Antitrust Law Blog

Posted at 2:45 PM on September 16, 2010 by Sheppard Mullin

Ninth Circuit Applies New "Quick Look Plus" Test To Invalidate Supermarket Mutual Strike Assistance Agreement

On August 17, 2010, the Ninth Circuit, in an opinion by Judge Steven Reinhardt, issued a potentially significant decision on the intersection between antitrust and labor law. *California v. Safeway, Inc.*, No. 08-55671. The decision resulted from a challenge to collective activity by four Southern California supermarket chains, Albertson's, Von's, Ralph's and Food 4 Less, in response to a strike by the United Food and Commercial Workers ("UFCW") after expiration of a collective bargaining agreement in October, 2003. The response, as described below, prompted a lawsuit by the California Attorney General alleging that the collective action was either a per se violation of Section 1 of the Sherman Act, or was unlawful under an abbreviated rule of reason "quick look" analysis. The district court denied cross-motions for summary judgment, and entered final judgment after a stipulation in which the State of California agreed not to pursue judgment under a full rule of reason analysis, and defendants withdrew all affirmative defenses except for the claim that the profit sharing agreement at issue was protected from antitrust review by the non-statutory labor exemption.

Anticipating what the Ninth Circuit called "whipsaw tactics," in which a union would strike or picket only one employer in a multi-employer bargaining unit, the four supermarket chains entered into a mutual strike assistance agreement (the "MSAA"). The MSAA contained an agreement that all four supermarket chains would lock out their union employees within 48 hours of a strike against any one or more of them, a traditional tactic in labor disputes. However, the MSAA also contained a "profit sharing provision" providing for the sharing of profits during the strike regardless of its length. The profit share provision called for any firm that earned revenues above its historical share of the combined revenues of all four firms to redistribute 15% of those surplus revenues among the other chains according to a fixed formula. Testimony before the trial court established that the 15% number was intended as an estimate of the profit that a chain would earn on increased sales without having to increase fixed costs. The avowed purpose of the profit sharing provision was to maintain each defendants' pre-labor dispute market share. Profit sharing was to continue for two full weeks after termination of any strike or lock out.

According to data presented to the trial court, the number of supermarkets covered by the agreement accounted for 55-64% of the Los Angeles/Long Beach market and 66-75% of the San Diego metropolitan market. On October 11, 2003 the unions struck local Von's stores, and Ralph's and Albertson's locked out their employees. The Unions picketed all three supermarket chains but stopped picketing Ralph's on October 31, 2003.

The decision begins in an orthodox enough fashion by preliminarily focusing on whether the challenged restraint can simply be condemned as *per se* illegal. The State of California argued that the profit sharing arrangement was *per se* illegal either as a profit pooling agreement or as a market allocation agreement. The Court dismisses the market allocation agreement contention out of hand as inapplicable on the facts, and devotes its *per se* analysis to whether the MSAA is a profit pooling agreement of the sort condemned by previous Supreme Court cases as *per se* illegal. At this point, the Panel's antipathy for the MSAA begins to become apparent. It is characterized as a profit pooling arrangement of the sort generally recognized by the Supreme Court to eliminate incentives to compete for customers along virtually every competitive dimension.

Defendants attempted to defend the MSAA in three ways. They first contended that the MSAA would share only 15% of an increase in relative revenue, not profits, as an estimate for total additional profits to be earned as a result of any increase in relative market share. The Ninth Circuit goes on to dismiss this as "meritless" by opining that the practical impact of the increased revenue share will be a profit share and that the intent to share profits was sufficiently injurious to motivations to compete vigorously that the characterization was unpersuasive.

However, defendants' other two proffered defenses: (1) the short duration of the proposed pooling arrangement, and (2) a number of competing supermarkets in the geographic markets that were not party to the profit pooling, fared somewhat better, at least initially. The Ninth Circuit's discussion of what it saw as the relevant Supreme Court law on these two arguments is neither detailed nor particularly penetrating. However, the panel seems to content itself with the premise that since none of the prior cases were exactly on point, the profit pooling arrangement at issue could at least escape *per se* treatment because of its short duration and involvement by less than all the market participants.

Having decided that the restraint was not *per se* illegal, the Ninth Circuit swings into its "quick look" analysis, and things begin to get interesting. The Court starts by noting that it does not intend to use a standard "quick look" analysis. The Court notes that the Supreme Court's standard definition of "quick look" in *California Dental Association*, 526 U.S. at 770, which enables an arrangement to be condemned when "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers in markets", is insufficient without more to decide the case. Instead, it describes its analysis as "quick look plus" and announces an intention to look at the history of judicial experience with profit sharing arrangements, applying the rudimentary economic principles called for by *California Dental Association*, and then thoroughly analyzing "the circumstances, details and logic of the agreement in an order to determine the likelihood of anticompetitive effects." This "quick look plus" approach would then be followed by the standard balancing in which the court then considers any proffered pro-competitive effects that defendants suggest would outweigh the anticompetitive effects of the agreement at issue.

