITY 43-71 (1971); E. MCSWENEY, MANAGING THE MANAGERS 105-07 (1978); Brudney, *The Independent Director — Heavenly City or Potemkin Village?*, 95 HARV. L. REV. 597, 610-16 (1982).

30. See F. SCHERER, *supra* note 15, at 38.

31. In addition to market or competitive managerial imperfections, another factor that can dampen the Darwinian struggle is a managerial policy of "satisficing." Satisficing refers to a policy of generating satisfactory profits, rather than maximal profits. See, *e.g.*, R. CYERT & J. MARCH, A BEHAVIORAL THEORY OF THE FIRM 26-44 (1963); Simon, *Theories of Decision-Making in Economics and Behavioral Science*, 49 AMER. ECON. REV. 253, 262-65 (1959).

Furthermore, firms are often so large or resilient that they can absorb a great deal of mismanagement without being driven to the brink. In recent years, the challenge of Japanese competition has exposed the pervasively poor management practices of American automobile companies. See D. HALBERSTAM, *THE RECKONING* (1986); B. YATES, *THE DECLINE AND FALL OF THE AMERICAN AUTOMOBILE INDUSTRY* 242-52 (1983); see also W. ABERNATHY, K. CLARK & A. KANTROW, *supra* note 17, at 72-94. While poor management in the face of effective foreign competition did almost bankrupt Chrysler and American Motors, General Motors and Ford were far from destroyed, although they were seriously damaged. The firms were simply big enough to tolerate persistent mismanagement.

short job tenure of many of their executives. In contrast to Japanese firms, American executives tend to change employers frequently.³² If the consequences of bad management practices are felt after an executive has left the firm, that executive may escape blame. Indeed, under some circumstances, the former executive's reputation may be *enhanced* by his prior bad management practices. For example, take the chief executive officer (CEO) of a manufacturing concern. The CEO may be faced with a decision of whether to invest in research and development which will ensure the firm's competitive position in future years. If the CEO chooses not to make the investment, the firm will be able to show higher current income and dividends. The CEO may then be hired at a new firm on the basis of the enhanced earnings of his previous employer. When the CEO's previous employer begins reaping the consequences of its failure to invest in research and development, the blame may not fall on the departed CEO's decisions, but on the CEO's departure.³³

Finally, the nature of the securities markets may exacerbate the tendency of managers to look to their own interests. Some microeconomists have argued that the securities markets force executives to attempt to maximize their firm's profits.³⁴ These economists claim that if profits are not maximized, the value of the firm's stock will drop, making the firm a prime takeover target and the firm's management vulnerable to displacement if such a takeover occurs.³⁵ Under this view, the securities markets exercise a disciplinary effect which causes the interests of a firm and its management to converge. However, even if such a disciplinary effect exists, the discipline of the

32. See L. THUROW, *supra* note 17, at 149-50; Hayes & Abernathy, *Managing Our Way to Economic Decline*, HARV. BUS. REV., July-Aug. 1980, at 67, 74.

33. The failure to draw the connection between the CEO's past policies and his former firm's present difficulties will probably be the result of a combination of mental laziness and ideology. As economist Lester Thurow points out, evaluating performance on the basis of simple short-run, bottom-line figures is relatively easy. L. THUROW, *supra* note 17, at 152. Judging how well an executive has positioned his firm for the future "requires real skill," which many executives and directors have been unwilling or unable to exercise. *Id.* The discounting of short-run profit data and the visualization of a linkage between a manager's past policies and a firm's present problems take similar skills. There is no more incentive for evaluators to try to abandon simple mechanical rules in favor of tough judgment calls in this situation than there is in any other situation involving executives. Moreover, if the CEO pursued short-run policies which successfully inflated the price of the former employer's stock (as is quite likely), the claim that the policies were actually destructive of the long-range future of the firm would likely be ignored by those who believe that the stock markets are efficient and reflect accurately all known information about a company. For an exposition of the efficient-market hypothesis, see Fama, *Efficient Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383 (1970).

34. See, e.g., Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965).

35. See *id.*

stock markets may push managers to take steps which perhaps are in their own short-term interests, but damage the firm in the long-run.

Examination of the psychological time frame of managers illustrates this phenomenon. As will be discussed later, managers tend to refuse to engage in projects which do not show profitability in a year or two, no matter how vital the project is for the long-term stability of the firm.³⁶ The stock markets in general, and institutional investors in particular, also seem to be more interested in short-run profits than in long-term viability.³⁷ Thus, the discipline of the markets may push managers to take steps which increase immediate profitability (and, given short job tenure, the manager's stature) at the expense of long-term survivability.³⁸ For example, managers of many American firms have chosen to forego needed commitments to research and development, or to new plants and equipment, because such commitments will diminish short-run earnings and dividends which in turn may lower the market value of a firm's stock.³⁹ In these cases, the "rational" firm would be interested in maintaining its competitive position and surviving over the long term. If the managers were rational profit-maximizers, they would make the necessary investments. Instead, the perceived need to please securities markets and avoid hostile takeovers forces managers to sacrifice long-term survivability for short-term profit. In these cases, the securities markets have not unified the inter-

36. See notes 42-47 *infra* and accompanying text.

37. See L. THUROW, *supra* note 17, at 156.

38. *Id.* at 150. While this article suggests that the managers of firms often do what is necessary for the advancement of their careers rather than for the survival of their firms, it does not mean to suggest that business executives are unique in this behavior. Such behavior may be common to all leaders of bureaucratic organizations. Indeed, an analogous process is now occurring in labor unions. Most labor leaders claim that organizing is crucial for the continued survival of the labor movement. See, e.g., Kuttner, *Will Unions Organize Again?*, *DISSENT*, Winter 1987, at 52, 55. However, there is little internal pressure within unions to organize. In fact, the job of organizer is generally a low-status, low-paying job within a union. *Id.* Being a union organizer is not the way to advance within a union. Instead, the business agent, who deals with the needs of current members, is at the top of the hierarchy of jobs in a union. *Id.* As a consequence, the work of organizing languishes even though it is crucial to the long-term survival of the union. *Id.* Just as catering to the needs of current shareholders, even at the expense of the firm and future shareholders, is the way to advance within a firm, catering to current members' needs, even at the expense of future members and the union itself, seems to be the way to advance within a union.

39. See L. THUROW, *supra* note 17, at 150. The managers who fail to make needed investment in plant and equipment may not be acting out of selfish motives, but out of sincere if mistaken views on sound management. As Professors Hayes and Garvin of the Harvard Business School point out, the widely used analytical techniques used to discount investments in plant and equipment to present value lead to a systematic erroneous bias against making investments in productive technology, capacity, and worker skills. Hayes & Garvin, *Managing as If Tomorrow Mattered*, *HARV. BUS. REV.*, May-June 1982, at 70, 71. The widespread utilization of analytical techniques which lead to erroneous results once again demonstrates the absurdity of the assumption that managers are robot-like profit-maximizers. It also underscores the importance of analyzing how real-world managers in fact make decisions.

ests of a firm and its management, as predicted by some microeconomists, but have caused the two interests to draw even farther apart.

In sum, the record of contemporary management strongly suggests that we must look to actual management beliefs and practices in order to predict the behavior of real-world firms; we cannot assume that managers are merely profit-maximizing robots. This article will now turn to such an examination.

II. THE RULES OF THE GAME FOR MANAGERIAL ADVANCEMENT

Any attempt to describe a contemporary American "style" of management must inevitably lead to oversimplification. Given the plethora of firms and managers, a myriad of exceptions to any systematized portrait of American management is bound to exist.⁴⁰ Nonetheless, the characteristics of American management discussed in this section are sufficiently widespread and salient that they affect the performance of American firms vis-à-vis their foreign competition on a macro level.⁴¹ Therefore, these characteristics can be used to make generalized predictions on how real-world firms are likely to perform in situations involving the application of the federal antitrust laws. The modes and methods of modern American management give rise to four "rules of the game" for managers who wish to advance their careers.

The first rule of the modern management game is that a manager's and firm's success is to be judged by bottom-line financial measures such as current earnings or short-term return on investment.⁴² Both top and middle management are evaluated on this basis. Directors and upper-level managers often use these quantitative methods of judgment because of mental laziness. As economist Lester Thurow has noted,

Any board of directors, no matter how inept, can hand out bonuses to top management based on current profits; but to know whether top

40. See, e.g., M. GREEN & J. BERRY, *supra* note 11, at 80-101 (discussing how some firms have tamed corporate bureaucracies); T. PETERS & R. WATERMAN, IN SEARCH OF EXCELLENCE 171-86, 242-60 (detailing how some exceptional firms are particularly responsive to customer needs and encourage individuality among their employees). The managers of the firms discussed in these sources likely do *not* play by the rules discussed in this section.

41. See, e.g., R. HAYES & S. WHEELWRIGHT, *supra* note 18, at 7-19; P. PASCARELLA, *supra* note 18, at 163-67; R. REICH, *supra* note 17, at 140-45, 170-72; L. THUROW, *supra* note 17, at 144-57.

42. E.g., M. GREEN & J. BERRY, *supra* note 11, at 38-39; R. HAYES & S. WHEELWRIGHT, *supra* note 18, at 8-12; L. THUROW, *supra* note 17, at 149-57; Thompson, Kirkham & Dixon, *Warning: The Fast Track May Be Hazardous to Organizational Health*, ORGANIZATIONAL DYNAMICS, Spring 1985, at 21, 23-24.

management has positioned the company well for the long haul requires real skill. Mechanical judgments of middle-level managers based on earnings of their profit centers generate no controversies. Such judgments favor managers who may be making good profits now but who should be investing to make much larger profits later, and discourage managers who are doing a good job in areas where the external environment makes profits difficult or impossible to obtain.⁴³

Professor Thurow's comment leads us directly to the second rule of the management game — all management decisions must show a profit in the short-run, with no more than two or three years as the outer limit.⁴⁴ If a venture will not show a short-run profit, many modern American managers believe it is not worth undertaking.

Following the first two rules, and thus engaging in a "brilliant piece of short-run profit maximizing," can result in a manager being placed on the highly desirable "fast track."⁴⁵ Keeping on the "fast track" requires adherence to two other rules, the first of which is "[A]void any risks that might lead to mistakes which would knock one off the fast track."⁴⁶ To state the rule another way, "Be risk averse in seeking gains for your firm."⁴⁷

The other rule for managers who wish to stay on the fast track is to avoid controversy or, as the common cliché runs, "Don't make waves."⁴⁸ Under this rule, the manager whose actions generate complaints and controversy is a bad manager who may be removed from the fast track.

The managers who play by these rules are not the profit-maximizing automatons depicted by classical microeconomists. Instead, they

43. L. THUROW, *supra* note 17, at 152.

44. *See* note 42 *supra*.

