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Respecting the Limits of Antitrust: The Roberts Court Versus the Enforcement Agencies

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Abstract

Antitrust, the body of law aimed at protecting consumers from exercises of market power, is inherently limited in what it can accomplish. Accordingly, courts and antitrust enforcers should strive to optimize the law's effectiveness. This Legal Memorandum *assesses the degree to which the Supreme Court of the United States and the federal antitrust enforcement agencies have respected the limits of antitrust and embraced an optimizing approach. It concludes that the Court under Chief Justice John Roberts has done an admirable job in attempting to maximize antitrust's social value but that the federal enforcement agencies have not.*

Key Points

- The Roberts Court and the federal enforcement agencies have taken strikingly different stances on the limits of antitrust. The Roberts Court has crafted rules calculated to maximize antitrust's social value in light of its inherent limitations. The agencies seem skeptical of the very existence of antitrust's limits.
- Generalist judges regularly confront cases across the legal spectrum; know the limits of their expertise; and, in light of their life tenure and limited opportunities for advancement, have no obvious need to expand their turf. Agency staff tend to gain both prestige and financial rewards as their authority expands, so their natural tendency is to expand the law's reach.
- Two things are clear: Recent enforcement agency policies are in severe tension with the philosophy that informs Supreme Court antitrust jurisprudence, and if the agencies do not reverse course, acknowledge antitrust's limits, and seek to optimize the law in light of those limits, consumers and the competitive process will suffer.

The Basic Structure of American Antitrust Law

When it comes to assuring low prices, high-quality goods and services, and product variety, there is no better regulator than market competition. Accordingly, the federal antitrust laws—chiefly, the Sherman and Clayton Acts—aim to promote vigorous competition among providers of goods and services. They do so by policing the two situations in which competition breaks down: monopoly (when there is a single dominant seller) and collusion (when nominal competitors agree not to compete).

The two main provisions of the Sherman Act correspond to these defects in competition. Section 1 forbids any "contract, combination ... or conspiracy" in restraint of trade, which would cover collusion.[1] Section 2 addresses monopoly, making it illegal to "monopolize" or "attempt to monopolize" a market.[2] These provisions may be enforced by the government: the Federal Trade Commission (FTC)[3] and the Antitrust Division of the Department of Justice

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(DOJ). They are also enforceable by private plaintiffs who are "injured in [their] business or property" by antitrust violations.[4]

Because many antitrust violations, especially those involving collusion, occur in secret and cannot be successfully prosecuted, successful private plaintiffs are entitled to recover treble damages (*i.e.*, three times the amount of loss occasioned by the antitrust violation).[5] Multiplying damages in this fashion aims to ensure "optimal deterrence" by creating appropriate incentives for potential violators, who are caught only a fraction of the time, to obey the law.

Implementing the antitrust laws has proven somewhat difficult. Much of the difficulty has stemmed from the breadth and generality of the statutory prohibitions.

- By its terms, Section 1 forbids all agreements that restrain trade, but virtually every commercial contract restrains trade: When I promise to sell something to you, I "restrain" myself from selling the thing to another. The U.S. Supreme Court has thus ruled that Section 1 forbids only agreements that "unreasonably" restrain trade.[6]

- Section 2's prohibition of actual and attempted monopolization has been interpreted to require that the defendant (1) possess some degree of market power and (2) engage in "exclusionary" conduct,[7] but a great many pro-consumer business activities—*e.g.*, price cuts and product enhancements—win business for the actor and thereby tend to "exclude" its rivals. Accordingly, courts now understand that a Section 2 violation requires "unreasonably" exclusionary conduct.

In most antitrust actions, courts must therefore assess the reasonableness of the conduct being challenged. They have generally done so by focusing on whether the challenged conduct enhances or reduces overall, quality-adjusted market output. If the practice at issue increases market output, benefiting consumers, the practice is reasonable; if it reduces market output, injuring consumers, the practice is unreasonable. Most of the time, reasonableness is assessed on a case-by-case basis, following a "rule of reason" that takes account of market features and the actual effect of the practice being challenged. For some practices, though, experience has consistently shown that the activity reduces market output, so an in-depth judicial evaluation seems unnecessary. Such practices are deemed to be "*per se*" unreasonable and thus illegal.

In the end, then, antitrust consists of a body of law that (1) attempts to ensure competition among market participants; (2) involves statutory prohibitions that are quite general and must be "fleshed out" by courts, which perform their task by assessing the likely effects of challenged conduct on overall market output; and (3) is highly attractive to private plaintiffs (and plaintiffs' lawyers) seeking treble damages. Taken together, these features limit the benefits that antitrust confers on society.

The Limits of Antitrust and an Optimizing Approach

Antitrust is limited in its ability to enhance overall social welfare because its implementation is costly. Most obviously, there are significant costs in simply reaching a decision as to whether a particular business practice violates the antitrust laws. Because many business practices are "mixed bags" in that they may reduce competition on some fronts while enhancing it on others, the legality of a challenged practice generally turns on whether the practice, on the whole, is likely to enhance or reduce overall market output.

Answering that question, which ultimately determines whether the practice is "reasonable," frequently requires a good deal of economic inquiry. Unless a practice has been classified as *per se* illegal, decision makers—both business planners assessing

1. 15 U.S.C. § 1.
2. 15 U.S.C. § 2.
3. The FTC enforces the Clayton Act and the FTC Act, 15 U.S.C. §§ 41–58, which forbids all activity that violates the Sherman Act.
4. 15 U.S.C. § 15.
5. *Id*.
6. *See* Bd. of Trade of the City of Chicago v. United States, 246 U.S. 231, 238 (1918).
7. *See* United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

proposed conduct in advance and courts and enforcers evaluating it in retrospect—must often incur considerable costs in defining and evaluating the relevant market, studying the practice at issue, and assessing the conduct's actual or likely effects on market output. Those are antitrust's "decision costs."

Antitrust adjudication will impose additional costs whenever the adjudicator reaches an incorrect liability decision. If the adjudicator wrongly fails to condemn an anticompetitive practice, the perpetrator(s) will gain "market power"—the ability to enhance profits by reducing output and hiking prices. The existence of such power tends to reduce social welfare as productive resources are allocated away from their highest and best ends.[8] On the other hand, if the adjudicator wrongly condemns a practice that enhances overall market output, consumers will be denied the benefit of enhanced production.

Such false condemnation of an efficient practice is likely to be even more costly than a false acquittal of an anticompetitive one. Whereas market power exists only in a particular market and tends to self-correct as new sellers enter that market in response to high prices, condemnation of an efficient business practice—the result of a false conviction—has economy-wide effects that cannot be corrected absent a court decision or statute overruling the decision that wrongly condemned the practice at issue. Taken together, the welfare losses from improper acquittals of anticompetitive practices and unwarranted convictions of output-enhancing practices comprise antitrust's "error costs."

Decision costs and the two types of error costs (from false acquittals and false convictions) are in inexorable tension. Simplifying a liability rule in an effort to reduce decision costs will tend to increase the incidence of wrong decisions and thereby enhance error costs. Making a rule more plaintiff-friendly in an effort to reduce false acquittals will increase false convictions. On the other hand, tweaking the rule in a defendant-friendly fashion may reduce false convictions but will increase false acquittals.

