IS THERE LIFE AFTER TRINKO AND CREDIT SUISSE?: THE ROLE OF ANTITRUST IN REGULATED INDUSTRIES

HEARING

BEFORE THE

SUBCOMMITTEE ON COURTS AND COMPETITION POLICY

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

JUNE 15, 2010

Serial No. 111–119

Printed for the use of the Committee on the Judiciary

Available via the World Wide Web: http://judiciary.house.gov

U.S. GOVERNMENT PRINTING OFFICE

56–952 PDF WASHINGTON : 2010

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

COMMITTEE ON THE JUDICIARY

JOHN CONYERS, JR., Michigan, *Chairman*

HOWARD L. BERMAN, California
RICK BOUCHER, Virginia
JERROLD NADLER, New York
ROBERT C. "BOBBY" SCOTT, Virginia
MELVIN L. WATT, North Carolina
ZOE LOFGREN, California
SHEILA JACKSON LEE, Texas
MAXINE WATERS, California
WILLIAM D. DELAHUNT, Massachusetts
STEVE COHEN, Tennessee
HENRY C. "HANK" JOHNSON, JR., Georgia
PEDRO PIERLUISI, Puerto Rico
MIKE QUIGLEY, Illinois
JUDY CHU, California
TED DEUTCH, Florida
LUIS V. GUTIERREZ, Illinois
TAMMY BALDWIN, Wisconsin
CHARLES A. GONZALEZ, Texas
ANTHONY D. WEINER, New York
ADAM B. SCHIFF, California
LINDA T. SÁNCHEZ, California
DANIEL MAFFEI, New York
JARED POLIS, Colorado

LAMAR SMITH, Texas
F. JAMES SENSENBRENNER, JR., Wisconsin
HOWARD COBLE, North Carolina
ELTON GALLEGLY, California
BOB GOODLATTE, Virginia
DANIEL E. LUNGREN, California
DARRELL E. ISSA, California
J. RANDY FORBES, Virginia
STEVE KING, Iowa
TRENT FRANKS, Arizona
LOUIE GOHMERT, Texas
JIM JORDAN, Ohio
TED POE, Texas
JASON CHAFFETZ, Utah
TOM ROONEY, Florida
GREGG HARPER, Mississippi

PERRY APELBAUM, *Majority Staff Director and Chief Counsel*
SEAN MCLAUGHLIN, *Minority Chief of Staff and General Counsel*

SUBCOMMITTEE ON COURTS AND COMPETITION POLICY

HENRY C. "HANK" JOHNSON, JR., Georgia, *Chairman*

JOHN CONYERS, JR., Michigan
RICK BOUCHER, Virginia
CHARLES A. GONZALEZ, Texas
SHEILA JACKSON LEE, Texas
MELVIN L. WATT, North Carolina
MIKE QUIGLEY, Illinois
DANIEL MAFFEI, New York
JARED POLIS, Colorado

HOWARD COBLE, North Carolina
JASON CHAFFETZ, Utah
F. JAMES SENSENBRENNER, JR., Wisconsin
BOB GOODLATTE, Virginia
DARRELL ISSA, California
GREGG HARPER, Mississippi

CHRISTAL SHEPPARD, *Chief Counsel*
BLAINE MERRITT, *Minority Counsel*

CONTENTS

JUNE 15, 2010

IS THERE LIFE AFTER TRINKO AND CREDIT SUISSE?: THE ROLE OF ANTITRUST IN REGULATED INDUSTRIES

TUESDAY, JUNE 15, 2010

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COURTS AND
COMPETITION POLICY
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:21 a.m., in room 2237, Rayburn House Office Building, the Honorable Henry C. "Hank" Johnson, Jr. (Chairman of the Subcommittee) presiding.

Present: Representatives Johnson, Conyers, Quigley, Polis, Coble, Chaffetz, and Goodlatte.

Staff present: (Majority) Anant Raut, Counsel; Rosalind Jackson, Professional Staff Member; (Minority) Stewart Jeffries, Counsel; and Tim Cook, Staff Assistant.

Mr. JOHNSON. This hearing of the Committee on the Judiciary Subcommittee on Courts and Competition Policy will now come to order. Without objection, the Chair is authorized to declare a recess.

Today's hearing is the latest in the series of hearings I call, "An Antitrust System for the 21st Century." I have initiated these hearings to consider some of the issues raised by the bipartisan Antitrust Modernization Commission created by the Judiciary Committee.

The question before us today is this: Did the Supreme Court's decision in the *Trinko* and *Credit Suisse* cases sound the death knell for antitrust enforcement in regulated industries? In the 100-plus years since the antitrust laws were enacted they have coexisted with other types of regulations.

The reason Congress wrote both is that different types of laws provide different types of protection for consumers. Antitrust has always been concerned with promoting competition; when businesses compete consumers win. But regulators may have other concerns, such as safety or policy goals other than fair competition.

In some cases the antitrust laws may be in tension with other regulations. In rare instances, following one law might result in the violation of an antitrust duty.

In a few of these cases Congress has expressly created exemptions from the antitrust laws. In others, courts have implied an immunity, as is the case with certain rights under labor and employment law.

Traditionally, such implied immunities have been narrow in scope because the courts have assumed that, unless Congress has said so explicitly, it intends for all laws that it passes to coexist. But in *Trinko* and *Credit Suisse* the Supreme Court appears to have abandoned this traditional perspective. In a most unjudicial way the Court went beyond ruling on the facts at hand and took a skeptical approach to the antitrust laws and the competence of our Federal judges and juries in applying them.

As a Member of Congress and as the Chairman of the Subcommittee on Courts and Competition Policy, I find this to be offensive. Our Federal courts and juries handle complex matters all the time, and if the judges of the Supreme Court believe our system is not up to the task they should make suggestions for improving the system, not take swipes at it in their opinions.

The past century has been one of growth and innovation, and time and again the courts have proven well capable of adjusting and refining the antitrust laws to reign in excess and ensure that antitrust rules are fair, efficient, and predictable. As a result, our antitrust laws police business excesses but do not hamper legitimate innovation. That is an approach I support, but it is one that the Supreme Court appears to have inexplicably cast aside in these cases.

In a few short years the effect of those decisions has been devastating. Instead of the default being that the antitrust laws apply, *Trinko* and *Credit Suisse* have been cited to dismiss antitrust cases in the securities and telecom industries before they can even be tried on their merits, nor is there anything that limits these decisions to their respective industries. Under *Trinko*, will courts start looking skeptically at all antitrust claims?

I am also concerned by what appears to be a trend of the Supreme Court legislating from the bench. As a former judge I take the role of the court very seriously, and I also respect its limits. The regulatory laws in both *Trinko* and *Credit Suisse* contain savings clauses that Congress has specifically written-in in order to ensure that antitrust law was not displaced by regulation, yet that is exactly what happened.

As Justice Thomas wrote in a scathing decent in *Credit Suisse*, "The regulatory statutes explicitly say the very remedies the Court hopes to be impliedly precluded." It is not every day that I agree with Justice Thomas, but on this one I do.

The role of the courts is to interpret the law, not to rewrite the law or usurp the role of Congress in setting economic policy for this Nation. If these cases were correctly decided, what more does Congress have to do to keep the antitrust laws in effect?

I will now recognize my colleague, Howard Coble, the distinguished Ranking Member of the Subcommittee, for his opening remarks.

Mr. COBLE. Thank you, Mr. Chairman. Thank you for calling this hearing of the Courts and Competition Policy Subcommittee.

Today's hearing could have profound implications for the jurisdiction of this Subcommittee. It deals with two Supreme Court cases that you mentioned that, if the critics are correct, could severely limit the reach of antitrust laws in regulated industries.

I am of two minds on today's hearing, Mr. Chairman. On the one hand, I am an avid supporter of our Federal antitrust laws. They are critical to ensuring that customers receive the benefits of competition, namely lower prices and greater choices. So, to the extent that these decisions can be read as a blanket exemption from the antitrust laws, I am skeptical of their reach.

On the other hand, I am wary of overregulating businesses, or what is worse, giving businesses conflicting regulatory demands; to the extent that these decisions can be read as merely clarifying the regulatory burden borne by businesses, I am supportive.

The fact that these decisions can be read two different ways really complicates matters, it seems to me. For example, is *Trinko* merely a limit on the extent that antitrust law can compel a dial-up firm to deal with its rivals, or is it a blanket antitrust exemption for the telecommunications industry despite an antitrust savings clause in the 1996 Telecommunications Act?

These are very complicated and weighty issues, as we all know, in antitrust law, and I am pleased that we have such a diverse panel of experts to assist us in understanding the reach of these decisions. These questions are hardly just academic.

Currently, members of both the House and Senate are meeting to reconcile the financial services regulatory bill. Those versions of that legislation contain antitrust savings clauses. Depending on what we learn here today we may need to revisit that language to ensure that courts will honor congressional intent with respect to the role that antitrust will play in the financial services industry going forward.

With that, Mr. Chairman, I look forward to hearing from our witnesses on this important topic and I yield back the balance of my time.

Mr. JOHNSON. Thank you, Mr. Coble.

I now recognize John Conyers, a distinguished Member of the Subcommittee and the Chairman of the full Committee on Judiciary.

Mr. CONYERS. Thank you, Chairman Johnson, and Howard Coble, and my other colleagues here. This is an important hearing in many respects and unusual. The part that makes it so unusual for me is we have attorney John Thorne, who argued the *Trinko* case, as a witness.

We are very honored to have you here.

Mr. THORNE. I argued the case in the Second Circuit, where we lost, however, and left it to my colleague to argue successfully in the Supreme Court.

Mr. CONYERS. Yes, but you were assisting those that argued it in the Supreme Court, where you did a lot better, and we thank you for coming here today, because we look forward to your analysis and experience in this matter.

As both the Chairman and Howard Coble have suggested, this is a hugely important matter, and this Committee in the judiciary is very important. One way to look at it is that we are caught between Thurgood Marshall's calling antitrust laws "the Magna

Carta of free enterprise" and the fact that the courts are implying that antitrust is more subordinated to other regulatory concerns.

And Thorne goes even as far as to say that—well, he goes further than anybody else: "The result in *Trinko* did not depend on regulatory context."

And so there is a pattern and direction that has been determined by the courts that I think we don't disagree on, and the question is, is antitrust just a good law and look, we have got the Sherman and Clayton Acts, and then Rodino—the Hart-Scott-Rodino—came in even later. So what the Committee is asking is, what direction are we going in and what direction ought we go in?

Now, I would like to describe my take on what the relationship of the three branches of government are, because sure, the Court takes swipes at legislation, but we take swipes at the Court all the time. We don't do so badly ourselves.

Matter of fact, we can take out a Court decision if we want to, and they can find unconstitutional or some other problem of our legislation. And, of course, that is the genius with the system, isn't it, that we have three branches coequal?

And there are always these tugs of war and differing interpretations that are going on, and so I am anxious to hear from the witnesses. I will put my statement—the rest of my statement—in the record. And thank you for calling this hearing.

[The prepared statement of Mr. Conyers follows:]

PREPARED STATEMENT OF THE HONORABLE JOHN CONYERS, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN, CHAIRMAN, COMMITTEE ON THE JUDICIARY, AND MEMBER, SUBCOMMITTEE ON COURTS AND COMPETITION POLICY

Statement of the Honorable John Conyers, Jr.
for a hearing on

"Is There Life After Trinko and Credit Suisse?:
The Role of Antitrust in Regulated Industries"

before the Subcommittee on
Courts and Competition Policy
of the Committee on the Judiciary

Tuesday, June 15, 2010, at 10:15 a.m.
2237 Rayburn House Office Building

Thank you Chairman Johnson for convening this hearing today. I look forward to discussing with our distinguished witnesses what we can do to strengthen our antitrust laws and ensure that competition in our nation is free, strong and fair.

In 1972, Justice Thurgood Marshall described the federal antitrust laws as "the Magna Carta of the free enterprise system." [1]

[1] United States v. Topco Associates, 405 US 596 (1972) (holding that the members of a grocery cooperative violated the antitrust laws when they divided up territories).

In recent years, however, our Magna Carta is starting to look a bit worse for wear.

The Bush Administration's failure to carry out meaningful antitrust enforcement is well known. As the New York Times explained last year "As a result of the Bush administration's interpretation of antitrust laws, the enforcement pipeline for major monopoly cases — which can take years for prosecutors to develop — is thin. During the Bush administration, the Justice Department did not file a single case against a dominant firm for violating the antimonopoly law."[2]

In addition, the Courts also appear overly hostile to cases seeking to hold businesses accountable for illegal and anticompetitive acts. One recent study of antitrust cases over the past 10 years found that – quote – "plaintiffs almost never win" – and determined that 221 out of 222 "rule of reason" cases were decided in the defendant's favor.[3]

In March 2008, former Deputy Assistant Attorney

[2]Labaton, Obama Takes Tougher Antitrust Line, New York Times, May 11, 2009.

[3]Carrier, The Rule of Reason: An Empirical Update for the 21st Century, George Mason Law Review, Vol. 16, No. 827, 2009.

General in the DOJ Antitrust Division William Kolasky observed that the outlook for antitrust cases in the Supreme Court has been especially bleak. Mr. Kolasky wrote "Our Supreme Court, especially under the leadership of Chief Justice John Roberts, seems equally intent on cutting back on private enforcement. It has been more than fifteen years since the Supreme Court last decided an antitrust case in favor of a plaintiff. Over this fifteen-year period, [private] plaintiffs have gone 0-for-16, with not a single plaintiff winning an antitrust case in the Supreme Court since the first George Bush was president."[4]

While I do think the plaintiffs may have notched a victory or two since this was written, the larger point stands - our federal courts have become more and more inhospitable to those who would assert their rights under antitrust.

Which brings us to the subject of our hearing today. In the *Trinko* and *Credit Suisse* cases, the Supreme Court held that antitrust claims will almost never be available

[4]Kolasky, Reinvigorating Antitrust in the United States: A Proposal, 22 Antitrust 85 (2008).

in cases involving regulated industry. Even worse, the Court in this cases seemed to go out of its way to criticize our antitrust laws – arguing that antitrust often does more harm than good and that courts and juries are especially prone to getting antitrust cases wrong. According to the Roberts Court, these arguments suggest that antitrust cases should be looked at with great skepticism. We have come quite a ways from the days of Justice Marshall and the "Magna Carta of free enterprise."

Well, I side with Justice Marshall on this one. I think we must do all we can to strengthen antitrust enforcement, and to ensure that the Sherman Act is given a fair hearing in the courts. Both government enforcers and private litigants need strong antitrust laws to ensure that our corporate leaders compete fairly and honestly.

With those concerns in mind, I have three questions I hope our witnesses will address:

First, the *Trinko* and *Credit Suisse* cases both involved regulated industries – but I worry that the Roberts court's hostility to antitrust will continue and the rollback will reach unregulated businesses as well. Do you think that the approach of *Trinko* and *Credit Suisse* are limited to regulated industry or is there a broader threat here?

Second, what does it take for an industry to be considered "regulated" in the eyes of this Court? Virtually all business in the United States is subject to some regulation. Does it matter if specific regulations actually address the conduct being challenged? Or does the mere possibility of regulation suffice? Does state regulation block antitrust, or only federal?

Third, can you suggest any changes to federal law that would ensure that the values of antitrust and fair competition are given greater weight by the Courts? What next steps – if any – would you recommend we take?

Thank you very much – I look forward to your testimony and our discussion this afternoon.

5

Mr. JOHNSON. I thank you, Mr. Chairman, for your statement.

And are there any other statements?

I am now pleased to introduce the witnesses for today's hearing. Let the record show that there was no affirmative response to my last question.

Our first witness is Howard Shelanski, Deputy Director of Antitrust for the Bureau of Economics at the Federal Trade Commission. Mr. Shelanski is also a former Supreme Court clerk for Justice Antonin Scalia.

Our next witness is Mr. John Thorne, Senior Vice President for Verizon Communications. Mr. Thorne successfully argued the *Trinko* case before the Second Circuit in 2004.

Next we have Professor Mark Lemley, from Stanford University School of Law.

Finally, we have Dr. Mark Cooper, Director of Research for the Consumer Federation of America.

Thank you all for your willingness to participate in today's hearing. Without objection, your written statement will be placed into the record, and we would ask that you limit your oral remarks to 5 minutes.

You will note that we have a lighting system on the table that starts with the green light. After 4 minutes it turns yellow, then red at 5 minutes.

After each witness has presented his or her testimony Subcommittee Members will be permitted to ask questions subject to the 5-minute rule.

Mr. Shelanski, will you begin your testimony?