45. L. THUROW, *supra* note 17, at 151.

46. *Id.*; *see also* Thompson, Kirkham & Dixon, *supra* note 42, at 24.

47. The qualification "in seeking gains" is quite important. Psychological studies indicate that when it comes to avoiding what they view as certain losses, managers, like other human beings, are willing to accept tremendous amounts of risk. *See generally*, P. SCHOEMAKER, EXPERIMENTS ON DECISIONS UNDER RISK: THE EXPECTED UTILITY HYPOTHESIS 45-90, 109-25 (1980); Fishburn & Kochenberger, *Two-Piece Von Neumann-Morgenstern Utility Functions*, 10 DECISION SCI. 503 (1979); Kahneman & Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 ECONOMETRICA 263 (1979); Laughhunn, Payne & Crum, *Managerial Risk Preferences for Below-Target Returns*, 26 MGT. SCI. 1238, 1247-49 (1980). *But see* Fagley & Miller, *The Effects of Decision Framing on Choice of Risky vs. Certain Options*, 39 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES 264 (1987) (empirical results suggesting that subjects avoid risk in situations where attempting to avoid near-certain loss). For an application of the findings of experimental psychology on the psychology of risk-taking to the decision of managers to engage in predatory pricing or to enter into a market where such pricing has been practiced, *see* Gerla, *The Psychology of Predatory Pricing: Why Predatory Pricing Pays*, 39 SW. L.J. 755 (1985).

48. Thompson, Kirkham & Dixon, *supra* note 42, at 24; *see also* M. GREEN & J. BERRY, *supra* note 11, at 25; T. PETERS & R. WATERMAN, *supra* note 40, at 43.

tend to be risk-averse short-run profit-maximizers who are unwilling to "rock the boat." Such real-world managers in fact direct the affairs of many U.S. firms. The remainder of this article will be devoted to an examination of how these real-world managers are likely to behave in scenarios involving the antitrust laws.

III. MANAGERIAL GAMES AND THE ANTITRUST LAWS

A. *New Entry into Markets*

While the antitrust laws do not directly address the problem of firms entering new markets, the phenomenon plays a vital role in the contemporary interpretation of those laws. For the Chicago School, new entry into markets is something of a wonder drug which will, at least in the long run, cure any ill effects of many practices currently prohibited by the antitrust laws, such as unreasonable restraints of trade, monopolization, and anticompetitive mergers.

Under this Chicago School view, if a cartel attempts to fix prices, its supracompetitive profits will attract new entrants who will undermine the arrangement.⁴⁹ If a monopolist attempts to gouge consumers through monopoly-level pricing, new entrants, attracted by the high prices, will soon ruin the monopolist's plans.⁵⁰ Similarly, new entry can prevent price gouging by newly merged firms even in a highly concentrated market.⁵¹ While the most devoted Chicago Schooler would not claim that the possibility of new entry should cause the antitrust laws to overlook price fixing among competitors,⁵² most members of the Chicago School do insist that the possibility of new entry into markets often makes it unnecessary and inefficient to prosecute monopolization and block mergers through the antitrust laws.⁵³

The rosy scenario of new entry is, of course, complicated by the problem of entry barriers. During the 1940s and 1950s, many antitrust theorists focused on what they believed to be significant "natural" barriers to market entry created by the size of existing firms and

49. See, e.g., E. GELLHORN, *ANTITRUST LAW AND ECONOMICS IN A NUTSHELL* 156, 158 (3d ed. 1986); Hovenkamp, *Rhetoric and Skepticism in Antitrust Argument*, 84 MICH. L. REV. 1721, 1726 (1986).

50. See R. BORK, *supra* note 1, at 195-96; cf. Easterbrook, *Predatory Strategies and Counter-strategies*, 48 U. CHI. L. REV. 263, 264-65 (1981) (arguing that new entry will frustrate a monopolist's attempt to recoup losses caused by predatory pricing).

51. See Hovenkamp, *supra* note 49, at 1726.

52. See *id.*; R. BORK, *supra* note 1, at 267-69.

53. Professor Hovenkamp has noted the inconsistency between the Chicago School views that new entry can cure the ills inflicted by monopolists and overly concentrated markets, but that it cannot cure the ills inflicted by cartel members. Hovenkamp, *supra* note 49, at 1726; see also R. BORK, *supra* note 1; E. GELLHORN, *supra* note 49.

the structure of the market.⁵⁴ Classical microeconomists deny that natural barriers to entry exist, and they maintain that the only significant entry barriers are those created by governmental intervention.⁵⁵ Some post-Chicago revisionists are willing to recognize strategic behavior by dominant firms as a source of barriers to entry.⁵⁶ All three groups in fact overlook what may be the most important entry barrier in the real world — the managerial ethos of potential entrants.

When we view the decision to enter a market from the oversimplified and unrealistic perspective of the profit-maximizing corporation and its robot-like managers, the decision to enter seems to be an easy one. If the firm can maximize its profits through new entry into a market, it will do so. Thus, if supracompetitive profits are being generated by a cartel, a monopoly, or firms in a highly concentrated market, new profit-maximizing entrants will come marching in, lured by the high profit levels, and quickly bring profits and prices down to competitive levels.⁵⁷

However, when new entry is viewed from the manager's perspective, it looks far less probable. The first problem is the time frame of any payoff resulting from a decision to enter. New entry into virtually any market, including one characterized by monopoly or cartelized high prices, is likely to result in a short-run diminution of profits or even in losses, as the new entrant becomes familiar with a new field or gets up to speed on the "learning curve" in a new industry.⁵⁸ Indeed, a profit may not be turned for several years. Thus, new entry may violate one of the prime rules for modern managerial success — that new ventures must show a short-run profit.⁵⁹ The manager making the decision to enter may be reluctant to enter because she may be blamed for any short-run losses, and she may not be credited for long-run profits ultimately resulting from entry because she may not even be with the same employer if and when the new venture begins to show a profit.

54. The pioneering work making this point was J. BAIN, *BARRIERS TO NEW COMPETITION* (1956).

55. See R. BORK, *supra* note 1, at 310-29; Demsetz, *Two Systems of Belief About Monopoly*, in *INDUSTRIAL CONCENTRATION: THE NEW LEARNING* 164, 181-84 (H. Goldschmid, H. Mann & J. Weston eds. 1974).

56. See Hovenkamp, *supra* note 1, at 260-83; see also Krattenmaker & Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over Price*, 96 *YALE L.J.* 209 (1986) (discussing how even nonmonopolists can use strategic behavior to exclude competitors from markets by forcing them to raise prices).

57. See, e.g., R. BORK, *supra* note 1, at 195-96; E. GELLHORN, *supra* note 49, at 156-58; Hovenkamp, *supra* note 49.

58. See F. SCHERER, *supra* note 15, at 250-51.

59. See text at note 44 *supra*.

The second problem with new entry from a manager's perspective is that the process almost always entails risks.⁶⁰ The risks are especially grave if entry is to be made in a field in which the firm has little or no experience.⁶¹ As noted previously, risk is something contemporary American managers eschew, especially if those managers are on the "fast track."⁶² New entry into a market is precisely the type of risky decision which many contemporary American managers would prefer not to make. Moreover, the managers' fear of market entry can be heightened by strategic behavior on the part of firms already in the market.⁶³

Take, for example, the case of a decision to enter a market domi-

60. See C. SUTTON, *ECONOMICS AND CORPORATE STRATEGY* 82-83 (1980); Porter, *How Competitive Forces Shape Strategy*, in *STRATEGIC MANAGEMENT* 37-39 (R. Hamermesh ed. 1983).

61. See T. PETERS & R. WATERMAN, *supra* note 40, at 292-305.

62. See notes 46-47 *supra* and accompanying text. To sound a recurrent theme of this article, a decision not to take the risk of entering a market may not be the product of a conscious decision by a manager to put her career ahead of the welfare of her firm; rather, it may result from miscalculation as to the best course of action for the firm. The profitability of entering a new market will depend not only on the actions of the potential entrant and of the existing firms in the market, but on the actions of other potential entrants as well. As economist Shlomo Maital and psychologist Sharone Maital have pointed out, many large companies are run by executives less eager to make big profits than to avoid large losses. S. MAITAL & S. MAITAL, *ECONOMIC GAMES PEOPLE PLAY* 88 (1984). Maital and Maital point out that such executives tend to view a decision on whether to invest in research and development of a new product as a game which they term "After You, Garçon." The game is represented by the following matrix:

		Competitors	
		Take the Plunge	Play It Safe
Company	Take the Plunge	Big Loss	Small Profit
	Play It Safe	Big Profit	Break Even

AFTER YOU, GARÇON

In the game of "After You, Garçon," large profits are garnered by the firm which lets others take the risks, and then moves in to take the "gravy." *Id.* at 87. The game can easily be applied to a decision on whether to enter a new market. If executives view the decision to enter as a game of "After You, Garçon," they are apt not to enter the market. As Maital and Maital point out, cautious managers, focused on quarterly profit-and-loss statements, are indeed likely to view market-entry decisions as games of "After You, Garçon" even when they are not forms of this game. *Id.* at 89. Thus, these managers are likely to avoid entry because they believe it is not in the best interests of their firm.

63. See Hovenkamp, *supra* note 1, at 260-83; Krattenmaker & Salop, *supra* note 56, at 230-48.

nated by a monopolist charging monopoly-level prices and reaping monopolistic profits. The monopolist can increase the level of perceived risk among the managers of potential entrants by utilizing a variety of tactics such as cutting off the entrant from low-cost sources of supply,⁶⁴ creating product differentiation and strong brand identification through massive advertising,⁶⁵ committing business torts or unfair business practices,⁶⁶ instituting harassing litigation,⁶⁷ or attempting to secure legislation unfavorable to new entrants.⁶⁸ Whether any of these tactics can succeed in the long run is irrelevant. Predatory behavior, as long as it increases perceived risk among the managers of potential entrants or decreases the short-run profitability of actual or potential rivals, will frustrate new entry by playing on the tendencies of American managers to avoid taking risks and to look almost exclusively at short-term profits.⁶⁹

An amusing and enlightening example of how a firm can eliminate

64. See Krattenmaker & Salop, *supra* note 56, at 234-36.

65. See Porter, *supra* note 60, at 38.

66. See B. KELLMAN, PRIVATE ANTITRUST LITIGATION 129-30 (1985).

67. See R. BORK, *supra* note 1, at 347-49.

68. *Id.*

69. Contrary to the assumptions of Chicago School analysis, predatory behavior need not be either ultimately successful or sustainable on a long-term basis in order to deter market entry. Chicago School analysis is premised on the notion that predatory conduct will not avail a firm seeking to deter or repel entry if the conduct will cost the predator more in the long run than it costs the victim. See, e.g., Easterbrook, *supra* note 10 (discussing unlikelihood of predatory pricing strategies being utilized or successful); Liebler, *Whither Predatory Pricing? From Areeda and Turner to Matsushita*, 61 NOTRE DAME L. REV. 1052 (1986) (same). Robert Bork argues that, in order to engage in nongovernmental predation, a firm must be able to impose larger costs on its victim than on itself and must have greater reserves or better access to capital than the victim. See R. BORK, *supra* note 1, at 348.

