

TENSIONS BETWEEN LAW AND REALITY

CHAPTER 2

The antitrust laws are schizophrenic when it comes to distribution arrangements and practices. This is because the normative view of channel structure and channel relations which underlies traditional antitrust analysis regards a distribution channel as a series of successive markets and hence sees channel relationships as relationships between nominally independent competitors. As noted in the previous chapter, this view is clearly at odds with the reality of modern-day competition between vertically integrated marketing systems. Moreover, since decisions in antitrust cases largely rest on economic theory, this normative view has proved to be a troublesome framework for guiding judicial decisions dealing with problems of distribution structure and channel conflict.

This contradiction between norm and reality reached its zenith in the 1967 Schwinn decision.¹ If taken literally, the Schwinn decision outlawed much of what was going on in modern marketing. As a consequence, it took only a few years for it to be radically modified. The controlling decision is now GTE Sylvania² which returned the law to the skepticism expressed in the 1963 White Motor case.³ In White, the Court had held that much of the substance of distributive relations needs to be subjected to a "rule of reason" analysis and that most vertical restrictions were not illegal in and of themselves without first looking at their competitive consequences.

Under Schwinn, the Court had interpreted the Sherman Act as making it unreasonable, without more,

¹ United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967).

² Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977).

³ White Motor Co. v. United States, 372 U.S. 253 (1963).

for a manufacturer to seek to restrict or confine areas or persons with whom an article may be traded after the manufacturer has parted with dominion over it.

Sylvania stands in sharp contrast with the per se attitudes espoused in Schwinn and its progeny which were decided largely on the principle that "the freedom guaranteed each and every business, no matter how small, is the freedom to compete--to assert with vigor, imagination, devotion and ingenuity whatever economic muscle it can muster." ⁴

The difficulty with exalting the independent channel member's economic freedom of action is that it is directly antithetical to the imperatives of the modern vertical marketing system. If the idea that every independent channel member has a right to act completely unfettered, should become the rule, the ability to manage vertical marketing systems would be greatly circumscribed since vertical restraints are essential to effective channel coordination and control. The concept of dealer autonomy is clearly at war with the proposition that the new unit of competition is the vertical system rather than the individual firms at each successive level of the system.

In Sylvania, Justice Powell recognized that the market impact of vertical restrictions is complicated because of their potential both for the simultaneous reduction of intrabrand competition and the stimulation of interbrand competition. It was his view that interbrand competition should be the primary concern of antitrust law. ⁵

As a result of this complex effect, the basic doctrine after Sylvania is that: ⁶

⁴ United States v. Topco Associates, 405 U.S. 596 (1972) and Albrecht v. The Herald Co. [III], 390 U.S. 145 (1968).

⁵ See Continental T.V., Inc. v GTE Sylvania Inc., 97 S. Ct 2549 at 2558, n. 19 (1977).

⁶ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 391 (1966).

All horizontal price fixing and horizontal market division agreements are illegal per se.

Vertical price fixing is illegal per se.

The legality of vertical market division is uncertain, and is subject to the "rule of reason."

Clearly, this resurrection of "reasonableness" as the basis for judging vertical nonprice restraints poses a number of problems in addition to deciding what general factors are to be considered. Obviously the court will have to decide what priority to give these factors, how to operationalize them, and to give them relative weight. What is needed is a new theory of channel competition, consistent with the realities of modern marketing, to guide them in their assessment of the competitive implications of channel arrangements. Without this, antitrust will remain in a fog regarding vertical marketing systems.

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To some extent, the courts have always recognized that some restraints upon intrabrand rivalry may be essential if society is to realize the potential efficiency of both ownership and contract integration. Basically, the difficulty has been to reconcile the tradeoffs between increased efficiency and increased output. This is clearly the legacy of Sylvania.⁷

By and large, the courts have sought to curb efforts to base market advantage on economic power rather than superior performance. No one quarrels with this objective. Unfortunately, the ability to distinguish these ends in vertical systems is not always easy. Historically, vertical arrangements have been condemned in two contexts:⁸

⁷ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 473 (1966).

⁸ United States v. Paramount Pictures, 334 US 131 (1948); United States v. Yellow Cab Co., 332 US 218 (1947); United States v. Colombia Steel Co., 334 US 495 (1948). Blake & Jones, "In Defense of Antitrust," 65 Col. L.Rev. 377 at 390 (1965).

