Interstate Circuit v. United States

306 U.S. 208 (1939)

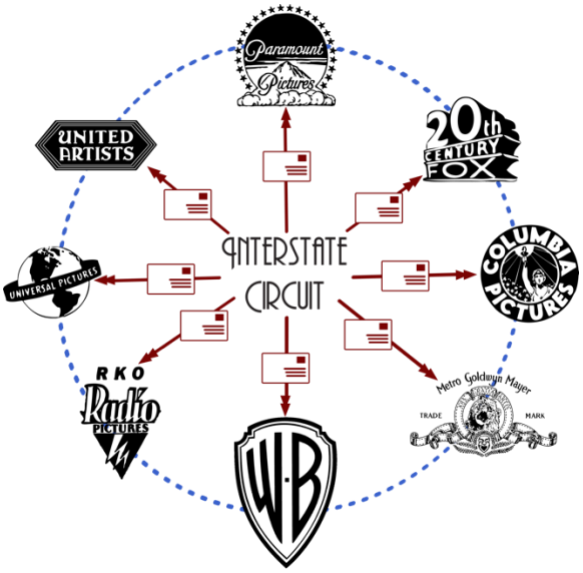
NOTE

An antitrust conspiracy is a horizontal agreement in restraint of trade in violation of Section 1 of the Sherman Act. Conspiracy cases often raise the question of whether the alleged conspirators entered into a conspiracy agreement. As interpreted by courts, an "agreement" in the context of Section 1 of the Sherman Act means "a conscious commitment to a common scheme designed to achieve an unlawful objective." *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 764 (1984). Often, there is no direct evidence of such agreements. Therefore, in many instances where direct evidence is absent, circumstantial evidence is used to prove the existence of the alleged conspiracy agreement.

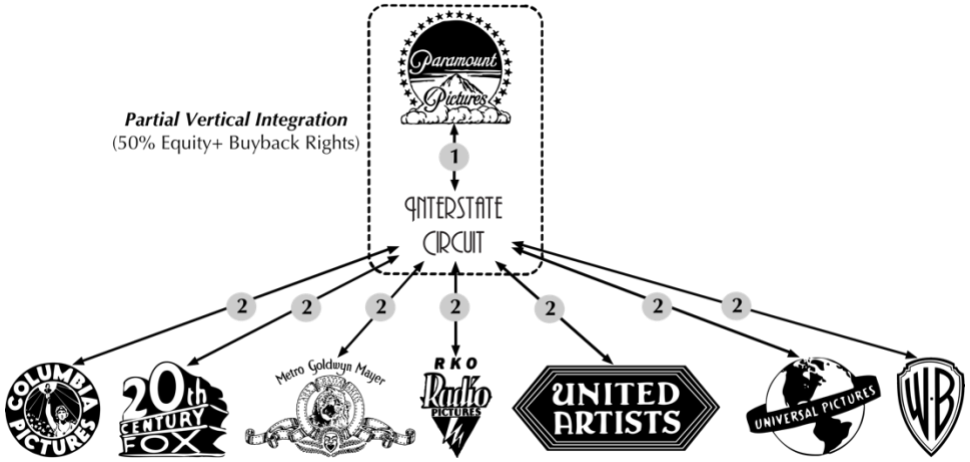
Interstate Circuit v. United States (1939) laid the foundation of conspiracy inference in antitrust law. Hundreds of judicial opinions, books, monographs, and articles summarize and interpret the facts of the case. With some minor variations, the summaries of the case are similar in their details, yet materially incomplete and erroneous.