TESTIMONY OF HOWARD A. SHELANSKI, DEPUTY DIRECTOR FOR ANTITRUST IN THE BUREAU OF ECONOMICS, FEDERAL TRADE COMMISSION, WASHINGTON, DC

Mr. SHELANSKI. Chairman Johnson, Ranking Member Coble, and Members of the Subcommittee, thank you for the opportunity to appear before you today. I am Howard Shelanski, deputy director for antitrust in the FTC's Bureau of Economics.

The written statement we have already submitted represents the views of the Commission. My oral testimony is my own and does not necessarily reflect the views of the Commission or any commissioner.

I would like to make two points in this statement: First, the Supreme Court's decisions in *Credit Suisse* and *Trinko* make it more difficult for antitrust law to play the important role it has long played in regulated sectors of the American economy. Second, the cost-benefit reasoning that led the Supreme Court to reject the private suits at issue in *Credit Suisse* and *Trinko* does not apply to public enforcement acts. Even if one assumes that those cases strike the correct balance in private suits, they should not be interpreted to block public cases where the Federal antitrust agencies find that antitrust enforcement would yield additional benefits for American consumers.

Before the 2004 *Trinko* decision public agencies and private plaintiffs have long enforced antitrust law in a variety of regulated settings. Those cases range from enforcement against collective refusals to deal in the securities industry to refusals to interconnect with rivals in the electricity and telecommunications markets. The most dramatic example, of course, is the government's 1973 suit against AT&T that culminated in the breakup of the bell system and to thwart competition in lower long-distance calling rates to American consumers.

But cases show that antitrust laws have played an important complimentary role to regulation. It can reach conduct that regulation did not anticipate, filling gaps left by agency rules, and often protect competition and innovation in a more targeted, less burdensome way than rules do. This is the role that antitrust, particularly public enforcement of antitrust, should be able to continue to play in the future, but which it may be impeded by *Credit Suisse* and *Trinko*.

Antitrust enforcement was not, of course, unlimited in regulated industries. The Supreme Court has long held that antitrust enforcement could not occur when it directly conflicts with regulation, but *Credit Suisse* and *Trinko* marks a significant change from that earlier doctrine.

Credit Suisse extended the definition of conflicts by blocking from antitrust claims that involve conducts not regulated by securities law, and it could only conflict with regulations through judicial error. The result could be gaps in enforcement when neither antitrust nor regulation can reach harmful conduct.

Trinko can be read to make it harder to bring antitrust claims against firms, since competitive conduct is subject to regulated—regulatory oversight, even when Congress has included a savings clause that expressly preserves the simultaneous operation of antitrust and regulation. In some instances this might make sense. For example, in the specific context where an agency actively administers a rule whose standard for the competitive conduct at issue is more demanding on the defendant than antitrust laws. In such cases the courts are right to ask whether the marginal gains from antitrust enforcement outweigh the potential costs.

Our concern is that *Trinko* could be read more broadly by the lower courts and block antitrust claims even when regulation does not directly or effectively address unfair methods of competition. Had the Supreme Court made clear that to preclude antitrust claims a regulatory structure must, like the one at issue in *Trinko*, be directly relevant to the conduct at issue, be more demanding than antitrust law, and be actively administered, one might worry less about harmful side effects of that ruling.

The risk for public enforcement agencies is that, given the *Trinko* Court's emphasis on the potential costs of antitrust, lower courts will block public antitrust cases where the regulatory scheme falls well short of the FCC's implementation of the 1996 act's competitive access provisions.

Why did the Court rule as it did in *Credit Suisse* and *Trinko*? Phrased broadly, the Court's concern was that antitrust is always costly, and in the presence of regulation is likely to have little additional benefit for competition.

If that cost-benefit calculation for the kinds of private suits at issue in *Credit Suisse* and *Trinko*, they differ greatly for public enforcement acts. A public agency's incentives are very different from those of private plaintiffs.

The FTC does not collect revenue or otherwise materially benefit from successful competition enforcement. The government has no incentive to use antitrust law or the Federal Trade Commission Act against a regulated firm unless doing so can yield benefits beyond those the market already gets through regulation.

The Federal antitrust agencies, therefore, have more incentive and obligation than private plaintiffs do to assess the potential cost of an antitrust case, to evaluate whether antitrust enforcement can provide benefits not provided by regulation, and to balance the two in the public interest. As a result, public enforcement is more likely than private litigation to avoid claims that would be prone to judicial errors, that will interfere with regulation, or that will fail to yield net benefits over regulation.

We therefore think it would be good policy for Congress to clarify that neither *Credit Suisse* nor *Trinko* prevents public antitrust agencies from acting when they conclude that anticompetitive conduct would otherwise escape effective regulatory scrutiny.

Thank you again for allowing me to appear today. I would be happy to answer any questions you may have.

[The prepared statement of Mr. Shelanski follows:]

PREPARED STATEMENT OF HOWARD A. SHELANSKI

Is There Life After *Trinko* and *Credit Suisse*?
The Role of Antitrust in Regulated Industries

Prepared Statement of
The Federal Trade Commission

Before the
United State House of Representatives
Committee on the Judiciary
Subcommittee on Courts and Competition Policy

Washington, D.C.
June 15, 2010

Chairman Johnson, Ranking Member Coble, and members of the Subcommittee, I am Howard Shelanski, Deputy Director for Antitrust in the Bureau of Economics at the Federal Trade Commission ("FTC" or "Commission").[1] Thank you for inviting the Commission to present its views on how the Supreme Court's decisions in *Verizon v. Trinko*[2] and *Credit Suisse v. Billing*[3] could affect public enforcement of the antitrust laws in regulated industries.

We would like to make two points in this statement. First, the combined effect of *Credit Suisse* and *Trinko* is to make it more difficult than before for either private plaintiffs or public agencies to bring important antitrust cases in regulated sectors of the American economy. Second, the heightened concerns about the high costs and questionable benefits of antitrust enforcement in regulated industries that motivate the Court's decisions in *Credit Suisse* and *Trinko* do not apply to public enforcement actions. While we do not take the position in this testimony that *Trinko* or *Credit Suisse* necessarily prevents the Commission from bringing any particular case or set of cases, we do argue that the federal courts should not be able to use those decisions to impose an unwarranted bar on public antitrust enforcement in regulated industries.

[1] This written statement represents the views of the Federal Trade Commission. My oral presentation and responses to questions will be my own and do not necessarily reflect the views of the Commission or of any Commissioner.
[2] *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004).
[3] *Credit Suisse Securities v. Billing*, 551 U.S. 264 (2007).

I. <u>Antitrust Enforcement in Regulated Industries Prior to *Credit Suisse* and *Trinko*</u>

Before the Supreme Court decided *Trinko* (2004) and *Credit Suisse* (2007), the Court had held in a line of cases stretching back 60 years that public agencies and private plaintiffs could enforce the antitrust laws in regulated industries. In those cases, the Court did not view it as surprising or troublesome for antitrust agencies or private parties to challenge conduct as anticompetitive even if that conduct was already subject to agency rules.

In 1963, for example, the Supreme Court in *Silver v. New York Stock Exchange* rejected the Exchange's attempt to block a group of securities dealers from pursuing an antitrust suit against the Exchange for having directed its members not to provide wire transfer services to the non-member plaintiffs.[4] The Court held that while the Securities Exchange Act of 1934 allowed the exchanges to engage in some self-regulatory conduct that might ordinarily run afoul of the antitrust laws, the group boycott at issue was outside the scope of such self-regulation and therefore not exempt from antitrust suits.[5] The Court's decision presumed against exemptions from the Sherman Act, the nation's principal antitrust statute, in order to advance Section 1's core objective of preventing anticompetitive collusion.

Similarly, in 1973 the Court in *Otter Tail Power v. United States* affirmed the government's application of Section 2 of the Sherman Antitrust Act[6] to

[4] 373 U.S. 341 (1963).
[5] *Id.* at 357.
[6] 15 U.S.C. § 2.

interconnection—or network sharing—among rival electric utilities.[7] The Federal Power Commission arguably had independent authority under the Federal Power Act to order and regulate such interconnection.[8] The Court nonetheless upheld the lower courts' decision to block a dominant utility from using its control over electrical generation to exclude a rival power distributor and monopolize the power market.[9] Likewise, the Department of Justice ("DOJ") has sued AT&T three times (in 1912, 1949, and 1974) for a variety of exclusionary practices against rivals in various telephone equipment and service markets.[10] These markets have long been subject to substantial regulation under federal statutes.

The clear trend in the cases that came before *Trinko* and *Credit Suisse* was that the federal courts generally allowed the simultaneous application of the general antitrust statutes and an industry-specific regulatory statute. The Supreme Court did wrestle in several cases with the question of whether a regulatory regime displaced the antitrust laws, characterizing the issue, among other things, as whether the regulatory regime impliedly repealed the antitrust laws or impliedly immunized the conduct from the antitrust laws. But the Court consistently disfavored antitrust immunity and required a fairly direct level of conflict—"plain repugnancy" in the Court's words—between antitrust law and the regulatory statute before courts could immunize the regulated conduct from antitrust law.[11] The rule that emerged from early cases was that the courts

[7] 410 U.S. 366 (1973).
[8] *Id.* at 373.
[9] *Id.* at 374-5.
[10] *See* STUART BENJAMIN, ET AL., TELECOMMUNICATIONS LAW AND POLICY 713 (2d ed. 2006) (discussing the antitrust actions).
[11] *Otter Tail*, 410 U.S. at 372.

should imply immunity from antitrust enforcement only where, and to the minimum extent, necessary for the relevant regulatory statute to achieve its purpose.[12]

II. The Potential Impact of *Credit Suisse* and *Trinko* on Antitrust Enforcement

Credit Suisse and *Trinko* went beyond the earlier decisions in allowing regulation to limit antitrust enforcement. *Credit Suisse* extended the idea of "repugnancy" between regulation and antitrust law by finding antitrust claims "repugnant" even if the only way they could conflict with regulation was through judicial error.[13] *Trinko* can be read to make it harder to bring antitrust claims that are not already established in precedent against firms whose competitive conduct is subject to regulatory oversight, even when Congress has included a savings clause that expressly preserves the simultaneous operation of antitrust and regulation.[14] The combined result is that through *Credit Suisse* and *Trinko*, the Supreme Court has shifted the earlier cases' balance between antitrust and regulation in favor of regulation.

A. *Credit Suisse*

Prior to *Credit Suisse*, the Supreme Court invariably drew a line between antitrust claims that could conflict with an agency's statutory authority to regulate a particular kind of conduct, and were thus "repugnant" to that statutory authority, and those claims

[12] *See, e.g., Silver*, 373 U.S at 357; *Georgia v. Pennsylvania R. Co.*, 324 U.S. 439, 456-457 (1945); *California v. Fed. Power Comm'n*, 369 U.S. 482, 485 (1962).
[13] 551 U.S. at 284.
[14] 540 U.S. at 410-11.

that could not conflict, principally because they addressed activities the agency had no power either to approve or prohibit.[15] In those cases, the Court did not imply immunity where the conduct underlying the antitrust claim was distinct from anything the securities laws would or could allow. In *Credit Suisse*, the Court extended its precedent in a way that could block some antitrust claims involving conduct the agency either has no specific statutory power to regulate or is certain to regulate in a manner that is consistent with the antitrust laws.

Credit Suisse involved an attempted antitrust suit for collusion in the underwriting of initial public offerings of securities. The applicable regulatory statute gave the SEC authority to review joint underwriting activities and contained no specific antitrust savings clause.[16] It did contain a general savings clause that "the rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity."[17]

The plaintiffs in *Credit Suisse* complained that the defendants, a group of underwriters, had violated Section 1 of the Sherman Act (the anti-collusion provision) by going beyond the kinds of joint setting of securities prices that the securities laws allow.[18] They alleged that the defendants had impermissibly engaged in tying and similar activities that are prohibited by both the antitrust laws and the securities statutes.[19] Importantly, the Court took as given that the defendants' conduct was unlawful under the securities laws and would remain so.[20] The Court nonetheless extended the potential-

---

[15] *See, e.g.*, *Silver*, 373 U.S. at 357-8; *Gordon v. New York Stock Exchange, Inc.*, 422 U.S. 659, 685 (1975); *U.S. v. Nat'l Ass'n of Securities Dealers*, 422 U.S. 694, 719-20 (1975).
[16] 551 U.S. at 271, 276.
[17] *Id.* at 275; 15 U.S.C. §§ 77p(a), 78bb(a).
[18] *Credit Suisse*, 551 U.S. at 269-70.
[19] *Id.*
[20] *Id.* at 279.

conflict rationale for immunity even to antitrust claims that, correctly construed, would not actually conflict with regulation.[21] *Credit Suisse* goes beyond prior implied immunity cases by blocking some antitrust claims that are based on legitimate antitrust principles, are consistent with securities laws, and are not potentially repugnant to the regulatory scheme, but where the underlying conduct is similar enough to regulated conduct that a judge might confuse the two and create a conflict with regulatory authority.

The Court's main concern was the potential for a flood of "lawsuits through the nation in dozens of different courts with different nonexpert judges and nonexpert juries."[22] If plaintiffs could "dress what is essentially a securities complaint in antitrust clothing," they could bypass the expert securities regulators in favor of generalist courts more prone to errors and more likely to impose unwarranted costs on defendants.[23] While the prevention of unnecessary litigation costs and meritless suits is a sound objective, the flood of private suits that motivated the Court in *Credit Suisse* is not an issue in public antitrust enforcement. The fact that the case does not distinguish the private litigation context that was before the Court from public enforcement could lead to unnecessary limitations on beneficial actions by the federal antitrust agencies; it could block the FTC from bringing cases clearly within the scope of antitrust law yet that would be just beyond the reach of regulation.

B. *Trinko*

[21] *Id.* at 283-4.
[22] *Id.* at 281.
[23] *Id.* at 284.

The Court considered *Trinko* against the backdrop of the Telecommunications Act of 1996 ("the 1996 Act"). A central goal of that statute was to foster competition in the provision of local telephone services by requiring incumbent monopolies to provide access to their networks to new entrants into the telecommunications market.[24] When such a new entrant wishes to provide service to customers in a given area, it typically asks the incumbent to connect the customer's line to the new entrant's routing and billing equipment.[25] In this way the new entrant can provide service without building all the "last mile" lines to each customer. AT&T, which had been out of the local telephone business since the company's divestiture in 1984, re-entered that market as a competitor after the 1996 Act. One of the retail customers AT&T signed up was the law office of Curtis V. Trinko. AT&T faced delays in providing service to the plaintiff because of a dispute with Verizon, the incumbent provider of local services in New York, over AT&T's access to Verizon's network facilities.[26]

The 1996 Act amended the Communications Act of 1934 to add an antitrust savings clause, which states that "nothing in this Act . . . shall be construed to modify, impair, or supersede the applicability of any of the antitrust laws" in telecommunications markets.[27] The plaintiff, ostensibly because he could not obtain his choice of telephone service provider, sued Verizon under Section 2 of the Sherman Act as well as under the 1996 Act.[28] He claimed that Verizon violated Section 2 and the 1996 Act by discriminating against rivals like AT&T by refusing to supply them with the network

[24] 47 U.S.C. § 151; *Trinko*, 540 U.S. at 402.
[25] *Trinko*, 540 U.S. at 402.
[26] *Id.* at 404.
[27] 47 U.S.C § 152.
[28] *Trinko*, 540 U.S. at 405.

connections they needed to provide service to customers like Trinko's law office.[29] The case reached the Supreme Court after the Second Circuit reversed the district court's dismissal of Trinko's suit.

The Supreme Court phrased the question presented in *Trinko* as "whether a complaint alleging a breach of the incumbent's duty under the 1996 Act to share its network with competitors states a claim under § 2 of the Sherman Act."[30] The Court answered that question in the negative, and reversed the Second Circuit. Our concern with *Trinko* is not with the Court's ruling against the plaintiff in that particular case, but that the decision may be susceptible to broad interpretations by lower courts that would preclude antitrust claims—both private and public—even absent some of the factors that might have justified the result in *Trinko* itself.

Present in *Trinko* were three critical factors. First, the duties to deal that the 1996 Act imposed on incumbent telephone carriers were stronger than any such duties under Section 2 of the Sherman Act, the anti-monopoly provision on which the plaintiff had based his claim. Second, the Federal Communications Commission (FCC) had issued a set of rules that directly regulated the conduct about which the plaintiff was complaining. And third, the FCC actively administered its duty-to-deal regulations under the 1996 Act. The Court's holding can be read to say that where such factors are present, a violation of the agency's rule does not constitute a separate violation of the antitrust laws. That ruling directly answers the question presented and establishes the principle that when regulatory statutes establish pervasive competition enforcement regimes they do not implicitly

[29] *Id.* at 404-5.
[30] *Id.* at 401.

enlarge the scope of substantive liability under the antitrust laws.[31] As the Court put it, "just as the 1996 Act preserves claims that satisfy existing antitrust standards, it does not create new claims that go beyond existing antitrust standards."[32]

Embedded in the Supreme Court's ruling so interpreted are underlying issues related to the comparative competency of sector-specific regulatory agencies and generalist courts or public antitrust authorities that are beyond the scope of this testimony. The Court speaks explicitly in both *Credit Suisse* and *Trinko* about the hazards of diverting claims from expert agencies to non-expert courts. The risk is that the ability of plaintiffs to seek through antitrust what they could not obtain through the regulatory process could lead to a flood of costly litigation that, when multiplied by the likelihood that generalist courts will make errors at both the pleading and merits stages of litigation, could distort firms' competitive and innovative incentives in a way that will be costly to society.