1. When the transaction places an unduly large share of the market under the control of one or a few firms--single firms of 40 -50 percent or several with 60 -70 percent.

2. Where the primary motivation of the transaction to preempt a market of substantial size rather than to achieve any improvement in technical efficiency.

Still, the key question remains: why, and how much do we care about competition within the channel of distribution for a single manufacturer's product? ⁹ In other words, why should we be interested in intrabrand competition? Parenthetically, it should be noted that the Sherman Act does not distinguish between interbrand and intrabrand competition. This is a distinction that is made in the White Motor case. ¹⁰

A related question is whether we should bother to distinguish between ownership integration, achieved by internal growth or merger, and contract integration achieved through agreement? Traditionally, under the Sherman Act, ownership integration has been judged on the basis of market size while questions about the absence of intrabrand competition are completely ignored. By contrast, contractual integration is treated quite differently in spite of the fact that contractually linked vertical marketing systems are as much a single organization in terms of their behavior and competitive consequences as are ownership channels. Often the only distinction is the one of title, a distinction which many feel to be largely irrelevant for antitrust purposes. ¹¹

"In assessing the validity of a business practice, one needs to look at the effect the practice has on competition, and not the legal form in which it is

⁹ Philip Areeda, *Antitrust Analysis: Problems, Text, Cases*, 2nd Edition (Cambridge, MA: Little Brown and Company, 1974), p. 500.

¹⁰ White Motor Co. v. United States, 372 U.S. 253 (1963).

¹¹ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 472 (1966).

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The problem is that if the treatment of contractual integration is more restrictive than the treatment of ownership integration, the ultimate result might be to undermine contractual integration, including franchising, as a means for the independent merchant to become an effective competitor of large integrated firms. ¹³ This would be too bad!

In fact, many feel that the efficiencies created through the contractual integration of the selected activities of firms that otherwise remain independent are preferable to those achieved through merger or corporate development. Contractual integration preserves rather than eliminates independent units. ¹⁴ Contractual integration also differs from the other modes of integration in terms of the degree of control and flexibility offered. In a sense, there is a trade-off between commitment and flexibility which is not unimportant. ¹⁵ The decentralization of initiative which accompanies the contractual system is also an important value to preserve. Thus it seems unwise to treat contractual integration more severely than other forms of integration. At the very least, they should all be treated alike.

In addition, large firms who are denied the use of less restrictive contractual vertical restraints may be forced to vertically integrate through ownership, even though ownership integration may be less efficient than the contractual system would have been. ¹⁶

¹² William E. Greene, v. General Foods Corp., 617 F.2d 635 (5th Cir. 1975) cert. denied, 424 U.S. 942 (1976).[7168]

¹³ GTE Sylvania Inc. v. Continental T.V., Inc., 537 F.2d 980 at 999 (1977).

¹⁴ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 396 (1966).

¹⁵ Frederich Kessler and Richard H. Stern, "Competition, Contract and Vertical Integration," 69 Yale L.J. 1 (1959)

¹⁶ 88 Harv L. Rev. 645 (1975).

A review of the court decisions dealing with problems of distribution, reveals that vertical integration by contract seems to be feared because of its potential for:

- a. foreclosing competitors from a source of supply.
- b. foreclosing competitors from customers.
- c. eliminating competition among firms controlled on a second level of the industry.¹⁷

Many question the grounds for this fear.

Basically, The theory underlying the law of contractual integration holds that actual or potential intrabrand competition between channel members at the same level or at vertically adjacent levels of the channel can be injured in two different ways:¹⁸

1. By elimination of competition between two consenting parties, that is by agreement.
2. By injuring intrabrand rivals.

This concern for preventing vertical agreements that may injure competition between potential intrabrand rivals underlies those sections of the antitrust law which regulate exclusive dealing agreements, customer and territorial restrictions, and price fixing.

The second proposition above, namely that overly aggressive competition can injure competition by injuring intrabrand rivals, underlies those areas of antitrust law which deal with price discrimination,

¹⁷ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 397 (1966).

¹⁸ Robert H. Bork, "Contrasts in Antitrust Theory, I," 65 Col L.Rev. 400 (1965).

tying, requirements contracts and foreclosure generally.¹⁹ Unfortunately, most of these targeted practices are also among the means for operating vertical systems more efficiently. Consequently, if they are suppressed indiscriminately, this will frustrate the very objectives the antitrust laws were designed to achieve. This is the problem the Court acknowledged in White Motor and reaffirmed in Sylvania.