The Court begins its analysis by repeating that profit sharing arrangements have historically been routinely condemned as *per se* illegal. However, the Court also notes that defendants point to the indefinite, and somewhat limited term of the agreement, and the presence of a number of supermarkets not party to the agreement in the Southern California market which would have ameliorated or eliminated any anticompetitive effects of the profit sharing agreement. But having thus framed the inquiry, the Court then proceeds to quickly discuss both of these arguments under its newly minted "quick look plus." First, the Ninth Circuit rejects the notion that a shorter duration for the profit sharing agreement would meaningfully reduce its inherent anticompetitive impact, noting only that confining the duration of the anticompetitive impact to a relatively shorter period was not a meaningful distinction between the profit sharing agreement at issue and those previously condemned as *per se* illegal.

The notion that there might have been competitive discipline by other market participants not party to the profit sharing agreement was given equally short shrift. Here the Court seemed to engage in a very truncated market power analysis, and noted that the market shares of the parties to the profit sharing agreement were high enough to activate the presumptions of market power contained in prior Ninth Circuit decisions dealing with single firm monopolization claims under Section 2 of the Sherman Act. And in so doing, albeit buried in a footnote, the decision appears to endorse prior cases holding that a presumption of market power could exist in the Ninth Circuit with market shares as low as 45% depending upon the level of fragmentation of other market participants. Moreover, the Court noted that given the relatively short time period at issue during the course of the strike, there would be little incentive for smaller market participants to expand operations. Finally, the Court noted that it was entirely possible smaller market participants would engage in "umbrella pricing," and actually raise prices so that they were still underneath the stable prices charged by the parties to the profit sharing agreement, but not materially lower.

The Court concluded its analysis of whether the MSAA could be found anticompetitive on a summary basis by dealing with the defendants' contention that there was no empirical evidence to demonstrate that the effects of the Agreement were anticompetitive in practice. The Court noted that "quick look" review does not require empirical evidence of anticompetitive effects and so such empirical evidence was also not required "for the combined or mixed *per se* quick look approach that we apply here."

With that, the Ninth Circuit turned to the next step in its "quick look plus" construction, a fairly orthodox determination of whether pro-competitive effects offered by defendants justify or excuse what the Ninth Circuit has by then determined is otherwise anticompetitive behavior. And it is at this point that the decision takes on a sufficiently ideological character to potentially make it the subject of en banc and/or Supreme Court review. According to the Ninth Circuit, defendants' "real defense" is an assertion that conduct reducing the cost of labor serves a pro-competitive purpose by increasing defendants' chances of winning the labor dispute, and thereby reducing the cost of the labor input. This argument is rejected because "driving down compensation to workers is not a benefit to consumers cognizable under our laws as a pro-competitive benefit." This broad categorical statement is not supported by any citation except a dissenting opinion by Justice Goldberg in *United Mine Workers v. Pennington* to the effect that human labor is not a commodity or article of Commerce. The Ninth Circuit then goes on to say that reducing workers' wages and benefits is not an objective that would justify an antitrust violation because of the policies embodied in the Labor Law, and to so find would therefore "unbalance the carefully developed legal structures relating to our laws governing collective bargaining."

Having thus decided that the Profit Sharing Agreement is anti-competitive, and lacks any pro-competitive counterweight, the Ninth Circuit then turns to whether the non-statutory labor exemption places the MSAA beyond the reach of the antitrust laws because of its role in a labor dispute involving a collective bargaining agreement. The balance of the opinion is a discussion of whether the MSAA is sufficiently related to the smooth functioning of the collective bargaining process that it can be collectively imposed on the situation by Defendants under the logic of the Supreme Court's decision in *Brown v. Pro Football*, 518 U.S. 231 (1996). In *Brown*, the Supreme Court held for the first time that an agreement among a group of National Football League teams to unilaterally impose certain terms and conditions from the lapsed collective bargaining agreement after reaching an impasse in bargaining with the Players Association constituted a well recognized procedure in the collective bargaining process and so was exempt from antitrust review. *Brown* 518 U.S. at 234-35.

Given the Ninth Circuit's antipathy for the MSAA expressed in its initial "quick look plus" analysis, it is hardly surprising that the opinion goes on to find the MSAA not covered by the non-statutory labor exemption. Essentially, the decision reads the Supreme Court's decision in *Brown* very narrowly, and as containing three independent, disjunctive requirements, all of which must exist for the non-statutory labor exemption to apply: (1) the agreement at issue must be essential to making the collective bargaining process work; (2) determining the legality of the agreement must only raise questions ordinarily resolved by or susceptible to resolution by the application of labor law principles; and (3) the agreement at issue cannot plausibly be characterized as having an adverse affect on the consumer and any product market.

The Ninth Circuit restrictively construes each of the three criteria. The "essentiality" requirement is defined so narrowly through selective quotations from *Brown* that it is difficult to imagine what beyond continuing to do business under the lapsed terms of the collective bargaining agreement -- the facts in *Brown* itself -- would qualify as essential to the process. The second criteria is also defined very stringently, with the Ninth Circuit observing that any action that cannot be directly regulated by labor law would fall outside the scope of the exemption. By definition, then, any activity which could be otherwise violative of the antitrust laws and not directly prohibited by federal labor law would fall outside the exception articulated in *Brown*. Finally, and of particular note, is the Ninth Circuit's construction of the third criteria concerning whether the agreement at issue affects consumers or a product market directly. As the Ninth Circuit reads *Brown*, any agreement which can even be characterized as hurting consumers by driving up the price of a product would fall outside the non-statutory labor exemption.

Authored by:

[David R. Garcia]
(310) 228-3747
DGarcia@sheppardmullin.com