No.

IN THE

Supreme Court of the United States

TEXACO, INC.,

Petitioner,

v.

FOUAD N. DAGHER, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

ROBERT A. MITTELSTAEDT
CRAIG E. STEWART
(Counsel of Record)
MARTHA BOERSCH
JONES DAY
555 California Street, 26th Floor
San Francisco, CA 94104
(415) 626-3939

JOE SIMS
LOUIS K. FISHER
JONES DAY
51 Louisiana Avenue, N.W.
Washington, D.C. 20001
(202) 879-3939

Counsel for Petitioner

QUESTION PRESENTED

Whether it is *per se* illegal concerted action under Section 1 of the Sherman Act for an economically integrated joint venture to set the selling price of its own products.

PARTIES TO THE PROCEEDINGS

The parties to the proceedings in the United States Court of Appeals for the Ninth Circuit were Fouad N. Dagher; Bisharat Enterprises, Inc.; Alfred Buczkowski; Esequiel Delgado; Mahwash Farzaneh; Nasser El-Radi; G.G.&R. Petroleum, Inc.; H.J.F. Inc.; Kaleco Co.; Carlos Marquez; Sami Merhi; Edgardo R. Parungao; Ron Abel Serv. Center, Inc.; Gullermo Ramirez; Jerry's Shell Serv. Center, Inc.; Leopoloo Ramirez; Nazar Sheibaini; Sitara Management Corporation; Tinsel Enterprises, Inc.; Quang Truong; Steven Ray Vezerian; Los Feliz Shell, Inc.; Nassim Hanna; Saudi Refining, Inc.; Texaco, Inc.; Shell Oil Company; Motiva Enterprises LLC; Equilon Enterprises LLC; Equiva Trading Company; and Equiva Services LLC.

Pursuant to Supreme Court Rule 29.6, petitioner Texaco, Inc. states that it is a wholly owned subsidiary of ChevronTexaco Corporation. ChevronTexaco Corporation has no parent company, and no publicly held company owns 10% or more of ChevronTexaco Corporation's stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Texaco, Inc. respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 2a-33a) is reported at 369 F.3d 1108. The opinions of the district court (Pet. App. 34a-69a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on June 1, 2004. Petitioner's timely petition for rehearing and rehearing en banc was denied on September 15, 2004. Pet. App. 1a. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, provides in pertinent part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce . . . is declared to be illegal.

STATEMENT OF THE CASE

This case presents the important, recurring question of when and to what degree the operational decisions of a single entity formed as a joint venture carrying out its own business are subject to scrutiny under Section 1 of the Sherman Act. In an opinion by Judge Reinhardt (over the dissent of Judge Fernandez), the Ninth Circuit ruled not only that Section 1 applies, but that it could be *per se* illegal for a joint venture entity to set the selling price of its own products. This ruling sharply conflicts with decisions of this Court and other courts of appeals, which have recognized that a single entity's operation of its business is not subject to Section 1 analysis at all, let alone to *per se* condemnation, and that this conclusion does not change simply because the

entity was formed as a joint venture combining the businesses of two former competitors. The Ninth Circuit's decision creates a dangerous precedent that will have a significant adverse impact on joint ventures that operate within the Ninth Circuit and will discourage the formation of legitimate, efficiency-enhancing joint ventures that are vital to the national economy. Any such venture that does business anywhere in the broad geographic reach of the Ninth Circuit, as most significant businesses do, now faces the threat of expensive litigation and treble damage liability for routine business conduct that has been and should be viewed as entirely lawful.

Because the Ninth Circuit's decision is so starkly contrary to common sense and basic antitrust principles—and because it significantly impairs the clear, predictable, and nationally uniform rules that are critical to the efficient operation of our economy—this Court should grant certiorari to correct this error, resolve the conflict in decisions, and bring needed certainty to this important area of antitrust law.

A. The Joint Ventures

In 1996, Shell and Texaco began discussing the formation of a new company to consolidate their domestic gasoline refining and marketing operations. After months of study, they concluded that the consolidation could result in reduced costs and increased efficiencies that would save approximately $800 million per year. A single new company would allow refineries located close together to share inputs and transportation costs, allow increased use of company-owned pipelines, and permit more effective advertising and sales promotion.

In 1998, the discussions culminated in the complete integration of the gasoline refining and marketing businesses of Shell and Texaco in the United States. The assets that Shell and Texaco contributed included twelve refineries, twenty-three lubricant plants, two research laboratories, 22,000 branded service stations, over 24,000 miles of

pipeline, 107 terminals, and approximately 24,000 employees. The new businesses formed in the integration (named Equilon and Motiva[1]) also received the exclusive rights to market gasoline in the United States under the Shell and Texaco brands.

The result of this transaction was that Shell and Texaco exited the gasoline refining and marketing business in the United States. They transferred the relevant assets to the joint ventures and signed non-competition agreements that prohibited them from competing with the joint ventures. Shell and Texaco thus became merely the owners of the new entities that had the sole rights to refine and market Shell and Texaco gasoline. The formation of these companies was effectively a merger of Shell's and Texaco's former gasoline refining and marketing businesses, and Shell and Texaco stood in the same relation to the new entities as do shareholders to a corporation.

Reflecting the complete integration of their former businesses, the profits Shell or Texaco could earn from the entities were no longer derived from the quantity of any specific brand the entities sold. Instead, Shell's and Texaco's gains or losses depended on the overall profitability of the entities, and were divided in proportion to the assets each company contributed at formation. Thus, neither Shell nor Texaco had a specific interest in the price charged for the particular brand sold by the ventures. Following their formation, the entities charged the same price in any particular region for Shell-branded and Texaco-branded gasoline.

