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# ANTITRUST AND THE SYSTEMIC BIAS AGAINST SMALL BUSINESS:

## *KODAK*, STRATEGIC CONDUCT, AND LEVERAGE THEORY

Warren S. Grimes<sup>†</sup>

### INTRODUCTION

I'll always remember the day I first read *Kodak*.<sup>1</sup> It was late June of 1992; a sunny, smog-free Los Angeles sky offered expansive views. The words of Justice Harry Blackmun, too, seemed clear and far-sighted. Yes, that's the same jurist who antitrust lawyers knew for offering "Casey at the Bat" and other baseball lore in an eclectically written but backwater opinion involving professional baseball's judicially crafted antitrust exemption.<sup>2</sup> But *Kodak* was not about baseball trivia.

Blackmun wrote for the Court that "[l]egal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored in antitrust law."<sup>3</sup> This straightforward endorsement of empiricism in judicial interpretation was a unifying theme for post-Chicago antitrust analysis. The Court refused to allow dismissal before trial of an antitrust claim backed by credible economic theory and the plaintiffs' threshold evidence of anticompetitive effects.<sup>4</sup> And there was more. The opinion showed an attention to and analysis of information problems that could be relevant to establishing the defendant's market power in the sale of aftermarket parts. The Court was unwilling to be constrained by rigid or artificial market definitions, instead guiding its analysis by considering actual

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<sup>1</sup> *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451 (1992).

<sup>2</sup> *See Flood v. Kuhn*, 407 U.S. 258 (1972).

<sup>3</sup> *Kodak*, 504 U.S. at 466-67.

<sup>4</sup> *Id.* at 485-86.

anticompetitive effects.<sup>5</sup> The outcome was consistent with some earlier cases, but *Kodak* offered a clarity of analysis and explanatory power lacking in past rulings.

Later in the summer, the smog returned to Los Angeles skies. As the first commentary on *Kodak* appeared, it was evident that what for me was clarifying and enlightening was for some impenetrable, obscuring, and perhaps even toxic to inhale. Through the ensuing decade, *Kodak* has engendered strong praise<sup>6</sup> and harsh criticism.<sup>7</sup> One key holding in *Kodak*, the Court's recognition of the coercive effect of sunk investments in a seller's line, has received a frosty reception in the majority of federal court decisions that have addressed it, but it has also been expressly embraced and followed by a few courts.

With the benefit of a decade of hindsight and ample commentary, I offer a different perspective on *Kodak*: as a key to a comprehensive strategy that addresses the modern marketplace's systemic bias against small business. Large power buyers and sellers up and down the distribution chain are common in most markets. These power players offset one another in buyer-seller relationships. The countervailing power that checks many potentially abusive exercises of market power is, however, lacking when power players compete with, buy from, or sell to non-power players. Small businesses, then, are opportune targets for strategic behavior that raises their costs or

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<sup>5</sup> See *id.* at 477 ("It is clearly reasonable to infer that Kodak has market power to raise prices and drive out competition in the aftermarkets, since respondents offer direct evidence that Kodak did so."). See also Steven C. Salop, *The First Principles Approach to Antitrust*, *Kodak and Antitrust at the Millennium*, 68 ANTITRUST L.J. 187 (2000) (describing and explaining this aspect of the *Kodak* holding). For a discussion of careful factual analysis as the hallmark of post-Chicago economics, see generally Lawrence A. Sullivan, *Post-Chicago Economics: Economists, Lawyers, Judges, and Enforcement Officials in a Less Determinate Theoretical World*, 63 ANTITRUST L.J. 669 (1995).

<sup>6</sup> Among the favorable commentary: Severin Borenstein et al., *Antitrust Policy in Aftermarkets*, 63 ANTITRUST L.J. 455 (1995); Warren S. Grimes, *Antitrust Tie-In Analysis After Kodak: A Reply to Larson's Comment*, 63 ANTITRUST L.J. 267 (1994); Robert H. Lande, *Chicago Takes it on the Chin: Imperfect Information Could Play a Crucial Role in the Post-Kodak World*, 62 ANTITRUST L.J. 193 (1993); Rudolph J.R. Peritz, *Theory and Fact in Antitrust Doctrine: Summary Judgment Standards, Single-Brand Aftermarkets and the Clash of Microeconomic Models*, 45 ANTITRUST BULL. 887 (2000); Salop, *supra* note 5; Gordon B. Spivack & Carolyn T. Ellis, *Kodak: Enlightened Antitrust Analysis and Traditional Tying Law*, 62 ANTITRUST L.J. 203 (1993).

<sup>7</sup> Among the critical commentary: Thomas C. Arthur, *The Costly Quest for Perfect Competition: Kodak and Nonstructural Market Power*, 69 N.Y.U. L. REV. 1 (1994); Dennis W. Carlton, *A General Analysis of Exclusionary Conduct and Refusal to Deal—Why Aspen and Kodak Are Misguided*, 68 ANTITRUST L.J. 659 (2001); George A. Hay, *Is the Glass Half-Empty or Half-Full?: Reflections on the Kodak Case*, 62 ANTITRUST L.J. 177 (1993); Herbert Hovenkamp, *Market Power in Aftermarkets: Antitrust Policy and the Kodak Case*, 40 UCLA L. REV. 1447 (1993); Benjamin Klein, *Market Power in Antitrust: Economic Analysis After Kodak*, 3 SUP. CT. ECON. REV. 43 (1993); Carl Shapiro, *Aftermarkets and Consumer Welfare: Making Sense of Kodak*, 63 ANTITRUST L.J. 483 (1995).

imposes discriminatory terms on them. As actual and potential rivals of power-wielding firms, small businesses are a vital cog in the competitive mechanism.

Current antitrust interpretation and enforcement contributes to the anti-small-business bias: (1) through relative intolerance of small firms' collective action that can generate offsetting countervailing power and (2) through unwarranted curtailment of antitrust claims that provide potential remedies for power abuses that typically target small business. Addressing this systemic bias against small business will require a comprehensive strategy. *Kodak* suggests a number of central elements to this strategy. The overarching theme is that an antitrust analysis must be based on real market effects, not on rote application of rules that ignore competitive realities. There are, in addition, a number of important corollary themes from *Kodak*: (1) in claims of seller power abuse, a full antitrust analysis cannot be done while wearing blinders that screen out the impact of buyer information inadequacies and the coercive effect of sunk investment; (2) leveraging theory<sup>8</sup> retains its validity when large power firms use tie-ins strategically to target non-power rivals or customers; and (3) antitrust claims backed by threshold evidence of anticompetitive effects and a credible economic theory should survive motions for pretrial dismissal. These points are explored and developed below.

## I. THE SYSTEMIC BIAS AGAINST SMALL BUSINESS

### A. *Power, Countervailing Power, and Strategic Behavior in Modern Markets*

Modern markets and antitrust policy combine to create a systemic bias against small business. The bias is created by the convergence of three factors: (1) the presence of large power firms in most markets; (2) the exercise of countervailing power in commercial transactions between power firms; and (3) the power firms' strategic exercise of power against non-power players, raising their costs or forcing them to accept unfavorable, discriminatory terms.

#### 1. *The Nature of Large Firm Power*

The large power firms in most markets lack pure monopoly power. Although such firms may price well above marginal cost, they lack the freedom of action of a true monopolist. These firms tend to be oligopolists in a market that may be dominated by two or more firms. The size advantages that large firms enjoy are natural

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<sup>8</sup> See leverage theory discussion *infra* Part III.

and inevitable and usually not a direct concern of competition policy. Attaining a size sufficient to achieve minimum efficient scale, for example, can be necessary to compete in a global market. A small business cannot hope to operate on the scale required to design, produce and market large passenger-carrying airplanes. But along with efficient scale, large firms often possess significant market power. That power may be employed strategically to the detriment of non-power players, a matter to be addressed below.

## *2. Power Firms and Countervailing Power*

Galbraith coined the term "countervailing power" in a book written in 1952.<sup>9</sup> The author viewed countervailing power as a positive and natural response to power firms; it allowed a large buyer or seller to negotiate competitive terms in dealing with the power firm. More recently, Porter has written about the role of power buyers and power sellers, suggesting that the presence of these power players is a key to assessing the performance of a particular firm.<sup>10</sup>

If all buyers and sellers up and down the distribution chain could wield power, one might expect the economy to perform adequately in some respects. Although vital dynamism in the market might be undermined, the allocation of goods and services could be reasonably efficient. Countervailing power might check power in every transaction down to the ultimate sale of goods and services to consumers. Assuming the absence of collusion, consumers too might fare well if retailing, although oligopolistic, remained effectively competitive. This description, however, does not comport with real markets, which are peppered not only with large power firms, but also with small players that are frequently the targets of strategic abuse. These small players, entering and leaving markets with greater frequency than the large firms, provide an essential element of dynamism to otherwise relatively static markets.

## *3. The Strategic Employment of Power Against Non-Power Players*

A world in which power checks power leaves little place for those economic players that do not and cannot wield power. Non-power players include, in addition to consumers, any player that buys or sells in relatively small quantities. The list of such players includes small businesses, franchisees, professionals practicing in small

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<sup>9</sup> JOHN KENNETH GALBRAITH, *AMERICAN CAPITALISM: THE CONCEPT OF COUNTERVAILING POWER* (1952).

<sup>10</sup> MICHAEL E. PORTER, *COMPETITIVE STRATEGY: TECHNIQUES FOR ANALYZING INDUSTRIES AND COMPETITORS* 3-6 (1980).

groups, non-profits, small governmental units, or even relatively large firms that buy or sell only small amounts of a product.

Small players can be the targets of antitrust abuse not only as purchasers from or sellers to such firms, but also as rivals of power firms. The facts in *Kodak* illustrate two of these potential injuries. The independent service providers that sought to compete against Kodak in servicing original micrographic equipment complained that their costs were raised (and many were driven from the market) by Kodak's policy of denying them access to needed spare parts. Small players as purchasers were also discriminated against because the tie-in required them to purchase Kodak service in order to obtain Kodak spare parts (Kodak did not enforce the tie-in against end users that serviced their own equipment).<sup>11</sup>

Small sellers are disadvantaged relative to their larger counterparts because they lack the leverage to check the power of a monopsonist buyer. Although pure monopsony is rare, many power buyers enjoy relational market power in dealing with small sellers who have committed their business to a selling relationship with the power buyer. Examples might be an independent contractor that works exclusively for a large firm (such as a taxicab or truck driver providing a vehicle and driving services under contract to a large firm, a franchisee selling distribution and promotion services under long term contract to a franchisor, or doctors selling their services to an HMO).

Indeed, the system bias against small players may undercut them even when they are not buying from or selling to power firms. For example, a small seller may be unable to sell at the same prices that are received by its large power-wielding rival. A monopolist usually can effect price discrimination that targets small buyers; so too might an oligopolist if the price discrimination scheme is followed by its major rivals. Of course, if price discrimination is a parallel practice in an oligopolistic industry, it can have anticompetitive effects on non-power buyers, but there is no obvious competitive disadvantage to the small rival seller—that rival can effect the same price discrimination under the price umbrella provided by the large oligopolist. But when the ability to discriminate in price is based on relational market power exercised over buyers who are locked into the seller's line, the large seller may reap supracompetitive returns that are unavailable to a smaller rival lacking relational power over its customers.

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<sup>11</sup> See discussion *infra* Part II (describing the injuries to small service providers that were Kodak rivals and to small purchasers of Kodak parts and service).

Consider a small soft drink bottler that would market its cola soft drink in competition with the Coca Cola or Pepsi Cola lines. Because of their strong brand image and market share, the large soft drink firms can demand a higher price from buyers. But there is often more to the large firms' advantage. If a large fast food franchisor picks Coke or Pepsi as the brand that will be carried at all of its outlets, the favored soft drink seller may now possess market power in its dealings with the franchisees. The market power is relational—arising from the enduring economic relationship between franchisee and franchisor and the franchisee's sunk costs that lock it into that relationship. For example, if the soft drink dispensers at each franchised outlet are owned and serviced by the designated bottler, the bottler may make repairs to such equipment its lowest service priority, knowing that franchisees are locked in and do not have the freedom to choose a different soft drink bottler. Smaller rivals of the favored soft drink seller are foreclosed from the franchisee trade, raising their cost in competing. And the franchisees themselves (a large class of small businesses) are subject to exploitation.<sup>12</sup>

*B. The Central Role of Small Business in Maintaining  
Competition*

Small businesses are only one group among many non-power players that can be the target of strategically employed power. Consumers, non-profits, small groups of professionals, small governmental units, and even large firms with insubstantial participation in a particular market are usually non-power players. Competition policy should be concerned about the abusive exercise of power that targets any of these groups. Is there a basis for according special attention to small business?

The answer is an emphatic yes. Allocative efficiency and the avoidance of market-power based wealth transfers, primary benefits of competition, can be achieved only if small firms are able to compete in the market place on their competitive merits. Small firms, unlike consumers, non-profits, or governmental units, are not only buyers and sellers in transactions with power firms; they are also the actual and potential rivals of these firms. They provide direct head-to-head competition that can inject new ideas and new competitive

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<sup>12</sup> This point is developed in Warren S. Grimes, *Market Definition in Franchise Antitrust Claims: Relational Market Power and the Franchisor's Conflict of Interest*, 67 ANTITRUST L.J. 243, 246-49 (1999).

vigor in the system. Maintaining dynamism in our economic system is (or ought to be) another central goal of antitrust policy.<sup>13</sup>

Small businesses are pivotal to competition policy for another reason: they are a natural and vital class of antitrust enforcers. As the frequent targets of power abuses, small businesses, unlike consumers whose injury from antitrust abuses may be too diluted to warrant a response, have the incentive, the information, and the financial backing to mount effective antitrust challenges. As theorists have long recognized, a rival, whether small or large, has an incentive to take legal action against any conduct that threatens its viability, even if that conduct is procompetitive.<sup>14</sup> This incentive suggests the need for careful antitrust analysis that can weed out opportunistic suits. But if screening rules are overreaching and eliminate meritorious claims, competition goals are not well served. Small businesses and other small players are the first to suffer from stifled competition, and that injury inevitably reaches consumers.

### C. *Could the Bias Against Small Business Promote Competition?*

Competition policy should not be anti-big business. Where being large is part of the natural, competitive order and necessary to survive in global markets, a competition policy that indiscriminately favored small businesses would be shortsighted. To the extent that attaining minimum efficient scale requires large size, antitrust should generally stand clear of behavior that allows the requisite growth. The goal of competition policy is to promote and preserve competition on its merits, ideally achieving a neutrality about firm size that is adjusted only if firm size correlates positively or negatively with competition goals.

Large size can lead to economies of scale, but it can also produce market power that is abusively exercised at the expense of small business. Is there an argument that such abuses should be tolerated in the interest of sound competition policy? Such an argument can be grounded in the large power-wielding firm's need for freedom of ac-

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<sup>13</sup> Of course, the case for small business could also rest on populist concerns, echoing Judge Learned Hand's view that small businesses contribute to the democratic social fabric, community values, and overall satisfaction. See *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 427 (2d Cir. 1945) (L. Hand, J.). One could also point to small business as a primary constituency that supported the Sherman Act and other antitrust legislation. These are concerns that have resonated over a century of antitrust.

<sup>14</sup> Easterbrook and Fischel were particularly critical of targets of takeover offers that might bring suits to challenge the takeover on antitrust grounds. See Frank H. Easterbrook & Daniel R. Fischel, *Antitrust Suits by Targets of Tender Offers*, 80 MICH. L. REV. 1155 (1982). A similar view is presented in HERBERT HOVENKAMP, *FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE* § 16.3a2, at 597-98 (2d ed. 1999). The standing requirements imposed on rivals in merger suits are addressed *infra* Part I.D.2.



tion. One might also find support for such a policy if it resulted in lower enforcement costs or greater certainty in the law. But any such argument, to be persuasive, must justify anticompetitive results. The anticompetitive conduct that victimizes small business often falls within the definition of clear-cut antitrust violations such as monopolization, tie-ins, and boycotts. Unless something more than a pretextual claim can be advanced for the efficiency-enhancing effects of the conduct, and unless that procompetitive effect cannot be attained by reasonable and less anticompetitive means, the conduct should be prohibited.

