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ANTITRUST'S PROTECTED CLASSES†

Herbert Hovenkamp*

For purposes of argument, this essay assumes that efficiency ought to be the exclusive goal of antitrust enforcement. That premise is controversial.¹ Nonetheless, several economic and legal theorists, primarily among the Chicago School of economics and antitrust scholarship,² have developed an Optimal Deterrence Model based on this assumption. The Model is designed to achieve the optimum, or ideal, amount of antitrust enforcement. The Model's originators generally believe that there is too much antitrust enforcement, particularly enforcement initiated by private plaintiffs. I intend to show that, even if efficiency is the only antitrust policy goal, a broader array of lawsuits should be permitted than the Optimal Deterrence Model has recognized.

I. THE OPTIMAL DETERRENCE MODEL

A. *The Optimal Enforcement of Legal Rules*

The Optimal Deterrence Model had its origin in Gary Becker's important 1968 essay, arguing that deterrence should be the primary goal of legal sanctions.³ According to Becker, the ideal legal sanction would make illegal conduct unprofitable whenever condemning the conduct would destroy less social wealth than allowing the conduct to continue. Becker argues that the social cost of illegal conduct includes three elements: (1) the costs imposed by the conduct itself; (2) the

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1. See Hovenkamp, *Antitrust Policy After Chicago*, 84 MICH. L. REV. 213 (1985).

2. The most orthodox and compact statement of the model is Landes, *Optimal Sanctions for Antitrust Violations*, 50 U. CHI. L. REV. 652 (1983). Other relevant literature includes W. SCHWARTZ, *PRIVATE ENFORCEMENT OF THE ANTITRUST LAWS* (1981); Block, Nold & Sidak, *The Deterrent Effect of Antitrust Enforcement*, 89 J. POL. ECON. 429 (1981); Easterbrook, *Treble What?*, 55 ANTITRUST L.J. 95 (1986); Landes & Posner, *Should Indirect Purchasers Have Standing to Sue Under the Antitrust Laws? An Economic Analysis of the Rule of Illinois Brick*, 46 U. CHI. L. REV. 602 (1979); Page, *Antitrust Damages and Economic Efficiency: An Approach to Antitrust Injury*, 47 U. CHI. L. REV. 467 (1980); Note, *Rethinking Antitrust Damages*, 33 STAN. L. REV. 329 (1981); see also W. BREIT & K. ELZINGA, *ANTITRUST PENALTY REFORM: AN ECONOMIC ANALYSIS* (1986).

3. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169 (1968). Also important is Stigler, *The Optimum Enforcement of Laws*, 78 J. POL. ECON. 526 (1970).

costs of detecting and apprehending suspected violators and of establishing their guilt; and (3) the costs of imposing sanctions.⁴ An ideal legal system would minimize the sum of these three costs. Unfortunately, these three costs of harmful conduct are mutually dependent. Catching more thieves costs more money. In order to reduce the number of violations (cost number one), society may have to spend more on enforcement (cost number two), or on long prison sentences (cost number three).

Antitrust enforcement in particular requires some difficult trade-offs both because the kinds of conduct that should be condemned are controversial and often hard to identify, and because the costs of prosecution are high.

In an effort to reduce the sum of the three costs, antitrust law has developed some simplifying devices. For example, the *per se* rule is designed to reduce costs of the second type, establishing guilt, to the extent that it limits the need for certain types of proof. In the process, however, the *per se* rule likely increases costs of the first type, the costs of the conduct itself, particularly to the extent that it is overdeterrent. Both underdeterrent and overdeterrent rules can increase the social cost of conduct. For example, an underdeterrent rule that fails to identify and condemn every instance of predatory pricing is socially costly to the extent that it permits some predators to charge monopoly prices without sanction. But an overdeterrent rule can be just as costly if it forces firms to refrain from hard competition in order to avoid legal sanctions. In the case of an overdeterrent rule, the social cost is equal to the value of the hard competition that a more accurate rule would have produced. To the extent that the *per se* rule against cartels reduces the cost of prosecuting them, it is good; but to the extent that it prevents some efficient cartels from forming, it is harmful.⁵ The acceptance of the *per se* rule is based on our feeling that over the long run *per se* condemnation will result in a greater savings in prosecution costs than it will cause in losses from overdeterrence. A rule of *per se* legality, incidentally, imposes the same trade-off: it reduces the cost of prosecution, but may fail to condemn some instances of socially harmful conduct.

The same can be said of punishment costs. If civil damage awards are too large, private plaintiffs will litigate too freely and too long.

4. Becker, *supra* note 3, at 181.

5. The physicians' maximum price fixing arrangement condemned in *Arizona v. Maricopa County Medical Socy.*, 457 U.S. 332 (1982), is probably an example of an efficient cartel. For an argument that many cartels are efficient, particularly in industries with high fixed costs, see L. TELSER, *A THEORY OF EFFICIENT COOPERATION AND COMPETITION* (1987).

The result will be an increase in costs of the second type. Further, excessive punishment increases the anticipated costs of a lawsuit. If the substantive rules are the least bit overdeterrent, firms will avoid some competitive, socially beneficial, but ambiguous conduct in an attempt to minimize these costs. The old "automatic damages" rule in secondary-line Robinson-Patman Act cases is a good example of this kind of trade-off. Under the rule, a supplier who was found to have engaged in illegal price "discrimination" by selling to competing dealers at different prices would have to pay damages to the disfavored dealer; those damages would be calculated as the price difference between the high price and low price sales multiplied by the number of units the plaintiff purchased (before trebling).⁶ Such a rule reduced the costs of determining the penalty (type-three costs) but almost certainly increased type-one costs because it was overdeterrent: it imposed penalties so large that they prevented manufacturers from engaging in efficient differential pricing.⁷

These trade-offs are further complicated by the fact that antitrust law must deal with the problem of marginal deterrence. Deterrence works because people find punishment unpleasant, and some kinds more unpleasant than others. Society will be better off if it can force violators to minimize the social costs of their violations, and violations are not equally costly. If both mugging and murder are punishable by death, the mugger has little incentive not to kill her victim. The punishment will be no greater, and the risk of apprehension and conviction will in fact be lower because an important witness will have been eliminated. On the other hand, if mugging is punishable by six months in prison and murder by death, the mugger must make a more difficult trade-off of the much higher penalty against the greater risk of apprehension and conviction.

The monopoly overcharge rule for antitrust damages — that damages before trebling equal the difference between the monopoly or cartel price and the presumed competitive price — is a fair example of marginal deterrence. The rule encourages the cartel to exact a small overcharge rather than a large one. Under the monopoly overcharge rule, the cartel must make some difficult calculations in setting its price. Its short-run profit-maximizing price, which it could obtain by equating marginal cost and marginal revenue, may provide it with the greatest current stream of monopoly profits. But cartels that charge

6. For example, if an automobile manufacturer sold automobiles to a favored dealer at \$8000 and to a disfavored dealer at \$9000, the disfavored dealer would be entitled to damages of \$1000 per unit sold, before trebling.

7. The rule was upset in *J. Truett Payne Co. v. Chrysler Motor Corp.*, 451 U.S. 557 (1981).

very high prices are generally easier to detect.⁸ Moreover, they generally encourage more cheating,⁹ and — because of the overcharge rule — they result in greater penalties if the cartel members are caught. After taking these things into account, the cartel is likely to charge less than its short-run profit-maximizing price.

B. *The Optimal Deterrence Model in Antitrust*

If maximizing social wealth were antitrust's only goal, its system of sanctions would make inefficient illegal conduct unprofitable but permit efficient illegal conduct to earn a profit. Taking the social costs of enforcement and penalties into account, the system should condemn inefficient conduct if the marginal gains of enforcement are greater than its marginal losses — *i.e.*, if the costs of detecting and penalizing the conduct are less than the social cost of the conduct thus prevented. Importantly, this is a long-run model because it is concerned with general rather than special deterrence. The value of prosecution in each individual case is equal to the social cost of future illegal conduct that the prosecution will prevent. For that reason, it might be quite justifiable to spend a great deal of societal resources prosecuting a particular violation whose social cost seems rather small, such as a cartel that is not working very well anyway, and whose sales involve a very small market, in order to discourage such behavior in potential cartel organizers. The social cost of the current violation can never be recovered. The only effective purpose of the prosecution is to deter future violations.

Optimal deterrence is a function of the anticipated profitability of conduct to a violator. If price fixing is calculated to produce an anticipated profit of \$100 and society deems price fixing undesirable, the anticipated penalty should be something greater than \$100. If it is less, the price fixer will fix prices even if it is absolutely certain that it will be caught and have to pay the penalty.

In the real world, however, the anticipated profitability of an antitrust violation often bears little relationship to the losses that the violation imposes on its victims. This poses a problem for people who take

8. A good recent illustration is *New York v. Hendrickson Bros.*, 840 F.2d 1065, 1084 (2d Cir.), *cert. denied*, 109 S. Ct. 128 (1988), in which colluding bidders had agreed with each other not to bid too high, in the belief that doing so would invite extra scrutiny from the government. See also Ayres, *How Cartels Punish: A Structural Theory of Self-Enforcing Collusion*, 87 COLUM. L. REV. 295 (1987); Block, Nold & Sidak, *supra* note 2, at 431.

9. The greater the difference between marginal cost and the cartel price, the more individual cartel members will be tempted to make secret sales in excess of their cartel output quotas. See H. HOVENKAMP, *ECONOMICS AND FEDERAL ANTITRUST LAW* § 4.1 (1985).

seriously the language of section 4 of the Clayton Act¹⁰ which creates the private treble damage action for federal antitrust violations. Section 4 unambiguously commands that the victim of an antitrust violation shall recover threefold the damages "by him sustained." The statute insists that damages be measured by the victim's losses rather than the violator's gains. In many cases the Optimal Deterrence Model requires measurement formulae for damages that are flatly inconsistent with the statute.¹¹

The degree of inconsistency between the Optimal Deterrence Model and the statutory language varies with the type of injury. If the defendant is a monopolist or cartel member and the plaintiffs are purchasers seeking damages based on a monopoly overcharge, the difference is relatively small. The profitability of a cartel is a function of the size of the overcharge, and the overcharge, of course, is also the measure of the purchaser's injuries. Although the equation is generally more complicated than this,¹² there is sometimes a good correlation between optimal and statutory damages in overcharge injury cases.

The great majority of antitrust cases, however, are much more problematic. Most plaintiffs are competitors, potential competitors, suppliers, terminated dealers, or franchisees, and the basis for damages is lost profits.¹³ Damages based on lost profits seem quite consistent with the statutory language of section 4, mandating damages based on the plaintiff's losses. In fact, lost profits were historically the preferred measure of damages.¹⁴ However, in most cases there is absolutely no useful correlation between the amount of the antitrust plaintiff's lost profits and the profitability of the antitrust violation to the defendant.¹⁵

1. *Optimal Damages for Overcharge Injuries*

a. Naked price fixing or monopolization. The simplest example of an overcharge case is the monopolist or cartel member charging its short-run profit-maximizing price. Figure One illustrates this situa-

10. 15 U.S.C. § 15 (1986).

11. See *infra* notes 28-31 and accompanying text.

12. See *infra* notes 17-21 and accompanying text.

13. See Salop & White, *Economic Analysis of Private Antitrust Litigation*, 74 GEO. L.J. 1001, 1005-06 (1986).

14. It took a Supreme Court decision before overcharge damages even became an acceptable alternative to lost profits. *Chattanooga Foundry & Pipe Works v. City of Atlanta*, 203 U.S. 390, 396 (1906); see also L. SULLIVAN, *HANDBOOK OF THE LAW OF ANTITRUST* 788 (1977); Harrison, *The Lost Profits Measure of Damages in Price Enhancement Cases*, 64 MINN. L. REV. 751, 760 (1980).

15. See *infra* notes 28-31 and accompanying text.

tion. In perfect competition, a firm would set the price of its product equal to the marginal cost of producing it, or P_c , and output would be Q_c . The monopolist or cartel, however, will reduce output to the point that marginal cost equals marginal revenue, or Q_m , and price will rise correspondingly to P_m . Rectangle 2-3-5-4 represents the subsequent transfer of wealth from consumers to the monopolist. Triangle 4-5-6 represents the traditional "deadweight loss" from monopoly — resources that are lost because they are denied to consumers but do not show up as gains to the monopolist either.¹⁶ If the demand curve is linear, as shown in Figure One, triangle 4-5-6 will be exactly half as big as rectangle 2-3-5-4.¹⁷ Assuming a wealth transfer of \$100 caused by this monopoly, the deadweight loss will be \$50. If the demand curve is not linear, the deadweight loss triangle may be greater than or less than half the wealth transfer.¹⁸

One might think that the optimum penalty for antitrust violations must be based on the deadweight loss, since that loss represents the "social cost" of monopoly. But clearly a penalty equal to the deadweight loss would be too small. The conduct represented in Figure One is inefficient from society's standpoint because it produces a deadweight loss of \$50 with no offsetting efficiencies. It generates \$100 in profits to the violator. A fine of \$50 would not deter the conduct, for the defendants could pay the fine and still have \$50 profit left over. Importantly, a fine equal to the deadweight loss does not in any way "reverse" the social cost of the cartel. By the time the cartel members are caught, those resources have been wasted and cannot practicably be recovered. The purpose of the fine is not to "restore" or recover the lost efficiency, but merely to prevent such losses from occurring in the future; the aim of the penalty is not compensation, but deterrence.

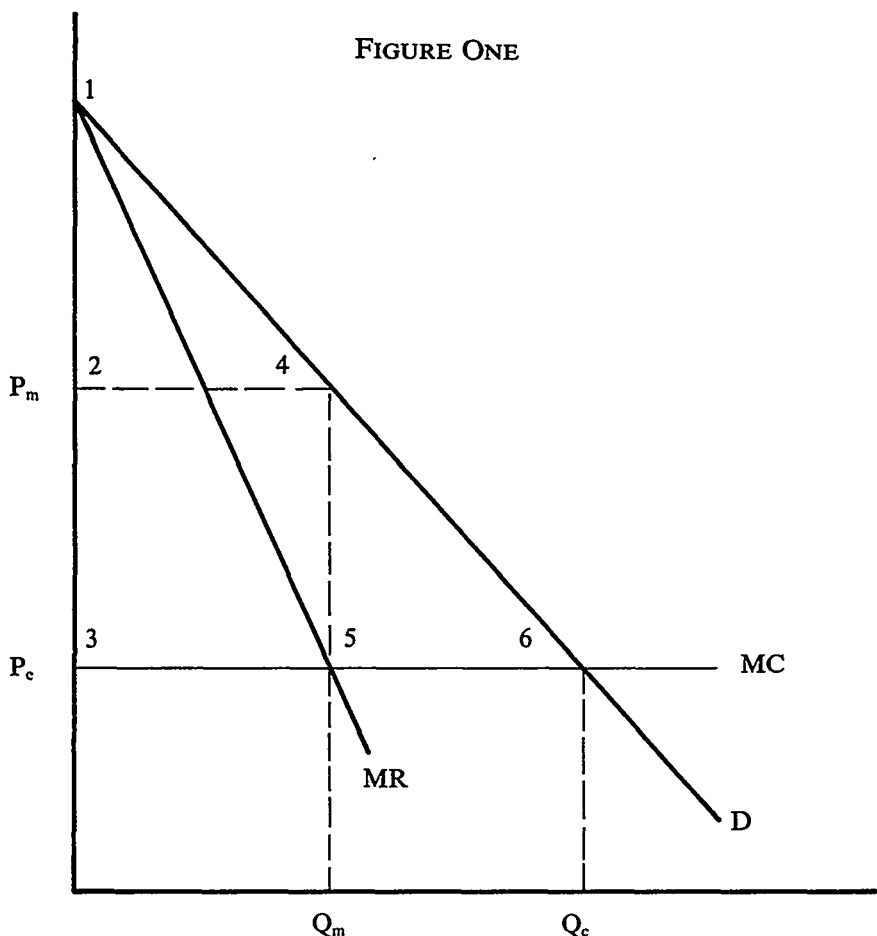
If the expected profitability of this monopoly or cartel is rectangle 2-3-5-4 with no offsetting social benefits, the optimal penalty should be slightly larger than the area described by 2-3-5-4. That is, the *wealth transfer* determines the optimal penalty. If the antitrust violation is secret, such as a bid-rigging or naked price-fixing agreement, then the

16. See H. HOVENKAMP, *supra* note 9, at §§ 1.2-.3; E. MANSFIELD, *MICROECONOMICS: THEORY AND APPLICATIONS* 293-95 (5th ed. 1985).

