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Ninth Circuit Rules Profit-Sharing Assistance Agreement During Labor Dispute Violates Sherman Act

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The United States Court of Appeals for the Ninth Circuit recently held that a profit-sharing assistance agreement instituted by employers in anticipation of a whipsaw strike is not protected from antitrust scrutiny by the nonstatutory labor exemption to the antitrust laws, and in fact violated Section 1 of the Sherman Act. *State of California v. Safeway, Inc.,* __ F. 3d __ , Nos. 08-55671, 08-55708 (August 17, 2010).

Three Southern California supermarket chains that were engaged in multiemployer bargaining entered into a Mutual Strike Assistance Agreement ("MSAA" or "agreement") among themselves and a fourth, nonmember supermarket chain. The agreement was intended to protect the employers from the effects of a whipsaw strike by ensuring that each chain maintained its historical profitability and market share. When one of the chains in the multiemployer group was struck, the two others in the group locked out, and the MSAA was implemented.

Although the strike eventually was settled, ending the MSAA, the State of California challenged the agreement's legality under Section 1 of the Sherman Act. The employers defended on the basis that the MSAA was not anticompetitive, but in any event was protected by the nonstatutory labor exemption from the federal antitrust laws. *See, e.g., Brown v. Pro Football, Inc.,* 518 U.S. 231 (1996). The district court bifurcated the case to allow the employers to seek summary judgment on the applicability of the nonstatutory labor exemption. The district court denied the employers' motion.

The State then sought summary judgment on the basis that the MSAA was either a *per se* violation of Section 1, or was unlawful under an abbreviated rule of reason "quick look" analysis. The district court also denied the State's motion.

The district court entered final judgment after a stipulation in which the State agreed not to pursue judgment under a full rule of reason analysis, and the employers withdrew all affirmative defenses except for the one based on the nonstatutory labor exemption. The State and the employers filed cross appeals in the Ninth Circuit.

The Court first addressed the State's claims that the MSAA violated Section 1 under either per se or quick look review. Because full rule of reason antitrust review is data-sensitive, expensive for the litigants, and consumes large amounts of courts' time and resources, the Court explained that courts have developed summary methods of identifying Section 1 violations without full rule of reason analysis: "per se"review and "quick look" review. Slip op. at 11938.

Per se analysis, the Court said, "examines whether prior judicial experience with the type of restraint at issue is sufficient to allow a determination that it would always or almost always tend to restrict competition or decrease output. . . . The focus of the inquiry is on accumulated data from prior decisions: an agreement may be declared unlawful with no further analysis simply because it is of the type that the courts have previously determined to have manifestly anticompetive effects and no redeeming virtue." *Id.* (citation and internal quotation marks omitted). The Court determined that the MSAA, which was limited in duration and did not include the entire retail grocery market in Southern California was not the type of restraint that prior cases demonstrate is anticompetitive and harmful to consumers. Thus, the Court declined to label the MSAA as a per se violation of the Sherman Act. Slip op. at 11944.

The Ninth Circuit next turned to the State's claim that the MSAA violated Section 1 under a quick look review. The Court observed that in contrast to per se review, "an arrangement is violative of § 1 under a quick look approach when an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets. . . . Quick look review is not necessarily based on a history of rule of reason adjudications; rather, it asks whether a great likelihood of anticompetitive effects can easily be ascertained by examining the restraint, and considering defendants' justifications of it." Slip op. at 11945-46(citation and internal quotation marks omitted).

However, rather than apply a strict quick look approach, the Court analyzed the MSAA under what it deemed a "combined or mixed approach." Slip. op. at 11946. It described the approach, in this case, as requiring it to "look to the history of judicial experience with profit-sharing agreements, apply rudimentary economic principles to the meaning and effects of the particular agreement in question, and thoroughly analyze the circumstances, details and logic of the agreement in order to determine the likelihood of anticompetitive effects." Slip op. at 1146. Next, the Court would "consider the purported procompetitive effects that the defendants suggest are sufficient to overcome any anticompetitive effects of the agreement." *Id.*

Applying the combined or mixed approach, the Court concluded that the MSAA has substantial anticompetitive effects because it removed fundamental incentives to engage in competition for an indefinite period. Slip op. at 11957. "In short, neither the fact that there are a number of smaller companies in the market, the fact that the agreement is of an indefinite though limited duration, nor the fact that the agreement takes effect during a strike, warrants a departure from the well-established rule that profit-sharing agreements are anticompetitive and violate section 1 of the Sherman Act." *Id.*

The Court then turned to defendants' procompetitive justification – that the MSAA would assist in winning the labor dispute, which would reduce the wages and benefits defendants would have to pay to their employees, thereby allowing the employers to lower prices and compete with other grocery stores in the market. The Court completely rejected this argument both as being speculative and contrary to public policy. It therefore found:

> Defendants have put forward no plausible procompetitive effects to overcome or neutralize the great likelihood of anticompetitive effects that would result from the implementation of their [MSAA]. That likelihood is evident from a plain reading of the agreement's terms, an examination of the ample case law regarding profit-sharing agreements, a rudimentary knowledge of economics, and our analysis of the 'circumstances, details and logic' of the agreement. . . . [W]e conclude with confidence and certainty that the [MSAA] violates § 1 of the Sherman Act, and that requiring [the State] to engage in a full rule of reason review would be contrary to the fundamental policies underlying our antitrust laws.