As summarized in judicial opinions and the literature, *Interstate Circuit* involved a powerful retailer that sent a letter to eight film distributors, requiring them to amend their distribution policies to raise its rivals' costs. The letter named all recipients, informing each distributor that its competitors received the same letter. The distributors' compliance was partial but relatively uniform. This account comprises four elements:

1. ***Letter.*** A powerful movie exhibitor sent a letter to eight film distributors. Copies of the letter named all recipients, so that each knew that its seven competitors had received the same letter.
2. ***Demand to Adopt New Policies.*** The letter demanded that each distributor modify its exhibition agreements to include a restriction on minimum admission prices and a ban on double features. These restrictions were beneficial to the distributors as they protected box office revenues and were advantageous for the exhibitor because they were disadvantageous to its rivals.
3. ***Partial and Uniform Compliance.*** The distributors partially complied with the demands. Their partial compliance was largely uniform, although not entirely simultaneous. The adopted restrictions involved "a radical departure from the previous business practices of the industry" and led to "a drastic increase in admission prices."
4. ***Finding of Unlawful Conspiracy.*** The Supreme Court upheld the trial court's finding that the adoption of the restrictions formed a conspiracy in violation of Section 1 of the Sherman Act.



Contrary to its summaries, *Interstate Circuit* presents a very different set of factual findings: a powerful retailer, which was a partially-owned subsidiary of one of its suppliers, negotiated a deal with its parent company and its rivals.



Interstate Circuit raises the question of whether parallel compliance with an invitation to collude permits the inference of conspiracy. The case became the paradigmatic illustration of hub-and-spoke conspiracies, the agreement requirement, conscious parallelism, tacit agreement, and the raising rivals' costs strategy.

Barak Orbach, *Interstate Circuit and Conspiracy Theories*, 2019 University of Illinois Law Review 1447 (2019).

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Mr. Justice STONE delivered the opinion of the Court.

This case is here on appeal . . . from a final decree of the District Court for northern Texas restraining appellants from continuing in a combination and conspiracy condemned by the court as a violation of § 1 of the Sherman Anti-Trust Act, and from enforcing or renewing certain contracts found by the court to have been entered into in pursuance of the conspiracy. . . .

Appellants comprise the two groups of defendants. . . . [One group consists of] eight corporations which are distributors of motion picture films. . . . The other group, corporations and individuals engaged in exhibiting motion pictures in Texas, and some of them in New Mexico.

The distributor appellants are engaged in the business of distributing in interstate commerce motion picture films, copyrights on which they own or control, for exhibition in theatres throughout the United States. They distribute about 75% of all first-class feature films exhibited in the United States. They solicit from motion picture theatre owners and managers in Texas and other states applications for licenses to exhibit films, and forward the applications . . . to their respective New York offices, where they are accepted or rejected. If the applications are accepted, the distributors ship the films from points outside the states of exhibition to their exchanges within those states, from which, pursuant to the license agreements, the films are delivered to the local theatres for exhibition. After exhibition the films are reshipped to the distributors at points outside the state.

The exhibitor group of appellants consists of Interstate Circuit, Inc., and Texas Consolidated Theatres, Inc., and Hoblitzelle and O'Donnell, who are respectively president and general manager of both and in active charge of their business operations. The two corporations are affiliated with each other and with Paramount Pictures Distributing Co., Inc., one of the distributor appellants.

Interstate operates forty-three first-run and second-run motion picture theatres, located in six Texas cities [(Dallas, Houston, San Antonio, Fort Worth, Austin, and Galveston)].[1] It has a complete monopoly of first-run theatres in these cities, except for one in Houston operated by one distributor's Texas agent. In most of these theatres the admission price for adults for the better seats at night is 40 cents or more. Interstate also operates several subsequent-run theatres in each of these cities, twenty-two in all, but in all but Galveston there are other subsequent-run theatres which compete with both its first- and subsequent-run theatres in those cities.

[1] A first-run theatre is one in which a picture is first exhibited in any given locality. A subsequent-run theatre is one in which there is a subsequent exhibition of the same picture in the same locality.