17. It can be shown that the slope of the marginal revenue curve (MR) is twice the slope of the demand curve (D) if the demand curve is linear. E. MANSFIELD, *supra* note 16, at 131-33. As a result, line 3-5 is the same length as line 5-6. Thus, 4-5-6 is a triangle with the same base and height as rectangle 2-3-5-4. Since the area of a triangle equals one-half the base times the height ($1/2BH$), triangle 4-5-6 is exactly half the size of rectangle 2-3-5-4.

18. J. ROBINSON, *THE ECONOMICS OF IMPERFECT COMPETITION* 144 (1934). In general, if the demand curve is concave (as viewed from the top down), the deadweight loss triangle will be smaller than one half of the wealth transfer. If the demand curve is convex, the deadweight loss triangle will be larger than one half of the wealth transfer.

FIGURE ONE



damages must be increased by a multiplier to account for the probability that it will go undetected.¹⁹ Treble damages, which Clayton Act section 4 currently requires, is the correct multiplier only if we can assume that the probability of detection is one in three.²⁰ Thus, if a cartel member anticipates profits of \$100 from the cartel and calculates a one in three chance it will be caught, a fine of marginally greater than \$300 should be sufficient to deter the conduct.

b. Violations with offsetting efficiencies. Computing the optimal penalty becomes more complex if an antitrust violation also produces offsetting efficiencies. Mergers often fall into this category, as do joint ventures and single-firm monopolization. If enforcement tribunals had perfect information, they would be able to balance the social gains

19. See Landes, *supra* note 2, at 654; Easterbrook, *supra* note 2, at 95.

20. For the rationality of this assumption, see Hovenkamp, *Treble Damages Reform*, 33 ANTITRUST BULL. 233, 251-57 (1988).

of such activities against the losses and condemn only those that were, on balance, inefficient. But they do not have such information, so they generally look for threats to competition and — if such threats are found — ignore claimed offsetting efficiencies, unless the case for them is very strong. The 1984 Justice Department Merger Guidelines take this position.²¹

It is possible to levy a fine or damage award sufficiently large to deter inefficient violations, but not large enough to deter efficient ones. Figure Two illustrates this principle. It shows a market containing two firms which, if they behaved competitively, would each set price equal to P_c . Their total output would be Q_c . If the two firms joined through a merger or joint venture, however, two things would happen. First, the firms would collectively acquire the power to monopolize the market; second, they would reduce their costs of production or distribution by achieving economies of scale or scope. Accordingly, the firms will set a price determined by the intersection of the marginal cost and marginal revenue curves, rather than the intersection of the marginal cost and demand curves; however, their marginal cost curve will be lowered from C_2 to C_1 . Output will be Q_m and price will be P_m . In the illustration Q_m is less than Q_c , and P_m is greater than P_c , but this will not always be the case. If the amount of market power created by the merger or joint venture is relatively small and the cost savings are relatively large, the new “monopoly” price might actually be lower than the old “competitive” price.²² Furthermore, the net efficiency of the merger or joint venture will not depend on whether the resulting price is higher or lower than the older price. The merger might facilitate a price increase but nevertheless produce efficiency gains, which accrue to the firm in the form of higher profits and outweigh the losses in allocative efficiency.

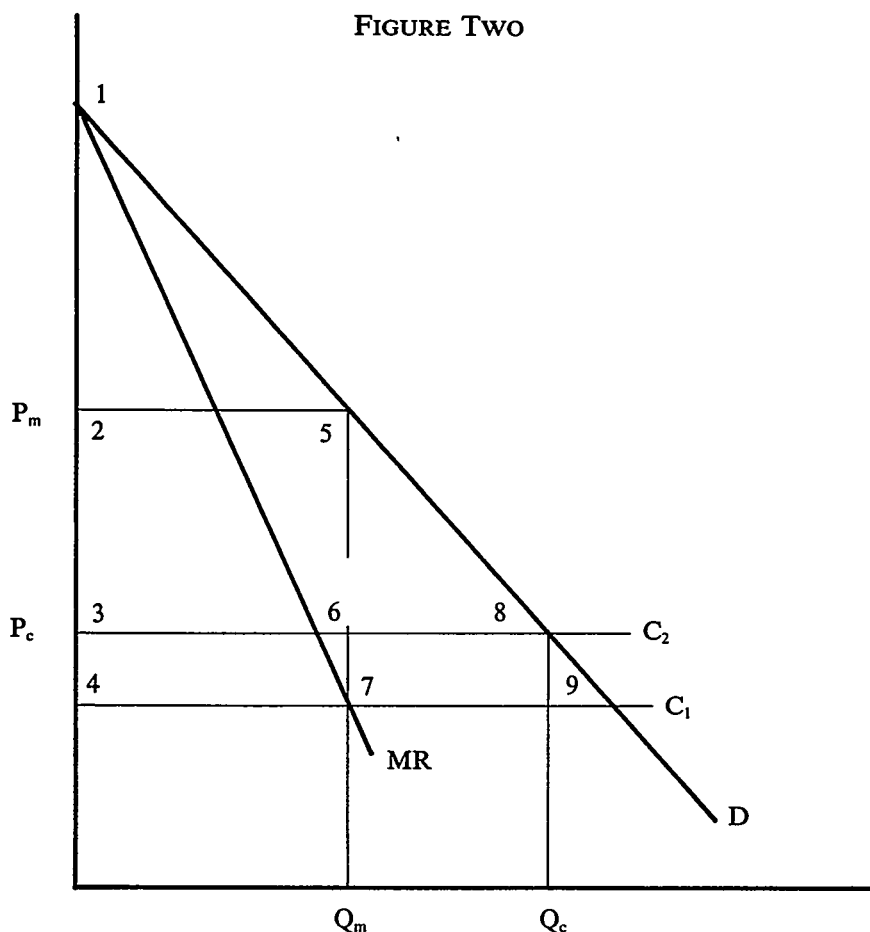
An optimal damages rule would not be concerned with whether the price following the joint venture was higher or lower,²³ but rather with whether the gains in productive efficiency outweighed the losses in allocative efficiency. The way to sanction only those joint ventures in which the productive efficiency gains do not outweigh allocative effi-

21. 49 Fed. Reg. 26,823, 26,831, 26,834 (1984); see P. AREEDA & H. HOVENKAMP, *ANTI-TRUST LAW* §§ 939', 940' (Supp. 1989).

22. Fisher, Lande & Vandaele, *Afterword: Could a Merger Lead to Both a Monopoly and a Lower Price?*, 71 CALIF. L. REV. 1697 (1983).

23. Although it would be concerned in one sense: if the resulting price were lower there would be no consumer injury as a result of the violation, and thus no private cause of action by consumers. A competitor injured by a post-merger firm's lower prices would not have a cause of action, for it would not be a victim of “antitrust injury” unless the prices were predatory. See *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104 (1986); P. AREEDA & H. HOVENKAMP, *supra* note 21, at §§ 340.2d-2e.

FIGURE TWO



ciency losses is to set damages as the sum of the wealth transfer and the traditional deadweight loss.

For example, suppose that a merger like the one illustrated in Figure Two yielded a traditional deadweight loss of \$100 (triangle 5-7-9) and a wealth transfer of \$200 (rectangle 2-4-7-5), but at the same time produced a cost savings of \$90 (rectangle 3-4-7-6). Damages set as the sum of the wealth transfer and the deadweight loss would be \$300. In this case, the firms would not pursue the merger, because its profitability (wealth transfer plus cost savings) would be only \$290. Likewise, in this case the merger would be socially inefficient: its deadweight loss of \$100 would be weighed against its cost savings of \$90, and the wealth transfer of \$200 would appear on both sides of the equation and would therefore be a wash. The calculation shows a net social loss of \$10.

But suppose that the cost savings were \$125 rather than \$90. A

penalty of \$300 would not deter the merger, because its value to the merging firms would now be \$325. Likewise, the merger would be efficient overall because the cost savings would be greater by \$25 than the traditional deadweight loss. In short, an optimal damages rule fixing damages as the sum of the wealth transfer and the deadweight loss would make inefficient mergers unprofitable but leave efficient ones profitable.

Whether damages equal to the sum of the wealth transfer and traditional deadweight loss are "optimal" in cases of efficiency-creating mergers is a matter of some dispute, even within the Chicago School. The alternative position is that there should be an efficiency "defense" in merger cases — *i.e.*, if a merger yields higher prices but produces gains in productive efficiency that exceed any losses in allocative efficiency, damages should be set at zero.²⁴

The choice between the optimal damages rule and the efficiency defense rule depends largely on how naive a model one uses for analysis. Both rules would deter inefficient mergers. The efficiency defense rule — zero damages for efficient mergers — would make efficient mergers more profitable than the rule awarding damages equal to the wealth transfer plus deadweight loss. Under perfect information, both rules should permit the creation of all efficient mergers, for any amount of net profitability would encourage the merger. As soon as a little indeterminacy is thrown in, however, it seems clear that the efficiency defense rule would facilitate more mergers than the "optimal" damages rule. Drawing on the above example, suppose that a firm in a position to merge calculates that the proposed merger would yield a traditional deadweight loss of \$100, a wealth transfer of \$200, and a cost savings of \$125. Under the optimal damages rule, this merger is worth \$25 (wealth transfer plus cost savings, less the sum of wealth transfer and deadweight loss). Under the efficiency defense rule, the merger is worth \$325 (wealth transfer plus cost savings; no damages). But suppose in addition that the firm calculates there is a fifty percent chance that the court will miscalculate the deadweight loss as \$150 rather than \$100. In this case, the expected value of the merger under the optimal damages rule is zero;²⁵ its expected value under the efficiency defense rule is \$150.²⁶ In the presence of uncertainty, the effi-

24. R. BORK, *THE ANTITRUST PARADOX* ch.10 (1978); Muris, *The Efficiency Defense Under Section 7 of the Clayton Act*, 30 CASE W. RES. L. REV. 381, 392 n.41 (1980).

25. Expected damages (wealth transfer plus dead weight loss) are now \$325, since there is a 50% chance that the court will measure the deadweight loss as \$100 and a 50% chance that it will measure the deadweight loss as \$150.

26. That is, if the court calculates the deadweight loss correctly, the value of the merger will be \$325, as noted previously. If the court miscalculates the deadweight loss as \$150, the firm will

ciency defense rule would permit relatively more mergers.

The rule that optimal damages equals the sum of the wealth transfer plus the traditional deadweight loss applies to both naked and efficiency-creating antitrust violations. In the case of naked violations, such as bid-rigging, overdeterrence is not much of a problem because, almost by definition, there is little likelihood of offsetting efficiencies, and any expected penalty greater than the monopoly gains will deter the conduct. But if the conduct produces any efficiencies, the potential defendants will be obliged to compare the efficiency-creating potential with the deadweight loss. They will then pursue the conduct only if the efficiency-creating potential is greater.

2. *Optimal Damages for Competitor Injuries*

The difference between the Optimal Deterrence Model and the current regime of private antitrust enforcement is much greater when the plaintiff is a competitor or potential competitor of the violator, as is true in the great majority of antitrust cases.²⁷ In such cases the plaintiff's damages are based on lost profits or sometimes lost investment.²⁸ However, these profits or investments are not transferred to the monopolist or cartel as monopoly overcharges. They are lost resources that result from the defendant's exclusionary practices, not from its monopoly pricing.

In the case of consumer lawsuits, monopoly overcharges and monopoly profits are rough "mirror images,"²⁹ so the consumer who recovers the statutory damages "by him sustained" is also depriving the monopolist of monopoly profits. But, as a general rule, the amount of money that an excluded rival loses as the result of a monopoly, and the amount that the monopolist gains, bear little relationship to one another.

The Optimal Deterrence Model is not concerned with compensation for victims, but rather with deterrence of violators. The proper measure of deterrence is the same whether the plaintiff is a consumer or a competitor: damages should equal the sum of the overcharge from any monopoly created by the antitrust violation and the tradi-

lose its efficiency defense and have to pay \$350 in damages, against cost savings of \$325, for a net loss of \$25. Since the likelihood of this is .5, the expected value of the merger is $[325 + (-25)]/2$, or \$150.

27. See Salop & White, *supra* note 13, at 1005 n.25, 1005-06, Table 5; see also Easterbrook, *supra* note 2, at 95; Posner, *A Statistical Study of Antitrust Enforcement*, 13 J.L. & ECON. 365 (1970).

28. See *infra* section IV.C.

29. Total consumer injury and monopoly profit are not identical, however. Consumer injury is greater by the amount of the traditional deadweight loss.

tional deadweight loss. This rule would permit efficient exclusionary practices to continue while stopping inefficient ones.

Once again, one may wish to dispute whether the Optimal Deterrence Model really yields "optimal" damages at all. A strong case can be made that optimal damages for efficient exclusionary practices are zero damages. Competition is by nature exclusionary, and we do not want to penalize companies for engaging in efficient competition.³⁰ In fact, the law of monopolization, much more than the law of mergers, recognizes such an "efficiency defense." As a general rule, unilateral practices by a dominant firm that reduce its costs or give it a better product are legal, even if the practices permit the firm to charge a price well above its marginal cost and injure competitors in the process. For example, successful innovation produces both monopoly profits and competitor injuries, but we do not penalize innovation with a fine equal to the wealth transfer plus the deadweight loss. The general antitrust rule is that innovation is legal, regardless of the amount of monopoly profits it produces or the extent to which it injures competitors. The penalty is zero.³¹

Nonetheless, in a world of perfect information, a rule setting damages for exclusionary practices as the sum of the monopoly wealth transfer and traditional deadweight loss would deter inefficient exclusionary practices while permitting efficient ones.

