No. 13-1297

United States Court of Appeals
For The Eighth Circuit

D&G, Inc., doing business as Gary's Foods,

Plaintiff-Appellant,

v.

SuperValu Inc. and C&S Wholesale Grocers, Inc.,

Defendants-Appellees.

On Appeal from the United States District Court
for the District of Minnesota

**BRIEF OF AMICUS CURIAE
THE AMERICAN ANTITRUST INSTITUTE IN SUPPORT OF
NEITHER PARTY AND SEEKING CLARIFICATION OF THE LAW
REGARDLESS OF AFFIRMANCE OR REVERSAL**

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Fed. R. App. P. 26.1, the American Antitrust Institute states that it is a nonprofit corporation and, as such, no entity has any ownership interest in it.

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INTEREST OF AMICUS CURIAE

The American Antitrust Institute (AAI) is an independent and nonprofit education, research, and advocacy organization devoted to advancing the role of competition in the economy, protecting consumers, and sustaining the vitality of the antitrust laws. AAI is managed by its Board of Directors, with the guidance of an Advisory Board that consists of over 130 prominent antitrust lawyers, law professors, economists, and business leaders.[1] Pursuant to Fed. R. App. P. 29(a), amicus states that all parties have consented to the filing of this brief by AAI. AAI submits that the goals of U.S. competition policy would be seriously undermined if this Court does not clarify that (1) naked, horizontal customer allocation remains in the per se category of Sherman Act offenses, and (2) any form of horizontal market allocation must be found ancillary to a legitimate and competitive business association before the rule of reason will be substituted for the per se rule.

[1] The Board of Directors of AAI alone has approved this filing for AAI; individual views of members of the Advisory Board may differ from AAI's positions. Pursuant to Fed. R. App. P. 29(c)(5), amicus states that no counsel for a party has authored this brief in whole or in part, and no party, party's counsel, or any other person or entity – other than AAI or its counsel – has contributed money that was intended to fund preparing or submitting this brief. Certain members of AAI's Advisory Board represent or have advised both appellants and appellee SuperValu Inc., but played no role in the Directors' deliberations or the drafting of the brief.

SUMMARY OF ARGUMENT

The district court's analysis of Plaintiffs' per se claims is contrary to well established antitrust case law and should be disavowed by this Court. The district court misstated the law when it suggested that non-exclusivity is a basis for removing otherwise naked, horizontal customer allocation agreements from the per se category of Sherman Act offenses. The district court also erred in applying the "full blown" rule of reason to Plaintiffs' customer allocation claims without deciding whether the Defendants' restraint was ancillary rather than naked.

If this Court's de novo review of the record reveals that Defendants' bilateral non-compete agreement was ancillary to their asset exchange, it should affirm the district court's decision to apply the rule of reason to Plaintiffs' customer allocation claims, but correct the district court's analysis and its statement of the law. If, however, this Court finds that Defendants' bilateral non-compete agreement was a naked, horizontal division of customers, it should reverse and apply the per se rule.[2] Amicus writes to ask this Court to clarify

[2] Amicus notes that Plaintiffs brought claims of geographic market allocation in addition to customer allocation, *In re Wholesale Grocery Prod. Antitrust Litig.*, Civ. Action No. 0:09-md-02090, 2013 U.S. Dist. LEXIS 4584, 30 (D. Minn. Jan. 11, 2013). The district court suggested that Plaintiffs sought inferences of a geographic market allocation agreement drawn from, among other things, circumstantial evidence the court characterized as "AEA negotiations," *id*. at 31 (describing, for example, Plaintiffs' evidence purporting to show that both parties intended to close all of the distribution centers they were exchanging). Because certain relevant facts may be sealed under a protective order, amicus takes no

Eighth Circuit law and ensure (1) naked, horizontal customer allocation remains in the per se category of Sherman Act offenses, and (2) any form of horizontal market allocation must be found ancillary to a legitimate and competitive business association before the rule of reason will be substituted for the per se rule.

Plaintiffs alleged that Defendants used a sham asset exchange to achieve "a naked agreement between [horizontal] competitors not to compete for over a thousand customers in New England and the Midwest." Second Consolidated Am. Class Action Compl. ¶ 2 (Plaintiff-Appellant's Appendix at 193). A horizontal customer allocation agreement is per se illegal under the Sherman Act, *Cont'l Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 708 (1962), unless it is "ancillary to the legitimate and competitive purposes of [a] business association," *Texaco Inc. v. Dagher*, 547 U.S. 1, 7 (2006). "The Court has long held that certain ancillary restraints of trade may be defended as reasonable." *Business Elec. Corp. v. Sharp Elec. Corp.*, 485 U.S. 717, 737 (1988) (Stevens, J., dissenting). But "'[t]he contract must be one in which there is a main purpose, to which the

