

## linkLine: Supreme Court Weighs Survival of Price-Squeeze Claims

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Then-Chief Judge Stephen Breyer, writing for the First Circuit in *Town of Concord v. Boston Edison Co.*,<sup>1</sup> in 1990 held that a price squeeze occurring in a fully regulated industry generally will not violate Section 2 of the Sherman Act. Whether a price squeeze in a partially regulated industry would violate Section 2 was left “for another day.”<sup>2</sup>

That day may have arrived with the Supreme Court’s granting certiorari in *Pacific Bell Telephone Co. d/b/a AT&T California v. linkLine Communications, Inc.*<sup>3</sup> The Supreme Court can decide whether price-squeeze claims survive the recent Supreme Court decisions in *Trinko*<sup>4</sup> and *Brooke Group*,<sup>5</sup> and, if so, in what form.<sup>6</sup> The circuits have split on this issue, divided over whether recognizing a price-squeeze claim conflicts with modern antitrust jurisprudence or comports with sound antitrust policy.<sup>7</sup>

### The Margin-Based Price Squeeze Claim

The “traditional” or “margin-based” price-squeeze claim, classically articulated in Judge Learned Hand’s Supreme Court certified opinion in *United States v. Aluminum Co. of America*,<sup>8</sup> arises

<sup>1</sup> 915 F.2d 17 (1st Cir. 1990) (Breyer, C.J.), *cert. denied*, 499 U.S. 931 (1991).

<sup>2</sup> *Id.* at 43.

<sup>3</sup> 128 S. Ct. 2957 (2008) (No. 07-0512) (granting certiorari in *linkLine Commc’ns v. SBC Cal., Inc.*, 503 F.3d 876 (9th Cir. 2007)).

<sup>4</sup> *Verizon Commc’ns, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004).

<sup>5</sup> *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993).

<sup>6</sup> The formal issue is framed as “[w]hether a plaintiff states a claim under Section 2 of the Sherman Act, 15 U.S.C. 2, by alleging that the defendant—a vertically-integrated retail competitor with an alleged monopoly at the wholesale level but no antitrust duty to provide the wholesale input to competitors—engaged in a “price squeeze” by leaving an insufficient margin between wholesale and retail prices to allow the plaintiff to compete.” Petition for Certiorari, *Pac. Bell Tel. Co. d/b/a AT&T Cal. v. linkLine Commc’ns, Inc.*, 128 S. Ct. 2957 (2008) (07-0512), available at [http://www.scotusblog.com/movabletype/archives/07-512\\_pet.pdf](http://www.scotusblog.com/movabletype/archives/07-512_pet.pdf).

<sup>7</sup> Our discussion will primarily address price-squeeze claims as applied to markets that are partially or fully regulated, such as the telecommunications industry. An open issue is whether a margin-based price-squeeze claim should be limited in unregulated markets. Price-squeeze claims have been alleged in the context of unregulated industries, including the seminal price squeeze case, *United States v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945) (*Alcoa*) unregulated aluminum sheet industry). See *Schor v. Abbott Labs.*, 457 F.3d 608, 611 (7th Cir. 2006), *cert. denied*, 127 S. Ct. 1257 (2007) (price-squeeze claim made in pharmaceutical industry where defendant had monopoly over patented input for HIV treatment); Case L-284/41, *Napier Brown-British Sugar*, 1988 O.J. (L 284) 41 at ¶¶ 3–6, 4 C.M.L.R. 196 (1990) (European Commission decision re: price squeeze in granulated beet sugar industry), available at <http://eur-lex.europa.eu/smartapi/cgi/sgadoc?smartapi!celexplus!CELEXnumdoc&lg=en&numdoc=388D0518>. Abbott Laboratories, a pharmaceutical company, submitted a brief as amicus curiae in *linkLine*. Brief for Abbott Labs as Amicus Curiae Supporting Petitioners, *Pac. Bell Tel. Co. d/b/a AT&T Cal. v. linkLine Commc’ns, Inc.*, 128 S. Ct. 2957 (2008) (No. 07-512).

<sup>8</sup> 148 F.2d 416, 437–38 (2d Cir. 1945). *Alcoa* has special precedential value because the Supreme Court certified the case to a panel of judges of the Second Circuit Court of Appeals on the basis that the number of Justices qualified to hear the case was insufficient for a quorum. *Am. Tobacco Co. v. United States*, 328 U.S. 781, 812–13 & n.10 (1946) (Second Circuit decided *Alcoa* “under a new statute authorizing it to render a decision ‘in lieu of a decision by the Supreme Court’ and providing that such decision ‘shall be final and there shall be no review of such decision by appeal or certiorari or otherwise.’”). The origins of the price-squeeze claim can be traced back to *United States v. Corn Products Refining Co.*, 234 F. 964 (S.D.N.Y. 1916).

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when: (1) a firm has a monopoly over an upstream product; (2) its wholesale price for that product is “higher than a ‘fair price;” (3) that firm’s downstream rivals require that product to compete in the downstream market where the monopolist itself competes; and (4) the monopolist’s retail price for the downstream, competitive product is so low that competitors cannot match it and still earn a “living profit.”<sup>9</sup> Determining whether these elements were present has proved challenging for the courts, and lower courts in the United States principally resorted to three tests to determine if a price squeeze claim was shown. Under the “transfer price test,” a price squeeze is presumed to exist if the monopolist could not have made a profit by selling at its retail rates if it had purchased at its own wholesale rates.<sup>10</sup> This test is similar to the “equally efficient competitor” test used in Europe.<sup>11</sup> The other two tests are the “comparative billing” test and the “comparative rate of return” test.<sup>12</sup>

After the Supreme Court decisions in *Brooke Group* and *Trinko*, however, two circuits differed as to whether those decisions limited or precluded margin-based price-squeeze claims.<sup>13</sup> In *Brooke Group*, the Supreme Court held that a predatory pricing claim under Section 2 of the Sherman Act could only be asserted against a firm with monopoly power or one with a dangerous probability of obtaining monopoly power, if (1) “the prices complained of are below an appropriate measure of its rival’s costs” and (2) that firm “had . . . a dangerous probability [ ] of recouping its investment in below-cost prices.”<sup>14</sup> In its later *Trinko* decision, the Supreme Court ruled that even incumbent monopolists generally had no antitrust duty to cooperate with potential rivals, whether or not they had to provide such cooperation under other statutes governing telecommunication utilities. Absent conduct amounting to an independent antitrust violation, the Court declined to impose an expanded duty to aid competitors under the antitrust laws in light of the

<sup>9</sup> *Alcoa*, 148 F.2d at 437–38.

