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U.S. Chamber of Commerce

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U.S. Chamber of Commerce*

With domestic divergence on display and new leadership poised to assume command at both U.S. antitrust agencies, now is an appropriate time to take a fresh look at the Department of Justice Section 2 Report[1] ("Report"). Last year, the U.S. Chamber of Commerce had hoped that the Federal Trade Commission ("FTC") and Department of Justice ("DOJ") hearings on single-firm conduct would produce a consensus statement of U.S. policy in this important area of the law; providing sensible guidance to businesses and their counselors, the courts, global enforcement authorities, and others. Instead, their joint efforts resulted in the unilateral release of the Department of Justice Section 2 Report and the quick condemnation of that Report by three FTC Commissioners. The Chamber testified as part of the joint hearings and in its testimony emphasized the need for antitrust rules (particularly those governing single-firm conduct) that are transparent, predictable, consistent across jurisdictions, and reasonably stable over time. In addition, the central message in the Chamber's testimony was the need for U.S. antitrust enforcement officials to recognize the growing conflicts internationally with respect to

* This submission was compiled by the staff of the Chamber's Global Regulatory Cooperation Project, Sean Heather, Executive Director.

[1] U.S. Department of Justice, *Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act* (Washington: U.S. Department of Justice, 2008), available at http://www.usdoj.gov/atr/public/reports/236681.pdf.

enforcement involving single-firm conduct and the costs associated with such divergence. The Chamber called on the United States to lead a cooperative effort among industrialized nations to develop and recommend appropriate standards for single-firm conduct, and to promote their adoption around the world.

The Chamber argues in the following essay that the Section 2 report should not be summarily dismissed and believes that it is a credible and worthy contribution to the debate on single-firm conduct. Regardless of whether future agency leaders adopt the specific approaches taken in the Report, the Chamber urges those leaders to recognize that much of the Report is comfortably within the mainstream of current antitrust analysis, which cannot necessarily be said of all of the criticism of the Report. The Report represents a substantial body of work that, at a minimum, should be carefully considered as future leaders develop their enforcement policies. Any alternative policy prescriptions should be justified by analysis and support that is as substantial as that presented in the Report.

I. A SERIOUS AND IMPORTANT DEBATE WITH A LONG AND COMPLEX HISTORY

From the earliest days of federal antitrust enforcement, setting the rules of competition for market-leading firms has been a difficult task. Policy makers rightly fear that permissive standards might allow dominant firms to stifle competition in key industries, while restrictive standards may punish successful innovators and discourage the creativity essential to growth. Achieving proper balance is especially complex because often the very conduct that is challenged as anticompetitive—aggressive price-

cutting, for example—is the essence of healthy competition. The quest for rules that efficiently distinguish between aggressive competition and monopoly abuse has generated an enormous amount of research, scholarship, and commentary over many years. The landmark cases that have formulated and applied these rules—*United States v. Standard Oil Co.*, *United States v. Alcoa*, *United States v. IBM Corp.*, *United States v. AT&T Co.*—provoked controversy not only when they were filed and litigated but long after they were finally decided, as they were reassessed in light of experience.[2]

Reflecting the continuing importance of the issue, a number of recent high-level studies and reports have attempted to identify and address many of the key legal, economic, and institutional questions involving the antitrust rules applicable to single-firm conduct. Following an extensive public consultation process begun in 2005, the European Commission issued a *Guidance Paper* on the subject in December, 2008.[3] Significant portions of the April, 2007 Report and Recommendations of the U.S. Antitrust Modernization Commission[4] were devoted to the subject. The Canadian Bureau of Competition just issued draft Enforcement Guidelines on the abuse of dominance provisions of Canadian competition law, seeking public comment.[5]

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[2]A leading example of this continuing reassessment process is provided by *United States v. Standard Oil Co.*, one of the first landmark antitrust cases, decided in 1911. The case resulted in the break-up of the Standard Oil Trust—one of the largest antitrust divestitures in history. The case continues to be analyzed and reassessed, almost a century after the final decision. *See, e.g.*, E. Granitz & B. Klein, *Monopolization by "Raising Rivals' Costs:" The Standard Oil Case*, 39 J.L. & ECON. 1 (1996).

