Federal Trade Commission

Intel, Apple, Google, Microsoft, and Facebook:
Observations on Antitrust and the High-Tech Sector

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Good afternoon. Over the last few years—and the last year, in particular—the Commission has tackled several challenging and thought-provoking cases in the high-tech sphere. The leading cases that come to mind are the Commission's decisions not to challenge the Google/DoubleClick and Google/AdMob mergers and the Commission's litigation against (and settlement with) Intel. In bringing these cases, the Commission has not been without its critics who say these cases are too high stakes, involve industries that are too fast-moving, and are essentially too difficult for the Commission to handle. It may surprise you to learn that I share some of these concerns; indeed, in the throes of

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The views stated here are my own and do not necessarily reflect the views of the Commission or other Commissioners. I am grateful to my attorney advisor, Amanda Reeves, for her invaluable assistance preparing this paper.

these cases, I have spent hundreds of hours trying to make sure that the Commission gets it right. These concerns will be the subject of my remarks today.

First, I will discuss the arguments against the Commission challenging mergers and conduct in the high-tech sphere. Second, I will discuss some considerations that I believe should inform the Commission's analysis when it does decide to litigate a case in the high-tech sphere.

I.

Over the last year, I have heard the FTC's opponents make six arguments as to why the agency should, as a general matter, stay out of cases involving high-tech industries.

The first argument is that market definition in these cases – a necessary prerequisite to any litigation – is too difficult because of the multi-sided nature of the markets generally at issue. That is to say, in these cases, the Commission is not looking at a conduct or transaction's effect on just one market (such as whether consumers will pay more for a product), but at how the conduct or transaction will affect at least two interrelated markets. In the online advertising cases, for example, those two markets are typically the market for advertisers and the market for consumers of those ads. As a firm's control over one increases, it inherently enjoys benefits in the others; the more users (i.e., consumers) for which a firm can claim credit, the more advertisers that will flock to that firm's service. The alleged problem is that looking at the effects in both of these markets (to say nothing of defining them, given that they are sometimes in a nascent state) is too hard for the agencies. I half agree.

The second argument I have heard is that the transactions or practices involved in high-tech cases are too dynamic to effectively challenge. There is certainly some validity to this critique. For one, the constant innovation in fast-moving markets means the market at issue in a case or investigation can literally change. One moment we may be claiming Intel is a monopolist in the market for the x86 processor (the only major processor that most of us use for daily computing) and is seeking to take control of the entire computing platform, but the advent of tablets and smartphones may mean that the market tips such that ARM or some other processor is the dominant processor. In other instances it may be that when we start an investigation, mobile advertising is offered through one means (such as cost-per-click), but that some new, better technology (be it developed by Apple, Google, Microsoft, or a startup we've never heard of) comes up with a better means to deliver targeted advertising. This can make market definition very challenging – particular when these events occur (as they sometimes have) during our investigations. Indeed, one can argue that the more thorough the agencies are in their investigations (or, to put it bluntly, the longer the investigations drag on), the more we risk having events overtake us.

This raises a related problem with fast-moving high-tech markets which is that they do not fit snugly into the drawn out litigation process that we have in the U.S. By my estimate, from the time an agency sues until all appeals are exhausted, a case can take (conservatively) 3-4 years to work its way through our court system – and that assumes no bumps along the way. In this regard, while I laud the Justice Department for their suit against Microsoft, I think it's safe to say that the drawn out process there to secure a remedy is a cautionary tale that we at the government live with every time we decide to sue a major player under Section 2 or Section 5 in the high-tech sector. The flipside to this, of course, is that in an effort to avoid drawn out litigation and remedies that come too late, the agencies run a serious risk of doing quick and dirty investigations or accepting less than optimal settlements because litigation simply takes too long. The Commission's settlement in Intel—which Chairman Leibowitz explicitly noted was an attempt to avoid drawn out litigation[5]—has been criticized on this ground.

