

National Society of Professional Engineers v. United States

435 U.S. 679 (1978)

Mr. Justice STEVENS delivered the opinion of the Court.

This is a civil antitrust case brought by the United States to nullify an association's canon of ethics prohibiting competitive bidding by its members. The question is whether the canon may be justified under the Sherman Act § 1 because it was adopted by members of a learned profession for the purpose of minimizing the risk that competition would produce inferior engineering work endangering the public safety. The District Court rejected this justification. . . . Because we are satisfied that the asserted defense rests on a fundamental misunderstanding of the Rule of Reason frequently applied in antitrust litigation, we affirm.

I

Engineering is an important and learned profession. There are over 750,000 graduate engineers in the United States, of whom about 325,000 are registered as professional engineers. Registration requirements vary from State to State, but usually require the applicant to be a graduate engineer with at least four years of practical experience and to pass a written examination. About half of those who are registered engage in consulting engineering on a fee basis. . . . Engineering fees, amounting to well over \$2 billion each year, constitute about 5% of total construction costs. . . .

The National Society of Professional Engineers (Society) was organized in 1935 to deal with the nontechnical aspects of engineering practice, including the promotion of the professional, social, and economic interests of its members. Its present membership of 69,000 resides throughout the United States and in some foreign countries. Approximately 12,000 members are consulting engineers who offer their services to governmental, industrial, and private clients. Some Society members are principals or chief executive officers of some of the largest engineering firms in the country.

This case . . . involves a charge that the members of the Society have unlawfully agreed to refuse to negotiate or even to discuss the question of fees until after a prospective client has selected the engineer for a particular project. Evidence of this agreement is found in § 11(c) of the Society's Code of Ethics, adopted in July 1964.³

. . . The Society's Code of Ethics thus prohibits engineers from both soliciting and submitting such price information, and seeks to preserve the profession's "traditional" method of selecting professional engineers. Under the traditional method, the client initially selects an engineer on the basis of background and reputation, not price.

³ "[The Engineer] shall not solicit or submit engineering proposals on the basis of competitive bidding. Competitive bidding for professional engineering services is defined as the formal or informal submission, or receipt, of verbal or written estimates of cost or proposals in terms of dollars, man days of work required, percentage of construction cost, or any other measure of compensation whereby the prospective client may compare engineering services on a price basis prior to the time that one engineer, or one engineering organization, has been selected for negotiations. . . . An Engineer requested to submit a fee proposal or bid prior to the selection of an engineer or firm subject to the negotiation of a satisfactory contract, shall attempt to have the procedure changed to conform to ethical practices, but if not successful he shall withdraw from consideration for the proposed work. These principles shall be applied by the Engineer in obtaining the services of other professions."

In 1972 the Government filed its complaint against the Society alleging that members had agreed to abide by canons of ethics prohibiting the submission of competitive bids for engineering services and that, in consequence, price competition among the members had been suppressed and customers had been deprived of the benefits of free and open competition. The complaint prayed for an injunction terminating the unlawful agreement.

. . . [T]he Society averred that the standard set out in the Code of Ethics was reasonable because competition among professional engineers was contrary to the public interest. It was averred that it would be cheaper and easier for an engineer “to design and specify inefficient and unnecessarily expensive structures and methods of construction.” Accordingly, competitive pressure to offer engineering services at the lowest possible price would adversely affect the quality of engineering. Moreover, the practice of awarding engineering contracts to the lowest bidder, regardless of quality, would be dangerous to the public health, safety, and welfare. For these reasons, the Society claimed that its Code of Ethics was not an “unreasonable restraint of interstate trade or commerce.”