The case for tolerating anticompetitive conduct harmful to small business may be strongest in an area such as price discrimination. All sellers seek the means to discriminate in price, charging those buyers with higher limit prices a premium not demanded of buyers with lower limit prices. Many forms of such discrimination are widely practiced and condoned, such as restaurant discounts for seniors or children. One might also argue that broadly limiting price discrimination could cause power buyers to lose their ability to force lower prices. This might occur because power sellers, knowing that they are restrained from maintaining higher prices in sales to non-power buyers, would have a stronger incentive to resist the discount demands of the power buyers. Indeed, the power sellers might even resort to cartel practices to maintain uniformly high prices against all types of buyers. Consumers would end up paying higher overall prices and the goals of competition policy would be undermined.

This description may accurately highlight a risk from curtailing price discrimination that targets non-power wielding firms. But the risk is easily overstated. True price discrimination is charging different prices to two buyers when the difference is not based on the competitive merits of the buyer's purchase.<sup>15</sup> Large volume orders often entail efficiencies because per unit administrative and transportation costs are less than those generated by a small order. So a price differential that reflects only these cost savings is not price discrimination and should not be vulnerable to antitrust attack. Large buyers would still enjoy the benefits of any efficiency linked to volume purchasing.

Any non-efficiency related price discount would constitute price discrimination. But all such price discrimination should be vulnerable to antitrust attack primarily when it targets non-power buyers and when it is reachable through traditional antitrust claims. Strategic conduct attacking small players might be attacked in Sherman Act

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<sup>15</sup> I attempt no analysis here of the extent to which the Robinson Patman Act, 15 U.S.C. § 13 (1994), is consistent with the goal of prohibiting only price differentials that constitute true price discrimination.

section 1 claims such as tie-ins, exclusive dealing, and vertical maximum price-fixing, and related Sherman Act section 2 offenses. Even true price discrimination might be tolerated if it were unlikely to produce anticompetitive results.

There is, in any event, a more fundamental difficulty in the logic of any argument that price discrimination that targets non-power firms has substantial competitive benefits. The argument leads inexorably to the conclusion that small firms are needed as punching bags for power buyers or sellers so that society can enjoy the maximum benefits of competition. Yet, the very act of tolerating strategic predation or discrimination makes it more difficult for these non-power firms to survive.

#### *D. Current Competition Policy Reinforces the Systemic Bias Against Small Business*

Lacking the countervailing power to deal on equal terms with power buyers or sellers, small players still have several options for addressing the power disparity: (1) they can consolidate with one another or sell out to a larger rival, abandoning the ranks of small business, but attaining through business marriage the desired countervailing power; (2) they can form collective buyers' or sellers' associations that will exercise countervailing power; or (3) they can seek antitrust remedies for abusive conduct of power buyers or sellers. Current U.S. antitrust law gives small business substantial latitude in arranging a merger or acquisition. For some small businesses or professionals, however, consolidation is unworkable or unpalatable, so only the second and third options remain.

##### *1. Antitrust's Relative Intolerance of Cooperative Buying and Selling*

The antitrust laws have allowed small firms some latitude in engaging in collective action to create countervailing power. A critical limit to antitrust's tolerance of such conduct has been the per se rule under section 1 of the Sherman Act. The Supreme Court has held that individually powerless criminal lawyers violated the per se rule when they formed a collective to pressure (through a boycott) the District of Columbia on the rates and terms of representing indigent defendants.<sup>16</sup> The Court has also held that small grocery stores that formed an association to purchase and promote a house brand of grocery products violated the per se rule when they divided retail territories among their members.<sup>17</sup> The law may be more tolerant of buyers co-

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<sup>16</sup> See *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990).

<sup>17</sup> See *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972).

operatives than sellers cooperatives.<sup>18</sup> The law also tolerates cooperative buying and selling more readily when accompanied by efficiencies, but the Joint Collaboration Guidelines issued by the federal agencies in 2000 provide that collective action that is unaccompanied by efficiencies will still be subject to the per se rule.<sup>19</sup> This places small firms at an unwarranted competitive disadvantage. As explained elsewhere,<sup>20</sup> antitrust law should adjust to permit small players (professionals practicing in small groups and small businesses) to engage in collective action designed to generate countervailing power, even when there are no evident efficiencies associated with the conduct, as long as the market share of the collective does not exceed the limits permitted under current merger enforcement policy.

## 2. *Well-Intentioned Rules That Bar Meritorious Claims*

A legal system operating under the rule of *stare decisis* tends to resist sudden changes in direction. Because the Sherman Act is written in general language comparable to provisions of the U.S. Constitution, judicial interpretations are pivotal in shaping antitrust law and policy. One of the defining characteristics of antitrust judicial interpretations may be that any doctrinal development, however soundly based in empirically determined realities, becomes deductive in its application. It is not unusual for a new development to be followed by a period of rote application to a widening universe of fact patterns. Such a course easily leads to extending a doctrine beyond its empirical roots.

Populist doctrines of the 1960s, such as the goal of protecting small business and of forestalling in their incipiency any trend toward market concentration,<sup>21</sup> were perceived as producing rote and excessive application of antitrust law. By the 1970s, many in the antitrust community were persuaded that overreaching enforcement was un-

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<sup>18</sup> See *Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990) (holding that a sellers' boycott was per se unlawful); *Northwest Wholesale Stationers, Inc. v. Pac. Stationery and Printing Co.*, 472 U.S. 284 (1985) (holding that the decision of a buyers' cooperative to exclude a member was not a per se unlawful boycott). See the discussion of these cases in Warren S. Grimes, *The Sherman Act's Unintended Bias Against Lilliputians: Small Players' Collective Action as a Counter to Relational Market Power*, 69 ANTITRUST L.J. 195, 217-25 (2001).

<sup>19</sup> FED. TRADE COMM'N & DEP'T OF JUSTICE, ANTITRUST GUIDELINES FOR COLLABORATIONS AMONG COMPETITORS §§ 3.2, 4.2 (2000).

<sup>20</sup> See Grimes, *supra* note 18, at 248 (urging that the Collaboration Guidelines be amended to allow small players greater latitude to use collective action to create countervailing power).

<sup>21</sup> See *Brown Shoe Co. v. United States*, 370 U.S. 294, 322, 344 (1962) (citing as goals of amendments to section 7 of the Clayton Act the protection of small business and the prevention in their incipiency of trends toward concentration).

dermining the goals of competition.<sup>22</sup> The courts responded by embracing doctrines and rules that limited access to the courts and made it more difficult for plaintiffs to prove a violation. Most (perhaps all) of these rules had an empirical basis: they grew out of genuine perceptions that some enforcement initiatives were stifling competition or were generating costs that outweighed any competitive benefit.

Over the past 30 years, traditional antitrust remedies for power abuses have been significantly curtailed. Rules of interpretation, designed with the commendable intent of screening out non-meritorious claims, have often been applied mechanically or blindly, just as populist doctrines were in the 1960s and 1970s. As a result, power players are invited to structure anticompetitive conduct in a manner that insulates it from antitrust attack. A de facto per se legality may attach to even blatantly anticompetitive conduct. Examples include the limiting of antitrust claims for (1) predatory pricing; (2) minimum vertical price-fixing and related retail power abuses; (3) seller power abuses such as tie-ins, exclusive dealing and vertical maximum price-fixing; and (4) Sherman Act section 2 abuses that target small rivals or small upstream or downstream players. In addition, small firms that would sue now confront stiffer standards for establishing antitrust injury and for surviving pre-trial motions for summary disposition.

This list, by no means exhaustive, is illustrative of screening devices that have evolved during the last three decades. There will be disagreement about the wisdom and extent of each individual curtailment. Most evolved as a response to perceived overreaching antitrust enforcement. However sound a doctrine's evolution, if the reaction to excessive enforcement is itself overreaching, small business will immediately experience perverse effects. Each of the power abuses identified above frequently target small businesses and some, such as strategic predatory conduct, exclusively attack small or less powerful rivals.

#### (a) *Predatory Pricing*

The shift in Supreme Court treatment of predatory pricing is captured in two cases: *Utah Pie Co. v. Continental Baking Co.*<sup>23</sup> in 1967 and *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*<sup>24</sup> in 1993. Here, as in other areas, the trend toward more onerous standards for a plaintiff may be defended as a response to overreaching

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<sup>22</sup> See, e.g., *United States v. Von's Grocery Co.*, 384 U.S. 270, 301 (1966) (Stewart, J., dissenting) (writing that the "sole consistency" to be found in the Court's merger jurisprudence was that "the Government always wins").

<sup>23</sup> 386 U.S. 685 (1967).

<sup>24</sup> 509 U.S. 209 (1993).

enforcement in the populist era.<sup>25</sup> A competitor that lowers its price is engaging in a fundamental act of competition that benefits consumers. But where the price cutting is strategic and targeted to a small rival, the Court's jurisprudence should recognize the legitimacy of a predatory pricing claim brought to protect and preserve the small firm's right to do business free of targeted predation by a power rival.<sup>26</sup> A recent district court ruling involving mechanical application of the Supreme Court's screening tests for below cost pricing and recoupment (and dismissal of a claim that strategic conduct was employed to eliminate small rivals) is *United States v. AMR Corp.*<sup>27</sup>

*(b) Vertical Maximum Price-Fixing and Related Power Buyer Abuses*

Vertical minimum price-fixing and related retail power abuses often target smaller retailers, or even relatively large retailers, that offer discount terms to consumers but have insufficient leverage with their suppliers to counteract the power of a larger retail buyer.<sup>28</sup> In *Business Electronics Corp. v. Sharp Electronics*,<sup>29</sup> a small retailer was terminated as a Sharp dealer because a larger rival retailer did not want the competition from the small retailer. A large buyer's leverage may also be exercised to force the manufacturer to fix the minimum retail price for the product in question. Although Supreme Court decisions have maintained the per se rule against vertical minimum price-fixing, cases such as *Business Electronics* and *Montano Co. v. Spray-Rite Service Corp.*<sup>30</sup> have considerably narrowed the area in which the per se rule is applied. If the law has made it easier to squelch a small discounting retailer, price competition from new and efficient retailers is made more difficult, and competition and consumers are the worse for the loss of these small players' ability to compete vigorously by lowering their prices.

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<sup>25</sup> The movement for stiffer standards governing predatory pricing gained momentum with the Areeda and Turner article proposing a price-based (average variable cost) screening standard for all predatory pricing claims. See Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975).

<sup>26</sup> For an overview of how strategic price predation may occur, see Jonathan B. Baker, *Predatory Pricing After Brooke Group: An Economic Perspective*, 62 ANTITRUST L.J. 585 (1994).

<sup>27</sup> 140 F. Supp. 2d 1141 (D. Kan. 2001), *appeal docketed* (10th Cir. 2001). This decision is addressed *infra* Part V.A.

<sup>28</sup> In *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928 (7th Cir. 2000), the victims of the large retailer's power were large warehouse clubs such as Price/Costco and Sam's Club.

<sup>29</sup> 485 U.S. 717 (1988).

<sup>30</sup> 465 U.S. 752 (1984).

*(c) Tie-ins and Related Power Seller Abuses*

Seller power may target small business through distribution practices such as tie-ins, forced exclusive dealing, or vertical maximum price-fixing. What each of these abuses has in common is the presence of a power seller that can coerce small buyers and, because the market power underlying each of these abuses is often relational, a relevance to the lock-in and informational issues raised in *Kodak*.

During the 1960s, there were three Supreme Court tie-in decisions favorable to the plaintiff in cases involving relational market power.<sup>31</sup> After the 1960s, these tie-in cases disappeared from the Court's docket, until *Kodak*. During this same period, various screening rules that constrain tie-in claims have found their way into the fabric of the law. An example of such a rule is the requirement recognized in some circuits that the defendant be shown to have an economic interest in the tied product.<sup>32</sup> The premise of this rule is that if the defendant has no economic interest in the sale of the tied product, then imposition of the tie is unlikely to have been driven by anticompetitive intent. A tying seller that itself does not benefit from the tie is likely to have sought benign or procompetitive goals in imposing the tie.

Because marketplace behavior is driven by the desire to make money, the premise that a seller would impose a tie on customers entirely free of any profit incentive is open to question. Whether imposed for procompetitive or anticompetitive reasons, a tie will likely make money for the tying seller. For example, if the tie is imposed because, by limiting the source of the tied product, the seller can ensure that the tying product performs well, then there is a goodwill gain for the tying seller in imposing the tie. Most sellers would not impose a tie-in without any financial incentive.<sup>33</sup>

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<sup>31</sup> See *FTC v. Texaco Inc.*, 393 U.S. 223 (1968) (upholding an order enjoining Texaco from requiring franchisee to purchase its products); *Perma Life Mufflers, Inc. v. Int'l Parts Corp.*, 392 U.S. 134 (1968) (upholding plaintiff dealers' tying claim against manufacturer); *Atlantic Ref. Co. v. FTC*, 381 U.S. 357 (1965) (upholding plaintiff franchisees' tying claim against oil company). In these franchising cases, the Court did not use the term "relational market power," but described facts that illustrated the franchisor's market power in dealing with franchisees.

<sup>32</sup> See Eric D. Young, Note, *The Economic Interest Requirement in the Per Se Analysis of Tying Arrangements: A Worthless Inquiry*, 58 *FORDHAM L. REV.* 1353 (1990) (describing and criticizing this screening rule). See also Warren S. Grimes, *Antitrust Tie-In Analysis After Kodak: Understanding the Role of Market Imperfections*, 62 *ANTITRUST L.J.* 263, 317-18 (1994).

<sup>33</sup> A seller's financial incentive may, however, be indirect and diluted. For example, law schools may impose certain threshold requirements (a college degree or a minimum score on an entry examination) for entering students that might be characterized as tie-ins. The school receives only indirect financial reward for the imposition of these requirements.

Even accepting the premise of the economic interest rule, the courts have, in some instances, overextended its reach. In *Directory Sales Management Corp. v. Ohio Bell Telephone Co.*,<sup>34</sup> the court held that no tie-in could be shown because the tying product (telephone service) and tied product (yellow pages listing) were sold by separate subsidiaries of the parent corporation.<sup>35</sup> In the court's view, the plaintiff had failed to trace the flow of funds to establish how the tying seller benefited from sale of the tied product.<sup>36</sup> The notion that a parent and subsidiary do not share a common economic interest must come as something of a shock to business owners and investors. It also seems inconsistent with the Supreme Court's recognition that, when it comes to showing a conspiracy, a parent and wholly-owned subsidiary must be considered a single entity.<sup>37</sup> The holding, then, illustrates the maxim that valid rules overextended are bad law.

Non-power firms have experienced similar escalations in the requirements for prevailing in exclusive dealing and vertical maximum price-fixing claims. The Court decided *Tampa Electric Co. v. Nashville Coal Co.*<sup>38</sup> in 1961, but has not revisited the area (except for Justice O'Connor's concurring opinion in *Jefferson Parish Hospital District No. 2 v. Hyde*<sup>39</sup>). Meanwhile, lower court decisions have probably materially narrowed the law in this area.<sup>40</sup> After deciding *Albrecht v. Herald Co.*<sup>41</sup> in 1968, the Court did not revisit the merits of vertical maximum price-fixing again until it decided *State Oil Co. v. Khan*<sup>42</sup> in 1997, at which point it discarded the per se rule against this form of price-fixing. Some of this retrenchment in the law governing seller power abuses was warranted, but current case law has unduly handicapped small firms in pressing meritorious claims. For

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<sup>34</sup> 833 F.2d 606 (6th Cir. 1987).

<sup>35</sup> *Id.* at 611.

