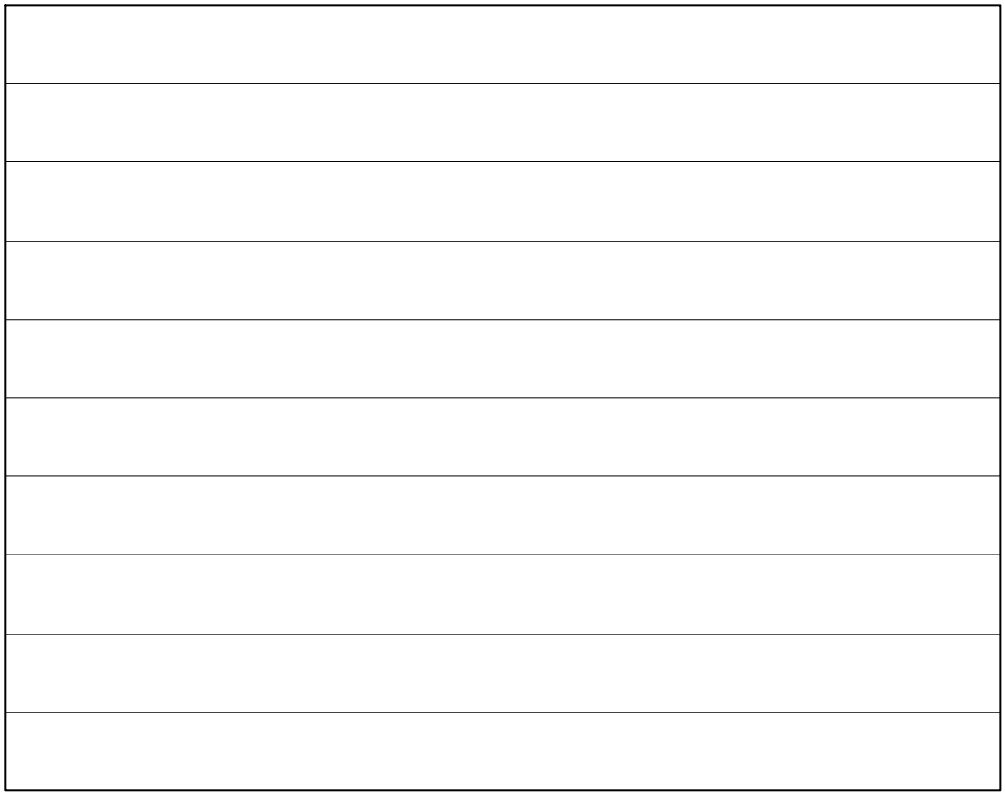
THEORY AND PRACTICE OF COMPETITION ADVOCACY AT THE FTC

The economic theory of regulation ("ETR") posits that because of relatively high organizational and transaction costs, consumers will be disadvantaged relative to businesses in securing favorable regulation.[4] This situation tends to result in regulations — such as unauthorized practice of law rules or per se pr

I. HISTORY OF MODERN COMPETITION ADVOCACY AT THE FTC

The use of the advocacy program has varied over time. Although imperfect, the number of annual advocacy filings (shown in Figure 1) provides a rough proxy for the vigor of the advocacy program over the past two decades. [5]

Figure 1
FTC Advocacy Filings 1980-2004



From 1980 to 2004, the 25 years for which reasonably comparable data exist, the FTC issued about 708 comments, an average of 28 per year. As readily seen in Figure 1, however, this average masks substantial swings in the Commission's use of advocacy over the years. The advocacy program has focused on competition, consumer protection, and regulatory fronts over the years, changing some with the public policy issues of the day. Several topic areas remained active over fairly long periods of time.[6] Certain other narrow topic areas generated significant advocacy action for only a year or so.[7]