<sup>10</sup> See 1 ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS 271 (5th ed. 2002) (citing *Ray v. Indiana & Mich. Elec. Co.*, 606 F. Supp. 757, 776–77 (N.D. Ind. 1984)) [hereinafter ANTITRUST LAW DEVELOPMENTS]. As discussed more fully below, Petitioners in *linkLine* argue that the “transfer price test” is inconsistent with the monopolist’s right to charge monopoly prices and will discourage investment in the upstream market. Reply Brief for Petitioners at 13, *linkLine*, 128 S. Ct. 2957 (2008) (No. 07-512) [hereinafter Petitioners’ Reply Brief].

<sup>11</sup> Case COMP/C-1/37.451, 35.578, 37.579, *Deutsche Telekom AG*, 2003 O.J. (L 263) 9 at ¶¶ 140–141, (a margin squeeze was present because DT “would have been unable to offer its own retail services without incurring a loss if . . . it had had to pay the wholesale access price as an internal transfer price for its own retail operations”), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2003:263:0009:0041:en:PDF>, *aff’d*, Case T-271/03, *Deutsche Telekom AG v. Comm’n* (Apr. 10, 2008); Case COMP/38.784, *Wanadoo España v. Telefónica*, 2008 O.J. (C 83) 5 (summary of Commission decision). The full text of the Commission’s *Wanadoo* decision is available at the DG Comp’s Web site. See *Wanadoo*, Case COMP/38.784, op. at 83, available at [http://ec.europa.eu/competition/antitrust/cases/decisions/38784/dec\\_en.pdf](http://ec.europa.eu/competition/antitrust/cases/decisions/38784/dec_en.pdf) (Commission held that a margin squeeze “can be demonstrated by showing that the dominant company’s own downstream operations could not trade profitably on the basis of the upstream price charged to its competitors by the upstream operating arm of the dominant company. . .”).

<sup>12</sup> See ANTITRUST LAW DEVELOPMENTS, *supra* note 10, at 271.

<sup>13</sup> See *Covad Commc’ns Co. v. BellSouth Corp.*, 374 F.3d 1044 (11th Cir. 2004) (price squeeze survives *Trinko* but must be pled under *Brooke Group*); *Covad Commc’ns v. Bell Atl. Corp.*, 398 F.3d 666 (D.C. Cir. 2005), *reh’g denied*, 407 F.3d 1220 (D.C. Cir. 2005) (price squeeze not pled under *Brooke Group* does not survive *Trinko*). The D.C. Circuit may actually allow a price-squeeze claim to proceed under *Brooke Group*. *Bell Atlantic*, 407 F.3d at 1222. Denying a petition for rehearing in *Bell Atlantic*, the D.C. Circuit rejected the argument that the court’s decision “eliminate[d]” price-squeeze claims, emphasizing that in its initial decision, the D.C. Circuit had not discussed the possibility of a *Brooke Group* price-squeeze claim because the plaintiffs had not made that claim. *Id.*

<sup>14</sup> *Brooke Group*, 509 U.S. at 222–24.

telecommunications regulatory structure and the practical obstacles that would attend judicial oversight of any order granting compulsory access.<sup>15</sup>

### The *linkLine* case

In *linkLine*, the plaintiff linkLine, an Internet Service Provider (ISP), purchased access to a vertically integrated incumbent local exchange carrier's (ILEC) digital service line (DSL) facilities. The DSL market was only partially regulated, because the FCC and state regulators regulated only wholesale DSL sales, leaving the ILECs with retail price discretion.<sup>16</sup> linkLine claimed that the ILEC's DSL facility was a "bottleneck"—an essential facility—which any ISP would have to interconnect with in the ILEC's service area to serve end-user customers. linkLine contended that the defendant ILEC (AT&T) had engaged in a price squeeze by charging linkLine a wholesale price for DSL transport that was so high at times that it exceeded AT&T's retail price for bundled DSL service to end-user consumers.<sup>17</sup> linkLine further alleged that AT&T's retail arms would not be able to cover their costs by buying wholesale DSL at AT&T's wholesale prices and selling retail DSL at AT&T's low retail prices.

In a 2004 Order, the district court denied AT&T's motion to dismiss the price-squeeze claim, holding that *Trinko* did not preclude such a claim.<sup>18</sup> Subsequently, the district court held that linkLine's allegations could satisfy the below-cost and dangerous probability of recoupment prongs of *Brooke Group*.<sup>19</sup> The district court then certified its 2004 Order for interlocutory appeal to the Ninth Circuit.<sup>20</sup>

The Ninth Circuit affirmed the district court's order in a 2–1 decision, beginning by recognizing the price squeeze as a traditional antitrust claim that survived *Trinko*.<sup>21</sup> Citing *City of Anaheim v. Southern California Edison*,<sup>22</sup> a Ninth Circuit decision predating *Brooke Group* and *Trinko*, the court held that a price-squeeze claim based on a showing of specific intent to monopolize could be viable even in a fully regulated industry.<sup>23</sup> By requiring specific intent to monopolize, the court of appeals found the *City of Anaheim* standard addressed *Trinko*'s point that overlapping telecommunications regulation should weigh against imposing antitrust liability for regulated conduct.<sup>24</sup>

**By requiring specific intent to monopolize, the court of appeals found the City of Anaheim standard addressed Trinko's point that overlapping telecommunications regulation should weigh against imposing antitrust liability for regulated conduct.**

<sup>15</sup> *Trinko*, 540 U.S. at 412–16 (holding that an antitrust "problem should be deemed irremedia[ble] by antitrust law when compulsory access requires the court to assume the day-to-day controls characteristic of a regulatory agency") (quoting Phillip Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 ANTITRUST L.J. 841, 853 (1989)). The Court also cited *Spectrum Sports v. McQuillan*, 506 U.S. 447, 459 (1993), in reaffirming that a monopoly leveraging claim could not be asserted absent a showing of a dangerous probability of success in monopolizing the second market. *Trinko*, 540 U.S. at 415 n.4.