II. THE OPTIMAL DETERRENCE MODEL AND THE SOCIAL COST OF MONOPOLY

The Optimal Deterrence Model is built on the theory that the exclusive goal of antitrust policy should be the pursuit of economic efficiency. Since efficiency consists of two parts, allocative efficiency and productive efficiency, which must sometimes be traded off against each other, the goal has been expressed in various ways. Most generally, the stated goal is that antitrust policy should seek to maximize allocative efficiency while doing as little harm as possible to productive effi-

30. One can suggest counterexamples. Suppose an unregulated ambulance company bribes a city council to deny a license to a potential competitor. As a result, the company is able to use its ambulances more frequently, and its average fixed costs are reduced. The practice is inefficient only if the welfare losses created by the perpetuation of the monopoly exceed the cost savings that result from more efficient use of equipment. Nevertheless, we may wish to penalize this conduct whether or not it is efficient, simply because we do not want monopolies to be created in this way.

31. See, e.g., *California Computer Prods. Co. v. IBM Corp.*, 613 F.2d 727 (9th Cir. 1979); *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093 (1980); see also P. AREEDA & H. HOVENKAMP, *supra* note 21, at ¶ 718'; Sidak, *Debunking Predatory Innovation*, 83 COLUM. L. REV. 1121 (1983).

ciency.³² Alternatively, one might argue that an antitrust policy whose goal is to maximize social welfare would try to minimize the sum of losses caused by allocative inefficiency and productive inefficiency.³³ The Optimal Deterrence Model precisely addresses this alternative statement of the goal: it makes monopoly-creating conduct unprofitable only if allocative efficiency losses exceed productive efficiency gains.

But no matter how this principle is defined, it clearly depends on some concept of the social cost of monopoly, which is the principal factor in determining allocative inefficiency. Other things being equal, the higher the social cost of monopoly in an unregulated market, the more intervention will be appropriate. The Optimal Deterrence Model compares the social cost of any monopoly created by an antitrust violation with the social value of any productive efficiency that might result from that violation.

Our notion of what ingredients must be included in the "social cost" of monopoly has changed over the last thirty-five years.³⁴ As a result, our ideas about the size of the social cost of monopoly have changed accordingly. Sections II.A and II.B briefly summarize the development of theory concerning the social cost of monopoly. Section II.C then argues that the current measures of social cost understate the true social cost of monopoly, perhaps by a very wide margin. Later, I will make some suggestions about the implications of this broader conception of the social cost of monopoly for antitrust policy.

A. *The Social Cost of Monopoly: Method I*

The orthodox determination of the social cost of monopoly is illustrated by the simple diagram in Figure Three, which depicts demand, price, and output under competitive and monopoly conditions. If the market represented by Figure Three is competitive, price will be relatively low, at P_c , and output will be relatively high, at Q_c . If the market falls to the control of a monopolist, however, output will drop to Q_m , and price will rise accordingly to P_m .

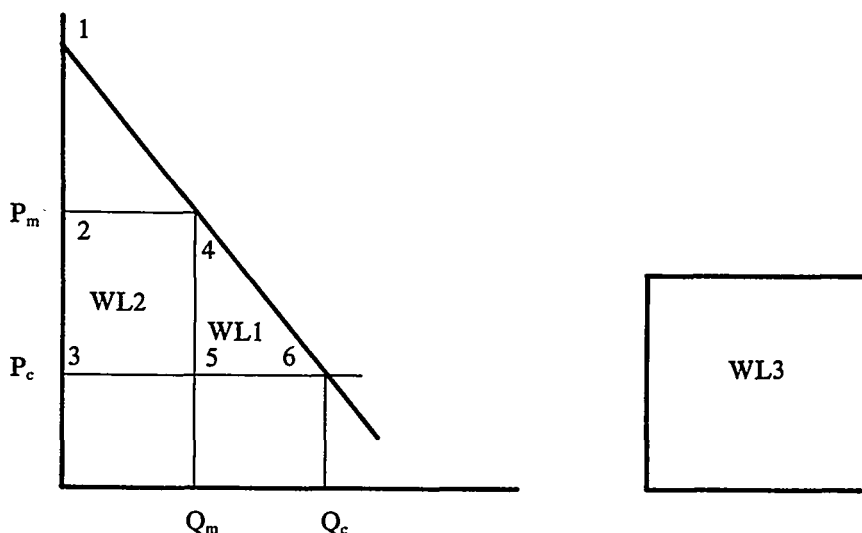
A loss in allocative efficiency consists of value that is taken away from one individual or group but not given to someone else. It simply

32. In Robert Bork's words: "The whole task of antitrust can be summed up as the effort to improve allocative efficiency without impairing productive efficiency so greatly as to produce either no gain or a net loss in consumer welfare." R. BORK, *supra* note 24, at 91.

33. See Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoffs*, 58 AM. ECON. REV. 18 (1968).

34. The modern debate over the nature and relative size of the welfare loss caused by monopoly began with the publication of Harberger, *Monopoly and Resource Allocation*, 66 AM. ECON. A. PAPERS & PROC. 77, 86 (1953).

FIGURE THREE



vanishes, because, like a lost opportunity, it has been wasted. The “social cost,” or allocative efficiency loss, illustrated in Figure Three is traditionally represented by triangle 4-5-6, the “deadweight” loss triangle. This triangle describes wealth that is taken away from consumers but which is not given to the monopolist, because the monopolist makes no profits on output it does not produce. This triangle is designated “WL1” in Figure Three, for it represents the first discovered element of welfare loss from monopoly.

Rectangle 2-3-5-4 in Figure Three consists of wealth that is taken away from consumers and transferred to the monopolist in the form of higher prices ($(P_m - P_c)Q_m$). Traditionally, neoclassical economists were very careful to distinguish the deadweight loss of monopoly from the mere wealth transfer. When wealth is merely transferred, society as a whole is neither better nor worse off. Society is injured collectively only when wealth is destroyed, or lost. For those who believe that efficiency is the exclusive goal of the antitrust laws, the wealth transfer is not a policy problem, for it represents no efficiency loss.³⁵ For them, the antitrust problem is the deadweight loss triangle.

This perspective on the social cost of monopoly is important, even if in practice one cannot distinguish the “deadweight loss” from the

35. Consider, for example, the comment of Robert Bork: “[C]ourts should ignore income distribution in deciding antitrust cases . . .” R. BORK, *supra* note 24, at 112. Or see economist Arnold C. Harberger’s statement that what monopoly “does through its effect on income distribution I leave to my more metaphysically inclined colleagues to decide.” Harberger, *supra* note 34, at 87.

wealth transfer. Our notion of what ingredients are included in the social cost of monopoly tells us something about the amount of intervention in the market that is appropriate. If we think the social cost of monopoly is small, a tiny amount of intervention or perhaps even no intervention at all is in order. Since intervention is itself a costly commodity — operating the intervening system is costly, as are any errors that might result — we might well conclude that the cost of any intervention is likely to be greater than the cost of the monopoly thus destroyed. Society would be better off if we did not intervene at all.

Using the definition given above, several economists have argued since the 1950s that the social cost of monopoly is quite small.³⁶ A few have disagreed.³⁷ What these studies share, however, is their regard for the difference between price and marginal cost, or, more precisely, the difference between actual output and output when price equals marginal cost, as the principal factor in determining the social cost of monopoly.

B. *The Social Cost of Monopoly: Method II*

In an important essay published in 1967, Gordon Tullock argued that any attempt to assess the social cost of monopoly must acknowledge the widespread existence of “rent seeking” in society.³⁸ A mo-

36. Harberger, *supra* note 34, at 86 (social cost may be as little as one-tenth of one percent of national income); Schwartzman, *The Burden of Monopoly*, 68 J. POL. ECON. 627, 629-30 (1960) (social cost of monopoly is less than \$234 million per annum); *see also* Goldberg, *Welfare Loss and Monopoly: The Unmaking of an Estimate*, 16 ECON. INQUIRY 310, 311 (1978) (arguing that others have overstated the social cost of monopoly); Goldberg, *A Note on the Costs of Monopoly*, 17 ANTITRUST BULL. 479, 482 (1982) (same).

37. *See* Comanor & Smiley, *Monopoly and the Distribution of Wealth*, 89 Q.J. ECON. 177 (1975) (social cost of pricing above marginal cost is large); Hall, *The Relation Between Price and Marginal Cost in U.S. Industry*, 96 J. POL. ECON. 921 (1988) (same); Kamerschen, *An Estimation of the “Welfare Losses” from Monopoly in the American Economy*, 4 W. ECON. J. 221, 235 (1966) (concluding that the social cost of monopoly may be as high as six percent of national wealth); Stigler, *The Statistics of Monopoly and Merger*, 64 J. POL. ECON. 33, 34-35 (1956) (arguing that Harberger and others understated the social cost of monopoly).

38. Tullock, *The Welfare Costs of Tariffs, Monopolies, and Theft*, 5 W. ECON. J. 224 (1967). Other important contributions to this argument include Krueger, *The Political Economy of the Rent-Seeking Society*, 64 AM. ECON. REV. 291 (1974), and Posner, *The Social Cost of Monopoly and Regulation*, 83 J. POL. ECON. 807 (1975). The argument’s predecessor is Plant, *The Economic Theory Concerning Patents for Inventions*, 1 ECONOMICA 30 (New Ser. 1934). In addition, much of the “social choice” literature of the mid-1980s dwells on the inefficiencies that attend lobbying and other forms of “rent seeking.” *See* R. POSNER, *ECONOMIC ANALYSIS OF LAW* 249-63, 317-64, 491-507 (3d ed. 1986); Easterbrook, *The Supreme Court, 1983 Term — Foreword: The Court and the Economic System*, 98 HARV. L. REV. 4, 45-58 (1984); Farber & Frickey, *The Jurisprudence of Public Choice*, 65 TEXAS L. REV. 873 (1987).

For criticism of the rent seeking theory as applied to merger cases, *see* Muris, *supra* note 25, at 381, 392 n.41, and Williamson, *Economies as an Antitrust Defense Revisited*, 125 U. PA. L. REV. 699, 713-23 (1977). Muris and Williamson do not object to the theory, but rather to any broad application of it in merger policy. They argue that, since the increase in market power that results from a marginally legal merger is small, firms will not spend vast amounts in rent seeking in order to merge.

nopoly is valuable to its owner. People who have monopolies will be willing to spend a certain part of their resources in order to maintain or enlarge them. Likewise, people who do not have monopolies will be willing to spend resources in an effort to acquire them. Some of these expenditures may result in social benefits. For example, our patent system is based on the premise that research and development is socially valuable, and ought to be rewarded with a finite period of monopoly profits.³⁹

But a good deal of rent seeking is inefficient. The taxicab company that petitions or perhaps bribes the city council for an airport monopoly, the dominant firm that uses patent fraud to exclude rivals, the cartel that goes to great lengths to make sure that its members do not cheat it through secret price concessions — all of these firms spend at least part of their anticipated monopoly returns in the enterprise of creating or retaining the monopoly itself. At the margin, rectangle 2-3-5-4, identified in Figure Three as a mere wealth transfer, is not a wealth transfer at all, but a wasted resource: money inefficiently spent by the monopolist or aspiring monopolist intent on retaining or attaining a monopoly position. In Figure Three, rectangle 2-3-5-4 is designated “WL2,” for it constitutes a second element of welfare loss, or loss in allocative efficiency, caused by monopoly.

A few observations about this second method for estimating the social cost of monopoly are in order:

1. Under Method II, the social cost of monopoly is larger than under Method I, for Method II includes the entire deadweight loss triangle (*WL1*) plus the sum of any resources inefficiently spent by the firm in attaining or retaining its monopoly position (at least part of *WL2*). How much larger the cost is when calculated under Method II instead of Method I is difficult to say. As noted earlier, if the demand curve is linear, rectangle 2-3-5-4 is precisely twice as big as triangle 4-5-6.⁴⁰ If a firm in such a market should spend its entire anticipated monopoly overcharge inefficiently in attaining its monopoly, the allocative efficiency loss caused by monopoly as measured under Method II would be precisely three times the loss as measured by Method I. This might happen if there were perfect competition in the “market” for a particular monopoly, where a firm would invest in prospective monopoly up to the point that investment equalled the anticipated

39. See Kaplow, *The Patent-Antitrust Intersection: A Reappraisal*, 97 HARV. L. REV. 1813 (1984).

40. See *supra* note 17 and accompanying text.

return.⁴¹

But in the real world demand curves are not linear. Further, not all the resources spent by the monopolist in attaining or retaining its position are spent inefficiently. For example, while innovation is a form of "rent seeking" in that a firm does it in order to earn monopoly profits, most innovation is efficient. Depending on the shape of the demand curve, the social cost of monopoly as measured by Method II could be either less than or greater than three times the traditional deadweight loss.

2. Although measuring the social cost of monopoly under Method I is very difficult, it is still more difficult to measure under Method II. Measuring the social cost of monopoly under Method I requires information about marginal cost at the competitive rate of output,⁴² current prices, and the shape of the demand curve.⁴³ Of these three elements, only current price is easy to obtain; the other two, marginal cost at the competitive rate of output and the shape of the demand curve, can perhaps be estimated with some difficulty.

Measuring the social cost of monopoly under Method II requires all of the information used in Method I plus information about the strategic, or rent-seeking, behavior of firms. We need to know not only how much the firm spends in attempting to attain or retain monopoly power, but also how much of this money is being spent efficiently and how much inefficiently. Such determinations raise difficulties of a different magnitude than those under Method I. For example, they involve such perplexing questions as whether advertising, product differentiation, or innovation are ever anticompetitive and, if so, how to disaggregate the cost of efficient advertising from inefficient advertising. These problems are almost certainly intractable by any methodology known today.

C. *The Social Cost of Monopoly: Method III*

Figure Three illustrates the two elements of the social cost of monopoly described to this point, *WL1* and *WL2*, as well as a rectangle, not part of the demand curve or its cost and revenue functions, called "*WL3*." Even the sum of *WL1* and *WL2* understates the social cost of

41. For example, if firms bid against each other for an exclusive monopoly franchise, the bid price can be expected to approach the present value of anticipated monopoly returns.

42. Because marginal cost is not necessarily constant, but may rise as output increases, marginal cost at the current, or monopoly, output is often the wrong figure.

43. Most models relate marginal cost to current price, or simply look at rates of return as a surrogate for the relationship between marginal cost and price. See, e.g., Hall, *supra* note 37, at 921-22; Harberger, *supra* note 34, at 77.

the kind of monopoly with which the antitrust laws are concerned. The missing element of the social cost of monopoly, *WL3*, is drawn away from the demand curve because *WL3* is not captured by the demand curve itself. Its definition, existence, or size is not clearly related to any of the cost or revenue functions ordinarily included in the demand curve.

Exclusionary practices, or rent seeking, by the monopolist generally impose costs on the monopolist itself. The costs can be diagrammed, for their outer limit is determined by the wealth transfer, which is itself a function of the demand curve and the monopolist's marginal cost curve. A firm will not spend more in acquiring or maintaining a monopoly than the value of the monopoly. Thus the outer boundaries of monopoly rent seeking are determined by the potential wealth transfer (*WL2*).

