No. 96-1570

OCTOBER TERM, 1997

NYNEX CORPORATION, ET AL., PETITIONERS
V.
DISCON, INCORPORATED

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES AND THE FEDERAL TRADE COMMISSION AS AMICI CURIAE

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QUESTIONS PRESENTED

1. Whether the court of appeals correctly held that a seller stated a claim under Section 1 of the Sherman Act, 15 U.S.C. 1, by alleging that it was excluded from the market as part of a conspiracy between a rival

seller and their buyer, a regulated monopolist, to raise prices to the monopolist's customers by circumventing regulatory constraints.

2. Whether the court of appeals correctly held that an entity may conspire to monopolize, in violation of Section 2 of the Sherman Act, 15 U.S.C. 2, when it acts with the specific intent to assist another entity to acquire or maintain monopoly power.

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This brief is filed in response to this Court's order inviting the Solicitor General to express the views of the United States.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-20a) is reported at 93 F.3d 1055. The opinion and order
of the district court (Pet. App. 2la-53a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on August 26, 1996. A petition for rehearing and suggestion for rehearing en banc was denied on January 7, 1997. The petition for a writ of certiorari was filed on April 3, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Respondent Discon Incorporated (Discon) com-

that were essentially derived from [NYT's] telephone monopoly," while avoiding "oversight from the state regulatory commission." Id. at 5a.

The complaint went on to allege that, in order to assure the success of the scheme, petitioners and AT&T conspired to exclude Discon from the removal services market. They did so because Discon not only refused to join in the scheme, but also engaged in acts that endangered the scheme's success, such as under-bidding AT&T's inflated bids and, on occasion, selling removal services directly to NYT, thus bypassing MECo. Complaint 1134,40-45,47,52-55. In response, the complaint alleged, petitioners granted contracts to AT&T instead of Discon, even when Discon sub-mitted a lower bid, and, in concert with AT&T, petitioners disseminated false information that led to Discon's decertification as an approved vendor for NYNEX affiliates. Id. TT 33-34150-55, 110. Because the conspirators and their affiliates were the domi-nant purchasers of removal services in New York State, Discon's exclusion from NYT's business caused it to cease operations. Id.¶¶ TT 299 557 1087 113. See Pet. App. 5a-6a.[2]

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2. Discon brought suit against petitioners in May 1990 and, following dismissal of its original complaint, filed an amended complaint in July 1992. The amended complaint alleged, in relevant part, that the above-described conduct violated Sections 1 and 2 of the Sherman Act, 15 U.S.C. ly 2. See Pet. App. 6a. In June 1995, the district court granted petitioners' motion to dismiss for failure to state a claim. With respect to the Section 1 claims, the court disagreed with Discon's contention that the alleged conspiracy between AT&T and petitioners could be characterized as an unlawful horizontal restraint or as vertical resale price maintenance. Pet. App. 28a-30a. The court further concluded that Discon's Section 1 claims failed because they did not adequately allege a

Discon’s Section 1 claim, albeit on "a different legal

liable for conspiracy to monopolize where it agrees with another firm to assist that firm in its attempt to monopolize the relevant market." Id. at 14a.

DISCUSSION

In our view, the court of appeals' interlocutory ruling does not warrant review. The court's holding that Discon's complaint states a claim under the Sherman Act is correct and creates no conflict with decisions of this Court or other courts of appeals. We nonetheless acknowledge that certain language in the court's opinion was not well-chosen, such as the court's use of the term "group boycott" to character-that certaintBe Tc 0.187

the Sherman Act to claims involving regulatory evasion schemes should await a lower court decision applying the law to a more fully developed record.