Texas Consolidated operates sixty-six theatres, some first- and some subsequent-run houses, in various cities and towns in the Rio Grande Valley and elsewhere in Texas and in New Mexico. In some of these cities there are no competing theatres, and in six leading cities there are no competing first-run theatres. It has no theatres in the six Texas cities in which Interstate operates. That Interstate and Texas Consolidated dominate the motion picture business in the cities where their theatres are located is indicated by the fact that at the time of the contracts in question Interstate and Consolidated each contributed more than 74% of all the license fees paid by the motion picture theatres in their respective territories to the distributor appellants.

On July 11, 1934, following a previous communication on the subject to the eight branch managers of the distributor appellants, O'Donnell, the manager of Interstate and Consolidated, sent to each of them a letter on the letterhead of Interstate.* [Each copy named all branch managers] as addressees. [In the letter, O'Donnell] asked compliance with two demands as a condition of Interstate's continued exhibition of the distributors' films in its 'A' or first-run theatres at a night admission of 40 cents or more.[4]

One demand was that the distributors 'agree that in selling their product to subsequent runs, that this 'A' product will never be exhibited at any time or in any theatre at a smaller admission price than 25¢ for adults in the evening.'

The other was that 'on 'A' pictures which are exhibited at a night admission of 40¢ or more-they shall never be exhibited in conjunction with another feature picture under the so-called policy of double features.'

The letter added that with respect to the 'Rio Grande Valley situation', with which Consolidated alone was concerned, 'We must insist that all pictures exhibited in our 'A' theatres at a maximum night admission price of 35¢ must also be restricted to subsequent runs in the Valley at 25¢.'

The admission price customarily charged for preferred seats at night in independently operated subsequent-run theatres in Texas at the time of these letters was less than 25¢. . . . In most of them the admission was 15¢ or less. It was also the general practice in those theatres to provide double bills either on certain days of the week or with any feature picture which was weak in drawing power. The distributor appellants had generally provided in their license contracts for a minimum admission price of 10¢ or 15¢, and three of them had included provisions restricting double-billing. But none was at any time previously subject to contractual compulsion to continue the restrictions. The trial court found that the proposed restrictions constituted an important departure from prior practice.

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* [A copy of the letter is included in the materials].

4 A Class 'A' picture is a 'feature picture' having five reels or more of film each approximately 1,000 feet in length, shown in theatres of the specified Texas cities charging 40¢ or more for adult admission at night. Approximately 50%. of the pictures released by the distributor defendants in the Texas cities in 1934-1935 were Class 'A' pictures.

The local representatives of the distributors, having no authority to enter into the proposed agreements, communicated the proposal to their home offices.

Conferences followed between Hoblitzelle and O'Donnell, acting for Interstate and Consolidated, and the representatives of the various distributors. In these conferences each distributor was represented by its local branch manager and by one or more superior officials from outside the state of Texas. In the course of them each distributor agreed with Interstate for the 1934-35 season to impose both the demanded restrictions upon their subsequent-run licensees in the six Texas cities served by Interstate, except Austin and Galveston. . . .

None of the distributors yielded to the demand that subsequent runs in towns in the Rio Grande Valley served by Consolidated should be restricted. One distributor, Paramount, which was affiliated with Consolidated, agreed to impose the restrictions in certain other Texas and New Mexico cities.

The trial court found that the distributor appellants agreed and conspired among themselves to take uniform action upon the proposals made by Interstate.* [It also found that the distributors] agreed and conspired with each other and with Interstate to impose the demanded restrictions upon all subsequent-run exhibitors in Dallas, Fort Worth, Houston and San Antonio; that they carried out the agreement by imposing the restrictions upon their subsequent-run licensees in those cities, causing some of them to increase their admission price to 25¢, either generally or when restricted pictures were shown, and to abandon double-billing of all such pictures, and causing the other subsequent-run exhibitors, who were either unable or unwilling to accept the restrictions, to be deprived of any opportunity to exhibit the restricted pictures, which were the best and most popular of all new feature pictures; that the effect of the restrictions upon 'low-income members of the community' patronizing the theatres of these exhibitors was to withhold from them altogether the 'best entertainment furnished by the motion picture industry;' and that the restrictions operated to increase the income of the distributors and of Interstate and to deflect attendance from later-run exhibitors who yielded to the restrictions to the first-run theatres of Interstate.