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position on the adequacy of the inferences drawn by the district court with respect to Plaintiffs' circumstantial evidence of geographic market allocation. However, to the degree the court held that geographic market allocation does not fall into the per se category of offenses as a matter of law, or that geographic market allocation need not be deemed vertical or ancillary before the rule of reason is properly applied, it has compounded the error discussed in this brief. Amicus also takes no position on whether the error discussed in this brief ultimately requires reversal, which may depend on facts bearing upon the ancillarity determination that are likewise sealed.

covenant in restraint of trade is merely ancillary.'" *Id.* at 738 (quoting *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 282 (6th Cir. 1898) (Taft, J.), *aff'd* 175 U.S. 211 (1899)). "'The main purpose of the contract suggests the measure of protection needed . . . .'" *Id.* (quoting same). "'[W]here the sole object of both parties in making the contract . . . is merely to restrain competition, and enhance or maintain prices, it would seem that there was nothing to justify or excuse the restraint, that it would necessarily have a tendency to monopoly, and therefore would be void.'" *Id.* (quoting same).

The district court made two crucial mistakes in its analysis. First, the court plainly misstated the law when it suggested that naked, horizontal customer allocation does not fit into an established category of per se offenses. *In re Wholesale Grocery Prod. Antitrust Litig.*, Civ. Action No. 0:09-md-02090, 2013 U.S. Dist. LEXIS 4584, 30 (D. Minn. Jan. 11, 2013) (hereinafter "Jan. 2013 Order"). Specifically, the court held that Plaintiffs did not allege a per se offense because they did not allege an "exclusive market allocation." *Id.* However, every authority known to amicus has held that customer allocation is a classic per se offense, notwithstanding that it is not "exclusive" insofar as it does not eliminate all competition between the parties. *See infra* Section I.B. That customer allocation is distinguishable from other forms of market allocation in this sense has been universally recognized as irrelevant. See *infra* Sections I.A, I.B.

An exception limiting the per se category of market allocation offenses to "exclusive" market allocation is not only unprecedented, it is economically illogical and would effectively swallow the per se rule. If courts were to differentiate between "exclusive" and non-exclusive market allocation agreements in applying the per se rule, they would not be able to determine the proper liability standard for *either* type of agreement without first defining the relevant market. In other words, a court would have to identify the boundaries of the hypothetical relevant market and determine whether this market is "exclusively" allocated before it could decide whether the per se rule applies.

Because market definition is a tool for measuring, rather than balancing, a restraint's likely competitive effects, it is erroneous to assign a liability standard based on market definition considerations. *See infra* Section I.C. Moreover, eliminating the cost, complexity, and delay associated with defining relevant antitrust markets is one of the primary purposes and effects of the per se rule. *Id*. By relying on a market definition inquiry to assess the applicability of the per se rule, the district court's analysis would sacrifice a key goal of the rule. The rule would be left only nominally available to plaintiffs and government enforcers. In theory the per se rule would continue to apply to "exclusive" market allocation, but in practice it would be eliminated for all forms of horizontal market allocation

because the exclusivity determination inevitably would demand that relevant antitrust markets be defined and analyzed.

Second, the district court erred when it invoked the ancillary restraints doctrine without resolving the question of whether the Defendants' non-compete agreement was an ancillary restraint. If the court had inquired and concluded that the Defendants' non-compete agreement was an ancillary restraint, its application of the rule of reason would be unexceptional. However, in its July 2010 order, the court concluded that "whether the non-compete agreements were ancillary to [the Asset Exchange Agreement (AEA)] in the sense that they were necessary to protect the value of the assets being exchanged and realize economic integration cannot be resolved on summary judgment." *In re Wholesale Grocery Prod. Antitrust Litig.*, 722 F. Supp. 2d 1079, 1094 (D. Minn. 2010) (hereinafter "July 2010 Order"). Nonetheless, the court stated that "[i]n the context of a transfer of business assets accompanied by a non-compete agreement, 'a per se approach does not seem warranted unless the restriction has no integrative prospects whatsoever.'" *Id.* at 1094 (quoting 13 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 2134e (3d ed. 2007)). It further noted that the Defendants *might be able* to show efficiencies from the AEA and that under these circumstances "executing the non-compete provisions [would] seem reasonably necessary to realize the procompetitive benefit of increased efficiency." *Id.*

An otherwise per se restraint should not be treated as ancillary and evaluated under the rule of reason solely on the basis that the underlying transaction has "integrative prospects." July 2010 Order at 1094. This treatment assumes away the core of the ancillary restraints inquiry, which asks courts to examine the fundamental purpose of a transaction. See *Business Elec. Corp.*, 485 U.S. at 737 (quoting *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 282 (6th Cir. 1898) (Taft, J.), *aff'd* 175 U.S. 211 (1899)). The district court's approach would encourage creative circumvention of the per se rule and be highly damaging to consumers. Because non-compete agreements can be used to allocate markets between horizontal competitors, Defendants should have the burden of showing that horizontal non-compete agreements are ancillary to a larger economic activity, warranting rule of reason analysis.