[3]European Commission, Guidance on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings (Dec. 3, 2008).

[4]Antitrust Modernization Commission, Report and Recommendations Chapter I.C., Apr. 2007.

[5]*Competition Bureau Seeks Comments on Abuse of Dominance Guidelines*, http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/02950.html (visited Jan. 23, 2009).

II. THE ANTITRUST DIVISION REPORT ON UNILATERAL CONDUCT AND THE FTC RESPONSE

One of the most thorough contributions to this recent outpouring emerged from work undertaken jointly by the DOJ and the FTC. In 2006 the agencies launched a year-long series of hearings on a wide range of subjects related to unilateral conduct, including how to identify a monopoly, the substantive standards used by courts and agencies to assess various forms of business conduct, the proper choice of remedies, and many others. The staffs of the two agencies had been working together on a report since the conclusion of the hearings. On September 8, 2008, the DOJ released the 213-page Report: outlining the main issues; analyzing the record of the hearings in the context of recent scholarship, commentary and case law; and, ultimately, announcing its standards for assessing unilateral conduct under Section 2 of the Sherman Act.[6] To the surprise of many, despite the close collaboration between the FTC and the DOJ throughout the process, the Report did not receive the endorsement of the FTC.[7]

Indeed, on the day the Report was released, two distinct statements were issued by the four incumbent FTC Commissioners, one by Commissioners Harbour, Leibowitz and Rosch ("HLR") and the other by Chairman Kovacic, speaking only for himself. HLR were sharply critical of the Report, calling it a "blueprint for radically weakened enforcement of Section 2 of the Sherman Act," and accusing the Report of being chiefly

[6] *Supra* note 1.

[7] The divergence between the agencies was not totally without precedent. The two agencies have differed publicly with regard to a variety of issues, including some recent high-profile cases involving unilateral conduct. *See, e.g.,* Statement of the Federal Trade Commission Declining To Join the U.S. Department of Justice Recommendation that the United States Supreme Court Review the Decision of the Court of Appeals for the Ninth Circuit in *linkLine Comm'ns v. Pacific Bell Tel. Co.* (May 23, 2008), available at http://www.ftc.gov/opa/2008/05/linkline.shtm (visited Jan. 27, 2009).

concerned with firms that enjoy monopoly or near monopoly power, and prescrib[ing] a legal regime that places these firms' interests ahead of the interests of consumers. The statement alleged that at almost every turn, the DOJ would place a thumb on the scales in favor of firms with monopoly or near-monopoly power and against other equally significant stakeholders.[8]

Chairman Kovacic's statement was considerably less critical, although he also declined to endorse the Report. He traced the development of modern Section 2 jurisprudence by the courts and commentators and summarized the key themes that have emerged, including an emphasis on economic efficiency, a presumption in favor of the individual firm's freedom to act unilaterally, concern for over-deterrence of pro-competitive conduct, and an emphasis on the need for legal rules that can be sensibly understood and administered in practice by courts, enforcement agencies, businesses, and the bar. Chairman Kovacic regretted the Report's lack of "more explicit consideration of…history and the institutional limitations of antitrust enforcement."[9]

Other voices joined in criticism of the Report, echoing HLR. For example, on November 1, 2008, the *New York Times*, in an editorial that took its title—*Another Thumb on the Scales*—from a key phrase in the HLR Statement, called the Report a

[8]Statement of Commissioners Harbour, Leibowitz and Rosch on the Issuance of the Section 2 Report by the Department of Justice 1 (Sept. 8, 2008), available at http://www.ftc.gov/os/2008/09/080908section2stmt.pdf.