Many commentators, argue that the law's present theory of contractual vertical restrictions is operating on incorrect assumptions concerning the purposes and effects of these contractual restrictions, and that these assumptions are in turn causing the law to attack efficiencies as well as restraints.²⁰ This is an issue that this study proposes to address. Is it properly the purpose of antitrust to compel competition among the dealers of a particular manufacturer's brand?²¹ Will the public actually benefit from this enforced intrabrand competition? Should the theory that guides horizontal relations in conventional markets be used to guide the development of the law of vertical relations? How can we distinguish between positive and negative vertical restrictions? Should all vertical restrictions be legal as some hold?²² Should they all be per se illegal as others hold?²³ Or, is there a workable "rule of reason" approach such as that advocated in the Sylvania decision?

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¹⁹ Robert H. Bork, "Contrasts in Antitrust Theory, I," 65 Col L.Rev. 400, 402 (1965).

²⁰ Robert H. Bork, "Contrasts in Antitrust Theory, I," 65 Col L.Rev. 400, 402 (1965).

²¹ Richard Posner, "Antitrust Policy and the Supreme Court," 75 Col.L.Rev. 282 at 297 (1975).

²² [See for example Robert Bork, The Antitrust Paradox: A Policy at War with Itself (New York: Basic Books, Inc., 1978 and Robert Posner, "Antitrust Policy and the Supreme Court: An analysis of Restricted Distribution, Horizontal Merger and Potential Competition Decisions," 75 Colum. L.Rev. 282 (1975).

²³ See for example, William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its Aftermath, 81 Harv. L.Rev. 1419 (1968) and softened somewhat in William S. Comanor, "Vertical Price Fixing, Vertical Market Restrictions, and the New Antitrust Policy," 98 Harv. L.Rev. 983 (1985).

As noted in Chapter 1, there are a number of reasons why manufacturers would want to impose restrictions on their channel members in order to realize potential efficiencies and scale economies. Generally, the following managerial and logistical reasons are cited:²⁴

Cost reduction

Stability of operations

Security of outlets, sources and quality

Facilitate long-range planning

Facility utilization

Inventories

Transfer costs --smoothing the productive flow from one stage to the next.

Marketing expenses -- credit loss, sales, advertising Transportation cost

In addition , there are often a number of important marketing reasons for seeking to regulate resale prices charged, products offered, territories covered and customers served. For example, a manufacturer may wish to exercise some control over minimum resale prices in order to protect his interest in the goodwill attached to the product. Control of minimum resale price may also be necessary to preserve the product's image.

Vertical controls also become especially important when a key element of a brand's appeal rests on the uniformity of the "product" sold by each outlet. Variations in price and quality and other dimensions of the "presentation" can often undermine the marketing impact of the "product." McDonalds doesn't want each of its franchisees charging different prices for its "Big Macs."

²⁴ Frederich Kessler and Richard H. Stern, "Competition, Contract and Vertical Integration," 69 Yale L.J. 1 (1959).

The repeated use of the product as a "loss leader" may undermine the consumer's perception of the "value" of the product, and thus may cause the product to become unprofitable to other dealers, who may in turn feature competing brands or even drop the discounted brand altogether and leave the manufacturer without sufficient outlets in a market area.

Vertical restrictions are also used to induce prospective dealers to invest capital in buildings and other fixed equipment.²⁵ This is especially true in the case of single line distributors where the distribution investment is highly specialized, or where the returns are highly speculative. Automobile and farm implement dealerships, and motel, fast food, and service franchises often contain such restrictions.

Often the manufacturer restricts the distributor's freedom to set price and select customers and markets because he wants to increase the amount of non-price competition among his dealers in the hope that this will stimulate the provision of point-of-sale support and after-sale services in the distribution of his product.²⁶ Without such restrictions, the conventional wisdom holds that many distributors will not undertake these costly selling activities, but will seek to benefit from the selling activities of others and in a sense try to obtain a "free ride." And since no distributor wants to give his intrabrand competitor a "free ride," none will offer the additional sales support without protective restrictions.

Vertical restrictions may also be useful for enhancing product differentiation. While product differentiation generally leads to higher prices, this does not automatically imply that in every instance differentiation is socially undesirable, much less that it should always be condemned under the antitrust laws.²⁷ The fact is that low consumer substitutability between brands often results from valued differences

²⁵ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its Aftermath," 81 Harv. L.Rev. 1419 at 1428 (1968).