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II

In *Goldfarb v. Virginia State Bar*, 421 U.S. 773 (1975), the Court held that a bar association’s rule prescribing minimum fees for legal services violated § 1 of the Sherman Act. In that opinion the Court noted that certain practices by members of a learned profession might survive scrutiny under the Rule of Reason even though they would be viewed as a violation of the Sherman Act in another context. The Court said:

“The fact that a restraint operates upon a profession as distinguished from a business is, of course, relevant in determining whether that particular restraint violates the Sherman Act. It would be unrealistic to view the practice of professions as interchangeable with other business activities, and automatically to apply to the professions antitrust concepts which originated in other areas. The public service aspect, and other features of the professions, may require that a particular practice, which could properly be viewed as a violation of the Sherman Act in another context, be treated differently. We intimate no view on any other situation than the one with which we are confronted today.” *Goldfarb*, 421 U.S. at 788-789, n. 17.*

Relying heavily on this footnote, and on some of the major cases applying a Rule of Reason, petitioner argues that its attempt to preserve the profession’s traditional method . . . is a reasonable method of forestalling the public harm which might be produced by unrestrained competitive bidding.

. . .

A. The Rule of Reason.

One problem presented by the language of § 1 of the Sherman Act is that it cannot mean what it says. The statute says that “every” contract that restrains trade is unlawful. But, as Mr. Justice

* [The cited passage, known as *Goldfarb’s* footnote 17, is a peculiar antitrust dictum that the Supreme Court has not repudiated yet].

Brandeis perceptively noted, restraint is the very essence of every contract;¹⁰ read literally, § 1 would outlaw the entire body of private contract law. . . .

Congress, however, did not intend the text of the Sherman Act to delineate the full meaning of the statute or its application in concrete situations. The legislative history makes it perfectly clear that it expected the courts to give shape to the statute's broad mandate by drawing on common-law tradition. The Rule of Reason, with its origins in common-law precedents long antedating the Sherman Act, has served that purpose. It has been used to give the Act both flexibility and definition, and its central principle of antitrust analysis has remained constant. Contrary to its name, the Rule does not open the field of antitrust inquiry to any argument in favor of a challenged restraint that may fall within the realm of reason. Instead, it focuses directly on the challenged restraint's impact on competitive conditions. . . .

Unreasonableness under [the Rule of Reason] test could be based either (1) on the nature or character of the contracts, or (2) on surrounding circumstances giving rise to the inference or presumption that they were intended to restrain trade and enhance prices. Under either branch of the test, the inquiry is confined to a consideration of impact on competitive conditions.

In this respect the Rule of Reason has remained faithful to its origins. From Mr. Justice Brandeis' opinion for the Court in *Chicago Board of Trade*, to the Court opinion written by Mr. Justice Powell in *Continental T. V., Inc.*, the Court has adhered to the position that the inquiry mandated by the Rule of Reason is whether the challenged agreement is one that promotes competition or one that suppresses competition. "The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition." *Chicago Board of Trade v. United States*, 246 U.S. 231, at 243 (1918).¹⁷

There are, thus, two complementary categories of antitrust analysis. In the first category are agreements whose nature and necessary effect are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality—they are "illegal *per se*." In the second category are agreements whose competitive effect can only be evaluated by analyzing the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed. In either event, the purpose of the analysis is to form a judgment about the competitive significance of the restraint; it is not to decide whether a policy favoring competition is in the public interest, or in the interest of the members of an industry. Subject to exceptions defined by statute, that policy decision has been made by the Congress.

B. The Ban on Competitive Bidding.

Price is the "central nervous system of the economy," *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 226 n. 59 (1940), and an agreement that "interfere[s] with the setting of price by free market forces" is illegal on its face. *United States v. Container Corp.*, 393 U.S. 333, 337 (1969). In this case we are presented with an agreement among competitors to refuse to discuss prices with potential customers until after negotiations have resulted in the initial selection of an engineer. While this is not price fixing as such, no elaborate industry analysis is required to demonstrate the anticompetitive

¹⁰ "But the legality of an agreement or regulation cannot be determined by so simple a test, as whether it restrains competition. Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence." *Chicago Board of Trade v. United States*, 246 U.S. 231, 238 (1918). . . .