[9]Chairman Kovacic linked recent court decisions defining explicit limits on certain types of antitrust claims to concerns about "overreaching" by private antitrust litigants, and pointed out that such limits also apply to claims by the government agencies. Accordingly, he encouraged "additional empirical research on the effect of private rights of action" to show "how the government enforcement agencies can challenge individual firms under Section 2 without imposing the same burdens as those resulting from private rights of action." Statement of Federal Trade Commission Chairman William E. Kovacic, Modern U.S. Competition Law and the Treatment of Dominant Firms: Comments on the Department of Justice and Federal Trade Commission Proceedings Relating to Section 2 of the Sherman Act (Sept. 8, 2008), available at http://www.ftc.gov/os/2008/09/080908section2stmtkovacic.pdf.

"deregulatory gift [by the Bush Administration] aimed at getting pesky antitrust enforcers off of the back of big business." Claiming that "new doctrine" fashioned in the Report "bends over backward to protect big firms," the Times claimed that "the next administration can ignore this report," going so far as to state flatly, "It should."[10]

Given the tone of this criticism, casual readers and others not following the "inside baseball game" of antitrust might assume that the Report took a superficial or ideological approach to this longstanding and complex problem. The tone of the criticism suggests that the Report may have glossed over complexities, ignored authority or evidence contrary to its positions, or used faulty logic to go from premises to conclusions. But any fair reading of the Report shows that such assumptions would be wrong. The Report is extensively documented and carefully reasoned, based on the wide-ranging hearing records and a balanced survey of judicial decisions, legal and economic scholarship, and enforcement experience. That its conclusions are not the only ones that could be drawn based on the record does not make those conclusions unreasonable, nor does it justify the tone of the Report's harshest critics.

It is hard to sort out precise differences between the Report and the Commission statements because the DOJ has issued a comprehensive document, while the FTC statements merely identify key disagreements. The HLR Statement does provide some commentary on each specific competitive practice covered in the Report: predatory pricing, loyalty discounts, bundled discounts, tying, unconditional refusal to deal with rivals, and exclusive dealing. HLR also takes direct issue with some of the more general

[10] *Another Thumb on the Scales*, N.Y. TIMES, Nov. 1, 2008, available at http://www.nytimes.com/2008/11/01/opinion/01sat2.html (visited Jan. 23, 2009).

policy assumptions explained in the Report. But there is much more that can be said regarding these differences, and a full airing of the issues would require a rehash of the full content of the Report, if not the hearing record itself. On January 24 the Commission released four FTC staff papers prepared for the joint project, but they cover only a minority of subjects addressed in the Report and, in any event, carried no official imprimatur of the Commission.[11] The HLR Statement asserts disagreements with the DOJ Report, but sound judgments about each of the specific issues addressed would require an independent and careful reassessment of the review that took place during the joint hearings.

As a result, how the FTC's specific enforcement prescriptions would differ from those given in the Report, and how they might be justified in light of the explanations given by the DOJ, remain largely undetermined. The DOJ authors would be justified in challenging the FTC to say what its own enforcement prescriptions would be, if different from those adopted in the Report, and why those prescriptions would be appropriate. The answer to this challenge is not fully discernable from the brief FTC statements, although it seems clear that HLR would take a more aggressive enforcement stance on the issues they address. The Report also covers a wider range of issues including economic theory, procedures, remedies, and international implications that are not mentioned by the Commission statements. As to these, there is even less of a basis for understanding how the FTC's approach would differ from the Report.

[11]Public Hearings: Federal Trade Commission and Department of Justice Hearings on Section 2 of the Sherman Act: Single-Firm Conduct As Related to Competition, http://www.ftc.gov/os/sectiontwohearings/index.shtm (visited Jan. 23, 2009).

III. AN IDEOLOGICAL EXTREME, OR ONE CHOICE AMONG REASONABLE ALTERNATIVES?

Even so, focusing on points of difference that are apparent from the FTC statements illuminates why it would be a mistake to ignore the Report, even if the new agency leadership ultimately adopts different enforcement approaches than those advocated in the Report. One almost universally acknowledged point is that while a broad consensus has developed on many fundamental issues in antitrust analysis, some issues remain the subject of debate, and, accordingly, many of the specific enforcement positions taken in the Report are debatable. As a result, HLR's repeated observation that few of the Report's positions are truly compelled by Supreme Court precedent, overwhelming consensus of the antitrust bar, or respected legal and economic scholarship is unpersuasive criticism where unilateral conduct is concerned. Given the range of uncertainty and disagreement that persists among reasonable discussants, however, a fair reading of the Report indicates that it is comfortably within range of the "center." The positions taken are well-supported by mainstream scholars, practitioners, and leading judicial precedents. It is important to bear this point in mind, lest the debate be misconstrued as involving a Report that tilts away from mainstream views versus an HLR response that takes more reasonable, pro-enforcement views.