We do not here address the Court's institutional presumption favoring the administrative processes of expert regulatory agencies over antitrust litigation where the three factors discussed earlier are present. Where a competent agency actively administers a rule whose standard for the competitive conduct at issue in litigation is more demanding on the defendant than antitrust law, the Court was right to find it relevant whether the marginal gains outweigh the potential costs of antitrust enforcement against the same conduct.

---

[31] The specifics of the regulation will matter in deciding how a regulatory statute affects antitrust law; not every statute should be read to limit expansion of antitrust law. In the Court's words, "[j]ust as regulatory context may in other cases serve as a basis for implied immunity, it may also be a consideration in deciding whether to recognize an expansion of the contours of *§ 2*." *Id.* at 412 (internal citations omitted).
[32] *Id.* at 407.

Our concern is that *Trinko* could be read more broadly by lower courts to block antitrust claims even where regulation does not as directly or effectively address the alleged competitive harm as the Supreme Court found the FCC rules at issue in *Trinko* to do. *Trinko* states that one key factor in deciding whether to recognize an antitrust claim against a regulated firm "is the existence of a regulatory structure designed to deter and remedy anticompetitive harm" because "[w]here such a structure exists, the additional benefit to competition provided by antitrust enforcement will tend to be small."[33] Had the Court made clear that to preclude antitrust claims a regulatory structure must, like the one at issue in *Trinko*, be directly relevant to the conduct at issue, be more demanding than antitrust law, and be actively administered, one might worry less about any collateral consequences on public antitrust enforcement. The Court, however, goes on to pose as the contrasting scenario in which antitrust might be worthwhile the case where "[t]here is nothing built into the regulatory scheme which performs the antitrust function."[34] Between "nothing" and the actively enforced duties to deal under the 1996 Act there is a lot of room. The risk for public enforcement agencies is that, given the *Trinko* Court's emphasis on the "sometimes considerable disadvantages" of antitrust, lower courts will preclude antitrust suits where the regulatory scheme is something greater than "nothing" but something well short of the FCC's implementation of the 1996 Act's competitive access provisions.

The Supreme Court's line between the novel claims its rule would preclude and established antitrust claims that could proceed in light of the 1996 Act's savings clause does not alleviate our concern. As a practical and legal matter, that line may be difficult

[33] *Id.* at 412.
[34] *Id.* (quoting *Silver*).

to draw, especially in activities analyzed under the fact-intensive rule of reason. The more factual dimensions there are to a liability determination, the more likely it is that every example of some kind of conduct will be distinguishable from every other example and, therefore, to some extent a novel expansion of doctrine that came before.

After *Trinko*, therefore, the presence of regulatory authority over a competition-related matter may make it more difficult for a plaintiff to pursue an antitrust challenge to the same conduct if the antitrust claim in any way exceeded the clear boundaries of antitrust precedent. Perhaps the most illustrative way to explain *Trinko*'s effect is this: had the decision been in place 40 years ago, the government's ability to pursue the antitrust suit that led to the break-up of AT&T, and other cases in which the government publicly enforced the antitrust laws in regulated industries, would have been in question. To the extent regulatory authorities have become more successful or active in enforcing competition-enhancing rules than they were in the past,[35] one might be inclined to worry less about the loss of such antitrust enforcement. But to the extent the net benefits of antitrust enforcement in regulated industries have declined in light of better competition-oriented regulation, we think they must necessarily have done so less for public enforcement whose net costs, as we will discuss below, are likely to be much lower than the costs of the kind of private suit at issue in *Trinko*. We see no reason, therefore, for the presumption of regulatory effectiveness implicit in *Trinko* to preclude the FTC from pursuing an antitrust case where it finds that a regulatory structure does not adequately "perform the antitrust function."

[35] The FCC had acknowledged its own ineffectiveness as a regulator in the antitrust case leading up to the 1982 AT&T divestiture. *United States v. AT&T*, 552 F. Supp. 131, 168 (D.D.C. 1982).

In sum, *Credit Suisse* and *Trinko* could together make it more difficult for antitrust plaintiffs to bring claims against regulated firms where the conduct subject to complaint could be confused with conduct subject to regulation or where the claim could in some way be characterized as beyond the boundaries of established antitrust precedent. Of the two cases, *Credit Suisse* may be the more far-reaching because it could immunize some anticompetitive yet unregulated conduct from scrutiny. *Trinko* could, as in the case itself, strike a beneficial balance between antitrust and regulation if interpreted narrowly. But the questions *Trinko* leaves open about the standard regulation must meet before it displaces antitrust creates the risk that courts will apply the decision in ways that block public antitrust enforcement that would be beneficial to American consumers.

III. Why *Trinko* and *Credit Suisse* Should Not Apply to Public Enforcement

Both *Trinko* and *Credit Suisse* involved private antitrust suits rather than public enforcement actions by the Federal Trade Commission or the Department of Justice. The Supreme Court's decisions appear, however, to apply to both public and private actions. This is unfortunate because the Court's core concern in both cases about the costs and potential deterrent effects of antitrust are more relevant to private suits, while the benefits of antitrust law as a complement and substitute for regulation are likely to be greatest through public enforcement. The lower costs and higher benefits of cases brought by public agencies arise because of differences in the incentives and capabilities of public and private antitrust plaintiffs.

Phrased broadly, the Court's concern is that antitrust litigation is always costly and in the presence of regulation is likely to have little additional benefit for competition. Treble damages and class action litigation could make erroneous antitrust liability particularly costly in private cases. The government, however, has no reason to use antitrust law against regulated firms unless doing so could yield net benefits on top of those the market already achieves through regulation. The FTC does not collect revenue or otherwise materially benefit from successful competition enforcement. Federal antitrust authorities also have greater resources than private plaintiffs to assess the costs and benefits of a particular antitrust enforcement action and to avoid interfering with regulatory objectives. The FTC and DOJ can both investigate private conduct through a variety of tools that can be focused on specific conduct and information.[36] These procedures are not costless, but they can be narrowly tailored and they occur in advance of litigation, unlike private discovery which occurs after litigation has been initiated and where plaintiffs have incentives to be much less discriminating in the information they demand from defendants.

Importantly, public antitrust agencies can better coordinate with relevant government regulatory agencies to avoid conflicts and unnecessary administrative costs. This ability to coordinate with regulatory authorities relates directly to the Supreme Court's concerns in both *Credit Suisse* and *Trinko*. Coordination could reduce the risk of the kind of judicial error the Court identified in *Credit Suisse* and of the costly duplication and deterrent effects that motivated the Court's decision in *Trinko*.

The federal antitrust agencies therefore have more incentive and ability than private plaintiffs do—not to mention an obligation to the American public—to assess the

[36] ABA SECTION OF ANTITRUST LAW, FTC PRACTICE AND PROCEDURE MANUAL 86 (2007).

potential costs of an antitrust case, to identify the potential benefits that would not be achieved through regulation, and to balance the two in the public interest before deciding to issue a complaint. As a result, public antitrust enforcement is much more likely than private litigation to avoid claims that will be prone to judicial errors, that will interfere with regulation, or that will fail to yield net benefits over regulation.

We are concerned that although the rationales of *Credit Suisse* and *Trinko* apply more to private suits than public enforcement actions, the decisions themselves may sweep more broadly. *Credit Suisse* and *Trinko* could have negative spillover effects on public enforcement and could impede the FTC from bringing cases that would benefit American consumers and promote economic growth. The Commission believes that its authority to prevent "unfair methods of competition" through Section 5 of the Federal Trade Commission Act[37] ("the FTCA") enables the agency to pursue conduct that it cannot reach under the Sherman Act, and thus avoid the potential strictures of *Trinko*.[38] There is good reason for the courts applying *Trinko* to treat FTCA actions differently from private suits under the Sherman Act given, among other things, the absence of treble damages under the FTCA. We nonetheless believe that the better course is for Congress to clarify that neither *Credit Suisse* nor *Trinko* prevents public antitrust agencies from acting under any of the antitrust laws when they conclude that anticompetitive conduct would otherwise escape effective regulatory scrutiny.

[37] 15 U.S.C. § 45.
[38] *See* How the Federal Trade Commission Works to Promote Competition and Benefit Consumers in a Dynamic Economy, Prepared Statement of the Federal Trade Commission Before the United States Senate Committee on the Judiciary, Subcommittee on Antitrust, Competition Policy and Consumer Rights 10-12 (June 9, 2010), *available at* http://www.ftc.gov/os/testimony/100609dynamiceconomy.pdf.

Mr. JOHNSON. Thank you, Mr. Shelanski.
Mr. Thorne?

TESTIMONY OF JOHN THORNE, SENIOR VICE PRESIDENT, VERIZON COMMUNICATIONS, INCORPORATED, ARLINGTON, VA

Mr. THORNE. Likewise, I want to thank——

Mr. JOHNSON. And, Mr. Thorne, could you make sure that that mic is on? Okay.

Mr. THORNE. Mr. Chairman, Mr. Ranking Member, Chairman Conyers, Members of the Subcommittee, thank you for inviting me to testify today, and thanks for the introduction. I want to clarify one small point: I argued the *Trinko* case in the Second Circuit, and unfortunately, I lost it. My good friend, Richard Taranto, argued it in the Supreme Court, and the Court was so impressed with his argument that there was no dissent from the decision in that case.

So I am very familiar. One effect of losing a case is you really do come to understand it well. I am familiar with the *Trinko* case. I am, unfortunately, much less familiar with *Credit Suisse*. I am not an expert in SEC regulation, and so I am not going to be able to say very much about that today.

I want to point out, as a matter of Verizon's interest in this hearing, is it is primarily as a customer. We buy—and these are rough numbers—$30 billion every year of products from other firms. We buy enormous amounts of health care, and medicine, and telecom infrastructure, and devices of various sorts to build our networks. So we are extremely focused on effective, vigorous antitrust enforcement.

And so, for example, I pointed out in my written testimony, we brought affirmative, offensive antitrust cases to enforce the antitrust laws. We believe in it that strongly.

Let me just make two quick points, and these are elaborated on in the written testimony. First of all, as I read the *Trinko* decision it did not depend on a regulatory context. The facts came out of regulation because the things that Verizon was selling to its competitors were things that had been compelled by the FTC rules under the 1996 act, so the fact-setting was a regulatory fact-setting, but the decision was straight antitrust.

The Supreme Court's decision itself said so. It said that because of the—regulation that might have been a good candidate for regulatory immunities, but because of the savings clause they weren't going to think immunity, they were just going to apply the existing antitrust precedents. That is what the Court said. So you don't have to take the Court at its word, you can ask people like the people on this panel, "What do you think the Court meant? Does its reasoning or decision go broader?"

A few years back Congress commissioned the Antitrust Modernization Commission to do a full study of how are the antitrust laws working? And in particular, one of the things that the commission was charged with looking at was, how is the intersection between antitrust and regulation going? And so there is a chapter in the Antitrust Modernization Commission's report on the intersection of antitrust and regulation, how antitrust applies with these regulated industries.

If you spend time with this, as I have done, it has got a series of findings and recommendations for congressional action peppered throughout it. They are in the gray boxes. And most of the gray boxes have an asterisk or two indicating that one or another of the members of the commission disagree with the particular consensus that the commission came up with. So it will say Cochairman Yarowsky dissented from a particular recommendation, or Commission member Kempf dissented—lots of dissents from the recommendations.

There is one—one of the findings that the commission made that was unanimous—this was a bipartisan commission, and a unanimous finding—that the *Trinko* decision—I am going to quote from it—"is best understood only as a limit on refusal-to-deal claims under Section 2 of the Sherman Act. It does not displace the role of the antitrust laws in regulated industries." So since Congress asked the commission to study how things were going and they looked at *Trinko*, their view, like mine, is *Trinko* did not displace antitrust in regulated industries.

Now, the second thing I will just say a word about, and it is elaborated on in the written testimony, is there is a series of Supreme Court decisions going back to 1920 that say—this could have been a controversial decision back in 1920, but it is well established in the subsequent 90 years—if you get to a monopoly position lawfully by being the first in the market, by having a better product, by having a government franchise—if you get to a lawful monopoly you are not required to dismantle the monopoly by giving it up to rivals.

All of the cases involving refusal-to-deal, all of the Supreme Court cases involve a situation where you are voluntarily dealing with some folks and then you discriminate against your rival. In that situation you can have antitrust liability for refusal-to-deal, but it is based on discrimination between voluntary dealing and refusal to deal with rivals or customers of rivals, and there is no Supreme Court decision that is different from what *Trinko* has said in 90 years of history on those sorts of cases.

So thank you again for the invitation, and I look forward to the questions.

[The prepared statement of Mr. Thorne follows:]

PREPARED STATEMENT OF JOHN THORNE

Testimony of John Thorne
Senior Vice President and Deputy General Counsel
Verizon

June 15, 2010

Hearing on: Is There Life After *Trinko* and *Credit Suisse*?:
The Role of Antitrust in Regulated Industries

House of Representatives
Committee on the Judiciary
Subcommittee on Courts and Competition Policy

Mr. Chairman, Mr. Ranking Member, and Members of the Subcommittee: Thank you for inviting me to testify. I am a senior vice president and deputy general counsel of Verizon, with responsibility principally for antitrust and intellectual property. In my spare time I have taught classes on telecom law at Columbia University Law School and Georgetown University Law Center, and have written a few books and articles on telecom law and antitrust. My bio is attached to this testimony.

I represented the petitioner in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), where a unanimous Supreme Court dismissed antitrust claims against a regulated company. In my testimony, I will explain that the result in *Trinko* did not depend on the regulatory context. I will then offer some brief thoughts on how antitrust and regulation can work together to protect consumers, even though antitrust and economic regulation are often at odds both in their means and goals. In the course of doing that, I'd like to make clear that *Trinko* would not preclude the bringing of cases like the 1974 government antitrust case that led to the 1982 AT&T Bell System breakup consent decree. Finally, I'd like to point out that large and successful firms (the ones most likely to be the subjects of regulation) should not be subject to special antitrust condemnation when they cut price, invest, or innovate because those actions are good for consumers.

Verizon purchases tens of billions of dollars of products and services from other companies in the U.S. and around the world, and is keenly focused on how competition keeps its own costs low. Verizon and its predecessor companies have been a plaintiff in five major antitrust cases against suppliers and others. Over the past year, we helped to organize a coalition of companies that seeks to improve the detection of antitrust offenses in order to protect and promote competition among our suppliers. Verizon supports sound antitrust enforcement because it is a beneficiary of competition.

Summary of the *Trinko* decision.

The question presented in *Trinko* was whether the extraordinary regulatory requirements imposed by the Federal Communications Commission (FCC) under the 1996 Telecom Act are also mandated by antitrust law. In its complaint, Trinko broadly alleged that Verizon violated § 2 of the Sherman Act by discriminating between itself and rivals in the use of essential "loops"—the copper wires that connect customers to switching centers:

> [Verizon] has not afforded [rivals] access to the local loop on a par with its own access. Among other things, [Verizon] has filled orders of [rival] customers after filling those for its own local phone service, has failed to fill in a timely manner, or not at all, a substantial number of orders for [rival] customers substantially identical in circumstances to its own local phone service customers for whom it has filled orders on a timely basis, and has systematically failed to inform [rivals] of the status of their customers' orders with [Verizon].[1]

[1] Amended Complaint, *Law Offices of Curtis V. Trinko, LLP v. Bell Atlantic Corp.*, No. 00-1910, *6 (SDNY filed Jan. 19, 2001).

Trinko alleged that rivals found it "difficult" to provide service "on the level that [Verizon] is able to provide to its customers."[2] Trinko sued on behalf of a putative class of all customers of rival firms.