1. The court of appeals correctly reversed the district court's dismissal of Discon's claim that the vertical conspiracy between petitioners and AT&T violated Section 1 of the Sherman Act. It should be emphasized that the courts were assessing that claim at the outset of the case on a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6)., This Court has repeatedly instructed that complaints, including antitrust complaints, are to be "liberally construed" at that stage, and "should not be dismissed unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." Hartford Fire Ins. Co. v. California, 509 U.S. 764, 811 (1993) (internal quotation marks omitted). A dismissal at the pleading stage is "especially disfavored" where, as here, the case presents "a novel legal theory that can best be assessed after factual development." Baker v. Cuomo, 58 F.3d 814, 818-819 (2d Cir.) (citing 5A Charles A. Wright, et al., Federal Practice and Procedure § 1357, at 341-343 (1990)), cert. denied, 116 S. Ct. 488 (1995). Liberally construed, Discon's complaint alleges that petitioners and AT&T agreed (1) that petitioners would purchase removal services from AT&T at inflated prices, a portion of which would be returned to petitioners in the form of secret rebates, so that they could evade regulatory constraints on the pricing of local telephone services; and (2) that petitioners and AT&T would seek to exclude Discon from the market for removal services because its conduct threatened petitioners' ability to evade regulation and

thus overcharge NYT's customers (Complaint ¶ 41).[4] Such a conspiracy could cause anticompetitive effects in both the local telephone market and the removal services market.

The primary object of the alleged conspiracy was to garner for petitioners the very supracompetitive profits that state regulation of NYT's rates was designed to prevent.[5] According to the complaint, petitioners' and AT&T's agreement to exclude Discon, as part of their effort to avoid regulatory scrutiny, was designed to facilitate petitioners' exercise of market power over NYT's customers. An increase in consumer prices resulting from the exercise of market power is an anticompetitive effect of the sort that Section 1 is designed to prevent. See, e.g., Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 13 n.19 (1984) (explaining that exercise of market power through tying arrangements has "anticompetitive effects" when "used to evade price control in the tying product through clandestine transfer of the profit to the tied product") (quoting Fortner Enterprises, Inc. v. United States Steel Corp., 394 U.S. 495, 513 (1969) (White, J., dissenting)); id. at 35 & 36 n.4 (O'Connor, J., concurring) (acknowledging that tying arrangements may present antitrust concerns when they "abet the harmful exercise of market power that

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[4] Although the complaint does not explain why Discon's continued participation in the market threatened the scheme's success, it may be that Discon's competing bids constrained the conspirators' ability to mask the regulatory circumvention.

[5] See generally Thomas G. Krattenmaker, Telecommunications Law & Policy 516 (1994) (explaining that inflating the price of equipment through an unregulated affiliate is a substitute, albeit an "imperfect" one, for a "straightforward monopolistic" price increase).

the seller possesses in the tying product market" by enabling the seller to evade price controls).[6] Although here the exercise of market power occurred in a market different from the one in which the restraint was imposed, that fact does not place a restraint beyond the reach of Section 1. See, e.g., Jefferson Parish, 466 U.S. at 29-30 (noting that exclusive dealing arrangement may involve restraint in one market that causes anticompetitive effects in another market)[7]

The alleged agreement to exclude Discon also had the potential to distort competition in the market for removal services, thereby causing additional injury to consumers in the downstream telephone services market.[8] A monopolist, even if regulated, ordinarily

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[6] The anticompetitive effect flowing from petitioners' and AT&T's scheme is the exercise of market power, and not its creation or augmentation. Section 1, however, is not concerned only with the creation and augmentation of market power. Section 1 condemns restraints that cause "detrimental effects," for which market power is "but a 'surrogate.'" FTC v. Indiana Fed'n of Dentists, 476 U.S. 447, 460-461 (1986) (quoting 7 Phillip E. Areeda, Antitrust Law ¶ 1511, at 429 (1986)).

[7] Absent unusual circumstances, when an exercise of market power produces higher consumer prices, a decrease in output will also occur. Thus, petitioners' and AT&T's alleged agreement to exclude Discon, by enabling petitioners to raise their "monopoly profits over what they would be absent the [restraint]," undesirably "increase[d] the social costs of market power." Jefferson Parish, 466 U.S. at 14-15 (discussing tying that facilitates price discrimination); id. at 36 n.4 (O'Connor, J., concurring) (acknowledging that tying arrangements may violate Section 1 when they decrease output).