These problems, however, are not insurmountable. In fact, while I know we are not without our critics, I think the Commission's experiences in Google/DoubleClick and Google/AdMob show that we can change on the fly. In the former, over an objection from Commissioner Harbour, the Commission declined to challenge a merger because the majority of the Commission could not find a reason to believe that the merger of the leading provider of sponsored search advertising (Google) and the leading firm in the United States serving third-party ad markets (DoubleClick) would be anticompetitive.[6] In the latter case, the Commission unanimously closed its investigation after it became clear that Apple was in a position to (and likely would) nullify any anticompetitive

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[5] FTC News Release, FTC Settles Charges of Anticompetitive Conduct Against Intel (Aug. 4, 2010), *available at* http://www.ftc.gov/opa/2010/08/intel.shtm ("By accepting this settlement, we open the door to competition today and address Intel's anticompetitive conduct in a way that may not have been available in a final judgment years from now. Everyone, including Intel, gets a greater degree of certainty a gr4001 tobuiw[(n th, on unan)4.6rw[(nova8.6

effects of the Google-AdMob merger.[7] Likewise, while the Intel settlement was not perfect, I think the Commission did a good job of exercising its prosecutorial discretion in, first, deciding to sue Intel when it did not think there was a viable settlement on the table and, second, settling the case when it became clear that consumers (and Intel for that matter) would be better served by a quick resolution, than by a drawn out *Microsoft*-type litigation. To be sure, I personally would have liked to have seen the Section 5 issues in the Intel case litigated to a conclusion simply to get some more clarity on the issues, but even I had to admit that the settlement that Intel agreed to was not worth rolling the dice on some interesting questions of law.

The third argument that I have heard against challenging conduct by firms in high-tech markets is that we can't challenge conduct by firms that only have "incipient" monopoly power, as may be the case in conduct cases where a firm is on the cusp of achieving monopoly power, but the market has not yet tipped. This, for example, could have become an issue in the Google/AdMob merger. Google and AdMob were the number 1 and 2 mobile advertising networks, respectively. Apple was not in the market when the investigation began. As the Commission noted in its closing statement, however, during the investigation, Apple acquired the third largest mobile advertising network and soon thereafter unveiled its own mobile advertising network, iAd.[8] Given that mobile advertising appears on apps—and at the time the Commission closed its investigation, approximately 85 percent of those apps were on the Apple platform—the Commission concluded that "Apple's ownership of the iPhone software development

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[7] Statement of the Federal Trade Comm'n concerning Google/AdMob, FTC File No. 101-0031 (May 21, 2010), *available at* http://www.ftc.gov/os/closings/100521google-admobstmt.pdf.

[8] *Id*.

answer is not to deny the FTC Section 5 authority, though it may be to augment DOJ's powers with Section 5 authority.[11] I have yet to make up my mind on that one, which, in any event, is a debate for another day.

A fourth challenge I have heard is that we should stay out of high-tech markets because, as a matter of policy, we should not be in the business of challenging an inventor's conduct. Or, to put it differently, we don't wa for work around innovators), we must also protect the incentives of parties to compete with the original innovator.[13]

Moreover, from a doctrinal standpoint, I'm not sure the rule of reason is all it's cracked up to be. Professor Hovenkamp (one of the principal champions of a full-blown challenge to a transaction or conduct that threatens innovation alone. In fact, the best case on this point to my knowledge is the Second Circuit's 1981 decision in *SCM Corp. v. Xerox Corp.*[16] There, the Second Circuit held that a defined product market is a prerequisite to an antitrust claim.[17] Moreover, while there have been challenges to innovation markets in pharmaceutical merger cases, those challenges have all resulted in consents that the parties agreed to in order to get the deal through.[18] I find this objection—that we should not be in the business of challenging innovation markets as such—to have the most credibility.