Making the liability rule more nuanced in an attempt to reduce both false acquittals and false condemnations will raise decision costs. As in a game of Whack-a-Mole, hammering down costs in one area causes them to spike elsewhere.

In light of this unhappy situation, then-Professor (now Judge) Frank H. Easterbrook, in an influential article entitled "The Limits of Antitrust," recommended that antitrust tribunals give up trying to catch every anticompetitive act and endeavor instead to optimize antitrust. Specifically, Easterbrook argued, courts and enforcers should craft liability and procedural rules that minimize the sum of antitrust's error and decision costs.[9] Taking that tack will ensure that the inherently limited antitrust laws generate as much social value as possible.

So how have the courts and enforcement agencies fared in harnessing Easterbrook's insights to maximize antitrust's social value? In recent years, the U.S. Supreme Court seems largely to have recognized antitrust's limits and to have adopted rules consistent with Judge Easterbrook's overarching policy prescription. The Court's holdings are aimed at making it clearer to businesses what they can and cannot do, consistent with antitrust, and also providing substantial leeway for businesses to compete aggressively.

This approach helps consumers: When businesses have greater legal certainty, they have a stronger incentive to bring forth the new products and services that the public desires. Moreover, when companies spend less time treading cautiously to avoid antitrust investigations, their costs are lower, and this means that they can provide new offerings at lower prices than would otherwise be possible.

In recent years, however, the enforcement agencies have adopted various positions that are at odds with a "limits of antitrust" approach. This approach has spawned costly new uncertainty for American businesses and has prevented them (and thus consumers) from reaping the full benefits of the Supreme Court's pragmatic and enlightened antitrust holdings.

8. Firms with market power are not constrained by competition into providing the maximum level of value for consumers. They tend to channel productive resources in a manner that maximizes their own profits but not overall social welfare. *See generally* Herbert Hovenkamp, Federal Antitrust Policy: The Law of Competition and Its Practice 19–21 (4th ed. 2011). Such an "allocative inefficiency" is the primary adverse effect that antitrust seeks to prevent.

9. *See* Frank H. Easterbrook, *The Limits of Antitrust*, 63 Tex. L. Rev. 1, 16 (1984) ("The legal system should be designed to minimize the total costs of (1) anticompetitive practices that escape condemnation; (2) competitive practices that are condemned or deterred; and (3) the system itself.").

The Roberts Court's Respect for Antitrust's Limits

Since John Roberts became its Chief Justice, the U.S. Supreme Court has taken quite an interest in antitrust.[10] Consideration of the Roberts Court's seven decisions addressing vertical restraints of trade, exclusionary conduct, and antitrust enforcement reveals that each is consistent with a limits-of-antitrust approach, with several expressly seeking to minimize error and decision costs.[11]

Vertical Restraints. Vertical restraints of trade are trade-limiting agreements between economic actors at different stages in the distribution scheme (*e.g.*, between a manufacturer and a retailer that carries its brand). One such restraint, "minimum resale price maintenance" or "RPM," occurs when a manufacturer prohibits resellers of its brand, usually retailers, from selling below a certain price level.

The Supreme Court held in 1911 that RPM is always ("*per se*") illegal as a form of "price fixing" that prevents price competition among retailers. Subsequent research, however, revealed that RPM often is used by manufacturers to incentivize distributors to provide point-of-sale services that consumers desire. Indeed, studies revealed that most instances of the practice increase rather than reduce market output. Thus, the *per se* rule generated substantial error costs by precluding many distribution contracts that could have raised consumer welfare.

Recognizing this, in 2007, the Supreme Court in *Leegin* overruled the old precedent and held that instances of RPM should be evaluated on a case-by-case basis under the antitrust "rule of reason." By encouraging socially beneficial RPM contracts to proceed while maintaining courts' ability to strike down truly harmful examples of RPM, the *Leegin* decision embodied a welfare-enhancing limits-of-antitrust approach to this important business practice.[12]

In its *Independent Ink* decision, the Court corrected another vertical restraints doctrine that threatened substantial error costs. Under long-standing precedent, tying—agreeing to sell some "tying" product (for example, a printer) on the condition that the buyer also purchase your "tied" product (for example, toner cartridges)—is *per se* illegal if (among other conditions) the defendant has market power (the ability to raise price and restrict output to less than competitive levels) over the tying product.[13]

The Court had suggested many years ago that the defendant's mere possession of a patent on the tying product would be enough to establish market power over the tying product.[14] Such an understanding threatened to produce many false convictions because, in reality, most patents do not confer market power.[15] To prevent false convictions stemming from its improvident remark about patents and market power, the Court clarified in *Independent Ink* that mere possession of a patent on a tying product could not establish tying market power for purposes of a *per se* tying claim.

Both *Leegin* and *Independent Ink*, then, promise to reduce the error costs associated with antitrust regulation of vertical restraints.

Exclusionary Conduct. The Roberts Court has decided two cases involving conduct alleged to be unreasonably exclusionary and thus violative of Sherman Act Section 2. In *Weyerhaeuser*, the Court

10. Whereas the Rehnquist Court decided one antitrust case from 1993 through 1995, one each year from 1996 through 1999, and none from 2000 through 2003, the Roberts Court decided six antitrust cases in 2006 and 2007 alone. It has since decided four others.

11. In addition to the antitrust decisions discussed here, the Roberts Court has decided three cases involving horizontal restraints of trade. As I have elsewhere explained, two of those decisions—Texaco Inc. v. Dagher, 547 U.S. 1 (2006), and American Needle, Inc. v. NFL, 560 U.S. 183 (2010)—are consistent with an effort to minimize the sum of antitrust's error and decision costs. *See* Thomas A. Lambert, *The Roberts Court and the Limits of Antitrust*, 52 B. C. L. Rev. 871, 906–09, 920–28 (2011). The third decision involving horizontal restraints—FTC v. Actavis, 133 S. Ct. 2223 (2013)—is admittedly difficult to square with a limits-of-antitrust approach. The position espoused in the dissent by Chief Justice Roberts seems to fit better with Easterbrook's overarching policy prescription.

12. Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007).

13. Illinois Tool Works, Inc. v. Independent Ink, Inc., 547 U.S. 28 (2006).

14. *See* Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 16 (1984) (observing that "if the Government has granted the seller a patent or similar monopoly over a product, it is fair to presume that the inability to buy the product elsewhere gives the seller market power").

15. The product that a patent covers often competes vigorously with many other products, preventing the seller of the patented product from exercising market power. In many other cases, a patent covers such a small component of a larger product that the patent cannot make the product unique enough to confer market power on its seller. *See* U.S. Dep't of Justice and U.S. Fed. Trade Comm'n, *Antitrust Guidelines for the Licensing of Intellectual Property* 4 (1995) (U.S. federal antitrust agencies will not presume that a patent confers market power on its owner).

held that a plaintiff complaining of "predatory overbidding" by a rival buyer of inputs must demonstrate that (1) the defendant bid up input prices so high that the prices it charged for its output were below its own cost and (2) the defendant was likely to recoup its losses from below-cost pricing by underpaying for inputs once its predatory strategy eliminated rival input buyers.[16] The Court reasoned that its bright-line rule would capture most instances of anticompetitive bidding yet refrain from chilling legitimate bidding behavior. In other words, the two-part liability test would minimize social losses from false convictions and false acquittals while keeping administrative (decision) costs in check.

