Tying Should Be Analyzed Under The Rule Of Reason

Donald J. Russell
Robbins, Russell, Englert, Orseck & Untereiner LLP
November 1, 2006

- For tying law, the easiest and the most important step for the antitrust agencies to take is to say publicly, clearly, frequently, and (at the first opportunity) to the Supreme Court: "Tying should be analyzed under the rule of reason."

- The Supreme Court has signaled clearly that it is ready to abandon the remaining vestiges of the "per se" rule against tying.

Jefferson Parish Hospital District No. 2 v. *Hyde*

466 U.S. 2 (1984)

District court ruled for defendant in tying case.

Court of Appeals reversed.

Supreme Court reversed the Court of Appeals, holding that the tying arrangement was not *per se* unlawful because defendant lacked the requisite market power in the tying product.

Jefferson Parish Hospital District No. 2 v. *Hyde*

Five Justices joined in the majority opinion by Justice Stevens:

"It is far too late in the history of our antitrust jurisprudence to question the proposition that certain tying arrangements pose an unacceptable risk of stifling competition and therefore are unreasonable 'per se.'"

Jefferson Parish Hospital District No. 2 v. *Hyde*

Two of the five justices in the majority joined a separate concurring opinion:

"Whatever merit the policy arguments against [the per se rule] might have, Congress, presumably aware of our decisions, has never changed the rule by amending the Act. In such circumstances, our practice usually has been to stand by a settled statutory interpretation."

Jefferson Parish Hospital District No. 2 v. *Hyde*

Four Justices joined a concurring opinion that said tying should be analyzed under the rule of reason:

"[T]ying doctrine incurs the costs of a rule of reason approach without achieving its benefits: the doctrine calls for the extensive and time-consuming economic analysis characteristic of the rule of reason, but then may be interpreted to prohibit arrangements that economic analysis would show to be beneficial."

"The legality of petitioners' conduct depends on its competitive consequences, not whether it can be labeled "tying." If the competitive consequences of this arrangement are not those to which the per se rule is addressed, then it should not be condemned irrespective of its label."

Jefferson Parish Hospital District No. 2 v. *Hyde*

Justice Stevens identified two competitive concerns with tying:

The defendant's "potentially inferior [tied] product may be insulated from competitive pressures."

Tying "can increase the social costs of market power [in the tying product] by facilitating price discrimination, thereby increasing monopoly profits over what they would be absent the tie."

Illinois Tool Works, Inc. v. *Independent Ink, Inc.*

District court ruled for the defendant in a tying case, because the plaintiff had not proved the requisite market power in the tying product.

Court of Appeals reversed, holding that a patent on the tying product creates a presumption of market power. The decision rested, in part, on Justice Stevens's observation in *Jefferson Parish* that "if the government has granted the seller a patent . . . it is fair to presume that the inability to buy the product elsewhere gives the seller market power."

Supreme Court unanimously reversed, holding (in an opinion written by Justice Stevens) that the plaintiff must prove market power "in all cases involving a tying arrangement."

Illinois Tool Works, Inc. v. *Independent Ink, Inc.*

Why the change between *Jefferson Parish* and *Independent Ink*?

Court easily could have distinguished its old patent and copyright cases or simply treated language from those cases as dicta. See Kevin D. McDonald, *There's No Tying In Baseball*, Antitrust Source (September 2005).

Instead, it offered four reasons for "overruling" those prior decisions. Those reasons strongly suggest that the Court is prepared to overrule prior decisions characterizing tying as per se unlawful.

Why The Change?

Reason # 1: The presumption that a patent confers market power is "a vestige of the Court's historical distrust of tying arrangements, that we address squarely today."

- "Over the years, however, this Court's strong disapproval of tying arrangements has substantially diminished."
- "The [*Fortner*] dissenters' view that tying arrangements may well be procompetitive ultimately prevailed."
- "The assumption that 'tying arrangements serve hardly any purpose beyond the suppression of competition,' rejected in *Fortner II*, has not been endorsed in any opinion since."

Why The Change?

What about the concern that tying will lead to price discrimination?

"While price discrimination may provide evidence of market power . . . it is generally recognized that it also occurs in fully competitive markets."

Why The Change?

Reason # 2: Scholarly consensus

- "Our review is informed by extensive scholarly comment."
- "[T]he vast majority of academic literature recognizes that a patent does not necessarily confer market power."
- There is a "virtual consensus" among economists

Why The Change?

