FOREIGN AND INTERNATIONAL COMPETITION LAW DEVELOPMENTS

THE PETROLEUM PRODUCTS LITIGATION ADDS TO THE DEBATE AND DOUBT OVER WHAT CONSTITUTES A "CONSPIRACY"

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Few things are more central to modern antitrust jurisprudence than the legal standards used to determine whether a "conspiracy" exists in suspicious circumstances. If the evidentiary standards are too high, many probable conspiracies are likely to escape the *Sherman Act* net; if the standards are too low, however, unilateral (and even innocuous) business conduct may be pronounced a "conspiracy" and subjected to the *Sherman Act* penalties under a *per se* rule.

Because the U.S. Constitution guarantees a jury trial on antitrust damage claims, the practical question in civil cases becomes, has the plaintiff established a set of facts from which a jury could rationally infer a "conspiracy"? If the answer is "yes", the case goes to the jury for trial. If it is "no", the trial judge enters summary judgment for the defendant and the plaintiff (normally) appeals.

The Supreme Court muddied the waters on antitrust summary judgment standards more than a little in its 1986 *Matsushita* decision.[1] There (by a 5:4 vote) the Court granted summary judgment for the defendants on grounds that the alleged conspiracy "makes no economic sense" and the defendants "lacked any rational motive to join" it. The majority then seemed to offer a broad new standard for summary judgment in a horizontal conspiracy case:

> [A]ntitrust law limits the range of permissible inferences from ambiguous evidence in a §1 [conspiracy] case. ... To survive a motion for summary judgment ... a plaintiff seeking damages for violation of §1 must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently.

Now the Supreme Court has a chance to revisit this issue in the context of a fascinating "price-fixing" conspiracy case brought by five state attorneys general against eight major oil companies for conduct occurring two decades ago. In the *Petroleum Products Antitrust Litigation*, the U.S. Court of Appeals for the Ninth Circuit reversed the District Court's summary judgment for the defendants and sent the case back for trial on a broad conspiracy theory.[2] The defendants have petitioned the Supreme Court for *certiorari*.

Matsushita, which involved an alleged predatory conspiracy by Japanese companies, was a unique case. *Petroleum Products* is not. Thus, if the Supreme Court grants *certiorari* in *Petroleum Products*, it will have a chance to illuminate its new horizontal conspiracy doctrine in the context of a very old-fashioned market. Indeed, the market is so old-fashioned that it is the same one–wholesale gasoline–which was at issue in the Supreme Court's seminal *Socony-Vacuum* decision, in which the Court established, beyond any doubt, that price-fixing is *per se* illegal.[3] Thus, half a century after *Socony*, antitrust practitioners and scholars may be reintroduced to the "tank wagon price" and other memorabilia of the gasoline business, should the Supreme Court make *Petroleum Products* into a latter-day landmark.

Matsushita's holding that an antitrust plaintiff "must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently" has apparently created a substantial hurdle even for a plaintiff seeking to establish an old-fashioned, naked horizontal conspiracy. This hurdle results from the Court's mixing of vertical "agreement" and horizontal "agreement" ideas without sufficient explanation.

The long-standing (and stricter) approach to *horizontal* agreements had been based on Adam

Smith's celebrated comment that "People of the same trade seldom meet, even for merriment or diversion, but the conversation ends in a conspiracy against the public or in some contrivance to raise prices."[4] Therefore the Supreme Court, in its landmark cases from the *Socony-Vacuum* era, was willing to go a long way in allowing a conspiracy to be inferred from less-than-conclusive evidence, on the implicit assumption that competitors need not talk to each other and hence no useful dialogue would be chilled by a strict rule.[5]

The considerations are quite different in the *vertical* area where manufacturers, distributors and dealers have to be able to communicate (even about pricing) in order to serve the legitimate goals of interbrand competition. Accordingly, the Supreme Court, going all the way back to the 1919 *Colgate* case,[6] has applied a much narrower approach to inferring "agreements" in the vertical context. Most recently in its 1982 *Monsanto* decision,[7] the Court held that a "conspiracy" question for the jury was not raised where one dealer simply complained to the manufacturer about another price-cutting dealer, who was subsequently terminated by the manufacturer. The *Monsanto* court stressed that,

> if an inference of ... an agreement may be drawn from highly ambiguous evidence, there is considerable danger that [established pro-competitive vertical] doctrines enunciated in [earlier cases] will be seriously eroded. [Accordingly] there must be evidence that tends to exclude the possibility that the manufacturer and the non-terminated distributors were acting independently.