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[1] Because Texaco had previously formed a venture with Saudi Refining, Inc. that included its refining and marketing assets in the eastern half of the country, this new combination took the form of two separate ventures—one (Motiva) covering the eastern part of the country and including SRI, and the other (Equilon) involving just Shell and Texaco covering the western half of the United States.

The Federal Trade Commission and the attorneys general of four western States comprehensively reviewed the effective merger of these businesses for compliance with the antitrust laws. Each of these antitrust regulators concluded that, with certain divestitures, the combination did not violate either Section 7 of the Clayton Act or Section 1 of the Sherman Act, and allowed the transaction to proceed. Consent decrees were entered to that effect in 1997 and 1998. The consent decrees reflected that the ventures achieved significant economic efficiencies. As the Ninth Circuit acknowledged, "[t]here is a voluminous record documenting the economic justifications for creating the joint ventures." Pet. App. 4a.

B. This Lawsuit

In 1999, service station owners who bought gasoline from Equilon filed this lawsuit under Section 1 of the Sherman Act. Without challenging Equilon's legitimacy or its right to produce and sell gasoline, the plaintiffs alleged that it was *per se* illegal price-fixing for Equilon to charge the same price for the Shell brand as for the Texaco brand.[2] The plaintiffs (understandably) disavowed any attempt to prove a violation of Section 1 under a "rule of reason" analysis, which would have required that they demonstrate that Equilon's pricing decision actually had anticompetitive effects in some relevant market. Instead, they sought to prevail solely on the basis that Equilon's pricing of its own gasoline could be held unlawful without any analysis of its actual competitive impact.

The district court, which had jurisdiction under 28 U.S.C. § 1331, granted the defendants' motion for summary

[2] The plaintiffs asserted a similar claim against Motiva, but the district court dismissed that claim, and the Ninth Circuit affirmed, because none of the plaintiffs had purchased from Motiva. *See* Pet. App. 34a-45a; *id.* at 10a-12a. The only claims at issue are therefore those related to Equilon.

judgment. The court concluded that Equilon was bona fide and could not reasonably be viewed as a sham designed to disguise an ulterior anticompetitive purpose. Pet. App. 54a-66a. The district court further ruled that it did not violate the antitrust laws for this bona fide single entity to price its own products "[l]ike any other business." *Id.* at 63a. The court found it irrelevant that Equilon charged the same price for the Shell and Texaco brands. As the court explained: "Whether Equilon and Motiva charge the same or different prices for both brands, each literally 'fixes' a price where [Shell and Texaco] formerly set prices independently. Yet they and every other joint venture must, at some point, set prices for the products they sell." *Id.* at 52a-53a. Holding that it is illegal for a joint venture to fix the prices of its various brands would "act as a *per se* rule against joint ventures between companies that produce competing products." *Id.* at 54a.

C. The Ninth Circuit's Divided Decision

In a split decision, the Ninth Circuit reversed. The majority (Reinhardt and Rawlinson, JJ.) held that Equilon's decision to charge the same price for the Shell and Texaco brands was *per se* illegal unless the defendants could show that that particular pricing decision was "reasonably necessary" to achieve the anticipated efficiencies that led to Equilon's creation. Pet. App. 21a.

The majority acknowledged that, "for some purposes at least," joint ventures that consist of a true pooling of assets and sharing of risks are to be considered "single firms competing with other sellers in the market." Pet. App. 16a (quoting *Arizona v. Maricopa Cty. Med. Soc'y,* 457 U.S. 332, 356 (1982)). The majority further acknowledged that Equilon involved such a "collective assumption of risk and resource pooling." Pet. App. 5a. But the majority concluded that Equilon's integrated nature did not prevent application of Section 1 to Equilon's pricing of its own products because there supposedly was evidence that Shell and Texaco had

agreed "in advance" that, once Equilon was formed, it would charge the same price for each brand. *Id.* at 19a n.11. To the majority, this meant that the pricing decision "was not a decision made by a single economic entity—it was a decision made by competitors." *Id.*

Applying Section 1, the majority concluded that the legality of Equilon's pricing depended on whether "setting one, unified price for both the Texaco and Shell brands of gasoline instead of setting each brand's price independently on the basis of normal market factors . . . is reasonably necessary to further the aims of the joint venture." *Id.* at 21a. If not, the court held, it might be simple naked price-fixing, and thus *per se* illegal.

Applying its narrow focus on Equilon's actual pricing strategy, the majority concluded that the evidence did not establish the requisite necessity because, in the court's view, the defendants did not view unified pricing of the two brands as critical to the efficiencies and anticipated cost savings from Equilon's creation. *Id.* at 23a. And the court rejected the argument that businesses must have the freedom to choose the prices at which they will sell their products without being second-guessed by the courts. It asserted that that argument "proves too much" because it would permit companies to "create joint ventures as fronts for price-fixing"—although the court did not suggest that Equilon was a sham or anything other than a bona fide single entity merely pricing the products it produced, owned, and sold. *Id.* at 26a. The majority dismissed as irrelevant whether Equilon's pricing strategy had any actual competitive consequences. Having labeled Equilon's price-setting as "price-fixing," the majority held that the *per se* rule forbids any such inquiry.

