Appendix K

APPLICATION OF ANTITRUST PRINCIPLES TO VOLUNTARY INDUSTRY EFFORTS TO RESTRICT MARKETING AND SALES OF VIOLENT ENTERTAINMENT TO CHILDREN

Industry self-regulatory efforts to discourage marketing and sale of entertainment media products with violent content to children can take various forms, such as: (i) creation and operation of rating systems to identify and classify those products that warrant parental caution; (ii) industry self-regulatory codes that prohibit members from selling, renting, or marketing such restricted products in a way that undercuts the effectiveness of parental cautions; (iii) trade association rules that provide sanctions for failing to adhere to such a self-regulatory code; (iv) actions by manufacturers to discourage retailers from selling or renting violent products that warrant parental caution to children; and (v) advertising restraints, such as agreements with media members or groups to screen all advertising from manufacturers for excessively violent content. Although each of these measures has a somewhat different competitive implication, none is likely to violate the antitrust laws so long as the rules are sensibly designed and implemented to achieve the stated objective and not restrict competition in ways unrelated to the basic objective.[1]

Rating Systems. The creation and operation of a rating system to identify and classify entertainment products that warrant parental caution is unlikely to have a restrictive effect on competition because a rating system generally would not restrict the products that may be produced or sold.[2] Rather, the function of a rating system is informational. Like a safety standard for products, a rating system conveys information about the suitability of a product for a particular use. Rather than restrict competition in the market, a well-designed rating system can enhance the functioning of the market by enabling consumers to make useful comparisons and purchase decisions with minimal search costs.[3] A rating system may increase overall demand for products by reducing consumer confusion or uncertainty, and by increasing consumer confidence that the relevant attributes of the product will be as advertised.[4]

Restriction on Sales and Marketing to Children. Industry codes that prohibit members from selling, renting, or marketing certain entertainment products to children constitute a higher level of self-regulation, and could be challenged as agreements to restrain competition. So long as the industry limits the restraint to children, competition in sales to the adult audience is not likely to be affected. With respect to children, the restraint is fundamentally different from the

typical price-output restraint where competitors collectively seek to restrict supply and raise prices, and reap the economic benefits of the restraint: An agreement to refrain from sales to children would appear to be against the firms' immediate economic self-interest. Revenues from sales to children would not be enhanced; rather, they would decline (to zero, if the restraint is fully effective). The presence or absence of economic self-interest in imposing a restraint is a relevant consideration in assessing the asserted justifications.[5] Lack of economic self-interest would tend to lend greater credence to those justifications.[6] Here, the restraints would appear to reflect a determination not only by the industry, but also by the broader public, that sale to children of entertainment products that warrant parental caution is inappropriate.[7] Further, the sale of such products to children could undermine the efficient functioning of the market by creating mistrust of the industry and apprehension among consumers, possibly leading to a longer-term dampening effect on overall sales.[8] Consequently, restrictions on sales to children appear likely to have a legitimate justification if appropriately targeted.[9]

Disciplining Members for Non-Compliance. Industry codes that impose disciplinary measures on members that fail to adhere to rules regarding the sale, rental, or marketing of restricted entertainment products to children are yet another step in the self-regulatory process. Possible forms of discipline might include expulsion from membership in the association, or other withdrawal of membership privileges. Such rules could be challenged as an agreement to restrain the competition offered by the disciplined member. Although such disciplinary actions potentially could affect the disciplined member's sales not only to children but also to other segments of the market, they generally are unlikely to impose a significant restraint on competition unless two conditions are present: (i) the withdrawal of membership or of membership privileges would substantially impair the disciplined member's ability to compete, and (ii) the market has so few competitors that the loss of one competitor would significantly lessen competition.[10] These conditions appear unlikely to be found in the entertainment media industry. Association membership generally is not so important that loss of membership would effectively exclude a firm from the market. In addition, there may be a sufficient number of other firms to keep the market competitive even if one firm were expelled from membership for violating the codes. The use of clear and fair procedures in the design, implementation, and enforcement of such restrictions should further lessen any antitrust concerns.[11] Such procedural safeguards help ensure that the self-regulatory group's actions are impartial and not calculated to gain an economic or competitive advantage. Further, such rules may be justified because the

prohibited conduct, if left unchecked, may subvert or distort the competitive process if other firms succumb to a temptation to compete at the same level and consumers lose confidence in the industry's ability to properly market its products. Thus, appropriately designed code mechanisms to enforce reasonably designed restrictions also are likely to avoid antitrust problems.