<sup>16</sup> Pac. Bell Tel. Co. d/b/a AT&T Cal. v. linkLine Commc'ns, Inc., 503 F.3d 876, 885 (9th Cir. 2007), *cert. granted*, 128 S. Ct. 2957 (2008).

<sup>17</sup> linkLine Commc'ns, Inc. v. SBC Cal., Inc., No. CV 03-5265 SVW, at 6 (C.D. Cal. Apr. 1, 2005) (order denying AT&T's motion to dismiss and certifying for interlocutory review).

<sup>18</sup> linkLine Comm'ns, Inc. v. SBC Cal., Inc., No. CV-03-5265 SVW, 2004 U.S. Dist. LEXIS 30761 (C.D. Cal. Oct. 25, 2004).

<sup>19</sup> linkLine Commc'ns, Inc. v. SBC Cal., Inc., No. CV 03-5265 SVW, at 6 (C.D. Cal. Apr. 1, 2005) (order denying AT&T's motion to dismiss and certifying for interlocutory review).

<sup>20</sup> *Id.* at 32–33 & n.22.

<sup>21</sup> *linkLine*, 503 F.3d at 880, 885 ("For over six decades, federal courts have recognized price squeeze allegations as stating valid claims under the Sherman Act.").

<sup>22</sup> *City of Anaheim v. S. Cal. Edison*, 955 F.2d 1373 (9th Cir. 1992).

<sup>23</sup> *City of Anaheim* held that a price squeeze could be viable against a regulated monopolist because the presence of multiple regulators regulating at different levels of the market could produce disharmonious rate regulation. *Id.* at 1377.

<sup>24</sup> *linkLine*, 503 F.3d at 883.

The Ninth Circuit distinguished *linkLine* on the grounds that the industry was only partially regulated, unlike in previous price-squeeze cases, such as *City of Anaheim*, where the industry at issue was fully regulated.<sup>25</sup> The antitrust laws thus presented the primary check against consumer harm from AT&T's alleged anticompetitive conduct at the unregulated retail level.<sup>26</sup>

Judge Ronald Gould, in dissent, asserted that *linkLine* should not have been able to base its price-squeeze claim on AT&T's allegedly high wholesale price because that claim would have amounted to a refusal to deal precluded by *Trinko*.<sup>27</sup> According to the dissent, *Trinko* prevented *linkLine* from proceeding on any claims other than a downstream predatory pricing claim that could satisfy *Brooke Group*.<sup>28</sup>

AT&T petitioned for certiorari, urging the Supreme Court to reject the Ninth Circuit's articulation of the price-squeeze doctrine. *linkLine* opposed AT&T's petition, arguing that the Court should allow the Ninth Circuit's decision to stand.<sup>29</sup> The 2005 district court Order, dealing with the applicability of *Brooke Group* to price squeezes, *linkLine* argued, was not within the scope of the interlocutory appeal to the Ninth Circuit of the distinct Court's 2004 Order, and thus was not within the certiorari petition. The Supreme Court nevertheless granted certiorari and permitted an amicus group, the American Antitrust Institute, to participate in oral argument in order that the *Trinko* questions framed by the 2004 district court order and the Ninth Circuit's majority ruling can be addressed. The Supreme Court heard oral arguments on this issue on December 8, 2008. Given the odd procedural posture, it is unclear whether the Supreme Court will ultimately reach the merits. However, the briefing and arguments have illuminated the issues well.<sup>30</sup>

## The Issues

***Does the Existence of a Regulatory Duty Preclude a Price Squeeze Claim?*** Petitioner AT&T and amici supporting its position have challenged the price squeeze's status as a standalone antitrust claim, arguing that it is simply a variation of a refusal to deal claim.<sup>31</sup> In *Trinko* the Supreme Court held that a refusal to deal claim exists only where: (1) the parties had "voluntarily engaged in a course of dealing"; (2) the defendant refused to sell to its competitor even at retail rates; and (3) the services it was withholding were "otherwise marketed or available to the public."<sup>32</sup> AT&T argues that it had no antitrust duty to deal with *linkLine* because the source of that duty was sole-

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<sup>25</sup> *Id.* at 885.

<sup>26</sup> *Id.* ("All of this regulation, however, applies only to wholesale prices the SBC Entities charged *linkLine*: there is no comparable regulatory attention paid to the retail market. Any restrictions on pricing at the retail level derive primarily from the antitrust laws.")

<sup>27</sup> *linkLine*, 503 F.3d at 886–87 (Gould, J., dissenting).

<sup>28</sup> *Id.* at 885.

<sup>29</sup> Brief in Opposition at 14–15, *linkLine*, 128 S. Ct. 2957 (2008) (No. 07-512), available at [http://www.scotusblog.com/movabletype/archives/07-512\\_bio.pdf](http://www.scotusblog.com/movabletype/archives/07-512_bio.pdf). During its oral argument, however, *linkLine* later argued that the Supreme Court should vacate the Ninth Circuit's opinion and remand the case back to the district court for consideration of the *Brooke Group* issues.

<sup>30</sup> This discussion is not intended to be exhaustive, and will be limited to the issues raised by the parties and their amici at the *linkLine* oral arguments and what we found were the most critical issues raised by the parties and their amici, the American Antitrust Institute, COMPETEL, the United States, and a group of law professors and economists, in briefs filed with the Court. These briefs and those briefs filed by other amici are available at [http://www.scotuswiki.com/index.php?title=Pacific\\_Bell\\_Telephone\\_Co.%2Cdba\\_AT%26T\\_California\\_v.\\_linkLine\\_Communications](http://www.scotuswiki.com/index.php?title=Pacific_Bell_Telephone_Co.%2Cdba_AT%26T_California_v._linkLine_Communications).