A. COMPETITION ADVOCACY FROM 1974 TO 2004

One can argue that the advocacy program (known internally as the "intervention" program in the 1970s and 1980s) dates back to the earliest days of the Commission, when the FTC submitted comments to the Fuel Administration (on coal pricing) and the War Industries Board (on steel). If we do not want to ascribe the origins of a program to distant and idiosyncratic events, a more representative date for the beginning of the program, and certainly for the program's "modern era", would be October 7, 1974 when Chairman Louis Engman spoke about the broader use of antitrust policy as an alternative to the regulation of markets. In referring to the nation's macroeconomic problems — in 1974 the U.S. economy was suffering

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[6] These hardy perennials and the years when they were most active included: restraints on international trade (1975-1990), restraints on health care advertising and commercial practices (1978-1994), horizontal restraints and erection of entry barriers via legislation (1980-2003), regulation issues in airline, rail, and truck transportation (1980-1993), comments regarding regulatory reform in telecommunications, broadcasting, and cable TV (1983-1995), regulation of food claims in advertising and labeling (1987-1993, 2000, 2003), and, most recently, restructuring of the electricity generation, transmission, and distribution industry (1995-2003). Several filings concerning various postal regulation issues appeared between 1981 and 1989.

[7] For example, in 1993, and later in 2004, there were many comments about "any willing provider" laws, as pharmacy groups and others were lobbying state legislatures for protection against the anticipated effects of health care reforms. Most of these health care-related comments have been requested by and issued to state and local legislatures and other government bodies. In 1987, the FTC staff filed over a dozen comments with states regarding potentially anticompetitive aspects of attorney ethics codes.

placing coordination of the program in the Bureau of Consumer Protection.[14] The program under Miller also included a new-found emphasis on state level activity, in addition to the federal level activity that had previously been the mainstay of the program.[15] The program was further bolstered by complementary Bureau of Economics research on restraints involving transportation, telecommunications, healthcare, licensure, and international trade.[16]

As Figure 1 indicates, at least in numbers of filings, the program grew significantly from 1982 through 1987, when the program reached its apex with 90 comments.[17] The number of filings increased during this period for a least three reasons: (1) there was a greater emphasis on the program generally, and thus more opportunities were pursued; (2) there was an increase in the already broad range of the issues covered (e.g., postal practices and taxicab regulation); and (3) there were certain policy issues that were playing out in many states simultaneously, resulting in a large number of advocacy opportunities on a single issue (e.g., attorney ethics codes, professional advertising, gasoline marketing, retail dealer protections, optometry retailing, etc.).

The annual number of annual filings from 1990 to 2001 fell markedly compared to the 1980s. As part of the winding down, various categories of filings were avoided altogether; comments to the Postal Service and most comments on international trade issues ended in 1990,

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[14] *See* MCCHESNEY ET AL., *supra* note 3; Robert D. Tollison, *Antitrust in the Reagan Administration: A Report from the Belly of the Beast*, 1 INTERNATIONAL JOURNAL OF INDUSTRIAL ORGANIZATION, 211, 217-218 (1983). The program was to be based on longer term empirical research that would be the foundation for multiple comments, and procedures were set up to allow a one-week turnaround for comments.

[15] The ratio of state to federal filings rose steadily from 1982 to a peak in 1988, when state filings outnumbered federal filings by 4 to 1. Thereafter, except for the outlier year of 1993, relative state level activity fell to a level roughly equal to federal activity.

[16] Such filings were a staple of the 1970s and 1980s advocacy program with about 51 individual filings (in dozens of product categories) from 1982 to 1989. *See* Figure 1.

[17] From 1983-1989, 56 comments were filed in an average year.

virtually none were supported by empirical work because by that time the agency did little research on regulatory issues.[21]

With Timothy Muris as Chair (June 2001 – August 2004) came a renewed emphasis on the FTC's advocacy program. There were 21 filings in 2002, a level that has risen slightly since. Further, the program sought to expand beyond electricity into areas that were familiar ground in the 1980s — restraints on entry in local markets and governmental restrictions on competition. Although the general regulatory research that had been used to support the program in the 1980s was no longer an ongoing project, the comment topics became more diverse, including, for example, comments on the retail marketing of gasoline, wine distribution, licensure, and the unauthorized practice of law.