The analysis put forth by Bork and his fellow Chicagoans fails to comprehend that, in the real world of late twentieth-century American managerialism, the ability of predatory tactics to succeed in the long run is largely irrelevant. Given managers' short-term profit orientation and unwillingness to take risks, any predatory tactic which diminishes a new entrant's short-run profit or significantly increases the riskiness of its new venture is likely to make managers extremely hesitant to proceed with new entry, regardless of the long-term prospects of the new entrant or the predator. The success of the tiny maker of Formula 409 in driving giant Proctor and Gamble from the spray-cleaner market is illustrative of this point. See notes 70-71 *infra* and accompanying text.

Of course, the predator will often incur short-run losses in carrying out its predatory strategy. The obvious question arises of why the management of the predator is willing to incur short-term losses in search of long-term gain while the management of the new entrant is unwilling to make such a trade off. The answer to this seeming paradox is that the managers of the predator and new entrant are in quite different positions. The managers of the new entrant are in search of gains. The managers of the predator are trying to avoid what they probably view as a certain loss of their competitive position. Psychological evidence suggests that the managers of the predators are apt to be risk affinitive in seeking to avoid losses while the managers of the new entrant are likely to be risk averse in seeking gains. See Gerla, *supra* note 47, at 761-62, 768-70. Even conventional microeconomics recognizes that persons may place a higher price on not being deprived of a good than on acquiring the good in the first place. Cf. E. MISHAN, COST-BENEFIT ANALYSIS, 134-37 (1976) (discussing microeconomic concepts of "compensation value" and "equivalence value"). Thus, the managers of the predator may well be more willing to take

a rival from a market by taking advantage of the psychological predispositions of the rival's managers is the manner in which the maker of "Formula 409" drove Proctor and Gamble (P & G) out of the spray-cleaner market.⁷⁰ Formula 409 was made by a small manufacturer, Wilson Harrell. Harrell learned that P & G, the nation's largest manufacturer of laundry products, wished to introduce a new spray cleaner called "Cinch." Harrell also learned that P & G had decided to use Denver as a test market for the new cleaner. When P & G began test marketing Cinch in Denver, Harrell deliberately inflated P & G's expectations for Cinch by subtly pulling Formula 409 from the Denver market. When Cinch began to be marketed nationally, Harrell offered deep discounts on Formula 409 which encouraged consumers to buy six-month supplies of the product. Sales of Cinch were extremely poor because consumers already had more spray cleaner than they could possibly use. In light of Cinch's spectacular debut in Denver, the managers of P & G were especially discouraged by the product's poor national sales. P & G withdrew Cinch from the market within a year of its introduction. In the theoretical world of classical microeconomics, Wilson Harrell could not have bested P & G. A small manufacturer could not sustain the deep discounts on its product when its gigantic rival had the capacity to absorb huge losses. Nevertheless, in the real world, Wilson Harrell was able to oust P & G from the spray-cleaner market by taking advantage of the risk aversion and inflated expectations of the P & G managers.⁷¹

The reluctance of real-world managers to bring their firms into new markets has a number of important implications for antitrust law and policy. First, new entry cannot be relied upon to destroy cartels and eliminate consumer harm caused by horizontal price-fixing or territorial division. Thus, vigorous antitrust enforcement against such arrangements is still justifiable.⁷² Second, new entry cannot be relied

greater risks and incur short-term losses in their effort to preserve the predator's market position than will the managers of the new entrant in their effort to enhance their firm's market position.

70. See P. SOLMAN & T. FRIEDMAN, *LIFE AND DEATH ON THE CORPORATE BATTLEFIELD* 25-26 (1982).

71. As Solman and Friedman put it, "It was a close shave for Wilson Harrell. . . . But Harrell knew the psychology of big companies." *Id.* In the theoretical world of profit-maximizing managers, the psychology of those in charge of firms should be irrelevant in determining behavior. In the real world of real businesses, the psychology of those in charge plays a large role in determining how "firms" will actually behave.

72. Not even the most devoted members of the Chicago School would subscribe to the proposition that barring cartelization is unnecessary because new entry will foil attempts to charge supracompetitive prices. As Professor Hovenkamp notes, the Chicago School's advocacy of continued antitrust enforcement against cartelization is inconsistent with their belief in the insignificance of entry barriers. Hovenkamp, *supra* note 49, at 1726. But see D. ARMENTANO, *ANTITRUST POLICY: THE CASE FOR REPEAL* 64-65 (1986) (explicitly arguing that antitrust

upon to spoil attempts by monopolists or oligopolists to reap supracompetitive profits. Therefore, the theoretical ease of entry or the mere possibility of entry should not rule out enforcement action against monopolies or mergers which unduly increase market concentration.⁷³

That antitrust enforcement authorities or courts might fall into the trap of assuming that the theoretical ease of entry is equivalent to entry in fact is more than just speculation. Both the 1982 and 1984 Department of Justice *Merger Guidelines* rely heavily on theoretical entry barriers in determining whether a merger should be challenged under the antitrust laws.⁷⁴

The other federal antitrust enforcement agency, the Federal Trade Commission, has also succumbed to the temptation to equate theoretical ease of market entry with actual entry. In *In re Echlin Manufacturing*,⁷⁵ the Commission dismissed a staff complaint against a merger in the carburetor-kit-production industry between competitors with thirty-six percent and ten percent of a small, declining, highly concentrated market (six firms accounted for ninety-five percent of sales).⁷⁶ The primary basis for the Commission's dismissal of the staff complaint was its finding that, under a narrow definition of entry barriers, such barriers were not a significant factor in the relevant market.⁷⁷ The Commission made its findings on the ease of market entry in the face of evidence that "the recent record of new entrants is especially

prohibition against cartels is unnecessary because new entry will frustrate the achievement of cartel objectives).

73. While the implications of the "entry is easy" thesis have not slackened the hostility of commentators to cartel-like behavior, they have "inspired many people — Chicago School as well as others — to become more tolerant of mergers." Hovenkamp, *supra* note 49, at 1726 (footnote omitted). In light of the reluctance of real-world managers to take risks and to forego profits for extended periods, that tolerance may well be undeserved.

74. Both the 1984 and 1982 merger guidelines use "ease of entry" as a key determinant in the decision to challenge a merger as anticompetitive. *U.S. Dept. of Justice Merger Guidelines*, reprinted in 2 Trade Reg. Rep. (CCH) ¶ 4493.30 (1984); *U.S. Dept. of Justice Merger Guidelines*, reprinted in 2 Trade Reg. Rep. (CCH) ¶ 4503.20 (1982). Those actually charged with the antitrust enforcement at the Antitrust Division of the Department of Justice may, in practice, not rely as heavily on the theoretical ease of entry as the *Merger Guidelines* would suggest. At an antitrust conference, then-Deputy Attorney General Mark Leddy stated that in determining whether to challenge a merger, the Antitrust Division looked at more than the theoretical ease of entry into the market: "The pertinent question is how *likely* entry is." Leddy, *Entry Issues in Merger Analysis*, 54 ANTITRUST L.J. 1257, 1258 (1986) (emphasis in original). In response to a questioner who pointed out that likelihood of entry might be different from ease of entry, Leddy went on to say that in determining the likelihood of entry, the Division looked first to the actual past history of entry into the market. Yoerg, Hill & Leddy, *Panel Discussion*, 54 ANTITRUST L.J. 1271, 1271-72 (1986). This article also favors the approach of relying on the actual history of market entry. See note 83 *infra* and accompanying text.

75. 105 F.T.C. 410 (1985).

76. 105 F.T.C. at 492 (Bailey, Commr., dissenting).

77. See 105 F.T.C. at 487.

poor in [the carburetor-kit] industry, and . . . at least one case of targeted market retaliation by the market leader against a new firm [has occurred]."⁷⁸ In effect, when the Commission was faced with a choice between reality and theory, it chose the latter.

The United States Court of Appeals for the Second Circuit made a similar error in its decision in *United States v. Waste Management, Inc.*⁷⁹ Here the Second Circuit held that theoretical ease of entry into the solid waste disposal market allowed a defendant to rebut successfully a presumption of anticompetitive effect created by the merger of two firms with a combined 48.8% market share.⁸⁰ The judges on the panel that decided *Waste Management* (as well as those at the Federal Trade Commission and the drafters of the 1982 and 1984 Justice Department *Merger Guidelines*) erroneously equated the existence of low entry barriers with the actual entry of new firms into a market. In the theoretical world of profit-maximizing firms, the equation is understandable.⁸¹ In the real world of contemporary American business management, the equation is untenable.

Of course, merely because modern American managers are loathe to enter new markets does not mean that such entry is nonexistent. There are too many examples of firms entering markets against seemingly hopeless odds to claim that entry into new markets is illusory.⁸² However, the reticence of American executives to take risks or to look beyond relatively short time horizons does suggest that the mere possibility of entry should not be determinative in gauging the long-term effects of mergers or of persistently large market-share concentrations. To judge accurately the effects of new entry or potential new entry on the ability of a monopolist or near-monopolist to reap supracompetitive profits in the long term, courts or enforcement authorities should look to *actual* successful entry into the market rather than the presence or absence of theoretical entry barriers.⁸³

78. 105 F.T.C. at 498 (Bailey, Commr., dissenting).

79. 743 F.2d 976 (2d Cir. 1984).

80. 743 F.2d at 982-83. The court's conclusion in *Waste Management* was somewhat more defensible than the FTC's conclusion in *Echlin*, given that some successful entry into the market in *Waste Management* had in fact occurred. 743 F.2d at 982-83. However, this limited successful market entry cannot justify the conclusion either that entry was easy, or more importantly, that from the perspective of the managers of a potential entrant, entry was a relatively risk-free proposition. As the court itself noted, most of the new entrants in the market were no longer in existence at the time of suit. 743 F.2d at 982. For critiques of the *Waste Management* decision, see P. AREEDA & H. HOVENKAMP, *ANTITRUST LAW* ¶ 917.1b, at 668 (Supp. 1987); and Lipner, *Horizontal Mergers, General Dynamics and Its Progeny: Requiem for a Presumption*, 27 S. TEX. L. REV. 381, 397-99 (1986).