In *LinkLine*, the Court addressed "price squeezes" by "vertically integrated monopolists."[17] In a price squeeze, a firm that has monopoly power over some input (*e.g.*, aluminum ingots) but competes with others in selling a final product incorporating that input (*e.g.*, rolled aluminum sheets) simultaneously raises its input price and lowers or holds constant its output price. Rival producers in the competitive output market find their profits "squeezed" because their costs rise, but they cannot increase their output prices without losing business to the vertically integrated input producer.

LinkLine held that a price squeeze does not constitute an independent violation of the Sherman Act.[18] To reach that conclusion, the Court relied on two precedents that had embraced a limits-of-antitrust approach. One was *Trinko*, which held that there is no general antitrust duty for a monopolist to deal with its rivals.[19] Any such duty, the *Trinko* Court reasoned, would (1) generate numerous and costly errors by encouraging collusion and reducing firms' incentives to invest in economically beneficial facilities[20] and (2) entail high decision costs by "requir[ing] antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill suited."[21]

The other precedent upon which the *LinkLine* Court relied was *Brooke Group*, which held that a firm cannot be liable for predatory pricing unless it sets its price below its cost.[22] The *Brooke Group* Court emphasized that the liability rule it was imposing was not aimed at capturing every instance of anticompetitive low pricing, but rather was designed to condemn as many as possible without chilling procompetitive discounting practices and while keeping decision costs in check.[23]

Trinko and *Brooke Group* collectively foreclose liability based on a price squeeze. *Trinko* precludes liability based on the defendant's hiking of input prices: If a firm has no general duty to deal with its rivals at all, then it certainly has no duty to sell to them at low prices. *Brooke Group* prevents liability for reducing output price to a non-predatory level (*i.e.*, one that exceeds or equals the defendant's cost). Given that *Trinko* and *Brooke Group* were themselves efforts to minimize the sum of error and decision costs, *LinkLine*'s holding—the logical result of combining the two precedents—similarly reflects such an effort.

Enforcement. The Roberts Court has decided three antitrust cases focusing not on substantive standards of liability for specific business practices but on antitrust enforcement generally. Again, each is consistent with a limits-of-antitrust approach.

In *Twombly*, the Court held that a plaintiff cannot plead the "agreement" (contract, combination, or conspiracy) element of a Section 1 claim merely by pointing to parallel behavior by the defendant and its alleged coconspirators and baldly asserting that

16. Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 549 U.S. 312 (2007).

17. Pacific Bell Tel. Co. v. LinkLine Communications, Inc., 555 U.S. 438 (2009).

18. *Id*. at 452.

19. *See* Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, 540 U.S. 398, 408–11 (2004).

20. *Id*. at 407–08 ("Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of the antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities.... Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion.").

21. *Id*. at 408.

22. *See* Brooke Group v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222–24 (1993). Specifically, Brooke Group required a predatory pricing plaintiff to establish both below-cost pricing by the defendant and a "dangerous probability" that the defendant would recoup its losses from below-cost pricing by charging supracompetitive prices once its rivals were extinguished. *Id*. at 223–24.

23. *Id*. at 223–24.

the parties must have agreed to act in concert.[24] To survive a motion to dismiss for failure to plead an agreement, the Court held, a Section 1 plaintiff must make non-conclusory allegations "plausibly suggesting (not merely consistent with) agreement."[25]

That holding recognized and attempted to address an inherent limitation in antitrust's private enforcement scheme: The prospect of costly discovery and treble damages based on far-reaching economic harms often leads defendants to settle even meritless antitrust actions, and plaintiffs' lawyers, well aware of defendants' tendency to settle, have an incentive to conjure up bogus conspiracy claims any time they observe competitors acting in parallel fashion. By heightening the requirements for proceeding to discovery on an antitrust conspiracy claim, the *Twombly* Court reined in the costs associated with private enforcement of the antitrust laws.

The issue in the Court's *Credit Suisse* decision was whether certain securities marketing practices that seemed to create an anticompetitive effect but were regulated by the Securities and Exchange Commission (SEC) could give rise to a private antitrust action.[26] In holding that they could not, the Supreme Court explicitly embraced a limits-of-antitrust approach, comparing the error costs of allowing versus not allowing an antitrust claim to proceed. Permitting the antitrust action, the Court reasoned, would entail a significant risk of false convictions, given that judges, unlike SEC officials, generally lack the ability to distinguish between desirable and undesirable securities marketing practices.[27] Moreover, the practices likely to be wrongly convicted or chilled tend to create significant social value.[28]

Taken together, these considerations suggest that error costs from allowing the action at issue could be quite large. On the other hand, any costs from not permitting the antitrust action to proceed would likely be small. Because the activity at issue was already regulated by the SEC, which has been directed "to take account of competitive considerations" in crafting its rules, there was little need to worry about social losses from falsely acquitting the behavior under the antitrust laws.[29] In the end, then, the *Credit Suisse* Court rested its holding on an explicit comparison of the error costs of false convictions versus false acquittals.

While the Roberts Court's most recent enforcement decision expanded the scope of potential antitrust liability, it too is consistent with an effort to reduce the sum of antitrust's error and decision costs. The issue in *Phoebe Putney* was whether a merger orchestrated by a local hospital authority was immune from federal antitrust liability.[30] Prior Supreme Court precedents had established that when a substate entity (*e.g.*, some unit of local government) acts pursuant to authority granted by the state, its actions will be immune from federal antitrust law if the anticompetitive effect at issue was the "foreseeable result" of what the state authorized.[31]

The court of appeals had held that the loss of competition from the hospital merger being challenged was a foreseeable result of the state statute conferring general corporate powers, including the power to buy and sell hospitals, on the local hospital authority. In a unanimous reversal, the Supreme Court ruled that it is not enough for the state simply to grant general corporate powers, even acquisition authority. Instead, substate entities will be immune from antitrust liability only if either the authorizing legislature expressly contemplated the anticompetitive effect at issue or such effect was "the inherent, logical, or ordinary result of the exercise of the authority delegated by the state legislature."[32]

This holding is consistent with an approach aimed at minimizing antitrust's error and decision

24. Bell Atlantic Co. v. Twombly, 550 U.S. 544, 569–70 (2007).
25. *Id*. at 557. In particular, a plaintiff that seeks to plead agreement by alleging parallel conduct must also allege "plus factors" suggesting that the parallelism is more likely the product of conspiracy than of independent action.
26. *See* Credit Suisse Secs. (USA) v. Billing, 551 U.S. 264 (2007).
27. *Id*. at 279–81.
28. *Id*. at 282.
29. *Id*. at 283.
30. F.T.C. v. Phoebe Putney Health Sys., Inc., 133 S. Ct. 1003 (2013).
31. Hallie v. Eau Claire, 471 U.S. 34, 42–43 (1985).
32. F.T.C. v. Phoebe Putney Health Sys., Inc., at 1012–13.

costs. Allowing a state's granting of general corporate powers to immunize a substate entity from antitrust liability simply because the granted power could be exercised in an anticompetitive fashion creates a huge loophole that would acquit a significant number of truly anticompetitive acts. The Court's holding avoids those errors without significantly increasing the likelihood of false convictions. After all, any state legislature that wishes to stay antitrust's hand in order to pursue other laudable policies could express its intention to displace competition with the legislation delegating authority to the substate entity. Such intentional displacement of competition is likely to be uncommon, but it can be accomplished when desired.