Take, for example, the HLR criticism of the Report's "general" test for single-firm conduct. In many areas—tying, predatory pricing, exclusive dealing, etc.—the Supreme Court has provided at least some specific objective criteria against which a

firm's conduct can be measured.[12] In contrast, because the variety of business conduct that may come to be judged is so enormous, diverse, and evolving, a general test is needed as the default to assess practices for which no specific test has yet been formulated. The Report advocates that, in the "general" case, liability for unilateral conduct with both beneficial and harmful tendencies should attach only where the harm is "disproportionate" to any benefit. (Of course, conduct that is purely harmful can be condemned, while conduct that is purely beneficial should be cleared. Only where good and bad effects mix is there any debate.)

HLR points out that this standard would place a heavier burden on claimants than the "rule of reason" standard, an approach first developed with regard to anticompetitive agreements. The "rule of reason" standard typically requires only that the anticompetitive effect outweigh the pro-competitive effect of the conduct.[13] HLR cites an appellate decision in the *United States v. Microsoft* litigation that endorses such a balancing approach in the single-firm context, suggesting that the Report's position is more restrictive than precedent would support, or otherwise unwise and out of the mainstream.[14]

Closer examination, however, shows that these criticisms were anticipated by the Report, which carefully marshals authority and presents specific reasoning to support its

[12]Thus, for example, "tying" is deemed illegal only where the seller of the tying product exploits its market power to force buyers to accept a second distinct product. *Eastman Kodak Co. v. Image Technical Svs., Inc.*, 504 U.S. 451 (1992). Similarly, predatory pricing requires proof of pricing below cost with a reasonable prospect that the monopolist's losses can be recouped due to the anticompetitive impact of the predation. Brooke Group Ltd. v. Brown & Williamson Tobacco Co., 509 U.S. 209 (1993).

[13]In re: Polygram Holding, 136 F.T.C. 310 (2003), a*ff'd*, 416 F.3d 29 (D.C. Cir. 2005), contains a comprehensive history and analysis of the rule of reason approach in the horizontal agreement context.

[14]HLR p.5 & n.19.

choice of the "disproportionality" test.[15] The Report describes how a "balancing" test in effect subjects all unilateral conduct to the threat of extended litigation involving complex fact patterns, all within the shadow of extraordinarily severe antitrust penalties. The Report rightly demonstrates concern that applying a mere "balancing" test in this manner threatens the core antitrust values of preserving competitive initiative and avoiding punishment of successful innovators underlying much recent scholarship and Supreme Court jurisprudence in this area. The Report also points out that, despite literal application of the rule of reason, empirically it can be shown that courts rarely perform any true balancing. Indeed, it was suggested in the hearings—by a staunch opponent of the "disproportionality" approach—that the *Microsoft* decision cited by HLR in fact did not engage in "balancing."[16]

There is more. The "disproportionality" standard has been advocated by leading, mainstream antitrust scholars;[17] and the Report is, itself, a middle ground for the DOJ, located somewhat closer to the mainstream than earlier positions taken before the courts. In its *amicus* brief to the Supreme Court in *Trinko*,[18] the Solicitor General's brief, also signed by the DOJ, advocated a narrower "no-economic-sense" test (at least for the refusal-to-deal argument challenged in that case)—a test regularly advocated by the DOJ

[15]Report Ch. I § III.B, Ch. 3 § III.A.

[16]Report Ch. 3 § III.A & n.40 (quoting testimony of former FTC Chair Robert Pitofsky).