<sup>31</sup> Brief for Petitioners at 13–16, *linkLine*, 128 S. Ct. 2957 (2008) (No. 07-0512) (U.S. Aug. 28, 2008).

<sup>32</sup> See *Trinko*, 540 U.S. at 409–10.

*The issue in linkLine is whether a regulatory duty to deal with respect to the regulated aspect of the parties' relationship is relevant to an antitrust claim based on its impact in the unregulated aspect of their relationship.*

ly regulatory. AT&T has never voluntarily dealt with the plaintiff, at a retail rate or otherwise.<sup>33</sup> And if AT&T had no antitrust duty to deal with rivals, then AT&T had no antitrust duty to deal on any particular terms that would assist its rivals to compete.<sup>34</sup>

As a threshold matter, the reference to an “antitrust duty to deal” is a misnomer. Antitrust law imposes no general affirmative duty to deal with anyone.<sup>35</sup> Nevertheless, antitrust cases have recognized in special circumstances that a firm can be liable for an anticompetitive “refusal to deal.”<sup>36</sup> The issue in *linkLine* is whether a regulatory duty to deal with respect to the regulated aspect of the parties’ relationship is relevant to an antitrust claim based on its impact in the unregulated aspect of their relationship. Professor J. Gregory Sidak has argued that when an upstream price regulator can consider downstream competition,<sup>37</sup> a court should not consider the margin between upstream and downstream prices.<sup>38</sup> On the other hand, if that regulator can consider only one of the two affected markets (or lacks authority to consider either market, leaving a regulatory gap), then the court can consider whether the price charged constitutes a refusal to deal violating that antitrust laws.<sup>39</sup> Professor Sidak is of the view that a court may consider whether the monopolist’s unregulated retail price is predatory even if an upstream price regulator could consider downstream competition.<sup>40</sup> He argues, however, that a price squeeze should be understood as a “rule of price regulation” arising in the context of an already regulated industry,<sup>41</sup> and permitting courts to inject themselves based on antitrust law would result in inappropriate overlap because (1) courts should not re-regulate an unregulated or lightly regulated market, and (2) courts lack the institutional competence to act as public utility regulators.<sup>42</sup>

<sup>33</sup> Brief for the United States as Amicus Curiae Supporting Petitioners at 9, *linkLine* 128 S. Ct. 2957 (2008) (No. 07-512) [hereinafter U.S. Amicus Brief]; see also Brief for Petitioners, *supra* note 31, at 19–20 (“no allegation that AT&T ever refused to provide to respondents any product ‘that it already sold at retail’ to other customers”).

<sup>34</sup> Brief for Petitioners, *supra* note 31, at 20 (“*Trinko* . . . establishes that where AT&T has no duty to deal with respondents, it likewise has no duty to deal with them in a manner that would promote their success in the alleged downstream market for DSL-based Internet-access service.”).

<sup>35</sup> *United States v. Colgate Co.*, 250 U.S. 300, 307 (1919) (“In the absence of any purpose to create or maintain a monopoly, the [Sherman] [A]ct does not restrict the long recognized right of trader or manufacturer . . . to exercise his own independent discretion as to parties with whom he will deal. . . .”).

<sup>36</sup> *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 483 n.32 (1992) (stating that though a firm generally can refuse to deal with its competitors, it must have a legitimate competitive reason for doing so”); *Trinko*, 540 U.S. at 408 (“[T]he high value that we have placed on the right to refuse to deal with other firms does not mean that the right is unqualified.”) (quoting *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 601 (1985)); *Lorain Journal Co. v. United States*, 342 U.S. 143, 155 (1951).

<sup>37</sup> In response to Justice Stephen Breyer’s query of whether there was an alternative forum where *linkLine* could bring its margin-based price-squeeze claim, AT&T argued that *linkLine* could have brought such a complaint to the FCC, the wholesale DSL transport price regulator. Transcript of Oral Argument, *linkLine*, at 16, 128 S. Ct. 2957, No. 07-0512 (Dec. 8, 2008), available at [http://www.supremecourtus.gov/oral\\_arguments/argument\\_transcripts/07-512.pdf](http://www.supremecourtus.gov/oral_arguments/argument_transcripts/07-512.pdf).

<sup>38</sup> J. Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4 J. COMPETITION L. & ECON. 279, 282 (2008).

<sup>39</sup> *Id.* at 282.

<sup>40</sup> *Id.* at 294.

<sup>41</sup> *Id.*

<sup>42</sup> *Id.* Indeed, the FCC has entertained (and rejected) price-squeeze claims made under the 1996 Telecommunications Act, although it seems that no plaintiff has made a price-squeeze claim to the DSL-market regulators. See, e.g., *In re Application of Verizon New England Inc.*, CC No. 01-9 (Feb. 20, 2004) (NYNEX Section 271 proceeding), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DA-04-422A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-04-422A1.pdf).

The antitrust laws, however, especially in the telecommunications space, have historically coexisted with overlapping regulatory regimes.<sup>43</sup> Moreover, *Trinko* held that Congress intended the antitrust laws and telecommunications laws to coexist, because the antitrust-specific saving clause in the Telecommunications Act of 1996 precluded an interpretation of implied antitrust immunity.<sup>44</sup>

In its brief supporting *linkLine*, COMPTTEL, an industry association representing communications service providers and their supplier partners, argues that the monopolist could have an incentive to seek any uncaptured monopoly profit from the regulated market level.<sup>45</sup> COMPTTEL also argues that even in industries where one or both of the relevant markets are regulated, regulation may be lax, imperfect, or unable to prevent a predatory price squeeze.<sup>46</sup> As emphasized by the Ninth Circuit, regulatory imperfections can enable a price squeeze.<sup>47</sup>

Petitioners respond that to the extent there is effective upstream regulation, the regulator can protect consumers by considering whether it enables a price-squeeze claim in the downstream unregulated market. To the extent such upstream regulation is ineffective, a downstream price-squeeze claim makes little economic sense because the ineffectively regulated monopolist would have no need to evade upstream regulation by capturing some of its monopoly rents downstream.<sup>48</sup>