B. Explaining Variation in the Volume of Advocacy Comments

1. *Political and Economic Developments*

Developments exogenous to decisions made within the Commission may explain some of the changing fortunes of the advocacy program over time. In the late 1970s and 1980, regulation of several inherently competitive industries, such as certain transportation markets, were obvious targets for advocacy efforts. By the mid-1990s, however, most of those de-regulation targets were gone, as regulation of transportation, certain utilities, and telecommunications had been altered significantly or eliminated. Thus, there may have been somewhat less need for an advocate for rational analysis of federal regulatory and competition issues than there was in the 1970s and 1980s.

[21] The electricity comments were not based on research done at the FTC. Substantive empirical work on those issues is done by the state regulators, private parties, and academics. The FTC did, however, hold a conference on electricity regulation in Summer 1997 and compiled a report on state retail electricity regulation in 2001. The large number of state-specific electricity filings in 1998 (17 filings) accounted for the bump-up in filings that year.

Other political and legal developments may also generate increases or decreases in advocacy activity. In recent years, a series of important decisions regarding commercial speech and product health claims has generated an overhaul of the FDA's regulation of these claims.[22] Given the FTC's expertise in this subject area, the FTC has filed a series of comments on topics

Internet casket sales,[27] contact lenses,[28] and other industries, renewed efforts have been made by entrenched interests to block this new form of competition. In many situations, moreover, the beneficiaries of anticompetitive regulations are in-state merchants, whereas many Internet sellers do a modest amount of business in many states. As a result, in-state merchants have the incentive and influence to lobby effectively for protection, whereas out-of-state sellers lack the

and federal regulators, Chairman Janet Steiger began to de-emphasize the advocacy program in 1989, as Figure 1 clearly shows.[30]

3. Internal Resource Constraints

One additional factor that might explain the lack of more advocacy activity in the late-1990s is the merger wave of that era. Although the advocacy program itself required a relatively small resource commitment, the FTC efforts in dealing with the merger wave may have had an indirect effect on the advocacy program. The need to examine the large number of mergers may have drawn off Bureau of Economics resources from the primary research necessary to generate effective advocacies, as well as taxing the small staffs of the individual Commissioners. Thus, there are various chokepoints in the advocacy production pipeline that can be affected by resource constraints that are not captured simply by noting the relatively small size of the program.

II. THE ECONOMIC THEORY OF REGULATION

Although regulation sometimes is needed to correct a market failure, it also can be used to restrict competition in order to transfer wealth from consumers to a favored industry. It has long been recognized that because of industry's superior efficiency in political organization relative to consumers, consumer interests often are subservient to industry interests in the regulatory process.[31] Beginning with the seminal work of Stigler (and later more formally

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advocacy across the agency). As of 2002, the total agency workyears devoted to advocacy might have been closer

developed by Peltzman and Becker), however, the notion that regulation is produced in a black box to maximize social welfare has given way to what has become known as the economic theory of regulation (ETR).[32] The foundation of ETR is that politicians and constituents are

political arena [than the marketplace] because information must be sought on so many issues of little or no direct concern to the individual, and accordingly he will know little about most matters before the legislature."[36] Holding constant the size of a wealth transfer, the larger the interest group size, the smaller the per capita benefit; as per capita benefits diminish, the less likely it is that informing one's self on the impact of a regulation makes economic sense.

Second, once individuals recognize their interest in the outcome of the regulatory process, they must organize to translate their demand for policy into political pressure. Because the benefits from acquiring a desired regulatory outcome is a public good for members of an interest group, however, each member has an incentive to shirk his obligation to the group and free-ride of the contributions of others.

