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> If an economist finds something—a business practice of one sort or another—that he does not understand, he looks for a monopoly explanation. And as in this field we are very ignorant, the number of understandable practices tends to be very large, and the reliance on a monopoly explanation, frequent.[2]

Ronald Coase surveyed the state of the industrial organization literature some 27 years ago and identified what he perceived as the economics profession's reflexive tendency to rely on anticompetitive explanations for business practices that were difficult for economists to understand. This reflex could be attributed, at least in part, to the fact that novel business practices deviated from the abstract, textbook model of perfect competition. Nearly three decades later, a review of modern industrial organization textbooks or leading economic journals increasingly reveals a nearly endless collection of sophisticated and elegant mathematical models of firm behavior largely dedicated to identifying the possibility of anticompetitive equilibria. One suspects that the economics profession has not done much to change Coase's mind over the last three decades.

Coase's critique was not specifically aimed at the field of antitrust economics, but it could have been. The incorporation of economic thought into antitrust is a complex matter with a nuanced history. It is difficult, however, to contemplate that history without noting a pattern of reflexive condemnations of new business practices on grounds consistent with "state of the art" theory only to quietly discover, decades later, that the underlying efficiency explanations for the practices at issue had been ignored. This is the tale of 1960s merger analysis and its reliance on the structure-conduct-performance paradigm which had yet to come under the scrutiny of Harold Demsetz and others.

It is also the tale of vertical restraints jurisprudence during the next two decades. Novel and innovative business practices including franchise agreements, resale price maintenance, exclusive territories and other vertical restraints, vertical integration, and exclusive dealing were routinely condemned. Each new business practice was initially condemned, followed by a period of stockpiling new economic knowledge, followed by legal changes reflecting updated economic thinking. And so the antitrust cycle continued. *Per se* rules were eliminated or pared down. Rule of reason analyses were structured to reflect greater awareness of potential efficiency justifications.

Lest one think that these tales are simply antitrust history and have little to do with the new and improved modern approach to antitrust, it is appropriate to note that federal courts and antitrust agencies have continued this trend by condemning shelf-space slotting contracts,[3]

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[2] Ronald Coase, *Industrial Organization: A Proposal for Research*, in 3 POLICY ISSUES AND RESEARCH OPPORTUNITIES IN INDUSTRIAL ORGANIZATION 59, 67 (Victor Fuchs ed. 1972).

[3] *See, e.g.*, FTC v. McCormick, FTC Dkt. No. C-3939 (2000).

category management arrangements,[4] and good faith renegotiations of licensing arrangements in the standard setting context.[5] Of course, the most well known example of the application of newly minted economic theory on network effects and interoperability to novel business practices is *U.S. v. Microsoft*. To date, the debate between economists as to whether that particular enforcement action has produced net consumer benefits continues.[6]

The strength of antitrust doctrine has been its ability to incorporate economic thought and empirical evidence over time. The consumer benefits from that incorporation are well known and uncontroversial. But change in economic thought can be slow. And in the sometimes lengthy period before those changes are incorporated into antitrust doctrine and enforcement decisions, the history of antitrust suggests a tendency toward false positives when innovative business practices are involved.

Consider for example, the work of the most recent Nobel Laureate in Economics, Oliver Williamson.[7] As Coase lamented the state of the modern industrial organization literature, Oliver Williamson, Ben Klein,[8] and others, in keeping with Coase's observation, were applying the insights of transaction cost economics to provide pro-competitive economic explanations of the vertical restraints being routinely condemned at the time. Thirty years later, the best available empirical evidence demonstrates that Williamson and Klein were largely correct about vertical contractual arrangements and these insights have largely been reflected in the shift toward rule of reason analysis for vertical restraints.[9]

What does any of this have to do with antitrust and the dynamics of competition in high-tech industries? Modern antitrust economics still exhibits the reflexive tendency to rely on anticompetitive explanations for new business practices and methods that are not well understood. This tendency has been historically proven to be a formula for Type I errors[10] in cases involving innovative business practices or arrangements in innovative industries. Unfortunately, nowhere is it more important for antitrust enforcers and courts to exhibit an awareness of the large social costs associated with Type 1 errors than in innovative industries.

Put simply, given the link between innovation and economic growth, the stakes of "getting it right" are higher. Caution and humility are warranted in light of both the historical hostility towards innovative business practices by competition policy as well as the large gaps of empirically-validated theory in the economic literature on competition and innovation. The traditional problem of identifying and distinguishing pro-competitive from anticompetitive conduct faced by enforcers and courts in all monopolization cases is a difficult one. But those difficulties are exacerbated in innovative industries.

Even more unfortunately in light of these concerns, the Obama administration's new approach to antitrust enforcement has explicitly been to specifically target successful firms in innovative industries. While this new approach gives significant reason for concerns from a consumer welfare perspective, there are at least two reasons to be optimistic that a more

[4] Conwood Co. v. United States Tobacco Co., 290 F.3d 768 (6th Cir. 2002). *See also* Joshua D. Wright, *An Antitrust Analysis of Category Management:* Conwood Co. v. United States Tobacco Co., 17 SUP. CT. ECON. REV. 311 (2009).

[5] *In re* Negotiated Data Solutions LLC (N-Data), No. 051-0094 (F.T.C. January 23, 2008).

[6] *See, e.g.*, William H. Page & John E. Lopatka, THE MICROSOFT CASE: ANTITRUST, HIGH TECHNOLOGY, AND CONSUMER WELFARE (Chicago Press 2007).

[7] OLIVER E. WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM (1985).

[8] Joshua D. Wright, *Benjamin Klein's Contributions to Law and Economics, in* PIONEERS IN LAW AND ECONOMICS (Lloyd R. Cohen & Joshua D. Wright, eds., 2009)

[9] Antitrust analysis of vertical restraints cannot yet be declared a success story for economics as pending legislation at the federal and state levels restoring the *per se* rule against minimum resale price maintenance threaten to undo this progress—despite overwhelming evidence that resale price maintenance is not associated with the anticompetitive consequences for which *per se* condemnation is reserved.

[10] Type 1 errors are false positive errors, i.e. the firm is falsely accused or convicted of an antitrust violation.

moderate approach to antitrust enforcement in innovative industries will prevail. The first is that, despite the Obama administration's protestations to the contrary, the Supreme Court's interpretation of monopolization standards reflects the same concerns for Type 1 errors and preference for enforcement modesty as expressed in the now discarded Section 2 Report.[11] This places significant constraints on innovative thinking on enforcement strategies within the agencies. The second reason is that the latest Nobel Prize awarded to Oliver Williamson gives some hope that the economics profession will shift its focus in the direction called for by Coase three decades ago.

[11] U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT (2008). This report was issued by the DOJ under the George W. Bush administration and subsequently withdrawn by the DOJ after the new Obama administration took office.