Judge Fernandez dissented. He began with the undisputed premise that there was "no doubt that each of the new entities is a true, bona fide, economically integrated joint venture." *Id.* at 29a. He concluded that "nothing more

radical is afoot than the fact that an entity, which now owns all of the production, transportation, research, storage, sales and distribution facilities for engaging in the gasoline business, also prices its own products." *Id.* at 31a-32a. Judge Fernandez rejected the majority's assertion that liability depended on whether the defendants could show that Equilon's specific pricing strategy was "essential [or] 'reasonably ancillary to the legitimate cooperative aspects of the venture.'" *Id.* at 31a. Instead, it was enough that Equilon needed "to price its own goods." *Id.* at 32a. As he stated, "[w]hat could be more integral to the running of a business than setting a price for its goods and services?" *Id.* Because Equilon was thus a "separate entity" entitled to price its own products, it was irrelevant that it "decided to price them the same, as any other entity could." *Id.* at 31a, 32a. The result of the majority's ruling, Judge Fernandez concluded, was that bona fide joint ventures would be subject "to the severe sting of antitrust liability" simply for conducting themselves on the same basis as any other "true business." *Id.* at 32a.

REASONS FOR GRANTING THE WRIT

Mergers, joint ventures, and other forms of business combination have long been recognized as an important means of achieving pro-consumer business objectives favored by the antitrust laws. They allow companies to achieve procompetitive efficiencies by eliminating redundancies, obtaining economies of scale, and facilitating access to complementary resources. *E.g., Copperweld Corp. v. Independence Tube Corp.,* 467 U.S. 752, 768 (1984) ("[M]ergers, joint ventures, and various vertical agreements, hold the promise of increasing a firm's efficiency and enabling it to compete more effectively.").[3]

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[3] *Accord Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.,* 472 U.S. 284, 295 (1985) (joint purchasing venture

Recognizing these procompetitive benefits, this Court has evaluated joint ventures under antitrust rules that do not needlessly deter or penalize them. In an important trilogy of cases, for example, the Court established that restraints ancillary to legitimate joint ventures are to be judged under the rule of reason. *See Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.,* 472 U.S. 284, 295 (1985); *NCAA v. Bd. of Regents*, 468 U.S. 85, 100-01 (1984); *Broadcast Music, Inc. v. CBS, Inc.,* 441 U.S. 1, 19-20 (1979). As observed by leading antitrust commentators, "the legal and economic literature on joint ventures is largely favorable toward them, and antitrust generally begins its analysis with a presumption of legality." XIII Herbert Hovenkamp, *Antitrust Law* ¶ 2121b, at 117-18 (2d ed. 2005).

The Ninth Circuit's decision radically departs from this law, and creates a circuit split on an issue that demands clear, nationally uniform rules. Its ruling that Section 1 applies here conflicts with the conclusions of other courts and the leading antitrust commentators that a joint venture entity is a single firm when it runs its own business by, for example, selecting suppliers, purchasing inputs, choosing what markets to sell in, or selling its own output. As a single firm, its actions, like those of any other single company that buys or sells products in the marketplace, are unilateral actions not

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"permits the participating retailers to achieve economies of scale in both the purchase and warehousing of wholesale supplies, and also ensures ready access to a stock of goods that might otherwise be unavailable on short notice"); *NCAA v. Bd. of Regents,* 468 U.S. 85, 103 (1984) ("a joint selling arrangement may be so efficient that it will increase sellers' aggregate output and thus be procompetitive"); Thomas A. Piraino, Jr., *Reconciling Competition and Cooperation: A New Antitrust Standard for Joint Ventures*, 35 Wm. & Mary L. Rev. 871, 876 (1994) ("A joint venture may allow its partners to achieve economic efficiencies that they could not have accomplished on their own. In the long run, such efficiencies may outweigh any restriction of competition caused by a joint venture.").

subject to Section 1. Similarly, even in circumstances in which Section 1 may properly be applied to restraints related to a legitimate joint venture, other circuits have held that those restraints must be evaluated under the rule of reason, not condemned as *per se* illegal without any evaluation of their actual effects in the marketplace. The First and Eleventh Circuits have specifically so held with respect to pricing decisions associated with a joint venture. The Ninth Circuit's ruling directly conflicts with those rulings. The Ninth Circuit's decision also conflicts with decisions of other circuits that have applied the rule of reason to evaluate similar kinds of restraints associated with joint ventures.

This Court's resolution of this conflict is urgently needed. The Court recently granted certiorari in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP,* 124 S. Ct. 872 (2004), to address the much-litigated question of a firm's liability under Section 2 for refusing to deal with rivals. In overturning the Second Circuit's ruling, the Court warned that mistaken application of the antitrust laws "and the resulting false condemnations are especially costly, because they chill the very conduct the antitrust laws are designed to protect." *Id.* at 882 (internal quotation marks omitted). That is precisely the consequence that will flow from the Ninth Circuit's mistaken ruling here, which is no less pernicious than the Second Circuit's ruling in *Verizon* and which, because of the Ninth Circuit's size and the national scope of many joint ventures, has implications for businesses throughout the national economy.

This case is an ideal vehicle for resolving these issues, as it vividly illustrates the unfairness that results from misapplication of the antitrust laws. Equilon is a classic example of a bona fide, efficiency-enhancing integrated business. Its creation was extensively reviewed, and consented to, by federal and state antitrust regulators. No challenge is made to its existence or right to produce and sell its own products. Yet, the Ninth Circuit has ruled that the act of pricing its own products is subject not only to antitrust

scrutiny but to *per se* condemnation. No conceivable antitrust policy is served by this judicial intrusion into the internal decisionmaking of a legitimate business. The conduct here was the competitive equivalent of General Motors (itself the product of various business combinations in the past) deciding to set the same price for its Chevrolet Malibu and Pontiac Grand Am. Condemning such conduct will unfairly penalize legitimate behavior, burden the courts with pointless litigation, and deter the formation of procompetitive businesses.