The important implication of this insight is that policies that reduce the welfare of a majority for the benefit of a minority are within the set of feasible outcomes.[37] Indeed, one readily can see how consumer interests give way to the interests of a small industry in the regulatory process. Beyond a certain point, per capita benefits from a preferred regulatory outcome are diluted such that it becomes irrational to take part in the political process. A practical consequence of this is that small groups with similar interests — like members of a particular industry — can organize political support more effectively than large diffuse groups — like consumers generally. Thus, the equilibrium outcome of the political process is likely to be regulation that harms consumers by protecting a favored industry from competition.

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[36] Stigler, *supra* note 32, at 11.

[37] *See* Peltzman, *supra* note 31, at 213 ("In consequence the numerically large, diffuse interest group is unlikely to be an effective bidder, and a policy inimical to the interest of a numerical majority will not be automatically rejected.").

Take the example of unauthorized practice of law ("UPL") rules, which prohibit anyone other than a licensed attorney from performing those tasks that courts, bar associations, and/or legislatures have deemed to be the practice of law. By protecting attorneys from having to

this political market failure.[39] Indeed, because anticompetitive regulation that results from a political market failure can have just as pernicious effects on consumer welfare as private conduct that harms competition, there does not appear to be a reasoned justification for the FTC to police the former but not attempt to ameliorate consumer harm from the latter.[40]

By representing consumer interests in the political process, the FTC is able to affect political outcomes through three, non-mutually exclusive channels. First, to the extent that a comment informs the public of the way a proposed regulation is likely to affect them, it can spur political action, and thus increase the political costs associated with supporting anticompetitive regulation. In this manner, competition advocacy can move the political equilibrium towards one that is more favorable to competition. Similarly, an FTC comment can provide "political cover" for politicians to take a position against favored industry; regardless of whether an FTC comment increases the political cost to supporting anticompetitive regulations, a politician can claim that it has as an excuse for not supporting a favored industry. Finally, a comment simply

regulation restricts competition more than is necessary to promote some consumer protection goal, and therefore is not in the public interest.[41]

ETR also can help to explain why it is uniquely appropriate to have a federal agency tasked with carrying out the advocacy function. As noted by James Madison in Federalist 10, state and local governments are often the most prone to the sort of factions and interest-group activity that generates anticompetitive regulation. Thus, a particular interest group may be especially concentrated or strong in a particular state, and that group may have undue influence in the political process of that state. In addition, the anticompetitive regulations of one state may have major spillovers, or other externalities, that impose burdens on national markets.[42] As a result, it is appropriate for the advocacy function to rest with a national actor that will be less prone to capture by parochial interest groups, but instead will be attenuated from some local political pressures and will be able to look out for the national goals of preserving robust economic market competition. In addition, the FTC's status as a bipartisan independent agency may also increase its effectiveness on advocacy issues. Because critics often will characterize FTC interventions as "taking sides," the Commission's status as a bipartisan expert agency may insulate it from some of the attacks that might otherwise be leveled at its advocacy activities.[43]

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[41] As discussed *infra*

Despite these justifications for an advocacy program, there are some inherent limits on the benefits that advocacy can provide. For example, although advocacy provides regulators with information concerning the likely economic consequences of a policy choice, the FTC is not a constituent. FTC opposition to a protectionist piece of legislation, therefore, is not the same as constituent opposition because the FTC cannot provide political support in the form of votes or campaign contributions. In addition, FTC advocacy only can inform the debate and suggest appropriate action; it cannot compel that action.