²⁶ Richard Posner, "Antitrust Policy and the Supreme Court," 75 Col.L.Rev. 282 (1975).

²⁷ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its

between brands and from important differences in the attributes of particular firms, including their distribution policies. In such instances the price effects of product differentiation are partially offset by the real social gains resulting from the existence of product variety, availability and point-of-purchase support.²⁸ The question that remains, however, is whether socially desirable product differentiation, achieved in part through the imposition of vertical contractual restrictions, should shield those restrictions from antitrust attack, or whether these gains should be sacrificed for enhanced intrabrand competition and lower price. Which is more important?²⁹ Unfortunately, one of the obvious consequences of product differentiation is the insulation of a manufacturer's products from interbrand price competition. This is why product differentiation generally leads to higher prices. It is also one of the situations where vertical restrictions not only curb intrabrand competition, but interbrand competition as well. The greater the degree of product differentiation that is achieved from the vertical restrictions, the greater the need for preserving effective intrabrand competition to compensate for the loss of this interbrand competition. Intra-brand competition now becomes indispensable in order to protect customers from the enhanced interbrand market power. This is the problem. Thus, product differentiation, even when socially desirable, can probably never serve as an acceptable justification for allowing vertical restrictions, although it helps explain why manufacturers would seek to impose them.³⁰

Another marketing justification for vertical restrictions is that they lead to increased sales by virtue of

Aftermath," 81 Harv. L.Rev. 1419 at 1434 (1968).

²⁸ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its Aftermath," 81 Harv. L.Rev. 1419 at 1424 (1968). See also Edward H. Chamberlain, "Product Heterogeneity and Public Policy," in Richard Heflebower and Geo. Stocking, (eds.) Readings in Public Policy and Industrial Organization, (Homewood, IL: Richard D. Irwin, 1958) pp. 236-243,

²⁹ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its Aftermath," 81 Harv. L.Rev. 1419 at 1424 (1968).

³⁰ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its Aftermath," 81 Harv. L.Rev. 1419 at 1451 (1968).

more intense coverage of geographic markets. Without vertical restrictions, dealers would be tempted to skim the cream off of markets and leave the hard-to-sell customers untouched. If high-cost and low-cost customers are to be charged a single price, absent restrictions, the high-cost customers would not be served.³¹

Finally, support for the legality of vertical restrictions is often sought on the grounds that restrictions are essential for quality control. This is a traditional defense of agreements which tie a franchisee's requirements for certain competitive goods and services to the use of the franchisor's trademark or tradename or marketing system. This defense has been upheld in various instances.³² It has also been struck down when less restrictive ways of achieving quality control are available.³³

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The discussion in the preceding section confirms the wisdom of the Court's skepticism, first expressed in White Motor and Sandura and subsequently reaffirmed in Sylvania.³⁴ Vertical restrictions do have important economic justifications as well as potentially serious anticompetitive consequences. As a consequence, a blanket per se prohibition against all vertical agreements between channel members which restrain trade seems to be inappropriate. Prohibiting all such agreements would undermine the viability of

³¹ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and its Aftermath," 81 Harv. L.Rev. 1419 at 1431 (1968).

³² See for example United States v. Jerrold Electronics Corp., 187 F.Supp. 545 (E. D. Pa. 1960), aff'd per curiam, 365 U.S. 567 (1961).

³³ See Siegel v. Chicken Delight, 448 F.2d 43 (9th Cir. 1971) cert. denied, 405 U.S. 955 (1972) and Chock Full O'Nuts Corp., 83 F.T.C. 575 (1973).

³⁴ White Motor Co. v. United States, 372 U.S. 253 (1963); Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 38 (1977); Sandura Co. v Federal Trade Commission, 339 F.2d 847 (6th Cir. 1964).

contractual marketing systems and encourage ownership integration when the discrepancy of assortments would permit. Where ownership integration was not possible, it would return channels of distribution to their former fragmented, and less efficient state. Neither of these outcomes would seem to be in the public interest. We do not want to throw out the baby with the bath water. The only remaining choice is between a strictly hands-off policy which would legalize all vertical agreements, including those controlling resale prices, or a case-by-case, "rule of reason" approach advocated by the Court in its Sylvania decision. There are strong arguments for both positions.