[8] In certain circumstances, a purchaser's agreement to exclude a supplier of particular goods or services might also harm other purchasers of those goods or services. Discon, however, did not expressly allege such an effect. It identified NYT and

has an incentive to purchase from the supplier who offers the lowest price, because that enables the monopolist to maximize its profits by lowering its costs and increasing its sales. That incentive is aligned with the interests of consumers. A regulatory

market, when that agreement has the purpose and effect of enabling the monopolist to evade regulatory scrutiny and exercise market power in a downstream market, violates Section 1 in the absence of any procompetitive justification. We do not suggest that there will be many cases in which such a claim can be substantiated. Nor do we rule out the possibility of summary judgment in favor of petitioners here. The court of appeals, however, was correct to reverse the dismissal on the pleadings and remand the case for further proceedings.

2. Petitioners contend (Pet. 12) that this case warrants review at this preliminary stage because the court of appeals' opinion creates a "two-firm supplier-purchaser group boycott rule [that] threatens to swallow up the rule that purchasers may choose their suppliers." Although the court misused the "group boycott" label in describing the claim, we do not believe that its opinion threatens the mischief that petitioners suggest. And because "[t]his Court reviews judgments, not statements in opinions," *California v. Rooney*, 483 U.S. 307~ 311 (1987) (per curiam) (internal quotation marks omitted), the court's incorrect description of the claim does not justify review.

a. The court of appeals characterized the charged conspiracy as a "two-firm vertical" agreement "to discriminate in favor of one supplier over another." Pet. App. 12a. Although the court's opinion is not completely clear, it suggests a three-step analysis for such schemes: (1) the scheme will be denominated a "group boycott" if it is alleged to have anticompetitive effects and no procompetitive justification; (2) such a

scheme might be unlawful per se if the defendant fails to advance a valid procompetitive justification; and (3) if a procompetitive justification is substantiated, the scheme should be evaluated under the rule of reason.'O

This Court, however, consistently has used the term "group boycott" to describe a category of conduct that is illegal per se; that is, conduct properly labeled a "group boycott" is condemned without any further inquiry into its anticompetitive effects or procompetitive justification. See, e.g., *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207, 212-213 (1959); see also *FTC v. Indiana Fedn of Dentists*, 476 U.S. 4477 458 (1986); *Northern Pac. Ry. v. United States*, 356 U.S. 1~ 5 (1958). Application of the *per se* rule serves the salutary purpose of "provid[ing] guidance to the business community" and "minimiz[ing] the burdens on litigants and the judicial system of the more complex rule-of-reason trials." *Continental T. V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 50 n.16 (1977).

Because the *per se* rule applicable to group boycotts permits no defense, this Court has mandated the exercise of Islome care" in defining "[exactly what

tionery & Printing Co., 472 U.S. 284, 294 (1985); *Indiana Fed'n, of Dentists*, 476 U.S. at 458 ("the category of restraints classed as group boycotts is not to be expanded indiscriminately"). The category is thus restricted to "form[s] of concerted activity characteristically likely to result in predominantly anticompetitive effects," Northwest Wholesale Stationers, 472 U.S. at 295, such as where "firms with market power boycott suppliers or customers in order to discourage them from doing business with a competitor," Indiana Fed'n of Dentists, 476 U.S. at 458.

Under this Court's cases, the type of restraint at issue here-a two-firm vertical agreement to exclude a supplier-cannot properly be termed a group boycott. As the court of appeals acknowledged (Pet. App. 12a), "[”In the vast majority of cases, the decision to discriminate in favor of one supplier over another will have a pro-competitive intent and effect." That correct observation precludes categorical condemnation of
such agreements."

The court of appeals, however, employed the terms "group boycott" and "per se" analysis differently than has this Court. The court used "group boycott" not to refer to a category of restraint that is condemned, in every case, because of its inherently anticompetitive character, but to denote a vertical agreement

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[11] Virtually any requirements contract could be characterized as a “two-firm vertical” agreement “to discriminate in favor of one supplier over another.”Pet. App. 12a. Yet, such agreements are considered to enhance efficiency, and thus are not subject to categorical invalidation. See Jefferson Parish, 466 U.S. at 45 (O’Connor, J., concurring); Tampa Elec. Co. V. Nashville Coal Co., 365 U.S. 320,334(1961) Standard Oil Co. V. United States,337 U.S. 293,306-307(1949); U.S. Healthcare, Inc. v. Healthsource, Inc., 986 F.2d 589, 595(1st Cir. 1993).