In sum, the Roberts Court's antitrust decisions addressing vertical restraints, exclusionary conduct, and antitrust enforcement have been uniformly consistent with an effort to minimize antitrust's error and decision costs. We turn now to consider the degree to which the enforcement agencies have followed the Supreme Court's lead.

The Enforcement Agencies' Disregard for Antitrust's Limits

During the time in which the Roberts Court has consistently crafted antitrust decisions that respect the law's inherent limitations, the Federal Trade Commission and Department of Justice have moved in the opposite direction. In at least four areas, these agencies have taken actions that are likely to increase the sum of antitrust's error and decision costs.

Exclusionary Conduct. The agencies' insensitivity to the limits of antitrust is perhaps most evident in their rejection of enforcement guidelines on challenges to unilateral (single-firm) "exclusionary" (harmful) conduct. Recognizing the difficulty of distinguishing unreasonably exclusionary conduct from aggressive but legitimate competition, the FTC and DOJ set out in 2006 to provide some guidance on how the agencies would enforce the unilateral conduct provisions of Sherman Act Section 2. Over the course of a year, the agencies heard from 29 panels featuring 119 witnesses and considered substantial empirical evidence.[33]

The final Section 2 Report, released in September 2008 and comprising more than 200 pages, set forth principles to guide agency enforcement decisions in cases involving various categories of single-firm practices.[34] The report also addressed potentially exclusionary conduct not falling into one of the highlighted categories and thus not subject to a conduct-specific liability test. Such conduct, the report concluded, should be deemed unlawful under Section 2 only if its anticompetitive harms were shown to be substantially disproportionate to its procompetitive benefits.[35]

The Section 2 Report was closely attuned to the limits of antitrust. For each of the particular practices addressed, the report assessed why it is a competitive mixed bag—*i.e.*, how it could occasion anticompetitive harm but might also create procompetitive benefits. The report then set forth liability rules designed to be both administrable and capable of condemning most anticompetitive instances of a practice while screening out those likely to create net benefits.

The report was particularly concerned about overdeterring output-enhancing behavior, reflecting a belief that market power is self-destructive (so that false conviction is of greater concern than false acquittal). In particular, the report sought to avoid overdeterrence by requiring that under Section 2 rule of reason analysis, a practice should be condemned only if it "disproportionately" impairs consumer welfare.

In the end, both enforcement agencies abandoned the Section 2 Report. The FTC never even signed on, with a majority of commissioners asserting that the report was deficient because it endorsed a limits-of-antitrust approach.[36] Specifically, the commission majority downplayed the risk of error, rejected the view that overdeterrence is of greater concern in antitrust than is underdeterrence, questioned the degree to which market power tends to be self-correcting, and discounted the value of administrable

33. *See* U.S. Dep't of Justice, Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act 1 (2008).

34. *See id.* at 49–76 (predatory pricing/bidding); 131–42 (exclusive dealing); 77–90 (tying); 91–118 (bundled and loyalty discounts); 119–30 (refusals to deal).

35. *Id.* at 45–46.

36. *See* Statement of Commissioners Harbour, Leibowitz, and Rosch on the Issuance of the Section 2 Report by the Department of Justice 1 (Sept. 2008).

rules and screening devices.[37] Within a few months, the DOJ followed suit.[38]

The enforcement agencies' abandonment of the Section 2 Report has liberated them to take aggressive enforcement actions against single-firm conduct that disadvantages a defendant's rivals. It is doubtful, however, that such aggressive, competitor-focused enforcement will benefit consumers.

Consider, for example, the FTC's late 2009 action against Intel Corp. The commission accused Intel of violating Section 2 by offering "loyalty rebates"[39] that would have passed muster under the guidelines in the Section 2 Report.[40] To settle the FTC action, Intel entered a consent decree in which it agreed not to give loyalty discounts in the future.[41] Surely, many of the forbidden discounts, which would have lowered consumer prices, would have been procompetitive.

Moreover, the FTC's action reaches far beyond Intel. Because of the FTC action and subsequent settlement, similarly situated firms are likely to forgo their own loyalty discounts; they certainly have a fair response when purchasers of their products request such price cuts. To the extent that it increases the likelihood of enforcement actions like that in *Intel*, the agencies' abandonment of the limits of antitrust–inspired Section 2 Report is likely to injure consumers.

Vertical Restraints. Despite empirical evidence demonstrating that most vertical trade restraints enhance rather than reduce market output,[42] the enforcement agencies remain hostile to such practices. With respect to minimum RPM, the FTC has indicated that it will continue to place a heavy burden on defendants. The commission has also taken a tough stance against exclusive dealing arrangements between manufacturers and retailers.

Minimum RPM. The commission set forth its position on minimum RPM in response to a request by women's shoemaker Nine West to modify a consent decree the company had entered into when the practice was *per se* illegal. After the *Leegin* Court abrogated the *per se* rule, Nine West sought to void the parts of the consent order forbidding the company's use of the practice.

The FTC ultimately agreed to loosen the constraints on Nine West, but in so doing, it set forth an evaluative approach that places a heavy burden on manufacturers considering—and thus discourages

37. *Id*. at 3–4.

38. In her first public remarks after President Obama appointed her to head DOJ's Antitrust Division, Assistant Attorney General Christine Varney announced that the Department would no longer adhere to the principles set forth in the Section 2 Report. She explained that she "d[id] not share" either the report's "skepticism regarding the ability of antitrust enforcers as well as antitrust courts to distinguish between anticompetitive acts and lawful conduct" or its "related concern that the failure to make proper distinctions may lead to 'over deterrence' with regard to potentially anticompetitive conduct." Christine A. Varney, *Vigorous Antitrust Enforcement in this Challenging Era* (May 11, 2009) (*available at* http://www.justice.gov/atr/public/speeches/245711/pdf).

39. Loyalty rebates involve discounts for firms that buy a specified percentage of their needs from a single seller.

40. *See* Complaint, *In re* Intel Corp., No. 9341 (F.T.C. Dec. 16, 2009).

41. *See* Decision and Order, *In re* Intel Corp., No. 9341 (Oct. 29, 2010) (stating that Intel shall not, for a 10-year period, "condition[] any Benefit to a Customer based on the Market Segment Share of a Relevant Product or a Computer Product Chipset that a Customer awards to [Intel] or to any competitor").

42. See, *e.g.*, Francine Lafontaine & Margaret Slade, *Exclusive Contracts and Vertical Restraints: Empirical Evidence and Public Policy* in Handbook of Antitrust Economics 391 (Paolo Buccirossi ed., 2008) ("[I]t appears that when manufacturers choose to impose restraints, not only do they make themselves better off but they also typically allow consumers to benefit from higher quality products and better service provision"); Daniel O'Brien, *The Antitrust Treatment of Vertical Restraints: Beyond the Possibility Theorems* in The Pros and Cons of Vertical Restraints 40, 72–73 (2008) (observing that "with few exceptions, the literature does not support the view that [vertical restraints] are used for anticompetitive reasons" and that vertical restraints "are unlikely to be anticompetitive in most cases").

firms from implementing—RPM policies.[43] It therefore discourages the use of RPM arrangements, a perverse result in light of the evidence showing that such arrangements usually increase overall market output.

