The Bipartisan Legacy

by Thomas B. Leary

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[*] Commissioner, Federal Trade Commission. The thoughts expressed here are my own, and are not necessarily shared by my colleagues.

[1] *See* Industrial Concentration: The New Learning (Harvey J. Goldschmid *et al.*, eds., 1974).

necessary to rehash that great debate here,[2] other than to observe, first, that actual antitrust enforcement practice was never as polarized by party as popular rhetoric suggested and, second, that in recent years even the rhetoric has cooled down as the areas of difference have narrowed dramatically.[3]

We play the antitrust game between the 40-yard lines today. The AAI still has an unabashedly pro-enforcement agenda, but the AAI does not emphasize the political and social content of antitrust. It does not argue that efficiency is bad. In fact, my experience in a bipartisan agency like the FTC - - as both a minority and a majority member - - is that no one,

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[2] For an extended discussion, *see*, *e.g.*, William Kovacic, The Modern Evolution of U.S. Competition Policy Enforcement Norms, Keynote Remarks at the Antitrust Practice Group Retreat sponsored by Washington, D.C. law firm Howrey, Simon, Arnold & White, Chantilly, Virginia, May 2, 2003, *available at* <http://www.ftc.gov/speeches/kovacic/htm>.

[3] *See* Thomas B. Leary, The Essential Stability of Merger Policy in the United States, 70 Antitrust L. J. 105 (2002).

[4] For example, Robert Pitofsky, who had been critical of enforcement policies during the 1980s, agrees that there has been a bipartisan consensus for the past fifteen years. *See* Robert Pitofsky, Past, Present, and Future of Antitrust Enforcement at the Federal Trade Commission, 72 U. Chi. L. Rev. 209 (2005).

[5] Each year, AAI sponsors a workshop on electricity restructuring and antitrust. Other AAI workshops have focused on defense procurement, retail category management, network access and e-commerce supplier joint ventures. *See* <http://www.antitrustinstitute.org>.

[6] The words have stuck, but I cannot remember the time or place.

[7] *See* Letter from Oliver Cromwell to the Genera

case, there is evidence of what has happened in the marketplace to date, but it is still necessary to weigh this outcome against a prediction of what is likely to have happened if the challenged conduct had not occurred.

The chief tools for these predictions are objective historical experiences, the opinions of people in the industry, other experts from the outside, and calculations based on various economic models. Of course, the past does not necessarily portend the future, inside and outside experts are often mistaken,[9] and economic models depend on initial assumptions that may or may not reflect reality. These uncertainties affect even predictions of the near term (a so-called "static analysis") but, obviously, things get progressively more difficult as you look further and further ahead.

In order to make the standards for antitrust liability predictable in an inherently unpredictable world, we rely on rules of thumb or presumptions of varied strengths. Price-fixing or market allocation is conclusively presumed to be illegal; internal capacity growth or expansion into new markets is conclusively presumed to be legal. On the other hand, the once conclusive presumptions against tying arrangements or group "boycotts" are now weaker, and presumptions based solely on market shares have become weaker still. Conversely, the common

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[9] We tend to give particular weight to so-called "hot documents" from company files that predict anticompetitive consequences because they appear to be statements against interest, but they might not have been against interest at the time they were made.

assumptions that supra-competitive prices will promptly be disciplined by entry, or that predation is rarely successful, have been weakened.[10]

Obviously, ongoing research and debate could further modify these various presumptions, or perhaps suggest other ones. I do not know whether more aggressive or less aggressive antitrust policies will emerge. Given the uncertainties of predictions, it has been argued that risks of over-enforcement are most serious because competition will ultimately erode transitory market power gained when a strategy is mistakenly allowed, while the efficiencies lost when a strategy is mistakenly prohibited are gone forever.[11] This rhetoric sounds good but, in my experience, efficiencies are rarely dependent on a single competitive strategy; one-shot efficiencies (like some in a merger) tend to erode; and, in some industries, the existence of market power may impede rather than speed competitive responses. In any event, I do not know how the issue could be resolved empirically.[12] I may be particularly wary of over-enforcement myself, but for a different reason.[13]

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[10] *See* Leary, *supra* n.3 at 115 (on entry); Susan Creighton, Cheap Exclusion, Remarks Before the Charles River Associates 9th Annual Conference on Current Topics in Antitrust Economics and Competition Policy, Washington, DC, February 8, 2005, *available at* <http://www.ftc.gov/speeches>. *See also* discussion of "agency" issues at pp. 7-9 *infra*.