<sup>36</sup> *See id.* In another case in which the economic interest standard was applied beyond its rationale, the court refused to acknowledge a common economic interest between a manufacturer that imposed a tie on aftermarket parts and service and the firm's dealers that provided the parts and service. *See Mitel Corp. v. A & A Connections Inc.*, 1998-1 Trade Cas. (CCH) ¶ 72,120 (E. D. Pa. 1998). The notion that a supplier has no economic interest in keeping its dealers happy is counterintuitive and contrary to the Supreme Court's well-founded recognition that a whole range of vertical restraints are imposed by suppliers to keep dealers content and motivated to actively promote the supplier's products. *See Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 55 (1977).

<sup>37</sup> *See Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 771-72 (1984) ("[T]he parent may assert full control at any moment if the subsidiary fails to act in the parent's best interests.").

<sup>38</sup> 365 U.S. 320 (1961).

<sup>39</sup> 466 U.S. 2 (1984).

<sup>40</sup> *See* LAWRENCE A. SULLIVAN & WARREN S. GRIMES, *THE LAW OF ANTITRUST: AN INTEGRATED HANDBOOK* § 7.3d, at 336-39 (2000) (citing relevant cases).

<sup>41</sup> 390 U.S. 145 (1968).

<sup>42</sup> 522 U.S. 3 (1997).

example, in *Khan* the Court abandoned the per se rule without any apparent recognition that vertical maximum price-fixing, just as a tie-in or forced exclusive dealing, can be an abusive exercise of a seller's power over a relatively powerless buyer.<sup>43</sup>

(d) *Monopolization and Attempted Monopolization*

The Court's contemporary section 2 jurisprudence includes *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*,<sup>44</sup> a case that can be explained by the plaintiff's sunk investment in reliance on an efficient cooperative practice of issuing an all-area lift ticket. The case is a powerful post-Chicago precedent that relies on a factual inquiry into actual anticompetitive consequences to a smaller rival firm. The plaintiffs' victory in *Kodak* may be described in similar terms. But so far, neither *Aspen* nor *Kodak* has produced widespread recognition of the vulnerability of small firms to strategic market power abuses.

A case that illustrates this vulnerability (decided after *Aspen* but before *Kodak*) is *Alaska Airlines, Inc. v. United Airlines, Inc.*<sup>45</sup> The Ninth Circuit Court of Appeals affirmed a judgment that United Airlines and American Airlines had not violated section 2 through their control of computer reservations systems ("CRS") used by travel agents to book airline flights. In order to be listed on the defendants' systems, the plaintiffs (four smaller airlines) had to pay high fees and endure discriminatory listings. The defendants' flights were always listed before any rival's flights, even if a rival's flight more closely matched the time at which the customer wished to fly. If the rival airline refused to pay the access fee, it would lose access to thirty to forty percent of all travel agents (who used only the United or American CRS).<sup>46</sup>

In the face of evidence that the defendants possessed the power to impose supracompetitive terms for listings on their systems, the court nonetheless ruled for the defendants because the plaintiffs had not established monopolization, or a threat of monopolization, in the air travel market.<sup>47</sup> This showing, the court reasoned, was required to

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<sup>43</sup> The Court's insensitivity to targeted abuse of small retailers may be traced in part to the imbalanced discussion of vertical maximum price-fixing in the amicus brief filed by the Department of Justice and Federal Trade Commission. See Warren S. Grimes, *Making Sense of State Oil Co. v. Khan: Vertical Maximum Price Fixing Under a Rule of Reason*, 66 ANTITRUST L.J. 567, 574 (1998).

<sup>44</sup> 472 U.S. 585 (1985).

<sup>45</sup> 948 F.2d 536 (9th Cir. 1991).

<sup>46</sup> These facts were found by the district court in *In re Air Passenger Computer Reservations Systems Antitrust Litigation*, 694 F. Supp. 1443, 1449-50 (C.D. Cal. 1988).

<sup>47</sup> See *Alaska Airlines*, 948 F.2d at 545.



establish a leveraging abuse of monopoly power. The holding is responsive to criticism of leveraging theory that has received support from some theorists, a point that is developed *infra* in Part III. But the ruling is revisionist and inconsistent with Supreme Court language in cases such as *United States v. Griffith*.<sup>48</sup> It would erect yet another obstacle in the path of smaller rivals that seek relief from strategic conduct that raises their costs in competing.

(e) *Limiting Access to the Courts*

At a point in time when private antitrust suits peaked (in 1977), the Supreme Court decided *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*,<sup>49</sup> a case which is the genesis of the antitrust injury doctrine. The injury that the plaintiff complains of, the Court explained, must be of a type that the antitrust laws were designed to prevent.<sup>50</sup> If the injury was simply the result of healthy competition, as the Court concluded was the case with the *Pueblo* plaintiff, there should be no antitrust relief. But here, again, a sound doctrine overextended is bad law. In *Cargill, Inc. v. Monfort of Colorado, Inc.*,<sup>51</sup> the Court extended the antitrust injury doctrine to prevent a smaller rival from obtaining injunctive relief to halt the merger of the second and third largest meat packing firms in the industry. The Court ordered dismissal of the case notwithstanding lower court holdings that the plaintiff met its burden of establishing that the acquisition would likely violate section 7 of the Clayton Act.<sup>52</sup> As a rival, the Court concluded, the plaintiff could benefit from the pricing umbrella established if the merged firm became the price leader in an oligopolistic industry. Hence, the most likely injury that the plaintiff could sustain as the result of the merger was if the merged firm were more efficient and could lower prices. This injury would be due to competition, not anticompetitive conduct.<sup>53</sup>

Read broadly, the decision is troubling because it limits the most knowledgeable and motivated class of plaintiffs, smaller rivals of the combining firms, in mounting even the soundest of antitrust challenges to the merger.<sup>54</sup> In many instances, it is likely that this class of

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<sup>48</sup> 334 U.S. 100 (1948).

<sup>49</sup> 429 U.S. 477 (1977).

<sup>50</sup> *See id.* at 489.

<sup>51</sup> 479 U.S. 104 (1986).

<sup>52</sup> *See id.* at 107-08.

<sup>53</sup> *See id.* at 117 (“[T]he threat of loss of profits due to possible price competition following a merger does not constitute a threat of antitrust injury.”).

<sup>54</sup> For a discussion of the *Cargill* holding, see Joseph Brodley, *Antitrust Standing in Private Merger Cases Reconciling Private Incentives and Public Enforcement Goals*, 94 MICH. L.

plaintiffs will be threatened with anticompetitive injury because of the power players' ability to engage in strategic conduct. For example, even a strong price leader in an oligopolistic industry may occasionally have to resort to targeted price predation in order to maintain the oligopolistic price umbrella. Small firms that might cut their prices to win market share are now particularly vulnerable to this strategic predation exercised by the combined firm.<sup>55</sup>

Another procedural obstacle for small business plaintiffs was erected when the Supreme Court decided *Matsushita Electric Industrial Co. Ltd. v. Zenith Radio Corp.*<sup>56</sup> In this massive proceeding involving conspiracy claims against Japanese producers of television sets intended for the U.S. market, the Supreme Court reversed the court of appeals and reinstated summary judgment for the defendants that had been granted by the district court. In key language, Justice Powell wrote that "if the factual context renders respondents' claims implausible—if the claim is one that simply makes no economic sense—respondents must come forward with more persuasive evidence to support their claim than would otherwise be necessary."<sup>57</sup> *Matsushita* was read by some as establishing a generous standard for granting summary judgment for defendants, and perhaps as an endorsement of a defendant-friendly Chicago School approach to economic analysis.

The *Kodak* Court discouraged any such reading of *Matsushita*, rejecting arguments that Kodak's small market share in the original equipment market *a priori* precluded any antitrust claims. *Matsushita* meant only that if "the plaintiff's theory is economically senseless, no reasonable jury could find in its favor, and summary judgment should be granted."<sup>58</sup> This language suggests that no particular school of economic thought should be given precedence. But the issue has not come fully to rest. In *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*,<sup>59</sup> a divided Court once again gave credence to a disputed economic theory in granting summary judgment for the defendants in predatory pricing claims. However, the *Brooke Group* Court rested, some would say disingenuously, on the failings of the plain-

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REV. 1, 4 (1994). For a discussion of antitrust standing, see Joseph P. Bauer, *The Stealth Assault on Antitrust Enforcement: Raising the Barriers for Antitrust Injury and Standing*, 62 U. PITT. L. REV. 437 (2001).

<sup>55</sup> See Baker, *supra* note 26, at 590-91 (describing how a large firm may, through selective predation targeting small rivals, gain a reputation as a predator that enables it to enforce high prices at relatively low cost to it).

<sup>56</sup> 475 U.S. 574 (1986).

<sup>57</sup> *Id.* at 587.

<sup>58</sup> *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 468-69 (1992).

<sup>59</sup> 509 U.S. 209 (1993).

tiff's factual support, not on the unacceptability of its economic theory.<sup>60</sup>

*Kodak* may have restored some balance to the law governing summary judgment in antitrust claims, but other procedural obstacles (including antitrust injury) remain as major obstacles in some suits brought by small business rivals.

### 3. *Kodak and Competition Policy*

As it should be, the curtailment of antitrust remedies for power abuses identified above is the subject of ongoing discourse. The outcome of this dialogue and its impact on future antitrust policy remain uncertain. That outcome will likely vary depending on the particular power abuse at issue. There is, however, an overarching and straightforward rule that ought to guide the doctrinal discussion in each of these areas: *whether the exercise of power produces anticompetitive results*. That is the fundamental message underlying *Kodak's* insistence that "actual market realities" instead of "legal presumptions that rest on formalistic distinctions" guide antitrust analysis. The principle that antitrust analysis should be guided by evidence of actual anticompetitive effects has been traced to Judge Taft's 1898 opinion in *United States v. Addyston Pipe & Steel Co.*<sup>61</sup> This proposition may seem self-evident, yet it is commonly ignored, as, for example, when a court disregards evidence of substantial anticompetitive effects and dismisses an antitrust claim because of a mechanical rule, whether that rule be a contrived and rigid market definition or an unyielding requirement that no above-marginal-cost pricing can ever be predatory.<sup>62</sup>

There is, however, a narrower but nonetheless vital aspect to *Kodak* that also speaks to the systemic bias against small business. *Kodak's* tie-in of service and parts is an example of a power seller's strategic behavior that can raise rivals' costs and target non-power buyers with unfavorable and discriminatory terms. The theory underlying *Kodak* speaks not only to tie-ins, but also to other seller power abuses such as forced exclusive dealing and vertical maximum price-fixing. The next section addresses this aspect of *Kodak*.

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<sup>60</sup> For another perspective on the interaction of *Kodak* and *Brooke Group*, see Peritz, *supra* note 6, at 896 n.19 (discussing how market realities and record facts take precedence over economic theory in determining liability).

<sup>61</sup> 85 F. 271, 292 (6th Cir. 1898). Salop attributes this insight to Alfred Kahn's careful reading of Judge Taft's opinion. See Salop, *supra* note 5, at 200 n.38.

<sup>62</sup> See Salop, *supra* note 5, at 194-201 (listing commonly occurring "traps" that cause courts to ignore evidence of actual anticompetitive effects).

## II. THE KODAK STORY

A. *Kodak's Relational Market Power—Sunk Costs and Information Asymmetries*

*Kodak* is about strategic behavior that targets small business in two ways. *Kodak's* tie-in of aftermarket parts and service: (1) was crafted to raise the costs of, or eliminate, its small business rivals in the service market and (2) allowed *Kodak* to charge discriminatory high prices for aftermarket parts and service to non-power buyers. *Kodak* possessed relational market power, the power that arises when enduring commercial relationships and sunk costs combine to give one party, often the seller, control over price, quality and output in dealings with a non-power possessing party. *Kodak* enjoyed this relational market power because of what is known as installed-base opportunism. Buyers of its micrographic equipment would have a sunk investment in its line of equipment, a non-recoverable or, in the Supreme Court's jargon, a switching cost incurred in giving up the *Kodak* line in favor of a rival's equipment.<sup>63</sup> This cost might be related to the depressed resale value of used *Kodak* equipment, the transaction costs involved in researching, negotiating, and implementing the purchase of a rival's line, or the time and investment in retraining employees to use the rival's products. Aside from any economic loss, there might also be a psychological constraint involved in switching equipment, particularly if this involved selling a machine that still has a substantial useful life. For managers of small firms that buy micrographic equipment infrequently, the instinctive reaction might be to keep the equipment until its useful life is over. The result of these sunk costs and psychological barriers to switching would be what the Supreme Court described as a lock-in. Buyers would be locked into *Kodak's* micrographic line and would be vulnerable to high prices for complementary products or aftermarket parts controlled by *Kodak*.<sup>64</sup>

Installed-base opportunism is of course related to informational problems. The seller's power is limited if the buyer, at the point of purchasing original equipment, can easily and accurately compare life cycle costs for rival offerings. The Supreme Court described the difficulties in engaging in accurate life cycle pricing.<sup>65</sup> The buyer cannot know at the time of purchasing original equipment the frequency and severity of breakdowns or the cost of purchasing aftermarket

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<sup>63</sup> See *Kodak*, 504 U.S. at 476-77.

<sup>64</sup> The *Kodak* case was focused on anticompetitive prices for the sale of aftermarket parts and service. There is no indication in the record that plaintiffs pressed any claims involving complementary parts used with *Kodak* equipment.

<sup>65</sup> See *Kodak*, 504 U.S. at 473-75.

parts or service. Parts suppliers and servicing firms may enter or leave the market during the life cycle of the equipment, so accurately predicting future market options for servicing will be impossible. If the original equipment buyer is told in advance that parts availability will be tied to the purchase of service from the manufacturer, the buyer will still have difficulty evaluating the value of the parts and service that will be received. Although the manufacturer's reputation may guide the buyer,<sup>66</sup> the quality and cost of the manufacturer's service may vary over the product's life cycle. The equipment buyer's difficulty in computing a life cycle price in combination with the substantial switching costs associated with abandoning an installed-base product leave the buyer vulnerable to opportunistic pricing for aftermarket parts that are manufactured or controlled by the seller.

The seller would have market power in the sale of aftermarket parts without imposing a tie-in. This power could be exercised, for example, by increasing price or by decreasing quality of aftermarket parts. As long as the seller controls access to critical parts, the seller can insist on high prices. If so, use of a tie that required a buyer of aftermarket parts to also purchase aftermarket service would be unnecessary to exploit the seller's market power. If the tie-in has additional anticompetitive effects, they still must be explained.

#### *B. The Kodak Tie-In as Strategic Behavior to Exclude Rivals and Effect Price Discrimination*

Much of the commentary on *Kodak* has focused on the informational problems (life cycle pricing) and sunk costs (lock-in) that are integral to the *Kodak* story. Harmful tie-ins are usually related to informational problems.<sup>67</sup> In contrast to bundling that may simplify a buyer's purchasing, all tie-ins complicate the buyer's desired transaction. Those tie-ins that most complicate buyers' decisions more acutely raise information problems. The bulk of the tie-ins that the Supreme Court has viewed skeptically over the past century have involved deferred purchases of the tied product, a circumstance that necessarily complicates the buying decision.<sup>68</sup> Conversely, the Court

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<sup>66</sup> The value of the manufacturer's reputation as a guide to the buyer can be limited if, for example, all major manufacturers of original equipment have established high prices for aftermarket parts and service, leaving the buyer with no clear competitive options in reducing those costs.

<sup>67</sup> See Richard Craswell, *Tying Requirements in Competitive Markets: The Consumer Protection Issues*, 62 B.U. L. REV. 661, 671-79 (1982) (discussing issues of fraud or surprise where the seller knowingly conceals the existence of the tying requirement); SULLIVAN & GRIMES, *supra* note 40, §§ 7.2, at 387-88, 7.2c3, at 405-06 (noting that informational deficiencies are a significant factor in determining a tie's anticompetitiveness).