Horizontal market allocation is extremely harmful to consumers and should remain in the per se category of antitrust offenses. Like price fixing agreements, market allocation agreements eliminate price competition between competitors, but they go further and eliminate non-price competition as well. Market allocation agreements also may be easier to establish, easier to police (when participants would otherwise cheat to the benefit of consumers), and more durable than price fixing agreements. For consumers, the result of market allocation may be not only higher prices but also diminished quality and reduced innovation. Application of

the rule of reason to non-ancillary horizontal market allocation schemes would badly under-deter an overwhelmingly anticompetitive practice. *See infra* Section III. For all of these reasons, this Court should make clear that (1) naked, horizontal customer allocation remains in the per se category of Sherman Act offenses, and (2) any form of horizontal market allocation must be found ancillary to a legitimate and competitive business association before the rule of reason will be substituted for the per se rule.

ARGUMENT

I. THE DISTRICT COURT MISSTATED ESTABLISHED LAW ON THE APPLICABILITY OF THE PER SE RULE TO MARKET ALLOCATION

A. The Per Se Rule is Not Reserved for "Exclusive" Market Allocation

In rejecting the per se rule as a matter of law, the district court found it dispositive that the Defendants' bilateral non-compete agreement eliminated competition only for customers served out of distribution facilities that were swapped in the AEA. Jan. 2013 Order at 32-33. In the court's view, Defendants did not allocate the entirety of the markets affected by the AEA. The court stressed that the non-compete agreement did not encompass new customers, or customers not served from the distribution facilities included in the AEA. The court "refused to find the non-compete provisions per se unlawful in part because the non-compete provisions *did not entirely prohibit competition* between SuperValu and C&S." *Id.* at 28-29 (citing July 2010 Order) (emphasis in original). It also "determined that 'per se' analysis was inappropriate because the non-compete provisions *did not exclude* SuperValu and C&S from competing for customers not covered by the AEA." *Id.* at 29 (citing same) (emphasis in original).

"Particularly problematic to characterizing the alleged conspiracy in this case as a market or territorial allocation," said the district court, "is that the non-

compete provisions did not entirely prohibit SuperValu from serving and soliciting *all* customers in the New England region or C&S from serving and soliciting *all* customers in the Midwest region." July 2010 Order at 1982 (emphasis in original). Because the non-compete provisions left open competition for some customers, "[t]he transaction between Defendants is not a true allocation of entire markets or territories." *Id*. The court also cited *Craftsmen Limousine, Inc. v. Ford Motor Co.*, 491 F.3d. 380, 386-87 (8th Cir. 2007), *cert. denied*, 552 U.S. 1040 (2007), to suggest that courts traditionally treat only "exclusive market allocation" as a per se offense. Jan. 2013 Order at 27.

The district court concluded that "a market allocation . . . requires a restraint on competition affecting the entire market to be thought of as a true 'market allocation.'" July 2010 Order at 1093. It stated that, in contrast, "[t]he alleged conspiracy is probably more appropriately described as a customer allocation." *Id*. at 1092. Without drawing any further conclusions on the applicability of the per se rule, the court held that "[b]ecause the AEA does not prohibit SuperValu and C&S from competing for customers not covered by the AEA, SuperValu and C&S did not make an exclusive market allocation. Therefore, the AEA does not fall into an established 'per se' category." Jan. 2013 Order at 29.

The district court's suggestion that market allocation must be "exclusive" to be "true" is not correct. The Supreme Court has held the allocation of "markets,"

Palmer v. BRG of Georgia, Inc., 498 U.S. 46, 49 (1990) (per curiam), "submarkets," *id.*, or "customers," *Cont'l Ore Co.*, 370 U.S. at 708, to be per se illegal. The district court's distinction between "exclusive" territorial allocation and non-exclusive customer allocation has been correctly described as "a distinction without substance." *United States v. Cadillac Overall Supply Co.*, 568 F.2d 1078, 1088 (5th Cir. 1978). "We use [the term] 'market' division . . . to refer to agreements to divide geographic territories, markets for products or services, and agreements to divide customers. The same basic analysis applies to all." Herbert Hovenkamp, Federal Antitrust Policy § 5.2b4 (1994); *accord id.* (4th ed. 2011). "It should be clear that an agreement between rivals is not saved merely because it is not 'air tight.' . . . The fact that the two firms are competing in part of their output does not change the status of the agreement pertaining to the other part." Areeda & Hovenkamp, *supra*, ¶ 2030c.