81. See note 57 *supra* and accompanying text.

82. See, e.g., P. SOLMAN & T. FRIEDMAN, *supra* note 70, at 19-20, 34-35.

83. Of course, the concept that actual successful entry is the best evidence that new entry

B. *Exclusionary Practices Aimed at Competitors*

The antitrust laws do not automatically forbid efforts to drive competitors from the market. Indeed, excluding competitors from the market through competition on the merits is part of what the antitrust laws are supposed to encourage.⁸⁴ On the other hand, use of certain tactics to oust competitors from the market does run afoul of the antitrust laws.⁸⁵ One of these tactics is the classic group boycott. Professor Lawrence Sullivan defines the classic group boycott as an effort "by traders at one level to keep others out or inhibit their competitive efforts at that level by making it more difficult for them to find what traders at that level need, usually suppliers or customers."⁸⁶ Certain classic group boycotts are per se violations of the antitrust laws.⁸⁷ Thus, if a group of dealers pressures a common supplier to cut off a rival dealer from a necessary resource, they may well be committing a per se violation of the antitrust laws.⁸⁸ For example, in *United States v. General Motors Corp.*, the Supreme Court held that an attempt by Los Angeles-area General Motors dealers to defeat rival discounters by inducing General Motors to cut off the discounters constituted a per se illegal group boycott.⁸⁹

One of the problems with evaluating classic group boycotts under the antitrust laws is that they are difficult to distinguish from cases in which a supplier for non-price-related reasons of its own decides to cut off a distributor.⁹⁰ A distinction between the two situations is crucial for two reasons. First, in cases involving the latter pattern, the defendant's conduct is evaluated under a rule-of-reason analysis, if not given de facto, per se, *legal* status.⁹¹ Second, if the supplier's decision

into a market is likely did not originate with this article and does not depend on the acceptance of a micro-microeconomic approach to antitrust law. See 4 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 917c, at 88 (1980); see also *Echlin*, 105 F.T.C. at 498 (Bailey, Commr., dissenting); Yoerg, Hill & Leddy, *supra* note 74, at 1272 (indicating that the Antitrust Division of the Justice Department in practice relies heavily on historical patterns of entry in assessing the likelihood of new entry). A focus on managers as the key actors in antitrust law does, however, strengthen the importance of a demonstrated history of successful entry. Once a firm has successfully entered the market, riskiness of entry as perceived by managers of other would-be entrants is probably decreased. Aside from a herd instinct pushing managers toward the now tried-and-true path, the managers may subscribe to the maxim that "what one fool can do, so can another."

84. See, e.g., B. KELLMAN, *supra* note 66, at 41.

85. See *id.* at 41-42.

86. L. SULLIVAN, *HANDBOOK OF THE LAW OF ANTITRUST* 232 (1977).

87. See *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.*, 472 U.S. 284, 293-94 (1985).

88. See, e.g., B. KELLMAN, *supra* note 66, at 51-52.

89. 384 U.S. 127, 146-48 (1966).

90. See Gerla, *Discounters and the Antitrust Laws: Faces Sometimes Should Make Cases*, 12 J. CORP. L. 1, 25-26 (1986).

91. *Compare Burlington Coat Factory Warehouse Corp. v. Esprit De Corp.*, 769 F.2d 919

is truly unilateral, its conduct lies outside the scope of section 1 of the Sherman Act, which prohibits only concerted actions.⁹²

In light of classical microeconomic theory, many present day anti-trust suits involving claims by plaintiffs that competitors on the same level of distribution have pressured powerful suppliers to cut off the plaintiffs from goods or other items needed for continuance of their businesses⁹³ seem somewhat incredible. As Tyler Baker put it:

In general, it would be unlikely that an individual dealer could force a manufacturer to take action against its own interest. . . . It [also] seems relatively unlikely that even coordinated dealer pressure in one regional market could force a firm to make a nationwide policy decision with which it fundamentally disagreed.⁹⁴

If *Matsushita* is taken to its logical extreme, many of these anti-trust suits should be dismissed on motion for summary judgment because they are microeconomically implausible.⁹⁵ Indeed, some commentators have questioned the result in *General Motors* itself on the ground that the government's claim in that case was dubious as a matter of microeconomic theory.⁹⁶

In *General Motors*, the vehicle through which GM sought to discipline dealers who engaged in discounting was the location clause in the dealership franchise agreement.⁹⁷ This clause required GM deal-

(2d Cir. 1985) (upholding a distributor termination made because distributor was not properly displaying supplier's wares) and *A.H. Cox & Co. v. Star Mach. Co.*, 653 F.2d 1302 (9th Cir. 1981) (upholding distributor termination by supplier who wanted to implement system of exclusive distributorships), with *Service Merchandise Co. v. Boyd Corp.*, 722 F.2d 945 (1st Cir. 1983) and *Com-Tel, Inc. v. DuKane Corp.*, 669 F.2d 404 (6th Cir. 1982) (upholding liability in cases where distributor termination motivated by pressure from coalition of terminated distributor's competitors).

Some courts and commentators have questioned whether the distinction between classic group boycotts, and dealer-initiated nonprice terminations, is feasible or meaningful. See, e.g., *Business Elec. Corp. v. Sharp Elec. Corp.*, 780 F.2d 1212, 1217-18 (5th Cir. 1986), cert. granted, 107 S. Ct. 3182 (1987); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982); Baker, *Interconnected Problems of Doctrine and Economics in the Section One Labyrinth: Is Sylvania A Way Out?*, 67 VA. L. REV. 1457, 1488-93 (1981); Liebler, *Intrabrand "Cartels" Under GTE Sylvania*, 30 UCLA L. REV. 1, 10-13 (1982). Nonetheless, controlling Supreme Court precedent requires that the distinction be made. See *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 58 n.28 (1977) (although vertical nonprice restraints are to receive rule-of-reason treatment, horizontal restrictions "originating in agreements among retailers" remain per se illegal) (citing *United States v. General Motors Corp.*, 384 U.S. 127 (1966)).

92. See, e.g., *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919); *Garment Dist., Inc. v. Belk Stores Servs., Inc.*, 799 F.2d 905, 908 (4th Cir. 1986); *O.S.C. Corp. v. Apple Computer, Inc.*, 601 F. Supp. 1274, 1290 (C.D. Cal. 1985), *aff'd.*, 792 F.2d 1464 (9th Cir. 1986).

93. E.g., *Garment Dist., Inc. v. Belk Stores Servs., Inc.*, 799 F.2d 905, 907 (4th Cir. 1986); *National Marine Elec. Distrib., Inc. v. Raytheon Co.*, 778 F.2d 190, 191-92 (4th Cir. 1985); *Burlington Coat Factory Warehouse Corp. v. Esprit De Corp.*, 769 F.2d 919, 921-22 (2d Cir. 1985).

94. Baker, *supra* note 91, at 1507-08.

95. See text at notes 4-8 *supra*.

96. Baker, *supra* note 91, at 1501-04; Liebler, *supra* note 91, at 31-36.

97. 384 U.S. 127, 139 (1966).

ers to sell only at the location specified in their contract.⁹⁸ If GM, in cutting off discounting dealers, was merely attempting to enforce its own vertical territorial restraints, as opposed to bowing to pressure from a coalition of its dealers, that action would today either get rule-of-reason treatment (under the law as enunciated by the Court in *Continental T.V., Inc. v. GTE Sylvania, Inc.*⁹⁹) or, perhaps more likely, be held to be totally outside the ambit of section 1 of the Sherman Act because such action was "unilateral" on the part of GM.¹⁰⁰

The spectacle of a group of automobile dealers forcing one of the United States' largest corporations to adopt a policy which ran contrary to its own interests does seem to be economically farfetched. In fact, the claim seems so farfetched from a classical microeconomic perspective that if the government were to bring a similar action today, it might be subject to dismissal on motion for summary judgment under *Matsushita*. According to some microeconomic theorists, GM had no interest in preventing sales by discounters because the firm wanted to increase total sales.¹⁰¹ Thus, the only reason GM cut its own revenues by enforcing the location clauses against the discounters was to increase its long-term profitability by protecting its franchise system from disruption by free-riding discounters.¹⁰²

Similar reasoning can be used to reject many contemporary claims involving pressure by rival distributional outlets on mutual suppliers. For example, take the typical scenario in which an established, traditional, full-price retail outlet allegedly pressures a supplier to cut off a rival discounter by threatening to withdraw its business from the supplier.¹⁰³ Under microeconomic theory, the supplier faced with a choice between the two outlets will pick the one which maximizes its profits. In theory, that should be the discounter, given its higher sales volume.¹⁰⁴ If the supplier chooses the traditional retailer, it must be because using that outlet somehow provides a more efficient means of distributing the supplier's goods. The efficiencies most often alleged by modern microeconomists are the prevention of free riding by dis-

98. 384 U.S. at 139.

99. 433 U.S. 36 (1977).

100. See note 92 *supra*.

101. Liebel, *supra* note 91, at 32.

102. See Baker, *supra* note 91, at 1502; Liebel, *supra* note 91, at 32-33; Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision*, 45 U. CHI. L. REV. 1, 7 (1977).

103. See note 93 *supra*.

104. See E. GELLHORN, *supra* note 49, at 284 (manufacturer's interest is in having its sellers sell more of its product, so long as the wholesale price the manufacturer receives does not drop); Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. 135, 147 (1984) (manufacturers desire the lowest possible retail price to sell more units).

count outlets, the validation function of more prestigious outlets, or the rental of desirable shelf space by the supplier.¹⁰⁵ It follows inexorably from this chain of reasoning that if the supplier chooses to cut off the discounter, it does so to enhance its efficiency in distributing its products, and the supplier's decision, as a vertical territorial restraint, should be reviewed under a rule-of-reason analysis (if it is not per se legal under the antitrust laws¹⁰⁶) or be exempt from scrutiny under section 1 of the Sherman Act because of a lack of concerted action.¹⁰⁷

The problem with the microeconomists' neat scenario, in which suppliers (be they contemporary suppliers of discounters or GM in the 1950s and 1960s) are merely enforcing their own contractual rights in their own best interests, is that the scenario contains a fundamentally erroneous assumption: that the outlets are pressuring "the suppliers." A decision by a supplier to cut off or restrain a customer is not made by "the supplier," but by the human managers of the supplier. When we view that decision in light of the interests and behavior of those managers, a rather different outcome than that posited by classical microeconomists may in fact occur.

A reexamination of the situation in which traditional, full-price retail outlets pressure the managers of a powerful mutual supplier to stop selling to rival discounters demonstrates the differences between theoretical profit-maximizing firms and real-world firms run by human managers. While continued dealings with the discounters may be in the long-term interests of a supplier from a profit-maximizing perspective, such a course of action may not be in the interests of the supplier's managers. First, if the traditional retailers stop dealing with the supplier, the supplier's short-run sales and profits may decline.¹⁰⁸ Of course, this short-run decline may eventually be more than offset by increased sales through the discounters.¹⁰⁹ Unfortunately, such a

105. See, e.g., R. BORK, *supra* note 1, at 435; H. HOVENKAMP, *supra* note 14, at 253-58 (emphasizing the free rider problem); Goldberg, *The Free Rider Problem, Imperfect Pricing, and the Economics of Retailing Services*, 79 NW. U. L. REV. 736 (1984) (emphasizing the shelf space and validation functions of vertical restraints).