<sup>68</sup> See *Kodak*, 504 U.S. 451 (1992); *N. Pac. Ry. Co. v. United States*, 356 U.S. 1 (1958) (land lease and sale contracts with a preferential routing clause requiring plaintiffs to purchase

has been somewhat more tolerant of tie-ins in which no deferred purchase is involved—the purchaser simultaneously purchases the tying and tied product.<sup>69</sup> How do these informational concerns apply to the parts-service tie-in at issue in *Kodak*?

The use of a tie-in on aftermarket parts and service was in itself not a deferred purchase tie-in—the parts and services were purchased simultaneously. But the purchase of both parts and service was deferred, sometimes long after the installed-base product was purchased. So informational issues are evident.

In defense of its behavior, Kodak urged that powerful and knowledgeable buyers were in a position to punish it if it charged supracompetitive prices for its aftermarket parts. Who were these power buyers and how could they control Kodak's pricing of aftermarket parts? Any purchaser of multiple units of Kodak's equipment would quickly learn a great deal about life cycle costs of maintaining this machinery. But these purchasers, individually and collectively, possessed power along with knowledge. They had the ability and the incentive to change their supplier of original equipment if life cycle costs were out of line and, in doing so, deprive Kodak of substantial market share, perhaps driving production and marketing below minimum efficient scale and, ultimately, pushing Kodak out of the micrographic equipment business. In the face of this substantial threat, Kodak singled out large buyers for favorable treatment.

Kodak apparently offered these power buyers attractive prices on aftermarket parts and the original Kodak equipment.<sup>70</sup> But Kodak wanted to preserve as much of its market power over the sale of aftermarket parts as possible. How could it do this? The obvious answer is to discriminate against non-power buyers and charge them a significantly higher price for aftermarket parts. But such discrimina-

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future rail transport service from defendants); *Int'l Salt Co. v. United States*, 332 U.S. 392 (1947) (salt refining equipment lease tied to future purchase of defendant's salt); *IBM Corp. v. United States*, 298 U.S. 131 (1936) (tabulating equipment lease tied to future purchase of defendant's punch-cards).

<sup>69</sup> See *United States Steel Corp. v. Fortner Enters., Inc.*, 429 U.S. 610 (1977) (credit financing tied to the simultaneous promise to purchase prefabricated house); *Times Picayune Pub. Co. v. United States*, 345 U.S. 594 (1953) (advertisers required to buy space in both morning and evening editions). *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2 (1984), also involved a simultaneous purchase, and, although that case did involve substantial information issues, was also found outside federal antitrust proscription. Of course, some non-deferred tie-ins have been held to be unlawful. See, e.g., *United States v. Loew's Inc.*, 371 U.S. 38 (1962). *Loew's* is a controversial but defensible holding. See SULLIVAN & GRIMES, *supra* note 40, § 7.2 at 421-424 (describing cases involving a non-deferred tied product).

<sup>70</sup> See *Kodak*, 504 U.S. at 457 (stating that Kodak "charges, through negotiations and bidding, different prices for equipment, service, and parts for different customers"). Later, the Court stated: "Kodak's own evidence confirms that it varies the package price of equipment/parts/service for different customers." *Id.* at 477.

tion might be undercut by arbitrage in the parts market. Large buyers might overbuy and sell their excess inventory of parts to service providers such as the plaintiffs, making it more difficult for Kodak to maintain its price discrimination scheme. Such arbitrage was likely if Kodak placed no restrictions on the sale of aftermarket parts and if the discrepancies in the prices it charged various buyers were large.

Kodak may have been more acutely concerned about its dwindling market share in providing service for its own line of equipment. Independent service providers, as long as they had ready access to Kodak parts, might service owners' equipment on terms superior to those that Kodak offered. Even if the independents had to pay high prices for Kodak parts, they might still undercut Kodak's combined price for service and parts.

Thus, the tie-in, along with Kodak's discriminatory exception that permitted continued sale of aftermarket parts to equipment owners who serviced their own equipment, allowed Kodak to target small buyers with discriminatory prices in two ways: (1) by lessening the risk of arbitrage in aftermarket parts sales and (2) by eliminating (or raising the costs of) independent service providers.<sup>71</sup> Using the tie-in, Kodak could now exercise its installed-base market power against small purchasers in a variety of ways: (1) by charging high prices on parts; (2) by charging high prices on service; (3) by lowering the quality of parts or service; or (4) by some combination of these actions. That Kodak did at least some of these things is consistent with evidence offered by the independent service providers that their service was preferred by some customers for its quality and cost components.<sup>72</sup>

The story of Kodak's conduct offered here is for the most part told in the Court's description of the plaintiff's theory of the case. What the Court failed to provide is a comprehensive picture of the tying seller's efforts to employ its market power strategically. Without the tie, Kodak could not have fully exploited its installed-base market power against non-power buyers. And without the tie, Kodak could not stifle competition from the small firms that were Kodak's direct rivals in providing service. A primary competitive benefit of countervailing power—that it can force power sellers to lower their

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<sup>71</sup> For a discussion of the use of market power to raise rivals costs, see Thomas G. Krattenmaker & Stephen C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over Price*, 96 YALE L.J. 209 (1986). In theory, the Kodak restriction allowed both large and small owners to purchase parts as long as they did their own servicing. But owners of only a few Kodak machines were unlikely to do their own servicing, so the policy favored large owners of multiple Kodak units.

<sup>72</sup> See *Kodak*, 504 U.S. at 465.

prices to more competitive levels for all customers—was blocked through a price discrimination scheme implemented by the tie-in.

### III. KODAK AND THE BOWMAN CRITIQUE OF LEVERAGE THEORY

Under traditional leverage theory, a monopolist or powerful tying seller was thought capable of using its power in one product market as a lever to extend power into complementary or related product markets. The theory postulated that the seller was in a position to increase anticompetitive gains beyond those that would be available if the seller operated only in its original market. In the tie-in context, the seller was able to extend its anticompetitive gains from the tying product market into the tied product market. A primary anticompetitive effect from leveraging was thought to be the foreclosure effect on rivals in the leveraged or tied product market.

In 1957, Bowman published an influential article challenging traditional leverage theory.<sup>73</sup> Bowman argued that most tying sellers could not increase overall return by leveraging. The tying seller could exploit its power in the tying product market without leveraging, or it could transfer some of its power into the tied product market, but it could not increase overall return through use of the tie. This was so because an informed buyer would calculate its limit price for the tying product, and would further determine the competitive price for the tied product, and would not pay more than the sum of the two prices. A simple example based on one used by the Supreme Court is a seller with market power in the flour market and no market power in the sugar market.<sup>74</sup> The seller requires the buyer to purchase together a package of flour and a package of sugar. Can the seller increase its supracompetitive return above the level that could be extracted if the flour and sugar were sold separately? The answer, probably, is no. If the consumer wants to buy only flour, the additional charge for the sugar may deter the buyer from buying the flour at all. Even if the buyer wants to buy both sugar and flour, the tying seller may not succeed in raising its return through use of the tie. The bundled sale price will be the sum of the buyer's limit price for flour and the competitive price for sugar. Because consumers can readily calculate the combined price, any price above that level will result in decreased sales that reduce seller profits.

Of course, the tie makes the consumer's comparison shopping more complex. A careless or inattentive consumer may fail to make

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<sup>73</sup> Ward S. Bowman, Jr., *Tying Arrangements and the Leverage Problem*, 67 YALE L.J. 19 (1957).

<sup>74</sup> See *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 6-7 (1958).



these simple but necessary calculations and pay too much for the bundled flour and sugar. But Bowman's analysis could still work if a significant body of informed consumers refused to pay a surcharge for the bundled items. As long as the seller cannot discriminate in the price charged to various types of consumers, the ignorant or careless consumer would gain from the price discipline imposed by the informed consumer. The tying seller would have little or nothing to gain through the tied sale of flour and sugar.

The Bowman critique of traditional leverage theory, initially embraced by Chicago theorists, continues to find favor among some commentators.<sup>75</sup> In the tie-in context, this critique attracted the votes of four concurring Justices in *Jefferson Parish Hospital District No. 2 v. Hyde*.<sup>76</sup> The critique is elegant, logical, and persuasive under its operative assumptions and has forced a healthy reexamination of leverage theory. But the Bowman analysis remains vulnerable.<sup>77</sup> Its validity can extend only as far as the soundness of its underlying assumptions. Two key assumptions are: (1) that the seller has substantial market power in the tying product that can be exercised without the tie-in and (2) that the market for the tied product remains effectively competitive after imposition of the tie (and in this way provides the buyer a competitive benchmark against which to measure the value of the seller's bundled products). If both of these assumptions hold, the tying seller could not enhance market power profits by leveraging into the tied product market. Instead, there would be a zero sum game in which profits are shifted back and forth between the tying and tied products, with no net gain to the seller. If one or both of the pivotal premises is lacking, the Bowman critique is flawed and traditional leverage theory may provide a more accurate description of the competitive effects of the tie-in.

#### *A. The Premise That Tying Sellers Have Exercisable Market Power in the Tying Product*

In most tie-in cases, the seller has substantial market power in the tying product, but it falls short of a textbook monopoly that allows full exploitation of monopoly profits. Kodak, for example, had sub-

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<sup>75</sup> See, e.g., HOVENKAMP, *supra* note 14, § 7.9, at 317-18 (describing leveraging as "a dubious theory whose main effect had been to preserve the Sherman Act as a small business protection statute").

<sup>76</sup> 466 U.S. 2, 36 (1984) (O'Connor, J., concurring). Justice O'Connor, after restating Bowman's critique of leveraging, concluded that "[t]ying may be economically harmful primarily in the rare cases where power in the market for the tying product is used to create *additional* market power in the market for the *tied* product." *Id.* (footnote omitted).

<sup>77</sup> A forceful critique of the Bowman thesis was offered in Louis Kaplow, *Extension of Monopoly Power Through Leverage*, 85 COLUM. L. REV. 515 (1985).

stantial power in the tying product market (aftermarket parts). Kodak probably had tight control only over those parts that were unique to the Kodak line, some of which were patented. Even if these parts were twenty percent or fewer of the parts needed to service a Kodak machine, an independent service provider could not effectively compete in servicing Kodak machines without access to these parts.<sup>78</sup> But tight control over these brand-specific parts might still confer insufficient power to impose supracompetitive prices on power buyers that possessed countervailing power. Without a workable price discrimination scheme, Kodak's power to raise prices on aftermarket parts could have been held in check by these power buyers.

By implementing the tie on aftermarket parts and service, and excluding from this tie only those (usually large) buyers who serviced their own equipment, Kodak should be able to implement a price discrimination scheme and limit arbitrage sales of parts. Kodak should also be able to eliminate or severely handicap independent service organizations that might discipline service prices. In this way, Kodak could reap supracompetitive gains against non-power buyers that were unattainable without the use of the tie-in. The essential premise of leveraging theory is thus vindicated, and the Bowman critique does not apply.

A critical question is whether Kodak's ability to expand anti-competitive gain through a tie-in would be, as Justice O'Connor suggested in *Jefferson Parish*, a rare event. If so, Bowman's thesis might describe the bulk of the cases in which a tie-in is challenged. But many of the underlying market conditions confronted by Kodak are anything but rare. Large and powerful buyers are ubiquitous in modern markets for products and services. That such powerful buyers will possess countervailing power that constrains even powerful sellers is also widely acknowledged. Porter's paradigm for measuring firm performance requires, for example, that the analyst measure whether the firm is constrained by power buyers or power sellers.<sup>79</sup>

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<sup>78</sup> A market definition that includes all aftermarket parts for Kodak machines has been criticized as illogical because the aftermarket parts did not compete against one another. See Herbert Hovenkamp, *The Reckoning of Post-Chicago Antitrust 8* (2000) (unpublished manuscript, on file with author). Properly viewed, however, the aftermarket parts that fit Kodak machines might be a cluster market—each of these products was needed in order for a service organization to provide full aftermarket service to owners of Kodak machines. But whether the market definition is considered a cluster, limited to a series of individual markets for parts that fit Kodak machines, or defined in some other way, the ultimate question remains the same: were there anticompetitive effects arising from Kodak's conduct? In the Court's view, the plaintiffs had offered relevant evidence tending to show anticompetitive effects. See *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 477 (1992).

<sup>79</sup> See PORTER, *supra* note 10.

The constraining role of power buyers is a reality that the federal agency merger guidelines also acknowledge.<sup>80</sup>

For additional evidence of the influence of power buyers, one need only look to the Supreme Court's pre-*Kodak* tie-in cases. For example, in *United States v. IBM Corp.*,<sup>81</sup> purchasers of IBM tabulating machines were required to purchase the tied product (punch cards that were run through the tabulating machines) only from IBM.<sup>82</sup> But IBM made an exception to the tie-in requirement for at least one major purchaser—the United States Government. Similarly, in *Northern Pacific Railway v. United States*,<sup>83</sup> the railroad imposed a tie-in that limited the freedom of purchasers or lessees of railroad-owned land to ship products produced on the land on rival railroads, but made exceptions for 390 (primarily large) shippers.<sup>84</sup>

The record in other Supreme Court tie-in cases does not disclose discrimination in favor of large buyers, but there is evidence that the tie-in may have been shaped by a desire to limit the impact of power buyers. For example, in *International Salt Co. v. United States*,<sup>85</sup> the tying seller of machinery for injecting salt into food products placed limitations on the purchasers' use of salt obtained from anyone other than the seller. One limitation allowed the purchaser of salt injection machinery to obtain a lower salt price from International only if International had offered that lower price to other customers.<sup>86</sup> This type of "most favored nation" provision can operate to control the incentives of both the seller and the buyer to negotiate discounts. The seller, when confronted with the demands of a power buyer for a lower salt price, will counter that it cannot offer the lower price without also lowering the price to other customers. The power buyers, in turn, may back down from their demands for a discounted price, realizing that they cannot obtain a price advantage over their rivals because the most favored nation clauses protect all customers. Reviewing the impact of these restrictions, *International Salt's* tie-in might

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<sup>80</sup> See DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 2.12 (rev. ed. 1997) reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104, at 20,569 (Apr. 8, 1997) (noting that large buyers may create conditions incenting firms to deviate from coordinated interaction in a market).

<sup>81</sup> 298 U.S. 131 (1936).

<sup>82</sup> See *id.* at 134.

<sup>83</sup> 356 U.S. 1 (1958).

<sup>84</sup> See *id.* at 2. The exceptions for the 390 shippers are described in two economists' analysis of the case. See F. Jay Cummings & Wayne E. Ruhter, *The Northern Pacific Case*, 22 J.L. & ECON. 329, 344-45 (1979).

<sup>85</sup> 332 U.S. 392 (1947).

<sup>86</sup> Another clause allowed a customer to obtain a lower price from International only if there was a general market reduction to that price level. See *Int'l Salt*, 332 U.S. at 396.

have been designed to facilitate cartel behavior at both the buyer and seller levels.<sup>87</sup>

This brief survey of Supreme Court cases suggests that the presence of power buyers that limit the tying seller's exercise of market power was not unique to the *Kodak* case. The survey also suggests that the seller whose exercise of market power is constrained by power buyers can use a tie-in in a number of ways to enhance supra-competitive returns (1) to suppress competition from small rival service providers that serve non-power buyers; (2) to foster a price discrimination scheme that limits arbitrage and targets non-power buyers; or (3) to facilitate cartel practices that limit competition in the tied product market. In any of these circumstances, the tie-in will increase the tying seller's anticompetitive gain and the Bowman critique will not apply.

### *B. The Premise That the Tied Product Market is Workably Competitive*

A second key premise of Bowman's critique is that before and after imposition of the tie, there is effective competition for the tied product. If this premise is not met, the buyer will lack competitive alternatives and a benchmark for measuring the value of the seller's combined offer. In either case, the buyer may end up paying a supra-competitive price.