Exclusive Dealing. Recent FTC enforcement actions have displayed a similarly unwarranted hostility toward exclusive dealing arrangements. Exclusive dealing occurs when a seller (often a manufacturer) conditions the sale of its product on an agreement by the buyer (often a retailer) to purchase all of its requirements from that seller.[44]

Given that exclusive dealing frequently benefits consumers, the Supreme Court has long insisted that harm to competition—an actual or likely reduction in overall market output, not simply harm to an individual competitor—is necessary for antitrust liability based on the practice.[45] In recent months, however, the FTC has condemned exclusive dealing arrangements despite both a lack of evidence of anticompetitive harm and a procompetitive rationale for the arrangements under attack.

In its January 2014 *McWane* decision,[46] for example, the FTC condemned an exclusive dealing arrangement even though there was no direct evidence of consumer harm (*i.e.*, higher prices or reduced output), but there was evidence that rivals of the manufacturer implementing the policy had entered the market and grown their market shares with the policy in place.[47] The record even demonstrated that the allegedly disadvantaged rival experienced the very same growth rate while the exclusive dealing policy was in place that it experienced in the periods before and after imposition of the policy.[48]

On top of all that, there was a procompetitive rationale for the policy: It protected McWane, which made a full line of domestic pipe fittings, from adverse cherry-picking by rivals that produced only the most popular, high-margin fittings. Such cher-

43. *See* Order Granting in Part Petition to Reopen and Modify Order Issued April 11, 2000, In re Nine West Group, Inc., No. C-3937 (F.T.C. May 6, 2008), at 13–16. Under the Commission's approach, a manufacturer that has required dealers of its product to charge minimum prices can avoid having its RPM deemed presumptively illegal only if it shows that (1) the manufacturers using RPM do not comprise a significant portion of the relevant market; (2) the RPM was initiated by the manufacturer, not its dealers; and (3) there is no dominant manufacturer or dealer. If the defendant fails to make any of these showings, its RPM will be presumed unreasonable (and thus illegal) unless the defendant proves that the RPM had the effect of increasing its total sales. The burden that the FTC's approach places on a manufacturer that chooses to use RPM is considerable. The manufacturer must be prepared to establish the contours of the relevant market (always a difficult task); produce data on the use of RPM by other manufacturers in that market; and show that those utilizing the practice do not account for a large share of the overall market. The manufacturer must also be able to show that it, not its dealers, initiated the RPM. That showing would be difficult to make if there were any evidence that dealers providing a high level of customer service had complained about free-riding by their low-service, cheaper rivals. While such dealer complaints may simply have alerted the manufacturer to its need to induce higher dealer quality by reducing price competition among dealers, they could easily be taken to suggest that dealers, not the manufacturer, initiated the restraint. Finally, a defendant manufacturer must be prepared to show that neither it nor any of its dealers possessed market power. That would require the manufacturer to define a second (dealer) market. If the defendant failed to make any of these showings, it could avoid liability only by proving that its RPM increased its overall output. To do that, it would have to engage in sophisticated statistical analysis to isolate the effects of RPM from other factors that could affect overall output.

44. *See* Single-Firm Conduct Report, *supra* note 33, at 131. Exclusive dealing may cause anticompetitive harm if buyers' exclusivity commitments foreclose the seller's rivals from so many available sales opportunities that those rivals are forced to reduce their production below "minimum efficient scale"—the level of output at which economies of scale are exhausted so that producing more does not reduce the producer's average costs. See Joshua D. Wright, *Moving Beyond Naïve Foreclosure Analysis*, 19 Geo. Mason L. Rev. 1163, 1166–67 (2012). Exclusive dealing may cause anticompetitive harm if buyers' exclusivity commitments foreclose the seller's rivals from so many available sales opportunities that those rivals are forced to reduce their production below "minimum efficient scale." At the same time, exclusive dealing arrangements may be used to secure a number of output-enhancing benefits. They may (1) encourage manufacturers to invest in their retailers' operations by preventing other manufacturers from free-riding on those investments; (2) reduce consumer prices by intensifying competition among producers for distribution; (3) enhance consumer welfare by reducing the costs associated with uncertain supply and demand; and (4) encourage the production of multi-component systems by protecting producers of complete systems from adverse "cherry-picking" by producers of popular, high-margin individual components. *See* Howard P. Marvel, *Exclusive Dealing*, 25 J. L. & Econ. 1, 6–11 (1982); Benjamin Klein & Kevin M. Murphy, *Exclusive Dealing Intensifies Competition for Distribution*, 75 Antitrust L. J. 433 (2008); Hovenkamp, *supra* note 8, at ___; and Roy W. Kenney & Benjamin Klein, *The Economics of Block Booking*, 26 J. L. & ECON. 497 (1983).

45. *See* Tampa Electric Co. v. Nashville Coal Co., 365 U.S. 320, 329 (1961) (requiring showing of harm to competition).

46. Opinion of the Commission, *In re* McWane, Inc., No. 9351 (F.T.C. Jan. 30, 2014).

47. *See* Dissenting Statement of Commissioner Joshua D. Wright, *In re* McWane, Inc., No. 9351 (Jan. 30, 2014), at 5, 30–32, 35.

48. *See id*. at 45.

ry-picking could have injured consumers by creating gaps in product availability.[49] The FTC's condemnation of McWane's exclusive dealing therefore thwarted a procompetitive benefit despite a lack of credible evidence of anticompetitive harm.

The commission's recent *Graco* settlement similarly involved reflexive and unwarranted condemnation of exclusive dealing.[50] Graco, the leading manufacturer of "fast set equipment" (FSE) used to apply polyurethane coatings, acquired its two primary rivals in 2005 and 2008. The mergers extinguished competition in the North American FSE market, but a breakup of the companies was impracticable. The FTC therefore imposed restrictions on Graco's conduct. The evidence showed that Graco had coerced FSE distributors into not carrying products of Graco's rivals and had filed a questionable lawsuit against a rival supplier, causing FSE distributors to grow leery of that supplier and drop its products. Accordingly, the consent order prohibited Graco from engaging in distributor coercion and required dismissal of its questionable lawsuit.

But the order then went further. It prohibited Graco from entering into exclusive dealing contracts with distributors, and it placed limits on Graco's freedom to grant loyalty discounts to distributors.[51] The problem with this is that there was no evidence that those last forbidden activities—exclusive dealing arrangements and loyalty discounts—contributed to the absence of competition in the FSE market; rather, they likely made the market more competitive.[52] By forbidding exclusive dealing and loyalty discounts, the commission's consent order threatened to cause a consumer injury, and there was no reason to take such risk absent evidence that exclusive dealing had been used or was likely to be used in the future to create anticompetitive harm.

Intellectual Property Rights and Technology Standards. Back in the days when antitrust was less tightly moored to consumer welfare, the enforcement agencies were quick to find antitrust violations based on the exercise of intellectual property rights.[53] In recognition of the key role such rights play in furthering consumer welfare, however, the federal antitrust enforcement agencies eventually adopted a policy of treating intellectual property (IP) rights the same as conventional forms of property.[54]

49. Because McWane's fixed costs (*e.g.*, the cost of casting a die) were similar for both rarely used and popular fittings, McWane's average production cost for a rarely used fitting [*i.e.*, (fixed costs + variable costs)/number of units produced] was higher than its average cost for an oft-used part. That meant that if McWane charged similar prices for technologically similar parts—a pricing practice that purchasers often expect—it needed to "subsidize" production of rarely used fittings with margins earned on popular parts. An equally efficient producer of only popular fittings would not have to engage in such "cross-subsidization" to finance the production of rarely used parts and would be able to sell its popular fittings at a lower price. But if too many buyers purchased their often-used fittings from the partial line producer, McWane could no longer afford to produce rarely used parts, and gaps in product availability would result. By requiring buyers of its fittings to refrain from handling those of other producers, McWane could prevent the sort of cherry-picking that would have rendered its production of obscure parts uneconomical.