Robert Bork and Judge Posner, along with the late Professor Bowman at Yale and many "Chicago School" economists doubt that there is any real possibility of subverting the market process through vertical agreements in restraint of trade. They hold the same vertical arrangements are open to any competitor to adopt or not as he sees fit. If a vertically integrated concern prevails over one not so integrated, it is simply a sign that vertical integration is more efficient than operation of successive stages as independent enterprises. To upset such an arrangement is to stand in the way of progress.³⁵

It is their position that economic analysis indicates that only cartel arrangements, that is, horizontal agreements in restraint of trade, eliminate competition without creating corresponding efficiencies. Thus, a per se rule against horizontal/cartel agreements is still held to be sound policy.³⁶ But, since economic theory discloses no threat whatever to competition from vertical agreements, every vertical agreement should be held to be lawful in their view. Since the vertical elimination of competition by a single manufacturer can, by definition, never affect a larger proportion of the total output of the industry than the manufacturer produces, they would also argue that vertical price fixing and market division can create no additional horizontal market control.³⁷ And since, in their view,

³⁵ Blake & Jones, "In Defense of Antitrust," 65 Colum L.Rev. 377 at 391 (1965).

³⁶ Robert H. Bork, "Contrasts in Antitrust Theory , I," 65 Col L.Rev. 400, 410 (1965).

³⁷ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 402 (1966).

the only valid economic argument against vertical integration arises in those limited situations in which vertical integration is used as a means of perpetuating or increasing an undesirable horizontal market position, this group asserts that there can be no serious economic grounds for opposing vertical restrictions.³⁸

From this argument, it follows that in the case of an individual manufacturer's imposition of restraints upon competition among its resellers, the manufacturer's motive can never be restriction of output. Thus, the only satisfactory alternative hypothesis is that the manufacturer believes the restraint will increase its net revenue by increasing distributive efficiency.³⁹ Nor, could it be imagined, they would argue, that a competitive manufacturer using vertical price fixing or market division is moved by an "altruistic impulse, verging on the suicidal," to give its resellers greater - than-competitive profits at its own expense.⁴⁰

Thus, it is the position of this group that all vertical price fixing and market division agreements should be lawful regardless of the parties' market size, since such agreements always have the effect of creating efficiency beneficial to consumers. They do not create the ability to restrict output. They only increase the parties' revenue to the extent that efficiency is created.⁴¹ Consequently, this group would treat every price and non price restriction the same. Also, the distinction between agency and sale to channel members would be eliminated as a factor in applying antitrust to vertical relations.⁴²

³⁸ Robert H. Bork, "Contrasts in Antitrust Theory, I," 65 Col L.Rev. 400, 405 (1965).

³⁹ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 403 (1966).

⁴⁰ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 403 (1966).

⁴¹ Robert H. Bork, "The Rule of Reason and the Per Se Concept: Price Fixing and Market Division, II," 75 Yale L.J. 373 at 391 (1966).

⁴² Richard Posner, "Antitrust Policy and the Supreme Court," 75 Col.L.Rev. 282 at 297 (1975).

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Not all economists agree with the above position regarding vertical agreements, especially the blanket approval of vertical price fixing. Moreover, this "hands-off" position is not yet the view of the court. In fact, the current view of the court is that vertical price fixing and tying are still per se illegal, and that all other vertical agreements in restraint of trade are subject to review for competitive impact.

There are numerous assumptions that underlie the "hands-off" position which need to be examined before one completely "buys" that view. Clearly, the argument supporting a "hands-off" position depends upon the operation of a vigorous interbrand competition. And of course, we have already discussed how vertical agreements can increase product differentiation, which in turn substantially weakens interbrand competition as a check on dealer markups, and hence, final prices.⁴³

Also a point was raised in the White Motor case which needs to be resolved before the "hands-off" position can be accepted without reservation. In that case, White did not contend that its distribution system had any tendency to restrain competition among its distributors and dealers than a horizontal agreement among such distributors and dealers themselves.⁴⁴ It is still not clear why public policy should place a "halo" around agreements just because they are vertical.⁴⁵ Is a vertical agreement any less likely to have a negative effect on competition than a horizontal agreement? Why should various horizontal agreements be held to be illegal, while the same arrangement is held to be completely legal when it is set up vertically? It can't be because vertical restrictions often produce efficiencies, and horizontal agreements don't. This is not true. For example, agreements not to engage in excessive brand advertising

⁴³ See p. ?? where this is discussed.