B. Customer Allocation Falls into an Established 'Per Se' Category

Every antitrust authority known to amicus, including the Eighth Circuit and the Supreme Court, has conclusively and overwhelmingly maintained that naked, horizontal customer allocation is per se illegal. *See Cont'l Ore Co.*, 370 U.S. at 708 ("[A]n allocation of customers [is a] per se violation under § 1 of the Sherman Act."); *Nitro Distrib., Inc. v. Alticor, Inc.*, 565 F.3d 417, 423 (8th Cir. 2009) ("customer allocation agreements are among the most elementary violations [of

Section 1]"); *Blackburn v. Sweeney*, 53 F.3d 825, 827 (7th Cir. 1995) ("To fit under the per se rule an agreement need not foreclose all possible avenues of competition."); *Hammes v. AAMCO Transmissions, Inc.*, 33 F.3d 774, 782 (7th Cir. 1994) ("elementary prohibition of section 1"); *United States. v. Brown*, 936 F.2d 1042, 1045 (9th Cir. 1991) (customer allocation via non-compete agreement is per se illegal); *United States v. Suntar Roofing, Inc.*, 897 F.2d 469, 473 (10th Cir. 1990) (customer allocation is per se illegal); *United States v. Coop. Theatres of Ohio, Inc.*, 845 F.2d 1367, 1372 (6th Cir. 1988) (same); *United States v. Koppers Co., Inc.*, 652 F.2d 290, 296-97 (2d Cir. 1981) (same); *Cadillac Overall Supply Co.*, 568 F.2d at 1088 (same).

Whenever courts have applied the rule of reason, it has been because the customer allocation agreement is vertical rather than horizontal, or ancillary rather than naked. *Cont'l T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 59 n.28 (1977) (restraint was vertical); *Polk Bros., Inc. v. Forest City Enter., Inc.*, 776 F.2d 185, 190 (7th Cir. 1985) (restraint was ancillary).

None of the cases cited by the district court requires exclusivity to apply the per se rule to any form of naked, horizontal collusion, or distinguishes between allocating an entire market versus a submarket, line of business, or group of customers. For example, the district court cited *Coop. Theatres of Ohio,* 845 F.2d at 1371, and *Augusta News Co. v. Hudson News Co.*, 269 F.3d 41, 48 (1st Cir.

2001), purportedly to distinguish non-exclusive customer allocation from "a true allocation" of an entire market. These cases do not support the district court's statement of the law. The court's quote from *Augusta News* omits the first half of the sentence, in which Judge Boudin explains that the conduct described is a per se offense. *Augusta News*, 269 F.3d at 48. *Cooperative Theatres* holds unequivocally that customer allocation is per se illegal. *Coop. Theatres*, 845 F.2d at 1372.

The district court also cited the lower court opinion in *Cardizem* in support of an exclusivity requirement, emphasizing on its own that the *Cardizem* defendants allocated the entire U.S. market to a lone competitor. July 2010 Order at 1092. But there is no indication that the district court in *Cardizem* applied the per se rule on the basis that the entirety of the defined market was allocated. Importantly, all of the opinions the *Cardizem* court cited as grounds for applying the per se rule hold that non-exclusive *customer* allocation is per se unlawful, notwithstanding that by definition it does not necessarily eliminate all competition between the conspiring parties. *See In re Cardizem CD Antitrust Litig.*, 105 F. Supp. 2d 682, 699 (E.D. Mich. 2000) (citing *United States v. Topco Associates, Inc., 405 U.S. 596 (1972)*, *Palmer*, *Cooperative Theatres*, and *Sweeney*).[3] It is

[3] Moreover, although the *Cardizem* court did note that defendants allocated the entire market for "Cardizem CD and its bioequivalents," 105 F. Supp. 2d at 685, the court never defined this market as a *relevant antitrust market*. *See infra* note 4.

simply incorrect to find that *Cardizem* requires the allocation of the entirety of a defined market to invoke the per se rule.

The district court later cited *Craftsmen II* in support of its suggestion that only "exclusive market allocation" receives per se treatment. Jan. 2013 Order at 27. The plaintiffs in the *Craftsmen* cases alleged a novel conspiracy theory whereby Ford Motor Company instituted a group boycott under the pretense of creating a program to certify vehicle compliance with National Highway Traffic Safety Administration standards. *See Craftsmen Limousine, Inc. v. Ford Motor Co.*, 363 F.3d 761, 766 (8th Cir. 2004) ("*Craftsmen I*"). The *Craftsmen II* court, mindful that the defendants' plausible safety justifications could have procompetitive effects, came to the unexceptional conclusion that the rule of reason is appropriate when a market's experience with a given restraint does not lend itself to "a confident conclusion about the principal tendency of [the] restriction." *Craftsmen Limousine, Inc. v. Ford Motor Co.*, 491 F.3d 380, 387 (8th Cir. 2007) ("*Craftsmen II*") (citing *Calif. Dental Ass'n v. FTC*, 526 U.S. 756, 780-81 (1999)); *see also Craftsmen I*, 363 F.3d at 774 (emphasizing that restraint occurred in standard setting context) (citing Areeda & Hovenkamp, *supra*, ¶ 2232b).

But nothing in *Craftsmen II* calls into question the Eighth Circuit's ability to draw confident conclusions about the principal tendency of naked, horizontal

market allocation agreements. Indeed, the court in *Craftsmen I* had no doubt at all: it expressly included market allocation in its list of recognized per se offenses. 363 F.3d at 773 ("Among the practices which the courts have heretofore deemed to be unlawful in and of themselves [is] . . . division of markets.") (quoting *Northern Pacific Ry. Co. v. United States*, 356 U.S. 1, 5 (1958)). The *Craftsmen* cases simply do not support the district court's circumscribed application of the per se rule to market allocation agreements.