Of course, in many cases, the tied product market may lack effective competition even before the tie is imposed. For example, the tied product market may be oligopolistic. This might explain the seller's incentive for imposing the tie-in—to participate in the supra-competitive gain available to participants in the tied product market. But leverage theory suggests more—that through imposition of the tie, competitive conditions are somehow worsened.

Why would a seller with coercive power decide to enforce a tie if, as Bowman's critique suggests, there would be no increase in overall return? Bowman's answer to this question was that tie-ins could serve various procompetitive purposes, such as providing a metering device for structuring charges based on the intensity of use of the tying product.<sup>88</sup> These and other potential procompetitive effects of tie-ins are addressed in the next section. But there is another and obvious reason why a seller with the power to coerce would impose a

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<sup>87</sup> See Grimes, *supra* note 32, at 300 ("A buyer of salt who knows that his competitors will be no more or less favorably treated may have reduced motivation for cost-conscious behavior. Sellers . . . who realized that International could retain its customers by merely meeting a competitor's offer might also be discouraged from competing for the salt business.")

<sup>88</sup> See Bowman, *supra* note 73, at 28.

tie: that it will increase the seller's overall supracompetitive gain by restricting competition in the tied product market.

Even if the tying seller has no market power in the tied product market, that market can become oligopolistic as the result of a wealth-enhancing tie-in that is copied by the seller's major rivals. Tie-ins that increase the tying seller's return are likely to be attractive to, and will be quickly copied by, the seller's rivals. In *IBM Corp. v. United States*, for example, the tie-in imposed by IBM had also been imposed by other sellers of tabulating machines.<sup>89</sup> Even if the tie-in does not foster copy-cat anticompetitive behavior, the tie-in, if it complicates the buyer's decision, can enable the seller to charge supracompetitive prices for the tied product.

In *Kodak*, the tied product was service on Kodak original equipment. Kodak may have been a monopolist in the service market when its original equipment was first introduced, but later lost market share to independent service organizations. The tie-in (selling aftermarket parts only to those who purchased Kodak service) made it difficult or impossible for independent service providers to obtain parts. This difficulty raised costs for the independent service rivals and drove some out of business. The tie-in, then, was a strategic move to preserve and restore Kodak's pre-existing power in the service market. The premise of Bowman's critique—that the tied product market was and remained effectively competitive—may have been approaching reality before the tie-in was imposed; that premise was thwarted by Kodak's strategic implementation of the tie.

The conditions that gave rise to this anticompetitive injury are likely to apply broadly when the seller of an installed-base product ties the sale of its aftermarket parts to the purchase of its service. In all such cases, there is a high risk that independent service providers will face increased costs or be driven from the market. The service provided by an original equipment manufacturer may be overpriced, shoddy, and unresponsive to the disciplining effect that independent service providers might otherwise generate.<sup>90</sup> Rival producers of original equipment may impose similar tie-ins, leaving even the most informed purchaser no real opportunity to shop for competitive aftermarket parts and service.

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<sup>89</sup> See *IBM Corp.*, 298 U.S. at 135.

<sup>90</sup> In franchising, a franchisee that is required to purchase input products only from a seller approved by the franchisor will suffer similar injury.

### C. Procompetitive Benefits of Tie-Ins

Bowman offered more than simply a critique of traditional leverage theory. He offered a new paradigm in which tie-ins might be viewed as natural and competitive responses to a variety of market circumstances. Unquestionably, bundled sales can promote competition. What appears to be a tie may be an efficient bundling desired by informed consumers. A right and left shoe are sold as a pair; a steering wheel and tires are sold as a part of an automobile. Properly applied, antitrust law would not consider such bundled sales to be tie-ins. A tie-in occurs only when the bundled sale is coerced—when a considerable body of informed consumers would prefer to buy the two products separately.<sup>91</sup>

A related concept is the use of a tie-in to force purchasers to do what is in their own best interest. If buyers don't have sufficient information to purchase the correct complementary products that will make a machine function properly, a seller of the machine might impose a tie to ensure that a suited product is purchased. This is the quality control defense. Although the defense has occasionally allowed a defendant to prevail,<sup>92</sup> its use is open to question if the tying seller might have simply provided information to buyers of the machine, indicating the quality or grade of complementary product that is needed to ensure proper functioning.

The list of potential benefits of a tie-in has been canvassed and analyzed elsewhere.<sup>93</sup> It is sufficient here to examine a benefit that Bowman accorded substantial weight: the metering hypothesis.<sup>94</sup> Bowman postulated that market power exercised through metered use of the tying product will reduce perverse allocative effects. If monopoly profits were extracted solely through high prices on the tying product (with no tie-in), infrequent users of the product might be unable or unwilling to purchase it. With the tie-in, the market-power profits could be more heavily extracted from the tied product, which, if it is complementary to the tying product, might be a measure of the intensity of use of the tying product. For example, if x-ray film is tied to the purchase of an x-ray camera, a buyer of the camera will pur-

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<sup>91</sup> Determining when two products are efficiently bundled can be problematic in high tech areas where new products or services are frequent and consumer buying patterns constantly changing. Thus, a major issue in the Antitrust Division's suit against Microsoft has been whether bundled software sales constitute an efficient bundling or a tie-in. See the discussion of this issue in *United States v. Microsoft Corp.*, 253 F.3d 34, 84-89 (D.C. Cir. 2001).

<sup>92</sup> See cases cited *infra* note 117.

<sup>93</sup> See, e.g., Grimes, *supra* note 32, at 284-92 (1994).

<sup>94</sup> See Bowman, *supra* note 73, at 23-24 (listing benefits of ties including efficient marketing or distribution of complementary products, maintaining quality control, and enhancing market entry or penetration).

chase the film in direct proportion to use of the camera. If the tying seller's market power is exercised by raising the price of the film, intensive users will end up paying a market-power premium. If the tying seller reduces its price for the tying product (the camera) to a level that resulted in more sales of that product, an allocative gain may be the result. But the surcharge for the tied product (the film) will distort use patterns for both products. For example, a high price for x-ray film will create a disincentive for intensive use of the x-ray camera. This distortion creates uncertain and potentially harmful effects on the primary as well as on downstream or secondary markets. Many less intensive users of an x-ray camera may be able to purchase it, but the machine may be inefficiently used because of the high cost of x-ray film.

As the preceding analysis suggests, the hypothesis that metering will produce allocative benefits is uncertain even under the theoretical market conditions that its proponents presume. These deficiencies are likely to be amplified under real market conditions. Sellers with market power are usually constrained by power buyers. If, as the factual underpinnings of *Kodak* suggest, tie-ins are often a tool for a power seller to extract gains from non-power buyers while excepting the power buyer, the allocative analysis is further skewed. Intensive users of the tying product will have to pay more, but only up to the point that they become sufficiently powerful to negotiate an exception to the tie-in. Power buyer exceptions to a tie can be documented not only in *Kodak* but in at least two other Supreme Court tie-in cases.<sup>95</sup> At best, then, the allocative effects of a tie-in operating under such real market conditions are highly ambiguous and may be harmful.

There is less ambiguity, however, about the wealth-transfer effects of a metering tie. All purchasers who end up paying more than the competitive price for the bundled products will suffer a wealth transfer loss. If Bowman's critique of leverage theory were widely descriptive, the wealth transfer losses suffered by buyers would be no greater as a result of use of a tie-in (although the wealth transfer payments might target different buyers). The previous analysis suggests, however, that under widely applicable conditions, a tying seller will increase anticompetitive gains through use of a metering tie-in, so wealth transfer losses will increase proportionately. Wealth transfer losses from exercises of market power are likely to be substantial,

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<sup>95</sup> See *IBM Corp. v. United States*, 298 U.S. 131, 134 (1936) (tie was not imposed against the government). In *Northern Pacific v. United States*, the railroad apparently did not impose the tie against 390 of its large customers. See *supra* note 83 and accompanying text.

probably significantly larger than the allocative losses associated with exercises of market power.<sup>96</sup>

Perhaps the point is obvious, but it warrants restating here: sellers don't engage in tying because it allocates products more efficiently. Ties are imposed to increase profits. Sellers are not prescient and will not know about the nuances of efficient allocation in the primary market, much less the secondary markets, that will be affected by the tie-in. The tying seller would not be heard to say: "Let's do this tie because it will more efficiently distribute our product." Instead, the seller would say: "let's do this tie because we can make more money." Granted that if markets (aside from the market power the seller possesses in the tying product) were competitive and buyers were prescient, making more money through a metering tie-in might lead to a more efficient allocation. But that is never evident in the litigated cases. A survey of the Supreme Court's tie-in cases and a sampling of roughly fifty court of appeals cases was unable to identify a single one in which the metering hypothesis would apply.<sup>97</sup> A separate analysis of *International Salt*, a case that some have suggested fits the metering hypothesis, concluded that a metering explanation is unlikely.<sup>98</sup>

Finally, even if all of the factual suppositions for efficient metering were in place, there are likely to be more efficient and less harmful ways of measuring and charging for intensity of use of the tying product.<sup>99</sup> For example, franchisors can require franchisees to use computerized cash registers that make a record of every sale of a franchised product. By avoiding use of tie-ins, the tying seller can adjust pricing to intensity of use without the anticompetitive effects attending many tie-ins. A seller that abjures the use of such readily available (and less anticompetitive) metering mechanisms is vulnerable to the conclusion that it chose the tie-in for anticompetitive gain.

#### IV. OBJECTIONS TO KODAK

Critics of the *Kodak* decision have raised a variety of objections, including (1) that *Kodak* is revolutionary and will spark a flood of

<sup>96</sup> In the neo-classical economist's model, monopoly profits (wealth transfer) are represented by a rectangle that may have twice the volume of the triangle representing allocative or deadweight losses. See DENNIS W. CARLTON & JEFFREY M. PERLOFF, *MODERN INDUSTRIAL ORGANIZATION* 135, fig.5.2 (2d ed. 1994) (depicting monopoly profit maximization). See also HOVENKAMP, *supra* note 14, § 1.3c, at 20-23 (explaining that much of what might have been the wealth transfer loss will be eaten up by entrenching or rent-seeking behavior).

<sup>97</sup> See Grimes, *supra* note 32, at 299-315.

<sup>98</sup> See John C. Peterman, *The International Salt Case*, 22 J.L. & ECON. 351, 352-59 (1979).

<sup>99</sup> See Kaplow, *supra* note 77, at 541-42 (defining metered pricing and alternatives in relation to tying arrangements).



meritless or unwise litigation; (2) that the information theories underlying *Kodak* do not raise legitimate antitrust issues and should be addressed, if at all, through contract remedies or consumer protection law; (3) that the decision will create cost, uncertainty, and administrative nightmares for litigants and courts because of the complexity of the required analysis; and (4) that workable remedies for antitrust violations based on *Kodak* are difficult or impossible to devise. For the most part, these objections do not question that abusive or anticompetitive conduct could occur as the result of the relational market power identified in *Kodak*, but rather focus on whether antitrust law can or should address these issues.

#### A. Is *Kodak* Revolutionary or Evolutionary?

Justice Scalia's dissent in *Kodak* provided a preview of the arguments that critics have advanced in challenging *Kodak*. The dissent suggested that the majority's holding would unleash a torrent of litigation against every producer of original equipment that sold aftermarket parts.<sup>100</sup> Indeed, the relational market power that was at issue in *Kodak* extends to franchise relationships or to any enduring economic relationship in which one firm is locked in as the result of sunk costs.

In the ten years since *Kodak*, plaintiffs have sought to rely on *Kodak*'s holding primarily in aftermarket cases and in franchise cases. The majority of the reported cases were victories for the defendant.<sup>101</sup> Whatever the outcome, two questions arise: (1) would the application of *Kodak* principles in these cases abruptly alter or revolutionize the law and (2) would such an application produce a torrent of litigation that is inconsistent with fundamental antitrust principles?

*Kodak*'s focus on information imperfections as a basis for finding a coercive tie-in is novel in Supreme Court cases. But it also has great descriptive power in explaining older cases that had found unlawful ties. At least on six occasions prior to *Kodak*, the Supreme Court ruled for the plaintiff in a tie-in case involving deferred purchases of the tied product and, transparently, significant information issues.<sup>102</sup> Information issues were not squarely addressed in any of

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<sup>100</sup> See *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 489 (1992) (Scalia, J., dissenting).

<sup>101</sup> See *infra* Part V.

<sup>102</sup> See *FTC v. Texaco Inc.*, 393 U.S. 223 (1968) (alleging oil company induced gas stations to buy tires, batteries, and accessories); *Perma Life Mufflers, Inc. v. Int'l Parts Corp.*, 392 U.S. 134 (1968) (conditioning award of a franchise on purchase of Midas Muffler products); *Atlantic Ref. Co. v. FTC*, 381 U.S. 357 (1965) (alleging tire company required ARCO dealers to buy its products); *No. Pac. Ry. Co. v. United States*, 356 U.S. 1 (1958) (alleging that Railway induced lessees to use only freight transport as condition of awarding the lease); *Int'l Salt Co. v.*

these opinions nor, apparently, were they briefed by the parties. Pre-1980 tie-in decisions rarely addressed information issues for the simple reason that theorists had not made the necessary connection between the tying seller's coercive power and possible information inadequacies of the buyer. It was not until Craswell's 1982 article that information issues were out of the closet.<sup>103</sup>

*Kodak* analysis offers potential insight and explanatory power in re-examining these old cases.<sup>104</sup> Vindication of past rulings on new or different grounds cannot fairly be labeled revolutionary. A reassessment based on new market insights offers hope of greater clarity and certainty in future counseling, enforcement choices, and court decisions. The broader or revolutionary implications of *Kodak*, whatever they might be, have yet to be demonstrated in the case law.

### B. Do Information Theories Underlying *Kodak* Raise Legitimate Antitrust Issues?

Justice Scalia's dissent argued that whatever information imperfections may arise in tie-in cases such as *Kodak* do not implicate antitrust: "this 'circumstantial' leverage created by consumer investment regularly crops up in smoothly functioning, even perfectly competitive, markets, and in most—if not all—of its manifestations, it is of no concern to the antitrust laws. . . . [The leverage] produces only 'a brief perturbation in competitive conditions—not the sort of thing the antitrust laws do or should worry about.'"<sup>105</sup>

Information issues have been a part of antitrust analysis for the better part of a century. In Justice Brandeis' influential 1918 opinion in *Chicago Board of Trade v. United States*,<sup>106</sup> the Board had issued a rule freezing the price at the closing market level for after-hours trades of grain futures. The Government attacked the rule as unlawful price-fixing. In upholding the rule under rule of reason analysis, the Court cited in support the information inadequacies confronting after-hours traders.<sup>107</sup> The high Court's most recent acknowledgment of the relevance of information issues came in *California Dental Ass'n*

United States, 332 U.S. 392 (1947) (conditioning lease of salt refining equipment on future purchase of defendant's salt); *IBM Corp. v. United States*, 298 U.S. 131 (1936) (alleging that defendant's tabulating equipment lease was tied to future purchase of punch-cards).

<sup>103</sup> See Richard Craswell, *Tying Requirements in Competitive Markets: The Consumer Protection Issues*, 62 B.U. L. REV. 661, 671-78 (1982) (identifying three types of informational deficiencies).

<sup>104</sup> See Grimes, *supra* note 32, at 299-307 (reassessing past Supreme Court holdings in light of *Kodak*).

<sup>105</sup> *Kodak*, 504 U.S. at 497-98 (quoting *Parts & Elec. Motors, Inc. v. Sterling Elec., Inc.*, 866 F.2d 288, 236 (7th Cir. 1998) (Posner, J., dissenting)).

<sup>106</sup> 246 U.S. 231 (1918).

<sup>107</sup> See *id.* at 244-45.

v. *FTC*.<sup>108</sup> Whether the Court's analysis in these cases was correct can be debated. The point is that buyers' ability to assess and weigh information has long been a part of the fabric of antitrust decision.