After the district court twice dismissed the case, the Second Circuit reinstated it, using broad language to allow proof of a Sherman Act § 2 violation based on a determination that Verizon was not providing "reasonable access" to its network.[3] By the time of the Supreme Court's ruling in the case, the federal appellate courts had split sharply on whether antitrust law might impose interconnection and sharing requirements comparable to or even more far reaching than those set out in the FCC's rules. Saying no to such claims were the Fourth and Seventh Circuits—the latter, speaking through Judge Diane Wood, recognizing that these claims were different from the claims found valid in the famous 1983 *MCI v. AT&T* case.[4] Saying yes to these new claims were the Second, Ninth, and Eleventh Circuits.[5]

The Supreme Court resolved the conflict, holding without dissent that "alleged insufficient assistance in the provision of service to rivals is not a recognized antitrust claim."[6] The Supreme Court also made it clear, however, that the regulated telecom context was unimportant to that fundamental ruling. The bi-partisan Antitrust Modernization Commission explained in one of its major (and unanimous) conclusions: "*Verizon Communications[] Inc. v. Law Offices of Curtis V. Trinko LLP* is best

---

[2] *Id.* at *12.

[3] *Law Offices of Curtis V. Trinko, LLP v. Bell Atlantic Corp.*, 305 F.3d 89, 107 (2d Cir. 2002) (rejecting the district court's rationale that "a monopolist has no general duty to cooperate with its competitors," because in fact "a monopolist has a duty to provide competitors with reasonable access to 'essential facilities,' facilities under the monopolist's control and without which one cannot effectively compete").

[4] *Cavalier Telephone, LLC v. Verizon Virginia, Inc.*, 330 F.3d 176, 188 (4th Cir. 2003) (explaining that "Congress enacted §§ 251 and 252 of the Telecommunications Act to impose entirely new duties, which were in addition to the duties imposed by § 2 of the Sherman Act," and that the Telecommunications Act "obligations exceed the duties imposed by the antitrust laws"), *cert. denied*, 124 S. Ct. 1144 (2004); *Goldwasser v. Ameritech Corp.*, 222 F.3d 390, 400 (7th Cir. 2000) ("A complaint like this one, which takes the form 'X is a monopolist; X didn't help its competitors enter the market so that they could challenge its monopoly; the prices I must pay X are therefore still too high' does not state a claim under Section 2.").

[5] *Trinko*, 305 F.3d 89; *MetroNet Services Corp. v. US West Communications*, 329 F.3d 986, 1012 (9th Cir. 2003) (permitting the plaintiff to establish a § 2 claim by proving the price of available access was so high it "discourage[d]" the plaintiff "from staying in the business"); *Covad Communications Co. v. BellSouth Corp.*, 299 F.3d 1272, 1283 (11th Cir. 2002) (holding that a § 2 claim is established "when a monopolist improperly withholds access to an 'essential facility' without which a competitor cannot enter or compete in a market").

[6] *Trinko*, 540 U.S. at 410.

understood only as a limit on refusal-to-deal claims under Section 2 of the Sherman Act; it does not displace the role of antitrust laws in regulated industries."[7]

In fact, the Court began its analysis by noting that a regulatory scheme as comprehensive as the 1996 Telecom Act's would ordinarily be "a good candidate for implication of antitrust immunity, to avoid the real possibility of judgments conflicting with the agency's regulatory scheme."[8] But, the Court immediately explained, Congress had provided otherwise in the antitrust-specific savings clause found in § 601 of the 1996 Telecom Act.[9] Therefore, the Court concluded that the Act neither narrowed nor expanded existing antitrust standards.

The basis for the Court's decision in *Trinko* is unexceptionable—antitrust has never required the dismantling of lawful monopolies. The 1996 Act did impose such duties through § 251 and § 252 as those provisions have been implemented. But the 1996 Act is a comprehensive regime for making, calibrating, and flexibly adjusting the judgments that are unavoidably needed to implement a duty to share assets at special discounts. Just to contemplate the nature and scope of such judgments is to recognize that they are foreign to the historic tasks of antitrust courts. As Judge Diane Wood recognized for the Seventh Circuit, distinguishing its own 1983 *MCI* case and other cases, "[t]hese are precisely the kinds of affirmative duties to help one's competitors that . . . do not exist under the unadorned antitrust laws." 222 F.3d at 400.

The claim by Trinko would have changed § 2 into a condemnation of monopoly itself. But § 2, going back at least to the 1920 case *United States v. United States Steel Corp.*, 251 U.S. 417 (1920) (*U.S. Steel*), has not done that. *U.S. Steel* declares that § 2 "does not compel competition" and does not condemn "size."[10] Other cases have reaffirmed that possession of a monopoly, if obtained without violating the Sherman Act, is not a § 2 offense.[11] What that means is that § 2 does not compel a monopolist to give rivals a helping hand in displacing its own sales, that is, in dispossessing itself of its monopoly. Although the 1996 Act does impose a duty to create competition, § 2 of the Sherman Act has been restricted to preventing monopolists from interfering with independently arising competition through conduct that can properly be condemned.

---

[7] Antitrust Modernization Commission, REPORT AND RECOMMENDATIONS 340 (April 2007).

[8] *Trinko*, 540 U.S. at 406.

[9] Telecommunications Act of 1996 § 601(b)(1), 110 Stat. at 143 ("[N]othing in this Act or the amendments made by this Act shall be construed to modify, impair, or supersede the applicability of any of the antitrust laws.").

[10] *Id.* at 451.

[11] See, for example, *National Biscuit Co. v. FTC*, 299 F. 733 (2d Cir. 1924); *United States v. Aluminum Co. of America*, 148 F.2d 416, 430 (2d Cir. 1945) ("The successful competitor, having been urged to compete, must not be turned upon when he wins.").

The distinction between affirmative assistance and negative interference is fundamental.[12] Section 2 has never required a retailer to change itself into a wholesaler, or a service provider to transform itself into a renter of facilities.[13] In common sense and doctrinal terms, it is a legitimate business decision as a matter of law to just continue making one's sales and enjoying the fruits of one's investments, as much for a monopolist as for any other firm. In a system premised on competition, not cooperation, any firm may refuse to turn over its business to rivals, let alone refuse to create an elaborate and burdensome apparatus for entertaining the requests of every would-be intermediary that asks for a piece of the business—an apparatus that, in the context of the 1996 Act, has required billions of dollars in investments to create special ordering systems, has forced involvement of different companies to get to the bottom of service problems, and has engendered constant negotiations and disputes over the prices of individual access elements and the when and how of making them available.

There are two core reasons why § 2 has—independent of any regulatory context—never been applied to impose a duty to start sharing assets with rivals at special discounts: the institutional limits of antitrust courts and the dampening of pro-consumer investment incentives. In short, an antitrust sharing duty presents unmanageable risks of doing more harm than good—of impairing the short-run and long-run investment incentives that the Sherman Act most fundamentally protects, and of generating transaction and administrative costs that offset benefits. The antitrust system is not institutionally suited to reliably counterbalance those risks and costs. The antitrust system therefore has never taken on the challenges that are inherent in implementing duties of sharing—challenges that Justice Breyer recognized in his opinion in *AT&T*

[12] Antitrust properly focuses on *negative* duties (to avoid acts that hinder rivals' independent efforts to attract customers) and not *affirmative* ones. *See Illinois ex rel. Burris v. Panhandle Eastern Pipe Line Co.*, 935 F.2d 1469, 1484 (7th Cir. 1991) (negative/affirmative line); *Olympia Equip. Leasing Co. v. Western Union Telegraph Co.*, 797 F.2d 370, 375-76 (7th Cir. 1986) ("'There is a difference between positive and negative duties, and the antitrust laws, like other legal doctrines sounding in tort, have generally been understood to impose only the latter.'"); S. Breyer, REGULATION AND ITS REFORM 157 (1982) (antitrust laws "act negatively, through a few highly general provisions *prohibiting* certain forms of private conduct. They do not affirmatively order firms to behave in specified ways; for the most part, they tell private firms what not to do."). The distinction between acts negatively interfering with others, on one hand, and a failure to lend affirmative assistance, on the other, is fundamental elsewhere in the law. *See DeShaney v. Winnebago County Dep't of Social Servs.*, 489 U.S. 189 (1989) (relying on same line to hold that failure to provide assistance is not "deprivation" under Due Process Clause).

[13] See, for example, *Laurel Sand & Gravel, Inc. v. CSX Transportation, Inc.*, 924 F.2d 539, 545 (4th Cir. 1991) (explaining that it is not "feasible" for CSX to change its business of providing rail transportation service into a business of renting track to other railroads). *See also* Richard A. Posner, ANTITRUST LAW 224 (Chicago 2d ed. 2001): "Were vertical integration deemed a suspect practice under the antitrust laws because of its potential exclusionary effect, all commercial activity would be placed under a cloud as courts busied themselves redrawing the boundaries of firms, even though the normal motivation for and consequence of vertical integration are merely to reduce the transaction costs involved in coordinating production by means of contracts with other firms."

Corp. v. Iowa Utilities Board[14] and that the D.C. Circuit, speaking through Judge Williams, discussed in *United States Telecom Association v. FCC*[15] a few years later. These are challenges that historically have been left to regulatory regimes, not the antitrust system.[16]

Today, the 1996 Act assumes those challenges in the telecommunications setting. The 1996 Act's sharing duties require decisions about what network elements and services must be shared, at what prices, with what level of care and on what other terms, and for how long. These judgments are technically complex, requiring an understanding of the operation and economics of telecommunications networks and services. They must be based on facts and reasoned economic analysis and must operate within the statutory constraints of the 1996 Act, like any agency decisions. But the judgments are necessarily experimental. They require assessing, on the one hand, when sharing seems likely to produce the kinds of benefits contemplated by the statute—an assessment necessarily dependent on the proposed terms of the sharing—and, on the other hand, when such sharing, by making piggybacking too attractive, is likely to undermine the kind of independent competitive investment the statute seeks to promote. The judgments must be ever-changing. The 1996 Act assigns to both federal and state commissions the comprehensive task of making, and then flexibly adjusting, the necessary judgments. That separate regime highlights why the antitrust system is not suited to the task.

The only circumstance where § 2 has recognized a single-firm duty to engage in some kinds of dealing with rivals is a narrow one: where the firm has refused to sell to rivals (or rivals' customers) what the firm was already voluntarily selling to others on the desired terms. That particular kind of stark discrimination has been present in every one of the Supreme Court's cases finding liability for a refusal to deal.[17] It was also present

---

[14] 525 U.S. 366, 430 (1999) (Breyer concurring in part and dissenting in part) (explaining the difficulties of an incumbent being forced to share "virtually every aspect if its business" with its competitors, ultimately leading to "a world in which competitors would have little, if anything, to compete about").

[15] 290 F.3d 415, 429 (D.C. Cir. 2002) ("In sum, nothing in the Act appears a license to the Commission to inflict on the economy the sort of costs noted by Justice Breyer under conditions where it had no reason to think doing so would bring on a significant enhancement of competition."), *cert. denied sub nom. WorldCom, Inc. v. United States Telecom Association*, 538 U.S. 940 (2003).

[16] Then-Judge Breyer explained this in his opinion in *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990) (explaining that to impose an antitrust duty that monopolists sell inputs to rivals at "fair prices" requires the court to conclude that "the anticompetitive risks [of ignoring the monopolist's conduct] outweigh the possible benefits and the adverse administrative considerations" of intervention) (internal citations omitted).

[17] Such discrimination was present in the cases condemning unilateral refusals to deal. *See Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 459, 463 n.8 (1992) (characterizing as not a lawful "unilateral refusal to deal" the refusal by a defendant, while selling parts to customers generally, to sell parts to customers who bought service from competing service providers); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 593-94, 608, 610-11 (1985) (observing that the defendant refused to make full retail price ski-lift ticket sales to its competitor, although it was making such sales to customers generally and had previously voluntarily made such sales in collaboration with the competitor itself); *Otter Tail Power Co. v. United States*, 410 U.S. 366, 371, 378 (1973) (involving a defendant who refused to

in the Seventh Circuit's *MCI Communications Corp. v. AT&T*,[18] apparently the first and only case of liability for unilateral firm conduct under the "essential facilities doctrine."[19]

The discrimination situation—the stark refusal to make available to competitors (or their customers) the very services and terms being voluntarily made available to other customers—has been the precondition to demanding of a monopolist an explanation for a refusal to share: if you are selling this to others at a price that is profitable and lets you recoup your investment, what reason is there for not selling the same thing at the same price to a rival? There might be answers—differential treatment can be justified; it is not by itself illegal—but without that discrimination there has not been liability for refusals to share. In the discrimination situation, the two basic objections to antitrust duties to deal are weakened. First, where the defendant is already voluntarily offering the desired terms, there is no antitrust intrusion on the basic competitive choices of (a) what to sell and (b) at what price—the choices through which a firm enjoys the rewards of successful investments. There is, accordingly, much less reason to worry about deterring long-run and short-run investments by requiring the results to be shared. Second, the institutional task for courts is much more manageable in this situation. The voluntary sales to others furnish a standard of conduct—equality—that the courts do not have to define on their own.

The situation is sharply different where a claim is made for sharing on newly forced terms (as opposed to terms already being offered voluntarily)—making sense of why § 2 has never recognized such a claim. Any effort to demand sharing of assets on new terms requires definition of those terms and in particular the setting of "fair" prices, to strike a balance so as not to do more harm than good, both in the long run and in the short run. This is a task antitrust law has never undertaken because it is something antitrust juries and judges, through a treble damages system, cannot reliably do—as Justice Breyer explained when he was a First Circuit judge.[20]

---

wheel power for certain local-distribution competitors even though it was in the business of wheeling power for other such customers); *Lorain Journal Co. v. United States*, 342 U.S. 143, 149-50 (1951) (involving a defendant newspaper publisher's flat refusal to sell advertising space, otherwise generally available to all advertisers, to parties who advertised on a competing radio station); *Eastman Kodak Co. v. Southern Photo Materials Co.*, 273 U.S. 359, 368-69, 375 (1927) (involving a defendant manufacturer that suddenly "refused" to sell to the plaintiff dealer "on the same terms as other dealers"). Such discrimination also was present in the concerted action cases of *United States v. Terminal Railroad Association*, 224 U.S. 383, 394 (1912) (involving a multiparty agreement for operating a terminal railroad facility, in which members discriminated against nonmembers), and *Associated Press v. United States*, 326 U.S. 1, 10-11 (1945) (involving a multiparty agreement that openly discriminated between those who would compete against existing members and those who would not).

[18] 708 F.2d 1081, 1144 (7th Cir. 1983) (upholding liability based on AT&T's refusal to sell to MCI, as a competitor, the very same connections that AT&T was already in the business of offering to "local customers, independent telephone companies and others").

[19] That doctrine, as *Trinko* noted, is not a Supreme Court doctrine. 540 U.S. at 411 ("We have never recognized such a doctrine . . . and we find no need either to recognize it or to repudiate it here.").

[20] In *Town of Concord*, 915 F.2d at 25, then-Judge Breyer stressed the near impossibility for antitrust courts attempting to set prices of monopoly inputs sold to rivals:

In the long run, investment incentives would be threatened by a § 2 rule that says firms must share the rewards if their investments are successful enough. The essence of the *U.S. Steel* point about the limited reach of § 2 is that antitrust respects that truth.[21]

Even in the short run, there are multiple problems with sharing duties—as recognized in the FCC's orders implementing these duties under the 1996 Act and in the opinions of Justice Breyer, Judge Wood, and Judge Williams mentioned above. First: a duty to share assets risks diminishing the incumbent's investments in creating those assets in the first place, and in maintaining and upgrading them, for the rewards must be shared but not the risks. For example, local telephone networks require continuing investment; they require the constant attention of tens of thousands of employees and billions of dollars of investment. Second: a duty to share risks deterring independent investments by new entrants; sharing may be cheaper, and is certainly less risky, than investing in one's own facilities. Third: a duty of incumbents to share can harm the best new entrants, those who do build their own facilities; they are faced with competition not just from the incumbent but from all the rivals who can cheaply share the incumbent's assets. On top of these risks, the costs of implementing and administering any sharing duty can be very substantial, so that any market benefits must be large enough to exceed those costs. And: if the incumbent cannot reliably determine the required sharing terms in advance—if there are vague legal standards requiring years of costly and uncertain litigation—the risk of retrospective treble damages skews choices toward overgenerous sharing that further deters pro-consumer investments.

For all of these reasons, Section 2 of the Sherman Act has never imposed the kind of affirmative duties to assist rivals that were urged by the plaintiff in *Trinko*. The Supreme Court so concluded entirely independent of the existence of the regulatory regime established in the 1996 Act. And the reasons for not recognizing such Section 2

> Judge Hand's price squeeze test . . . makes it unlawful for a monopolist to charge more than a "fair price" for the primary product while simultaneously charging so little for the secondary product that its second-level competitors cannot make a "living profit." But how is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" Must it be large enough for all independent competing firms to make a "living profit," no matter how inefficient they may be? If not, how does one identify the "inefficient" firms? And how should the court respond when costs or demands change over time, as they inevitably will? We do not say that these questions are unanswerable, but we have said enough to show why antitrust courts normally avoid direct price administration.