106. See Baker, *supra* note 91, at 1467-68; Phillips & Mahoney, *Unreasonable Rules and Rules of Reason: Economic Aspects of Vertical Price-Fixing*, 30 ANTITRUST BULL. 99 (1985) (arguing for rule-of-reason treatment for vertical restraints); Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 8 (1981) (arguing for per se legality for vertical restraints); see also Liebler, *supra* note 91 (arguing for per se legal treatment of all restraints imposed within same brand).

107. See note 92 *supra*.

108. See Steiner, *The Nature of Vertical Restraints*, 30 ANTITRUST BULL. 143, 162 (1985) (alternate channels of distribution may not have reached a "critical mass size" large enough to make up for traditional retailers who refuse to carry a supplier's wares).

109. Discounters tend to be high-volume outlets. See E. CUNDIFF, R. STILL & N. GOVONI, *FUNDAMENTALS OF MODERN MARKETING* 222 (4th ed. 1985); C. SCHEWE & R. SMITH, *MARKETING: CONCEPTS AND APPLICATIONS* 419 (2d ed. 1983).

turnaround may take some time. As we have seen, contemporary American managers tend to look almost exclusively to the short run.¹¹⁰ Thus, the short-run diminution in profits caused by the loss of the traditional retailers' business may unjustifiably outweigh the long-run increase in profits that could be garnered through continued sales to the discounters. Second, by not remedying the traditional retailers' complaints, the managers may be violating a commandment of modern American management practice: "[T]hou shalt not make waves."¹¹¹ The complaints by long-time customers cannot reflect well on the managers' ability to keep things running smoothly. Of course, the discounters will complain to the suppliers if *they* are cut off; however, their complaints may not create the same level of dissatisfaction as the complaints of traditional retailers. First, the traditional retailers may have the advantage of numbers.¹¹² Thus, they can generate a larger volume of complaints than the discounters. Second, and more importantly, the conventional retailers may have been dealing with the supplier for a longer time than the discounters. The longer course of dealing can give the traditional retailers superior personal contacts among the supplier's management.¹¹³ These superior contacts can result in the traditional retailers' complaints being seen as generating more of a "problem" than the discounters' complaints. In sum, if the managers follow their own rules of the game rather than act as profit-maximizing robots, they may well succumb to the pressure of buyers without market power even if such a capitulation is not in the best interests of their employer.

The possibility of management capitulating to further their personal interests exists even in the case of a firm as large and powerful as GM. The nondiscounting dealers in *General Motors* probably did not have a feasible means of switching their franchises to another automaker. Therefore, they probably could not pressure GM's management by creating a short-run reduction in sales of Chevrolets. The dealers did, however, possess a credible threat of making the GM officials responsible for dealer relations appear to be making great "waves" within the company. In fact, the Los Angeles Chevrolet Dealers Association "flood[ed] General Motors and the Chevrolet Division with letters and telegrams asking for help" in stopping discount-

110. See text at note 44 *supra*.

111. See text at note 48 *supra*.

112. Historically, traditional retailers have used their large numbers to combat innovative retail competitors. See J. PALAMOUNTAIN, *THE POLITICS OF DISTRIBUTION* 44-45 (1955).

113. See generally R. CIALDINI, *INFLUENCE* 173-84 (1984) (detailing psychological evidence establishing that persons are more trusting of those with whom they are familiar).

ing.¹¹⁴ The arrival of a flood of complaining letters and telegrams from dealers did not instill confidence in the superiors of those managers charged with dealer relations. A cutoff of discounters through enforcement of the locations clauses was not likely to generate the same amount of controversy within the company because the outlets dealing with the discounters were vastly outnumbered by the ordinary automobile dealers.¹¹⁵ The managers of GM may have yielded to dealer pressure not to advance the long-term interests of the automaker, but to advance the short-term management objective of not being seen as "making waves" within the company.¹¹⁶

Focusing on managers rather than on profit-maximizing firms as key economic actors does not necessarily mean that the actions of GM in the early 1960s, or the actions of contemporary firms which have stopped dealing with discounters after complaints by traditional retailers, were the product of self-interested decisions by the firms' managers. What a micro-microeconomic approach does suggest is that a competitor can, by taking advantage of the modern style of American management, induce a much larger supplier to terminate the competitor's rival even though such a termination is not in the best long-run interests of the supplier. This micro-microeconomic insight has a number of significant implications for contemporary antitrust law.

First, we should reject the claim made by some commentators (and uncritically accepted by at least one United States Court of Appeals) that no meaningful difference exists between a distributional restraint unilaterally imposed by a supplier and a termination foisted upon the supplier by any of its outlets which lack market power.¹¹⁷ Perhaps in the theoretical world of microeconomics no supplier will bow to pres-

114. *United States v. General Motors Corp.*, 384 U.S. 127, 134 (1966).

115. Of the 85 Chevrolet dealers in the Los Angeles area, only a dozen were selling through discounters. 384 U.S. at 132.

116. By not immediately terminating the dealers supplying discounters, the Chevrolet zone manager for Los Angeles was certainly "making waves" within GM. Within a week of the receipt of the flood of telegrams, this manager's superiors in Detroit ordered him to furnish "a detailed report of the discount house operations . . . as well as what action we in the Zone are taking to curb such sales." 384 U.S. at 134.

At the time the events described in the case took place, GM placed a particularly heavy emphasis on its managers acting as "team players." One observer described the atmosphere at GM as follows:

Those pledges willing to obey the rules were promoted. In the vernacular, they were the company's "team players." Those who didn't fit into the mold . . . who didn't adhere to the rules . . . generally weren't promoted. "He's not a team player," was the frequent, and many times only, objection to an executive in line for promotion. It didn't mean he was doing a poor job. It meant . . . *[h]e rocked the boat.*

J. WRIGHT, ON A CLEAR DAY YOU CAN SEE GENERAL MOTORS 40 (1979) (emphasis added).

117. For claims that no meaningful distinction exists, see Liebler, *supra* note 91, at 8-13. See also *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982) (Posner, J.) (dictum). This view was recently accepted by the United States Court of Appeals for

sure from one of its outlets without market power. Under this view, any restriction the supplier adopts in response to pressure from its outlets would have been adopted even without that pressure. In the real world of American firms, however, human managers may bow to such pressure to further their personal interests. We should not automatically assume that the true impetus for such a restriction stemmed from the supplier rather than from the outlets.

Second, claims that suppliers ceased to deal with discounters at the behest of rivals should not be dismissed out-of-hand merely because the coalition of rivals seems to lack market power.¹¹⁸ A micro-economic approach to antitrust law demonstrates that even firms without market power can damage rivals and reduce competition by taking advantage of the tendencies of American management to look to short-run profits and to avoid causing internal corporate friction.

Third, vertical restraints which currently receive rule-of-reason treatment should be examined carefully to see if the restraints are truly vertical rather than horizontal restraints foisted on the supplier by an outlet or a coalition of outlets. One of the justifications for according territorial vertical restraints rule-of-reason treatment is that the supplier imposing the restraint lacks the anticompetitive motive that competitors would possess had they imposed the very same restraint.¹¹⁹ One of the traditional counters to this justification is that the restraint may in fact be the product of a horizontal dealer cartel rather than of the supplier's independent judgment.¹²⁰ A focus on the managers of suppliers as the key actors in antitrust scenarios strongly supports this traditional counter by demonstrating how suppliers can be coerced into applying "vertical" restraints much more easily than static microeconomic models would predict. The ease with which outlets can in fact coerce suppliers into imposing restraints justifies a careful look into whether an apparent vertical restraint is truly vertical or is instead a horizontal restraint clothed in the garb of a vertical restraint.¹²¹

the Fourth Circuit. *Garment Dist., Inc. v. Belk Stores Servs., Inc.*, 799 F.2d 905, 909 (4th Cir. 1986).

118. For an argument that coalitions of distributors which lack market power are unlikely to force a supplier to adopt policies contrary to its self-interest, see Baker, *supra* note 91, at 1507-08. For a more general argument that proof of any antitrust violation ought to require that the defendant possess market power, see Easterbrook, *The Limits of Antitrust*, 63 TEXAS L. REV. 1, 19-23 (1984).

119. *E.g.*, R. BORK, *supra* note 1, at 290.

120. *E.g.*, H. HOVENKAMP, *supra* note 14, at 248-49.

121. That distributors are able to coerce managers of suppliers to impose "vertical" restraints, even when those restraints may not be in the best long-term interests of the supplier, is supported by observations of two former antitrust-enforcement officials that many so-called verti-

C. Collusion Among Competitors

Price-fixing arrangements and market allocations among competitors have long been subject to per se condemnation under the antitrust laws.¹²² The vast majority of commentators, from populist to Chicago School devotee, agree with the out-of-hand condemnation of both practices, especially when such practices have no legitimate enterprise to which they are ancillary.¹²³ Classical microeconomics does not suggest that price fixing and market allocations are beneficial to consumers. Indeed, classical microeconomic analysis suggests that cartels engaging in those practices are apt to cause a net social-welfare loss.¹²⁴ Classical microeconomics also suggests, however, that the harm caused by such arrangements may be more minimal or short-lived than might be supposed given the harsh treatment of the practices under the antitrust laws.

Microeconomists point out that cartels are extremely fragile. Two phenomena, market entry and cheating, eventually tend to undermine cartels. As a cartel begins to reap supracompetitive profits, the high prices charged by its members will lure other firms into the market.¹²⁵ The members of the cartel can, of course, attempt to co-opt the new entrants by having them join the cartel. Such a course, however, plants the seeds for the cartel's demise. First, the larger the number of participants in the cartel, the greater the problems of coordination and enforcement of cartel agreements.¹²⁶ Second, the larger the number of participants in the cartel, the greater the likelihood that at least one of the participants will begin to engage in the activity which will eventually bring down the arrangement — cheating on the terms of the cartel

cal restraints are in reality horizontal restraints imposed by distributor cartels. See Litvack, *The Future Viability of the Current Antitrust Treatment of Vertical Restraints*, 75 CALIF. L. REV. 955, 957 (1987) ("[M]ost resale price maintenance schemes are hatched, nurtured, or preserved by the retailers in a cartel-like manner. That is the reality."); Pitofsky, *Antitrust in the Next 100 Years*, 75 CALIF. L. REV. 817, 831 (1987) ("In most instances, vertical price fixing is adopted to placate powerful groups of distributors who induce suppliers to assist dealer cartels. . . .").