Information and lock-in issues have also played a silent but pivotal role in cases involving small players that are likely targets of relational market power. *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*<sup>109</sup> is a prime example. A ski lift operator brought a section 2 action claiming that a larger rival firm's refusal to continue past cooperation in issuing all-area lift tickets constituted a monopoly abuse. The Supreme Court affirmed lower court decisions that found a section 2 violation. The relevant market issue was not open at the point of review, so the Court accepted the Aspen area resorts as the appropriate market. Yet, in the words of one commentary, one town "cannot possibly be a plausible relevant geographic market for downhill skiing services provided by destination ski resorts."<sup>110</sup> One might still defend the *Aspen* result based on harm to the small percentage of local users of the ski facilities. Still, eight years after the Court's decision, the larger resort was allowed to purchase its smaller rival without any challenge under the merger laws, an enforcement decision that suggests that there was not a significant local relevant market that would be at risk.<sup>111</sup>

The *Aspen* result does make sense, however, as an exercise of relational market power that was harmful to consumers. The defendants terminated all-area lift tickets that had been initiated when Aspen had only three resorts, each under separate ownership. All-area lift tickets were apparently efficient. Similar tickets are issued at destination ski resorts throughout the world. And record evidence indicated that Aspen skiers preferred to have the option of purchasing an all-area ticket.<sup>112</sup> So the plaintiff might quite logically make investments in its resort, some of which would be sunk or unrecoverable, based on the assumption that efficient cooperation in issuing all-area lift tickets would continue. Indeed, the cooperation did continue until the larger rival ended up with three of the four local resorts, and was in a position to profit at its smaller rival's expense by offering three-area tickets that excluded the plaintiff's ski lifts. These three-area

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<sup>108</sup> See 526 U.S. 756, 778 (1999) ("The existence of significant challenges to informal decisionmaking by the customer for professional services suggests that advertising restrictions arguably protecting patients from misleading or irrelevant advertising call for more than cursory treatment . . .").

<sup>109</sup> 472 U.S. 585 (1985).

<sup>110</sup> DANIEL J. GIFFORD & LEO J. RASKIND, *FEDERAL ANTITRUST LAW, CASES AND MATERIALS* 386 (1998).

<sup>111</sup> See *Ski Merger May Perk up Aspen*, N.Y. TIMES, Nov. 20, 1993, § 1, at 37.

<sup>112</sup> See *Aspen*, 472 U.S. at 605-07 (surveying expert testimony and anecdotal evidence of consumer preference).

tickets were not the most efficient marketing mechanism (because they were not the consumer's preference), but they raised the costs of plaintiff, allowed the defendant to profit at the plaintiff's expense, and put pressure on the plaintiff to sell out at a depressed price. Plaintiff's resort would be worth less because the pattern of efficient cooperation that had been the basis of past sunk investments had now been terminated.

Relational market power may also be a basis (frequently unstated) for sustaining antitrust claims brought by employees. In *Law v. National Collegiate Athletic Ass'n*,<sup>113</sup> a class of entry level assistant basketball coaches successfully sued the NCAA based on a rule that limited to \$16,000 the salary that Division I schools could pay these coaches. Member schools were allowed to hire up to four full-time coaches, but the NCAA rule was designed to limit the amount that its member schools could pay to the fourth coach. The court of appeals affirmed the district court's judgment that the NCAA's action was unlawful price-fixing under a truncated rule of reason analysis. As in *Aspen*, the relevant market was not defined. To make sense, however, a price-fixing claim must assume that the defendants exercised power over a market consisting of this narrow class of assistant basketball coaches working for a group of NCAA member schools. Yet any person working in such a position would have other basketball coaching positions available at other NCAA schools, junior colleges, professional or semi-professional teams, in high schools, or in community or youth programs.<sup>114</sup>

In explaining its holding, the court of appeals looked to the anti-competitive effects of the price-fixing arrangement. There was undisputed evidence that the rule resulted in lowering the pay for many of the coaches holding the fourth full-time position.<sup>115</sup> The market power that the NCAA might exercise over this narrow class of assistant coaches may be linked to the reputation of basketball programs at Division I schools. Working for such a program, even if it had a consistent losing record, might be seen as a good experience for a novice coach seeking to build a resume. But there is also a link to the sunk costs that any employee has in a permanent position.<sup>116</sup> To accept another position, the employee must contemplate the costs of a job

<sup>113</sup> 134 F.3d 1010 (10th Cir. 1998).

<sup>114</sup> The NCAA argued for such a broader market definition. See *id.* at 1019 n.12.

<sup>115</sup> See *id.* at 1020 ("The NCAA adopted the REC ("restricted earnings coach") Rule to reduce the high cost of part-time coaches' salaries, over \$60,000 annually in some cases, by limiting compensation to entry-level coaches to \$16,000 per year. The NCAA does not dispute that the cost-reduction has effectively reduced restricted-earnings coaches' salaries.").

<sup>116</sup> For a discussion of the relational market power that employers often have in dealings with employees, see Grimes, *supra* note 18, at 199-200, 201-04.

search, of learning to work with new people and under different conditions and rules, and probably of moving possessions and family to a new location, a move that may involve selling one house and purchasing another. These costs are not so high as to deter employees from searching for new opportunities, but they are sufficiently high to give additional power to an employer in bargaining with an employee. The NCAA case, then, is illustrative of employee antitrust claims that involve a significant albeit usually unmentioned component of relational power built upon information and lock-in realities.

In tie-in cases, information issues also have a venerable tradition, albeit the pre-*Kodak* history was almost exclusively on the defense side. Defendants have argued, sometimes successfully, that a tie-in may be required to assure that complementary products used with the tying product are of an adequate quality to ensure that the tying product functions properly (and that the tying seller's quality reputation is not undermined).<sup>117</sup> The quality control defense is based on the premise that the purchaser has insufficient information or understanding to make wise choices for the complementary product. This information-based defense is well-anchored in tie-in law and has been endorsed by Chicago theorists such as Bork.<sup>118</sup>

Can it be that information-based theory is appropriate fodder for the defendant but not for the plaintiff? Such a discriminatory approach is difficult to justify. But some critics of *Kodak* suggest that while plaintiffs may raise legitimate information-based issues in the context of a tie-in, those issues should be addressed through contract law or consumer protection law, not through antitrust law.

### 1. Contract Law As an Alternative Remedy

Protecting the integrity of the contract enforcement system against antitrust incursions is a worthy goal if contract law provides better or more refined remedies for information-based competition abuses.<sup>119</sup> But proponents of this view apparently favor contract law

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<sup>117</sup> For example, the quality control defense was invoked in three cases involving an automobile manufacturer's requirements that dealers purchase only manufacturer approved spare parts. The defendants prevailed in *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792 (1st Cir. 1988) and in *Mozart Co. v. Mercedes-Benz of N. Am., Inc.*, 833 F.2d 1342 (9th Cir. 1987). A jury verdict for the plaintiff was upheld in *Metrix Warehouse, Inc. v. Daimler Benz Aktiengesellschaft*, 828 F.2d 1033 (4th Cir. 1987).

<sup>118</sup> See ROBERT BORK, *ANTITRUST PARADOX* 380 (1978) ("The problem is one of information and policing. The manufacturer is likely to understand the technical problems of his machines better than the lessees.").

<sup>119</sup> See, e.g., Benjamin Klein, *Market Power in Franchise Cases in the Wake of Kodak: Applying Post-Contract Hold-Up Analysis to Vertical Relationships*, 67 *ANTITRUST L.J.* 283 (1999) (offering support for this view). I offered a different view in Warren S. Grimes, *Market Definition in Franchise Antitrust Claims: Relational Market Power and the Franchisor's Con-*

in part because it does not provide remedies for claims that might be heard under the Sherman Act.<sup>120</sup> Contract-based remedies, assuming they are available, will be unlikely to address competition issues adequately. Preserving or protecting competition is not a primary policy goal of contract enforcement. Perhaps most decisively, it would be foolish to carve out of tie-in cases information issues that are integrally related to the competitive assessment of the tie-in. For example, tie-ins may have cartel enhancement effects (an issue theorists would generally agree is within the parameters of an antitrust claim). But a tie-in's cartel enhancement effects can be increased if the tie-in exploits the buyer's information inadequacies. A court should not be forced to put on blinders when making an assessment of factors that might enhance or mitigate these cartel effects. Just as a defendant is able to raise information inadequacies as a part of a quality control defense for a tie-in, a plaintiff must be allowed to raise information issues that might exacerbate the anticompetitive effects of a tie-in.

As an example of the potential overreaching impact of *Kodak*, critics point to the simple contract holdup. If a landowner contracts to have a building constructed, the contractor, after doing substantial construction work, might delay performance and demand additional compensation as a condition for going forward. As a result of the landowner's sunk investment in the contract and the high cost in negotiating with a new contractor, the landowner may be coerced into additional payments.

A contractor that engages in such holdup behavior is not an appropriate antitrust target. But how is this behavior to be distinguished from the facts in *Kodak*? The answer lies in antitrust's commitment to address only those competitive abuses that arise from an exercise of market power. *Kodak* suggests such an abuse of market power. The tie-in allowed *Kodak* to raise prices, limit output, or reduce the quality of aftermarket parts and service. If the abuse substantially raised *Kodak*'s anticompetitive gain, one could anticipate that similar ties would be adopted by rivals and by other sellers of installed-base products. In contrast, the contract holdup may not involve market power as understood in antitrust. The starting point for a definition of market power is the ability to limit output and raise price without incurring a decrease in sales such as to make the price rise unprofit-

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*flict of Interest*, 67 ANTITRUST L.J. 243 (1999) (arguing that franchisors exercise relational market power over franchisees and contract-based remedies are insufficient to prevent such anticompetitive activity).

<sup>120</sup> See Klein, *supra* note 119, at 325 n.104 (arguing that contract law should be favored because it is less likely than antitrust law to interfere with literal enforcement of contract language).

able.<sup>121</sup> But there is more to an antitrust definition of market power. In particular, theorists generally agree that market power does not include temporary market perturbations<sup>122</sup> such as might occur in the contract hold-up. A contract hold-up might cross the market-power threshold only if it occurs in the context of an enduring economic relationship in which continuing or repeated exercises of power are possible.

Tie-in law, as circumscribed by the Supreme Court, also contains a requirement that in order to prevail, a plaintiff must demonstrate that the tie-in involves substantial commerce in the tied product.<sup>123</sup> A contract hold-up involving a one-time contractual relationship often will not involve a significant amount of commerce in the tied product market. These distinctions offer a principled basis for distinguishing a contract hold-up from a legitimate antitrust claim. That application of these principles can be difficult in factually complex cases affords no basis for abandoning legitimate antitrust tie-in claims.

## 2. Consumer Protection Law As an Alternative Remedy

Other critics of *Kodak* have suggested that the remedy for information abuses that underlie a tie-in should be through consumer protection law. This was Justice Scalia's view expressed in the dissent and was the suggestion of Craswell in his landmark 1982 article that first analyzed the risks of information abuses in tie-ins.<sup>124</sup>

Statutes that address deceptive advertising and consumer deception have a long history and substantial judicial interpretations to guide their application. But consumer deception laws primarily address deceptive or misleading statements, not the lack of information that may be the basis of a tie-in's anticompetitive effects. Although competition issues sometimes guide consumer protection enforcement, these laws are not primarily concerned with anticompetitive effects. A deceptive advertisement that materially deceives consumers can be unlawful regardless of its competitive effects or, indeed, even if there is evidence that the deceptive ad might have procompetitive effects. A seller that deceives the public about the source of a product will be guilty of deceptive advertising even if its price/quality mix is superior to all rival products, including the one that the de-

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<sup>121</sup> See SULLIVAN & GRIMES, *supra* note 40, § 2.2, at 22.

<sup>122</sup> See *id.* § 2.2, at 23.

<sup>123</sup> See *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 462 (1992).

<sup>124</sup> See *id.* at 495 (Scalia, J., dissenting); Craswell, *supra* note 103, at 679-81 (comparing consumer concern regarding tie-ins with unenforceable contract clauses placing unconscionable obligations on buyers).

ceived consumer thought it was purchasing.<sup>125</sup> There is no consumer protection remedy that will allow a seller to avoid the information losses (arising from inadequate consumer information about properly performing complementary products) that are the basis for invoking the quality control defense to a tie-in claim. Likewise, there is no established consumer protection remedy for addressing a tie-in's anti-competitive effects that spring from a lack of buyer information about life cycle pricing or related matters. Neither a defendant invoking a quality control defense nor a plaintiff seeking to demonstrate a tie-in's anticompetitive effects should be precluded from introducing evidence of informational problems because of any pretense that consumer protection law adequately addresses the issue. Those who say that the remedy for a tie-in's information problems should lie with consumer protection law may be advocating no remedy.<sup>126</sup>

Even assuming that there were a consumer protection remedy for exploitation of the lack of consumer information in a tie-in, it is unclear how the consumer protection issues would be separated from the tie-in's anticompetitive effects. The anticompetitive effect of a harmful tie-in is frequently linked to the deferred purchase of the tied product, a circumstance that usually raises information problems. But that same tie-in may raise a number of other competition issues, including: (1) raising the costs of or foreclosing rivals in the market for the tied product; (2) implementing a price discrimination scheme that targets small buyers; or (3) fostering cartel practices among rivals of the tying seller or among purchasers of the bundled products. These anticompetitive effects, although they could occur in a world of perfect information, can be exacerbated by information inadequacies. For example, if the information deficiencies of purchasers are substantial and widespread, this will likely increase the tie's effectiveness in attaining any of the three listed anticompetitive effects.

*Kodak* illustrates this difficulty in separating information issues from other anticompetitive effects. If *Kodak's* tie of aftermarket parts and service is successful in part because of consumer difficulty in projecting life cycle costs, this success will contribute directly to the tie's other anticompetitive effects. The tie will be more effective in effecting a price discrimination scheme and will give *Kodak* more

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<sup>125</sup> Deceptive advertisements about the source of a product would violate section 43 of the Lanham Act, 15 U.S.C. § 1125 (1998) (private enforcement), Section 5 of the FTC Act, 15 U.S.C. § 52 (1998) (FTC enforcement), and numerous state law provisions (private or state enforcement).

<sup>126</sup> In his dissent, Justice Scalia did not contend that *Kodak's* conduct violated any consumer protection law. He asserted only that the conduct "may have implicated truth-in-advertising or other consumer protection concerns." *Kodak*, 504 U.S. at 494-95 (Scalia, J., dissenting).



power to affect price, quality and output of the bundled products. Rivals in the service market will face higher costs in obtaining after-market parts and may be foreclosed entirely from the Kodak service market.

### C. *The Cost and Workability of Kodak Theories*

Another concern is that *Kodak* claims will confront counselors and courts with difficult and intractable issues that are beyond their powers to resolve.<sup>127</sup> *Kodak* itself is a complicated three level case involving an installed-base product, and a second-level tie-in linking aftermarkets for parts and service. On remand, the tie-in issue was sufficiently complex that the plaintiff's attorney chose not to pursue it, relying only on the section 2 monopolization claims.<sup>128</sup>

One cannot be sure what future use will be made of *Kodak*. It is possible that future litigants will propose creative but complex case theories that will severely challenge juries and courts. So far, at least, that has not happened. In reported lower court decisions,<sup>129</sup> *Kodak* has been relied upon primarily in tie-in cases brought under section 1 or section 2 of the Sherman Act. One can foresee that *Kodak*'s information analysis will apply for other claims in which a seller's power dictates downstream behavior for a relatively powerless buyer. Thus, some exclusive dealing and vertical maximum price-fixing cases will include *Kodak* issues.

But all of these claims are traditional antitrust claims. *Kodak*'s information analysis would be a supplement to traditional analysis, not a new paradigm that discards past law. In many cases, the supplement would be enlightening and clarifying, one that could lead to greater confidence and predictability in the results. As courts become more experienced in addressing information issues, presumptions and precedents can provide further guidance, some of it helpful to defendants in obtaining dismissal of non-meritorious actions, some of it helpful to plaintiffs in demonstrating genuine anticompetitive conduct.