Another important consideration is that the FTC is itself a regulatory body and may be subject to political pressure from interest groups in much the same manner as federal or state agencies or legislatures. As Timothy Muris, who has served as chairman and bureau director, has observed, "Congress can, and often does, exert considerable influence over an agency such as the FTC."[44] Indeed, some studies have found a relationship between the preferences of congressional oversight members' constituencies and FTC policy.[45] And due to constituent complaints, in the late 1980s, moreover, Congress attempted to cripple, if not totally eliminate

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governments. This criticism, however, is fundamentally misplaced, as the Commission has followed a general long-standing policy of pursuing advocacy filings with state officials only where

the advocacy program.[46] That the FTC is an independent and bipartisan agency, however, is likely to limit the ability of an industry to capture it. Almost uniformly, the Commission gives unanimous approval for comments. Because one industry would be unlikely to effectively capture all Commissioners, the views put forth in advocacy comments are highly unlikely to have resulted from interest group pressure. Further, the FTC deals with a wide range of industries, making it less likely than agencies that serve only one or a few industries to be subject to capture by any single interest group.

IV. ASSESSMENT OF THE COMPETITION ADVOCACY PROGRAM

One of the FTC's core goals is to prevent anticompetitive business practices. Competition advocacy furthers this goal by attempting to prevent government action that restricts competition. Important to determining the cost-effectiveness of the advocacy program is examining its efficiency in preventing anticompetitive regulations versus that of FTC enforcement.

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FDA,[53] and CFTC[54] all appear to have positively affected regulatory outcomes. At the same time, the track record with state regulators appears less successful. For example, although the FTC's efforts to allow entry into taxicab services in the latter 1980s achieved certain successes, for the most part, cities chose not to listen to the FTC's advice that free entry in conjunction with fare competition would likely provide a better outcome for consumers. These observations are consistent with ETR, which predicts that regulators who are insulated from direct political influence are more likely to act independently based on policy considerations rather than

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automobile fuel efficiency standard on analyses provided by FTC staff. *See* Comments from the FTC Staff to the

constituent interests.[55] This insight offers an explanation as to why comments may have more effect before non-elected federal regulators rather than elected state legislators.

Second, in situations where one industry (or a subgroup within an industry) is attempting to secure regulation that would hinder competition by favoring it at the expense of a rival industry (or group), competition advocacy is likely to be more successful. This prediction follows from ETR because comments supporting a position taken by another industry rather than only consumers are more likely to be successful given industry's superior political organization ability. Casual empiricism provides some support for this hypothesis.[56] For example, recent FTC comments opposing legislation that would have regulated PBMs' contractual relationships with health plans and pharmacies have appeared to have had an impact.[57] PBMs and major health plans, which have powerful lobbies, opposed such legislation as well.[58] Comments and

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55 *See e.g.*, Kalt & Zupan, *supra* note 41; Thomas H. Hammond & Jack H. Knott, *Who Controls the Bureaucracy?: Presidential Power, Congressional Dominance, Legal Constraints, and Bureaucratic Autonomy in a Model of Multi-Institutional Policy Making*, 12 J.L. ECON. & ORG. 119 (1996); Thomas H. Hammond & Gary J. Miller, *The Core of the Constitution*, 81 AM. POL. SCI. REV. 1155 (1987).

56 This may be the case because organized industry groups are able to publicize FTC comments to achieve maximum effect. It may also be because an industry group is more likely than consumers to mount successful opposition to a regulation regardless of FTC intervention.

57 *See* Letter from Maureen K. Ohlhausen, Director of the Office of Policy Planning, Federal Trade Commission, et al. to North Dakota Senator Richard L. Brown (March 9, 2005), *at* http://www.ftc.gov/os/2005/03/050311northdakotacomnts.pdf; Letter from Susan Creighton, Director of the Bureau of Competition, Federal Trade Commission, et al. to Greg Aghazarian, Assemblyman of California (Sept. 7, 2004) (hereinafter "California Letter"), *at* http://www.ftc.gov/be/V040027.pdf. Letter from Susan Creighton, Director of the Bureau of Competition, Federal Trade Commission, et al. to Patrick Lynch, Attorney General of Rhode Island (Apr. 8, 2004) (hereinafter "Rhode Island Letter"), *at* http://www.ftc.gov/os/2004/04/ribills.pdf. Governor Schwarzenegger cited an FTC comment explaining how a law that would require would be likely to increase the cost of pharmaceuticals was explicitly cited by in his veto message. *See* Letter from Arnold Schwarzenegger, Governor of California, to Members of California State Assembly (Veto of Assembly Bill 1960) *at* http://www.governor.ca.gov/govsite/pdf/vetoes/AB_1960_veto.pdf.