Actions Against Retailers. Entertainment media producers might also act collectively to discipline retailers that sell or rent restricted products to children. An appropriately structured collective action of this type appears unlikely to violate federal antitrust laws. As with a collective self-restriction on such sales by producers themselves, a restraint directed toward inappropriate retailer sales is fundamentally unlike other restraints because it is contrary to immediate self-interest.[12]

Advertising Restraints. Efforts by producers to place appropriate limitations on the advertising of products that warrant parental caution need not restrict competition unreasonably. If, as suggested above, it is reasonable to impose certain restrictions on actual sales of inappropriate products to children, it should be reasonable under the antitrust laws to restrict advertising of these products to children. So long as the content and means available for marketing these products to adult audiences are not unduly restricted, consumers will continue to have access to product information, and sellers can continue to compete for their patronage.[13] Consequently, self-regulation reasonably tailored to prevent the advertising of restricted entertainment products to children should not impose a significant restraint on legitimate competitive activity. In fact, reasonable self-regulation should further the competitive process by focusing competitive efforts on legitimate marketing activities and by lessening the need for government regulation.

ENDNOTES

1. The antitrust laws are concerned about conduct that unreasonably restricts competition (*e.g.*, increases prices, reduces output, lowers quality or variety, or lessens innovation) and harms consumers. Self-regulation reasonably designed to discourage the marketing to children of entertainment media products that warrant parental caution – without undue effects on marketing to adults – is unlikely to have those prohibited effects. Under the antitrust laws, the legal test applicable to most kinds of self-regulation is called the "rule of reason." This test has two components: (1) whether the conduct significantly restricts competition; and (2) whether there are legitimate justifications for the conduct that further, rather than restrict, the competitive process. *See, e.g., Chicago Board of Trade v. United States,* 246 U.S. 231 (1918). The rule of reason test requires a balancing of these two elements. The exceptions to the application of the rule of reason test involve agreements that are not truly efforts at self-regulation, but rather are attempts to fix prices, restrict price competition, reduce output, or exclude competitors, without any legitimate justification. Such agreements are *per se* unlawful.

2. However, manipulation of a rating system to put a product in a restricted category without substantial justification can be problematic. *See Allied Tube & Conduit Corp. v. Indian Head,* 486 U.S. 492 (1988) (manufacturers of metal pipe unlawfully manipulated the certification process to deny market access for manufacturers of plastic pipe). Participation in the process by persons without an economic interest in stifling competition can help ensure that the result is not anticompetitive. *See id.* at 501 ("When . . . private associations promulgate safety standards based on the merits of objective expert judgments and through procedures that prevent the standard-setting process from being biased by members with economic interests in stifling product competition, those private standards can have significant procompetitive advantages." (citation omitted)). This suggests that public input into private industry's efforts to block children's access to products that warrant parental caution would tend to reduce antitrust risk.

3. *See Clamp-All Corp. v. Cast Iron Soil Pipe Inst.*, 851 F.2d 478, 487 (1st Cir. 1989) (Breyer, J.). *See also Tropic Film Corp. v. Paramount Pictures Corp.*, 319 F. Supp. 1247, 1254 (S.D.N.Y. 1970) (independent movie producer sought preliminary injunction against movie studio's refusal to distribute an unrated film, alleging violations of Sections 1 and 2 of the Sherman Act and asking the court to enjoin Paramount and the MPAA from carrying on an asserted industry-wide refusal to deal in and distribute, advertise, and exhibit the film *Tropic of Cancer* without an X rating; court denied the motion, stating that the rating system was "not designed to eliminate competition, but to advise motion picture exhibitors and, through them, the public, of the content of films which the Supreme Court has held that states have the constitutional right to prevent minors under seventeen from viewing").

4. *See generally* Self Regulation and Antitrust, Prepared Remarks of Robert Pitofsky, Chairman, Federal Trade Commission, Before the D.C. Bar Association Symposium (Feb. 18, 1998).