But monopoly rent seeking also imposes inefficient losses on competitors, or perhaps others, and these losses are potentially unlimited. They can certainly be substantially larger than either the traditional deadweight loss (*WL1*) or the loss that results from rent seeking (*WL2*). To take an extreme example, suppose that the world market contains two aircraft manufacturers, each of which owns a single plant. The chief executive officer of one of the firms creates a monopoly by visiting the other firm's plant one night with a can of gasoline and a match, and burning it down. In this case, *WL1* is indeterminate; *WL2* is the cost of the match, the gasoline, the opportunity cost of the CEO's time, and the risk and expected consequences of getting caught. At the very least, *WL3* is the cost of the destroyed plant, inventory, and perhaps goodwill, of retraining employees whose jobs have been lost, and of reliance interests lost by broken contracts.⁴⁴

What is the size of *WL3* in real-world monopolization or cartel cases? Generalizing is difficult, but it could be substantial.⁴⁵ Con-

44. For example, if a supplier has invested heavily in a contractual commitment to supply the victim firm with some input, that investment may now be lost if it cannot be redeployed.

45. One might argue that in a world without transaction costs *WL3* can never be greater than the net wealth transfer (the wealth transfer rectangle less the resources spent in acquiring the monopoly), for if it were, competitors would pay the monopolist in order to be free of the exclusionary practice. For example, if the monopoly that is created when the CEO torches a competitor's plant has a net value to the monopolist of \$1000, but the destroyed plant costs the competitor \$5000, the competitor will pay the aspiring monopolist something between \$1000 to \$5000 not to destroy its plant. See Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960).

The possibility of this transaction actually occurring is decreased by several factors. Most important, it is illegal to destroy a competitor's plant. The aspiring monopolist would have to make a credible threat that it could destroy the plant without leaving evidence sufficient for conviction, and the threat itself would have to be unprovable in court. Further, the aspiring monopolist would have to make some kind of credible commitment that, once the bribe was paid, it would not make the same threat again and again and again.

If the aspiring monopolist were caught, its damages under the antitrust laws would be at least

sider, for example, the Supreme Court's recent decision in *Allied Tube & Conduit Corp. v. Indian Head, Inc.*⁴⁶ The plaintiff, Indian Head, had developed a plastic electrical conduit that threatened substantial injury to the market for traditional steel conduit. Defendant Allied, a manufacturer of steel conduit, conspired with others to "pack" a meeting of a standard-setting organization, with the result that approval of the plastic conduit was successfully delayed for several years. Because government building codes generally incorporated the standard-setting organization's standards verbatim, the effect was that the plaintiff's plastic conduit could not be used in most construction.

In *Indian Head*, *WL1* is the deadweight loss caused by any monopoly perpetuated by Allied's conduct.⁴⁷ *WL2* is wealth transferred from consumers to Allied and its co-conspirators, discounted by the costs of packing the meeting and campaigning for disapproval of the plastic conduit, and the risk of a lawsuit and its costs. *WL3* is the lost investment suffered by Indian Head in research and development of a product that now has no market, or whose introduction into the market has been delayed. If Allied had succeeded in delaying the marketing of plastic conduit indefinitely, Indian Head's entire investment in researching and developing a socially valuable product would have been lost.

Most bona fide monopolization cases produce more than trivial amounts of *WL3* loss. Often the amount of *WL3* loss will be proportional to the plausibility of the basic offense. For example, monopolizing conduct is most likely to succeed in markets where assets are specialized, durable, and costly, because new entry into such markets can be deterred most easily. These markets are said to be subject to high barriers to entry.⁴⁸ *WL3* loss is also likely to be larger in such markets, because it is more likely that investment in production facili-

\$15,000 (lost investment plus lost profits, trebled). The intended victim might prefer to lie in wait and catch the CEO in the act, *after* the plant has been destroyed in order to benefit from the trebled damages.

WL3 losses might also include practices that raise the marginal costs of rivals, thus causing deadweight losses in secondary markets. See Salop & Scheffman, *Raising Rivals' Costs*, 95 AM. ECON. A. PAPERS & PROC. 267 (1982); Note, *Rationalizing Antitrust Cluster Markets*, 95 YALE L.J. 109, 117 n.42 (1985).

46. 108 S. Ct. 1931 (1988). A similar case is *American Socy. of Mechanical Engrs. v. Hydrolevel Corp.*, 456 U.S. 556 (1982).

47. Actually, the *Indian Head* situation may be a little more complex. Presumably, the demand curve for conduit would shift to the right in response to the introduction of Indian Head's product. The result of the conspiracy was to delay this shift, yielding a deadweight loss analogous to that caused by monopolization of a market in which no technological change is occurring.

48. See 2 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 409 (1978); P. AREEDA & H. HOVENKAMP, *supra* note 21, at ¶¶ 711.2d, 917.1.

ties or research and development cannot be recovered in the event of failure. In short, under this method for calculating the social cost of monopoly, monopolization is the biggest threat in situations where *WL3* loss is likely to be highest.⁴⁹

D. *The Optimal Deterrence Model Reconsidered*

Consider the firm that excludes its rival by engaging in patent fraud,⁵⁰ or the colluding joint venture that uses a boycott to deprive a disruptive competitor of an essential input.⁵¹ Suppose that the activity creates or perpetuates a monopoly that results in a traditional dead-weight loss of \$100 and a wealth transfer of \$200. The activity may or may not produce some compensating cost reductions but, for the sake of argument, assume cost reductions of \$125. If damages are measured by the Optimal Deterrence Model, the violators will pursue their activity because it promises a profit of \$325 and a fine of only \$300.

But suppose in addition that the activity forces the competitor to exit from the market, requiring the closure of a specialized plant or the loss of expenditures on research and development or advertising equal to \$35. In that case, the activity is inefficient; yet, the Optimal Deterrence Model would permit the activity, despite this inefficiency, for the Model neglects to take *WL3* losses into account.

E. *Antitrust Injury*

One possible defense of the Optimal Deterrence Model is that *WL3* losses are not really a social cost of monopoly as such, but rather the social cost of harmful conduct generally. For example, arson imposes a social cost when property is destroyed and we condemn arson for that reason alone, without regard to its potential for creating a monopoly. We should not use the antitrust laws to condemn arson, this argument goes, even though arson is socially costly. The antitrust laws should be used only to condemn monopoly.

49. One important exception to this is strategic entry deterrence, or exclusionary conduct directed at potential, rather than actual, competitors. Potential competitors may be deterred easily precisely because they have not yet made irreversible investments in a market. *WL3* losses in such situations are accordingly smaller. See P. AREEDA & H. HOVENKAMP, *supra* note 21, at ¶ 340.2j; Salop, *Strategic Entry Deterrence*, 91 AM. ECON. A. 335 (1978); Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284 (1977).

50. For example, by suing or threatening to sue on patents that it knows to be invalid. See 3 P. AREEDA & D. TURNER, *supra* note 48, ¶ 708; P. AREEDA & H. HOVENKAMP, *supra* note 21, at ¶ 708'.

51. A disruptive competitor is one who refuses to go along with the express or tacit collusion of others. See United States Department of Justice, Merger Guidelines § 3.44(c), 49 Fed. Reg. 26,823, 26,833 (1984). For the general problem of joint ventures' exclusion of competitors, see United States Department of Justice, International Operations Antitrust Enforcement Policy, 24 Trade Reg. Rep. (CCH) § 3.42 (Supp. Nov. 10, 1988).

The response to this argument is that although arson is not generally an antitrust problem, it can become one when it is used by a firm in order to create a monopoly or when it naturally has the effect of creating a monopoly. Further, not all activities that result in *WL3* losses are illegal under some independent body of law. The relevant question for antitrust policy is not whether conduct is independently illegal, but whether it is anticompetitive and calculated to create or maintain a monopoly. The so-called *Brunswick*, or "antitrust injury," doctrine addresses these concerns.⁵² In order to prevail, the Sherman Act plaintiff must show first that the challenged conduct was anti-competitive — *i.e.*, calculated to create a monopoly. Second, the plaintiff must show that it suffered an injury of the type that the antitrust laws were intended to condemn, and which "flow[ed] from that which makes the defendants' acts unlawful" under the antitrust laws.⁵³ The fact that an efficient plant was forced to close or that a potentially successful product was kept off the market is part of the social cost of monopoly only if the person responsible did it in order to attain or retain a monopoly position. In that case, the victim has been injured by the kind of activity that the antitrust laws were designed to protect against. A properly constructed Optimal Deterrence Model must consider *all* the social costs of monopoly, or it will underdeter.⁵⁴

III. THE LEGISLATIVE HISTORY OF THE ANTITRUST LAWS

The legislative history of the antitrust laws makes clear that injuries caused by monopoly were prominent in the minds of the Sherman Act's framers. While the economic concepts of allocative efficiency and social cost were unknown to them,⁵⁵ some members of Congress realized that monopoly yielded both high prices and reduced output. Some were concerned about the injuries that powerful firms might

52. See *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977); see also *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104 (1986); P. AREEDA & H. HOVENKAMP, *supra* note 21, at ¶ 334.2.

53. *Brunswick*, 429 U.S. at 489.

54. As Landes formulates the Optimal Deterrence Model, the optimal fine "should equal the net harm to persons other than the offender." However, Landes neglects to take *WL3* losses into account. See Landes, *supra* note 2, at 656.

55. The geometric illustration of monopoly is attributable chiefly to Alfred Marshall, whose *Principles of Economics* was first published in 1890. Marshall relied on Augustin Cournot's *Researches into the Mathematical Principles of the Theory of Wealth* originally published in 1838 (English ed. 1929). See A. MARSHALL, *PRINCIPLES OF ECONOMIES* 493-94, 820 (8th ed. 1938); Stigler, *Perfect Competition, Historically Contemplated*, 65 J. POL. ECON. 1 (1957). Cournot's book was generally not accessible in the United States in the nineteenth century. The modern notion of the "social cost" of monopoly and the welfare loss triangle is really a product of the welfare economics of the 1920s. See Hovenkamp, *The Sherman Act and the Classical Theory of Competition*, 75 IOWA L. REV. (forthcoming 1989).

visit upon their smaller competitors. At the same time, many were also concerned that successful firms not be condemned as illegal monopolists merely because they were somehow superior to their rivals.⁵⁶

In 1966, Robert Bork attempted to show that Congress' dominant concern in passing the Sherman Act was allocative efficiency, neoclassically defined.⁵⁷ According to Bork, wealth transfers from consumers to dominant firms were really not all that important as far as the Congress of 1890 was concerned. Neither was it concerned about injury to competitors. Congress' principal concern, Bork argued, was that monopoly would lower output and force consumers to make inefficient substitutions for the monopolized product.⁵⁸

But Bork's analysis of the legislative history was strained, heavily governed by his own ideological agenda. He concluded all too quickly that because some members of Congress knew that demand curves slope downward (*i.e.*, that output is reduced as prices rise),⁵⁹ that they also had a modern conception of allocative efficiency and the social cost of monopoly. Not a single statement in the legislative history comes close to stating the conclusions that Bork drew.⁶⁰

In 1982, Robert Lande looked at the same legislative history — in fact, at many of the same statements that Bork had highlighted — and concluded that Congress' primary concern was not allocative efficiency, but rather wealth transfers away from consumers and to the monopolist.⁶¹ The difference between Bork's and Lande's conclusions is important. For example, under Bork's analysis an efficiency-creating agreement among competitors, or even a horizontal merger that actually results in higher prices, should be legal if the gains to the

56. See *infra* note 64.

57. Bork, *Legislative Intent and the Policy of the Sherman Act*, 9 J.L. & ECON. 7 (1966) [hereinafter Bork, *Legislative Intent*]. Bork made the same argument, although in less detail, in R. BORK, *supra* note 24, at chs. 1 & 2.

58. See Bork, *Legislative Intent*, *supra* note 57, at 47.

59. See 21 CONG. REC. 2462 (1890) (statement of Sen. Sherman) (noting that contracts that increase prices also "diminish the amount of commerce"); see also 21 CONG. REC. 2558 (1890) (statement of Sen. Pugh) (noting that the aim of trusts is "to limit the production of articles . . . for the purpose of destroying competition in production and thereby increasing prices to consumers"); 21 CONG. REC. 4101 (1890) (statement of Rep. Heard) ("[T]he very object of these giant schemes of combined capital is not to increase the volume of supply, and thus lessen the cost of any useful commodity, but rather to repress, reduce, and control the volume of every article that they touch, so that the cost to consumers is increased while the expenditure for production is lessened, and thereby their profit secured.").

60. About the best Bork could come up with were a few statements that combinations whose impact is merely to reduce the costs of production should not be condemned. See Bork, *Legislative Intent*, *supra* note 57, at 26-31.

61. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 34 HASTINGS L.J. 67, 150 (1982) [hereinafter Lande, *Wealth Transfers*]; see also Lande, *The Rise and (Coming) Fall of Efficiency as the Ruler of Antitrust*, 33 ANTITRUST BULL. 429, 449 (1988).

participants are greater than the losses to the consumers and so long as no one else is affected. Under Lande's analysis, however, such mergers or joint ventures should be illegal, because Congress was more concerned about the transfer of wealth away from consumers than it was about efficiency as such.

My own reading of the legislative history of the Sherman Act suggests the following:

(1) The members of Congress in general, and particularly Senator John Sherman, wanted to preserve something they called "competition." Although "competition" was never defined formally, most of the speakers appeared to use it to mean "rivalry," or the presence of multiple sellers in a market. Never once was "competition" defined as a state of affairs in which price equals marginal cost, or any other measure of cost. That is not surprising, since in 1890 the conception of "competition" as a state of affairs in which price equals marginal cost was not yet formulated in the economic literature.⁶²

(2) Several members of Congress understood that high prices and lower output went hand-in-hand — that is, that demand curves slope downward.⁶³

(3) Most members of Congress who spoke on the question believed that combinations should not be condemned if their *only* effect was to lower the costs of production.⁶⁴

(4) The members of Congress who spoke on the question believed that combinations that lowered the costs of production *but that also* decreased output or increased prices *should* be condemned⁶⁵ — herein lies the difference between Bork and Lande.

(5) Nearly every member of Congress who spoke on the issue suggested that consumer lawsuits would be ineffectual because individual consumer injuries were too small; further, everyone agreed that

62. See Hovenkamp, *supra* note 55. However, the basic concept of marginal cost, unlike the modern concept of allocative efficiency, was known in the economics literature by 1890. *E.g.*, A. MARSHALL, *supra* note 55, at 151-75; see generally Howey, *The Origins of Marginalism*, in *THE MARGINAL REVOLUTION IN ECONOMICS* 15 (R. Black, A. Coats & C. Goodwin eds. 1973). The term "marginal cost" never appears in the legislative history of the Sherman Act. How Congress could have been thinking of allocative efficiency without mentioning marginal cost, Bork fails to tell us.

63. See *supra* note 59 and accompanying text.

64. See 21 CONG. REC. 2457 (1890) (statement of Sen. Sherman) (The bill "does not in the least affect combinations in aid of production where there is free and fair competition." Senator Sherman also praised corporations to the extent that they "lessen the cost of production."); see also 21 CONG. REC. 3151-52 (1890) (statement of Sen. Hoar) (arguing that section 2 would not condemn a corporation that acquired the "whole business" merely because it was the best competitor).