58 Retail pharmacies and unions were the primary proponents of this legislation. Aetna, Blue Cross of California, the California Association of Health Plans, and Pacificare opposed the bill. *See Pharmacy Benefits Management: Analysis of A.B. 1960 Before the Senate Health and Human Services Committee*, 2003-2004 Sess. (Ca. Jun. 14, 2004), *at* http://www.leginfo.ca.gov/pub/03-04/bill/asm/ab_1951-2000/ab_1960_cfa_20040614_134801_sen_comm.html.

amicus briefs opposing UPL restrictions that would bar non-attorneys from performing certain real estate settlement tasks (*e.g.*, title searching, performing closings) have been relatively successful, perhaps in part because the title company industry is affected directly by these restrictions.[59] The lack of organized opposition to restraints on competition may also offer a partial explanation for the lack of success in taxicab advocacies. Those who might gain from taxi deregulation are unorganized consumers and small, would-be taxi entrepreneurs. The FTC's relative impotence in affecting trade policy, moreover, may be due in part to the fact that trade barriers are the quintessential example of restrictive regulations that provide substantial benefits to specific industries and impose smaller per capita costs widely upon consumers and other industries.

Third, empirical substantiation for a position is important; if a comment can point to careful empirical work demonstrating that the regulation in question is likely to harm consumers, it is likely to be more persuasive. This may be why comments with a substantial empirical component appear to have met with success.[60]

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[59] *See, e.g*, Brief Amici Curiae of the Federal Trade Commission and the United States of America, McMahon v. Advanced Title Serv. Co. of West Virginia, 607 S.E.2d 519 (W. Va. 2004) (No. 31706), *at* http://www.ftc.gov/be/V040017.pdf; Letter from Federal Trade Commission & Department of Justice to John B. Harwood, Speaker of the House of Representatives of Rhode Island, et al. (Mar. 29, 2002), *at* http://www.ftc.gov/be/v020013.pdf; Letter from the Federal Trade Commission & the Department of Justice to North Carolina State Bar Ethics Committee (Dec. 14, 2001), *at* http://www.ftc.gov/be/V020006.htm. Efforts to persuade the Georgia Supreme Court not to adopt a rule that would bar non-attorneys from providing real estate settlement services, however, were unsuccessful. *See* Brief Amici Curiae of the United States of America and the Federal Trade Commission, On Review of UPL Advisory Op. 2003-02, 588 S.E.2d 741 (Ga. 2003) (No. S03U1451), *at* http://www.ftc.gov/os/2003/07/georgiabrief.pdf; Letter from Federal Trade Commission & Department of Justice to State Bar of Georgia (Mar. 20, 2003), *at* http://www.ftc.gov/be/v030007.htm.

[60] Comments containing original empirical research on specific regulatory issues were filed with many agencies including the FCC, the DOT, and the FDA. These filings tended to be the most convincing work of the program, because the empirical work made the filings more valuable and more credible than they might otherwise be. *See, e.g.*, Comment on the Federal Communications Commission's AM/FM Radio and Television Ownership Rules, (July 15, 1987); Comment on Boston's Airport Authority Program for Airport Capacity Efficiency (Feb. 29, 1988); Comment on the FCC's Rules Concerning FM Translator stations, MM Docket 88-140 (Jan. 23, 1989); Comments

Finally, comments involving consumer protection appear to be more successful. The Commission's dual expertise in competition and consumer protection will often enable it to speak with great force and credibility on those issues.[61] In these areas, the FTC's input can be especially valuable in debunking consumer protection rationales for anticompetitive regulations. Notably, in most debates on trade restraints, competition and consumer welfare play little or no role.[62]