Petitioners argue that, in any case, there is “no incremental harm from price squeezes as distinct from an outright refusal to deal.”<sup>49</sup> A contrary view, however, is that a price squeeze may actually be a more refined anticompetitive tool than an outright refusal to deal because a price squeeze allows the monopolist to win the sales of those downstream customers it prefers. The monopolist can supply preferred customers, presumably the lowest-cost and most profitable customers, by pricing below the wholesale price plus the additional costs that its most efficient competitor would incur. A price squeeze also allows the monopolist to let its wholesale customer win those high-cost or lower-profit downstream customers the monopolist does not wish to serve.<sup>50</sup> A lost sale is a win because it allows the monopolist to (1) utilize its spare capacity in the upstream market, (2) realize lower costs through greater economies of scale, and (3) share in the proceeds of those sales through the inflated portion of the wholesale price. With a refusal to deal, on the

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<sup>43</sup> See *Phonetele, Inc. v. AT&T Co.*, 664 F.2d 716 (9th Cir. 1989) (holding no implied immunity because no “actual repugnancy” between telecommunications regulation and antitrust laws).

<sup>44</sup> *Trinko*, 540 U.S. at 406–07 (holding that antitrust-specific savings clause in section 601(b)(1) of the Telecommunications Act of 1996 barred finding of implied antitrust immunity from coexisting telecommunications regulation) (citing 47 U.S.C. § 152 (2007)). The European Commission (EC) similarly views regulation and antitrust as complements, and not substitutes. Joachim Luecking, Head of Unit Antitrust: Telecoms, DG Competition, European Comm’n, Remarks at Teleseminar, *The Supreme Court’s Pending Review of linkLine: The Death Knell for Price Squeeze Claims in the U.S. and Another Basis for Divergence with the E.U.?* (Nov. 18, 2008). In the European Union, regulation and competition share the same frameworks of analysis and can be applied in parallel.

<sup>45</sup> Brief of Amicus Curiae COMPTTEL in Support of Respondents at 20, *linkLine*, 128 S. Ct. 2957 (No. 07-512) (2008) [hereinafter COMPTTEL Amicus Brief].

<sup>46</sup> *Id.* at 21; *linkLine*, 503 F.3d 876 (noting that courts find agency attentiveness to alleged anticompetitive conduct as “relevant” to determining whether judicial intervention through the antitrust laws is necessary to remedy such conduct). *linkLine* also recognized the possibility of regulatory failure, stating that “[w]here the regulatory agencies have failed to prevent or remedy anticompetitive conduct, the balance may tilt in favor of judicial intervention. *Id.* at 885 n.12.

<sup>47</sup> *linkLine*, 503 F.3d at 885 n.12. See 3B PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW* ¶ 767a at 139 (3d ed. 2008) (acknowledging that “[t]he most difficult [price-squeeze] case” arises where a monopolist’s pricing is regulated at the wholesale, but not the retail level”).

<sup>48</sup> Petitioners’ Reply Brief, *supra* note 10, at 20–21.

<sup>49</sup> *Id.* at 12.

<sup>50</sup> A monopolist may incur higher costs serving these customers because, for example, they are small or are located in costly-to-serve geographical areas.

other hand, the monopolist must serve all end users, even those higher-cost, lower-margin, end-user customers.

**The Below-Cost Price-Squeeze Claim and the Equally Efficient Rival Standard.** Those supporting Petitioners argue that even in an unregulated market a margin-based price-squeeze claim should not lie,<sup>51</sup> and that if such a claim survives *Trinko*, it must be alleged as predatory pricing under *Brooke Group*. Amici supporting Petitioners cite Judge Gould's dissent, arguing that a plaintiff must show that (1) "the prices complained of are below an appropriate measure of its rival's costs," and (2) "the competitor had . . . a dangerous probability of recouping its investment in below cost prices."<sup>52</sup>

Amici supporting linkLine argue that contrary to these assertions, a price squeeze cannot be subsumed under the predatory-pricing rubric. Indeed, predatory pricing may not even be relevant to a price-squeeze claim<sup>53</sup> because the monopolist can maintain a squeeze on its competitors by charging an above-cost retail price so long as its wholesale price is sufficiently high—that is, a price-squeeze monopolist could simply raise its wholesale prices to cross-subsidize its low (but not necessarily below-cost) retail rates.<sup>54</sup> Moreover, the amici submit that meeting the *Brooke Group* recoupment prong is not necessary in determining whether a price squeeze has occurred. Unlike in predatory pricing, a price-squeeze monopolist can simultaneously lose profits at the retail end, while compensating for lost retail profits on the wholesale end.<sup>55</sup> In other words, recoupment in a price squeeze is comparatively easy, because a price-squeezing monopolist need not sacrifice profits in the short or long run.<sup>56</sup> Also, whereas many predatory-pricers could face renewed competition during the recoupment period after having priced the competition out of the market, a price-squeezing monopolist will be relatively safe from such competition.<sup>57</sup>

Even if *Brooke Group* applies, the applicable measure of cost may vary depending on the antitrust violation at issue. In a predatory pricing case, the price would be predatory only if it was below an appropriate threshold, such as below short-term average variable cost or average-avoidable cost.<sup>58</sup> Stated more generally, however, as to any particular antitrust claim the appropriate cost threshold should be one that prevents a monopolist from excluding an equally efficient single-product competitor. In price-squeeze cases, the appropriate measure of cost may therefore be the imputed wholesale price to independent purchasers: the European Union's measure

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<sup>51</sup> Transcript of Oral Argument, *linkLine*, at 10–11, 128 S. Ct. 2957, No. 07-0512 (Dec. 8, 2008), available at [http://www.supremecourtus.gov/oral\\_arguments/argument\\_transcripts/07-512.pdf](http://www.supremecourtus.gov/oral_arguments/argument_transcripts/07-512.pdf).

<sup>52</sup> U.S. Amicus Brief, *supra* note 33, at 15–16 (internal citations and quotations omitted).

<sup>53</sup> COMPTEL Amicus Brief, *supra* note 45, at 4.