65. See *supra* notes 57-61 and accompanying text.

competitors should be entitled to sue.⁶⁶

(6) Although the drafters of the Sherman Act were concerned about injury to consumers, they were at least as concerned with various kinds of injury to competitors.⁶⁷

On point (4) — the heart of the dispute between Bork and Lande — Lande clearly appears to have the better supported argument. Senator Sherman's own view was that a combination that resulted in higher prices to consumers would not be exempt even though it reduced production costs as well:

It is sometimes said of these combinations that they reduce prices to the consumer by better methods of production, but all experience shows that this saving of cost goes to the pockets of the producer. The price to the consumer depends upon the supply, which can be reduced at pleasure by the combination. It will vary in time and place by the extent of competition, and when that ceases it will depend upon the urgency of the demand for the article.⁶⁸

A. *The Efficacy of Consumer Lawsuits*

On point (5), several members of Congress questioned consumer lawsuits as antitrust enforcement devices. To the extent that the Sherman Act purported to enact the common law of trade restraints, there was good reason for such doubts. The common law generally denied consumer damages actions for overcharge injuries.⁶⁹ As a general matter, cartels were unenforceable at common law; yet neither were they challengeable by third parties such as consumers. Boycotts could be challenged by nonparticipants, but the challengers were almost always competitors.⁷⁰

Further, the Congressmen who spoke to the issue of consumer lawsuits were generally doubtful about their efficacy. For example, Senator James Z. George of Mississippi objected that individual consumers would suffer a very small injury:

It is manifest that in nearly every instance the damage by the advanced

66. See *infra* note 70 and accompanying text.

67. For the concerns for consumer or competitor welfare expressed by the framers of the Sherman Act, see the Appendix to this Article *infra*.

68. 21 CONG. REC. 2460 (1890). Although the Senate at one point adopted an amendment that would have exempted combinations that lessened production costs (provided that they did not do so by lowering wages) without regard to where the profits went, see *id.* at 2654-55, this language did not survive to the final bill as it came out of the conference committee. See *id.* at 6208, 6312.

69. See Hovenkamp, *supra* note 55.

70. *Id.* One important exception was an employer's challenge to labor strikes. Courts frequently treated labor strikes as boycotts and permitted employers to bring actions as consumers of labor. The remedy in such cases was ordinarily an injunction. See Hovenkamp, *Labor Conspiracies in American Law, 1880-1930*, 66 TEXAS L. REV. 919 (1988).

price of each article affected by these combinations would be — though in the aggregate large, indeed — so small as not to justify the expense and trouble of a suit in a distant court. The consumer claims a loss of, say, \$25, on a particular article, as sugar, affected by the combination. If he succeeds he gets double damages;⁷¹ that is, \$50. He may live in Missouri, or Texas, or Kansas; he must go to New York, or Boston, or Chicago, or some distant city to bring his suit. He is poor, a farmer, or mechanic, or laborer. He undertakes to get damages from a powerful and rich corporation, or combination of corporations and persons. . . .

I do not hesitate to say that few, if any, of such suits will ever be instituted, and not one will ever be successful.⁷²

Senator George later attempted to remedy this situation with an amendment that would have permitted a type of plaintiff class action in which liability would be determined as to a large group of plaintiffs but damages would be assessed to each individually.⁷³ The amendment was rejected,⁷⁴ despite Senator George's protests that consumer injuries would be too small to warrant bringing suits individually.⁷⁵

Senator Frank Hiscock of New York likewise noted that the consumers of trust articles were often located in different states than the trust itself, that their particular injuries were small, and that lawsuits would require travel. Furthermore, the plaintiffs would almost certainly have to be final consumers, for the "middlemen will never commence these actions" since they are not the ultimate victims.⁷⁶

In one dialogue involving Senator Sherman, Senator John T. Morgan of Alabama described two different abuses by trusts. The first abuse involved exclusionary, predatory practices by the cottonseed-oil trust against a competitor.⁷⁷ The second abuse involved injuries to consumers caused by monopoly price increases.⁷⁸ With respect to the

71. Senator Sherman's amended bill provided for double damages. S. 1, 51st Cong., 1st Sess. § 2 (1890) (as reported by the Senate Committee on Finance on Jan. 14, 1890). The bill that eventually came out of the Judiciary Committee contained a treble damages provision. S. 1, 51st Cong., 1st Sess. § 7, 21 CONG. REC. 3145 (1890).

72. 21 CONG. REC. 1768 (1890).

73. *Id.* at 3148. The amendment would have permitted any number of persons complaining of such injuries committed by the same defendant against each of them separately, to join as plaintiffs, and the court or jury trying the issues of fact in any such cause shall find the amount of the separate damages sustained by each plaintiff and may also find in favor of a part of said plaintiffs and against the others, as the proof shall warrant.

Id.; see also *id.* at 3150 (statement of Sen. George).

74. *Id.* at 3148.

75. *Id.* at 3147-48.

76. *Id.* at 2571.

77. *Id.* at 2609.

78. *Id.* at 2610. See also the comments by Senator Richard Coke, attacking the private remedy provision as a "wasp without a sting" with respect to consumers who paid higher prices. *Id.* at 2615. And see the comments by Senator Teller of Colorado, criticizing the bill's private

second, Senator Morgan noted the problem of tracing the product to the wrongdoer, particularly where the product was a fungible commodity, such as sugar. Senator Morgan noted that double damages would not be available unless the consumer could "identify the sugar, or the molasses, or whatever it is, and run it back to the manufacturer or to the refiner and prove the conspiracy."⁷⁹

Senator Sherman responded to Senator Morgan by observing that the competitor injured by the cottonseed-oil trust's predatory practices could sue under his bill. He made no response to Senator Morgan's difficulties with consumer actions and the problem of tracing damages.⁸⁰

Senator Sherman himself paid little attention to the question of private enforcement, preferring to emphasize the power of the United States government to bring suit.⁸¹ Importantly, no one defended the efficacy of consumer lawsuits.

On the other hand, no one doubted that competitor lawsuits would work. Everyone who spoke about them believed that competitors should be freely permitted to enforce the antitrust laws. Senator Sherman himself spoke of the "humble man" who dares to start a business "in opposition to" a giant trust, such as Standard Oil. He knew of such men, he said, and his bill was meant to give them a right to sue.⁸² Senator George F. Hoar of Massachusetts, who was more responsible than Senator Sherman for the final language of the Sherman Act,⁸³ defended the monopolizing prohibition of section 2 entirely in terms of injury to competitors. Section 2 was necessary, Hoar argued, because section 1 required a combination, while section 2 referred to the unilateral "engrossing to a man's self by means which prevent other men from engaging in fair competition with him."⁸⁴ Senator George F. Edmunds of Vermont agreed, citing the *Webster's Dictionary* definition of "to monopolize" not as obtaining power to raise price or reduce output, but rather "[t]o purchase or obtain possession of the whole of . . . with the view to appropriate or control the exclusive sale."⁸⁵

remedy provision because the damages caused to consumers were "inconsequential individually, but great to the whole mass of people." *Id.* at 2571.

79. *Id.*

80. *Id.*

81. *See, e.g., id.* at 2461.

82. *Id.* at 2569.

83. *See* H. THORELLI, THE FEDERAL ANTITRUST POLICY 210-14 (1955); Letwin, *Congress and the Sherman Antitrust Law: 1887-1890*, 23 U. CHI. L. REV. 221, 254-55 (1956).

84. 21 CONG. REC. 3152 (1890).

85. *Id.*

Thus, built into the legislative history was a concept roughly akin to the "antitrust injury" requirement of today:⁸⁶ only conduct calculated to create a monopoly is to be condemned. However, competitors, at least as much as consumers, are to be considered among antitrust's protected classes.

Of course, private antitrust actions today are governed by sections 4 and 16 of the Clayton Act, which was passed in 1914,⁸⁷ and not by the Sherman Act. However, those sections of the Clayton Act were passed with almost no legislative discussion. Their purpose was to extend the power of private enforcement to all the federal antitrust laws, including both the Sherman Act and the Clayton Act.⁸⁸ In substance, section 4 of the Clayton Act is otherwise identical to its predecessor, section 7 of the Sherman Act.⁸⁹ Although the debate surrounding passage of the Clayton Act is voluminous, it contains virtually no discussion of the respective merits of consumer or competitor lawsuits.

B. *The Significance of Congressional Concern About Monopoly Prices*

My point (6) is that Congress was as concerned about injury to competitors as injury to consumers. Judge Easterbrook has argued that when Senator Sherman and his colleagues "protested the sugar trust and other malefactors," their principal concern was high consumer prices.⁹⁰ "However you slice the legislative history," he concludes, "the dominant theme is the protection of consumers from overcharges. . . . The few references in the legislative history to 'small dealers' are a sideshow."⁹¹

The legislative history of the Sherman Act contains ample reference to both high consumer prices and injury to competitors. But a good deal of *external* history suggests that Judge Easterbrook has the sideshow and the main event reversed.

86. See *supra* notes 52-54 and accompanying text.

87. 15 U.S.C. § 15 (1986) (private treble damage actions); 15 U.S.C. § 26 (1986) (private injunctive relief).

88. See H.R. REP. NO. 627, 63d Cong., 2d Sess., pt. 1, at 14 (1914) (purpose of then § 5, now § 4, of the proposed Clayton Act was to supplement § 7 of the Sherman Act by creating a damages action for violation of "any of the antitrust laws").

89. Section 7 of the Sherman Act provides:

Any person who shall be injured in his business or property by any other person or corporation by reason of anything forbidden or declared to be unlawful by this act, may sue therefor in any circuit court of the United States in the district in which the defendant resides or is found, without respect to the amount in controversy, and shall recover three fold the damages by him sustained, and the costs of suit, including a reasonable attorney's fee.

Sherman Act, ch. 647, § 7, 26 Stat. 209, 210 (1890).

90. Easterbrook, *Workable Antitrust Policy*, 84 MICH. L. REV. 1696, 1702-03 (1986).

91. *Id.* at 1703 (footnote omitted).

Much of the wrath of the Sherman Act's framers was directed at the sugar trust and at Standard Oil Company of Ohio, then facing a forced dissolution and reorganization under the corporate law of New Jersey.⁹² Were the real complaints about the sugar trust and Standard Oil directed at their high prices? Hardly. From 1880 through 1890, the price of refined petroleum in the United States fell by sixty-one percent, by far the largest decrease in a decade of generally decreasing prices, and there was over the same period an almost four-fold increase in output.⁹³ The Standard Oil Company was responsible for much of this,⁹⁴ and some members of Congress knew it.⁹⁵ George Gunton, a contemporary economist and observer, noted in 1888 that between 1871 and 1887 the price of crude fell from 10.52 cents per gallon to 1.59 cents, and the price of refined oil from 24.24 cents per gallon to 6.75 cents.⁹⁶ Gunton's figures also showed that the amount added to the price by the refining process itself fell from 13.72 cents per gallon in 1871 to 5.16 cents per gallon in 1887.⁹⁷ Whatever the cause for Congress' complaint about Standard Oil, it was *not* high consumer prices, not during the twenty-year period prior to the Sherman Act's passage.

The sugar trust, Congress' other big target⁹⁸ and the subject of the Supreme Court's first Sherman Act decision in 1895,⁹⁹ showed the same kind of performance, although the price decreases were not as dramatic. The price of sugar fell by more than eighteen percent between 1880 and 1889, and would fall another twenty-eight percent between 1890 and 1900, the decade during which the United States brought its antitrust action against the sugar trust.¹⁰⁰ The iron and

92. The court in *State v. Standard Oil Co. of Ohio*, 49 Oh. St. 137, 30 N.E. 279 (1892), forced Standard Oil Company to divest most of its assets. Standard Oil Company responded by expanding and reorganizing under a preexisting corporate structure in New Jersey. J. JENKS & W. CLARK, *THE TRUST PROBLEM* 347-48 (1929 & reprint 1973).

93. See L. TELSER, *supra* note 5, at 27.

94. See McGee, *Predatory Price Cutting: The Standard Oil (N.J.) Case*, 1 J.L. & ECON. 137 (1958).

95. See *infra* notes 124, 140 and accompanying text.

96. Gunton, *The Economic and Social Aspect of Trusts*, 3 POL. SCI. Q. 385, 394 (1888).

97. *Id.*; see also J. JENKS & W. CLARK, *supra* note 92, at 108, Chart V (showing steadily decreasing prices from 1880 to approximately the beginning of the first world war, even as Standard Oil was acquiring its dominant position); E. VON HALLE, *TRUSTS, OR INDUSTRIAL COMBINATIONS AND COALITIONS IN THE UNITED STATES* 72-74 (1900) (same). Von Halle's well-known book generally identifies the primary evils of the trusts as price cutting and granting rebates, the effect of which was to injure competitors. *Id.* at 79-91.

98. In part, because of the decision in *People v. North River Sugar Refining Co.*, 121 N.Y. 582, 24 N.E. 834 (1890).

99. *United States v. E.C. Knight Co.*, 156 U.S. 1 (1895); see L. TELSER, *supra* note 5, at 28.

100. L. TELSER, *supra* note 5, at 28-29; see also J. JENKS & W. CLARK, *supra* note 92, at 82, Chart I (showing steadily decreasing prices from 1880 to 1900).

steel industry, another target of the Sherman Act's proponents, had experienced price declines of twenty-one percent.¹⁰¹ Across the board, the prices of manufactured goods declined during the 1880s,¹⁰² and even the railroad cartels appeared not to be working very well.¹⁰³ Furthermore, Congress was not at all clear about whether it even intended railroads to be covered by the Sherman Act, given that the Interstate Commerce Act had been passed three years earlier. A Supreme Court decision in 1897 first established that railroads were covered by the Sherman Act.¹⁰⁴

One might suggest that although prices in fact fell during the 1880s, the common belief was that prices were rising and Congress was responding to this perception. But that does not seem to be the case either. Most of the contemporary evidence established without controversy that prices were indeed falling, a fact that contemporary economists readily confirmed.¹⁰⁵ In fact, "ruinous competition" was perceived to be a much bigger threat than high prices.¹⁰⁶

So to posit that Congress' principal concern in enacting the Sherman Act was high consumer prices is to suggest that Congress was dealing with a problem that did not exist. To be sure, economists had already developed a predatory pricing theory that dominant firms might use temporary periods of low pricing in order to drive out competitors and charge higher prices later.¹⁰⁷ But as of 1890 the trusts had not succeeded in doing this. The principal victims of the trust movement of the 1880s — certainly of the trusts that appeared most frequently on Congress' hit list — were inefficient small firms, rather than consumers. Competitors were the principal protected class of the Sherman Act.

101. L. TELSER, *supra* note 6, at 28.

102. *Id.* at 12, 27.

103. *Id.* at 30-31; see also T. Ulen, Cartels and Regulations: Late Nineteenth Century Railroad Collusion and the Creation of the Interstate Commerce Commission 224 (unpub. Ph.D. diss. Stanford Univ. 1979).

104. *United States v. Trans-Missouri Freight Assn.*, 166 U.S. 290 (1897).