This Court should grant certiorari to overturn the Ninth Circuit's ruling and make clear that a legitimately formed joint venture entity has the same right under the antitrust laws as does any other single entity to make unilateral decisions about its business operations without fear of attack under Section 1 of the Sherman Act and possible *per se* condemnation.

I. CERTIORARI SHOULD BE GRANTED TO RESOLVE THE CIRCUIT CONFLICT AS TO THE PROPER TREATMENT UNDER SECTION 1 OF THE SHERMAN ACT OF A JOINT VENTURE ENTITY'S OPERATION OF ITS OWN BUSINESS.

A. The Ninth Circuit's Ruling That Section 1 Applies Is At Odds With The Decisions Of This Court And Other Circuits.

The threshold question in any case under the Sherman Act is whether the conduct in question is that of a single firm or multiple firms. That is because "[t]he Sherman Act contains a basic distinction between concerted and independent action." *Copperweld*, 467 U.S. at 767 (internal quotation marks omitted). Section 1 "reaches unreasonable restraints of trade effected by a 'contract, combination . . . or conspiracy' between *separate* entities." *Id.* at 768 (quoting 15 U.S.C. § 1). It does not reach "[t]he conduct of a single firm," which "is governed by § 2 alone and is unlawful only when it threatens actual monopolization." *Id.* at 767

(footnote omitted). This more exacting standard for concerted action reflects Congress' judgment that concerted action carries greater competitive risk because it "represent[s] a sudden joining of two independent sources of economic power previously pursuing separate interests"—a "merging[] of resources" that "increases the economic power moving in one particular direction." *Id.* at 769, 771. By contrast, decisions within a single firm do not represent such a "merging[] of resources" and are not subject to Section 1 scrutiny, thus leaving companies free to vigorously compete without having their "every action [subjected] to judicial scrutiny for reasonableness." *Id.* at 775.

The Ninth Circuit's ruling that Equilon's operation of its own business is concerted action rather than single firm conduct is at odds with decisions of this Court and of other circuits. In a passage that describes this case nearly exactly, this Court observed in *Arizona v. Maricopa County Medical Society,* 457 U.S. 332 (1982), that a joint venture "in which persons who would otherwise be competitors pool their capital and share the risks of loss as well as the opportunities for profit. . . . is regarded as a single firm competing with other sellers in the market." *Id.* at 356. The Court thus recognized that, in such a cooperative venture, "a price-fixing agreement among the [partners] would be perfectly proper." *Id.* at 357. As discussed below, this principle should have led the Ninth Circuit to rule that Section 1 does not apply to the pricing decisions here.

Similarly, in *Chicago Professional Sports Limited Partnership v. NBA,* 95 F.3d 593 (7th Cir. 1996), the Seventh Circuit observed that the NBA may be "best understood as one firm when selling broadcast rights to a network in competition with a thousand other producers of entertainment, but is best understood as a joint venture when curtailing competition for players who have few other market opportunities." *Id.* at 600; *see also Mt. Pleasant v. Associated Elec. Coop.,* 838 F.2d 268, 276 (8th Cir. 1988) (holding that Section 1 does not apply to the pricing

decisions of an electric cooperative as a purported conspiracy among its members); *Nurse Midwifery Assocs. v. Hibbett,* 918 F.2d 605, 616 (6th Cir. 1990) (recognizing that Section 1 should not apply to decisions of "former competitors operating a joint venture which competes in the market with other sellers").[4]

The Ninth Circuit's decision conflicts with these authorities. In setting a price for its own gasoline, Equilon was acting "as a single firm competing with other sellers in the market." *Maricopa County,* 457 U.S. at 356. Like the "typical joint venture," it was engaged in "research, production [and] distribution *in its own right.*" VII Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law ¶* 1478a, at 319 (2003) (emphasis added). As Judge Fernandez correctly recognized, as a "separate entity," it was entitled to select the price for its own product "as any other entity could." Pet. App. 31a, 32a.

The Ninth Circuit's ruling is also inconsistent with and undermines the approach of the Federal Trade Commission and the Department of Justice in their *Antitrust Guidelines for Collaborations Among Competitors.*[5] Those guidelines recognize that competitor collaborations should be analyzed under the same standards as a merger (which do not subject the merged entity's operation to Section 1 scrutiny) where the collaboration involves an efficiency-enhancing integration of economic activity in the relevant market, ends all competition between the participants in that market, and lasts for a sufficiently long period. *Id.* § 1.3. The formation of

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[4] *See also Addamax Corp. v. Open Software Foundation,* 152 F.3d 48, 52 (1st Cir. 1998) (questioning how far the theory that "the operations of the joint venture represent collaboration of the separate entities that own or control it . . . can be pressed in the case of a truly integrated enterprise whose 'owners' were no more than stockholders").

[5] 4 Trade Reg. Rep. (CCH) ¶ 13,161 (2000) (available at <www. ftc.gov/os/2000/04/ftcdojguidelines.pdf>) [hereinafter *Guidelines*].

Equilon falls squarely within this description. Indeed, the *Guidelines* use an example that is based on Equilon to illustrate a venture that should be treated as a merger. *Id.* Example 1.

B. The Circuits Are Split Over The Circumstances In Which, Assuming Section 1 Applies, The Pricing Decisions Of A Joint Venture May Be Subjected To *Per Se* Treatment.