An example is the significance of a tie-in involving a deferred purchase of the tied product. Tie-ins that involve simultaneous purchase of both the tying and tied product may be anticompetitive, but they are less likely to raise information issues than ties that require the buyer to continue to purchase the tied product over a long or indefinite period. The life cycle pricing issues of *Kodak* arose because

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<sup>127</sup> See Hovenkamp, *supra* note 78, at 8-9.

<sup>128</sup> See *Image Tech. Servs., Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1202 (9th Cir. 1997).

<sup>129</sup> See *infra* Part V.B (surveying cases that followed or declined to follow *Kodak*).

purchase of both the tying and tied product was deferred, sometimes long after the purchase of the original equipment. These issues may not come up when there is no deferred purchase of either the tying or tied products. Some clarifying precedents, or even a presumption, might arise out of this simple, common sense observation. For example, courts might well decide to shift the burden of persuasion as to information claims depending on whether deferred purchases are involved.

With time and experience, courts will have an opportunity to pinpoint other critical factors.<sup>130</sup> For example, if the tie is imposed uniformly against all buyers, it will not discriminate against non-power buyers, a fact that may support a valid defense such as the quality control defense. A uniformly imposed tie may still have cartel enhancing effects, but the Court's competitive inquiry can be guided and narrowed through sensitivity to this factor.

#### *D. Are there Workable Remedies for Kodak Claims?*

One of the objections to *Kodak* theories has been a perceived difficulty in fashioning a remedy. In cases involving abuse of after-market product, it has been suggested that a court must respond not only by forcing a sale of aftermarket products, but "must also set the price at which these things are to be sold, and perhaps other terms as well."<sup>131</sup>

Many tie-in cases that might be brought under a *Kodak* theory would not involve aftermarkets. Tie-ins in franchising cases, for example, typically involve a forced tie of input goods that the franchisee resells to customers.<sup>132</sup> If such ties are found to be unlawful, the simplest of injunctive provisions would address the abuse: order the franchisor to stop requiring franchisees to purchase the input product only from the designated vendor. Of course, the plaintiff may also seek damages, and this may present the parties and the court with more difficult evidentiary problems. There is, however, nothing novel about damage claims in franchise tie-in cases, and nothing in *Kodak* that would make the burden of proving damages more difficult. The damages caused by the tie will not change simply because of a refinement in the underlying reasoning that led the court to conclude

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<sup>130</sup> See Grimes, *supra* note 32, at 273-79 (suggesting such factors as the complexity of the purchase decision, the frequency with which the product is required by the buyer, and the disparity in value between the tying and tied products).

<sup>131</sup> Hovenkamp, *supra* note 78, at 7.

<sup>132</sup> See, e.g., *Queen City Pizza v. Domino's Pizza, Inc.*, 124 F.3d 430, 433 (3d Cir. 1997) (requiring franchisee to purchase franchisor's pizza dough); *Siegel v. Chicken Delight*, 448 F.2d 43, 46 (9th Cir. 1971) (requiring purchase of supplies); *Collins v. Int'l Dairy Queen*, 59 F. Supp. 2d 1312, 1313 (M.D. Ga. 1999) (requiring purchase of food products).

that the tie was unlawful. If the plaintiff cannot bear its burden of proving damages, then damage relief should be denied, but that is no reason to deny a simple and effective injunction that would halt the abusive practice.

Cases involving claims of aftermarket abuse are, like franchise tie-in claims, not new to antitrust.<sup>133</sup> One type of aftermarket case involves efforts by a manufacturer to prevent dealers from selling spare parts produced or distributed by non-approved sources. Here again, simple injunctive relief should be effective (requiring the manufacturer to allow dealers to purchase from other sources). Where the tie-in, as in *Kodak*, was an effort to restrict or eliminate competition in the service market by limiting the sale of spare parts, the injunctive relief could be more complex. But this sort of relief should generally not require the court to become involved in the price or terms of sale. The injunction might simply require that the parts be sold to all comers on non-discriminatory terms, or that the manufacturer cease efforts to restrict the flow of parts to independent service providers. As to damages, the same points addressed in connection with franchise tie-ins are relevant here: the burden is on the plaintiff to establish damages and failure to bear that burden means that damage relief would be denied.

The great bulk of cases involving seller power abuses, whether those claims be based on tie-ins, forced exclusive dealing, or vertical maximum price-fixing, involve traditional antitrust law. The circumstance that a plaintiff might rely on a *Kodak* theory to establish a violation generally does not make the crafting of a remedy more or less complicated than would have occurred in a pre-*Kodak* era. To the extent *Kodak* takes courts into new or uncharted territory, there may be instances in which practical remedies are illusive or administratively infeasible. But those uncertain future cases are no reason to excuse anticompetitive conduct in mainline antitrust claims.

#### V. *KODAK* IN THE COURTS

Measured only by the frequency of citations, *Kodak* has had substantial impact on lower court decisions. Many of these citations have been to *Kodak's* recitation of the standards for summary judg-

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<sup>133</sup> See, e.g., *Pick Mfg. Co. v. Gen. Motors Corp.*, 299 U.S. 3, 3 (1936) (manufacturer required car dealers to use only new parts manufactured or approved by manufacturer); *United Shoe Mach. Corp. v. United States*, 258 U.S. 451, 456 (1922) (lease provisions required lessees to use lessor's machinery or forfeit right to its use); *Metrix Warehouse, Inc. v. Daimler-Benz Aktiengesellschaft*, 828 F.2d 1033, 1034 (4th Cir. 1987) (car dealership franchisor required franchisees to buy replacement parts only from franchisor).

ment.<sup>134</sup> This aspect of *Kodak* may have been somewhat obscured by the subsequent language in *Brooke Group*.<sup>135</sup> Moreover, citations to standards for granting or denying summary judgment are often perfunctory; after disposing of this necessary preliminary, the court proceeds to follow its own predispositions. *Kodak* notwithstanding, those predispositions are likely to be linked to the credibility that a judge grants to an economic theory and, in particular, to the court's willingness to address squarely the evidence (or lack of evidence) of actual anticompetitive effects.

Below *Kodak's* impact on federal and state antitrust litigation is addressed on two levels that are most likely to indicate the decision's longer term impact: (1) *Kodak* as a symbol of empiricism in antitrust, or as a reminder that evidence of actual anticompetitive effects (or the absence of those anticompetitive effects) should trump rote application of screening rules or doctrines that might dictate the outcome of the case and (2) *Kodak* as a precedent for looking to information inadequacies and the coercive effect of sunk investment in antitrust claims involving alleged seller power abuses (tie-ins, forced exclusive dealing, vertical maximum price-fixing, and related section 2 claims).

#### A. *Kodak and Empirical Analysis*

As described above in Part I.D.2, doctrinal developments in Sherman Act interpretation often lead to a period of mechanical or rote application to widening fact patterns. Screening rules developed to check perceived enforcement excesses of the Populist era are a prime example. Over time, lawyers and courts have predictably fallen into patterns of extending these rules to fact patterns that overreach the rule's empirical validity. That is why *Kodak's* call for returning to fundamental antitrust principles—asking whether a particular behavior produces anticompetitive effects—is critical. Looking at the ensuing decade, an observer might single out a number of cases where this rule was followed or ignored.

In *FTC v. Staples, Inc.*,<sup>136</sup> the agency successfully blocked a proposed combination of the two largest discount office supply chains in the country. The case was unusual for its use of direct pricing evidence to show that prices tended to be higher in cities in which only

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<sup>134</sup> See, e.g., *Rossi v. Standard Roofing*, 156 F.3d 452, 466 (3d Cir. 1998) ("In evaluating the sufficiency of the evidence, facts and inferences must be viewed in the light most favorable to the party opposing summary judgment."); *PSI Repair Servs. v. Honeywell, Inc.*, 104 F.3d 811, 814 (6th Cir. 1997) (reciting similar summary judgment standard); *City of Long Beach v. Standard Oil Co.*, 46 F.3d 929, 934 (9th Cir. 1994) (same); *Amerinet, Inc. v. Xerox Corp.*, 972 F.2d 1483, 1495 (8th Cir. 1992) (same).

<sup>135</sup> See *infra* Part I.D.

<sup>136</sup> 970 F. Supp. 1066 (D.D.C. 1997).

one office superstore operated than in areas in which two or more superstores were present.<sup>137</sup> This direct empirical support allowed the FTC to defend an unusually narrow market definition—a market consisting only of office supply superstores—in the face of the defendants' claims that customers could purchase office supplies from a variety of other types of stores. In sustaining the FTC's position, the court did not cite *Kodak*, but its holding was consistent with Justice Blackmun's focus on real market evidence of anticompetitive effects.

In *Toys "R" Us, Inc. v. FTC*,<sup>138</sup> the agency again prevailed in court on what some might perceive as a vulnerable market definition. Toys "R" Us ("TRU") was found to have violated the Sherman Act and the FTC Act through its efforts to organize toy manufacturers to limit sales to the warehouse clubs, perceived by Toys "R" Us as a threat to its leading position as a toy retailer. Although Toys "R" Us sold more than forty percent of the toys sold in some urban markets, its overall share of retail sales of toys in the U.S. was only about twenty percent.<sup>139</sup> But the court of appeals was unconcerned with this relatively small market share because of the demonstrated anticompetitive effects of the defendant's conduct. Without reference to *Kodak*, the court stated:

TRU seems to think that anticompetitive effects in a market cannot be shown unless the plaintiff, or here the Commission, first proves that it has a large market share. This, however, has things backwards. As we have explained elsewhere, the share a firm has in a properly defined relevant market is only a way of estimating market power, which is the ultimate consideration. The Supreme Court has made it clear that there are two ways of proving market power. One is through direct evidence of anticompetitive effects.<sup>140</sup>

There was evidence in the record that after several years of rapid increases in the warehouse clubs' share of the toy market, this growth was stifled or reversed after Toys "R" Us persuaded toy manufacturers to limit sales to the clubs.<sup>141</sup>

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<sup>137</sup> See *id.* at 1076 (finding that Staples charged thirteen percent more (and Office Depot five percent more) in one firm markets than in three firm markets).

<sup>138</sup> 221 F.3d 928 (7th Cir. 1999).

<sup>139</sup> See *id.* at 930.

<sup>140</sup> *Id.* at 937 (citations omitted).

<sup>141</sup> See *id.* at 933.

If *Staples* and *Toys “R” Us* are deemed victories for Kodak empiricism, then the district court’s dismissal of the Justice Department’s predatory pricing case against American Airlines was a defeat.<sup>142</sup> In the face of evidence that a small airline’s entry into a city-pair market had produced lower prices for consumers, and that American Airlines’ strategically employed increase in competing flights and discounted fares had driven the rival from the market, the court granted summary judgment for American Airlines “because it at most matched the prices of its competitors, and because there is no dangerous probability (even assuming below-cost pricing) of recoupment of American’s supposed profits by means of supra-competitive pricing.”<sup>143</sup> Assuming this mechanical application of the Supreme Court’s test was solidly rooted in the evidence (for purposes of summary judgment, to be construed in the light most favorable to the plaintiff), the decision gives short shrift to evidence of actual anti-competitive effects. For example, American increased the number of flights that it offered on the contested route, then discontinued the added flights after the smaller rival had abandoned the route, conduct that is comparable to the use of “fighting ships” long outlawed under maritime law<sup>144</sup> and difficult to construe as anything other than a strategic ploy to drive the smaller rival from the market. The prices paid by consumers were down during the contested phase but were raised to precontest (or higher) levels soon after the small rival was driven from the market. In addition, there was record evidence of American’s intent to drive its smaller rivals from the market, including a statement of American’s CEO to the effect that “If you are not going to get them out then no point to diminish profit.”<sup>145</sup>

The *AMR* decision notwithstanding, the federal agencies will likely have more success than private plaintiffs in resisting mechanical applications of screening rules that do violence to competition goals. One would expect this result because the agencies often have a credibility with the court that a private plaintiff may lack. The agencies may also possess the resources to do an empirical survey of anti-

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<sup>142</sup> *United States v. AMR Corp.*, 140 F. Supp. 2d 1141 (D. Kan. 2001), *appeal docketed* (10th Cir. 2001).

<sup>143</sup> *Id.* at 1218.

<sup>144</sup> Fighting ships used by international ocean cartels were banned by section 14 of the Shipping Act of 1916, 46 U.S.C. § 812 (codified as amended at 46 U.S.C. § 1709(b)(6)).

<sup>145</sup> *AMR Corp.*, 140 F. Supp. 2d at 1153. Intent evidence has had a long history in predatory pricing cases. See SULLIVAN & GRIMES, *supra* note 40, § 4.3c, at 155-56. Nevertheless, the Supreme Court disregarded intent evidence in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 232 (1993), because it was deemed implausible in light of the oligopolistic conditions prevailing in the cigarette industry. *Brooke Group* is distinguishable because American Airlines, unlike the cigarette firms, could act unilaterally (as a monopolist would) without the participation of other airlines.

competitive effects that private litigants cannot conduct. Nonetheless, one noteworthy success for private plaintiffs occurred in *Law v. NCAA*.<sup>146</sup> A price-fixing violation involving a limited class of assistant basketball coaches for Division I basketball universities was sustained by the court based on the showing of “actual anticompetitive effects.”<sup>147</sup>

## B. Kodak as a Precedent in Seller Abuse Cases

### 1. Cases Affirmatively Relying on Kodak

Looking only at seller abuse cases in which *Kodak* theories of information inadequacies and lock-in were alleged, *Kodak*'s impact has been measured. Most of the cases have involved aftermarket products (installed-base opportunism)<sup>148</sup> or franchising,<sup>149</sup> although there have been scattered cases involving other fact patterns.<sup>150</sup> The larger body of reported cases in which plaintiffs have advanced a *Kodak* theory resulted in litigated judgments for the defendants. There are, however, a number of significant cases in which the court, relying upon *Kodak*, has ruled for the plaintiff.

Federal courts of appeals have affirmatively relied on a *Kodak* theory in two cases involving a seller-abuse claim, one of them *Kodak* on remand.<sup>151</sup> A few district courts have affirmatively relied on *Kodak* in denying defendants' pretrial motions for summary judgment or dismissal.<sup>152</sup> And the Nebraska Supreme Court relied squarely on *Kodak* in applying state antitrust law in an aftermarket case with facts

<sup>146</sup> 134 F.3d 1010 (10th Cir. 1998).

<sup>147</sup> *Id.* at 1020-21. See also the discussion of this case *supra* Part IV.B.

<sup>148</sup> See, e.g., *Red Lion Med. Safety, Inc. v. Ohmeda, Inc.*, 63 F. Supp. 2d 1218, 1221 (E.D. Cal. 1999) (alleging manufacturer of medical anesthesia equipment tied parts and services); *Heath Consultants v. Precision Instruments*, 527 N.W.2d 596 (Neb. 1995) (alleging manufacturer of leak equipment tied parts).

<sup>149</sup> See, e.g., *Queen City Pizza v. Domino's Pizza, Inc.*, 124 F.3d 430 (3d Cir. 1997) (alleging franchisor required franchisees to purchase products); *Collins v. Int'l Dairy Queen*, 59 F. Supp. 2d 1312 (M.D. Ga. 1999) (same); *Wilson v. Mobil Oil Corp.*, 984 F. Supp. 450 (E.D. La. 1997) (same).

<sup>150</sup> See, e.g., *Eichorn v. AT&T*, 248 F.3d 131 (3d Cir. 2001) (alleged conspiracy to deprive employees of pension rights); *Mellon v. Cessna Aircraft Co.*, 7 F. Supp. 2d 1183 (D. Kan. 1998) (alleging section 2 claim in an alleged market confined to one type of the manufacturer's jet aircraft based on manufacturer's refusal to service the plaintiff's airplane).