[21] *See* Einer Elhauge, *Defining Better Monopolization Standards*, 56 Stan. L. Rev. 253, 278 (2003) ("If there were no right to exclude others from the fruits of investments made in the property, then the property right cannot provide the encouragement to invest that is the main purpose for recognizing property rights to begin with."). *See also U.S. Steel*, 251 U.S. at 452-53 (noting that equitable "discretion" in reviewing an antitrust decree requires respect for investments); *Standard Oil Co. v. United States*, 221 U.S. 1, 78 (1911) ("[O]ne of the fundamental purposes of the statute is to protect, not to destroy, rights of property.").

duties are compelling even apart from the existence of that regulatory regime. The Court then explained that the existence of the 1996 Act regime, a separate, non-antitrust avenue for the assertion of assistance duties, was one additional reason, if one were needed, for the Court to refrain from *adding such new duties* to Section 2.

Observations about regulation:

The general question for today's panel is how antitrust should apply to already-regulated industries. *Trinko*'s limited use of regulation—as a reason not to add a previously unrecognized Section 2 duty—is one quite proper use of regulation. The more challenging situation involves the question of relying on regulation to limit otherwise-established antitrust duties. I was not involved in the *Credit Suisse* case, which found a very context-specific conflict between a securities regulatory regime and a particular antitrust claim, a conflict that the SEC itself (though not the Justice Department's Antitrust Division) thought severe enough to require displacement of the latter in favor of the former. I cannot speak to that narrow result, so my observations here are general. Most important, I believe that the claim that there is some easy harmony to be achieved between antitrust and regulation is false. Regulation and antitrust differ not only in their details. Regulation is often contrary to antitrust either in its ends, in its means, or in both.

1. The goals of regulation and antitrust can be directly adverse.

Economic regulation can choose ends that are actually at odds with antitrust. Instead of promoting free markets, regulation may prohibit competition, whether to ensure subsidization of high-cost services or for other reasons. It may restrict entry, control price, skew investment (causing too much or too little), and limit innovation (delaying innovations by subjecting them to regulatory approval, barring marketing of innovations, or forcing innovations to be shared with rivals on regulated terms). There are many, many examples. Here are two:

<u>Telephones</u>. The early history of the telephone industry was characterized by cradle-to-grave regulation. Entry was forbidden. Prices were regulated. Investment initially was encouraged, some observers claim over-encouraged ("gold-plated"), by the prospect of guaranteed recovery of prudently-incurred costs. Investment later was discouraged by requirements that facilities be shared at super-low prices. Innovations were delayed while regulators scrutinized them. A simple innovation like letting phone lines carry data communications required multiple lengthy FCC proceedings before it could be offered.

The 1974 government antitrust case that led to the 1982 AT&T Bell System breakup consent decree was at its core attacking a market structure that had been created by regulation. The Justice Department antitrust case sought to correct market harms that had been not only tolerated but encouraged and imposed by federal and state utility regulators. *Trinko* would not preclude the government bringing a similar case today. In briefing the *Trinko* case to the Supreme Court, Verizon did not argue that the government's case 1974 against the Bell System was incorrect. Instead, we showed how dismissal of Trinko's complaint was consistent with the parallel result in the Seventh Circuit's approval of a limited refusal-to-deal claim brought by MCI against AT&T—a consistency Judge Wood had likewise found in her opinion for the Seventh Circuit in *Goldwasser*. Notably, the *MCI* case involved AT&T's flat refusal to connect MCI's independent long-distance facilities to AT&T's local network, even though AT&T was selling such connections for the very same services to other "'independent telephone companies.'"[22]

Cable TV. The multichannel video market was long kept non-competitive by regulation. The 1984 Cable Act prohibited telephone companies from competing with cable TV operators. When that ban was struck down as a First Amendment violation in the lower courts and then removed by Congress in the 1996 Telecom Act, incumbent cable TV operators asserted that the telephone rivals must obtain cable franchises, one by one, from thousands of local municipalities before they may compete. This has slowed down entry by Verizon's superior FiOS TV service. At the urging of incumbent cable operators, several states have increased the burdens of obtaining franchises with so-called "level playing field" laws.[23]

Verizon filed an antitrust and First Amendment case against one of the municipalities that was making it difficult to enter in competition against the incumbent cable monopolist. Despite the regulated context, we did not believe our case was precluded by *Trinko*. The case was promptly settled with the result that Verizon is now able to compete in the particular local market, and therefore we did not establish a legal precedent.

2. Even when regulation and antitrust have the same goals, regulators may choose methods that sometimes are substantively contrary to antitrust – indeed, regulatory methods may tend to preserve monopolies.

Ordinary public utility regulation may bear "a strong resemblance" to competition in ultimate objectives: it often is designed to produce the same end result, in particular certain pricing levels, that a competitive process would produce.[24] But the compatibility

[22] Brief for Petitioner Verizon at 42, *Verizon Comm. Inc. v. Law Offices of Curtis V. Trinko LLP*, No. 02-682 (May 23, 2003) (quoting 708 F.2d at 1144 and FCC decision). In fact, Trinko's demand was that Verizon "'fill in the gaps in its competitor's network,'" a duty the Seventh Circuit in *MCI* specifically rejected, and that Verizon do this gap-filling by giving up the opportunity to use the facilities surrendered, which *MCI* specifically did not require.

[23] *See* Thomas W. Hazlett & George S. Ford, *The Fallacy of Regulatory Symmetry: An Economic Analysis of the "Level Playing Field" in Cable TV Franchising Statutes*, 3 Bus. & Politics 21, 43 (2001) (describing the entry inhibitions of the level-playing-field statutes and cable incumbents' "strategic use of administrative processes to thwart entry" and preserve "a monopolistic equilibrium"). One Wall Street analyst observed that "[c]able providers are aware of the protective effects franchise requirements have and regularly tell their investors how the process will prevent near term competitive entry by the Bells." J. Hodulik, UBS, *Franchise Fight Likely To Delay Video Competition* at 3 (May 2, 2005).

[24] Alfred E. Kahn, 1 THE ECONOMICS OF REGULATION 63 (MIT reprint 1988).

of the desired end results does not mean that antitrust can borrow from regulation in defining duties. Even when the goals of antitrust and regulation are the same, their methods are very different. Antitrust fosters a competitive process. Regulation compels specific results. A few examples illustrate the difference:

Acquiring or continuing a monopoly. Antitrust does not require dismantling of a lawful monopoly.[25] Regulation may require dismantling.

Pricing. Antitrust does not require a monopolist to charge less than a monopoly price.[26] Regulation typically restricts price to some measure of costs.

Dealing. Antitrust generally does not require affirmative dealing with others.[27] Regulation often does. Common carriers by definition must deal with all customers.

Mergers. The antitrust agencies evaluate whether a merger will harm competition. If there is no likely harm, the agency doesn't challenge the merger. By contrast, the FCC requires mergers affirmatively to serve the public interest. This leads the FCC to impose conditions well beyond what either DOJ or the FTC thinks is needed to approve a merger.

Ironically, regulation that imposes a "competitive" *result* can have the effect of preventing competition itself. For example, the swiftest and surest way to end a monopoly is to let it charge a high price; high prices attract entry. Conversely, forcing a monopolist to share its productive facilities with rivals at low prices results in shared monopoly, and will deter rivals' independent investments in competing facilities.[28] Treating the symptoms of monopoly thus may keep it intact longer.

---

[25] *Trinko*, 540 U.S. at 407 ("To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive *conduct*."); *United States v. United States Steel Corp.*, 251 U.S. 417, 451 (1920) (Section 2 "does not compel competition"); *Eastman Kodak Co. Image Tech. Servs., Inc.*, 504 U.S. 451, 480 (1992) (power plus *conduct*); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 596 n.19 (1985); *United States v. Microsoft Corp.*, 253 F.3d 34, 51, 58 (D.C. Cir. 2001) (*en banc*) ("merely possessing monopoly power is not itself an antitrust violation"; "having a monopoly does not by itself violate § 2"; "'the successful competitor, having been urged to compete, must not be turned on when he wins,'" quoting *United States v. Aluminum Co. of America*, 148 F.2d 416, 430 (2d Cir. 1945) (L. Hand, J.)).

[26] *Trinko*, 540 U.S. at 407 ("charging of monopoly prices, is not ... unlawful").

[27] *Trinko*, 540 U.S. at 408 ("as a general matter, the Sherman Act 'does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal,'" quoting *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)).

[28] For example, a prominent former FCC economist has shown that the European model for broadband infrastructure sharing depresses investment. Scott J. Wallsten and Stephanie Hausladen, *Net Neutrality, Unbundling, and their Effects on International Investment in Next-Generation Networks* 107 (March 2009).

3. Regulation more readily admits of fine-tuning.

As discussed above, regulation operates procedurally very differently than antitrust. Regulation can be experimental, trying one approach, then another, changing course as the results are seen. Regulatory enforcement mechanisms can be calibrated to provide incentives that motivate desired conduct, making adjustments with experience. Enforcement penalties can be closely tied to the substance of the regulatory duties, with care taken that beneficial conduct such as price-cutting, investment, and innovation is not deterred by excessive or imprecisely administered penalties (which would cause the regulated firm to avoid entire areas out of caution). The administrative agency gains experience over time, and the same agency will be there to revisit specific requirements that prove ineffective or counterproductive.

Antitrust is substantively less fine-tuned and procedurally less fine-tunable. It forbids "monopolization" and restraints that are "unreasonable." Its enforcement, involving juries, class actions, and treble damages, is a potent but imprecise deterrent, making it important not to point this weapon in the direction of normally pro-competitive behaviors. The administration of antitrust by single-case lay juries means there is usually no opportunity to gain industry-specific expertise or to make adjustments in light of experience. In particular, a common-law antitrust process is not able reliably to make the right judgments about how much sharing and on what terms will do more good than harm.[29]

Consider the regulatory regime at issue in the *Trinko* case. Trinko alleged that Verizon failed to send prompt acknowledgements of rivals' orders for unbundled telephone lines. A precise specification of what Verizon was supposed to do was contained in three documents: (1) an interconnection agreement between Verizon and Trinko's carrier, AT&T; (2) Carrier-to-Carrier Guidelines established jointly by Verizon, its rivals (known in industry jargon as "CLECs"), and the New York Public Service Commission; and (3) a state-commission administered Performance Assurance Plan that defines automatic penalties to be paid to the CLECs for performance deficiencies. For example, performance measure "OR-8" requires Verizon to check each CLEC order to ensure it is "valid and complete" and then to return an acknowledgement to the CLEC within two hours, 95% of the time. The penalty for missing this performance measure was set with regard to the size of the performance shortfall, its effect on the CLEC business, and whether Verizon had missed this measure in the past. The state commission retained discretion to adjust the weights of penalties up or down as experience was gained.

The regulatory enforcement regime in New York, where Trinko's office is located, put at risk a sizeable fraction of Verizon's annual profits. The FCC approved the New York enforcement regime as potent: "We believe it is useful to compare the

---

[29] The common law reluctance to define and enforce terms on which mandated sharing of monopolist facilities with aspiring competitors is to be afforded, based only on general standards, is over a century old. *Express Cases*, 117 U.S. 1, 28-29 (1886).

maximum liability level to Bell Atlantic's net revenues derived from local exchange service – after all, it is primarily its local service profits that Bell Atlantic would have a theoretical incentive to 'protect' by discriminating against competing local carriers. * * * In 1998, Bell Atlantic reported a Net Return of $743 million in New York: $269 million [the amount then at risk under the Performance Assurance Plan] would represent 36% of this amount."[30]

There are profound problems accompanying calibration of any sharing duties. Excessive sharing (a) undermines the incentive of the regulated firm to invest in creating or maintaining or upgrading facilities (the entire risk is borne by the regulated firm, but rewards must be shared); (b) undermines the incentive of rivals to build or buy when renting at low prices from the regulated firm is cheaper and less risky (the regulated firm is stuck with the facility if demand is disappointing); and (c) harms *facilities-building* rivals, whose investments (*e.g.*, more efficient than the regulated firm but perhaps not as efficient as possible) must compete against rivals renting from the regulated firm at super-low prices. One of the strongest amicus briefs in the Supreme Court in *Trinko* came from the equipment manufacturers, who just want the market to grow so they can sell more equipment. The manufacturers argued that excessive sharing requirements were depressing investments by both the incumbents and new rivals.[31]

The above observations lead me to two conclusions:

Conclusion #1: Antitrust should not be rewritten or interpreted to encompass specific regulatory requirements.

As discussed above, there are two kinds of reasons that courts cannot soundly borrow violations of regulatory duties to define antitrust violations.[32]

First, the substantive policies are fundamentally different in what they do about the ideal of "competition." For example, in telephones, the 1996 Act seeks to "jumpstart" competition and "uproot" monopolies; antitrust does neither. The choices made under the 1996 Act about terms of sharing (including the all-but-confiscatorily low

[30] Application of Verizon New York, 15 FCCR 3953 (1999), ¶ 436. The available annual penalty under the New York plan subsequently was increased to $293 million although Verizon's profits from the state had declined. At the time of the *Trinko* decision, the total of available annual penalties in Verizon's states (not counting New Jersey) was $1.24 billion. New Jersey had no annual cap on the penalties that could be incurred.

[31] Amicus Brief of Telecommunications Industry Ass'n, 16 & n.6 (U.S. May 23, 2003) (citing Telecom. Industry Ass'n., 2003 Telecommunications Market Review and Forecast at 55, 60 (2003)).

[32] As the Supreme Court explained in *Trinko*, under the 1996 Telecommunications Act, there is also a textual reason for not incorporating regulatory duties into antitrust: The savings clause precludes using the new regulatory duties to "modify" (add to) pre-existing antitrust duties. It declares that Congress was *not* treating the new 1996 Act duties as if they defined a new standard for "restraint of trade" or "monopolizing" conduct under the Sherman Act. *Compare Robertson v. Seattle Audubon Soc'y*, 503 U.S. 429, 439-40 (1992) (law deeming certain conduct to come within prior statute "modified" prior statute).

prices) are *not* the choices antitrust makes. Most notably, antitrust does *not* require below-monopoly pricing for any sharing. The Supreme Court has specifically cautioned against confusing antitrust wrongs with other wrongs, including even the evasion of regulatory controls on exploitation of a monopoly.[33]

Second, enforcement systems differ. Agency decision-makers are able to act flexibly and prospectively and use calibrated penalties (*e.g.*, the 1996 Act regime), whereas juries act retrospectively through severe treble-damages penalties and judges adopt injunctions that typically are difficult to modify. Thus the Supreme Court has recognized that substantive policy choices now go hand in glove with particular enforcement regimes.[34] Respect for differences in implementation and remedial choices is most important when a regulatory regime "comes as close to the line of overregulation as possible–that is, to achieve the benefits of regulation right up to the point where the costs of further benefits exceed the value of those benefits."[35] The remedial choices of specific statutes thus trigger the principle that the "specific governs the general."[36] And antitrust litigation would inevitably operate as an "extraneous pull" on agency processes themselves (*Buckman Co. v. Plaintiffs' Legal Committee*, 531 U.S. 341, 353 (2001)), distorting the choices of participants and decision-makers alike.

Accordingly, because regulatory determinations are deeply experimental and uncertain, and price regulation in particular "inevitably distorts the incentive to reduce costs or engage in further innovation" and tends to chill new entry that higher prices

---

[33] *NYNEX v. Discon*, 525 U.S. 128, 136, 137 (1998). That violations of other standards overlap *as a matter of fact* with violations of antitrust standards (*see* ABA, Antitrust Law Developments 249 (5th ed. 2002)) does not mean that wrongfulness under the former is the reason, or even a reason, for finding the conduct wrongful under antitrust. An examination of the ABA statement and its footnote support confirms that it is, at best, a description of *de facto* overlap.

[34] *See* R. Fallon, D. Meltzer & D. Shapiro, *Hart & Wechsler's The Federal Courts and The Federal System* 841-42 (4th ed. 1996). In many contexts since the 1970s, the Court has rejected the notion that it is better, or even permissible, to add remedies to those Congress chose for particular statutory violations, recognizing the importance of congressional *remedial* choices, such as whether agencies (or numerous individual judges or juries) resolve disputes under potentially open-ended standards, and what remedies attach to violations. *See, e.g.*, *Alexander v. Sandoval*, 532 U.S. 275, 290 (2001); *Karahalios v. Nat'l Fed. of Federal Employees*, 489 U.S. 527, 533 (1989); *Merrell Dow Pharmaceuticals Inc. v. Thompson*, 478 U.S. 804 (1986); *Massachusetts Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 145, 146-147 (1985); *Middlesex County Sewerage Auth. v. Nat'l Sea Clammers Assn.*, 453 U.S. 1, 19-20 (1981); *Northwest Airlines, Inc. v. Transport Wkrs.*, 451 U.S. 77, 93-94 (1981); *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 19-20 (1979).