Even if Section 1 could apply, the Ninth Circuit's holding that a legitimate joint venture's pricing of its own products could be *per se* illegal independently justifies certiorari. The Ninth Circuit ruled that *per se* treatment is required unless the defendants can show that the *particular* pricing strategy adopted by the venture entity—as opposed to the setting of any price at all—is "reasonably necessary to further the legitimate aims of the joint venture." Pet. App. 21a. This ruling directly conflicts with decisions of the First and Eleventh Circuits. In cases in which they applied Section 1 (where the venture did not involve complete economic integration and the owners remained competitors in the relevant market), those circuits nonetheless rejected application of the *per se* rule to pricing decisions associated with a joint venture without requiring any showing of necessity of the kind demanded by the Ninth Circuit.

In *Augusta News Co. v. Hudson News Co.,* 269 F.3d 41 (1st Cir. 2001), the plaintiff sued a joint venture formed by newspaper and magazine distributors to service large chain retailers. The plaintiff alleged that the venture's setting of up-front fees to be paid to retailers in exchange for exclusive distribution contracts was *per se* illegal price-fixing. The First Circuit rejected this contention, holding that the agreement on fees must be evaluated under the rule of reason even though it was the type that would be *per se* illegal if not part of a joint venture. The court reasoned that "it is a standard form of joint venture for local firms to combine to provide offerings . . . that none could as easily provide by

itself, and a joint venture often entails setting a single price for the joint offering." *Id.* at 48. The court ruled that *per se* treatment is limited to the circumstance where the agreement on price is "not part of a larger, legitimate economic venture." *Id.* at 47. In conflict with the Ninth Circuit, the court did not require any proof that the particular fee set by the venture was necessary to the venture's success.

The First Circuit reached the same result in *Fraser v. Major League Soccer, L.L.C.,* 284 F.3d 47 (1st Cir. 2002), where it "disagree[d] completely" with the contention that restrictions on player salaries imposed by Major League Soccer should be treated as a *per se* illegal price-fixing conspiracy among the team operators. *Id.* at 56. The court found "rejection of the *per se* rule [to be] straightforward" because "the extent of real economic integration is obvious," the collaboration served procompetitive purposes, and the actual effects of salary restrictions were "simply too uncertain to warrant application of the *per se* rule." *Id.* at 59. The court evaluated the propriety of the particular details of the salary restrictions under the full rule of reason analysis, not as a prerequisite to applying the rule of reason at all.

Similarly, in *National Bancard Corp. v. Visa U.S.A.,* 779 F.2d 592 (11th Cir. 1986), the Eleventh Circuit held that an agreement among members of the Visa joint venture to charge an interchange fee was governed by the rule of reason. The court ruled that, "[f]or a payment system like VISA to function, rules must govern the interchange of cardholder's receivables" and the interchange fee "represents one such rule." *Id.* at 602. Again, in conflict with the Ninth Circuit's ruling, the court did not require proof that the particular level at which the fee was set was necessary to the enterprise.

The Ninth Circuit's ruling is also contrary to the repeated decisions of other courts of appeals applying the rule of reason to a wide range of other conduct by joint venture entities (including conduct that would be illegal *per se* if

unassociated with a joint venture) without imposing any threshold "necessity" requirement of the type the Ninth Circuit imposed. *See Rothery Storage & Van Co. v. Atlas Van Lines,* 792 F.2d 210, 224 (D.C. Cir. 1986) (applying rule of reason to rule prohibiting members from competing with the joint venture); *United States v. Visa U.S.A.,* 344 F.3d 229, 238 (2d Cir. 2003) (applying rule of reason to judge validity of rules prohibiting Visa member banks from issuing cards of other credit card companies), *cert. denied*, 125 S. Ct. 45 (2004); *Chicago Prof'l Sports,* 95 F.3d at 600 (holding that rule of reason applies to output restriction imposed by the NBA); *Polk Bros., Inc. v. Forest City Enters.*, 776 F.2d 185, 190-91 (7th Cir. 1985) (applying rule of reason to an agreement between members of a joint venture not to compete with respect to certain products from their adjoining stores).

Had this action been brought in any of these circuits, the analysis and the outcome would have been different. The court would have recognized that a bona fide venture must select some price for its products. And it would have found this necessity sufficient by itself to preclude *per se* treatment and would have required that the price-setting decision be evaluated under the rule of reason, if it were subject to Section 1 scrutiny at all.

II. THE PROPER ANTITRUST TREATMENT OF A JOINT VENTURE'S OPERATIONAL DECISIONS IS AN IMPORTANT QUESTION ON WHICH THIS COURT'S GUIDANCE IS URGENTLY NEEDED.

The proper resolution of these issues is a matter of great importance to businesses and the national economy. Businesses contemplating a joint venture (or participating in one already formed) must know the rules that govern their behavior. As this case illustrates, whether Section 1 applies and whether it imposes *per se* liability can have dramatic and potentially devastating consequences for joint venture

participants. Faced with conflicting decisions on these issues, and with the threat of after-the-fact antitrust condemnation and potential treble damage liability created by the Ninth Circuit's decision, companies will inevitably curtail or forego legitimate business ventures.

This threat to joint venture activity has broad practical ramifications. Joint ventures are present in nearly every sector of business and are an increasingly important source of economic growth. *See* Jon G. Shepherd, Editor's Note*, Symposium: Antitrust Scrutiny of Joint Ventures,* 66 Antitrust L.J. 641, 641 (1998); Thomas A. Piraino, Jr., *A Proposed Antitrust Approach to Collaborations Among Competitors*, 86 Iowa L. Rev. 1137, 1139 (2001). As the *Collaboration Guidelines* recognize, competitor collaborations "often are not only benign but procompetitive." *Guidelines,* Preamble. They can produce real consumer benefits because "[c]ooperation is the basis of productivity. It is necessary for people to cooperate in some respects before they may compete in others, and cooperation facilitates efficient production." *Polk Bros.,* 776 F.2d at 188. It is therefore critical that judicial and regulatory enforcement not foster "a perception that antitrust laws are skeptical about" such collaboration and thereby deter their development. *Guidelines*, Preamble.