This is the message that the Supreme Court carried over into the horizontal area in *Matsushita*. This was an unusual suit by a group of American television manufacturers against a group of Japanese television manufacturers, alleging that the Japanese defendants had, *inter alia*, agreed to maintain high prices in Japan in order to finance predatory pricing in the United States, to restrict their U.S. outlets to avoid competing with each other and to impose certain minimum price controls in the U.S. Applying established standing rules, the Supreme Court said that the only conspiracy for which the plaintiffs as competing manufacturers had standing to sue was the alleged conspiracy to charge predatory prices in the United States. The other alleged conspiracies were viewed as irrelevant to the predatory pricing conspiracy. The Court, in an opinion written by Justice Powell, applied a heavy dose of Chicago economics to the situation, and concluded that the alleged predatory pricing conspiracy would be "speculative" and "irrational". The Court emphasized that a predatory pricing conspiracy was especially hard to organize and would likely give rise to cheating. The Japanese defendants, stressed the Court,

> have no *motive* to sustain such losses absent some strong likelihood that the alleged conspiracy in this country will eventually pay off ... [and] there is nothing to suggest any relationship between petitioners' profits in Japan and the amount that petitioners could expect to gain from a conspiracy to monopolize the American market.

The Court added,

> [l]ack of motive bears on the range of permissible conclusions that might be drawn from ambiguous evidence: if petitioners had no rational economic motive to conspire, and if their conduct is consistent with other, equally plausible explanations, the conduct does not give rise to an inference of conspiracy.

Noting that the alleged conspiracy was to charge a low price, the majority stressed that the evidence must "'ten[d] to exclude the possibility' that petitioners underpriced respondents to compete for business rather than to implement an economically senseless conspiracy."

Justice White strongly dissented (joined by Justices Brennan, Blackmun, and Stevens), charging that the majority opinion "only muddies the waters." Among other things, he criticized the majority's Chicago-based "economic rationality" point, alleging that the majority "consistently assumes that petitioners valued profit-maximation over growth ... I believe that this is an assumption that should be argued to the factfinder, not decided by the Court."

In stark contrast, the *Petroleum Products* litigation involves much more pedestrian allegations of horizontal price fixing. There, the states' basic allegation is that the defendant oil companies conspired to stabilize and increase retail gasoline prices by conspiring to set the "tank wagon" prices at which they sold gasoline to independent dealers. The second basic charge is that they conspired in the early 1970s to create an

artificial shortage of crude oil through their consortium dealings with Iran and Saudi Arabia, and of refined products through limitations on refinery building. Finally, the attorneys general charge that the oil companies conspired not to bid on the various states' bulk sale supply contracts. It is the "tank wagon" conspiracy that is the most interesting and important because everyone had conceded that no direct evidence exists of a "conspiracy."[9] Instead, the states are relying on various forms of circumstantial evidence.

The alleged "tank wagon" conspiracy arose out of the familiar "price war" pattern that tends to recur in gasoline markets when OPEC or some other government agency is not controlling supply. As the District Court explained:

> In times when supply is plentiful, prices tend to work their way downward as some dealers seek to increase their market shares by charging less, prompting competitors to do likewise...
> If a retail gasoline dealer ... fails to participate in these price reductions, his market share decreases... Accordingly, the defendant companies, in order to enable their dealers to remain competitive, share with them the burden of having to reduce the retail prices by giving them discounts from the tank wagon prices. The continuation of these successive reductions in retail prices, known as "price wars," results in losses to everyone except the consumer. In due course, one or more of the defendant companies concludes that the market has "had enough" and removes or reduces the dealer discounts and thus restores or approaches the published tank wagon prices. (Such actions will be referred to hereinafter as "restorations.") The other majors usually make similar restorations and their respective dealers normally find themselves obliged to respond promptly with corresponding increases in their retail prices to consumers.

The states' essential contention is that these sometimes large "restorations" which ended price wars must have been agreed to in advance. The core of their theory is a sort of "reverse oligopoly" theory: there were so many competitors in the market that the commercial risks to a single initiator of a "restoration" were too large and, in any event, others would covertly "shade" or "cheat". The defendants responded that their individual actions were "independent" although "interdependent". The Ninth Circuit Court (citing a leading economics treatise) said that "[t]he gasoline markets under discussion here appear to be in that gray area where, although not altogether inevitable, interdependence is distinctly possible." Accordingly, the Court of Appeals concluded that one could not infer conspiracy from parallel pricing alone, even with sharp "restorations".

But the Court did not stop there. It pointed to "two additional classes of evidence" that it said would allow a jury to infer conspiracy when taken in conjunction with parallel pricing. These were the practices of some defendants of first issuing press releases at the time of a "restoration" and second, posting their current tank wagon prices and existing dealer discounts. The Court of Appeals then referred to evidence that "indicates that the publication of wholesale price increases was intended to make, and had the effect of making, restorations more effective by ensuring that competitors could quickly learn of, and respond to, any withdrawal of dealer aid." The Court then explained that the evidence regarding the purpose and effect of price announcements, together with the parallel price restorations, was sufficient to support a inference of an agreement to raise or stabilize prices.