<sup>54</sup> *Id.*

<sup>55</sup> *Id.*

<sup>56</sup> *Id.* at 12 (arguing that while predatory pricing may decrease the monopolist's revenues, a price squeeze can increase those revenues or at least reduce them less than a predatory pricing strategy, because the monopolist "can compensate for lost wholesale volume by selling the same products at the retail level") (citing 3B PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW* ¶ 767c5, at 141 & n.15 (3d ed. 2008)).

<sup>57</sup> A price-squeezing monopolist will likely face less competition during the recoupment period because unlike the predatory-pricer that is attempting to monopolize what was once a competitive market, the price-squeezing monopolist has a durable monopoly in the bottleneck input, and may be acting to maintain that monopoly by pricing such that only a downstream competitor with access to an independent input would be able to compete. In other words, margin-based price-squeeze claims can be based on a monopoly maintenance theory, as opposed to a predatory-pricing price-squeeze claim, which would be based on an attempted monopolization theory.

<sup>58</sup> See *United States v. AMR Corp.*, 335 F.3d 1109 (10th Cir. 2003); *Spirit Airlines, Inc. v. Nw. Airlines, Inc.*, 431 F.3d 917 (6th Cir. 2005); Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975).

of cost.<sup>59</sup> That is, for a price squeeze, the monopolist's retail price violates *Brooke Group* if it is below the opportunity cost of a forgone wholesale sale.

Where the monopolist is a multiproduct firm, a price squeeze might more properly be analyzed as a bundled discount or tying claim. A price-squeeze claim typically focuses solely on the upstream and downstream prices of a single product, when "the firm faces the challenge . . . of recovering not only the costs incurred in common among all products made by the firm, but also each mathematical combination of two or more products."<sup>60</sup> Analyzing a price squeeze as a bundled discount could focus instead on the ultimate retail bundle sold to consumers and whether that bundle is preventing equally efficient competitors from competing.

Bundling is common in telecommunications, and it may explain why an ILEC would prefer not to deal with its rivals.<sup>61</sup> DSL service, for example, is really just one product in a vertical bundle, within which an ILEC can incorporate DSL transport, necessary DSL equipment and services, Voice over Internet Protocol (VoIP), wireline and wireless telephone service, video, and a host of other ancillary services.<sup>62</sup>

Providing DSL service as part of a multiproduct bundle permits the ILEC more pricing flexibility. For example, the ILEC can selectively distribute common costs among the products in the bundle. The access price that would give a monopolist an incentive to deal with a rival would have to compensate the monopolist not only for investment and maintenance of its network and the cost of service provision, but also the opportunity costs.<sup>63</sup> By giving network access to an ISP, the ILEC loses not only revenue from displaced retail DSL sales, but also revenue from both advertisers and subscribers "associated with voice telephony and with ancillary products generating substantial net revenues—such as vertical services (caller ID, voicemail, call forwarding, and the like) Internet advertising, and value-added services generally."<sup>64</sup> The ILEC may also be more likely to lose primary-product sales to a competitor if the product is unbundled.<sup>65</sup>

The challenge in all of this is to determine when firms are "equally efficient." Professor Sidak argues that a multiproduct firm should not be penalized because its rival lacks the economies of scope and scale necessary to allocate its common costs among bundled products.<sup>66</sup> Though an ISP might be equally efficient at providing DSL service as a standalone product, it is arguably not equally efficient in the sense that it cannot supply an equivalent multiproduct bundle to con-

**Where the monopolist is a multiproduct firm, a price squeeze might more properly be analyzed as a bundled discount or tying claim.**

<sup>59</sup> See *supra* note 11 and accompanying text.

<sup>60</sup> Sidak, *supra* note 38, at 300.

<sup>61</sup> AT&T argues that "a wholesale monopolist already earns monopoly profits, and, in general, benefits from the presence of efficient downstream rivals, not from their absence." Petitioners' Reply Brief, *supra* note 10, at 15. While an upstream monopolist can earn revenue from selling to downstream competitors, it must balance those revenues against the costs of dealing with those competitors. That AT&T previously dealt with linkLine only under regulatory compulsion suggests that AT&T decided that it would profit more by refusing to deal with its downstream rivals.

<sup>62</sup> It is possible that these ancillary services are not actually "ancillary" because these often competitive products could be higher-value and more profitable for the defendant monopolist to provide than the monopolist's monopoly services, such as wireline telephone service. The bundle can assist the monopolist also by allowing it to increase the transaction costs for a customer to switch to another provider for any single product.

<sup>63</sup> Sidak, *supra* note 38, at 302–03.

<sup>64</sup> *Id.*

<sup>65</sup> Petitioners' Reply Brief, *supra* note 10, at 19 ("[A] customer who purchases voice service and DSL-based broadband service from a single provider may be less likely to switch *both* voice and broadband service to a competing provider. . .").

<sup>66</sup> Sidak, *supra* note 38, at 301.

sumers.<sup>67</sup> Professor Sidak questions whether it possible for any firm to profitably offer a service on a standalone basis when competitor multiproduct firms bundle, even when there is no price squeeze.<sup>68</sup>

The Supreme Court in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*,<sup>69</sup> however, held that a defendant had injured its smaller rival and competition by refusing to deal with the plaintiff in selling a bundled all-access skiing pass.<sup>70</sup> The Court found that competition had been harmed in part because the defendant's smaller rival could not profitably sell a standalone skiing pass, and was losing market share to the defendant.<sup>71</sup> The view of consumer welfare expressed in a recent appellate court bundling case,<sup>72</sup> by the Antitrust Modernization Commission,<sup>73</sup> and even by the DOJ<sup>74</sup> suggests that the equally efficient competitor standard should compare competitors on a standalone basis. For example, the DOJ Section 2 Report proposes evaluating a bundled discount claim involving a plaintiff and defendant that compete against one another by offering comparable bundles as being closer to a predatory pricing claim, such that *Brooke Group* would apply. In situations where a plaintiff is not able to compete with a defendant on a bundle-to-bundle basis, however, the DOJ Section 2 Report would analyze the bundled discount as being closer to a tying claim.<sup>75</sup> Equal efficiency, in other words, should be measured by referring to the competitive bundled or tied product, and not the entire bundle of products including the tying or bundling or monopoly product.