C. Using "Exclusivity" as a Basis for Applying the Per Se Rule to Market Allocation Agreements is Illogical and Would Eviscerate the Rule

If accepted uncritically, the district court's conclusion that non-exclusivity alone, absent ancillarity or verticality, can take market allocation out of the per se category of offenses would create an exception to the per se rule that would swallow the rule. If courts were to differentiate between "exclusive" and non-exclusive market allocation agreements in applying the per se rule, they would not be able to determine the proper liability standard for *either* type of agreement without first defining the relevant market. Whether an "entire" market versus a submarket or group of customers has been allocated is entirely a function of market definition.[4]

[4] Moreover, courts cannot presume to know the boundaries of a relevant market solely by reference to agreements like the AEA. What constitutes an "entire" market for antitrust purposes can be a vastly different question than it is for

Requiring market definition prior to assigning a liability standard is illogical. Market definition is commonly understood as a tool for measuring, rather than balancing, likely competitive effects. "Market definition plays two roles. First, market definition helps specify the line of commerce and section of the country in which the competitive concern arises. . . . Second, market definition allows the agencies to identify market participants and measure market shares and market concentration." U.S. Dep't of Justice & FTC, Horizontal Merger Guidelines § 4 (2010). As the Merger Guidelines make clear, "the measurement of market shares and market concentration is not an end in itself, but is useful to the extent it illuminates the [conduct's] likely competitive effects." *Id*.

Categorically, however, the competitive effects of per se restraints are well known and do not require further illumination. Market definition therefore isn't "useful." *Id*. It does not aid the court in determining the balance of the likely competitive effects of a given market allocation agreement. Using market

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ordinary business purposes. *See* Jonathan B. Baker, *Market Definition: An Analytical Overview*, 74 Antitrust L.J. 129, 138-39 (2007) ("Market definition for antitrust purposes . . . is an economic question . . .[;] there is no reason to expect that the concept of market employed by business executives when discussing issues of business strategy or marketing . . . would be the same as the concept of an 'antitrust market' or 'relevant market' defined for the purpose of antitrust analysis."). Market definition in antitrust cases "focuses solely on demand substitution factors." U.S. Dep't of Justice & FTC, Horizontal Merger Guidelines § 4 (2010). "If a hypothetical monopolist could profitably target a subset of customers for price increases, the Agencies may identify relevant markets defined around those targeted customers . . .". *Id*. § 4.1. 4 (2010).

definition considerations to assign a per se or rule-of-reason liability standard is therefore illogical.

Requiring market definition prior to assigning a liability standard also would undermine one of the primary purposes and effects of the per se rule, which is eliminating the complexity of defining markets and showing market power. "We have certainly learned from merger, monopoly, and rule of reason cases that proving markets and power is difficult, complex, expensive and time-consuming. The courts wisely decline to burden the system with such proof [in per se cases]." Phillip Areeda, *The Changing Contours of the Per Se Rule*, 54 Antitrust L.J. 27, 28 (1985); *see also* Robert Bork, The Antitrust Paradox 269 (1978) (describing the disutility of introducing the "enormous complexities of market definition" into cases involving per se conduct). By relying on a market definition inquiry to assess the applicability of the per se rule, the district court's analysis would sacrifice a key goal of the rule. The rule would be left only nominally available to plaintiffs and government enforcers. In theory, the per se rule would continue to apply to "exclusive" market allocation, but in practice it would be eviscerated for all forms of horizontal market allocation because the exclusivity determination inevitably would demand that relevant antitrust markets be defined.

It is easy to see why courts and antitrust authorities do not distinguish between allocating entire markets and allocating submarkets or customers. "[T]he

rationale for per se rules . . . in part is to avoid the necessity for an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries." *Arizona v. Maricopa Cnty. Med. Soc'y*, 457 U.S. 332, 351 (1982). Market definition is an extremely complex undertaking that makes no economic sense for restraints "that would always or almost always tend to restrict competition and decrease output." *Broad. Music, Inc. v. Columbia Broad. Sys., Inc.*, 441 U.S. 1, 19-20 (1979). "Hence per se rules have long been justified on the ground that certain kinds of conduct are so likely to prove to be unreasonably anticompetitive that time spent considering defenses would be time wasted." Andrew I. Gavil, William E. Kovacic & Jonathan B. Baker, Antitrust Law in Perspective 104 (2d ed. 2008). *See infra* Section III.B.

II. DEFENDANTS SHOULD HAVE THE BURDEN TO SHOW HORIZONTAL NON-COMPETE AGREEMENTS ARE "ANCILLARY" RESTRAINTS DESERVING RULE OF REASON TREATMENT

The district court invoked the ancillary restraints doctrine without resolving the question of whether the Defendants' non-compete agreement was an ancillary restraint. The court described the ancillary restraints doctrine and correctly stated, "some agreements [that] restrain competition may be valid if they are subordinate and collateral to another legitimate transaction and necessary to make that transaction effective." July 2010 Order at 1093. It added that "whether an agreement is ancillary requires a court to consider whether, at the time the

agreement was made, it was necessary to promote the enterprise and productivity of an underlying arrangement." *Id.* at 1093-94.