The issues here go to the core of these concerns, and their resolution will have wide application. Whether Section 1 applies at all is a critical threshold question of importance to a broad range of joint ventures. A ruling that Section 1 does not apply to the kind of conduct at issue here would eliminate much needless litigation and avoid the very kind of misapplication of the antitrust laws—and consequent deterrent to legitimate joint ventures—that this case exemplifies. As one commentator observed, in language that presaged the present case, "[t]reating joint ventures as single entities for limited purposes allows meritless group-boycott and price-fixing claims, which could be erroneously decided under the *per se* rule, to be rejected as a matter of law."

Gregory J. Werden, *Antitrust Analysis of Joint Ventures: An Overview*, 66 Antitrust L.J. 701, 705 n.18 (1998). Similarly, a ruling from this Court on whether and the degree to which proof of "necessity" is a prerequisite to applying the rule of reason in the joint venture context not only would decide the issue for this case and other cases challenging a joint venture's pricing decisions, but would provide guidance for any case involving a restraint alleged to be related to a joint venture.

This case is a compelling vehicle for providing this guidance. The factual setting here—an entity formed by former competitors to combine their production and marketing businesses—is a commonly recurring one. *See* VII *Antitrust Law* ¶ 1478a, at 319 ("typical joint venture" engages in "research, production, or distribution in its own right"). The issues have been illuminated by a detailed decision of the district court and divergent opinions in the Ninth Circuit. The issues have likewise been addressed in numerous other decisions, producing a sharp conflict of views with the decision below.

The Court also has the benefit of considerable scholarly and academic commentary—commentary which has remarked on the confusion in the law relating to joint ventures and the need for this Court's guidance. *See supra* p. 16 and *infra* pp. 19-20, 24-25; *see also* E. Gelhorn & W. Todd Miller, *Competitor Collaboration Guidelines—A Recommendation,* 42 Antitrust Bull. 851, 853 (1997) ("the legal rules and policies applied to competitor collaborations often are confused and confusing"); Howard H. Chang, *et al.*, *Some Economic Principles for Guiding Antitrust Policy Towards Joint Ventures,* 1998 Colum. Bus. L. Rev. 223, 225 ("The antitrust treatment of joint ventures is often tortured."); Piraino, 86 Iowa L. Rev. at 1189 ("Courts, commentators, and the enforcement agencies have disagreed over the standard for determining when a particular restraint should be upheld as ancillary to a joint venture.").

Indeed, the Ninth Circuit's decision itself has sparked recent (and critical) comment. Noting that the "[a]pplication of the antitrust laws to joint ventures has always been unusually enigmatic," the authors described the decision below as "resoundingly amplif[ying] these perplexities." Neal R. Stoll & Shepard Goldfein, *Catch 22 for Joint Ventures,* N.Y.L.J., Aug. 17, 2004, at 3. They concluded that the Ninth Circuit took "an analytically wrong turn" in applying *per se* treatment and should have affirmed the district court's ruling that Equilon's pricing was not unlawful. *Id.*

The issues presented here are fully ripe for review. Only a clear resolution by this Court can bring the needed certainty and predictability to this area of competition law. The Court should grant certiorari to reject the Ninth Circuit's ruling and remove the long shadow the ruling casts on legitimate joint venture activities.

III. THE NINTH CIRCUIT'S RULING WAS FUNDAMENTALLY MISTAKEN.

A. A Joint Venture Entity's Operation Of Its Own Business Is Single Firm Conduct, Not Concerted Action.

There is no question that the decision of two companies to form a joint venture itself is a "merging of resources" to which Section 1 applies (along with Section 7 of the Clayton Act), just as Section 1 (and Section 7) would apply to a complete merger of two previously independent companies. *See United States v. Penn-Olin Chemical Co.,* 378 U.S. 158 (1964) (analyzing under Section 1, and under Section 7 of the Clayton Act, the formation of a joint venture to build a chemical plant).

Similarly, if members of a joint venture entity agree to restrictions on their own activities outside of the venture or to other similar collateral restraints, the courts have recognized that Section 1 would apply to any such agreement. *See, e.g., United States v. Visa U.S.A.,* 344 F.3d

at 238 (applying Section 1 to judge validity of rules prohibiting Visa member banks from issuing cards of other credit card companies).

Neither circumstance is at issue here. The Ninth Circuit did not suggest that Equilon's formation violated Section 1. That formation decision was the subject of extensive antitrust review by the FTC and the state attorneys general, who found Equilon's formation to be lawful, conditioned on certain divestitures. Nor do plaintiffs challenge any collateral restraints entered into in connection with the venture. The pricing strategy at issue here applied only to Equilon's output.

Instead, plaintiffs attack Equilon's operation of its own separate business—*i.e.,* establishing a price for the products it sells. The Ninth Circuit's ruling that this is concerted action is unfounded. The "sudden joining of two independent sources of economic power previously pursuing separate interests" to which Section 1 applies (*Copperweld,* 467 U.S. at 771), is the entity's formation, not its operation once formed. The inapplicability of Section 1 is particularly clear in a case like this, where the joint venture is a complete merger of the former businesses of the companies involved and where the owners have a "complete unity of interest" (*id.*) in the entity's operation because the business' profits are divided based on total sales rather than the sale of any particular brand.