[11] *See* Frank H. Easterbrook, The Limits of Antitrust, 63 Tex. L. R. 1, 3 (1984) ("Judicial errors that tolerate baleful practices are self-correcting while erroneous condemnations are not").

[12] Calculations of consumer benefits from antitrust enforcement are themselves highly speculative; calculations of efficiencies lost when transactions are challenged - - or aborted early on because a challenge is feared - - would seem to be even more speculative.

[13] *See* pp. 14-15 *infra*.

B. The Agency Problem

The fundamental assumption of current antitrust analysis is that a business enterprise is a unitary entity dedicated to the maximization of profit. This means that we assume there must be a rational economic explanation for potentially troublesome conduct like acquisitions, restrictive agreements or aggressive prices. If there are no readily apparent short-term advantages, we assume that there must be subtle long-term strategies in play. These long-term strategies may have effects that are either benign or harmful. For example, we are likely to assume that a manufacturer's restrictions on dealer sales, with immediate adverse effects on volume and profit, must have been designed to motivate dealers to do a better job in the long run. On the other hand, we are also likely to assume that a manufacturer's sales below its own variable cost suggest a design to drive out competition and facilitate price increases later on.

In the real world, things are not so simple. In any enterprise, however large, business decisions ultimately are made by a single individual or a small group. These people have monetary and non-monetary "profit" objectives of their own, which do not necessarily coincide with those of the enterprise as a whole. There are abundant illustrations of situations where the individual incentives of employee agents can prompt conduct that does not maximize the profits of their employer. An understanding among competitors not to solicit business from a rival's best customers can make life much easier for some employees, even though it may sacrifice short-term profits of the enterprise and risk horrendous long-term legal consequences. Participants in a cartel may not "cheat," even if they could get away with it, out of perverse loyalty to the group. A manufacturer's employee, who depends on the goodwill of his dealer customers, may facilitate dealer activities that are not only anti-competitive but flatly contrary to his employer's interests.

Other employees may be overly aggressive. An employee whose compensation depends on sales volume may be tempted to get business below cost, particularly if it will hurt an unusually irritating rival, without any concern about the likelihood of recoupment. In fact, people with a keen competitive instinct seem to derive as much satisfaction from a hated rival's losses as they do from their own company's gains.[14] At a much higher level, a CEO under pressure from the Board, who has run out of good ideas or is simply frustrated by the demands of day-to-day management, may seek the diversion of a spectacular acquisition that is unlikely to benefit shareholders. I have personally seen all of these things; companies are managed by human beings, not robots.

The "agency problem" means that corporate "intent" is an elusive concept and that internal predictions of competitive consequences are apt to be particularly unreliable when they are affected by personal motivations. Practicality may demand that we ignore these individual motivations, for the most part. But, at the same time, it does not make sense to insist always that certain conduct must be efficient or must be predatory, based on what would be rational for the

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[14] Compare the avid Red Sox fans who are particularly elated when the Yankees lose, and vice versa.

entire enterprise. It might even be useful to take another look at the automatic application of vicarious criminal liability, or the enhanced penalties for concealment.

C. Non-Price Competition

When people in the antitrust community talk about competitive effects, they almost always have price effects in mind. An imaginary condition of perfect competition is the ideal against which the real world is measured; markets are viewed as non-competitive to the extent that prices deviate from marginal cost; and "quality" differences are an inconvenient nuisance if they cannot be captured in a measurement of price or cost. Market definition is the initial step for the analysis in most antitrust cases, and markets are defined in the first place by an

[15] U.S. Dep't of Justice and Federal Trade Comm'n, Horizontal Merger Guidelines (Apr. 2, 1992), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,104 at § 1.

[16] Thomas B. Leary, The Significance of Variety in Antitrust Analysis, 68 Antitrust Law Journal 1007 (2001).