122. See *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) (condemning horizontal price-fixing as per se illegal); *United States v. Topco Assoc., Inc.*, 405 U.S. 596 (1972) (condemning horizontal market divisions as per se illegal).

123. See, e.g., R. BORK, *supra* note 1, at 267 (price-fixing and market-division agreements which have no legitimate ancillary justification should be subject to per se condemnation); L. SULLIVAN, *supra* note 86, at 203-04, 224-29 (commentator with populist leanings arguing that price-fixing and market-division conspiracies should be per se illegal). But see Easterbrook, *supra* note 118 (even restraints of trade having no procompetitive justification should not be condemned under the antitrust laws if the firms imposing them lack market power).

124. See R. BORK, *supra* note 1, at 263-64; H. HOVENKAMP, *supra* note 14, at 83-84.

125. F. SCHERER, *supra* note 15, at 173.

126. H. HOVENKAMP, *supra* note 14, at 90-91.

agreement.¹²⁷

A participant in a cartel has a tremendous incentive to cheat on the arrangement — the prospect of huge profits. A cartel member, by secretly charging a lower (but still profit-making) price while its fellow members charge the cartel price, can increase sales volumes and profits.¹²⁸ The fragility is even greater where the cartel arrangement is a somewhat loose one that allows some sales by participants outside the bounds of the cartel arrangement.¹²⁹ In effect, such an arrangement allows official cheating on the cartel. Microeconomists tell us that cheating will eventually cause all cartels to dissolve.¹³⁰

Finally, microeconomists suggest that firms lacking market power (or its traditional surrogate, market share) cannot form an effectual cartel.¹³¹ If, for example, two small firms attempt to raise prices by cutting their output, the noncartel members will simply raise their output.¹³² The net result will be that prices and total output will remain stable, and the two cartel members will lose market share, having cut their own throats.¹³³ Thus, for example, the only likely result of a price-fixing cartel between two small grocery stores in an area served by numerous grocery outlets is to ensure the demise of the two price-fixing grocery stores.

A micro-microeconomic approach to antitrust law does not necessarily indicate that the conclusions drawn through classical microeconomic analysis are incorrect. However, a focus on managers as key actors rather than on firms does indicate the following: (1) Cartels are much more stable than classical microeconomics would predict; (2) Managers frequently will not seize even highly profitable opportunities to cheat on a cartel, whether those opportunities need to be taken in secret or can be grasped openly; (3) The co-optation of a new entrant into the cartel is much easier than one would suppose; and (4) Price-fixing or market-division cartels can diminish competi-

127. See C. FERGUSON, *MICROECONOMIC THEORY* 359-60 (3d ed. 1972); J. HIRSHLEIFER, *PRICE THEORY AND APPLICATIONS* 261-62 (3d ed. 1984); F. SCHERER, *supra* note 15, at 171.

128. See J. HIRSHLEIFER, *supra* note 127, at 261-62; H. HOVENKAMP, *supra* note 14, at 83-85; F. SCHERER, *supra* note 15, at 172-73.

129. Classical microeconomics questions the concept of a "loose" cartel in which the participants are allowed to engage in transactions outside the bounds of the cartel. Cf. H. HOVENKAMP, *supra* note 14, at 134 ("[N]o cartel could restrict its output and raise price if it permitted its members freely to come and go, or to make unlimited 'non-cartel' sales.").

130. See note 127 *supra*; see also W. SHEPHERD & C. WILCOX, *PUBLIC POLICIES TOWARD BUSINESS* 196 (6th ed. 1979).

131. See, e.g., Easterbrook, *supra* note 118, at 20.

132. See *id.*

133. *Id.*

tion and have adverse economic effects even where the members of the cartels collectively lack market power.

As discussed, cheating on a cartel makes eminent sense from the perspective of a profit-maximizing firm.¹³⁴ From the perspective of the managers of the firm, the decision whether to cheat on the cartel arrangements may not be so simple. Cheating on a cartel does create the opportunity for large short-run profits, and, as noted, modern American managers highly value short-run profits.¹³⁵ Thus, a concord of interest between the profit-maximizing firm and its human managers would seem to exist, and cheating on cartels would seem to be a frequent and predictable occurrence. However, a more careful examination of the motivation of the managers of members or putative members of a cartel indicates that from the perspective of those managers, the case for cheating is not clear-cut.

Cheating on the cartel arrangement involves a large degree of risk. If the cheating is detected, full-scale competition may erupt. Full-scale competition will, of course, diminish profitability.¹³⁶ In the eyes of managers contemplating cartel cheating, the risk of such competition may outweigh the lure of large short-run profits.

Managers of a cartel member who are thinking of cheating are faced with a choice between two alternatives. The first alternative is to continue cooperating in the cartel and take the sure profits that the firm has been garnering from the arrangement. The other alternative is to cheat, thereby making even higher profits. Unfortunately, this prospect of higher profits is coupled with a risk of diminished profits if full-scale competition erupts. Experimental psychology suggests that people (including business managers) are risk averse when it comes to potential gains.¹³⁷ The average person believes that, in the search for profits, the bird in the hand is better than two in the bush.¹³⁸ The data generated by experimental psychology indicate that the typical manager will choose to take the sure profits generated by continued cooperation in the cartel rather than run the risk of diminished profits should the attempt at cheating be discovered. The tendency of contemporary management to eschew risks (at least when not facing the prospect of a near-certain loss) suggests that managers will take the

134. See note 128 *supra* and accompanying text.

135. See notes 42-44 *supra* and accompanying text.

136. See F. SCHERER, *supra* note 15, at 13-14. Moreover, the threat of diminished profits through open competition may be augmented by various strategic moves on the part of cartel members designed to "punish" cheaters. See Ayers, *How Cartels Punish: A Structural Theory of Self-Enforcing Collusion*, 87 COLUM. L. REV. 295 (1987).

137. See note 47 *supra*.

138. S. MAITAL, *supra* note 23, at 198-200.

certain profits from continued cooperation rather than run the risks of full competition.¹³⁹

The threat to profits posed by the resumption of full-scale competition is not the only deterrent to managers considering cheating on collusive arrangements. Full-scale competition introduces uncertainty into the previously comfortable world of the managers of a cartel member. Suddenly, managers must unilaterally make difficult decisions on pricing and market strategy that were previously made jointly by the cartel. Moreover, the outcome of any such unilateral decisions may be quite uncertain. Uncertainty discomforts most human beings, including managers.¹⁴⁰

Perhaps the most serious threat posed by the resumption of full-scale competition is that it undermines the very ability of managers to pursue their own interests. As economist Harvey Leibenstein has pointed out, the more competitive a market, the less scope for managerial discretion.¹⁴¹ Managers, therefore, desire "shelters" from competition. As Professor Leibenstein put it:

Monopoly gives license for a high degree of discretionary behavior. It is a license for some in powerful positions to be arbitrary, sloppy, bureaucratic, arrogant and nonresponsive to the internal demands of other members of the firm. Competitive pressures do not eliminate such possibilities but they reduce the area of discretionary behavior. The obverse of license is obligation. Monopoly does not provide a sense of obligation for the monopolist to be considerate to fellow employees or to customers. Strictly speaking, neither does competition, but indirectly competition does provide pressures and incentives to do so.¹⁴²

Managers of firms in cartels may avoid cheating on the cartel (or avoid taking the opportunity to engage in extracartel transactions if the cartel is loose enough to allow such transactions) in order to preserve the very shelters which allow them to pursue personal goals independent of the firm which employs them. While cheating on cartel arrangements may be the winning move for a profit-maximizing firm, the threat to profits posed by full-scale competition, the increase in uncertainty generated by such competition, and the desire to seek shelters from competition in order to pursue personal goals, all combine to make cheating on a cartel a less desirable alternative from the standpoint of the manager seeking to advance his career.

A micro-microeconomic approach to antitrust law also indicates

139. See notes 46-47 *supra* and accompanying text.

140. See D. KRECH, R. CRUTCHFIELD & N. LIVSON, *ELEMENTS OF PSYCHOLOGY* 461 (3d ed. 1974).

141. H. LEIBENSTEIN, *supra* note 23, at 207-08.

142. *Id.*

that new entry is not a short-run panacea for collusive behavior among competitors. First, as mentioned, new entry into markets with supracompetitive profits generated by collusion is not as common as predicted by classical microeconomic models.¹⁴³ Second, co-optation of new entrants into the cartel is much easier than would be predicted by microeconomic models. A new entrant in a market dominated by a cartel can earn large profits by undercutting the cartel.¹⁴⁴ However, the managers of the new entrant, in deciding whether to undercut the cartel, face the same personal risks as do the managers of an existing cartel member who are considering cheating on the cartel. Competition by the new entrant threatens to lower profits, create uncertainty, and undermine the atmosphere which allows managers to pursue personal goals.¹⁴⁵ Thus, while vigorous competition by the new entrant may be the preferred strategy for the theoretical profit-maximizing firm, the real-world managers who run the firm may view cooperation with the cartel as the best strategy.

Finally, contrary to microeconomic theory, a micro-microeconomic approach suggests that collusive arrangements among firms which ostensibly lack market power may cause competitive harm. Micro-microeconomic theory suggests that managers of firms seek shelters from competition not necessarily to increase profits, but to avoid pressures to minimize costs and to create a more permissive atmosphere for arbitrary behavior by those managers.¹⁴⁶ Short of attaining a monopoly or creating a cartel including all firms in the market, the managers cannot create a completely sheltered environment. Nonetheless, managers are often content with "partial" shelters from what they believe is "excessive" competition.¹⁴⁷ When managers of firms without market power enter into collusive arrangements with competitors, they may not be seeking to influence the market price for their firms' goods, but to create partial shelters from competition through neutralization of what they perceive to be the most salient source of competitive pressure on them. In effect, the managers are seeking limited "peace treaties" with the managers of their most intense competitors.

These treaties, even if concluded between firms with small market shares, run contrary to the basic mandate of the antitrust laws — that competitors compete vigorously on the merits of their products — and

143. See notes 57-73 *supra* and accompanying text.

144. See notes 125 & 128 *supra* and accompanying text.

145. See notes 136-42 *supra* and accompanying text.

146. See H. LEIBENSTEIN, *supra* note 23, at 228-30.

147. *Id.*

ought to be objectionable on that ground alone.¹⁴⁸ Moreover, the implementation of such treaties injures consumers and societal productive efficiency even where the "signatories" collectively lack market power. For example, when the managers of two small firms enter into a collusive arrangement, they are most likely entering into a treaty with the managers of the firm which they view as placing the most competitive pressure on them. Micro-microeconomic theory suggests that even this "partial shelter" will allow the managers of the two firms to pursue wasteful and inefficient management policies or, as economist Harvey Leibenstein puts it, to generate "X-inefficiencies."¹⁴⁹

The economic problems created by the conclusion of collusive treaties goes beyond the generation of internal inefficiencies. The ability to create the partial shelter does not depend on the ability to control overall price competition; it merely depends on the capacity to dampen what the managers perceive as the source of their most intense competition. Thus, numerous individual treaties (as opposed to an all-encompassing cartel) may exist in a given market. This proliferation of treaties has the obvious effect of multiplying the X-inefficiencies in the firms entering into them. More significantly perhaps, a proliferation of collusive treaties can change the tone of a market from one of aggressive competition to one of "gentlemanly competition."¹⁵⁰ This change in market style can lead to an even greater opportunity for managers to pursue their inefficient personal goals because gentlemanly competition is itself a shelter under which X-inefficiency can flourish.