¹⁷ In *Continental T. V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 49 (1977), the Court explained [that under] the Rule of Reason standard . . . "the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition."

character of such an agreement. It operates as an absolute ban on competitive bidding, applying with equal force to both complicated and simple projects and to both inexperienced and sophisticated customers. . . . On its face, this agreement restrains trade within the meaning of § 1 of the Sherman Act.

. . . The Society nonetheless invokes the Rule of Reason, arguing that its restraint on price competition ultimately inures to the public benefit by preventing the production of inferior work and by insuring ethical behavior. . . . [T]his Court has never accepted such an argument.

It may be, as petitioner argues, that competition tends to force prices down and that an inexpensive item may be inferior to one that is more costly. There is some risk, therefore, that competition will cause some suppliers to market a defective product. Similarly, competitive bidding for engineering projects may be inherently imprecise and incapable of taking into account all the variables which will be involved in the actual performance of the project. Based on these considerations, a purchaser might conclude that his interest in quality—which may embrace the safety of the end product—outweighs the advantages of achieving cost savings by pitting one competitor against another. Or an individual vendor might independently refrain from price negotiation until he has satisfied himself that he fully understands the scope of his customers’ needs. . . . But these are not reasons that satisfy the Rule; nor are such individual decisions subject to antitrust attack.

The Sherman Act does not require competitive bidding; it prohibits unreasonable restraints on competition. Petitioner’s ban on competitive bidding prevents all customers from making price comparisons in the initial selection of an engineer, and imposes the Society’s views of the costs and benefits of competition on the entire marketplace. It is this restraint that must be justified under the Rule of Reason, and petitioner’s attempt to do so on the basis of the potential threat that competition poses to the public safety and the ethics of its profession is nothing less than a frontal assault on the basic policy of the Sherman Act.

The Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services. “The heart of our national economic policy long has been faith in the value of competition.” *Standard Oil Co. v. FTC*, 340 U.S. 231, 248 (1951). The assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain—quality, service, safety, and durability—and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers. Even assuming occasional exceptions to the presumed consequences of competition, the statutory policy precludes inquiry into the question whether competition is good or bad.

The fact that engineers are often involved in large-scale projects significantly affecting the public safety does not alter our analysis. Exceptions to the Sherman Act for potentially dangerous goods and services would be tantamount to a repeal of the statute. In our complex economy the number of items that may cause serious harm is almost endless—automobiles, drugs, foods, aircraft components, heavy equipment, and countless others, cause serious harm to individuals or to the public at large if defectively made. The judiciary cannot indirectly protect the public against this harm by conferring monopoly privileges on the manufacturers.

By the same token, the cautionary footnote in [*Goldfarb’s* footnote 17] cannot be read as fashioning a broad exemption under the Rule of Reason for learned professions. We adhere to the view expressed in *Goldfarb* that, by their nature, professional services may differ significantly from other business services, and, accordingly, the nature of the competition in such services may vary. Ethical norms may serve to regulate and promote this competition, and thus fall within the Rule of Reason. But the Society’s argument in this case is a far cry from such a position. . . . [W]e may assume

that competition is not entirely conducive to ethical behavior, but that is not a reason, cognizable under the Sherman Act, for doing away with competition.

In sum, the Rule of Reason does not support a defense based on the assumption that competition itself is unreasonable. . . .

III

Having found the Society guilty of a violation of the Sherman Act, the District Court was empowered to fashion appropriate restraints on the Society's future activities both to avoid a recurrence of the violation and to eliminate its consequences. While the resulting order may curtail the exercise of liberties that the Society might otherwise enjoy, that is a necessary and, in cases such as this, unavoidable consequence of the violation. Just as an injunction against price fixing abridges the freedom of businessmen to talk to one another about prices, so too the injunction in this case must restrict the Society's range of expression on the ethics of competitive bidding. . . .

The judgment of the Court of Appeals is *Affirmed*.