[17] *See*

[21] Mergers are in many ways like marriages, and the clash of egos can sink marriages that, objectively, appear to be made in Heaven.

competitive potency of a new entity. In the "merger wave" of the late 1980s (in contrast with the much larger "wave" of the late 1990s), many transactions were so-called "leveraged buyouts," in which a company or group of individuals bought a much larger publicly-held company with funds obtained by pledging the assets of the target company itself. If there were no horizontal overlaps between the buyer(s) and the target, there could be no effect on the number of competitors or the level of concentration. One competitor was substituted for another. In the 1980s, when concentration statistics were strongly emphasized, such a transaction was viewed as competitively benign, even though the surviving entity could be constrained by debt and unable to compete as effectively in its market. We pay less attention to concentration numbers today but the competitive impact of financial strength - - pro or con - - is still not formally recognized in our guidelines. At the same time, this factor is closely scrutinized when the agency is vetting a potential third-party buyer of divested assets. Again, I am not sure why this is different.

These are just illustrations of some perplexing issues we face in antitrust today, even with a common agreement that economic principles should drive our decisions. The basic problem is that economics is not Newtonian physics, but we are nevertheless required to make binary decisions up or down. I cannot get away with a statement that I am 60/40 persuaded a particular transaction will (or will not) have an anticompetitive effect. In theory, the "reason to believe" standard[23] accommodates these feelings of fuzziness but a vote will often be outcome

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[23] Under the FTC Act, the Commission has authority to issue a complaint when it has "reason to believe" that a violation has occurred and that a proceeding would be in the public interest. Sections 5 & 13(b) of the FTC Act, 45 U.S.C. §§ 45 & 53(b); *see, e.g.,* FTC v. Standard Oil Co.,

449 U.S. 232, 241 (1980).

regulators do not have a roving authority to impose their own ideas about optimal economic outcomes.

I would not attempt to justify this opinion by reference to anything specific in legislative history. (You can, in fact, find support for a variety of views in the history of the antitrust laws.) The opinion is rather based on my belief that producer and consumer freedom is what Western civilization is all about, and antitrust law (and consumer protection law) should be applied in a way that respects freedom of choice.[26] My particular preference for freedom may explain why, at the margin, I may be somewhat more concerned about the risks of over-enforcement than the sponsors of this event. When in doubt, I would tend to leave the private sector alone. This may be just a restatement of the government's burden of proof, but I think it is a little more than that. On the other hand, there are other preferences that pull in the opposite direction in some situations.

[26] I also firmly believe that the respect for freedom, unruly as it often is, contributes to innovation and overall economic welfare in the same diffused way that the respect for intellectual property rights does.

[27] *See* David Balto, The Efficiency Defense in Merger Review: Progress or Stagnation,

unlikely because they would not make economic sense for the entire enterprise, I also believe that individually motivated predatory conduct is particularly unlikely to result in antitrust harm.

The pros and cons of collective decision-making really merit a more extensive treatment. It obviously can be inefficient, and that inefficiency may be too high a price to pay when the issues are black and white. When we deal with shades of gray, however, I believe that the process is likely to produce better outcomes. It certainly nudges people toward the center.

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[30] Harold Demsetz, 100 Years of Antitrust, Should We Celebrate?, Brent T. Upson Memorial Lecture, George Mason University School of Law, Law and Economics Center (Sept. 21, 1989)(unpublished speech on file with Thomas B. Leary), italics in original.

[31] *See*, 94.2 196.56 Tm( )Tj/TT4 1 Tf0.cd.gTj/TT2 1 Tf1.319 ., Testimony at FTC Hearings on Global and In

are inconclusive or point in opposing directions, and various default assumptions become important. This process should be familiar to anyone who has had experience with high-level decisions in the business world - - except that we probably have less freedom to “fly by the seat of the pants” than business executives do, because we often are required to defend our decisions responses will continue to be affected by varied value judgements and life experiences. I have not always agreed with the sponsors of this event in the past, and I am sure that we will continue to have differences in the future, but I trust that we can always disagree with mutual respect and goodwill.