[17]HERBERT HOVENKAMP, THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION 152, 154 (2005) ("The law does not require consumer benefits of zero, but only that the amount of harm be significantly disproportionate to the benefits."). The Antitrust Division Report discusses the underlying issues relevant to the test, cites other authorities, and discusses several leading alternative formulations of a general test for monopolizing conduct. Chapter 3 § III.

[18]Verizon Communications, Inc. v. Trinko, 540 U.S. 398 (2004)

in other monopolization cases.[19] However, the Report takes a step back and explicitly declines to endorse the "no-economic-sense" test except as a potentially useful inquiry, rather than as a general test for legality.

Thus, in the Report, the DOJ reached an accommodation with other approaches supported by sound analysis and advocated by respected advocates and scholars. The Report's references to academic work, precedent, and the hearing record, as well as its analysis, deserve to be considered by anyone facing these important and complex issues. Even if the ultimate policy views of some subsequent reviewer may differ from the specific approaches adopted in the Report, those approaches and the support that underlies them hardly deserve to be ignored, or treated as a "thumb on the scales."

Moreover, regardless of whether one agrees that the "disproportionality" standard should be adopted by the courts as a matter of law, it may still be sensible, for those charged with enforcing Section 2, to bear in mind the rationales for that standard, especially when formulating their enforcement policy in this area. Just as the courts have rarely found it feasible to engage in actual "balancing" of competitive effects in Section 2 cases, the same is generally true for enforcers, who arguably should only bring such cases when highly confident that the competitive harm they are trying to prevent outweighs the benefits of that conduct. The fact that the federal agencies have brought relatively few Section 2 cases over the years, even when the agencies' leaders took generally pro-enforcement stances, suggests that they wisely avoided trying to fine-tune business conduct by bringing extremely close cases. This prudent approach to Section 2

[19] G. Werden, *Identifying Exclusionary Conduct Under Section 2: The "No Economic Sense" Test*, 73 ANTITRUST L.J. 413 (2006).

enforcement could be expressed as a legal standard requiring "disproportionate" harm, or as a prosecutorial standard that recognizes the need for careful enforcement decisions that are based on solid evidence of competitive harm and that seek to avoid deterring legitimate conduct.

Another example from the list of the Report's specific practices criticized by HLR reinforces the basic point that, while some of the Report's policy positions may be debatable, these positions and the analysis underlying them are well-supported. The appropriate rule for predatory pricing has long been considered among the most controversial of all antitrust topics. Early precedent[20] was heavily criticized.[21] More recently the debate about proper legal standards was clarified and stimulated by a path-breaking article written by two distinguished antitrust scholars.[22] The leading case on the issue is *Brooke Group Ltd. v. Brown & Williamson Tobacco Co.*, 509 U.S. 209 (1993). That case defined the predatory pricing offense as pricing below cost with a reasonable expectation that the resulting losses could be recouped through the anticompetitive effects of the pricing conduct.

In the wake of *Brooke Group*, a debate involving scholars, lower courts, and enforcement agencies has attempted to determine the appropriate cost standard to use in applying the "below-cost" prong of the definition. The Supreme Court's own precise words—"below an appropriate measure of cost"—are Delphic. Should there be one standard for all cases, or is one "measure of cost" appropriate for some cases and a

[20]Utah Pie Co. v. Cont'l Baking Co., 386 U.S. 685 (1967).

[21]K. Elzinga & T. Hogarty, *Utah Pie and the Consequences of Robinson-Patman*, 21 J.L. & ECON. 427 & n.3 (1978)("Criticisms of Utah Pie are too numerous to cite.").

[22]P. Areeda & D. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L.REV. 697 (1975).

different standard appropriate for others? Several alternatives have been suggested—marginal cost, average variable cost, and so forth. The Report, after reviewing the copious literature and numerous proposals, chooses as its standard "average avoidable cost."