The leading antitrust treatise makes the point clearly: where joint enterprises "are buying and selling in their own right, they can fairly be regarded as single entities whose selling decisions are not 'price-fixing conspiracies' and whose buying decisions are not 'boycott conspiracies.'" VII *Antitrust Law* ¶ 1477, at 316. Thus, "[o]nce a venture is judged to have been lawful at its inception and currently, decisions that do not affect the behavior of the participants in their nonventure business should generally be regarded as

those of a single entity rather than the parents' daily conspiracy." *Id.* ¶ 1478, at 325.

Other commentators agree:

> When a joint venture itself participates in the marketplace, its ordinary actions as a market participant are those of a single entity. Hence, a joint venture acts as a single entity when it purchases inputs from third parties or sets a price or output for sale to third parties of a product not sold to participants.

Werden, 66 Antitrust L.J. at 704-05 (footnotes omitted).

Applying Section 1 of the Sherman Act or Section 7 of the Clayton Act to the agreement to form the venture ensures that the entity itself serves legitimate procompetitive purposes that outweigh any harm to competition. Once that determination is made, no further purpose is served by applying Section 1 to each of the entity's ongoing business decisions, and it would be seriously disruptive to do so. *See* VII *Antitrust Law* ¶ 1478c, at 326 (once a joint venture is itself permitted, its "function will be performed most efficiently by an organization that can operate with the same legal freedoms as the ordinary business entity").

Indeed, permitting an attack on a joint venture's operation of its own stand-alone business would unfairly allow after-the-fact attacks on the entity itself. Equilon was an all-purpose company that produced and sold its own products. Its formation necessarily contemplated that it would set the price for those products, and the FTC and the States determined that it would not violate the antitrust laws for Equilon to have that power. That determination having been made, it is fundamentally unfair to now subject Equilon and its owners to antitrust litigation and potential *per se* condemnation for conducting the very business for which Equilon was created.

The Ninth Circuit tried to justify its contrary result on the ground that Shell and Texaco had allegedly agreed upon the

pricing strategy "in advance" when negotiating Equilon's formation. Pet. App. 19a n.11. But this reasoning only demonstrates the illogic of the Ninth Circuit's decision and highlights the need for this Court's review. When the operation of an economically integrated entity's business is at issue, Section 1's application should not turn on a judge or jury dissecting whether a given decision was that of the entity itself or its owners, or whether it was made when the entity was initially negotiated or thereafter. No competitive consequence attaches to such distinctions. Because the decision does not involve any non-venture activity but only the entity's own operation as to which its owners have no separate economic interests, the effect on the marketplace is identical regardless of when or how the decision was reached. Moreover, the feasibility of entering the joint venture at all, and of achieving any cost savings or potential efficiencies, often will depend on the parties' discussing or agreeing on these issues before the transaction is completed and the new entity formed. Making antitrust scrutiny turn on such timing would generate expensive and pointless litigation, while deterring firms from entering joint ventures or making their entry less well-informed.

The fallacy of the Ninth Circuit majority's approach is further demonstrated by the court's assertion that its "analysis would be different" if Equilon were producing a "new product" or if Shell and Texaco had "merge[d] their current product lines into one collective brand." Pet. App. 27a. The majority did not explain why Section 1 scrutiny should turn on such distinctions. If any competitive significance attends the fact that a joint venture entity is producing something one or more of its members had previously produced rather than a new product, such significance will be accounted for in evaluating the venture's formation and structure. Once the venture itself is found valid, whether it is producing a new product or an old one is irrelevant to any policy underlying Section 1. Nor is it relevant that the combined entity sells its product under two brand names rather

than one. A producer of consumer products is not subject to Section 1 merely because it sells those products under several different brands (a practice that is quite common in many markets), regardless of whether it sets the same price for each or how it reaches its pricing decisions. No different rule should apply to a fully integrated joint venture that chooses to sell its products under multiple brand names rather than one.[6]

B. The Ninth Circuit's Ruling That *Per Se* Treatment May Be Applied Conflicts With This Court's Decisions And Basic Antitrust Principles.

Even if a validly formed joint venture entity's operation of its own separate business could be viewed as concerted action, no conceivable basis exists for condemning it as *per se* illegal. *Per se* rules are reserved for cases in which it can be said confidently that the conduct at issue is "plainly anticompetitive" and likely to have no "redeeming virtue." *Broadcast Music, Inc. v. CBS, Inc.,* 441 U.S. 1, 8 (1979). *Per se* rules are not proper where the restraint is "imposed in the context of business relationships where the economic impact of certain practices is not immediately obvious." *FTC v. Indiana Fed'n of Dentists,* 476 U.S. 447, 458-59 (1986). Thus, as noted above (pp. 13-15), other lower courts

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[6] The Ninth Circuit also suggested that Section 1 scrutiny is necessary to prevent companies from using joint ventures as "fronts for price-fixing." Pet. App. 26a. But single firm treatment is reserved for decisions of a validly formed entity acting in its own right to conduct its own separate business. If no such business has been formed, or if the restraint at issue is something other than the entity conducting its own business, Section 1 may apply. For this reason, the Ninth Circuit's hypothetical of Pepsi and Coca-Cola forming a research joint venture and then using that as a front for fixing the price of soft drinks (Pet. App. 16a) is a straw man. Any such price-fixing would not be part of the research joint venture's business but would be a restraint on the members' activities outside the venture.

have repeatedly rejected *per se* treatment for decisions of the kind here associated with legitimate joint ventures.

The Ninth Circuit, however, held that the *per se* rule applies unless the defendants can show that Equilon's particular pricing strategy was "necessary." The court sought to ground this "necessity" requirement in this Court's decisions in *BMI,* 441 U.S. 1, and *NCAA v. Board of Regents*, 468 U.S. 85 (1984). *See* Pet. App. 21a-22a. But those decisions only confirm the Ninth Circuit's fundamental error.