50. *See* Decision and Order, *In re* Graco, Inc., No. C-4399 (F.T.C. Apr. 17, 2013).

51. *See id.* at pp. 6–7.

52. As the Commission acknowledged, the market for FSE is precisely the sort of market in which exclusive dealing arrangements achieve the procompetitive benefit of avoiding "inter-brand free-riding." Manufacturers of FSE will enhance total sales if they train distributors on the proper use and various complicated features of FSE. Consumers benefit from (and sales are increased by) such training, because the distributors pass along their learning to end-user purchasers. But if one FSE manufacturer trains a distributor on how to use and market the equipment, other manufacturers whose product is carried by that distributor will not need to do so themselves. The possibility that they will take a free ride at the expense of the manufacturer providing the training tends to dissuade all manufacturers from providing such training, to the detriment of consumers. Exclusive dealing or a loyalty discount that achieves near exclusivity may prevent extensive free riding and thereby assure a manufacturer that it will receive the full benefit of its training efforts. See Statement of Commissioner Joshua D. Wright, In re Graco, File No. 101-0215 (Apr. 17, 2013), at 3 ("[T]he Commission's Complaint describes the fast-set equipment market as one particularly well suited for exclusive arrangements. Specifically, the Complaint acknowledges the sale of fast-set equipment demands specialized third party distributors that possess the technical expertise to teach consumers how to use and maintain the manufacturer's equipment.").

53. Bruce B. Wilson, Deputy Assistant Att'y Gen., Antitrust Division, *Is the Past Prologue, or Where Do We Go from Here?*, Remarks before the Michigan State Bar Antitrust Law Section (Sept. 21, 1972), reprinted in 5 CCH Trade Reg. Rep. (CCH) ¶ 50,146 (setting forth then-prevailing antitrust law's "Nine No-No's" related to intellectual property licensing).

54. *See* U.S. Dep't of Justice & Fed. Trade Comm'n, Antitrust Guidelines for the Licensing of Intellectual Property § 2.1 (1995) ("Agencies apply the same general antitrust principles to conduct involving intellectual property that they apply to conduct involving any other form of tangible or intangible property….").

The agencies proceeded from the premise that patent and other IP rights create incentives for innovation and its dissemination and commercialization by establishing enforceable property rights for the creators of new and useful products. Substandard protection for those rights (treating them as "second class property rights" that can arbitrarily be limited by government action) reduces investment in the creation of IP, which in turn slows the rate of innovation and retards the introduction of goods and services that consumers desire.

Unfortunately, however, federal antitrust enforcers now seem to be departing from the policy of supporting robust IP rights. In recent years, they have sought to use antitrust (including unfair competition law)[55] to constrain patent holders' standard rights when their patents have been incorporated into technological standards.

The agencies' purported goal in invoking antitrust in this context is to prevent anticompetitive "hold-up" by holders of "standard essential patents" (SEPs)—*i.e.,* patents that a producer must license in order to utilize some technological standard (like the 4G standard for mobile telephones). "Commonly, businesses collaborate to establish [technology] standards by working through standard setting organizations ('SSOs') to develop a standard that all firms, regardless of whether they participate in the process, then can use in making products."[56]

Once a technology standard has been widely adopted, SEP holders are in a good position to demand higher royalties from the producers implementing that standard.[57] To prevent such "hold-up" of vulnerable producers that have become locked in to a certain technology standard, SSOs frequently require that businesses active in an SSO must commit to licensing their patents that implicate features of a standard on "reasonable and non-discriminatory" (RAND) or "fair, reasonable, and non-discriminatory" (FRAND) terms.[58] The U.S. federal enforcement agencies have invoked antitrust to police two behaviors by SEP holders that have previously committed to grant licenses on F/RAND terms: suing for injunctive relief (rather than monetary damages)[59] and attempting to renegotiate license terms.[60]

While anticompetitive hold-up may be a legitimate concern when an SEP holder takes one of these actions, invoking antitrust in this context seems unwarranted. Patent and contract law already prevent anticompetitive hold-up here. Because the patent law standard for granting injunctions requires courts to consider the public interest when deciding whether to grant such relief,[61] it is wholly capable of precluding anticompetitive injunctions. Attempted license renegotiations, then, are subject to well-established contract doctrines that permit renegotiation when it is justified by legitimate commercial considerations, but not otherwise (especially if the

55. Some of the agency action discussed here was taken pursuant to Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, which enables the FTC to police "unfair methods of competition" even when those methods would not constitute a stand-alone violation of the Sherman Act. Within this subpart, I refer to Section 5 actions as antitrust actions.

56. U.S. Dep't of Justice and Fed. Trade Comm'n, Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition 33 (2007), *available at* http://www.ftc.gov/sites/default/files/documents/reports/antitrust-enforcement-and-intellectual-property-rights-promoting-innovation-and-competition-report.s.department-justice-and-federal-trade-commission/p040101promotinginnovationandcompetitionrpt0704.pdf.

57. Those producers need to maintain adherence to a common technological standard (lest their products lose interoperability), but changing to another would involve great switching costs.

58. For purposes of this *Legal Memorandum*, "RAND" (the term typically used in the United States) and "FRAND" (the term typically employed outside the United States) are treated as equivalent and interchangeable terms. SSOs' RAND/FRAND requirements do not spell out precisely the meanings of those terms, which must be determined on a case-by-case basis among private parties through negotiations, alternative dispute resolution, or litigation. As of now, there is no universally agreed-to definition of the terms.

59. *See* Complaint at ¶ 20, *In re* Robert Bosch GmbH, Docket No. C-4377, File No. 121-0081, 2012 WL 5944820 (F.T.C. Nov. 21, 2012); Complaint at ¶¶ 25–26, *In re* Motorola Mobility LLC, Docket No. C-4410, File No. 121-0120, 2013 WL 3944149 (F.T.C. July 23, 2013). *See generally* Joshua D. Wright & Douglas H. Ginsburg, *Whither Symmetry? Antitrust Analysis of Intellectual Property Rights at the FTC and DOJ*, 9 Competition Pol'y Int'l __ (Fall 2013) (observing that *Bosch* and *Motorola* "complaints and consent orders, taken together, logically and necessarily depend upon the presumption that protecting a valid SEP against infringement by obtaining injunctive relief is itself anticompetitive").

60. *See* Complaint, *In re* Negotiated Data Solutions LLC, No. C-4234 (F.T.C. Sept. 22, 2008).

61. *See* eBay v. MercExchange, LLC, 547 U.S. 388, 391 (2006).

effort to renegotiate is really just a hold-up attempt).[62] Given that patent and contract law can prevent anti-competitive hold-up from SEP holders' injunction actions and attempted license renegotiations, invoking antitrust adds little, if any, social value.