Xerox, a joint venture in which Xerox had previously held a non-majority stake. Because Xerox had acquired patents to all of the technologies needed to engage in xerography, the Commission alleged that Xerox was eliminating the competition in the development and creation of office copiers. The Commission settled the *Xerox* suit in 1975 with a consent decree that required Xerox to permit the use of any three of its dry paper copier patents on a royalty-free basis and to desist in pursuing certain of its infringement suits.

[16] *SCM Corp. v. Xerox Corp.*, 645 F.2d 1195 (2d Cir. 1981).

[17] *Id*. at 1206 (rejecting the claim that acquisition of patents alone could create antitrust liability and observing that "[t]he patent system would be seriously undermined . . . were the threat of potential antitrust liability to attach upon the acquisition of a patent at a time prior to the existence of the relevant market

But the sixth and biggest stumbling block to the agencies challenging innovation markets is that, in my mind, the long-standing threshold question debated by Schumpeter, Arrow, and others—i.e., whether it is better to keep the scientists separate and in competition or put them together at the same place—has not been resolved. If it is the case that having all of the world's experts meet together leads to better innovation, then we should allow consolidation and coordination. Conversely, if we're better off having scientists and software developers in competition, then we should be vigilant about enforcement. For what it's worth and to complicate things further, I'm not even sure there is a "one size fits all" answer here. After all, it may be that the answers to that question are different depending on whether the challenge is made in the pharma context (where the scientists are seeking a clear objective—such as a cure for Alzheimer's) or in the high-tech context (where the sky is the limit as far as innovation goes). In any event, this objection was more persuasive to me when the challenge was to mergers/conduct in the pharmaceutical industry under the 1992 Guidelines. Then, we were limited to looking at whether entry was likely over a two-year time horizon.[19] The need in the pharma context to get FDA approval before acting combined with the fact that predicting entry in high-tech markets made the hard-and-fast two-year cutoff very problematic. Given that the new guidelines have done away with that requirement and emphasize that the agencies will look carefully at whether a merger will diminish innovation, we have more flexibility to look at innovation markets because we can look at longer time

[19] 1992 Horizontal Merger Guidelines, § 3.2 (entry is considered timely and can reverse any likely anticompetitive effects only if entry will be "achieved within two years from initial planning to significant market impact").

horizons. Over the long run, I think that should help lead the agencies to better results—

with other evidence.[20] Complex economic theories are simply not comprehensible to many specialists like myself, let alone to a generalist.

Moreover, framing a trial strategy around a story (as opposed to a formula) enables the introduction of more non-price evidence (i.e., evidence respecting effects on quality and safety), which gives courts more latitude. The FTC's recent loss in the *Ovation* repeat them here,[23]

intended, but because to the extent one believes (as I do) that Section 5 should apply in the "one off" case, predicting those elements in advance is a futile task.

Further, while I am on the topic of conduct cases that the Commission generally brings in Part 3 administrative litigation (and under Section 5 in particular), I believe there are a few additional considerations that should apply. To start, the Commission's story should, if possible, exhibit the expertise that the Commission can bring to the analysis, especially as compared with a generalist federal district court judge in private antitrust cases. I've already alluded to the Commission's expertise in analyzing conduct by a firm with "incipient" monopoly power, which may not amount to the market power required by the "attempt to monopolize" case law. The conduct may also, however, involve deception (as it did in *N-Data* and *Intel*) and hence trigger the agency's consumer protection expertise and Section 5's consumer protection prong. Indeed, the federal courts have recognized the Commission's special expertise in this respect.[33] And, as Commissioner Kovacic has observed, the FTC is a better antitrust agency because of its consumer protection mission.[34]

When the Commission brings a conduct case, it should be mindful that "collateral consequences" may follow from its decision and should limit the risk