The Court also explained its policy position in these broader terms, with copious citations to the writings of Professor Philip Areeda:

> Simple interdependent pricing does not violate the Sherman Act, not because it is desirable (it is not), but because permitting proof of conspiracy solely on the basis of price parallelism *is* undesirable. The [state attorneys general], however, have offered evidence indicating that the [oil companies] in this case did more than simply price interdependently. A jury could conclude that the oil companies agreed, either implicitly or explicitly, to create market conditions that would facilitate tacit or expressed price coordination.

It is here that the Court of Appeals begins to run into *Matsushita*. Even before *Matsushita*, it was a close call as to whether a party who publishes its pricing decisions to the whole market engages in a "conspiracy" because others act on this pricing information (whether or not the publisher anticipates it). Competitive markets, and prices, respond to information–this is why stock exchanges have instantaneous tickers and our securities laws seek to ensure that full information is available to markets. The Ninth Circuit Court responded to this point by stating that tank wagon prices and discounts are not of

interest to consumers and, therefore, "it appears that the public dissemination of such [pricing] information served little purpose other than to facilitate interdependent or collusive price coordination."

The *Petroleum Products* case, if taken by the Supreme Court, could clarify what the often mysterious *Matsushita* pronouncements were intended to mean. Here, there is nothing "irrational" about what the defendants are charged with doing, nor is there any element of charging *too low* a price. These defendants were charged with a classic exercise in interdependent pricing, which the Court of Appeals turned into a plausible "conspiracy" because the defendants were more than a few in number (making pure "conscious parallelism" difficult), and some defendants had published their "restorations," prices and price changes in the apparent hope that other competitors would follow. This is something less than a clear "conspiracy" case under pre-*Matsushita* law, and it seems to fall well short of the "tends to exclude the possibility" standard articulated by the Supreme Court in *Matsushita*.

Perhaps the Supreme Court will tell us that the "tends to exclude the possibility" standard is not to be applied literally to an alleged naked horizontal conspiracy case involving high prices rather than low ones. Such a course might make Adam Smith feel a little more comfortable, even if it does not guarantee that the attorneys general will get a jury trial on the "conspiracy" issue in the *Petroleum Products* case.

Regardless of whether *certiorari* is granted, *Petroleum Products* reminds us of two important truths in the 1990s. First, it shows again that the state attorneys general have now taken on a major role as antitrust enforcers.[10] Secondly, it shows again how very slow the U. S. judicial process can be in handling a major antitrust case: these now-consolidated cases were filed in the late 1970's, challenging conduct prior to the Arab Oil Embargo in 1973, and yet the case is still only at the *summary judgment* stage a decade and a half later – with the possibility that the parties will still have to face a jury trial in the District Court sometime before the end of the century.

Notes

1 *Matsushita Electric Industrial Co. Ltd.* vs. *Zenith Radio Corp.*, 475 U.S. 574 (1986).

2 *In Re Coordinated Pretrial Proceedings In Petroleum Products Antitrust Litigation*, 906 F.2d 932 (9th Cir. 1990), reversing 656 F. Supp. 1296 (D.C. Cal. 1986).

3 *United States* vs. *Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940).

4 See *United States* vs. *Realty Multi-List Inc.*, 629 F.2d 1351, 1368 (5th Cir. 1980).

5 See e.g., *Interstate Circuit* vs. *United States* 306 U.S. 208 (1939); *American Tobacco Co.* vs. *United States*, 328 U.S. 781

6 *United States* vs. *Colgate & Co.*, 250 U.S. 300 (1919)

7 *Monsanto Co.* vs. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984).

8 *Ibid.* at 763.

9 *Matsushita* decision, *supra*, note 1, at 593.

10 *Ibid.* at 596-97.

11 *Ibid.* at 597-98.

12 *Ibid.* at 604.

13 As the District Court explained, "[t]he plaintiffs have disclosed no direct evidence of conspiratorial conduct and, with [one] exception ... they almost admit such a lack." 656 F. Supp. at 1297.

14 *Ibid.* at 1299.

15 *In Re Coordinated Pretrial Proceedings in Petroleum Products Antitrust Litigation*, 906 F.2d 932 at 432.

16 *Ibid.* at 445.

17 *Ibid.* at 446.

18 *Ibid.* at 446-47.

19 *Ibid* at 448.

20 *Ibid.*

21 I discussed state activities in the merger area in "Expanding the Role of State Attorneys General in Mergers: *American Stores* as a Door Opener," *Canadian Competition Policy Record* (December 1990) p. 45.