On the other hand, using antitrust here does threaten significant error cost. There are legitimate reasons for an SEP holder that had previously made an F/RAND SSO commitment to engage in each of the "suspect" behaviors here. The SEP holder might appropriately seek injunctive relief rather than monetary damages against an infringer that was judgment-proof or had consistently and in bad faith rejected offered licenses in an attempt to gain bargaining leverage by forcing costly litigation. Or the SEP holder might legitimately try to renegotiate the case-specific meaning of F/RAND licensing terms in light of some market shift or other occurrence. Because SEP holders' injunctive actions and attempts to renegotiate licenses are sometimes socially beneficial, the law should take care not to overdeter them.

For that reason, it makes little sense to invoke antitrust here. As explained above, successful antitrust actions result in treble damages to account for the fact that much antitrust misconduct (*e.g.*, price-fixing) occurs in secret and is thus not successfully prosecuted; optimal deterrence requires a damages multiplier. For antitrust violations that do not occur in secret, however, the multiplier tends to create overdeterrence. That is the outcome here: Injunction actions and license renegotiations by SEP holders occur in the open, so applying a damages multiplier to account for the (nonexistent) difficulty of detection will overdeter.[63]

In sum, using antitrust to police hold-up stemming from injunctive actions or renegotiation efforts by SEP holders provides little marginal benefit (given that patent and contract law already police bad behavior here) while imposing significant marginal cost (given the likely overdeterrence resulting from potential antitrust liability). Respect for the limits of antitrust would call for the enforcement agencies to stay their hand in this context.

Merger Policy. The antitrust laws forbid business mergers that substantially lessen competition in a market.[64] To implement that prohibition, the FTC and DOJ review proposed mergers to assess their competitive effects. When an agency determines that a proposed merger is likely to lessen competition in a market, the agency may sue to enjoin the merger or may negotiate concessions (divestitures of certain business lines, etc.) designed to maintain competition. Two recent changes in the enforcement agencies' merger review practices—reliance on the "gross" upward pricing pressure index (GUPPI) and embrace of conduct vs. structural remedies—suggest a lack of respect for the limits of antitrust.

Reliance on the GUPPI. The agencies have recently endorsed a difficult-to-administer, untested, and overly sensitive metric for identifying likely anticompetitive harm from "horizontal" mergers (*i.e.*, mergers of competitors). Traditionally, the agencies assessed the likely competitive effects of planned mergers by first defining the market in which the merging parties participate and then evaluating a number of factors—the concentration of the market (*i.e.*, the number of significant competitors), the ease with which new competitors could enter the market, the efficiencies the merger would create—to predict whether the merger would reduce overall market output.[65]

In revised Horizontal Merger Guidelines promulgated in 2010, the agencies explained that they may now determine that a merger is likely to be anticompetitive without first defining the market and considering how other firms would respond to the merger. Instead, a horizontal merger may be condemned solely on the basis that the merger is likely to create "upward pricing pressure" on some product sold by the merged firm. The notion is that mergers that

62. *See* Restatement (Second) of Contracts §§ 89 ("Modification of Executory Contract"), 175 ("When Duress by Threat Makes a Contract Voidable") and 176 ("When a Threat Is Improper"); Uniform Commercial Code § 2-209 ("Modification, Rescission and Waiver").

63. Overdeterrence is a concern even if the antitrust action is brought under Section 5 of the FTC Act, which cannot be privately enforced by plaintiffs seeking treble damages. A successful Section 5 action may give rise to copycat private actions under Sections 1 or 2 of the Sherman Act or under privately enforceable state antitrust laws (including so-called little FTC Acts, many of which may be enforced in private actions). *See* Bruce H. Kobayashi & Joshua D. Wright, *The Limits of Antitrust and Patent Holdup: A Reply to Cary et al.*, 78 Antitrust L. J. 505, n. 15 (2012).

64. *See* 15 U.S.C. § 18.

65. *See* U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines (1997).

unite closely competing brands of a product allow a firm that now controls the close substitutes to raise prices.[66]

Section 6 of the 2010 Horizontal Merger Guidelines calls for upward pricing pressure to be assessed without considering, at least initially, the degree to which the merger may create efficiencies that *reduce* the merged firm's prices.[67] The guidelines thus contemplate the use of a "gross" upward pricing pressure index (GUPPI).[68] The GUPPI seeks to determine the likelihood, absent countervailing efficiencies, that the merged firm would seek to enhance its profits by raising the price of one of its competing products, knowing that some of the lost sales on that product will be diverted to the other.

Unfortunately, the GUPPI requires knowledge of complex economic data that are very hard to calculate in the real world.[69] Given the difficulty of figuring the GUPPI, mistakes are inevitable.

The agencies' embrace of the GUPPI is also troubling because the metric has not been empirically verified as a means of identifying anticompetitive mergers. As economist Dennis Carlton has observed, "[U]se of the UPP as a merger screen is untested.... [T]here has been no empirical analysis that has been performed to validate its predictive value in assessing the competitive effects of mergers."[70] This dearth of empirical evidence seems particularly troubling in that predicting the effects of mergers is no easy task.[71]

A third reason to be concerned about the agencies' reliance on the GUPPI is that the index excludes a key consideration influencing the likelihood of adverse unilateral effects: cost efficiencies stemming from the merger.[72] Any upward pricing pressure resulting from the incentive of a merged firm to divert sales from one product to a higher-margin substitute should be balanced against merger-induced cost savings that would put *downward* pricing pressure on one or more of the merged company's products. The 2010 guidelines, however, do not include an efficiencies credit in the initial calculation of upward pricing pressure. They instead relegate consideration of merger-induced efficiencies to a later analytical step under the standard efficiencies defense.[73]

In the end, the agencies' reliance on the difficult-to-administer, empirically unverified, and inherently biased GUPPI is likely to generate many false condemnations of mergers that are, on the whole, beneficial.[74]

66. *See* U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines 7, 20–22 (2010). The theory of upward pricing pressure is straightforward. Suppose five firms sell competing products (A–E) that, while largely substitutable, are differentiated by brand. Given the brand differentiation, some of the products are closer substitutes than others. If the closest substitute to Product A is Product B and vice-versa, then a merger between Producer A and Producer B may result in higher prices even if the remaining producers (C, D, and E) neither raise their prices nor reduce their output. The merged firm will know that if it raises the price of Product A, most of its lost A sales will be diverted to Product B, which that firm also produces. Similarly, sales diverted from Product B will largely flow to Product A. Thus, the merged company, seeking to maximize its profits, may face pressure to raise the prices of Products A and/or B.

67. *Id*. at 20–22.

68. *See* Steven C. Salop, Serge Moresi, & John R. Woodbury, *Scoring Unilateral Effects with the GUPPI: The Approach of the New Horizontal Merger Guidelines*, CRA Competition Memo (Aug. 31, 2010), at 2.

69. To assess the GUPPI on Product A in light of a planned merger with the producer of Product B, enforcers would need to know the "own-price elasticity of demand" for Product A (*i.e.*, the degree to which consumers will cut back on A purchases in response to a price increase); the "cross-price elasticity of demand" between Products A and B (*i.e.*, the degree to which a price increase on A will lead consumers to switch to B); and the profit margin on Product B (*i.e.*, the difference between the price and marginal cost of B).