The district court acknowledged in the July 2010 Order that "*questions remain* as to whether the transaction can avoid per se treatment because the non-compete provisions . . . qualify as ancillary restraints," *id*. at 1093 (emphasis added), and it did not decide the issue, *id*. at 1094 ("On the current record . . . whether the non-compete agreements were ancillary to [the] AEA in the sense that they were necessary to protect the value of the assets being exchanged and realize economic integration cannot be resolved on summary judgment."). Nonetheless, the court stated that "[i]n the context of a transfer of business assets accompanied by a non-compete agreement, a per se approach does not seem warranted unless the restriction has no integrative prospects whatsoever." *Id.* at 1094. It further noted that the defendants *might be able* to show efficiencies from the AEA and that under these circumstances "executing the non-compete provisions [would] seem reasonably necessary to realize the procompetitive benefit of increased efficiency." *Id.*

The district court in its Jan. 2013 Order, citing its July 2010 Order, stated that "Defendants could show that the acquisition of distribution facilities would be a pro-competitive benefit to the transaction, allowing customers to be served more efficiently through fewer distribution facilities." Jan. 2013 Order at 30. It made no

finding, however, as to the questions that remained from its July 2010 Order. Specifically, it did not determine "whether the non-compete agreements were ancillary to [the] AEA in the sense that they were necessary to protect the value of the assets being exchanged and realize economic integration," July 2010 Order at 1094. *See* Jan. 2013 Order at 30.

As the district court indicated in the July 2010 Order, horizontal non-compete agreements can serve a procompetitive purpose in conjunction with "a legitimate transaction." *Id.* at 1093. They can be used to facilitate beneficial economic collaboration. *Polk Bros.*, 776 F.2d at 190. For example, in the context of an asset sale, a limited horizontal non-compete agreement can protect the transferred customer goodwill that could otherwise be appropriated by the seller. *LDDS Commc'ns, Inc. v. Automated Commc'ns*, 35 F.3d 198, 199 (5th Cir. 1994). Under these circumstances, non-compete agreements are "ancillary" restraints that are part of a larger economic integration and promote competition, as opposed to "naked" restraints on competition that only injure consumers. *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 229 (D.C. Cir. 1986) (Bork, J.).

Although horizontal non-compete agreements in the context of an economic integration can be procompetitive and benefit consumers, they should not be treated as ancillary and evaluated under the rule of reason solely on the basis that the underlying transaction has "integrative prospects." July 2010 Order at 1094.

This treatment assumes away "the essential question [involving] an asset swap with a competitor: What is the central purpose of the transaction?" Maurice E. Stucke, *Evaluating the Risks of Market Swaps*, Antitrust, Fall 2003, at 67, 67.

The district court's approach would encourage creative circumvention of the per se rule and be highly damaging to consumers. To avoid per se illegality, businesses that wanted to allocate markets could engage in sham or token transactions and concurrently agree to horizontal non-compete agreements. *Id*. at 67-69. Horizontal market allocation would escape per se condemnation (and enjoy de facto legality under the rule of reason, *see* Douglas H. Ginsburg, *Vertical Restraints: De Facto Legality under the Rule of Reason*, 60 Antitrust L.J. 67 (1991)), provided it is disguised in an apparent economic integration. To avoid this result, which is antithetical to the "consumer welfare prescription" of the antitrust laws, *Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979), courts should "examine[] the substance, rather than the form, of the parties' agreement in evaluating its potential effect." *United States v. Village Voice Media, LLC*, Civ. Action No. 1:03CV0164, WL 21659092 (N.D. Ohio Feb. 12, 2003), Competitive Impact Statement at 11.

Because non-compete agreements can be used to allocate markets between horizontal competitors, Defendants should have the burden of showing that horizontal non-compete agreements are ancillary to a larger economic activity.

The Supreme Court has held that a "naked restraint on price and output requires some competitive justification." *NCAA v. Bd. of Regents of the Univ. of Oklahoma*, 468 U.S. 85, 110 (1984). To overcome the negative presumption and trigger the ancillary restraints doctrine, defendants should have to show that a horizontal non-compete is "*reasonably related to*, and *reasonably necessary* to achieve procompetitive benefits from, an efficiency-enhancing integration of economic activity." Fed. Trade Comm'n & U.S. Dep't of Justice, Antitrust Guidelines for Collaborations Among Competitors § 1.2 (Apr. 2000) (emphasis added). An agreement may be "reasonably necessary" without being essential. *Id.* at § 3.2. It is, however, not "reasonably necessary" if the party "could achieve an equivalent or comparable efficiency-enhancing integration through practical, significantly less restrictive means." *Id.* If defendants meet the burden of showing that a horizontal non-compete agreement is "reasonably related to and reasonably necessary" to achieve the benefits from an economic integration, *id.* at § 1.2, the restraint should be treated as ancillary and evaluated under the rule of reason. *PolyGram Holding, Inc. v. FTC*, 416 F.3d 29, 36 (D.C. Cir. 2005) (Ginsburg, J.). If they do not satisfy this burden, the restraint should be deemed naked and condemned as per se illegal. *Id.*