While none of the lower courts, antitrust scholars (legal or economic), or antitrust practitioners are unanimously in support of this rule, it is a logical, considered, and reasonable choice. It would not be correct to describe it as an enforcement policy choice that favors monopolists at the expense of consumers, nor does it fall outside the present antitrust mainstream. To the contrary, the "avoidable cost" standard drew favorable appellate-court notice and comment as early as 1983,[23] and more recent scholarship and court decisions also provide some support for this standard.[24] Yet HLR criticizes this approach because "[n]o Supreme Court decision has embraced . . ." it. But the Report can hardly be criticized for providing clear and reasonable guidance in an area where the Court has declined to resolve the specific question, or even to provide qualitative guidance. To await definitive guidance in an area as critical to business decision making as unilateral price-cutting—given the complexity, duration, expense, and potentially enormous penalties of litigation—is inferior in key respects to a clear and reasonable choice of a specific standard. This is especially so in light of the extreme rarity of Supreme Court cases addressing the issue. Twenty-six years passed between *Utah Pie* and *Brooke Group*. Should the agencies wait that long for more guidance on the cost standard before choosing any specific approach?

[23]Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 235-36 (1st Cir. 1983) (Breyer, J.).

[24]Report n.156.

Tying is another area that illustrates the fundamental legitimacy of the Report's analysis. The Report's conclusion that tying arrangements should be judged under the rule of reason, rather than the quasi-*per se* approach taken in much of the case law, arguably is a mainstream view that has broad support in the antitrust community. Indeed, the U.S. agencies in the Clinton Administration expressly took that position with respect to tying arrangements in intellectual property licenses in the 1995 *Intellectual Property Guidelines*.[25] The HLR statement, citing the Supreme Court's *Jefferson Parish* decision,[26] criticizes the Report for declaring, "[c]ontrary to existing Supreme Court case law," that tying is often pro-competitive, "even by a firm with monopoly or near-monopoly power."[27]

This criticism may be seen as simply restating the quasi-*per se* approach to tying arrangements—that a tie between two products, coerced by market power, is unlawful—which has been widely criticized by antitrust scholars, commentators, and some judicial decisions. A unanimous Supreme Court arguably signaled the demise of *per se* treatment of tying in the recent *Illinois Tool Works* decision.[28] The Report's analysis of tying is credible, well-supported, and consistent with longstanding agency policies.

IV. REASONABLE ALTERNATIVES THROUGH REASONABLE DISCUSSION

Debates about antitrust standards for single-firm conduct are not likely to be settled with epithets. The legal, economic, and policy issues are as important and as

[25]U.S. Department of Justice and Federal Trade Commission, Antitrust Guidelines for the Licensing of Intellectual Property (1995), Section 5.3.

[26]Jefferson parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2 (1984).

[27]HLR p. 8 & n. 26.

[28]Ill. Tool Works Inc. v. Indep. Ink, Inc., 547 U.S. 28, 35-37 (2006)(unanimous opinion by Stevens, J., noting how the Court's earlier "strong disapproval of tying arrangements has substantially diminished").

complex as any broad question about how best to structure economic activity for the maximum benefit of society. They are as intricate and controversial as any other area of antitrust doctrine or policy. The range of products, industries, technologies, and other circumstances to which the law is applied—as illustrated by the striking diversity of the leading cases that have arisen over the years—guarantees that generalities will often be proven wrong, and arguments about the best approach can be long and heated. Bringing to bear a vast record of scholarship, commentary, precedent, and analysis is a helpful approach—not an attempt to place a "thumb on the scales."

The Antitrust Division Report should be read, considered, and appreciated for its content and for the enormous effort it represents, not only by the agencies themselves but also by the numerous witnesses and commentators who submitted views and willingly gave their time and the benefit of their long experience in order to advance this important debate. It is also important that the analysis and scholarship of the report be recognized as a useful reference in the discussions of various international approaches to unilateral conduct, (signified, for example, by the EC Guidelines and the Canadian guidelines). It is not a repudiation of the Report to believe that different conclusions were indicated, viewing the record as a whole. But it is a departure from the long tradition of consensus-building and collegiality among antitrust agency officials, scholars, and practitioners (who must advise clients every day regarding practical answers to real-world issues) to portray a well-founded and serious contribution to this important debate as a voice to be ignored. Moreover, criticism of the Report and any alternative policy prescriptions that may be proposed should also be subjected to scrutiny, and any different conclusions

should be justified with equally substantial analysis and support.