105. See, e.g., J. JENKS, THE TRUST PROBLEM (1900); Clark, *The Limits of Competition*, in THE MODERN DISTRIBUTIVE PROCESS 11 (J. Clark & F. Giddings eds. 1888); Gunton, *supra* note 96, at 390-94; Jenks, *The Michigan Salt Assn.*, 3 POL. SCI. Q. 78 (1888); Jenks, *The Whiskey Trust*, 4 POL. SCI. Q. 296 (1889).

Even Brown University's Elisha Andrews, one of the most vehement critics of the trusts, conceded that Standard Oil's prices had declined through the 1870s and 1880s. Andrews argued that the rate of decline slowed somewhat after the trust was formed. Further, he argued, Standard Oil made its money by limiting production in order to maintain competitive prices. Andrews, *Trusts According to Official Investigations*, 3 Q.J. ECON. 117, 144-46 (1889).

106. See Hovenkamp, *The Antitrust Movement and the Rise of Industrial Organization*, 68 TEXAS L. REV. 105 (forthcoming 1989).

107. See, e.g., W. COLLIER, THE TRUSTS: WHAT CAN WE DO WITH THEM? WHAT CAN THEY DO FOR US? 123-24 (1900).

There is no evidence of any organized consumer lobbying for the Sherman Act. The principal constituencies of some of the Sherman Act's congressional supporters were owners of small businesses.¹⁰⁸ For example, Senator Sherman was from Ohio, a state that witnessed dramatic declines in the price of refined petroleum products. Senator Sherman was not speaking for consumers of refined petroleum products, but rather for the small producers and refiners whom Standard Oil had driven to ruin.

IV. ANTITRUST'S PROTECTED CLASSES AND PRIVATE ENFORCEMENT

A. *Who Should Be Permitted To Enforce the Antitrust Laws?*

Under the Optimal Deterrence Model, the identity of the person with the cause of action is not all that important, provided the potential plaintiff has the correct incentives. The incentives are not past injury done, but the prospect of recovery. The entire cause of action for the wealth transfer plus the deadweight loss could be given to consumers, to competitors, or, for that matter, to all of the country's identical twins, and the effect would be the same. If suit were profitable, these classes of people would sue.

But section 4 of the Clayton Act provides that only people who have been injured by antitrust violations may sue for damages, and that their damages are to be measured by their injury. Article III of the United States Constitution probably also requires that only people injured by antitrust violations be allowed to sue for damages.¹⁰⁹

As a rough approximation, giving consumers a damages action for overcharge injuries and competitors a damages action for *WL3* losses would appear to satisfy the statutory mandate, although it might be underdeterrent insofar as it fails to include damages based on the traditional deadweight loss caused by monopoly. Ironically, even though the traditional deadweight loss triangle is the oldest recognized and least controversial of monopoly's social costs, the existing rules of antitrust standing rarely permit the deadweight loss to become the ba-

108. This is further borne out by the fact that three months later Congress enacted the McKinley Tariff, one of the most repressive and inflationary in American history, in order to protect American business from foreign competition. See L. TELSER, *supra* note 5, at 21.

109. See *America West Airlines v. Burnley*, 838 F.2d 1343 (D.C. Cir. 1988) (plaintiff who could not show injury caused by defendant's conduct denied constitutional standing; court did not need to reach the issue of Clayton Act standing). But see *County of Oakland v. City of Detroit*, 866 F.2d 839, 845 (6th Cir. 1989) (direct purchaser who successfully passed on entire monopoly overcharge to its own customers might have constitutional standing in spite of the absence of any injury in fact). On the injury of such direct purchasers, see Hovenkamp, *The Indirect Purchaser Rule and Cost-Plus Sales*, 103 HARV. L. REV. (forthcoming 1990).

sis of a damages action. The immediate burden of the traditional social cost of monopoly is borne by consumers who would have purchased the product at a competitive price, but who refuse to buy at the monopoly price. The efficiency loss results from the fact that these consumers must make a substitute choice that gives them a lower consumer surplus than the surplus they would have enjoyed had the market been competitive.

But the courts have not been kind to damages actions by nonpurchasers — people who claim that they would have purchased at the competitive price but responded to the monopoly price by buying something else.¹¹⁰ Under traditional standing doctrine, the judicial skepticism has generally been warranted. In order to prove damages, a nonpurchaser must show (1) that it would have purchased the monopolized product at the competitive price; (2) how much it would have purchased; and (3) the amount by which its consumer's surplus was reduced as a result of the substitute purchase.¹¹¹ Often the first and almost always the second of these involves a great deal of speculation — more than attends the computation of an actual purchaser's overcharge injuries.

Given the existence of *WL3* injury, there is little to justify a rule denying a damages action to competitors, provided that the damages are measured properly.¹¹² In fact, competitors are often the most efficient enforcers of the antitrust laws, for they are in a position to catch monopolistic activity much earlier than are consumers.

B. *Antitrust's Early Warning System*

Of the three kinds of welfare loss caused by monopoly, *WL1* — the traditional deadweight loss caused by inefficient consumer substitution

110. See, e.g., *Montreal Trading, Ltd. v. Amax, Inc.*, 661 F.2d 864 (10th Cir. 1981), *cert. denied*, 455 U.S. 1001 (1982). Most of the cases have involved those claiming that they bought not from the cartel, but from an alternative supplier at a higher price. See, e.g., *Mid-West Paper Prods. Co. v. Continental Group, Inc.*, 596 F.2d 573, 583-87 (3d Cir. 1979). A few courts have granted standing under such circumstances. See, e.g., *In re Beef Indus. Antitrust Litig.*, 600 F.2d 1148 (5th Cir. 1979), *cert. denied sub nom. Safeway Stores v. Meat Price Investigators Assn.*, 449 U.S. 905 (1980). Some plaintiffs have convinced courts to grant standing on the theory that the plaintiff was the victim of a "boycott" — i.e., that in order to carry out its output reduction, the cartel effectively agreed not to deal with a particular class of customers. See, e.g., *Amey v. Gulf Abstract & Title*, 758 F.2d 1486 (11th Cir. 1985), *cert. denied*, 475 U.S. 1107 (1986).

111. For example, suppose that widgets at the competitive price yield a consumers' surplus of \$20, but widgets at the cartel price would yield a consumer's surplus of \$10. Buyer responds to the cartel, however, by purchasing gidgets, which yield a consumer's surplus of \$16. As a rough approximation, Buyer's injury is the number of gidgets it purchased multiplied by \$4 — the amount of lost consumers' surplus on each unit. But Buyer probably purchased fewer gidgets than it would have purchased widgets at the competitive price. In any event, computing the various amounts of consumers' surplus could be a monumentally complex task.

112. See *supra* notes 45-49 and accompanying text.

— is often the last to appear. *WL1* losses generally show up only after the monopolist has succeeded in reducing output and raising price. However, both *WL2* and *WL3* losses occur while the monopolist or aspiring monopolist is taking the anticompetitive actions that it hopes will create or protect its monopoly.¹¹³

This suggests that the argument of some that private damage actions in antitrust cases should be given only to the victims of monopoly overcharges¹¹⁴ amounts to shutting the barn door long after the horse has disappeared. Even an antitrust policy concerned exclusively with economic efficiency would wish to minimize the sum of *WL1* + *WL2* + *WL3*. Since the sum of *WL2* and *WL3* can be far larger than *WL1*, an enforcement policy that recognizes only the victims of *WL1* as members of antitrust's protected class is much too little, very much too late.

The welfare losses in *WL2* offer a deterrence of sorts to monopoly, since the losses fall on the monopolist itself. As a result, a firm will not spend money in creating monopoly if the expected return is less than its costs. But, for the same reason, *WL2* losses create no victims.¹¹⁵

WL3 losses are a different matter. These losses fall most frequently on the monopolist's competitors or potential competitors, although occasionally the victim may be a vertically related firm. For example, the first victims of predatory pricing are a firm's competitors. Consumers are the last. The same is true of most exclusionary practices, such as anticompetitive standard setting,¹¹⁶ patent fraud, and the

113. This is true even of the firm that already has monopoly power and is using an exclusionary practice to protect its position. In that case the deadweight (*WL1*) loss of the conduct is the market's failure to correct itself in the future. *Allied Tube & Conduit Corp. v. Indian Head*, 108 S. Ct. 1931 (1988), is, once again, a good example. Assuming that Allied already had a steel conduit monopoly (or was in a cartel with others), the *WL2* losses (resources expended in packing the standard-setting meeting and compromising its deliberations) and *WL3* losses (lost research investment to Indian Head) occur almost immediately. *WL1* losses are the result of the fact that the future market will contain only steel conduit in an amount controlled by Allied and its fellow cartel members, rather than steel conduit plus plastic conduit.

Sometimes *WL1* losses appear roughly simultaneously with *WL2* and *WL3* losses. For example, an action that raises a rival's marginal cost may immediately give the actor the power to increase price while imposing *WL3* losses on a rival. See Salop & Scheffman, *supra* note 45, at 268.

114. See Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263, 331 (1981) [hereinafter Easterbrook, *Predatory Strategies*]; Easterbrook, *supra* note 2, at 96.

115. One exception is the price-regulated firm entitled to pass *WL2* costs on to consumers. For example, a gas or electric utility company might engage in expensive exclusionary practices designed to deter rivals — such as building plants with large amounts of excess capacity — and then pass the costs on to customers. In that case, the monopoly "overcharge" would account for both *WL1* losses and *WL2* losses.

116. See the discussion of the *Indian Head* and *Hydrolevel* cases, *supra* notes 46-47 and accompanying text.

like. The fact that *WL3* losses are among the first to be experienced suggests that allowing damages actions by victims of *WL3* losses can reduce or eliminate *WL1* losses, reduce *WL3* losses, and even reduce *WL2* losses.

The Optimal Deterrence Model is concerned with deterrence, not with compensation. It might be objected that if the amount of deterrence is set properly, one need not worry about whether enforcement comes early or late. Why not wait until the monopoly is created, and then permit consumers to sue for *WL1* losses and competitors for *WL3* losses? If our deterrence system were perfect, there would be no inefficient antitrust violations under either enforcement system.

The answer is that our deterrence system is not perfect. As long as there is any indeterminacy or imperfection in our system of detecting and prosecuting antitrust violations — that is, as long as some people have reason to believe they can violate the antitrust laws and get away with it — violations will occur. An Optimal Deterrence Model that recognizes this fact must also be concerned with minimizing the social costs of those antitrust violations that will be attempted. In that case, a system that permits the first person injured by the violation to sue is more efficient than a system that requires the legal system to suspend enforcement until the last person has been injured. The competitor lawsuit may illumine the way for others, who may then tag along on the competitor's knowledge. In such circumstances, a little consumer free-riding would not be a bad thing. But such a system will work only if both competitor and consumer have sufficient incentives to sue.¹¹⁷

1. *The Fake Problem of False Positives in Competitor Lawsuits*

The most strongly stated objection to expansive use of competitor lawsuits in antitrust cases is that competitors can be injured by a dominant firm's superior efficiency or competitive prowess just as much as by its anticompetitive exclusionary practices. Furthermore, antitrust litigation does not discriminate very accurately between efficient and inefficient conduct that harms rivals. But we can be more confident that conduct is monopolistic when it actually eventuates in a monopoly.¹¹⁸ Thus, for example, Judge Easterbrook believes that only con-

117. The evidence suggests that consumers are quite likely to sue in the wake of prior determinations of guilt in government or earlier private suits. Whether the willingness to sue results from increased knowledge of the violation or from the effects of offensive collateral estoppel, which can greatly reduce the costs of suit, is difficult to assess. See P. AREEDA & H. HOVENKAMP, *supra* note 21, at ¶¶ 323', 323.1-323.2; Salop & White, *supra* note 13.

118. See, e.g., Easterbrook, *On Identifying Exclusionary Conduct*, 61 NOTRE DAME L. REV. 972 (1986).

sumers should be permitted damages actions for predatory pricing. When they complain, it will be of monopoly. The competitor is likely to complain about the efficient price cut of a superior rival just as much as the predatory price cut of an equally efficient one. The court, given its poor measurement capabilities, is likely to identify the competitive price as predatory.¹¹⁹

The possibility of false positives in antitrust cases generally must be conceded. But any argument that relies on the possibility of false positives to eliminate or limit competitor lawsuits must answer two questions. First, is the problem of false positives so substantial that it warrants throwing out competitor lawsuits altogether — particularly if competitors are able to catch incipient monopolization in its early stages? Second, does the problem go away when consumers rather than competitors bring the lawsuits? If it does not go away, then the first question is also answered: there is no reason for discriminating in favor of consumers and against competitors.

The logic of Judge Easterbrook's argument rests on the premise that courts can more easily recognize illegal monopoly after it has occurred than while it is being created; since we cannot be sure that what a competitor alleges to be predatory pricing is really so, we should wait until after the monopoly is created, and permit consumers to sue.

But this assumes that, once monopoly has allegedly been created, we will be in a better position to judge, first, whether a monopoly has really been created, and second, whether the conduct that created it was competitive or anticompetitive. Efficient as well as inefficient conduct can force rivals from a market. For example, monopolies can be created either by anticompetitive predation or by the efficient price cutting of a firm that has simply achieved lower costs than its rivals.

There is no reason to believe that predatory pricing will be easier to recognize in a later lawsuit by consumers (after rivals have been driven from the market and prices raised) than in an earlier lawsuit by competitors. Indeed, information is more likely to be current at the time of the competitor injury. Furthermore, the competitor or competitors, whose individual losses are relatively large, have incentives to sue that consumers often lack.¹²⁰ Finally, both competitive pricing by a more efficient firm and predatory pricing can produce monopoly. Granted that monopoly has been created, how will the court in the consumer lawsuit determine whether it has been created illegally?

119. See Easterbrook, *Predatory Strategies*, *supra* note 114.

120. Individual consumers will not likely have experienced the kind of dramatic impact on their well-being that would have inspired a competitor to sue. Indeed, consumers may never even realize that they were victims of a successful predation scheme.

Presumably, it will have to make some “guesstimate” by using the Areeda-Turner average variable cost test or some alternative, just as it would do in a competitor lawsuit.¹²¹

Consumer lawsuits are brought only after it seems that predation has succeeded. Competitor lawsuits may be brought after one or two periods of price cutting in which some but not all rivals have been forced from the market. At this stage, one cannot be certain that the predation will succeed — although one can certainly look for signals suggesting that predation cannot succeed, such as the absence of significant entry barriers or the generally competitive structure of the market. In such cases, the complaint should be dismissed. But denying a competitor a damages action merely because no monopoly has yet been created will enlarge, rather than diminish, the social cost of monopoly.

If competitors in the first suit are just as good at proving anti-competitive exclusionary practices as consumers in the later suit, but are in a better position to minimize the social cost of the monopoly at hand, then a competitor lawsuit is a more efficient enforcement device than a consumer suit.