Of these factors, organized political opposition to an anticompetitive regulation may the most important. For example, in trade policy, although the FTC staff undertook extensive investigations of trade restraints issues from the mid-1970s through the early 1990s, with many of the filings containing new empirical and conceptual work, two decades of work did not

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on FCC's financial interest and syndication rule which restricted ownership of the rights to re-run TV shows (3

observably alter policy or individual decisions.[63] Alternatively, FTC advocacy against laws that prohibit retailers from selling gasoline at prices below a defined measure of cost have met with a modest degree of success despite the concentrated parochial support that these laws enjoy from local gas station owners.[64] Although there is no local industry that is organized to resist sales-below cost regulations, these regulations primarily are targeted at warehouse stores like Costco and Sam's Club, which are able to effect local political opposition.

B. EFFICIENCY OF COMPETITION ADVOCACY VERSUS ENFORCEMENT

Although it is difficult to measure with any precision the impact of advocacy comments on regulatory outcomes, it is almost certainly the case that competition advocacy is a more cost-effective means than enforcement to attack state-imposed barriers to competition. The *Noerr-Pennington* doctrine immunizes certain attempts to lobby government for even anticompetitive regulation were immune from antitrust challenge,[65] and the State Action doctrine shields certain

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[63] There were many filings with the International Trade Commission from 1975 to 1982; *see* MCCHESNEY ET AL., *supra* note 3, at 38-42, A27-A28. *See, for example*, D. Tarr, Prehearing Brief of the Federal Trade Commission before the International Trade Commission on Stainless Steel and Alloy Tool Steel (Mar. 27, 1987) (No. TA-203-16). This was one of a long line of advocacy filings focusing on international trade restraints on products ranging from softwood lumber to DRAM computer chips. Almost all empirical FTC staff analyses of trade restraints found that the benefits obtained from trade restraints (in terms of jobs "saved", if indeed any jobs were saved in long-run equilibrium) were overwhelmed by the costs to consumers. But those benefits were very specific to the workers and industries, and the costs were widely dispersed, so trade restraints remain popular despite their negative net impact.

[64] For successes in opposing below-cost -sales laws *see, e.g.*, Letter from Susan A. Creighton, Director, Bureau of Competition, et al. to Michigan State Representative Gene DeRossett (June 18, 2004), *at* http://www.ftc.gov/os/2004/06/040618staffcommentsmichiganpetrol.pdf; Letter from Susan A. Creighton, Director, Bureau of Competition, et al. to Kansas State Senator Les Donovan (Mar. 12, 2004), *at* http://www.ftc.gov/be/v040009.pdf; Letter from Joseph A. Simons, Director, Bureau of Competition, Federal Trade Commission, et al. to Daniel G. Clodfelter, North Carolina State Senator (May 19, 2003), at http://www.ftc.gov/os/2003/05/ncclsenatorclodfelter.pdf

anticompetitive conduct from federal antitrust scrutiny when the conduct is (1) in furtherance of a clearly articulated state policy, and (2) actively supervised by the state.[66] Thus, FTC enforcement may be unable to reach some anticompetitive regulations, leaving advocacy as the only tool available to prevent consumer harm.

Even for cases where a court finds immunities not to apply, the high costs and inherent uncertainty of litigation and the extremely small amount of resources needed for advocacy suggest that advocacy is a more efficient vehicle than enforcement to attack state restrictions on competition. Further, by preventing or ameliorating anticompetitive restraints *before* they are

consumers face a higher cost/benefit ratio *vis-a-vis* industry in the political arena, they are unlikely to overcome this disadvantage and organize opposition to anticompetitive regulation. Antitrust immunities, moreover, sometimes put anticompetitive regulation beyond the reach of

circumstances, however, a cost-benefit approach may justify the use of advocacy when regulation is likely to impose substantial costs on consumers.