[35] Easterbrook, *Statutes' Domains*, 50 U. Chi. L. Rev. 533, 541 (1983).

[36] *Varity Corp. v. Howe*, 516 U.S. 489, 511-12 (1996); *see Patterson v. McLean Credit Union*, 491 U.S. 164, 180-82 (1989) (refusing "'to read an earlier statute broadly where the result is to circumvent the detailed remedial scheme constructed in a later statute'").

might attract, "[a]ntitrust courts have rightly resisted undertaking the heavy, continuous, and unguided burden of supervising the economic performance of business firms."[37]

Conclusion #2: Antitrust should not condemn large, successful firms for pro-competitive behaviors.

I want to emphasize a final point. Regulation sometimes inhibits large and successful firms from engaging in pro-competitive behaviors such as cutting prices, innovating, and investing. There is a popular view that antitrust, too, should specially scrutinize these behaviors by large firms because cutting prices, etc., can injure rivals.

That view is wrong. As a general rule, when non-dominant firms are observed commonly engaging in a particular form of conduct in the marketplace, such conduct should be presumptively permissible for a large firm also:

> If the practice is one employed widely in industries that resemble the monopolist's but are competitive, there should be a presumption that the monopolist is entitled to use it as well. For its widespread use implies that it has significant economizing properties, which implies in turn that to forbid the monopolist to use it will drive up his costs and so his optimum monopoly price.[38]

---

[37] 3 P. Areeda & H. Hovenkamp, ANTITRUST LAW ¶ 720b at 256 (2d ed. 2000) (footnote omitted, noting rare exceptions embodied in judicial decrees); *United States v. Trenton Potteries Co.*, 273 U.S. 392, 397-98 (1927) (recognizing problems with antitrust price administration); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 283 (6th Cir. 1898) (Taft, J.) (to examine reasonableness of price is to "set sail on a sea of doubt"); *see Image Technical Servs., Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1225 (9th Cir. 1997) (rejecting even a remedial "reasonable price" order, restricting order to "nondiscriminatory pricing"); *City of Milwaukee v. Illinois*, 451 U.S. 304, 325 (1981) ("Not only are the technical problems difficult–doubtless the reason Congress vested authority to administer the Act in administrative agencies possessing the necessary expertise–but the general area is particularly unsuited to the approach inevitable under a regime of federal common law."). *See also Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990).

[38] Richard A. Posner, ANTITRUST LAW 253 (2d ed. 2001); *see* Richard A. Epstein, *Monopoly Dominance or Level Playing Field? The New Antitrust Paradox*, 72 U. Chi. L. Rev. 49, 60 (2005) ("[T]he appropriate assumption is that these practices offer some efficiencies that improve the gains from trade, even if a reviewing court cannot quite understand exactly why these practices survive or how they work."); David S. Evans & A. Jorge Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 81 (2005) ("[N]ondominant firms regularly engage in unilateral practices challenged under the antitrust laws. These include tying; vertical restraints such as exclusive contracts and exclusive territories; nonlinear pricing, including loyalty discounts; and aggressive price cutting. Practices that generate efficiencies where firms lack market power logically should generate those same efficiencies where firms possess market power. There is no economic reason to believe that these efficiencies become less important as firms acquire market power. We therefore presume these practices are procompetitive, even if practiced by firms with monopoly power, unless shown otherwise."); *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 223-26 (1993) (adopting predatory pricing test for measuring the legality of single-product discounts by dominant firms); U.S. Br. in *3M v. LePage's*, 10 n.6, 14 n.11 (U.S. filed May 2004) (*Brooke Group* "plainly" applies to dominant firm pricing).

Monopolists, of all firms, should be *encouraged* to lower prices (to still-above-cost levels), invest, and innovate because by definition full market pressure to do so is missing, and there are more customers who stand to benefit.

Mr. JOHNSON. Thank you, Mr. Thorne.
Professor Lemley?

TESTIMONY OF MARK A. LEMLEY, WILLIAM H. NEUKOM PROFESSOR OF LAW, STANFORD UNIVERSITY, SCHOOL OF LAW, STANFORD, CA

Mr. LEMLEY. Thank you, Mr. Chairman, Ranking Member Coble, Members of the Subcommittee. I appreciate the invitation to speak here, and I want to start by saying that I agree, Mr. Chairman, with what you said in your opening statement.

I think it is right to say that the antitrust law traditionally opposed implied repeal of antitrust law by regulation, that that policy is a good one because it protects important competition interests in circumstances where regulated industries—where regulators—might not protect those interests. And I will also agree with you that that wise policy is under attack as a result of the *Trinko*, and particularly the *Credit Suisse* decisions, because the Supreme Court in the last 10 years seems to have backed off from the rule—longstanding rule—that there is no implied repeal of the antitrust laws in government regulation.

What I want to spend my time today talking about just briefly is one of the unfortunate consequences, which is the problem that I call regulatory gaming. There are a number of circumstances in which private parties engage in behavior that harnesses pro-competitive or neutral regulations and uses them for exclusionary purposes.

In the paper that is attached to my testimony, Stacey Dogan and I identify a number of those circumstances. Let me just give two examples: one is the Unocal case, in which the—an oil company participated before a government-run standard-setting organization to set air quality standards in California, persuaded the government to adopt as a mandatory rule a particular set of air quality standards, and then revealed that it had a patent covering that particular technology and no one else could use it unless they paid a super-competitive price.

Another example involves the pharmaceutical industry, which is engaged in a variety of techniques designed to try to extend the life of its patents covering certain drugs. One particular example involves so-called product-hopping, in which pharmaceutical patent owners make minor changes to their products that don't affect their FDA regulatory approval but make it impossible under the Hatch-Waxman Act for generic manufacturers to substitute generic drugs that are cheaper for those patented products.

The difficulty here is that these are actions which, in the absence of a regulatory system, wouldn't exist. There wouldn't be a problem but for the fact that the government regulation helps the gaming to take effect. It gives it cover. It gives it monopoly power. It gives it mandatory authority.

And in those circumstances where the regulation itself is not restricting competition but private action is restricting competition, antitrust law can and should step in. The worry is that under *Credit Suisse* and *Trinko* the reasoning of the Supreme Court suggests that antitrust law needs to back off, it needs to defer to the regulatory agency not just in circumstances where the regulatory agency has made an affirmative decision to restrict competition, but even in circumstances where the regulatory agency has merely been silent—has not acted—and I think that is a mistake.

Now, Mr. Chairman, you suggested correctly that we have long had a maxim in antitrust law that courts wouldn't assume the passage of a particular regulation impliedly repealed or limited the reach of that antitrust law. And I think that maxim is correct, and if the Supreme Court is no longer properly applying it the right solution, it seems to me, is to reverse the presumption.

Rather than simply having individual savings clauses in particular regulatory statutes, which seems in recent years to have been effective, we might consider a more general amendment to the antitrust law along the following lines: No regulation or act of Congress shall be interpreted to restrict or repeal the antitrust laws unless it expressly so provides.

And a provision along those lines would serve the same purpose—it would enact the no implied repeal rule—but it would effectively reverse the presumption. Rather than asking in any particular case, "Did Congress intend this regulation to change the antitrust laws?" the rule would be that unless Congress expressly said, "Here is an exemption from the antitrust laws," courts wouldn't be allowed to create one. And I think that would be wise policy.

[The prepared statement of Mr. Lemley follows:]

PREPARED STATEMENT OF MARK A. LEMLEY

Testimony of Mark A. Lemley, Stanford Law School

Is There Life After *Trinko* and *Credit Suisse*?
Hearing Before the House Subcommittee on Courts and Competition Policy, Committee on the Judiciary, June 15, 2010

Antitrust law promotes competition in the service of economic efficiency. Government regulation may or may not promote either competition or efficiency, depending on both the goals of the agency and the effects of industry "capture." Antitrust courts have long included regulated industries within their purview, working to ensure that regulated industries could not use the limits that regulation imposes on the normal competitive process to achieve anticompetitive ends. Doing so makes sense; an antitrust law that ignored anticompetitive behavior in any regulated industry would be a law full of holes.

The role of antitrust in policing regulated industries appears to be changing, however. A cluster of Supreme Court decisions in the past decade have fundamentally altered the relationship between antitrust and regulation, placing antitrust law in a subordinate relationship that, some have argued, requires it to defer not just to regulatory decisions but perhaps even to the silence of regulatory agencies in their areas of expertise. The most notable cases in this group are *Trinko* and *Credit Suisse*.

Absolute antitrust deference to regulatory agencies makes little sense as a matter either of economics or experience. Economic theory teaches that antitrust courts are better equipped than regulators to assure efficient outcomes in many circumstances. Public choice theory - and long experience - suggests that agencies that start out trying to limit problematic behavior by industries often end up condoning that behavior and even insulating those industries from market forces. And as history has shown, relying on regulatory oversight alone without the backdrop of antitrust law would leave both temporal and substantive gaps in enforcement, which unscrupulous competitors could exploit to the clear detriment of consumers. The mere existence of a competition-conscious regulatory structure cannot guarantee against abuses of that structure, or against exclusionary behavior that falls just beyond its jurisdiction. Indeed - and perhaps ironically - the very regulatory structure that exists to promote competition can create gaming opportunities for competitors bent on achieving anti-competitive goals. Such "regulatory gaming" undermines both the regulatory system itself and the longstanding complementary relationship between regulatory and antitrust law.

The risk of regulatory gaming provides an important example of the need for ongoing antitrust oversight of regulated industries. Regulatory gaming is private behavior that harnesses pro-competitive or neutral regulations and uses them for exclusionary purposes. In the attached paper, Stacey Dogan and I identify three instances of regulatory gaming: (1) product-hopping, in which the branded company makes repeated changes in drug formulation to prevent generic substitution, rather than to improve the efficacy of the drug product; (2) manipulation of government standard-setting organizations to push a technical standard that excludes competitor products; and (3) price squeezes by partially regulated industries that exclude competition in the unregulated product sector.

My goal here is not to argue that these particular examples of regulatory gaming do or do not violate the antitrust laws. Rather, my point is that whether or not particular acts of regulatory gaming harm competition is and should be an antitrust question, not merely one that involves interpreting statutes or agency regulations. Some level of antitrust enforcement - with appropriate deference to firm decisions about product design and affirmative regulatory decisions that affect market conditions - provides a necessary check on behavior, such as product hopping, that has no purpose but to exclude competition.

Until the past decade, it was a well-established maxim of antitrust law that courts would not assume the passage of a particular regulation impliedly repealed or limited the reach of antitrust law. The Supreme Court abandoned that maxim in *Trinko* and *Credit Suisse*. While the Supreme Court could reverse ground and permit antitrust scrutiny of regulatory gaming, the recent trend in its cases makes that unlikely. I believe Congress should act to preserve the traditional role of antitrust law in the face of regulation. The most straightforward way to do so would be to enact that time-honored maxim as law.

As a result, I offer the following possible amendment to the Sherman Act for the Subcommittee's consideration:

"No regulation or Act of Congress shall be interpreted to restrict or repeal the antitrust laws unless it expressly so provides."

ATTACHMENT

Antitrust Law and Regulatory Gaming

Stacey L. Dogan and Mark A. Lamley

John M. Olin Program in Law and Economics
Stanford Law School
Working Paper No. 367
October 2008

Antitrust Law and Regulatory Gaming[1]

Stacey L. Dogan[2] and Mark A. Lemley[3]

Antitrust law promotes competition in the service of economic efficiency. Government regulation may or may not promote either competition or efficiency, depending on both the goals of the agency and the effects of industry "capture." Antitrust courts have long included regulated industries within their purview, working to ensure that regulated industries could not use the limits that regulation imposes on the normal competitive process to achieve anticompetitive ends.[4] Doing so makes sense; an antitrust law that ignored anticompetitive behavior in any regulated industry would be a law full of holes.

The role of antitrust in policing regulated industries appears to be changing, however. A cluster of Supreme Court decisions in the past decade have fundamentally altered the relationship between antitrust and regulation, placing antitrust law in a subordinate relationship that, some have argued, requires it to defer not just to regulatory decisions but perhaps even to the silence of regulatory agencies in their areas of expertise.[5] While many of those decisions

2 Professor of Law, Northeastern University.

3 William H. Neukom Professor, Stanford Law School; of counsel, Keker & Van Nest LLP. Thanks to Tim Schneider, research assistant extraordinaire, and to Rose Hagan, Scott Hemphill and participants in a conference at the University of Minnesota School of Law for comments on an earlier draft.

4 *See, e.g.*, Otter Tail Power Co. v. United States, 410 U.S. 366 (1973); Northeastern Tel. Co. v. AT&T, 651 F.2d 76 (2d Cir. 1981); *see generally* Philip J. Weiser, *The Relationship of Antitrust and Regulation in a Deregulatory Era*, 50 **Antitrust Bull**. 549 (2005).

5 Credit Suisse First Boston Ltd. v. Billing, 127 S.Ct. 2383 (2007); *cf.* Nynex Corp. v. Discon, Inc., 525 U.S. 128 (1998); Verizon v. Trinko, 540 U.S. 398 (2004).

might be justified on their facts as a matter of antitrust law,[6] together they are leading courts and commentators to conclude that the antitrust laws are impliedly repealed by government regulation of a particular industry.[7] The new vogue for antitrust deference will come to a head in 2009, when the Supreme Court decides *Pacific Bell v. linkLine*, which raises the question whether a regulated monopoly with franchised rights of way violates the antitrust laws by engaging in a "price squeeze": charging broadband competitors wholesale prices for use of the right of way that exceed the retail prices its own subsidiary charges its customers.[8]

Absolute antitrust deference to regulatory agencies makes little sense as a matter either of economics or experience. Economic theory teaches that antitrust courts are better equipped than regulators to assure efficient outcomes in many circumstances. Public choice theory – and long experience – suggests that agencies that start out trying to limit problematic behavior by industries often end up condoning that behavior and even insulating those industries from market forces. And as history has shown, relying on regulatory oversight alone without the backdrop of antitrust law would leave both temporal and substantive gaps in enforcement, which unscrupulous competitors could exploit to the clear detriment of consumers.[9] The mere

---

[6] *See, e.g.*, CreditSuisse Securities, LLC v. Billing, 127 S.Ct. 2383, 2390 (2007) (Stevens, concurring) ("I … would hold … that the defendants' alleged conduct does not violate the antitrust laws, rather than holding that Congress has implicitly granted them immunity from those laws."). The exception is *Trinko*, which arguably produced anticompetitive results and which certainly misinterpreted prior law. *See infra* text accompanying notes __-__.

[7] Bruce H. Kobayashi & Joshua D. Wright, *Federalism, Substantive Preemption, and Limits on Antitrust: An Application to Patent Holdup* (working paper 2008); *cf.* Rambus, Inc. v. FTC, 522 F.3d 456 (D.C. Cir. 2008).

[8] linkLine Communications, Inc., v. SBC California, Inc., 503 F.3d 876 (9th Cir. 2007), *cert. granted sub nom.*, Pacific Bell Telephone Co. v. linkLine Communications, Inc., __ U.S. __, 128 S.Ct. 2957 (2008).

[9] Indeed, *Trinko* itself arguably illustrates the phenomenon of monopolists abusing their position in the face of ineffective regulatory oversight. *See generally* Spencer Weber Waller, *Microsoft and Trinko: A Tale of Two Courts*, 2006 UTAH L. REV. 741, 753-55 (2006)

existence of a competition-conscious regulatory structure cannot guarantee against abuses of that structure, or against exclusionary behavior that falls just beyond its jurisdiction.[10] Indeed – and perhaps ironically – the very regulatory structure that exists to promote competition can create gaming opportunities for competitors bent on achieving anti-competitive goals. Such "regulatory gaming" undermines both the regulatory system itself and the longstanding complementary relationship between regulatory and antitrust law.

We argue that the risk of regulatory gaming provides an important example of the need for ongoing antitrust oversight of regulated industries. We define regulatory gaming as private behavior that harnesses pro-competitive or neutral regulations and uses them for exclusionary purposes. Complex regulatory systems – particularly those requiring government approval for market entry – can create opportunities for such gaming, by enabling dominant parties to dictate industry standards while delaying entry of competing products. The pharmaceutical industry has witnessed this behavior for years, as branded drug companies have used exclusionary tactics to stay one step ahead of generic entry. In one species of this behavior – product-hopping – the branded company makes repeated changes in drug formulation to prevent generic substitution,

(questioning effectiveness of regulatory regime in *Trinko*); Adam Candeub, *Trinko and Re-Grounding the Refusal to Deal Doctrine*, 66 U. PITT. L. REV. 821 (2005) ("Trinko's implication that there can be no antitrust injury from refusing to deal, *i.e.*, provide interconnection, so long as regulation requires access, is probably not true.").