<sup>151</sup> See *Image Technical Servs., Inc. v. Eastman Kodak Co.*, 125 F.3d 1195 (9th Cir. 1997); *Virtual Maint., Inc. v. Prime Computer, Inc.*, 995 F.2d 1324 (6th Cir. 1993), *opinion withdrawn*, 11 F.3d 660 (6th Cir. 1993).

<sup>152</sup> See *Red Lion Med. Safety, Inc.*, 63 F. Supp. 2d at 1240 (denying defendants' motion for summary judgment in antitrust claims of an aftermarket tie and related section 2 offenses); *Collins*, 59 F. Supp. 2d at 1314 (denying motion to dismiss denied in a franchising tie-in claim); *Mellon*, 7 F. Supp. 2d at 1196 (denying summary judgment in section 2 claim based on defendant's refusal to service the plaintiff's aircraft).

strikingly similar to *Kodak*.<sup>153</sup> Although significant, this collection of affirmative citations hardly suggests the broad impact that proponents expected or that critics feared.

There may be a number of reasons for this relatively small number of affirmative citations. First, there is surely a body of unreported settled cases in which the plaintiffs had strong *Kodak* arguments.<sup>154</sup> One would expect that defendants would be most likely to settle a case in which the plaintiff's theory is strongly anchored in the law and facts. There may also be cases in which the parties simply failed to make *Kodak* arguments that might have been available to them. For example, in the Supreme Court briefs in *State Oil v. Khan*,<sup>155</sup> a case involving an alleged seller power abuse in which a *Kodak* theory was a natural fit, neither the parties nor the Federal Government's amicus brief relied upon *Kodak*. Even when a *Kodak* theory has explanatory power, the plaintiffs' bar may be hesitant to rely on *Kodak* because of the frosty reception that a number of appellate courts have accorded the decision, as discussed below.

## 2. Cases Declining to Follow *Kodak*

Turning to the larger body of cases that have declined to follow *Kodak*, the decisions generally have fallen into three categories: (1) cases in which the courts have interpreted *Kodak* narrowly to apply only when a defendant has changed its conduct after the tying product has been sold; (2) cases that refuse to recognize tie-in claims because antitrust law is trumped by intellectual property law; and (3) cases in which courts have simply ignored or misunderstood *Kodak* while rotely applying screening rules that would allow dismissal of a case.

### (a) Requiring a Change of Policy After the Lock-In

In *Lee v. Life Insurance Co. of America*,<sup>156</sup> in 1994, the First Circuit declined to follow *Kodak* because, in the panel's view:

[T]he *timing* of the 'lock in' at issue in *Kodak* was central to the Supreme Court's decision. . . . Had previous customers known, at the time they bought their Kodak copiers, that Kodak would implement its restrictive parts-servicing policy, Kodak's 'market power,' i.e., its leverage to induce custom-

<sup>153</sup> See *Heath Consultants v. Precision Instruments*, 527 N.W.2d 596 (Neb. 1995).

<sup>154</sup> I was a consultant in one such aftermarket tie-in case involving a major automobile manufacturer. A protective order precludes discussion of the parties or the settlement terms.

<sup>155</sup> 522 U.S. 3 (1997).

<sup>156</sup> 23 F.3d 14 (1st Cir. 1994).



ers to purchase Kodak servicing, could only have been as significant as its [market power] in the *copier market*, which was stipulated to be inconsequential or nonexistent.<sup>157</sup>

This reading was picked up in other circuits.<sup>158</sup> Although this interpretation finds some support in a cryptic footnote in Justice Blackmun's majority opinion,<sup>159</sup> the narrow construction of the *Kodak's* sweeping language seems strained.

One of the striking features of this line of cases is the apparent willingness of courts that follow it to put aside actual evidence of anticompetitive effects in favor of arid deductive logic. The syllogism that is applied is roughly as follows: (1) buyers will know of the terms of sale of aftermarket products at the time of purchase of the installed-base product; (2) if the aftermarket terms are unfavorable, the buyer will adjust its purchase decision; therefore, (3) if the seller made no change in the terms of aftermarket products' availability after the sale of its installed-base product, there can be no anticompetitive effect from the use of a tie-in on the aftermarket products. There is no place in this syllogism for disputing the conclusion—actual evidence of anticompetitive effects (the cardinal rule of *Kodak*) is *a priori* disregarded as inconsistent with deductive theory.

<sup>157</sup> *Id.* at 20.

<sup>158</sup> See *PSI Repair Servs., Inc. v. Honeywell Inc.*, 104 F.3d 811, 820 (6th Cir. 1997) ("We likewise agree that the change in policy in *Kodak* was the crucial factor in the Court's decision."); *Digital Equip. Corp. v. Uniq Digital Techs., Inc.*, 73 F.3d 756, 763 (7th Cir. 1996) (Easterbrook, J.) ("The Court did not doubt in *Kodak* that if spare parts had been bundled with Kodak's copiers from the outset, or Kodak had informed customers about its policies before they bought its machines, purchasers could have shopped around for competitive life cycle prices. The material dispute that called for a trial was whether the change in policy enabled Kodak to extract supra-competitive prices from customers who had already purchased its machines."). A number of district courts have followed this interpretation. See, e.g., *Metzler v. Bear Auto. Serv. Equip. Co.*, 19 F. Supp. 2d 1345, 1357 (S.D. Fla. 1998) (noting Kodak's emphasis on a change in company policy allowing an antitrust defendant to extract supra-competitive prices); *Wilson v. Mobil Oil Corp.*, 984 F. Supp. 450, 459 (E.D. La. 1997) (same).

<sup>159</sup> In the footnote, Justice Blackmun wrote that the dissent disagreed with the majority's conclusion based on the dissent's "hypothetical case of a tie between equipment and service. 'The only thing lacking' to bring this case within the hypothetical case, states the dissent, 'is concrete evidence that the restrictive parts policy . . . was generally known.' But the dissent's 'only thing lacking' is the crucial thing lacking—evidence." *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 477 n.24 (1992).

Commenting on the heavy reliance that some circuits have placed on this footnote, one district judge wrote:

This enigmatic comment, designed as a brisk rejoinder, is too slender a reed on which to base a significant restriction on the Court's holding particularly when in its very next sentence, the [*Kodak*] majority emphasizes that liability "depends on whether the equipment market prevents the exertion of market power in the [aftermarket]."

*Red Lion Med. Safety, Inc. v. Ohmeda, Inc.*, 63 F. Supp. 2d 1218, 1230 n.11 (E.D. Cal. 1999).

The premises that lead to the conclusion of no anticompetitive effect are highly vulnerable. As one district judge (who declined to follow the change of policy construction) put it:

It is noteworthy that in the [*Kodak*] Court's lengthy discussion of information costs it never once makes reference to Kodak's change in policy. Information costs may be high, and a manufacturer may thus have considerable market power in the aftermarket, even in the absence of a change in policy. As the [*Kodak*] Court pointed out, "even if consumers were capable of acquiring the complex body of [life cycle pricing] information, they may choose not to do so. Acquiring information is expensive. If the costs of service are small relative to the equipment price, or if consumers are more concerned about equipment capabilities than service costs, they may not find it cost efficient to compile the information."<sup>160</sup>

Despite its vulnerability, the "change in policy" construction of *Kodak* is likely to resonate with those who believe that antitrust should give way to freedom of contract, even in the face of clear evidence of anticompetitive effects. In its broadest application, the change of policy interpretation may swallow *Kodak* entirely. Consider a franchisor who writes boilerplate language into every franchise contract that entitles it to change, without prior notice, the terms and conditions of purchase for all input products required by the franchisee. Under Judge Easterbrook's interpretation in *Digital Equipment Corp.*, such blanket notice would be sufficient to avoid following *Kodak*.<sup>161</sup> But such generic notice of a franchisor's right to change policies, even if it is read and digested by prospective franchisees, will be next to useless because of the inability to predict what procurement policies might be instituted by the franchisor years after the original franchise agreement was signed.<sup>162</sup>

Notwithstanding its flawed underpinnings, the change of policy interpretation of *Kodak* seems entrenched in a number of circuits.

<sup>160</sup> *Red Lion Med. Safety, Inc.*, 63 F. Supp. 2d at 1231 (citation omitted).

<sup>161</sup> This appears to be precisely what happened in *Wilson v. Mobil Oil Corp.*, 984 F. Supp. 450, 461 (E.D. La. 1997) (finding that franchisees had sufficient information to conclude that they would be required to purchase from a single supplier indefinitely).

<sup>162</sup> In *Perna Life Mufflers, Inc. v. Int'l Parts Corp.*, 392 U.S. 134 (1968), the Supreme Court was unimpressed with arguments that the franchisees' act of signing boilerplate language in the franchise contract precluded any antitrust recovery. Justice Black reasoned that the franchisees "apparently accepted many of these restraints solely because their acquiescence was necessary to obtain an otherwise attractive business opportunity." *Id.* at 139.

Assuming the Supreme Court does not address this issue, the only uncertainty in circuits that follow this interpretation may be how far the interpretation is extended. In these circuits, there may still be room for plaintiffs to prevail on a *Kodak* theory if the defendant has effected a clear change in policy after the installed-base product is sold. In franchise cases, a related unsettled issue is whether a franchisor can wholly avoid *Kodak* liability by including broad boilerplate language in the franchise agreement that allows the franchisor to make unrestricted changes in requirements concerning input products that the franchisee must purchase.

(b) *Intellectual Property Defenses*

A second rationale for not applying *Kodak* is that its application might result in antitrust liability in contravention of intellectual property rights. *Kodak* pressed its patent rights arguments on remand, but the Ninth Circuit found these arguments “pretextual.”<sup>163</sup> Intellectual property rights were decisive, however, in *In re Independent Service Organizations Antitrust Litigation*.<sup>164</sup> The plaintiff, an independent service provider that had serviced Xerox original equipment, brought Sherman Act claims against Xerox for its refusal to sell patented parts and copyrighted manuals and to license copyrighted software. In affirming summary judgment for Xerox, the Federal Circuit declined to apply *Kodak* because the case involved a tying claim that had not been made against Xerox.<sup>165</sup> The court also interpreted broadly a patentee’s right to refuse to license or sell, even when that refusal could result in substantial anticompetitive effects in a secondary market.<sup>166</sup> The *Xerox* decision suggests a substantial curtailment not only of *Kodak* theories, but also of the reach of antitrust generally.

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<sup>163</sup> See *Image Technical Servs., Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1218-20 (9th Cir. 1997).

<sup>164</sup> 203 F.3d 1322 (Fed. Cir. 2000).

<sup>165</sup> See *id.* at 1327.

<sup>166</sup> In his critique of the *Xerox* decision, then FTC Chairman Pitofsky wrote:

In effect, the Federal Circuit has leaped from the undeniable premise that an intellectual property holder does not have to license anyone in the first instance to the unjustifiable conclusions that it can select among licensees to achieve an anticompetitive purpose or can condition a license (for example, you receive a license only if you agree not to do business with my competitor) to achieve an anticompetitive effect.

Robert Pitofsky, Chairman, FTC, *Antitrust and Intellectual Property: Unresolved Issues at the Heart of the New Economy*, at <http://www.ftc.gov/gov/speeches/pitofsky/ipf301.htm>. (Mar. 2, 2001). For a recent decision that suggests that intellectual property rights will not broadly displace antitrust claims, see *United States v. Microsoft Corp.*, 253 F.3d 34, 63 (D.C. Cir. 2001) (stating, in response to a sweeping claim that lawfully acquired intellectual property rights conferred antitrust immunity: “That is no more correct than the proposition that use of one’s personal property, such as a baseball bat, cannot give rise to tort liability.”).

(c) *Kodak Misunderstood*

Finally, there have been cases in which courts refuse to follow *Kodak* because they have apparently misunderstood the holding. In *Queen City Pizza v. Domino's Pizza, Inc.*,<sup>167</sup> a split panel declined to apply *Kodak* to Sherman Act claims that a franchisor had unlawfully required franchisees to purchase pizza dough only from the franchisor. At one point, the majority appeared to embrace a market definition of all investment opportunities available to a potential franchisee at the time the franchise contract was signed.<sup>168</sup> Earlier in the opinion, however, the majority declared the relevant market to be "commodities reasonably interchangeable by consumers for the same purposes."<sup>169</sup> Pizza dough was available to consumers from a wide variety of sources other than the Domino's chain, so such a market definition was fatal to plaintiffs. But the definition had nothing to do with the franchisor's power to coerce franchisees into purchases of overpriced or inferior quality pizza dough. *Kodak* was all about the Supreme Court's willingness to consider market power abuses in a single brand market, a circumstance not squarely addressed by the *Queen City* court.

This confusing discussion of relevant market highlights the importance of not rotely invoking market definitions to the exclusion of evidence of anticompetitive effects. In *Queen City*, the franchisee plaintiffs had offered evidence of the availability of comparable or superior pizza dough, produced by one of Domino's own franchisees, at a lower price.<sup>170</sup> To ignore this evidence is to depart from *Kodak's* central admonition that antitrust is about actual market effects, not "legal presumptions that rest on formalistic distinctions."<sup>171</sup>

## CONCLUSION

*Kodak* is a multi-faceted decision that turns out to have unique relevance for addressing the systemic bias against small business. The full extent of that bias, and why it is harmful to competition, remains to be forthrightly acknowledged and addressed by the antitrust community. That will be no mean task. But if competition works better, and the consumer is better served, when small businesses are

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<sup>167</sup> 124 F.3d 430 (3d Cir. 1997).

<sup>168</sup> See *id.* at 441.

<sup>169</sup> *Id.* at 438. The dissent argued that the majority had not properly applied *Kodak*. See *id.* at 444 (Lay, J., dissenting). The Third Circuit denied plaintiffs' petition for rehearing en banc, but the denial was accompanied by an unusual written dissent. See *id.* at 725-26 (Becker, J., dissenting from denial of petition for rehearing en banc).

<sup>170</sup> See *id.* at 434.

<sup>171</sup> *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 466 (1992).

given a fair and non-discriminatory opportunity to compete, then anti-trust must join the battle or forsake its most fundamental precepts.

Once the issue is acknowledged, *Kodak's* call for empirical honesty in assessing real market effects offers the starting point for a comprehensive response. Each of the many judicial rules and screening doctrines developed with the best of intent to cull out non-meritorious antitrust claims should be put to this test: *Does the rule, when applied, shield abusive strategic conduct that targets small business or other non-power players?* If the answer is yes, then the rule itself, or the extent of its application, should be reconsidered.

*Kodak's* corollary themes are also central to a coordinated response to the marketplace bias against small business. In particular, *Kodak* speaks to two pivotal issues involving seller power abuses such as tie-ins: (1) the recognition that information deficiencies and sunk investments can create a coercive relational power that victimizes small players and distorts competition and (2) the demonstration that leverage theory is often an accurate description of the anticompetitive effects that arise from strategic use of a tie-in to target small businesses and other non-power players.

Of course, *Kodak* has a legacy independent of the concern with marketplace bias against small business. As the tenth anniversary of *Kodak* nears, it is an opportune time to consider that legacy. Will it face a fate similar to *United States v. Arnold, Schwinn & Co.*,<sup>172</sup> overruled by the Court on its tenth anniversary? Will it survive as an emaciated precedent largely ignored and readily distinguished by federal courts? Or will its teachings about empiricism, informational problems, relational market power, and summary judgment guide the future evolution of antitrust theory and practice?

While no one can predict with assurance *Kodak's* life cycle in the courts, current trends suggest that *Kodak* will continue to be distinguished or simply ignored by courts that do not wish to follow it. But the ideas and issues raised in *Kodak* cannot and will not disappear, even if the case were expressly overruled. The Court's visionary insights in June of 1992 were a restatement in modern application of concepts that have resonated through a century of antitrust. They will not disappear.

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<sup>172</sup> 388 U.S. 365 (1967). *Schwinn* was overruled by the Court in *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977).