The court concluded . . . that the agreement of the distributors with each other and those with Interstate to impose the restrictions upon subsequent-run exhibitors . . . with the aid and participation of Hoblitzelle and O'Donnell, constituted a combination and conspiracy in restraint of interstate commerce in violation of the Sherman Act. . . .

It accordingly enjoined the conspiracy and restrained the distributors from enforcing the restrictions in their license agreements with subsequent-run exhibitors. . . . This included both the contracts of Interstate with the distributors and the contract between

* [Among other things, the trial judge wrote that "the record justifies the conclusion that the months over which the 1934-35 contracts were incubated were, to some extent, occupied in the reconciliation of the differences between the eight distributors, . . . to the point where all agreed that such provision might go into their contracts with the respondent exhibitors."].

Consolidated and Paramount, whereby the latter agreed to impose the restrictions upon subsequent-run theatres in Texas and New Mexico served by it.

Appellants assail the decree of the District Court. . . .

THE AGREEMENT AMONG THE DISTRIBUTORS.

. . . As is usual in cases of alleged unlawful agreements to restrain commerce, the government is without the aid of direct testimony. . . . In order to establish agreement it is compelled to rely on inferences drawn from the course of conduct of the alleged conspirators.

The trial court drew the inference of agreement from the nature of the proposals made on behalf of Interstate and Consolidated; from the manner in which they were made; from the substantial unanimity of action taken upon them by the distributors; and from the fact that appellants did not call as witnesses any of the superior officials who negotiated the contracts with Interstate or any official who, in the normal course of business, would have had knowledge of the existence or non-existence of such an agreement among the distributors. . . . We think this inference of the trial court was rightly drawn from the evidence. . . .

The O'Donnell letter named on its face as addressees the eight local representatives of the distributors, and so from the beginning each of the distributors knew that the proposals were under consideration by the others. Each was aware that all were in active competition and that without substantially unanimous action with respect to the restrictions for any given territory there was risk of a substantial loss of the business and good will of the subsequent-run and independent exhibitors, but that with it there was the prospect of increased profits. There was, therefore, strong motive for concerted action, full advantage of which was taken by Interstate and Consolidated in presenting their demands to all in a single document.

There was risk, too, that without agreement diversity of action would follow. Compliance with the proposals involved a radical departure from the previous business practices of the industry and a drastic increase in admission prices of most of the subsequent-run theatres. Acceptance of the proposals was discouraged by at least three of the distributors' local managers. Independent exhibitors met and organized a futile protest which they presented to the representatives of Interstate and Consolidated. . . .

[The] independent negotiations [with each distributor led to] modifications of the proposals [that] resulted in substantially unanimous action of the distributors, both as to the terms of the restrictions and in the selection of the four cities where they were to operate.

One distributor . . . did not agree to impose the restrictions in Houston, . . . where its own affiliate operated a first-run theatre. The proposal was unanimously rejected as to [Galveston, Austin, and] the cities of the Rio Grande Valley served by Consolidated.

We may infer that Galveston was omitted because in that city there were no subsequent-run theatres in competition with Interstate. But we are unable to find in the record any

persuasive explanation [for] . . . the singular unanimity of action . . . in four Texas cities but not in a fifth or in the Rio Grande Valley. . . . It taxes credulity to believe that the several distributors would, in the circumstances, have accepted and put into operation with substantial unanimity such far-reaching changes in their business methods without some understanding that all were to join, and we reject as beyond the range of probability that it was the result of mere chance. . . .