2. *The Vexing Problem of Failed Attempts*

One of the most perplexing questions in the economics-antitrust literature is whether failed attempts — conduct intended to create a monopoly but that fails to do so — should be the subject of private plaintiff damages actions. The courts generally recognize such actions,¹²² although they are more skeptical about the basic antitrust claim if the defendant was clearly unsuccessful in attaining market power.¹²³

Under the strict neoclassical model, the social cost of a failed attempt to create a monopoly is zero. The social cost of a monopoly is the deadweight loss triangle (*WLI*), which comes into existence only when a firm or group of firms with monopoly power reduces output

121. See 3 P. AREEDA & D. TURNER, *supra* note 48, at ch. 7C. The one opportunity for a false positive presented by the competitor lawsuit for predatory pricing, but not by the consumer suit, is the failed attempt. See *infra* section V.B.2. If an attempt to create a monopoly through predation fails, its only victims will be competitors driven from the market or forced to incur losses during the price war. Since no monopoly is created, consumers will enjoy a period of low prices which later will be restored to the competitive level.

122. See, e.g., *Multiflex, Inc. v. Samuel Moore & Co.*, 709 F.2d 980 (5th Cir. 1983), *cert. denied*, 465 U.S. 1100 (1984); *Blanton v. Mobil Oil Corp.*, 721 F.2d 1207 (9th Cir. 1983), *cert. denied*, 471 U.S. 1007 (1985); *Lessig v. Tidewater Oil Co.*, 327 F.2d 459 (9th Cir.), *cert. denied*, 377 U.S. 993 (1964).

123. See, e.g., *Nifty Foods Corp. v. Great Atlantic & Pacific Tea Co.*, 614 F.2d 832, 841 (2d Cir. 1980).

and raises price. In the case of the failed attempt, this never happens; there will be no output reduction and no welfare loss. Since enforcement is costly, the wealth-maximizing rule with respect to failed attempts may be a rule of no liability.

This same rule probably applies if our notion of the social cost of monopoly is expanded to account for *WL2* losses as well as those in the deadweight loss triangle (*WL1*). In this case, the failed attempt to create a monopoly will result in a social cost — namely, the resources spent by the aspiring monopolist in its attempt. However, in this case the conduct is self-detering: the aspiring monopolist itself bears the full social cost of its conduct. Since it is the only “victim” of the failed attempt, no externally imposed sanction is necessary. The advocates of the Optimal Deterrence Model generally argue that failed attempts should go unpunished.¹²⁴

To be sure, this argument has some weaknesses — principally, it seems to overlook the fact that, according to the Optimal Deterrence Model, *general* deterrence is the goal of antitrust policy. The fact that the social cost of a particular failed attempt is zero should not be particularly important. What is important to a deterrence-based enforcement scheme is how the intending violator feels *ex ante* about his plans, and *ex ante* it may not be clear whether an attempt to monopolize will succeed or fail. The point of deterrence-based antitrust policy is to discourage people from committing anticompetitive practices in the first place, and that decision must be made at a time when the prospect of success is less than one-hundred percent.

But more importantly, once the full social cost of monopoly — including *WL3* losses — is taken into account, the self-detering nature of failed attempts is no longer clear. First of all, failed attempts can impose large social costs. The aspiring monopolist may underestimate the tenacity or solvency of its rival. It may overestimate the extent of entry barriers in the market. It may misjudge the relevant market altogether and face massive consumer defections in response to its price increase.¹²⁵ As a result, its attempt to create a monopoly will fail, but the attempt itself can impose enormous losses on rivals who must spend resources defending themselves or make costly exits from the market in favor of other firms.

124. See, e.g., Easterbrook, *supra* note 2, at 101 (monopoly overcharge is the proper basis for damages); Landes, *supra* note 2, at 656 (“[T]he fine should equal the net harm to persons other than the offender.”).

125. For example, if a manufacturer of widgets should drive the only other widget manufacturer out of the market through predatory pricing, but the relevant market actually includes widgets plus gidgets, its later price increase will yield nothing but defections from widgets to gidgets.

As a basic premise, a firm will not undertake a costly attempt to monopolize unless it has made some kind of calculation that the attempt will likely succeed. That is, *ex ante*, the profitability of the monopoly discounted by the probability of failure or the likelihood of detection and suit makes the conduct appear profitable. *Ex post*, the guess turns out to be wrong. In such cases, recognizing a cause of action for failed attempts increases the cost of making them.

Once again, there may be a problem of false positives.¹²⁶ Courts may be more likely to identify conduct wrongly as anticompetitive when a firm fails to create a monopoly than when it succeeds. But this proposition is not self-evident and has never been proved. Just as both competitive and anticompetitive conduct can create monopolies, both competitive and anticompetitive conduct can fail. In some cases, of course, monopoly in a given market was never plausible to begin with, and the failed attempt is simply further evidence of that fact. But in the relevant range — where conduct, measured *ex ante*, could reasonably be predicted to yield a monopoly — there is no reason to believe that courts will be better at determining whether successful conduct was anticompetitive than they are at determining whether unsuccessful conduct was anticompetitive. This suggests that courts should not dismiss a complaint simply because a particular practice failed to produce a monopoly, but should instead take very seriously questions about the plausibility of monopoly in a particular market.

C. Damage Measurement for WL3 Losses

Clayton Act section 4 provides that the victim of an antitrust violation may “recover threefold the damages by him sustained.”¹²⁷ The statute makes no distinction between purely private losses (such as those that might result from a wealth transfer) and private losses that coincide with losses to society in general. Congress knew little or nothing of such distinctions, either in 1890 when it passed section 4’s predecessor, section 7 of the Sherman Act,¹²⁸ or in 1914, when it enacted the Clayton Act itself.

Not all the losses suffered by competitors in antitrust cases reflect net welfare losses. More importantly, not all the claimed losses are real losses at all. While competitor damage actions for antitrust violations should continue to be permitted, the basis for damages should be

126. See *supra* note 121.

127. Clayton Act § 4, 15 U.S.C. § 15 (1982) (original version at ch. 323, § 4, 35 Stat. 730, 731 (1914)).

128. Sherman Act, § 7, ch. 647, 26 Stat. 209, 210 (1890) (repealed by Act of July 7, 1955, ch. 283, 69 Stat. 283).

reexamined in order better to account for the societal costs of antitrust violations.

1. *Loss of Investment*

The clearest case for competitor damage recovery is the competitor's net loss of investment — *i.e.*, investment in research and development or in manufacturing or distribution facilities that have been wasted and cannot be recovered as a result of an antitrust violation. The *Indian Head* case¹²⁹ is a good illustration. Suppose that a competitor develops at great expense a superior technology. The dominant firm in the industry, seeing that the new technology threatens its market position and profits, manages to convince a standard-setting association or government regulator to close the market to the innovator's technology. The innovator suffers (a) the loss of its investment in developing the technology; and (b) the loss of whatever profits the new technology would have yielded during the period that the market remains closed. Ordinarily a court would not want to award both of these losses to the plaintiff-innovator, for they are cumulative. That is, if the technology had been marketed as planned, the plaintiff's gross profits would have been reduced by costs, including its investment in research and development. To award the plaintiff both its lost investment and its lost profits would effectively treat it as if it had no costs, giving it more than it would have gotten absent the antitrust violation. In such cases, a firm that can establish its lost profits in a convincing way should be able to recover only those lost profits, before trebling; a firm that cannot establish its lost profits should be able to recover only its lost investment, before trebling.

2. *Lost Profits Generally*

Competitor claims for lost profits often provide opportunities for excessive damage awards. As noted above, an award for both lost investment and lost profits would represent double-counting. Forced to choose between a recovery based on lost profits or lost investment, there may well be reason to prefer the latter. Loss of investment will almost always be easier to calculate. In most antitrust cases where lost profits are used as a basis for damages, the experts engage in the rankest speculation. For example, under the "yardstick" method sometimes used to estimate lost profits the plaintiff is permitted to identify a different firm, often in a different location, that is presumed

129. *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 108 S. Ct. 1931 (1988); see *supra* notes 46-47 and accompanying text.

to be like the plaintiff's firm in as many respects as possible but for the antitrust violation. The plaintiff then argues that this "yardstick" firm's profit-and-loss statement is what the plaintiff's profit-and-loss statement would have looked like but for the defendant's actions. Of course, in many businesses some firms do very well and others do very badly for reasons unrelated to the antitrust laws, and there may be a great deal of dispute over a suitable "yardstick." More importantly, however, the determinants of firm profitability are both stochastic, or somewhat random, and extremely complex.¹³⁰ There are no two identical firms in two different cities. Even two McDonald's franchises in identical buildings and traffic areas, and with equally capable management, can show widely different rates of profitability. Assuming that one firm's profits will reflect the damages suffered by a distant victim of an antitrust violation is, therefore, distinctly problematic.¹³¹ The "before-and-after" method, which attempts to reconstruct lost profits during the violation period by comparing the plaintiff's profits before the violation began and after it ended, poses similar difficulties.¹³² Equally speculative is the "market share" method, which attempts to determine what the plaintiff's market share would have been had the plaintiff not been victimized by the defendant's antitrust violation.¹³³

130. See F. SCHERER, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* 145-50 (2d ed. 1980).

131. See, e.g., *Home Placement Serv., Inc. v. Providence Journal Co.*, 819 F.2d 1199 (1st Cir. 1987) (rejecting a particular "yardstick" as too speculative). See also *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251 (1946), which originally approved the "yardstick" method. On the yardstick method generally, see E. TIMBERLAKE, *FEDERAL TREBLE DAMAGE ANTITRUST ACTIONS* ch. 21 (1965); Goetz, *The Basic Rules of Antitrust Damages*, 49 ABA ANTITRUST L.J. 125 (1980); Hoyt, Dahl & Gibson, *Comprehensive Models for Assessing Lost Profits to Antitrust Plaintiffs*, 60 MINN. L. REV. 1233 (1976); Parker, *Measuring Damages in Federal Treble Damages Actions*, 17 ANTITRUST BULL. 497 (1972).

132. See *Graphic Prods. Distrib. v. Itek Corp.*, 717 F.2d 1560 (11th Cir. 1983):

Proof of the diminution in the going concern value of a business is ascertainable by comparing the fair market value of the business before and after the antitrust violation. Testimony of business appraisal experts as to what a hypothetical willing buyer would pay a hypothetical willing seller on the open market would be one method of establishing loss in going concern value.

717 F.2d at 1580 n.37 (citation omitted). The going concern value of a business is generally a function of its anticipated profitability.

133. As described by one recent court, the market share theory "involves an estimation of the market share the plaintiff would have had but for the defendant's unlawful conduct. Based on the market size and an estimate of plaintiff's likely profit margin, the total profits the plaintiff would have earned if the estimated market share had been achieved are determined." *Consolidated Gas Co. of Fla. v. City Gas Co. of Fla.*, 665 F. Supp. 1493, 1543-44 (S.D. Fla. 1987). In *General Leaseways, Inc. v. National Truck Leasing Assn.*, 830 F.2d 716, 726 (7th Cir. 1987), the court relied on an accountant's projection of the market share that the plaintiff would have achieved had it not been subjected to illegal restrictions. The accountant did this by comparing market shares of Avis dealers in unrestricted markets (where the defendant Avis owned the dealerships) and those in the plaintiff's markets, which were subject to the restrictions. See also *Metrix Warehouse, Inc. v. Daimler-Benz Aktiengesellschaft*, 828 F.2d 1033 (4th Cir. 1987) (apparently accepting market share theory in principle, but rejecting particular application).

Secondly, and more importantly, profits in most cases are not what the antitrust plaintiff really "lost." What the plaintiff lost was a particular *opportunity* to make profits. Profit-making opportunities are a function of a firm's assets — its buildings, equipment, trademarks, personality, management skills. An antitrust violation may deprive a plaintiff of some of these things, but almost never all of them. If the assets taken were restored, the opportunity to make profits would be restored as well.

Our current system of estimating damages based on lost profits overcompensates to the extent that antitrust violations never deprive a plaintiff of everything that has made his or her investments profitable. Even the franchisee of a product whose trademarks are owned by the franchisor and who rents the franchisor's building does not lose everything when the franchise is terminated. The franchisee retains her management skills, a name in the community, willingness to work, and perhaps even the loyalty of some employees. The franchisee's loss is the cost of reconstructing a position to earn similar profits.¹³⁴

Loss of unrecoverable investment is inherently a better basis for estimating antitrust damages than lost profits. Not only is it easier to measure than lost profits, but it provides a better estimate of what the plaintiff really lost. Finally, it is more consistent with a model that tries to apply sanctions in such a way as to minimize the true social cost of monopoly in society.

CONCLUSION

Until now, antitrust scholars have almost unanimously agreed that a model of antitrust enforcement based exclusively on allocative efficiency would result in substantially less enforcement than we have had in the past, or even than we now have. This proposition may be true, but it is not self-evident and needs to be proven. To date it has not been proven because those who have argued it have based their ideas about allocative efficiency on a mistaken estimate of the social cost of the kind of monopolizing activity that antitrust is concerned about. When the full social cost of monopoly is considered, much broader antitrust enforcement seems appropriate, including damage actions by

134. For example, see *Pierce v. Ramsey Winch Co.*, 753 F.2d 416 (5th Cir. 1985), a resale price maintenance case involving termination of the plaintiff's distributorship of the defendant's winches. The plaintiff continued in business selling a different brand of winches. The court approved an award of lost profits based on the differences between the number of Ramsey winches that would have been sold and the number of substitute winches that were actually sold. See also *Lehrman v. Gulf Oil Corp.*, 500 F.2d 659, 663-64 (5th Cir. 1974) (damage award based on future profits), *cert. denied*, 420 U.S. 929 (1975).

competitors and potential competitors — groups that rightfully fall among antitrust's protected classes.

APPENDIX

CONGRESS' VIEW OF THE SHERMAN ACT'S PROTECTED CLASSES

In preparing this Appendix, I have simply quoted or summarized every reference in the legislative history of the Sherman Act that discusses the nature of the injuries Congress had on its collective mind in enacting the legislation. I have arranged these under three headings: (1) statements that clearly show a concern about injury to consumers; (2) statements that clearly show a concern about injury to competitors; (3) statements that show a concern about injury, but are ultimately ambiguous about the nature of the injury or the identity of the victim. Within each category, the statements are listed chronologically.

I. CONCERN WITH CONSUMER INJURIES

The following statements from the Act's legislative history reflect concern with consumer injuries,¹³⁵ resulting from both wealth transfers (Lande Model)¹³⁶ and allocative inefficiency (Bork Model).¹³⁷

— A Resolution reported by the House Committee on Manufactures asserted that "certain individuals and corporations . . . have combined for the purpose of controlling or curtailing the production or supply [of some articles], and thereby increasing their price to the people of the country."¹³⁸

— A Senate Resolution directed inquiry into practices that "tend to foster monopoly or to artificially advance the cost to the consumer of necessary articles."¹³⁹

— Senator Sherman's original bill was designed to condemn combinations "made with a view, or which tend, to prevent full and free competition . . . in the production, manufacture or sale of articles . . . or which tend to advance the cost to the consumer of any of such articles."¹⁴⁰ None of this language appeared in the bill that was finally passed as the Sherman Act.