5. *See FTC v. Superior Court Trial Lawyers Ass'n,* 493 U.S. 411, 427 (1990) (rejecting asserted First Amendment justification of boycott by court-appointed trial lawyers seeking higher fees; stating that the justification is not available to a boycott conducted by business competitors who "stand to profit financially from a lessening of competition in the boycotted market") (quoting *Allied Tube & Conduit*, 486 U.S. at 508)); *United States v. Brown University*, 5 F.3d 658, 677–

78 (3d Cir. 1993) (discussing contours of rule of reason analysis of an arrangement among universities to determine the level of financial aid to be offered needy students); *Kreuzer v. American Academy of Periodontology*, 735 F.2d 1479, 1494 (D.C. Cir. 1984) (analyzing professional rule imposed by dental society, stating that "[w]hen the economic self-interest of the boycotting group and its proferred justifications merge the rule of reason will seldom be satisfied"); *cf. NAACP v. Claiborne Hardware Co.*, 458 U.S. 886 (1982); *Missouri v. National Org. for Women*, 620 F.2d 1301 (8th Cir. 1980).

6. *See United States v. Brown University,* 5 F.3d at 677 ("To the extent that economic self-interest or revenue maximization is operative . . . , it too renders [defendant's] public interest justification suspect.").

7. That the restraints have broader public origins, and are not imposed solely by agreement of competitors, is a relevant consideration. The Supreme Court has been skeptical of arguments that competitors should be permitted to restrict consumer choice on grounds that consumers may make "unwise" or "dangerous" decisions under competitive market conditions. *See National Soc'y of Prof'l Engineers v. United States*, 435 U.S. 679 (1978). In *Professional Engineers*, an association attempted to justify a ban on competitive bidding by claiming that such competition would lead to "deceptively low bids, and would thereby tempt individual engineers to do inferior work with consequent risk to public safety and health." *Id.* at 693. The Supreme Court rejected the asserted justification, explaining that "the Rule of Reason does not support a defense based on the assumption that competition itself is unreasonable." *Id.* at 696. In contrast, an agreement to refrain from marketing restricted entertainment products to children would reflect a broader societal view that a portion of the marketplace should not be available to children, not simply a judgment by competitors that competition should be restrained.

8. Further, it is not entirely clear that the prohibited conduct – selling to children products that warrant parental caution – is one that the competitive process is intended to foster. Professional associations often adopt ethical standards to govern members' conduct. Such agreements are permissible so long as they do not unreasonably restrict competition.

9. Reasonable self-regulation to prevent marketing of restricted products to children, therefore, would not necessarily conflict with the ruling of the Supreme Court in *Professional Engineers*, 435 U.S. 679, where the Court held that the rule of reason analysis is limited to competitive considerations. Reasonable self-regulation to prevent marketing of such products to children can assist the functioning of the market as well as serve broader societal interests. The situation in *Professional Engineers* was different. As noted above, in *Professional Engineers*, an association attempted to justify a ban on competitive bidding by claiming that such competition would lead to "deceptively low bids, and would thereby tempt individual engineers to do inferior work with consequent risk to public safety and health." *Id.* at 693. The Supreme Court rejected the asserted justification.

10. *See Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co*., 472 U.S. 284, 296 (1985) (expulsion from a purchasing cooperative did not create a probability of anticompetitive effect "unless the cooperative possess[ed] market power or exclusive access to an element essential to effective competition").

11. *See, e.g., Allied Tube & Conduit*, 486 U.S. at 501.

12. *See supra* text accompanying notes 3–4. However, there may be some antitrust risk if manufacturers seek to preclude a retailer from dealing with a non-member manufacturer. *See Fashion Originators' Guild v. FTC*, 312 U.S. 457 (1941) (group of designers of higher-priced dresses unlawfully boycotted outlets that dealt with manufacturers that "pirated" the higher-priced designs).

13. Even if a restricted advertising venue has a substantial audience suitable for the advertised product, as well as a significant underage audience, competition will not be significantly affected if firms have adequate access to other, permissible advertising venues that reach adults. Only if the various advertising or marketing restrictions, taken together, significantly restrict the flow of information to adult consumers might there be an antitrust concern.