The trial court, interpreting [O'Donnell's] letter in the light of the whole evidence, [concluded that it] showed unmistakably that one purpose of both demands was to protect first-run houses from competition of subsequent-run houses. . . . Taken together, the circumstances of the case . . ., when uncontradicted and with no more explanation than the record affords, justify the inference that the distributors acted in concert and in common agreement in imposing the restrictions upon their licensees in the four Texas cities.

This inference was supported and strengthened when the distributors, with like unanimity, failed to tender the testimony, at their command, of any officer or agent of a distributor who knew, or was in a position to know, whether in fact an agreement had been reached among them for concerted action.

When the proof supported, . . . the inference of such concert, the burden rested on appellants of going forward with the evidence to explain away or contradict it. . . . The failure under the circumstances to call as witnesses those officers who did have authority to act for the distributors and who were in a position to know whether they had acted in pursuance of agreement is itself persuasive that their testimony, if given, would have been unfavorable to appellants. The production of weak evidence when strong is available can lead only to the conclusion that the strong would have been adverse. . . .

While the District Court's finding of an agreement of the distributors among themselves is supported by the evidence, we think that in the circumstances of this case such agreement for the imposition of the restrictions upon subsequent-run exhibitors was not a prerequisite to an unlawful conspiracy. It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it.

Each distributor was advised that the others were asked to participate; each knew that cooperation was essential to successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce, which, we will presently point out, was unreasonable within the meaning of the Sherman Act, and knowing it, all participated in the plan. The evidence is persuasive that each distributor early became aware that the others had joined. With that knowledge they renewed the arrangement and carried it into effect for the two successive years.

It is elementary that an unlawful conspiracy may be and often is formed without simultaneous action or agreement on the part of the conspirators. . . . Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act. . . .

THE PROTECTION AFFORDED BY THE COPYRIGHT ACT TO THE CONTRACTS BETWEEN INTERSTATE AND THE DISTRIBUTORS.

The [defendants argue that the challenged agreements constitute] a legitimate exercise of the monopoly secured to the distributors by their copyrights.

Granted that each distributor, in the protection of his own copyright monopoly, was free to impose the present restrictions upon his licensees. [However, the distributors] . . . were not free to use their copyrights as implements for restraining commerce in order to protect Interstate's motion picture theatre monopoly by suppressing competition with it. . . .

A contract between a copyright owner and one who has no copyright, restraining the competitive distribution of the copyrighted articles in the open market in order to protect the latter from the competition, can no more be valid than a like agreement between two copyright owners or patentees. . . . In either case if the contract is effective, . . . competition is suppressed. . . . An agreement illegal because it suppresses competition is not any less so because the competitive article is copyrighted. The fact that the restraint is made easier or more effective by making the copyright subservient to the contract does not relieve it of illegality.

UNREASONABLENESS OF THE RESTRAINT.

The restrictions imposed on the subsequent-run exhibitors were harsh and arbitrary. . . . The effect was a drastic suppression of competition and an oppressive price maintenance, of benefit to Interstate and the distributors but injurious alike to Interstate's subsequent-run competitors and to the public.

The benefit, at such a cost does not justify the restraint. . . . It does not appear that the competition at which they were aimed was unfair or abnormal. *Cf. Appalachian Coals v. United States*, 288 U.S. 344 (1933). The consequence of the price restriction, though more oppressive, is comparable with the effect of resale price maintenance agreements, which have been held to be unreasonable restraints in violation of the Sherman Act. *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). . . .

We think the conclusion is unavoidable that the conspiracy and each contract between Interstate and the distributors by which those consequences were effected are violations of the Sherman Act and that the District Court rightly enjoined enforcement and renewal of these agreements, as well as of the conspiracy among the distributors.

Affirmed.

Mr. Justice FRANKFURTER took no part in the consideration or decision of this case.

Mr. Justice ROBERTS, dissenting.

. . .

Mr. Justice McREYNOLDS and Mr. Justice BUTLER join in this opinion.