III. POLICY CONSIDERATIONS STRONGLY SUPPORT THE PER SE ILLEGALITY OF HORIZONTAL MARKET ALLOCATION

A. Horizontal Market Allocation Is Very Harmful to Consumers

Horizontal market allocation is of a piece with horizontal price fixing. From an economic perspective, the two restraints represent different routes to similar anticompetitive ends. Horizontal price fixing involves firms agreeing on a price at which to sell their products. In contrast, horizontal market allocation is the assignment of markets, submarkets, or customers to different firms. Rather than establish a price floor, it gives a firm market power over its designated market, submarket, or group of customers. Both practices reduce market output and produce higher prices for consumers. *Gen. Leaseways, Inc. v. Nat'l Truck Leasing Ass'n*, 744 F.2d 588, 594-95 (7th Cir. 1984).

Although its effects are often similar to those of horizontal price fixing, horizontal market allocation can be even more harmful to consumers than price fixing. Successful horizontal price fixing sets a price floor and eliminates head-to-head *price* competition between the parties involved. The parties, however, remain free to compete on non-price terms. Areeda & Hovenkamp, *supra*, ¶ 2002f5. Participants may follow the cartel price but try to capture market share through higher quality or better service. Horizontal market allocation goes further and eliminates both *price* and *non-price* competition between the parties involved. *Blue Cross & Blue Shield United of Wis. v. Marshfield Clinic*, 65 F.3d 1406, 1415

(7th Cir. 1995); Areeda & Hovenkamp, *supra*, ¶ 2031. When competitors allocate markets, they agree to serve only certain territories, product lines, or customers and refrain from all forms of competition. For consumers, the result of market allocation may be not only higher prices but also diminished quality and reduced innovation.

Horizontal market allocation is also often easier to establish than horizontal price fixing. In price fixing arrangements, the participants frequently disagree over the collusive price. Some firms may have lower costs and a lower profit-maximizing price. Others may have higher costs and favor a higher price. Heterogeneous cost structures can thus be an important obstacle to the formation of price fixing agreements and preserve competition to the benefit of consumers. Areeda & Hovenkamp, *supra*, ¶ 2002f3. Under a horizontal market allocation scheme, however, parties assign markets, submarkets, or customers and do not have to agree on a common price. *Id.* ¶ 2031. Once markets have been allocated, each participant can choose its profit-maximizing price and does not have to seek consensus on price with other firms. *Id.*

Because horizontal rivals that collude may still have strong incentives to cheat by undercutting the collusive price (to the benefit of consumers), *id.* ¶ 2002d1, colluding parties must be able to detect and punish cheating to preserve collusive agreements. If colluding parties find out that a cartel member is

deviating from the collusive price, they can respond with aggressive price competition and dissipate collective profits, limiting the gains from cheating. *Id.* A firm that recognizes that price discounting today may lead to higher profits today but lower profits in the future may be deterred from cheating on the collusive price. *Id.* If, however, cheating cannot be detected and punished through aggressive price competition, firms have a greater incentive to cheat and undercut the collusive price. *Id.*

Compared to horizontal price fixing agreements, horizontal market allocation agreements simplify the detection of cheating. In a market where prices and other transaction terms are nontransparent, parties to a horizontal price fixing arrangement may be able to undercut the collusive price, *id.,* or offer more generous non-price terms such as better service and longer warranties without fear of detection. *Id.* ¶ 2002f5. In contrast, horizontal market allocation allows for easier detection of cheating than horizontal price fixing does. "[C]rossing of market division lines is often more readily observable than secret price concessions." *Id.* ¶ 2031. Due to this simplified detection of cheating, horizontal market allocation agreements as a general matter are likely to prove more durable and even more damaging to consumers than horizontal price fixing.

B. Per Se Illegality Is Appropriate for Conduct, Like Horizontal Market Allocation, That Is Overwhelmingly Anticompetitive

Even as the Supreme Court has applied the rule of reason to a wider array of business practices in recent decades, *see, e.g.*, *Cont'l T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977); *Leegin Creative Leather Prod., Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007), it continues to recognize that the per se rule is appropriate for behavior that "will so often prove so harmful to competition and so rarely justified that the antitrust laws do not require proof that an agreement of that kind is, in fact, anticompetitive in the particular circumstances." *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128, 133 (1998). If the courts apply the rule of reason to conduct that is almost always harmful to consumers, they would be engaging in a judicial inquiry that is "needless and wasteful." *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 486 (1992) (Scalia, J., dissenting). And, even for conduct that may on occasion benefit consumers, judicial economy and greater legal certainty may still justify imposition of the per se rule if the effects of the conduct are generally harmful. *Leegin*, 551 U.S. at 915 (Breyer, J., dissenting). "[Antitrust] law, unlike [antitrust] economics, is an administrative system the effects of which depend upon the context of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients." *Id.* at 914-15.