135. "Consumer" injuries is defined here to include (1) high prices to consumers that result from a monopoly or sellers' cartel, and (2) low prices to producers of inputs that might result from a monopsonist or buyers' cartel. Farmers, one important protected class of the Sherman Act, were generally seen as experiencing injuries of the second type.

136. See Lande, *Wealth Transfers*, *supra* note 61.

137. See R. BORK, *supra* note 24; Bork, *Legislative Intent*, *supra* note 57.

138. 19 CONG. REC. 719 (1888).

139. *Id.* at 6041.

140. S. 3445, 50th Cong., 1st Sess. 1 (Aug. 14, 1888).

— Senator Jones noted that “[t]he sugar trust has its ‘long, felonious fingers’ at this moment in every man’s pocket . . . , deftly extracting with the same audacity the pennies from the pockets of the poor and the dollars from the pockets of the rich.”¹⁴¹ If Senator Jones was referring to high sugar prices he was wrong; the price of sugar was at an all-time low.¹⁴² Possibly he was referring to competitors rather than consumers.

— Senator Sherman stated that the bill would not apply to a farmers’ boycott of trust products, but would apply to combinations formed “to advance the price of the necessities of life.”¹⁴³ Did Sherman really mean to limit his bill to “necessaries of life”? That was generally the position of the common law.¹⁴⁴

— Senator Turpie defined “trust” as a combination formed with the intention of holding and selling [commodities] at an enhanced price, by suppressing or limiting the supply and by other devices, so that the price of such trust commodity shall depend merely upon the agreement made about it by those in the combination, without reference to the cost of its production.¹⁴⁵

— Senator George stated that he was anxious for a bill against the large corporations and wealthy individuals who “dictate to the people of this country what they shall pay when they purchase, and what they shall receive when they sell.”¹⁴⁶ He then objected that the proposed bill would condemn “defensive” as well as offensive combinations — e.g., an agreement among farmers not to buy jute bagging from the jute-bagging trust.¹⁴⁷

— Senator Sherman declared that “[i]t is sometimes said of these combinations that they reduce prices to the consumer by better methods of production, but all experience shows that this saving of cost goes to the pockets of the producer.”¹⁴⁸ This statement is consistent with the proposition that Congress intended to prevent “unjust” wealth transfers to monopolists (Lande model), rather than consumer welfare, neoclassically defined (Bork model).¹⁴⁹

— Senator Sherman quoted an earlier statement from Senator George that the trusts “increase beyond reason the cost of the neces-

141. 20 CONG. REC. 1457-58 (1889).

142. See *supra* notes 98-100 and accompanying text.

143. 20 CONG. REC. 1458 (1889).

144. See Hovenkamp, *supra* note 55.

145. 21 CONG. REC. 137 (1889).

146. 20 CONG. REC. 1458 (1889).

147. *Id.*

148. 21 CONG. REC. 2460 (1890).

149. See Lande, *Wealth Transfers*, *supra* note 61; R. BORK, *supra* note 24.

saries of life and business.”¹⁵⁰

— Senator Vest inquired whether the steel-makers created their combination in order to raise the price of steel.¹⁵¹

— Senator Teller stated:

When [Standard Oil interferes] with somebody who has sunk a well in Ohio and they run down the price of oil until they shut him up, he may have his remedy against them. But that is not what we are complaining of. We are complaining that . . . Standard Oil Company has a tendency to reduce and destroy competition, and thereby, by destroying competition, to put up improperly the price of oil.¹⁵²

— Senator Stewart argued that, although the beef trust raised prices, the remedy was for the farmers to have a countervailing combination to raise the price of cattle.¹⁵³ He was apparently claiming that the beef trust simultaneously (1) raised resale beef prices and (2) lowered the price of cattle it purchased. How a cattle producers’ cartel would lower the final price of beef, Senator Stewart did not explain.

— Senator Spooner declared that the beef trust had resulted in increased consumer prices, and that the purpose of the sugar trusts was to do so as well.¹⁵⁴

— Senator Reagan argued that the cottonseed-oil trust simultaneously drove competitors out of business, raised the price of refined cottonseed oil, and lowered the price it paid for the raw product.¹⁵⁵

— Senator Morgan inquired whether there were combinations of doctors or lawyers for raising prices.¹⁵⁶

— Representatives Culberson and Butterworth appear to have agreed that maximum resale price maintenance would be illegal under the Act if its purpose was to drive out competing dealers.¹⁵⁷

— Representative Henderson opined that the beef trust had been able simultaneously to reduce the price it paid for cattle and raise the price it charged for beef.¹⁵⁸

— Representative Taylor opined that the beef trust simultaneously harmed both farmers and consumers.¹⁵⁹

— Representative Heard opined that the beef trust “prostrated the

150. 21 CONG. REC. 2461 (1890).

151. *Id.* at 2472.

152. *Id.* at 2571.

153. *Id.* at 2606.

154. *Id.* at 2640.

155. *Id.* at 2645.

156. *Id.* at 2726.

157. *See id.* at 4090.

158. *Id.* at 4091.

159. *Id.* at 4098.

live-stock interest of the West" by paying farmers low prices for beef.¹⁶⁰

— Representative Fithian opined that trusts "enhance the price of commodities to the people beyond an honest profit."¹⁶¹

— Representative Moore noted that trusts "put up the price of necessities."¹⁶²

II. CONCERN WITH COMPETITOR INJURIES

— Senator Hoar, a principal author of the final bill known as the Sherman Act, moved to amend Senator Sherman's bill to read:

If one of the purposes of any such arrangement, contract, agreement, trust, or combination shall be to compel any person, partnership, or corporation to become a party thereto, or to cease from doing any lawful business, or to sell and dispose of any lawful business, . . . the person, partnership, or corporation injured thereby may sue¹⁶³

This language, however, was never passed.

— Senator Saulsbury believed Hoar's proposed amendment should be strengthened to cover not merely situations in which people are "compelled" to give up their businesses, but even to situations in which people are "induced by offers of stock," presumably in the trust combination, to give up their businesses.¹⁶⁴ Hoar then responded that Saulsbury's proposal "would apply not only to a harmful but to a meritorious arrangement."¹⁶⁵ Saulsbury's proposal did not pass.

— Senator Sherman stated:

I am not opposed to combinations in and of themselves; I do not care how much men combine for proper objects; but when they combine with a purpose to prevent competition, so that if a humble man starts a business in opposition to them, solitary and alone, in Ohio or anywhere else, they will crowd him down and they will sell their product at a loss or give it away in order to prevent competition, . . . then it is the duty of the courts to intervene and prevent it¹⁶⁶

— Senator George stated:

It is a sad thought to the philanthropist that the present system of production and of exchange is having that tendency which is sure at some not very distant day to crush out all small men, all small capitalists, all small enterprises. This is being done now. We find everywhere over our land the wrecks of small, independent enterprises thrown in our path-

160. *Id.* at 4101.

161. *Id.* at 4102.

162. *Id.* at 5953.

163. 20 CONG. REC. 1167 (1889).

164. *Id.*

165. *Id.*

166. 21 CONG. REC. 2569 (1890).

way. So now the American Congress and the American people are brought face to face with this sad, this great problem: Is production, is trade, to be taken away from the great mass of the people and concentrated in the hands of a few men who, I am obliged to add, by the policies pursued by our Government, have been enabled to aggregate to themselves large, enormous fortunes?¹⁶⁷

— Senator Edmunds stated:

I am in favor of the scheme . . . directed to the breaking up of great monopolies which get hold of the whole of a particular business or production in the country and are enabled, therefore, to command everybody, laborer, consumer, producer, and everybody else, as the sugar trust and the oil trust, and whatever. Although for the time being the sugar trust has perhaps reduced the price of sugar, and the oil trust certainly has reduced the price of oil immensely, that does not alter the wrong of the principle of any trust; and that . . . is a phrase which covers every combination to get control of the life and the industry and the producing and the consuming classes of the country. I am in favor, most earnestly in favor, of doing everything that the Constitution of the United States has given Congress power to do, to repress and break up and destroy forever the monopolies of that character, because in the long run, however seductive they may appear in lowering prices to the consumer for the time being, all human experience and all human philosophy have proved that they are destructive of the public welfare and come to be tyrannies, grinding tyrannies. . . .¹⁶⁸

— Senator George stated that “[b]y the use of this organized force of wealth and money the small men engaged in competition with [the trusts] are crushed out, and that is the great evil at which all this legislation ought to be directed.”¹⁶⁹

— Representatives Culberson, Butterworth, and Burrows opined that resale price maintenance contracts were covered by the proposed Act because they prevent dealers from setting prices independently or penalize them if they do.¹⁷⁰

— Representative Bland argued that the beef trust compelled independent butchers to buy their beef from the trust rather than from independent dealers; if the butcher resisted, the trust set up a competing butcher shop and drove the independent butcher out of business.¹⁷¹

— Representative Mason argued:

Some say that the trusts have made products cheaper, have reduced prices; but if the price of oil, for instance, were reduced to 1 cent a barrel it would not right the wrong done to the people of this country by the

167. *Id.* at 2598.

168. *Id.* at 2726.

169. 21 CONG. REC. 3147 (1890).

170. *Id.* at 4089-90.

171. *Id.* at 4099.

"trusts" which have destroyed legitimate competition and driven honest men from legitimate business enterprises.¹⁷²

III. AMBIGUOUS REFERENCES

— Senator Reagan's original proposed bill banned "trusts," which were defined as, among other things, combinations carried out "[t]o limit, to reduce, or to increase the production or prices of merchandise or commodities," or "[t]o prevent competition in the manufacture, making, sale, or purchase of merchandise or commodities," or "[t]o create a monopoly."¹⁷³ This language was never passed.

— Senator Jones opined that the trusts have "been allowed to grow and fatten upon the public, . . . preying upon every industry, and by their unholy combinations robbing their victims, the general public."¹⁷⁴ "Preying upon every industry" seems to refer to competitor injury; "robbing their victims" may refer to either competitors or consumers.

— Senator George denied that the purpose of combinations was to raise consumer prices. Rather, he argued, it was to play the market, "wholly for speculative purposes — intended alone to squeeze those who are 'short,' as the saying is. It is true they do, as an incident, sometimes affect, while they last, the price paid by the consumer; but that is not the intent . . ."¹⁷⁵ Senator George then went on to say that in the unusual case where the combination really did raise prices, consumers themselves and not middlemen would be injured, for even though the middlemen paid more, they would pass on their higher prices. However, consumer suits would not work as a practical matter. "[F]ew, if any, of such suits will ever be instituted, and none will ever be successful."¹⁷⁶ He concluded that the bill was an "abortion," and, in any event, unconstitutional.¹⁷⁷

— Senator Sherman requested the Chief Clerk to read his second amended bill, which gave a private antitrust action to "any person or corporation injured or damnified by such arrangement." The bill did not describe the nature of the injury.¹⁷⁸

172. *Id.* at 4100.

173. 19 CONG. REC. 7512 (1888).

174. 20 CONG. REC. 1457 (1889).

175. 21 CONG. REC. 1767 (1890).

176. *Id.* at 1758.

177. *Id.* at 1768.

178. *Id.* at 2455. Senator Sherman added that the bill did not "seek to cripple combinations of capital and labor, the formation of partnerships or of corporations, but only to prevent and control combinations made with a view to prevent competition, or for the restraint of trade, or to increase the profits of the producer at the cost of the consumer." *Id.* at 2457.

— Senator Sherman argued that his proposed bill

does not in the least affect combinations in aid of production where there is free and fair competition. It is the right of every man to work, labor, and produce in any lawful vocation and to transport his production on equal terms and conditions and under like circumstances. This is industrial liberty and lies at the foundation of the equality of all rights and privileges.¹⁷⁹

Later, he added:

The sole object of such a combination is to make competition impossible. It can control the market, raise or lower prices, as will best promote its selfish interests, reduce prices in a particular locality and break down competition and advance prices at will where competition does not exist. Its governing motive is to increase the profits of the parties composing it. The law of selfishness, uncontrolled by competition, compels it to disregard the interest of the consumer.¹⁸⁰

Senator Sherman concluded, "The point for us to consider is whether, on the whole, it is safe in this country to leave the production of property, the transportation of our whole country, to depend upon the will of a few men sitting at their council board in the city of New York" ¹⁸¹ The perceived evils appear to be bigness per se and absentee ownership.

— Senator Platt argued that the trusts were intended only to prevent ruinous competition and keep prices at a fair level. He stated that he was "sick of this idea that the lower the prices are the better for the country."¹⁸² Platt added:

The true theory of this matter is that prices should be just and reasonable and fair, that prices, no matter who is the producer or what the article, should be such as will render a fair return to all persons engaged in its production, a fair profit on capital, on labor and of everything else When the price of any commodity . . . is forced below that standard, the whole country suffers.¹⁸³

Then Platt concluded that the trust form of business was the exception rather than the rule; most business, he noted, was still carried on by firms of relatively small capital. Further, his experience with woolen mills was that their efforts to combine were merely to prevent losses.¹⁸⁴

— Senator George argued that consumer suits were not practical, for they would force consumers, whose individual injuries were small,

179. *Id.* at 2457.

180. *Id.*

181. *Id.* at 2570.

182. *Id.* at 2729-30.

183. *Id.* at 2729.

184. *Id.* at 2729-30.

to travel long distances to find a forum with jurisdiction over the defendants. "[H]ow can the small farmer thus injured from \$10 to \$50, with his witnesses, go to a distant town or city, employ a lawyer, and sue one of these great trusts in a United States court?"¹⁸⁵ Finally, he concluded:

I predict — and I put it on the record now as my deliberate judgment — that not one suit will ever be brought under this seventh section by any person who is simply damaged in his character as consumer. . . . I do not propose silently to sit here and be a silent partner . . . to the enactment of what I know to be, so far as a remedy to the real parties injured by these trusts is concerned, a sham, a snare, and a delusion.¹⁸⁶

— Representative Wilson stated that "it is one of the subtleties of the trust system that it can always have on hand a supply of corporations to be used as light cavalry to chase down the first competitor that dares to appear to contest the dominion of the trust over the home market."¹⁸⁷

— Representatives Culberson and Oates debated the anti-pooling provision of the Interstate Commerce Act. The debate led Representative Oates to suggest that the effect had been merely to force smaller railroads to merge and to ask whether it "resulted in accomplishing just the contrary to what was expected."¹⁸⁸ Representative Morse expressed the same opinion.¹⁸⁹

— Senator Stewart concluded that trusts, particularly the railroads, tended to reduce prices. The real problem, he said, was discrimination, or differential pricing, which was caused by competition.¹⁹⁰

— Representative Anderson disagreed with Stewart, and concluded that railroad combinations increased rates.¹⁹¹ This same debate, between the same members, was later repeated.¹⁹²

— Senator Vest asserted that railroad cartels were designed to increase rates rather than lower them.¹⁹³

— Senator Kerr objected to the fact that the sugar trust was profitable, but did not say why.¹⁹⁴

185. *Id.* at 3147-48.

186. *Id.* at 3150.

187. *Id.* at 4096.

188. *Id.* at 5951.

189. *Id.* at 5953.

190. *Id.* at 5956.

191. *Id.* at 5957.

192. *Id.* at 5959.

193. *Id.* at 6116.

194. *Id.* at 6313.