Micro-microeconomic theory also suggests that the costs of X-inefficiencies generated under the protection of noncompetition treaties may be passed to consumers even if many firms in the market remain fully competitive. Classical microeconomic theory postulates that if a firm attempts to pass higher costs on to consumers, they will desert the firm for its lower-price competitors.¹⁵¹ Micro-microeconomic theory,

148. Cf. Fox, *The Modernization of Antitrust: A New Equilibrium*, 66 CORNELL L. REV. 1140, 1154 (1981) (emphasizing preservation of the competition process as the key goal of the antitrust laws); Sullivan, *The Viability of the Current Law on Historical Restraints*, 75 CALIF. L. REV. 835, 853 (1987) ("protecting the competitive process is what antitrust is about").

149. H. LEIBENSTEIN, *supra* note 23, at 228-30.

150. "Gentlemanly competition" refers to a market in which the participants, while being ostensible competitors, do not compete vigorously, but are satisfied with earning a "good living" and not "rocking the boat." See Gerla, *supra* note 90, at 6 n.26. From the consumer's perspective, the presence of competitors engaged in gentlemanly competition can be extremely detrimental because the individual strategies and styles of competitors can be more important in yielding the lowest delivered cost to consumers than the aggregate number of firms in a market. See J. BOWER, *THE TWO FACES OF MANAGEMENT* 182-83 (1983).

151. E.g., R. BORK, *supra* note 1, at 92-93.

however, recognizes the common-sense reality that consumers often do not seek out the lowest price. Consumers, like firms, are neither profit-maximizers nor cost-minimizers. The unwillingness of consumers to maximize their utility may be caused by a number of factors. First, consumer behavior may be more often characterized by habit and reflex than by careful calculation.¹⁵² A consumer may ignore a price increase occasioned by a collusive arrangement because the consumer is acting on instinct rather than on cold calculation. Second, for emotional or practical reasons, it may not be worth the bother for the consumer to seek out new sources of supply.¹⁵³ Third, many consumer transactions may not be made by the actual consumers themselves, but by their household agents.¹⁵⁴ While the actual consumer might be price sensitive, his agent may not be.¹⁵⁵ For example, the person responsible for food preparation may be very cognizant of changes in the price of groceries. If, however, that person delegates the task of grocery shopping to someone else, the agent may be much more interested in factors such as the time shopping will consume or the ambience of the store than in the change in the price of groceries. In sum, consumers are not maximizers but are selectively rational. Therefore, they can be adversely affected even by small competitors who agree not to compete.

The insights gleaned from a micro-microeconomic approach yield two important policy implications for the application of antitrust law to competitor collusion. First, the antitrust laws should be used to attack cartels. The problem of competitor collusion will not automatically be solved by cheating or new entry.¹⁵⁶ This suggestion should

152. See G. KATONA, *THE POWERFUL CONSUMER* 139-45 (1960).

153. Of course, the notion that consumers may pay a supracompetitive price because they cannot or will not search for a superior deal is theoretically alien to classical microeconomics; under the classical microeconomic model, consumers are assumed to possess perfect information. *E.g.*, J. HENDERSON & R. QUANDT, *MICROECONOMIC THEORY: A MATHEMATICAL APPROACH* 136-37 (3d ed. 1980). Even economists now recognize that the search for information by consumers entails its own costs and that because of these costs consumers may lack perfect information. As Professors Heilbroner and Thurow put it,

Who has time to investigate which brand of toothpaste is really best or even tastes best? Even professional buyers, such as industrial purchasing agents, cannot know every price of every product, including all substitutes.

The lack of information can be remedied, at least up to a point; but the remedy costs money or its equivalent — time. Few of us have the resources or patience to do a complete research job on every item we buy. Would it even be rational to do so?

R. HEILBRONER & L. THUROW, *UNDERSTANDING MICROECONOMICS* 176 (4th ed. 1978). The technical economic term for the cost to consumers of acquiring information on alternative sources of supply is "search costs." *E.g.*, Schwartz & Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630, 635 (1979).

154. H. LEIBENSTEIN, *supra* note 23, at 196.

155. See *id.*

156. See notes 57-73 and 134-42 *supra* and accompanying text.

not be controversial. Indeed, even devotees of the Chicago School seem to agree with this proposition even though it runs contrary to their faith in efficient, self-correcting markets.¹⁵⁷

The second policy implication is more controversial: The antitrust laws should be used to attack cartels even where the members collectively lack market power.¹⁵⁸ Such combinations frustrate a basic value the antitrust laws were meant to promote — the competitive process.¹⁵⁹ A micro-microeconomic approach supplies additional reasons for attacking collusive arrangements among competitors lacking market power. This approach suggests that these arrangements are economically wasteful because they promote X-inefficiencies in firms¹⁶⁰ and because they diminish competition by changing the tone of a market from competitive to complacent.¹⁶¹ Consumers may bear the costs of such inefficiencies because they frequently behave in a non-profit-maximizing fashion.¹⁶²

While the concept that market power should not be used as a *sine qua non* of antitrust liability may offend devoted followers of the Chicago School, the concept is fully consistent with current Supreme Court antitrust jurisprudence. The Court, in the very same Term it decided *Matsushita*, reiterated its position that establishment of liability for practices which were per se violations of the antitrust laws did not require proof that the defendants possessed market power.¹⁶³ A micro-microeconomic approach to antitrust law suggests that the Court is correct in this stance. Indeed, a micro-microeconomic approach to antitrust law suggests that the Court's most controversial decision in the price-fixing area in recent years, *Arizona v. Maricopa County Medical Society*,¹⁶⁴ was in fact correctly decided.

In *Maricopa*, the State of Arizona challenged "maximum" price-fixing arrangements involving doctors in two counties and the county medical societies to which the doctors belonged. Each medical society set up a "foundation" that established a schedule of maximum fees its

157. See note 72 *supra*.

158. For the position that antitrust law should *not* be used to attack combinations lacking market power, see Easterbrook, *supra* note 118, at 20-21. See also Note, *Fixing the Price Fixing Confusion: A Rule of Reason Approach*, 92 YALE L.J. 706, 729 (1983).

159. See note 148 *supra* and accompanying text.

160. See notes 146-49 *supra* and accompanying text.

161. See note 150 *supra* and accompanying text.

162. See notes 152-55 *supra* and accompanying text.

163. *FTC v. Indiana Fedn. of Dentists*, 106 S. Ct. 2009, 2018-19 (1986). In fact, the Court went so far as to hold that even under a rule-of-reason analysis, the possession of market power by the defendants need not always be demonstrated. 106 S. Ct. at 2018-19.

164. 457 U.S. 332 (1982).

members would charge.¹⁶⁵ The foundations negotiated arrangements with various insurance companies whereby member doctors treating patients insured by the companies would bill the insurance companies no more than the maximums set by the foundation and would agree to accept the payments from the insurance companies as payment in full.¹⁶⁶ In a 4-3 decision, the Court held the arrangement to be a per se illegal maximum price-fixing arrangement.¹⁶⁷

The decision in *Maricopa* has occasioned a great deal of criticism.¹⁶⁸ Much of the thrust of this criticism is that the Court ignored the economic efficiencies that the maximum-fee arrangement allegedly generated and the utility of these efficiencies in containing rising health-care costs.¹⁶⁹ What led the Court to reject these purported "efficiencies" was not perversity or ignorance, but a profound suspicion of the need for competing doctors to be engaging in health-care cost containment when a customer of the competitors (insurance companies) could perform the task as well or perhaps even better. As Justice Stevens noted:

It is true that a binding assurance of complete insurance coverage — as well as most of the respondents' potential for lower insurance premiums — can be obtained only if the insurer and the doctor agree in advance on the maximum fee that the doctor will accept as full payment for a particular service. Even if a fee schedule is therefore desirable, it is not necessary that the doctors do the price fixing. . . . The [Arizona Comprehensive Medical/Dental Program for Foster Children] and the Blue Shield Plan challenged in *Group Life & Health Insurance Co. v. Royal Drug Co.*, 440 U.S. 205 (1979), indicate that insurers are capable not only of fixing maximum reimbursable prices but also of obtaining binding agreements with providers guaranteeing the insured full reimbursement of a participating provider's fee.¹⁷⁰

The majority of the Court, in effect, viewed the foundations' efforts as the utilization of joint bargaining power by doctors to obtain terms from insurance companies which they could not obtain through a process of free individual bargaining.

165. 457 U.S. at 339-41.

166. 457 U.S. at 341.

167. 457 U.S. at 356-57.

168. See, e.g., H. HOVENKAMP, *supra* note 14, at 132-34; Gerhart, *supra* note 1, at 344-48; Comment, *Physician Maximum Fee Reimbursement Agreements: Arizona v. Maricopa County Medical Society*, 31 EMORY L.J. 913 (1982). The Court's decision is not without its defenders. See, e.g., Richards, *Antitrust and the Future of Cost Containment Efforts in the Health Profession*, 62 NEB. L. REV. 49, 70-85 (1983); Note, *Arizona v. Maricopa County Medical Society: Supreme Court Refuses to Immunize Doctors Against Sting of Sherman Act Section 1*, 1983 WIS. L. REV. 1203.

169. See H. HOVENKAMP, *supra* note 14, at 132-33; Gerhart, *supra* note 1, at 346-47; Comment, *supra* note 168, at 946-56.

170. *Maricopa*, 457 U.S. at 352-53 (footnotes omitted).

Justice Powell, in dissent, challenged the view that the doctors were utilizing joint bargaining power to coerce insurance companies into granting favorable terms: "[T]here is no evidence of opposition to the foundation plan by insurance companies Rather seven insurers willingly have chosen to contract out to the foundations the task of developing maximum-fee schedules."¹⁷¹ Professor Hovenkamp has elaborated on Justice Powell's dissent by noting that the insurers would not have voluntarily entered into the foundation arrangement if the purpose of the arrangement had been to charge artificially high prices.