Market allocation, whether it involves markets, submarkets, or customers, should remain per se illegal because of its highly anticompetitive effects. It

eliminates *all* competition between the parties involved, resulting in higher prices and less attractive non-price terms for consumers. Areeda & Hovenkamp, *supra*, ¶ 2031. Allowing defendants to introduce justifications, "which are 'so unlikely to prove significant in any particular case,' costs society more by compromising 'business certainty and litigation efficiency' than society loses by ignoring a justification that could be persuasive and important in a particular instance." *Id.* ¶ 1510b (quoting *Maricopa Cnty. Med. Soc'y*, 457 U.S. at 344, 351).

C. Application of the Rule of Reason to Horizontal Market Allocation Would Result in Under-Deterrence of a Highly Anticompetitive Practice

Although the Supreme Court has stated that most forms of business conduct should be evaluated under the rule of reason, *State Oil Co. v. Khan*, 522 U.S. 3, 22 (1997), this analytical framework has serious shortcomings. The rule of reason requires a costly and ordinarily open-ended inquiry into the defendants' conduct. Some circuits in applying the rule of reason have imposed some structure and used a market power screen, as a way of terminating the judicial inquiry at an early stage. Mark R. Patterson, *The Market Power Requirement in Antitrust Rule of Reason Cases: A Rhetorical History*, 37 San Diego L. Rev. 1, 24-26 (2000). Yet, even examining the existence of market power "invites lengthy time-consuming argument among competing experts as they seek to apply abstract, highly technical criteria to often ill-defined markets." *Leegin*, 551 U.S. at 917 (Breyer, J.,

dissenting). Rule of reason litigation often entails substantial costs and involves "enlisting legions of economists, lawyers, and paralegals." Maurice E. Stucke, *Does the Rule of Reason Violate the Rule of Law?*, 42 U.C. Davis L. Rev. 1375, 1461 (2009).

Furthermore, conduct evaluated under the rule of reason has often, in practice, become de facto legal. Ginsburg, *supra*, at 67. Judge Posner has described the rule of reason in application as "no more than a euphemism for nonliability." Richard A. Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision*, 45 U. Chi. L. Rev. 1, 14 (1977). The statistics on antitrust cases lend strong support to this view. A 2009 study found that defendants won 221 out of 222 rule of reason cases that reached final judgment between 2000 and 2009. Michael A. Carrier, *The Rule of Reason: An Empirical Update for the 21st Century*, 16 Geo. Mason L. Rev. 827, 829-30 (2009).

Given this experience with the rule of reason, applying it to naked, horizontal market allocation would likely result in significant under-deterrence of an overwhelmingly anticompetitive practice. The costs involved and the low probability of success in a rule of reason case would likely discourage plaintiffs from bringing meritorious claims against parties alleged to have allocated markets. Stucke, *supra*, at 1466-67. As a result, defendants would often be absolved of

treble damage liability – a powerful deterrent against anticompetitive behavior. Robert H. Lande & Joshua P. Davis, *Comparative Deterrence from Private Enforcement and Criminal Enforcement of the U.S. Antitrust Laws*, 2011 B.Y.U. L. Rev. 315, 317 (2011). Moreover, the federal government would not realistically be able to compensate for the probable reduction in the number of private cases against parties alleged to have allocated markets. Robert H. Lande & Joshua P. Davis, *Benefits from Private Antitrust Enforcement: An Analysis of Forty Cases*, 42 U.S.F. L. Rev. 879, 906 (2008). And, when it did bring a case, the government would be very unlikely to bring a criminal enforcement action against conduct that the courts evaluate under the rule of reason. *See* Thomas O. Barnett, Assistant Attorney General Antitrust Division U.S. Dep't of Justice, Criminal Enforcement of Antitrust Laws: The U.S. Model, Presentation at the Fordham Competition Law Institute's Annual Conference on International Antitrust Law and Policy 2 (Sept. 14, 2006). Defendants would be able to engage in horizontal market allocation and injure consumers with virtual impunity.

CONCLUSION

If this Court's de novo review reveals that Defendants' bilateral non-compete agreement was ancillary to their asset exchange, it should affirm the district court's application of the rule of reason, but clarify that the court misstated and misapplied the law. If, however, this Court finds that Defendants' bilateral

non-compete agreement was a naked, horizontal division of customers, it should reverse and apply the per se rule. Amicus writes to ask this Court to clarify Eighth Circuit law and ensure (1) naked, horizontal customer allocation remains in the per se category of Sherman Act offenses, and (2) any form of horizontal market allocation must be found ancillary to a legitimate and competitive business association before the rule of reason will be substituted for the per se rule.

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation set forth in Fed. R. App. P. 32(a)(7)(B) as it contains 6,944 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). This brief also complies with the type face requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) as it has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in 14-point Times New Roman type style.

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