In holding that the rule of reason governed the joint venture's pricing of the blanket license in *BMI,* this Court did not ask whether the defendants' particular pricing strategy was necessary to achieve the venture's procompetitive purposes. Rather, it was enough that the defendants could not market the license without setting some price for it. In other words, setting a price—some price—was necessary to the venture's success. That is what this Court was referring to when it stated, in the passage quoted by the Ninth Circuit, that joint ventures are not unlawful as price-fixing schemes "where the agreement on price is necessary to market the product at all." 441 U.S. at 23. The ultimate legality of the particular pricing scheme "in all of its many manifestations" was to be examined under the "more discriminating examination" of the rule of reason itself, not through a truncated analysis that considers only its purported necessity. *Id.* at 24. As the Court explained, "[w]hen two partners set the price of their goods or services, they are literally 'price-fixing,' but they are not *per se* in violation of the Sherman Act." *Id.* at 9.

Similarly, the Court's application of the rule of reason in *NCAA* did not turn on the "necessity" of the particular details of the NCAA's rule restricting the number of football games individual schools could televise. In rejecting *per se* treatment for that output limitation (which normally would be subject to *per se* treatment if agreed to by multiple firms), the Court did not require proof that the particular number of

games set by the NCAA was necessary to the NCAA's purposes. Indeed, the Court did not require proof that any output restriction at all was necessary—and the Court's ultimate conclusion was that no output restriction was justified. Instead, *per se* treatment was improper simply because some "degree of cooperation is necessary" for the NCAA's product to exist. 468 U.S. at 117; *see id.* at 101 (citing need for rules governing player eligibility and the conduct of the games themselves).[7]

The Ninth Circuit also relied (Pet. App. 21a) on Professor Hovenkamp but his treatise rejects the Ninth Circuit's new rule. He points out that, where a joint venture makes one or more products, those products "are jointly owned and cannot be sold without an agreement between the owners as to the price that will be charged for them." XI Herbert Hovenkamp, *Antitrust Law ¶* 1908e, at 264 (2d ed. 2005). Nowhere does he suggest that any particular pricing scheme must be necessary. Instead, so long as the joint venturers do "not enter into any agreement to fix the price of their nonventure output," no charge of *per se* unlawful price fixing is legitimate. *Id.*; *see also id.* ¶ 1906d, at 239 ("[M]any forms of joint marketing require an agreement about the price to be charged."); *id.* ¶ 1908e, at 263-64 ("[A]greements about price are often essential to the administration of certain joint ventures, particularly in distribution."). Thus, Professor Hovenkamp concludes:

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[7] No issue appears to have been raised in *BMI* or *NCAA* whether the conduct there was concerted action or single firm behavior. As in the court of appeals cases discussed above (pp. 13-15), however, applying Section 1 was consistent with the fact that in both cases the venture participants continued to produce the underlying product and remained competitors in the relevant market. That is not true here, where Equilon was the sole producer and owner of the gasoline it sold, and Shell and Texaco had exited and no longer competed in the relevant market.

> Th[e] joint setting of a price may often be necessary in cases of joint ownership of the good or service being sold. When the joint owners are also competitors, the result is literally 'price fixing,' but it is a form of price fixing that should, when bona fide, be examined under the rule of reason.

XIII Herbert Hovenkamp, *Antitrust Law* ¶ 2132c, at 180 (2d ed. 2005).[8]

Indeed, applying the *per se* rule in this circumstance makes no sense. The Ninth Circuit effectively held that it could conclude with confidence (and without any market analysis) that Equilon's pricing was necessarily anticompetitive. But even if setting the same price for both brands were not necessary to Equilon's success, that would hardly establish that the pricing strategy was anticompetitive, let alone so inevitably anticompetitive that it may be condemned as *per se* illegal without requiring an evaluation of its actual effect in the marketplace.

The Ninth Circuit asserted that "[n]ormally" businesses will consider a variety of factors in pricing their products and that it "seems likely" that an "independent" analysis would

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[8] *Per se* treatment may be appropriate where the venture does not involve economic integration and the restraint governs the venture owners' conduct as continuing independent competitors in the relevant market. *See Maricopa County,* 457 U.S. at 356-57 (applying *per se* rule to fee schedule adopted by medical association in which the doctors had not "pool[ed] their capital and share[d] the risks of loss as well as the opportunities for profit"); *Citizen Publ'g Co. v. United States*, 394 U.S. 131, 135 (1969) (applying *per se* rule to a newspaper joint venture that set advertising and subscription rates for the individual newspapers but which did not integrate the underlying news and editorial departments of those newspapers, which remained independent competitors); *Timken Roller Bearing Co. v. United States*, 341 U.S. 593, 597-98 (1951) (applying *per se* rule because the "joint venture" involved was a mere sham designed to mask a naked horizontal agreement to allocate territories). That is not the situation here.

result in a "rational decision to sell the different brands at different prices." Pet. App. 23a. How a court could believe itself competent to engage in such analysis is hard to fathom. But even if this analysis were correct, it does not justify *per se* condemnation. Saying that a business might "rationally" decide to adopt one pricing scheme does not establish that any other pricing scheme is invariably anticompetitive and likely to have no redeeming value.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT A. MITTELSTAEDT
CRAIG E. STEWART
(Counsel of Record)
MARTHA BOERSCH
JONES DAY
555 California St., 26th Floor
San Francisco, CA 94104
(415) 626-3939

JOE SIMS
LOUIS K. FISHER
JONES DAY
51 Louisiana Avenue, N.W.
Washington, D.C. 20001
(202) 879-3939

Counsel for Petitioner

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