Reason # 3: Congressional action

- "[A]t the same time that our antitrust jurisprudence continued to rely on the assumption that 'tying arrangements generally serve no legitimate business purpose,' Congress began chipping away at the assumption."

- "After considering the congressional judgment reflected in the 1988 amendment" we conclude that the standards governing tying of unpatented products should also govern tying with patented products. "[S]ome such [tying] arrangements are still unlawful, such as those that are the product of a true monopoly or a marketwide conspiracy."

- But the Court has "made clear" that it can reexamine its antitrust precedents even if there has been no Congressional action. "[S]uch an invitation [by Congress] is not necessary with respect to cases arising under the Sherman Act."

Why The Change?

Reason # 4: The Government's Position

- "Our review is informed by . . . a change in position by the administrative agencies charged with enforcement of the antitrust laws."
- "Our opinion in *International Salt* clearly shows that we accepted the Government's invitation."
- "[T]he enforcement agencies [have now] reject[ed] the position the Government took" in *International Salt*.
- "While [the government's] choice is not binding on the Court, it would be unusual for the Judiciary to replace the normal rule of lenity . . . with a rule of severity for a special category of antitrust cases."

Why The Change?

To Sum Up:

"Congress, the antitrust enforcement agencies, and most economists have all reached th[is] conclusion. . . Today, we reach the same conclusion."

Independent Ink Clearly Signals The Court's Readiness To Abandon "Per Se" Treatment Of Tying

Is this reading too much into the *Independent Ink* decision?

Consider the questions and comments by Justices during oral argument.

Justice Stevens:

- "I think there's a good argument that if a patent is really a good patent, it doesn't really matter whether the patentee charges a very high royalty or gets a – reduces the royalty and gets profits out of the [tying] product."

- "Is the rule sound that if it is monopoly in the [tying] product, that there is an antitrust problem?"

- "I'm asking sort of an economic question . . . If your position is all the economists say this is a lot of nonsense, I think maybe it's nonsense even if there's a monopoly in the tying product is what I'm suggesting."

- "[I]t's a very interesting question as to whether it makes any difference whether the monopolist who happened to have a patent just charges high prices for product A or decides to charge a little less for product A and make hay out of product B.

- "It doesn't seem to me it makes any difference whether General Motors has a monopoly or not when it wants to sell, you know, two components as part of the same package."

Chief Justice Roberts:

- "Much of the economic literature . . . sort of sweeps aside the particular question today because it rejects the notion of tying as a problem in the first place."

Justice Breyer:

- A requirements tie "would be one of the strongest cases for not having a per se rule because if, in fact, you have a justification, in terms of sharing risk with a new product, that would be one of the cases where you would expect to find a tie."

- "[A]t the bottom, I think there are cases where tying is justified. But the way to attack that would be to say here, here, and here it's justified and that would have to do with the tied product. It would abolish the per se rule, making it into a semi-per se rule."

- "I'm not certain whether attacking the [market power] screen and insisting on a higher standard of proof is better than nothing or whether you should say, well, leave the screen alone and let's deal with the tied product on the merits. That I think is what Justice Stevens was getting at too."

- "Price discrimination, I gather, sometime good, sometimes not. . . And so I think most economists – in fact everyone I've read agrees with that."

Justice Scalia:

- "We're not even sure, are we, that – that you can extend, assuming that there is market power in the patent – we're not really sure that you can extend it through tying. I mean, there's – there's dispute among the economists even on that question."

Roadmap To A Supreme Court Decision That The Rule Of Reason Governs Tying Arrangements

- ☑ Supreme Court recognition that tying is often procompetitive
- ☑ Scholarly consensus
- ☑ Congressional action (helpful but not required)
- ☐ Support from antitrust enforcement agencies

From The Argument In *Independent Ink*

MR. HUNGAR: [I]s it rational to presume market power from the existence of a patent is quite separate and distinct in our view from the question whether it's rational to have a per se tying rule when there is market power. They're completely distinct.

CHIEF JUSTICE ROBERTS: And – and what is the government's position on the latter question?

MR. HUNGAR: Well, Justice O'Connor made persuasive points in her concurring opinion in Jefferson Parish . . . We have not taken a position on that question in this case.