In a bundled discount, the DOJ Section 2 Report suggests that a court should allocate all relevant discounts applying to a bundle of products to the competitive product before determining whether the monopolist was pricing below incremental cost.<sup>76</sup> Applying *Brooke Group's* predatory pricing analysis to a price squeeze would instead allocate the discount to the entire bundle rather than just the competitive product, which would result in underdeterrence and false negatives.

**Administrability and Effect of Price-Squeeze Liability on Business Incentives.** AT&T argues in *linkLine* that *Alcoa's* price-squeeze standard of ensuring that competitors can purchase a bottleneck input at a "fair price" and "living profit" is not administrable.<sup>77</sup> The Department of Justice, in an amicus brief supporting AT&T, argues that remedying a price squeeze would require judicial inter-

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<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> 472 U.S. 585, 601 (1985).

<sup>70</sup> See *id.* at 607–11. In *Aspen Skiing*, the Court found that the defendant skiing company was "willing to sacrifice short-run benefits and consumer goodwill in exchange for a perceived long-run impact on its smaller rival." *Id.* at 610–11. The Court in *Trinko*, however, held that "*Aspen Skiing* is at or near the outer boundary" of Section 2 liability. *Trinko*, 540 U.S. at 409.

<sup>71</sup> *Id.* at 607–08.

<sup>72</sup> See *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883 (9th Cir. 2007) (equally efficient competitor standard applies to bundled-discount claims).

<sup>73</sup> ANTITRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATIONS 83 (2007) (relevant cost measure for competitive product is the firm's cost of producing the competitive product after all discounts and rebates attributable to a bundle of products is allocated to the competitive product), available at [http://govinfo.library.unt.edu/amc/report\\_recommendation/amc\\_final\\_report.pdf](http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf).

<sup>74</sup> U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT 101 (2008) (where bundle-to-bundle competition is not possible, relevant cost measure is imputed cost proposed by Antitrust Modernization Commission) [hereinafter DOJ SECTION 2 REPORT], available at <http://www.usdoj.gov/atr/public/reports/236681.htm>.

<sup>75</sup> *Id.* at 101–02.

<sup>76</sup> *Id.*

<sup>77</sup> Brief for Petitioners, *supra* note 31, at 31 ("the *Alcoa* price-squeeze test . . . is famously difficult to administer").

vention in free-market pricing.<sup>78</sup> To remedy a high wholesale price, a court would have to intervene to depress that price. And to remedy an allegation of a low retail price, a court would have to require a firm to maintain a supracompetitive price downstream, which would harm consumers, who would pay higher prices for the same product.<sup>79</sup> The United States questions whether a court would be more effective than the market at setting prices and then supervising those prices.<sup>80</sup> The argument is that a court may be incapable of remedying an anticompetitive price squeeze.<sup>81</sup> And AT&T argues that the transfer-price test is not a solution because examining the monopolist's wholesale price to determine whether the monopolist is pricing below cost is an imputation exercise that courts are unable to implement, and as such is better left to a regulator.<sup>82</sup>

A group of law professors and economists in their amicus brief supporting AT&T similarly argue that the European experience shows that a U.S. court would have to grapple with an economically and factually complex imputation analysis.<sup>83</sup> To apply the equally efficient competitor standard in *Alcoa*, and in the European Union, the economists argue, a court would have to determine what the costs of an equally efficient competitor would be, and then determine whether the monopolist's upstream-downstream price differential would allow the hypothetical firm to compete. The judge's job as de facto rate regulator will be continuous because market forces will change wholesale and retail prices over time, such that a given profit margin may shrink and jeopardize the survival of competitors. The perverse outcome is that price-squeeze litigation becomes a kind of enduring cost-of-service regulation that taxes the resources of a district judge.

In its brief supporting *linkLine*, however, COMPTTEL argues that the imputation of an equally efficient competitor's costs will not always be necessary because a court can use the comparative billing test, when a monopolist's retail price is higher than its wholesale price, for example, to conclude a price squeeze has occurred without undergoing an imputation exercise.<sup>84</sup> Moreover, COMPTTEL urges that administrable remedies could be implemented by taking the monopolist's retail price as the benchmark for determining a wholesale price and directing the incumbent to charge a wholesale price below its retail price. A court could also impose semi-structural relief, such as functional (not structural) separation, which has the benefit of allowing the market to continue to control prices, and preserving innovation and investment incentives. This remedy also retains bona fide vertical efficiencies.

AT&T has argued that *Trinko's* concern that "enforced sharing" discourages investment applies to price squeeze as well as refusals to deal, because a price squeeze is nothing more than a refusal to deal.<sup>85</sup> By capping the wholesale price a monopolist may charge for its bottleneck input, AT&T argues, a court will reduce the funds available to the monopolist to invest in innovative technologies.<sup>86</sup>

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<sup>78</sup> U.S. Amicus Brief, *supra* note 33, at 24.

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

<sup>82</sup> *Id.* at 24–26.

<sup>83</sup> Brief of Amici Curiae Professors and Scholars in Law and Economics in Support of the Petitioners at 7, *linkLine*, 128 S. Ct. 2957 (2008) (No. 07-512) [hereinafter Economists' Amicus Brief].

<sup>84</sup> COMPTTEL Amicus Brief, *supra* note 45, at 16.

<sup>85</sup> *Trinko*, 540 U.S. at 408. See Brief for Petitioners, *supra* note 31, at 29–30; Petitioners' Reply Brief, *supra* note 10, at 13.

<sup>86</sup> Brief for Petitioners, *supra* note 31, at 29–30 (arguing that price squeeze claims could "undermine incentives for 'innovation and economic growth'" by stifling opportunities for monopoly pricing).

At issue is whether monopoly or competition is more conducive to market-driven innovation.<sup>87</sup> If competition promotes market-driven innovation, then innovative investment is not encouraged by allowing the upstream monopolist sufficient monopoly revenues to invest in monopoly-determined, but not market-driven, innovation. It is possible that because of persistent market dominance in the broadband access market, for example, the United States continues to lag behind the developed world in broadband penetration, speed, and pricing.<sup>88</sup> A price-squeeze monopolist could reduce both downstream and upstream innovation by eliminating rivals, or by appropriating a competitive rival's productivity gains. AT&T's argument overlooks the possibility that, as discussed below, a competitor could use its downstream position to enter the upstream market.