70. Dennis W. Carlton, *Revising the Horizontal Merger Guidelines*, 10 J. Competition L. & Econ. 1, 24 (2010).

71. *See, e.g.*, Craig Peters, *Evaluating the Performance of Merger Simulation: Evidence from the U.S. Airline Industry*, 49 J. L. & Econ. 627 (2006).

72. *See* James A. Keyte & Kenneth B. Schwartz, *"Tally-Ho!": UPP and the 2010 Horizontal Merger Guidelines*, 77 Antitrust L. J. 587, 629–30, 648–49 (2011).

73. 2010 Merger Guidelines, *supra* note 66, at 29–32. The merging partners must prove the likelihood and magnitude of each claimed efficiency, how and when it would be achieved, and how it would enhance the firm's ability and incentive to compete. These are extremely onerous conditions and more difficult to show than the likelihood of a GUPPI. Thus, the enforcement agencies in effect put a finger on the scale in favor of a finding of anticompetitive harm. The agencies instead should integrate the efficiencies inquiry into an analysis of a potential GUPPI in order to provide a more appropriate balanced assessment of a proposed merger's competitive effects.

74. According to veteran antitrust enforcers Joseph Simons and Malcolm Coate, the 2010 Merger Guidelines' upward pricing pressure screen "identifies as potentially problematic far more mergers than would be challenged or even investigated under the enforcement standards that have existed for more than twenty years." Joseph J. Simons and Malcolm B. Coate, *Upward Pressure on Price Analysis: Issues and Implications for Merger Policy*, 6 Eur. Competition J. 377, 389 (2010).

Conduct vs. Structural Remedies in Merger Review. Traditionally, when an enforcement agency concluded that a merger was likely to lessen competition, it imposed a "structural" remedy: either an order that the merger not proceed or a command that the parties divest some portion of the businesses to be merged. Enforcement of such a remedy was a simple matter; enforcers merely had to ensure that the parties did a single, discrete thing (*i.e.*, cancel their merger plans altogether or first sell off some line of business). In recent years, though, the agencies have taken to approving mergers on the condition that the parties follow some set of detailed conduct rules.

The agencies' embrace of a regulatory approach to merger remedies is most evident in DOJ's 2011 Antitrust Division Policy Guide to Merger Remedies.[75] That document replaced DOJ's 2004 Remedies Guide, which proclaimed that "[s]tructural remedies are preferred to conduct remedies in merger cases because they are relatively clean and certain, and generally avoid costly government entanglement in the market."[76] The 2011 Remedies Guide eliminated (1) that statement, (2) a discussion of the limitations of conduct remedies, and (3) an assertion that behavioral remedies would be appropriate only in limited circumstances. It instead staked out a neutral position, stating that "[i]n certain factual circumstances, structural relief may be the best choice to preserve competition. In a different set of circumstances, behavioral relief may be the best choice."[77]

Not surprisingly in light of the altered guidance, several of DOJ's recent merger challenges have resulted in settlements involving detailed and significant regulation of the merged firm's conduct. The settlements have featured mandatory licensing requirements, price regulation, compulsory arbitration of pricing disputes with recipients of mandated licenses, obligations to continue to develop and support certain products, establishment of informational firewalls between divisions of the merged companies, prohibitions on price and service discrimination among customers, and various reporting requirements.[78]

How this move toward regulatory merger remedies comports with a limits-of-antitrust perspective is somewhat unclear. On the one hand, if imposition of conduct remedies liberates procompetitive mergers that otherwise would have been barred outright, the trend toward greater use of such remedies may reduce overall error costs. By offering enforcers a less restrictive regulatory option—some middle ground between permitting the merger unconditionally and banning it or ordering divestment—conduct remedies could facilitate mergers that provide net benefits to consumers but raise concerns that cannot be addressed through divestiture. It appears, though, that conduct remedies are being used not to liberate otherwise banned mergers but to increase regulation of mergers that otherwise would have been approved unconditionally.

That is troubling, for conduct remedies present at least four difficulties from a limits-of-antitrust perspective.

- First and foremost, they are costly and hard to implement. They divert enforcers' attention away from ferreting out anticompetitive conduct elsewhere in the economy and require managers of regulated firms to focus on appeasing regulators rather than on meeting their customers' desires.

- Second, they may thwart procompetitive conduct by the regulated firm. When it comes to regulating how a firm interacts with its customers and rivals, it is extremely difficult to craft rules that will ban the bad without also precluding the good. For example, requiring a merged firm to charge all customers the same price (a commonly imposed conduct remedy) may make it hard for the firm to serve clients who impose higher costs.

75. U.S. Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies (June 2011).

76. U.S. Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies §III.A (October 2004).

77. 2011 Remedies Guide, *supra* note 75, at 4.

78. *See*, *e.g.*, Final Judgment, United States v. Ticketmaster Entertainment, Inc. and Live Nation, Inc., No. 1:10-cv-00139 (D.D.C., Jul. 30, 2010); Final Judgment, United States v. Comcast Corp., General Electric, and NBC Universal, Inc., No. 1:11-cv-00106 (D.D.C., Sept. 1, 2011); Final Judgment, United States v. Google, Inc. and ITA, Inc., 1:11-cv-00688 (D.D.C., Oct. 5, 2011).

- Third, conduct remedies tend to grow stale. Because competitive conditions are constantly changing, a conduct remedy that seems sensible when initially crafted may soon turn out to preclude beneficial business behavior.

- Finally, by transforming antitrust enforcers into regulatory agencies, conduct remedies invite wasteful lobbying and, ultimately, destructive agency capture.

In the end, these significant drawbacks likely outweigh any benefits from deterrence of anticompetitive conduct. As William Shughart and Diana Thomas have observed, "supervising compliance has been a backwater for the attorneys and economists employed by the federal antitrust agencies," most of whom "do not want to be involved with ensuring compliance with court orders—job assignments that rarely make headlines."[79] Accordingly, detailed conduct remedies often do not achieve their stated ends while still imposing significant costs. Their increased use seems inconsistent with a limits-of-antitrust approach.

Conclusion

The Roberts Court and the federal enforcement agencies have taken strikingly different stances on the limits of antitrust. The Roberts Court has generally respected them, crafting rules calculated to maximize antitrust's social value in light of its inherent limitations. The agencies, by contrast, seem skeptical of the very existence of antitrust's limits.

What is the reason for this divergence? An obvious explanation turns on the institutional features of federal courts versus agencies. Generalist judges, who regularly confront cases across the legal spectrum, know the limits of their expertise and, in light of their life tenure and limited opportunities for advancement, have no obvious need to expand their turf. Agency staff, by contrast, are constantly reminded of—and rewarded for—their specialized expertise, and they tend to gain both prestige and financial rewards as their authority expands. Their natural tendency is to expand the law's reach.

Regardless of the cause of the diverging stances on the limits of antitrust, a couple of things are clear. First, recent enforcement agency policies are in severe tension with the philosophy that informs Supreme Court antitrust jurisprudence. Second, if the agencies do not reverse course, acknowledge antitrust's limits, and seek to optimize the law in light of those limits, consumers and the competitive process will suffer. Let us hope that antitrust agency leaders heed this reality and adjust their enforcement policies accordingly.

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79. William F. Shughart II & Diana W. Thomas, *Antitrust Enforcement in the Obama Administration's First Term: A Regulatory Approach*, Cato Inst. Pol'y Analysis No. 739 (Oct. 22, 2013), 13–14.