Slip op. 11964.

The Court next addressed what it described as the "central issue: whether the fact that defendants' agreement was designed for use as an economic weapon in a labor dispute changes or excuses the anticompetitive nature of the [MSAA]." Slip op. at 11932-11933. The employers claimed that because the MSAA was an agreement reached in connection with a labor dispute, it was immune from antitrust scrutiny under the non-statutory exemption. The Court rejected the employers' argument.

The Ninth Circuit explained that the non-statutory exemption "'applies where needed to make the collective bargaining process work.'" Slip op. at 11968, *citing Brown,* 518 U.S. at 234. The exemption avoids "'requir[ing] antitrust courts to answer a host of important'" labor law questions, such as "'practical questions about how collective bargaining over wages, hours, and working conditions . . . is to proceed.'" Slip op. at 11970, *citing Brown,* 518 U.S. at 240-41 (ellipsis added). "Hence, in *Brown* the exemption was 'needed to make the collective bargaining process work' . . . because 'to permit antitrust liability [would have] threaten[ed] to introduce instability and uncertainty into the collective bargaining process,' with respect to core labor-management issues to which the NLRB, and the courts reviewing such issues, have habitually applied well-established principles of labor law." Slip op. at 11970, *citing Brown,* 518 U.S. at 242 (ellipsis added).

In contrast, profit-sharing such as that called for under the MSAA "implicates the core concerns of the antitrust laws, and such concerns are best resolved by courts steeped in antitrust law." Slip op. at 11970. "It is the labor law practices essential to collective bargaining that the nonstatutory exemption is designed to protect. Profit-sharing is not such a practice." Slip op. at 11971. The Ninth Circuit added that determining that the MSAA was unlawful under the Sherman Act did not require it "to answer a host of important practical questions about how collective bargaining over wages, hours, and working conditions is to proceed." Slip op. at 11972, *citing Brown,* 518 U.S. at 240-41.

Further, the nonstatutory exemption does not apply to agreements which place a direct and immediate restraint on the product market. Slip op. at 11974. Because the MSAA "creates a great likelihood of direct harm to the public through reduced competition," the Ninth Circuit concluded that "the implied nonstatutory exemption is not applicable to this case." *Id.* "The purpose of the nonstatutory exemption is not to suspend the consumer protections afforded by the antitrust laws in order to shift the balance in economic pressures that the parties may bring to bear in the course of labor disputes." *Id.* "[M]ultiemployer collective bargaining works efficiently without the need to engage in violations of the antitrust laws that would harm consumers in the very way that those laws are designed to prevent. The [MSAA] . . ., accordingly, is clearly not an agreement that is 'needed' for the operation of the collective bargaining process." Slip op. at 11975, *citing Brown,* 518 U.S. at 234.

The Court noted (slip op. at 11975) that the employers had several options for countering a whipsaw strike which did not violate the antitrust laws, including purchasing strike insurance. The Court explained that strike insurance paid for with premiums of a fixed amount (as opposed to an amount that varied with revenues) and that covered only fixed costs, such as property taxes, pension payments and interest charges on debt, would not violate the antitrust laws, *citing W.P. Kennedy v. Long Island R.R. Co.,* 319 F. 2d 366, 369. (2nd Cir. 1963). The Court concluded, "[u]nlike defendants under their profit-sharing scheme, individual firms purchasing such insurance would retain any increase in profits earned during the labor dispute and suffer fully any reduction." *Id.*

The Court also rejected the employers' argument that the Supreme Court in *Brown* "created a rule under which any employer conduct that occurs in the context of a collective bargaining dispute is insulated from antitrust review by the nonstatutory labor exemption." Slip op. at 11976 – 11978.

In sum, the Court stated that the MSAA was not needed to make the collective bargaining process work; did not raise questions that are ordinarily resolved, or susceptible to resolution, by the application of labor law principles; and had a direct adverse effect on the consumer and product market. "Accordingly, we hold that the nonstatutory labor exception does not apply to the [MSAA]." Slip op. at 11978-79.

Employers who engage in, or contemplate engaging in, multiemployer bargaining must be aware of the risks associated with agreements among the employer group and should ask themselves whether agreements that are contemplated are necessary to “make collective bargaining work”; whether they raise questions that are better and more easily addressed by the application of labor law or, instead, by antitrust principles; and whether they have a direct anticompetitive effect on the consumer and product market.

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