[10] *E.g.*, Covad Communications Co. v. BellSouth Corp., 374 F.3d 1044, 1050 (11th Cir. 2004) (upholding antitrust claim based on a "squeeze" between regulated wholesale prices and unregulated retail prices that plaintiff claimed were predatory); *cf.* Town of Concord v. Boston Edison Co., 915 F.2d 17, 29 (1st Cir. 1990) (Breyer, C.J.) ("We recognize that a special problem is posed by a monopolist, regulated at only one level, who seeks to dominate a second, unregulated level, in order to earn at that second level the very profits that regulation forbids at the first."). *See generally* Candeub, *supra* note __, at 841 ("Congress could quite reasonably have wanted the antitrust laws to enforce its access regime because, for better or worse, the FCC, structurally incapable of Olympian detachment from political influence, could be seen as a poor forum to decide such disputes. Or, at the very least, Congress could have intended the threat of antitrust action to discipline the behavior of the Baby Bells.").

rather than to improve the efficacy of the drug product.[11] Product-hopping raises difficult questions for antitrust courts. On the one hand, product hopping antitrust suits require courts to inquire into product design choices, something antitrust judges take pains to avoid; they also raise concerns about courts second-guessing judgments by agencies and legislators about how best to balance competition and innovation in regulated markets. On the other hand, if left unchallenged, this kind of behavior can cause sustained inefficiencies in markets.

Industry standards set or endorsed by government bodies offer a second example. If the government requires that products include particular features or perform in particular ways, private parties can sometimes hoodwink regulators into adopting standards that favor their proprietary technologies and exclude their competitors.[12] Of course, nothing prevents the government from settling on a patented standard, and private parties have a protected right to petition the government regardless of their motive. But when petitioning behavior contains material misstatements or omissions, and results in standards that exclude competition in ways the government did not anticipate, the petitioning party has abused the regulatory process. Here, too, antitrust courts must strike a delicate balance among several competing concerns – the right to petition the government, the legitimate enforcement of patent rights, and the very real problem of patent holdup and regulatory abuse.[13]

Our goal in this paper is not to persuade the reader that these particular examples of regulatory gaming violate the antitrust laws (though we think they do) or that other examples,

[11] FTC v. Warner Chilcott, 2005 WL 3439585 (D.D.C. Complaint Filed Nov. 7, 2005); Abbott Laboratories v. Teva Pharmaceuticals USA, 432 F. Supp. 2d 408 (D. Del. 2006).

[12] Opinion of the Commission, In re Matter of Union Oil Company of California, Docket No. 9305 (opinion issued July 7, 2004), *available at* http://www.ftc.gov/os/adjpro/d9305/040706commissionopinion.pdf.

[13] *See, e.g.*, Mark A. Lemley & Carl Shapiro, *Patent Holdup and Royalty Stacking*, 85 **Tex. L. Rev.** 1997 (2007).

such as regulatory price squeezes, do not violate the antitrust laws. Rather, our point is that whether or not particular acts of regulatory gaming harm competition is and should be an *antitrust* question, not merely one that involves interpreting statutes or agency regulations. Regulatory agencies and even Congress cannot prevent gaming ex ante. Experience with the pharmaceutical industry suggests that if Congress acts to squelch one form of gaming, companies will find other ways to game the system. And even if Congress or the regulating body can surgically fix a particular type of exclusionary behavior, such an ex post response (unlike the threat of antitrust treble damages) does nothing to compensate for past harm or to deter future gaming behavior. Some level of antitrust enforcement – with appropriate deference to firm decisions about product design and affirmative regulatory decisions that affect market conditions – provides a necessary check on behavior, such as product hopping, that has no purpose but to exclude competition.

Part I begins with an introduction to the relationship between antitrust law and industry-specific regulation. After briefly discussing the historical collaboration between antitrust and regulatory law, we explore the recent cases that show skepticism toward antitrust intervention in regulated industries – skepticism that represents a marked departure from antitrust history. In Part II, we contend that this skepticism, if applied too broadly, contradicts both logic and a rich economic literature that suggests that antitrust law generally does a better job of disciplining exclusionary behavior and achieving competitive outcomes than do government agencies. The decisions that have ushered in antitrust deference have perverted the lessons of law and economics, taking the efficiency-based attacks lodged against overly vigorous antitrust enforcement as license to cut back on *all* antitrust enforcement, even where antitrust offers the only hope of curbing regulatory abuse.

At the same time, we agree that antitrust courts must use caution in treating regulated industries, intervening only when the regulatory structure appears unable, for some identifiable reason, to ensure competitive outcomes. Thus, Part III distills a framework for evaluating the application of antitrust law to regulated industries. While we argue that antitrust should not defer to regulatory agencies merely because they operate in the area of inquiry, neither should antitrust ignore the decisions regulators make. Where a regulator has made a decision that affects competition – by setting a particular price, for example, or denying a license to a potential competitor – antitrust should not second-guess that decision absent evidence of outright corruption.[14] But the fact that a regulator does not object to or block a private company's anticompetitive practice does not mean that antitrust law must countenance that practice. When regulators lack the mandate or the commitment to protect against exclusionary behavior, antitrust courts have a continuing role to play.

Indeed, the existence of regulation not only fails to guarantee competitive outcomes in many cases, but can make things worse by creating opportunities for anticompetitive games. In Part IV, we turn to regulatory gaming as an example of behavior that justifies ongoing antitrust oversight of regulated markets. We use three examples – pharmaceutical product-hopping, abuse of government standard-setting, and regulatory price squeezes – to illustrate the phenomenon of

[14] *See, e.g.*, Federal Prescription Services, Inc. v. American Pharmaceutical Ass'n, 663 F.2d 253, 263 (D.C. Cir. 1981) ("Attempts to influence governmental action through overtly corrupt conduct, such as bribes (in any context) and misrepresentation (in the adjudicatory process), are not normal and legitimate exercises of the right of petition, and activities of this sort have been held beyond the protection of Noerr."); *id.* at 262 (*Noerr* is inapplicable to activity that "subverted the integrity of the governmental process"); *cf.* Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988) (finding antitrust violation based on wholesale capture of private standard-setting body). See Mark A. Lemley & David McGowan: *Antitrust Immunity: State Action and Federalism, Petitioning and the First Amendment*, 17 **Harv. J. L. & Pub. Pol'y** 293 (1994).

regulatory gaming, the risks that gaming can pose to competition and consumer welfare, and the appropriate limits of antitrust in this area. Part V concludes.

I. The Role of Antitrust in Regulated Industries

Antitrust is designed to protect competition.[15] But threats to competition do not come only from private conduct in unregulated industries, the traditional province of the Sherman Act. They can also come from government regulation itself, from government delegation of market control to private actors, and – most important for our purposes – from private actions designed to take advantage of a regulatory regime.

Courts have long recognized the potential for conflicts between an antitrust regime directed at encouraging efficient market competition and regulatory systems that are either deliberately anticompetitive or, more likely, simply indifferent to their competitive effects. But where it is the state itself that decides upon an anticompetitive end, the antitrust laws have not intervened, either because of worries about federal-state relations or (at the federal level) worries about the relationship between the judiciary and the administrative state. Thus, the state of California was free during the Great Depression to organize raisin-growing cooperatives that bought up and destroyed the majority of the raisin crop in order to create artificial scarcity, raising prices on food at a time when buyers could ill afford it.[16] This was undeniably stupid economic policy, but it was government-set economic policy, and the Supreme Court concluded that the courts did not have the constitutional power to reverse it.[17] That remains the rule: state

---

[15] *See* Standard Oil Co. v. FTC, 340 U.S. 231, 248 (1951) ("The heart of our national economic policy long has been faith in the value of competition."); Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962).

[16] Parker v. Brown, 317 U.S. 341 (1943).

[17] *Id.* at 350-52.

regulations that affect or even destroy competition are not antitrust violations.[18] This is true even if those actions are venal – if they are the result of capture or bribery of the government decision-makers by those who stand to benefit from their regulations. In *City of Columbia v. Omni Outdoor Advertising*, for example, the Court immunized city regulations that forbad construction of new billboards, even though the evidence established that those regulations were passed at the behest of the incumbent monopoly owner of existing billboards in the city in an effort to prevent new entry.[19]

States do not always act as brazenly as they did in *Parker v. Brown*, however. Sometimes governments will interfere with competition not by restricting it directly, but by setting up licensing schemes or rules that effectively delegate market control to private actors. For example, in *FTC v. Ticor Title*, the government challenged a state rule that allowed competitors to collectively agree on the rates they would charge for title insurance; the state then "adopted" those rates by default unless it affirmatively acted to veto or change the rates.[20] Those

[18] *See* 1 **Philip Areeda & Herbert Hovenkamp, Antitrust Law** para. 200, at 148 ("antitrust's intervention into the political process is inappropriate once it is determined that the government itself rather than a private actor is the relevant decision maker."). Because this rule derives from concerns about federalism and state sovereignty, it does not necessarily apply to acts by municipalities. *See* Community Communications Co. v. City of Boulder, 455 U.S. 40, 50-52 (1982) ("Our precedents thus reveal that [a municipality's action] cannot be exempt from antitrust scrutiny unless it constitutes the actions of the State … itself in its sovereign capacity, *see Parker*, or unless it constitutes municipal action in furtherance or implementation of clearly articulated and affirmatively expressed state policy ….") (other citations omitted). In the early 1980s, Congress passed a statute exempting municipalities and their employees from damages for antitrust violations, but the statute does not limit the availability of injunctive relief, and its passage confirms that municipalities' exemption is a statutory one, rather than one based on the federalism or constitutional concerns identified in *Parker*. *See* Local Government Antitrust Act, 15 U.S.C. §§ 34-35..

[19] 499 U.S. 365 (1991).

[20] Federal Trade Comm'n v. Ticor Title Ins. Co., 504 U.S. 621 (1992); *see also* Southern Motor Rate Carriers Conf. v. United States, 471 U.S. 48 (1985); California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980).

quasi-state actions are subject to a more complex set of antitrust rules, one that seeks to distinguish between restraints of trade that are effectively government-controlled and those that are effectively private, shielded merely by a "gauzy cloak" of government blessing.[21] Thus, government delegations of this sort are permissible only if the government clearly articulates its intent to displace market competition and actively supervises the activity of the private entities to which it has delegated control.[22]

A third set of cases involve purely private acts that occur in the shadow of a government regulatory regime. For example, government regulations often restrict entry into markets, sometimes expressly and sometimes by delaying that entry pending regulatory approval or raising its costs. Private actors can and do take advantage of these regulatory barriers to acquire or consolidate market power. Here too the antitrust laws have traditionally distinguished between limits on competition that result directly from the government's own acts – the inability of generic pharmaceutical competitors to enter the market without FDA approval, for example – and private acts designed to take advantage of the regulatory regime to exacerbate monopoly power or market harm. But where the conduct is clearly private, antitrust law has historically been unwilling to cede ground to administrative agencies at either the state or federal level. The

[21] *Cal. Retail*, 445 U.S. at 105-06. For skepticism as to whether this public-private distinction is plausible, see McGowan & Lemley, *supra* note __, at 315-22, 356-57; *cf.* Einer R. Elhauge, *The Scope of Antitrust Process*, 104 **Harv. L. Rev.** 668, 669 (1991) (rejecting the public-private distinction, and attempting to replace it with an assessment of the disinterestedness of the government actors).

[22] *Ticor Title*, 504 U.S. at 633 ("Actual state involvement, not deference to private pricefixing arrangements under the general auspices of state law, is the precondition for immunity from federal law.").

Supreme Court made it clear early on that it did not look kindly on claims that a regulatory regime impliedly repealed the antitrust laws.[23] As John Wiley observed in 1986:

> The Supreme Court's rules for finding exemptions to antitrust policy testify to the dominance of Sherman Act policy: the Court disclaims its authority to create antitrust exemptions;[24] is reluctant to imply them;[25] and construes express exemptions narrowly-often remarkably so.[26]

Government action may be exempt from antitrust scrutiny, but regulation traditionally has not meant a similar immunity for private action in regulated industries. Thus, in *Silver v. New York Stock Exchange*, the Court held that the Securities Exchange Act did not displace antitrust scrutiny over the NYSE, even though the antitrust issue – membership in the exchange – was one subject to SEC rules. The Court said that "repeal of the antitrust laws is to be regarded as implied only if necessary to make the Securities Exchange Act work, and even then only to the minimum extent necessary."[27]

The traditional coexistence of regulated industries and antitrust appears to be changing, however. In a number of cases in the past decade the Supreme Court has either found implied repeal of the antitrust laws in the face of regulation or has held that antitrust cannot or need not govern anticompetitive conduct in industries in which regulatory agencies are active, even if those agencies are not directly supervising the anticompetitive conduct at issue in the case.

---

[23] Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119, 126 (1982); John S. Wiley, Jr., *A Capture Theory of Antitrust Federalism*, 99 **Harv. L. Rev.** 713, 713 n.1 (1986).

[24] *See* National Soc'y of Professional Eng'rs v. United States, 435 U.S. 679, 692 (1978).

[25] *See* National Gerimedical Hosp. & Gerontology Center v. Blue Cross, 452 U.S. 378, 388-89 (1981).

[26] Wiley, *supra* note , at 713 n.1 (citing Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205 (1979)) (other citations converted to footnotes).

[27] Silver v. New York Stock Exchange, 373 U.S. 341, 357 (1963).

While the Court continues to recite the same legal standard, requiring a "plain repugnancy" between the antitrust and regulatory provisions,[28] it is plain that the Court views antitrust as more repugnant than it has in the past.[29]

In *Verizon v. Trinko*,[30] for example, the Court considered an antitrust claim against an incumbent local exchange telephone provider (LEC), alleging that the LEC had refused to deal on nondiscriminatory terms with customers of newly-created competitive local exchange carriers (CLECs), denying them effective access to the LEC's monopoly facilities. The Court could not conclude that the Telecommunications Act preempted antitrust law in this area, because the Act itself said that it didn't.[31] Nonetheless, the Court rejected the plaintiff's essential facilities antitrust claim, engaging in some revisionist history in saying that the Court had never endorsed such a claim before[32] and suggesting that antitrust courts should tread lightly around markets that have "a regulatory structure designed to deter and remedy anti-competitive harm."[33]

[28] CreditSuisse Securities, LLC v. Billing, 127 S.Ct. 2383, 2390 (2007).

[29] The Court's animosity to antitrust claims extends well beyond the issue of regulatory deference. It has been sixteen years since the Court has ruled for an antitrust plaintiff. *See, e.g.,* Leegin Creative Leather Products, Inc. v. PSKS, Inc., 127 S.Ct. 2705 (1007) (abandoning per se rule against vertical minimum resale-price agreements); Bell Atlantic Corp. v. Twombly, 127 S.Ct. 1955 (2007) (heightening pleadings requirement for private antitrust claims). While we have some concerns about this general contraction of antitrust's scope, they are beyond the scope of this article; our point here is that antitrust law's substantive standards – whatever they may be – should continue to play a role in regulated industries.

[30] Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004). For some reason, everyone calls the case "*Trinko*" even though the petitioner was Verizon, and we follow that convention here.

[31] 110 Stat. 143, § 601(b)(1). *See Trinko*, 540 U.S. at 406.

[32] *Id.* at 411. *Contra* Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) (finding liability on an essential facilities theory, ironically in a regulated industries case). The *Trinko* Court did not cite or discuss *Otter Tail*. *Cf.* AT&T Corp. v. Iowa Utilities Bd., 525 U.S. 366, 428 (1999) (Breyer, J., concurring) (describing essential facilities as "an antitrust doctrine that this Court has never adopted").

[33] *Id.* at 411.

Commentators have differed over the meaning of *Trinko*. Verizon views the opinion as a categorical rejection of antitrust enforcement in regulated industries,[34] but the Court in our opinion does not go that far. An alternative view of the opinion is as a rejection of the antitrust theory of essential facilities and unilateral refusals to deal, one applicable regardless of the industry context. It is true that the Court appears hostile to those claims. But the Court also spent a great deal of time discussing the regulatory structure of the market and how it made antitrust law unnecessary.[35] Finally, some discern in *Trinko* a more flexible discretionary principle, in which judges should consider the relative institutional competencies of courts and regulators before intervening in regulated markets.[36] Under this approach, courts should consider not only the existence of the regulatory agency, but its empowerment and commitment to addressing competition-related concerns.[37]

---

[34] *E.g.*, John Thorne, *A Categorical Rule Limiting Section 2 of the Sherman Act: Verizon v. Trinko*, 72 **U. Chi. L. Rev.** 289 (2005) (viewing case as a categorical rejection of refusal-to-deal claims in regulated industries).

[35] *Trinko*, 540 U.S. at 411-16.