For example, if the "maximum" price fixing agreement was really a disguised minimum price fixing agreement why did the insurance companies agree to participate? The doctors and the health insurers stand in a *vertical* relationship. As a general rule an insurer is made worse off by a price increase that increases the amount of its insured risk. Just as automobile insurance companies are better off in a world of safe drivers and cheap auto body repair shops, health insurers are better off in a world of healthy people and inexpensive doctors.¹⁷²

The mistake made by the dissenters in *Maricopa* and by Professor Hovenkamp is their assumption that because the rational profit-maximizing insurer would not voluntarily assent to cartel-level charges, the human managers of the insurers involved in *Maricopa* did not in fact assent. Perhaps rational profit-maximizing insurers would have no motive to assent. Real-world managers, however, do have a motive to accept artificially high health-care rates.

Over the last few years, the managers of health insurers have been under a great deal of pressure to help in the effort to contain health-care costs.¹⁷³ In particular, governmental authorities have pressured insurance company managers to assist in cost containment.¹⁷⁴ At the

171. 457 U.S. at 361 (Powell, J., dissenting).

172. H. HOVENKAMP, *supra* note 14, at 133 (emphasis in original); see also Comment, *supra* note 168, at 945.

173. In recent years, health-care costs have not only risen much faster than the general rate of inflation, but they have consumed an increasing share of gross national product. For a lucid and detailed exposition of the explosive growth of health-care costs, see Wing, *American Health Policy in the 1980's*, 36 CASE W. RES. L. REV. 608, 618-49 (1986).

174. For example, in 1977 the Massachusetts state insurance department insisted that Massachusetts Blue Cross/Blue Shield strictly limit the fees it paid to physicians as a condition of the department's approval of a rate-hike request. Law & Ensminger, *Negotiating Physicians' Fees: Individual Patients or Society?*, 61 N.Y.U. L. REV. 1, 27 (1986). By 1982, Blue Shield's payments were 30% less than physician charges. *Id.* As Professors Law and Ensminger note, "Blue Shield imposed these limitations, at least in part, because it believed that the Commissioner of Insurance would disapprove of its rates if Blue Shield did not aggressively limit physicians' fees." *Id.* State legislatures have also pressured insurers to engage in cost containment through legislation such as that requiring health insurance policies to contain insurer-paid, mandatory second opinion requirements for nonemergency surgery. *E.g.*, MD. ANN. CODE art. 48A, § 477DD (1986); N.J. STAT. ANN. § 17B:27-46.3 (West 1985).

same time, insurance company managers also may be under internal pressure to maximize short-term profits through health-care cost containment.¹⁷⁵ One possible response to these pressures is for the managers of insurers to obtain the type of cost-containment agreement that Justice Stevens described in his *Maricopa* opinion.¹⁷⁶ While cost-containment agreements do seem to be the ideal solution for relieving external and internal cost-minimization pressures, they do have a number of serious disadvantages when viewed from the perspective of real-world insurance fund managers such as those involved in *Maricopa*. First, the managers may sincerely, albeit mistakenly, believe that their companies individually lack the bargaining "clout" to negotiate such agreements.¹⁷⁷ Second, negotiating cost-containment agreements is a time-consuming and frustrating process.¹⁷⁸ Third, negotiating cost-containment agreements gives rise to ill feelings among health-care providers. Insurance managers probably do not relish generating ill will among a constituency with whom they have to

175. D. Ward Kallstrom has suggested several reasons why bottom-line-conscious health-insurance managers would want cost-containment agreements: (1) to reverse losses caused by skyrocketing health-care costs; (2) to allow their employer to capture a large segment of the health insurance market by offering low premiums; (3) to take the pressure for cost containment off the insurance companies and place it on doctors and hospitals; and (4) to make medical insurance plans consistent with the sensible insurance standard of restricting payouts. Kallstrom, *Health Care Cost Control by Third Party Payors: Fee Schedules and the Sherman Act*, 1978 DUKE L.J. 645, 648 n.9.

However, we should not necessarily conclude that managers of insurers are in fact under significant internal pressure to minimize costs through cost-containment agreements. The health-care-insurance industry has long been accustomed to the practice of passing along higher health-care costs through increased premiums. See Havighurst, *Professional Restraints on Innovation in Health Care Financing*, 1978 DUKE L.J. 303, 339, 342-43.

176. See text at note 170 *supra*.

177. If insurance managers believed that individual insurers could not negotiate cost-containment agreements with providers, then they were probably wrong in that belief. In the last few years, individual insurers have negotiated such agreements. See Capron, *Containing Health Care Costs: Ethical and Legal Implications of Changes in the Methods of Paying Physicians*, 36 CASE W. RES. L. REV. 708, 712 (1986). Several reasons may explain why managers would have held this erroneous belief. First, the belief attained the status of a nearly official ideology. The stated position of the Health Insurance Association of America (HIAA), the trade association for privately owned health insurers, was that no one insurer possessed sufficient bargaining leverage to negotiate cost-containment agreements with health-care providers and that Congress ought to pass an amendment to the antitrust laws to allow joint negotiations. Loos, *What Can Stop the Contagion?*, BEST'S REVIEW (Life & Health Ins. Ed.), Apr. 1984, at 35, 36. For a scholarly article defending the position of the HIAA in situations in which the insurer lacked monopsony power, see Gable & Monheit, *Will Competition Plans Change Insurer-Provider Relationships?*, 61 MILBANK MEMORIAL FUND Q. 614, 623-34 (1983). For an attack on the HIAA position, see Havighurst, *supra* note 175, at 328 n.121, 339-40. Second, insurance managers may have been reluctant to tamper with what they saw as the physician's professional discretion and expertise. *Id.* at 339. Third, managers may have been afraid that any competitive advantage they received from a cost-containment agreement could easily be duplicated by competitors. *Id.*

178. The time and effort spent negotiating such agreements would yield little benefit to an insurer if its competitors could "free ride" by simply duplicating the pioneer insurer's agreement or if health-care providers could not price discriminate and simply reduced their rates for all patients. See Gable & Monheit, *supra* note 177, at 629-32; Havighurst, *supra* note 175, at 339.

deal regularly.¹⁷⁹ Fourth, health-care providers have utilized, or threatened to utilize, various tactics designed to frustrate the attainment of cost-containment agreements, such as claiming that compliance with such agreements threatened the quality of care provided to patients,¹⁸⁰ declaring participation in such agreements to be unethical behavior,¹⁸¹ filing suits alleging that such agreements violate federal antitrust laws,¹⁸² and threatening to unionize in order to bargain collectively with insurers.¹⁸³ Provoking the use of any of these tactics cannot be an appealing prospect to managers of insurers.

External pressures for cost containment and possible internal pressures for cost minimization and improved profitability may leave managers of many insurers with no choice but to endure the unpleasantities and use their employer's bargaining clout to obtain cost-containing agreements. The managers of the insurers involved in *Maricopa* did, however, have an alternative — *i.e.*, to agree to the foundations' system of "cost containment." This option allowed the managers to "have their cake and eat it too." On the one hand, they would seem to be making sincere efforts at cost containment with the assistance of the "socially responsible" medical community, thus dampening external pressures for cost containment as well as any possible internal pressures to minimize costs.¹⁸⁴ On the other hand, the managers, by accepting the foundations' fee schedule, would avoid the unpleasantities and difficulties engendered by other insurance companies' efforts at cost containment. From the managers' perspective, yielding to the foundation's disguised cartel-level pricing made a great deal of sense, even if it were not in their employers' long-term interests. Therefore, while the *Maricopa* majority's portrayal of the insurers as victims of a doctor's price-fixing cartel may not be credible in the theoretical world

179. The unwillingness to irritate providers is especially acute when the insurers are attempting to sell malpractice policies to the same providers. M. GREEN & J. BERRY, *supra* note 11, at 317.

180. See *FTC v. Indiana Fedn. of Dentists*, 106 S. Ct. 2009, 2020 (1986); Havighurst, *supra* note 175, at 312 n.39; Weller, *Antitrust and Health Care: Provider Controlled Health Plans and the Maricopa Decision*, 8 AM. J.L. & MED. 223, 229, 241 (1982).

181. See Havighurst, *supra* note 175, at 312-13.

182. See, e.g., *Barry v. Blue Cross*, 805 F.2d 866 (9th Cir. 1986); *Brillhart v. Mutual Medical Ins. Inc.*, 768 F.2d 196 (7th Cir. 1985); *Kartell v. Blue Shield*, 749 F.2d 922 (1st Cir. 1984), *cert. denied*, 471 U.S. 1029 (1985).

183. See Kallstrom, *supra* note 175, at 679 n.143.

184. The illusion of effective cost containment or cost minimization could easily have been generated. The foundation's physician fees were apparently less than or equal to the fees charged by many, if not all, nonfoundation members. H. HOVENKAMP, *supra* note 14, at 133. Compared with what other physicians in the locality were charging, the managers of the insurers would have seemed to be doing well by accepting the foundation's fee schedule. However, the point of comparison should not be with nonfoundation physicians, but with physicians in locales where insurers have aggressively negotiated individual physician fee-limiting arrangements.

of profit-maximizing, cost-minimizing insurance companies, in the real business world of insurance company managers, the insurers may well have been victimized with the witting or unwitting cooperation of their own managers.

IV. CONCLUSION — MICRO-MICROECONOMICS AS AN OPEN SYSTEM

This article has attempted to begin constructing a micro-microeconomic theory of antitrust law in which the key actors are the real-world human managers of firms rather than the theoretical profit-maximizing firms posited by classical microeconomic theory. The words "begin" and "a" cannot be emphasized too strongly. The portrait of management behavior, which the micro-microeconomic approach set forth utilizes, is drawn from observations which are to a large extent both casual and anecdotal.¹⁸⁵ Micro-microeconomic theory would be much stronger if its description of managerial behavior were based on much more systematic observations. Such observations from sociologists, psychologists, organizational behavior specialists, management specialists, economists, historians, lawyers, or anyone else all have a place in micro-microeconomics. These observations may completely contradict the views of management behavior put forth in this article and may call for totally different conclusions with respect to antitrust law than the ones reached by this article.

So long as the conclusions are based upon careful observation, we should welcome the refutation. What neither we nor antitrust courts should welcome is a confusion between models based on empirically untested assumptions and reality.¹⁸⁶ Unfortunately, in *Matsushita* the Supreme Court went quite far toward substituting the neat theoretical models of classical microeconomics for the complex and messy reality of facts which courts must sort out in an antitrust case.¹⁸⁷ If the Court continues along the road it trod in *Matsushita*, we will have a theoretically perfect microeconomic policy which is a disaster in the real world because it bears precious little relation to that world.

185. See notes 42-48 *supra* and accompanying text.

186. Even within the economics profession, voices are beginning to argue for a more empirically based discipline which discards the assumptions that other social scientists disproved decades ago. *E.g.*, S. MAITAL, *supra* note 23, at 261-74; L. THUROW, DANGEROUS CURRENTS 216-37 (1983).

187. See Crew, *supra* note 13, at 11.