⁴⁴ White Motor Co. v. United States, 372 U.S. 253 at 376 (1973).

⁴⁵ White Motor Co. v. United States, 372 U.S. 253 at 376 (1973).

in the case of cigarettes say, or market area rationalization in the case of gasoline stations would probably produce substantial efficiencies and possibly positive social benefits. Nor can it be because the agreements are between firms that do not compete. Dual distribution often places a supplier in competition with its distributors. It can't be that the agreements don't effect competition between distributors of the same brand, because that is their avowed purpose. Why should an agreement between Los Angeles County -Orange County Chevrolet dealers and General Motors to restrict the sales of an aggressive dealer through discount store outlets be regarded as a conspiracy, while a uniform agreement between Chevrolet and each of its dealers separately not to sell through discount stores be legalized?⁴⁶ Isn't this horizontal -vertical distinction a difference in form rather than substance? What if General Motors insisted that its dealers adhere to the manufacturer's list price pasted on the car window, or not sell to customers that do not live in a designated territory? Would people who want to buy a Chevrolet be sufficiently protected by the option they have of buying a Toyota or Chrysler brand instead?

What about the argument that restrictive agreements would not increase General Motor's total market share, and hence, would create no additional market control? Isn't this true only in a static sense? Unless such agreements are adopted by competing manufacturers, won't market shares be different in the following periods as a result of the restrictions? And if the restrictions are copied by competitors, won't the market structure be radically changed in the subsequent years? Is there no horizontal impact from vertical restrictions?

The fact is that there are many economists who feel that to the extent that such restrictions are permissible, and are widely adopted by leading manufacturers, the structure of the retail market will come to resemble the structure of the manufacturing market. And it is not clear that the consumer would benefit from such a change in automobile market structure. Consumers collectively of course can influence GM's wholesale prices. Individually, however, they have no discernible impact. This is not true in the case of an

⁴⁶ United States v. General Motors Corp., 384 U.S. 127 (1966)

individual Chevrolet dealer. If the potential buyer can get a better deal from a second Chevrolet dealer, the first dealer may be inclined to make a counter offer. The individual consumer loses this opportunity for a better deal if Chevrolet prices are rigged and all competition between Chevrolet dealers is curbed. The consumer is not completely at his local Chevrolet dealer's mercy. He can still buy a Ford. But it would probably be hard to convince the individual consumer that he is better off, or that the gains from the more efficient operation were reflected in the rigged price that he was offered by his local dealer.

This is not the only loss from the legalization of vertical market restrictions. Where the market structure at the manufacturing level is oligopolistic, and all firms adopt vertical restrictions, local oligopolies will be created at the distribution stage. And in oligopolistic markets, interbrand rivalry generally assumes a non-price character. By definition, price changes are used reluctantly since they can easily be copied and neutralized. Since it is much more difficult for competitors to copy product changes or new selling or distribution agreements, they will be emphasized over price. The final result is that even the collective power of consumers to effect wholesale prices is blunted. In the end then, unfettered vertical restrictions will not only eliminate intrabrand competition, they will also, through their effect on product differentiation and the heightened emphasis on non-price competition at all levels including retail, serve to reduce interbrand price competition as well.⁴⁷ It appears as though such a system leads to product differentiation, market power, higher manufacturer prices, and higher dealer markups.⁴⁸

When a long-term contract is used to rig prices or to gain exclusive access to a processor, an outlet, or a source of supply, subsequent business dealings are not based solely on the merits of competing offers. A market in which rivals are fenced out is not a free market in any meaningful sense of the word.

⁴⁷ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and Its Aftermath," 81 Harv. L. Rev. 1419 at 1426 (1968).

⁴⁸ William S. Comanor, "Vertical Territorial and Customer Restrictions: White Motor and Its Aftermath," 81 Harv. L. Rev. 1419 at 1429 (1968).

This is still a major concern of the courts, and should be.⁴⁹

In the chapters that follow, we will examine the areas of vertical price fixing, dual distribution, tying, exclusive dealing and requirements contracts, and customer and territorial restrictions to see what public policy is and to determine what it should be.

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End Notes--Chapter 2

⁴⁹ Blake and Jones, "In Defense of Antitrust," 65 Colum. L.Rev. 377 at 389 (1965).