Focusing on the harm posed by exiting competitors, the United States argues a price squeeze is just a result of vertical integration, which can be "adverse, neutral, or beneficial."<sup>89</sup> Thus, the United States reasons, the price squeeze is a claim used to protect competitors rather than consumers. Agreeing with the United States, the economists use the EU margin-squeeze cases as an example of how the transfer-price test primarily protects competitor welfare by considering what prices a monopolist would have to charge to enable its downstream, equally efficient competitors to compete.<sup>90</sup> Those favoring the European Community's approach, however, argue that its standard does not protect competitors, but prevents harm to consumers that results from the loss of equally efficient competitors.

COMPTEL argues that application of the *Brooke Group* standard would ignore the fact that a price squeeze is more effective than predatory pricing because the monopolist excludes downstream rivals even as it minimizes its own revenue losses.<sup>91</sup> A price squeeze also allows a monopolist to realize the same end as predatory pricing without having to endure the same amount of cost and pain to itself as it would by having to reduce its own prices. And as then-Chief Judge Breyer recognized in *Town of Concord*, COMPTEL argues that a price squeeze can create barriers to entry into the upstream and downstream markets and eliminate non-price competition in the downstream market.<sup>92</sup>

Another argument is that a price squeeze can harm consumers because a monopolist could use a price squeeze to maintain an upstream monopoly through margin-based exclusionary pricing so that nascent upstream entrants cannot realize minimum viable scale. Price squeezes can also create a dangerous probability of monopolization in a downstream market like DSL service that, until the premature deregulation of the upstream market, was a viable, standalone competitive market. An ILEC derives control of the bottleneck facilities not so much by virtue of using superior skill, foresight, or industry as by benefiting from the legacy of a state-sanctioned monopoly. A price squeeze could allow equally efficient downstream competitors that lack access to the

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<sup>87</sup> See, e.g., Sherman Act Section 2 Joint Hearing: Empirical Perspectives Session, Sept. 26, 2007. (presentation materials of Michael Scherer), available at [http://www.usdoj.gov/atr/public/hearings/single\\_firm/docs/218696.htm](http://www.usdoj.gov/atr/public/hearings/single_firm/docs/218696.htm); F.M. Scherer, *Technological Innovation and Monopolization* (Mar. 2006) (unpublished draft article), available at [http://www.usdoj.gov/atr/public/hearings/single\\_firm/docs/218697.htm](http://www.usdoj.gov/atr/public/hearings/single_firm/docs/218697.htm).

<sup>88</sup> Organization for Economic Cooperation and Development, Broadband Portal, available at <http://www.oecd.org/sti/ict/broadband> (May 19, 2008) (the United States remains fifteenth in the number of broadband subscribers per 100 inhabitants).

<sup>89</sup> U.S. Amicus Brief, *supra* note 33, at 19 (citing 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW* ¶ 767c, at 126 (2d ed. 2002)).

<sup>90</sup> *Id.* at 7.

<sup>91</sup> *Id.* at 12 ("in a price squeeze, the upstream monopolist can reduce downstream competitors' profit margins not only by effectively reducing competitors' revenues (i.e. lowering retail prices), but also by increasing their costs (i.e., raising wholesale prices).")

<sup>92</sup> COMPTEL Amicus Brief, *supra* note 45, at 12–15 (citing *Town of Concord*, 915 F.2d at 28–29).

input because they were not the prior state-sanctioned monopolist, to be foreclosed from competing on price and innovative services.

Professor Sidak argues that if a court were to require a monopolist to maintain a specific retail rate based on an equally efficient competitor's costs, the result would be the same as that achieved by an unlawful cartel of downstream competitors. The concern is that an erroneous finding of liability in cases involving "price cutting" would "chill the very conduct the antitrust laws are designed to protect."<sup>93</sup> If a firm must reduce its wholesale prices lockstep each time that it reduces its retail prices to preserve a specific cost-based profit margin for its downstream competitor-customers, then price-based competition will be chilled.<sup>94</sup> A monopolist may want to reduce retail prices because of changing market demand conditions, yet may not because the specter of price-squeeze liability would compel it to simultaneously lower wholesale prices.

But AT&T and its amici have not cited any empirical or anecdotal evidence that possible price-squeeze liability has deterred vertically integrated monopolists from legitimate price cutting. Also, price-squeeze theory posits the downstream market is competitive, so that competition ought to reduce retail prices to cost regardless of the conduct of the monopolist. In a price-squeeze case, it is the wholesale price that is set at the monopoly profit-maximizing level. The focus should arguably be on creating an administrable, judicially imposed remedy that would create incentives for the monopolist to reduce the wholesale rate to cost.

### What Is the Supreme Court Likely to Do?

The Court has a number of possible paths it can take in *linkLine*. Perhaps the Supreme Court should simply decide that certiorari was improvidently granted, not only because *linkLine* has decided not to challenge the petition, but also because the second district court Order, dealing with the applicability of *Brooke Group*, was not within the scope of the interlocutory appeal to the Ninth Circuit and thus within the certiorari petition. Or, the Court could decide in favor of AT&T and preclude margin-based price squeeze claims in unregulated and regulated markets by overturning *linkLine* and *Alcoa*. Rather than issue a broad ruling on the margin-based price squeeze by overturning *linkLine* and *Alcoa*, however, the Court might tailor its decision to the particular circumstance presented by this case. For instance, the Court could vacate *linkLine* and decide that in a market with even partial regulation, if a complainant can seek a remedy for anticompetitive conduct under existing regulatory procedures, then the intrusion of judicially imposed antitrust remedies might do more harm than good. On the other hand, if a market is unregulated or even very lightly regulated, it is possible that the Court would, and in our view should, hold that the margin-based price-squeeze claim—and *Alcoa*—survive *Trinko*. ●

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<sup>93</sup> *Town of Concord*, 915 F.2d at 23.

<sup>94</sup> Sidak, *supra* note 38, at 294.