to exclude a supplier when, in a particular case, the agreement allegedly has solely anticompetitive effects. And the court stated that the *per se* rule applies to such agreements only after a detailed

inquiry into effects and justification-the very sort of inquiry that, as this Court has explained, the *per se* rule is designed to avoid. See *Northwest Wholesale Stationers*, 472 U.S. at 289; *Continental T.V.*, 433 U.S. at 50 n.16.'

b. Although the court of appeals' use of the terms "group boycott" and "*per se"* is at odds with this Court's decisions, we do not believe, as petitioners and amici assert (Pet. 12-13; CEMA Br. 9-12; N.Y. Bar Br. 5), that the court's opinion threatens to undermine the analysis of vertical non-price restraints articulated in *Continental T.V.* and *Business Electronics Corporation v. Sharp Electronics Corp*., 485 U.S. 717 (1988). The court of appeals declined to decide whether a per se analysis or a rule of reason analysis should be applied on remand to the scheme at issue here. See Pet. App. 13a n.6. And the court confirmed that the rule of reason continues to apply to most "two-firm vertical combinations." See id. at

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[12] The court purported to derive its understanding of group boycotts from Klor's, although conceding that klor's was not "directly on point." Pet. App. 11a. In fact, Klor's turned not on a case-specific assessment of anticompetitive effects and procompetitive justifications, but on a categorical evaluation of

12a ("in general, two-firm vertical combinations will be scrutinized as exclusive distributorship controversies, " which "are generally considered permissible under the rule of reason" (citing Sharp, 485 U.S. at 725-731 & n.4)).

The court of appeals did not precisely delineate the analysis that the district court is to conduct on remand. The court did make clear, however, that petitioners' conduct could not be condemned, whether under rule of reason analysis or under its version of *per se* analysis, without an evaluation of its procompetitive justifications. See Pet. App. 12a (recognizing

Rep. (CCH) T 50,157 at 49,191 (Nov. 7, 1996) (noting that the Department of Justice uses such an approach to analyze certain types of horizontal restraints). Nothing in the court of appeals' opinion precludes the district court from employing such an approach here. Accordingly, petitioner and *amici* err in asserting (Pet. 9-10; CEMA Br. 7-8; NY Bar Br. 5) that review is justified because the decision below conflicts with decisions of this Court and other courts of appeals. To be sure, the court of appeals' use of certain terminology differs from that of this Court and, arguably,
of those courts of appeals that have required an agreement between competitors in order to invoke the "group boycott" label, see Pet. 9-10 & n.4 (collecting cases); CEMA Br. 7-8 & n.4 (same); see also U.S. Healthcare, Inc. v. Healthsource, Inc., 986 F.2d 589, 594 1st Cir. 1993).[13] The substance of the analysis that the court below suggested, however, does not conflict with this Court's precedents or those of other circuits.

3. The court of appeals' reinstatement of Discon's Section 2 claim likewise does not merit this Court's review, The court correctly held (Pet. App. 14a-15a) that a firm may be liable for conspiring to monopolize when it acts with the specific intent to secure for another firm, although not itself, monopoly power in the target market. See Perington Wholesale, Inc. v.

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[13] We say "arguably" because none of those decisions considered the type of conspiracy alleged in this case. Sherman Act "cases must be read in the light of their facts and of a clear recognition of the essential differences in the facts of those cases, and in the facts of any new case to which the rule of earlier decisions is to be applied." Maple Flooring Mfrs. Assn v. United States, 268 U.S. 5631 579 (1925).

Burger King Corp., 631 F.2d 1369, 1377 (10th Cir. 1979).

Petitioners contend (Pet. 14-15; Reply 3) that this holding conflicts with decisions of several courts of appeals finding permissible a buyer's selection of a particular supplier. The court of appeals, however, did not read the complaint to allege merely that petitioners' use of AT&T instead of Discon conferred a large market share on AT&T; rather, the court appeared to find allegations that petitioners intended

"manifestly anticompetitive" effects and, assertedly, no procompetitive justification.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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