The Supreme Court has issued several decisions designed ostensibly to rein in those cases.[35] But to put it bluntly, I worry that the Supreme Court is not only modifying procedural rules to cabin the private plaintiff's bar, but that it is curbing the substantive rules as well. Since 2004, the Supreme Court has decided ten antitrust cases – not one of those cases was brought by the government.[36] This means that the vast majority of substantive antitrust law is being made in cases involving private plaintiffs.[37]

Second, the story in any high-tech case should include all factors that may affect consumer choice and the flip-side—consumer opportunity—which is a supply side consideration. Why? For one thing, consideration of consumer choice enables consideration of all dimensions of competition, including non-price factors, that may be less measurable. Moreover, consideration of consumer opportunity enables one to take into account consumer preference that may be irrational (as behavioral economics suggests) as well as rational consumer preferences (which the Chicago and post-Chicago Schools assume). If one truly believes in the market, producers will gravitate toward producing goods/choice that most consumers want, whether their preferences are rational or irrational. Indeed, there is a strong argument that having the state call the shots respecting consumer choice not only defeats the outcome that market forces would dictate, but also smacks of the kind of "central planning" characteristic of a totalitarian state.

Third, as noted earlier, I still believe that an important element of all cases—including high tech cases (mergers and otherwise)—is defining the relevant market. I feel compelled to mention that because in some of the recent commentary on the revised merger guidelines, I think that requirement has gotten lost in translation. In my experience in cases involving the high-tech sector, the easiest way to define the relevant market is to figure out how the firm at issue monetizes its intellectual property or innovation. How does Google monetize its searches? How does Apple monetize its apps and iTunes? How does Facebook monetize public profiles? And so on. Identifying how firms monetize their bread and butter enables the agencies to zero in on who the customers are, whether there is competition, and whether the absence or potential absence of competition is a result of business acumen or anticompetitive conduct.

Fourth and finally, I believe that when the agencies bring cases in the high-tech sector, their story must be flexible not only to account for changes in the market place (be it competition for the x86 platform in the Intel litigation or Apple's entry into mobile advertising in the Google/AdMob merger), but that it should also account for dynamic effects and efficiencies. As I have said elsewhere, in my view, antitrust law has for far too long largely applied a static analysis, which looks mostly at marginal prices and costs in the short run.[38] In contrast, dynamic analysis focuses on the long-run considerations that capture the goals associated with innovation, including, among other things, the creation of new products and services. As economist Joseph Schumpeter long ago recognized—and with particular application to the high-tech sector, I might add—a certain amount of protection from competition is necessary for a firm to undergo the risks and costs of innovating and that innovation can ultimately have a great effect on consumer welfare.[39] The question is how much? I don't know the answer to that, but I do think we are shooting ourselves and consumers in the foot if we don't take very seriously the dynamic nature of these markets – even if it is very hard to quantify – when we tell our story in cases in the high-tech sector.

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[38] Commissioner J. Thomas Rosch, Promoting Innovation: Just How "Dynamic" Should Antitrust Law Be?, Remarks before the

All of this said, why do I dwell on the characteristics of

Right now we are seeing firms respond to this need to balance in very different ways. On the one hand, you have firms like Google that pride themselves on maintaining an open platform. This means that any app developer that wants to get on the Android platform or any smartphone developer that wants to use the Android operating system is free to do so. This may mean that consumer data is handled more loosely than some would like, but it also means that there is competition along many different axes that we might not otherwise see. In contrast, there are firms like Apple that pride themselves on a closed platform not only because it allows them to control the quality of the operating system and content better, but also because it gives them much greater control over users' privacy. The issue here, of course, may be that the claim of privacy protection itself may become a barrier to entry in the sense that Apple may be able to leverage its power over iPhone, iPad, and other devices (and its sole control over user data) to eliminate competition in things like mobile advertising or app development.

To be clear, I am not saying Google is clearly good here or Apple is somehow bad. Rather, I am simply noting that an issue we will likely face on the horizon is what to do when high tech firms start using the need to protect consumers' privacy as a defense to