[36] *See, e.g.*, Weiser, *supra* note 1, at 10 (suggesting that "the extent of antitrust restraint should vary depending on whether the regulatory regime is reasonably effective at addressing the relevant anticompetitive conduct"); Herbert Hovenkamp, *Antitrust and the Regulatory Enterprise*, 2004 **Colum. Bus. L. Rev**. 335; *cf.* Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 **Antitrust L.J**. 3, 42 (2004) ("At its core, [*Trinko*] suggests little more than that courts should be reluctant to scrutinize pure, unilateral refusals to assist rivals by dominant firms in industries subject to extensive, competition-focused regulation, particularly if the government scheme regulates access to the dominant firm's facilities."); C. Scott Hemphill, *Paying for Delay: Pharmaceutical Patent Settlements as a Regulatory Design Problem*, 81 **N.Y.U.L. Rev.** 1553, 1557 (2006) ("Identifying the impact of an industry-specific regulatory regime in a particular context requires careful, sustained attention to the principal features of the relevant regulatory structure.").

[37] Phil Weiser, for example, has advocated a hands-on approach for antitrust courts in communications cases, based on what he sees as the FCC's "deliberate under-enforcement strategy" in the current deregulatory era. Weiser, *supra* note 1; *see also* Hovenkamp, *supra* note __, at 352; Covad Communications Co. v. BellSouth Corp., 374 F.3d 1044 (11th Cir. 2004) (holding that predatory price squeeze claim survives *Trinko*, when the antitrust claim "depends upon [a specific regulatory decision] only in a circular sense") ; Z-Tel v. SBC, cite (limiting

Regardless how one reads the opinion, however, the Court seems inclined to think that the existence of a regulated industry makes antitrust law less important. Its reasoning is two-fold. First, if an industry regulator is evaluating competition issues, "the additional benefit to competition provided by antitrust enforcement will tend to be small,"[38] presumably because the regulators can serve that role.[39] Second, the Court emphasized the risk of mistaken findings of antitrust liability, describing them as "especially costly, because they chill the very conduct the antitrust laws were designed to protect."[40] Relevant to both points, the Court suggested that specialist regulators were likely to be better at evaluating competition economics than a generalist antitrust court.[41]

This theme – the comparative advantage of regulators over antitrust courts in promoting competition – shows up in other Court opinions as well. In *CreditSuisse Securities v. Billing*,[42] for instance, which involved allegations of clearly anticompetitive collusion by underwriters, the Court nonetheless rejected application of the antitrust laws because it found that the Securities

---

Trinko to cases involving novel antitrust claims – even in regulated industries – but finding traditional antitrust claims viable even in regulated markets: "As a legal matter, *Trinko* instructs us that antitrust liability is live and well in the context of regulated industries."); Stand Energy Corp. v. Columbia Gas Transmission Corp., 373 F. Supp. 631, 641 (S.D.W.Va. 2005) (relying upon *Otter Tail* to allow essential facilities claim in regulated industry, when "FERC's authority to remedy anti-competitive behavior is decidedly less than the regulatory authority in *Trinko*"). *In re Remeron* (important, because it's an orange book/patent case); *linkLine Communications, Inc. v. SBC California, Inc.*, 503 F.3d 876, 882 (9th Cir. 2007) ("Importantly, the Court did not say that the existence of a regulatory scheme was a per se bar to judicial enforcement of the antitrust laws, only that 'the existence of a regulatory structure' is '*[o]ne factor* of particular importance.'") (quoting *Trinko*, 540 U.S. at 412).

38 *Trinko*, 540 U.S. at 412.

39 Even where regulation doesn't serve a competition-protecting function, the Court was hesitant to endorse antitrust scrutiny, pointing to its "sometimes considerable disadvantages." *Id.*

40 *Id.* at 414.

41 *Id.*

42 127 S.Ct. 2383.

and Exchange Commission (SEC) was heavily involved in regulating what underwriters could do, and while the SEC too forbad much of the conduct complained of, it would be too hard for antitrust courts to prevent collusion without deterring conduct the SEC had chosen to permit. *CreditSuisse,* like *Trinko,* concludes that "any enforcement-related need for an antitrust lawsuit is unusually small" because the SEC can step in to prevent collusion.[43] The Court also emphasized the limitations of antitrust's "nonexpert judges and nonexpert juries" and the "unusually high risk that different courts will evaluate similar factual circumstances differently."[44] And like *Trinko*, it emphasized the risk of false positives while not discussing the risk of false negatives, worrying that "antitrust courts are likely to make unusually serious mistakes in this respect."[45]

CreditSuisse, like *Trinko*, is capable of various readings. The actual holding of the case is quite limited, and the Court's reliance on the strict legal standard from prior cases suggests that the case might stand for no more than the application of that standard to a precise set of facts. But the Court's long discussion of the comparative advantages of regulation over antitrust enforcement, a discussion that never mentions *Trinko* but echoes its arguments almost completely, suggests that something broader is going on here: a move toward antitrust deference in the face of regulation.

In short, antitrust courts seem increasingly willing to permit private anticompetitive acts that occur in the shadow of regulation, relying on regulators to perform the traditional antitrust function of protecting competition and sometimes turning a blind eye even when regulators cannot or do not do so.

---

[43] *Id.* at 2396.

[44] *Id.* at 2395.

[45] *Id.* at 2396.

II. The Relative Efficiency of Antitrust and Regulation

The growing antitrust deference to regulation is cause for concern. Both antitrust and regulation are economic responses to market failures.[46] Implemented correctly, both are designed to serve the ends of economic efficiency.[47] It is therefore reasonable to judge the relative efficacy of antitrust and regulation by economic criteria. And judged by those criteria, virtually all economists would agree that antitrust-overseen market competition is superior to industry regulation. In particular, none of the arguments the Court has offered as a reason to prefer regulation to antitrust withstand scrutiny.

Relative expertise. It is true, as the Court emphasized in *Trinko* and *CreditSuisse*, that antitrust courts are generalist courts, while regulatory agencies tend to specialize in a particular industry and its problems. That specialization should, all other things being equal, mean that expert regulators will do a better job than judges or juries of reaching the right result. But other things are far from being equal. Antitrust courts have two significant advantages over regulatory agencies when it comes to promoting competition.

First, antitrust courts are trying to promote economic efficiency, while regulators often aren't. For decades, efficiency has served as the sole criterion on which to judge antitrust rules. And courts have had over a century in which to hone those rules to achieve that end. Without question, courts have made mistakes in the past. But there is a strong consensus among antitrust scholars that the wave of cases in the last 30 years has largely moved antitrust in the right

[46] *See, e.g.*, Hovenkamp, *supra* note __, at 336-37 (noting complementarity of antitrust and regulation); Stephen Breyer, **Regulation and Its Reform** 156-57 (1982).

[47] Of course, antitrust and regulation take different approaches to achieving their common goal, but both ultimately aim to maximize efficiency in markets. *See* Breyer, *supra* note __, at 156-57 ("The antitrust laws seek to create or maintain the *conditions* of a competitive marketplace rather than replicate the *results* of competition or correct for the defects of competitive markets.").

direction, eliminating any significant risk that antitrust enforcement will do more harm than good.[48] Scholars may fight over whether a Chicago School or a post-Chicago School approach will achieve the right result in specific cases,[49] but for the most part they are tinkering at the margins: the law and the scholarship have converged with respect to both the proper goals of antitrust and the general rules that will achieve those goals.

Regulation, by contrast, is frequently not even intended to achieve economic efficiency through competition. Occasionally that is because of a legislative judgment that competition is impossible, though the number of industries thought to be natural monopolies for which markets won't work has shrunk dramatically in the past four decades.[50] Industry regulation that excludes entry in order to promote a natural monopoly, as telephone regulation did before 1984, is not likely to achieve a competitive outcome.

More often, the goals of the legislators who establish regulatory agencies, or the goals of the regulators who run those agencies, are to achieve something other than competition. Indeed,

---

48 *See* Areeda & Hovenkamp, *supra* note __, at ¶ 110a ("Today it seems clear that the general goal of the antitrust laws is to promote 'competition' as the economist understands that term. Thus we say that the principal objective of antitrust policy is to maximize consumer welfare by encouraging firms to behave competitively while yet permitting them to take advantage of every available economy that comes from internal or jointly created production efficiencies, or from innovation producing new processes or new or improved products."); Michael S. Jacobs, *An Essay on the Normative Foundations of Antitrust Economics*, 74 **N.C. L. Rev.** 219, 220-22 (1995) (noting increasing consensus between Chicago and post-Chicago views on antitrust's appropriate goals); *cf.* William E. Kovacic, *The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Conduct: The Chicago/Harvard Double Helix*, 2007 **Colum. Bus. L. Rev.** 1 (2007) (noting influence of both "Harvard School" and "Chicago School" in narrowing and focusing the scope of antitrust claims in recent decades); Richard A. Posner, *The Chicago School of Antitrust Analysis*, 126 **U. Penn. L. Rev.** 925 (1979) (observing increased convergence of scholars' views on the appropriate role of antitrust laws).

49 *See* Areeda & Hovenkamp, *supra* note __, at ¶ 112d (summarizing remaining doctrinal and methodological differences between the "Chicago School" and the "Harvard School").

50 *See* Herbert Hovenkamp, **The Antitrust Enterprise: Principle and Execution** 228 (2006) (noting the success of deregulation in recent decades in industries once viewed as natural monopolies that required regulatory oversight).

many regulations are aimed precisely at *eliminating* competition, as was the government-sponsored raisin cartel in *Parker v. Brown*[51] or any of its modern descendent crop-support programs administered by the Department of Agriculture. It should be obvious that regulations intended to reduce competition will not promote it. But even if the regulation is not directly inimical to competition, competition is frequently irrelevant to, or at best a minor consideration in, a regulator's agenda. Regulators may care about the safety and efficacy of a drug, for example, and only incidentally about whether there is competition in the sale of that drug. They may seek to reduce traffic deaths or air pollution by mandating technology, regardless of the effect that mandate has on the price manufacturers can charge or the number of products they sell. These are laudable goals, to be sure, but they are not *competition-related* goals. An agency tasked with achieving these goals is likely to ignore threats to competition from the industry it regulates so long as those threats do not compromise its core mission. Thus, the state and local governments that enacted the privately-drafted National Fire Protection Code at issue in *Allied Tube* into law were interested in stopping fires; doubtless they thought little if at all about the competitive effects of the code, even though it turned out that the code was drafted by interested private parties with the purpose of impeding competition rather than promoting fire safety.[52]

Even those agencies whose mission expressly involves consideration of competition issues will not necessarily make it their first among potentially conflicting priorities. The SEC, for example, which as Justice Breyer pointed out is dedicated to improving market information and expressly considers competition among other issues in setting regulation,[53] is first and foremost an investor-protection and information-disclosure agency, not an agency that

---

[51] Parker v. Brown, 317 U.S. 341 (1943).

[52] Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988).

[53] *CreditSuisse*, 127 S.Ct. at 2396 (citing 15 U.S.C. §§ 77b(b), 78w(a)(2)).

investigates and weeds out cartels or other anticompetitive practices. It is unlikely to devote much in the way of time or resources to such issues, because even if it is tasked to consider such issues they do not reflect the agency's primary purpose. Similarly, even an agency like the Federal Communications Commission that is directly focused on competitive conditions in a particular market may naturally pay attention primarily to that market, and give less if any attention to the effect its rules might have on competition in adjacent markets or competition from unanticipated new businesses. This arguably explains the FCC's willingness to largely ignore the effects of its decisions on the Internet, for example: it is telecommunications, not the Internet, that the FCC is tasked to regulate.

Agencies that view competition as secondary, or view it through the lens of a particular industry's characteristics and interests, are less likely to create and enforce rules that optimally encourage competition.[54] At a bare minimum, therefore, the industry-specific expertise of an agency must be balanced against the competition-specific expertise of the specialist antitrust agencies: the Federal Trade Commission (FTC) and the Department of Justice Antitrust Division.

The problem with agencies is much greater than just their questionable mandate to promote competition, however. Agencies are famously subject to "capture" by the industries they are supposed to regulate.[55] That capture can take many different forms. Sometimes

[54] *See* 1A Areeda & Hovenkamp, *supra* note __, at 283 ("agencies and antitrust courts have often had different attitudes toward the importance of competition in the regulated sector. Often the antitrust authorities are more skeptical than regulators about industry claims of efficiency or the social benefits of restraints on competition.").

[55] Among the considerable literature on agency capture, see, e.g., Stephen G. Breyer, Regulation and Its Reform (1994); 1A Areeda & Hovenkamp, *supra* note __, para. 241b2; James Buchanan & Gordon Tullock, The Calculus of Consent (1962); Daniel A. Farber & Philip P. Frickey, Law and Public Choice, a Critical Introduction (1991); George J. Stigler, *The Theory of*

regulators or legislators are captured in the most venal sense – they are bribed or otherwise given personal benefits in exchange for voting a particular way. This seems to have been the case in *Omni Outdoor Advertising*, for example. Regulators who accept bribes (or politicians who accept campaign contributions in exchange for a particular vote) are not acting in the public interest but in their private interest, a private interest that necessarily aligns with the industry participant doing the bribing. Even a regulator who would never accept bribes may still seek to maximize, not the public interest, but his own power or the power and interests of his agency, a fact that industry can often use to its advantage.

Capture need not be so brazen, however. Even honest regulators and legislators can be captured through the mechanism of public choice theory.[56] A legislator that tries to maximize her constituents' expressed preferences may still end up supporting legislation that benefits private firms at the expense of the public interest, because the private firms will frequently have a concentrated interest – and therefore show up to lobby on a particular issue – while the public is hard to organize even around issues that may affect a great many of them diffusely. Regulators are subject to the same effect. A notice and comment rulemaking is likely to produce more comments from people with a concentrated interest in the outcome, and fewer comments from those with a more diffuse interest. Thus, regulators who try in good faith to determine what the public thinks of a particular regulation may still end up with a skewed view of the pros and cons. This may be particularly likely with competition issues. While the public as a whole has a strong interest in unfettered competition, any individual member of the public is unlikely to be affected much by a particular regulatory decision. And particularly where the industry as a

---

Economic Regulation, 2 **Bell J. Econ. & Mgmt. Sci.** 3 (1971); Richard A. Posner, *Theories of Economic Regulation*, 5 **Bell J. Econ. & Mgmt. Sci.** 335 (1974).

[56] Mancur Olson, **The Logic of Collective Action** (1965).

whole colludes to seek regulatory intervention that benefits them, as in *Ticor Title*, there are unlikely to be competitors who can stand as proxy for the interests of the public.

Finally, even legislators and regulators aware of the existence of public choice problems and determined to do the right thing are still susceptible to forms of what we might call "soft" capture. Acquiring accurate information about market conditions is often very difficult, for example. Companies with a vested interest in the outcome can hire lobbyists that provide information helpful to their side, and a regulator who cannot get information except from those lobbyists may have little choice but to accept that information as true. Even if there are competing sources of information, interested parties can and do hire as lobbyists former employees, colleagues, or friends of the regulator, and it is natural human instinct to trust those people more than strangers. And regulators tend to come from the industries they regulate, which may mean that they start out seeing things from the industry's perspective.

Judges, by contrast, are much less subject either to having their purpose diverted or to capture. While some have tried to argue that judges face some of the same interest group constraints as legislators and administrative agencies,[57] the fact is that antitrust courts are trying to achieve the goal of economic efficiency, they are doing it in industries in which they have no direct financial interest, they cannot act to benefit their "agency" in rendering a decision, and the structure of the litigation process helps ensure to the extent possible that both sides are presented in a relatively balanced way. Courts aren't perfect, of course. But all advantages are comparative, and the fact that antitrust courts are trying to promote competition rather than to achieve some other end (whether legislated or self-motivated) provides a powerful counterweight to the industry expertise of administrative agencies. It is important to keep in mind, as Areeda

[57] *See* Einer Elhauge, *Does Interest Group Theory Justify More Intrusive Judicial Review?*, 101 **Yale L.J.** 31 (1991).

and Hovenkamp summarize, that "it often turn[s] out that the principal beneficiaries of industry regulation were the regulated firms themselves, which were shielded from competition and guaranteed profit margins."[58] Courts should not assume that regulation will lead to competition merely because regulators know more than courts about the industries they regulate.

False positive and false negatives. A second concern expressed by the Court is that the risk of false positives – courts finding antitrust violations when in fact there are none – far outweighs the risk of false negatives, and that this is particularly true in regulated industries. That concern may once have had some force, but it no longer does.

To begin, it is worth noting the recent history of antitrust decisions – a history that is, almost without exception, one that makes it harder over time for antitrust plaintiffs to win cases. Judge Easterbrook could speak in 1984 of the asymmetry between false positive and false negatives,[59] but the antitrust law he was talking about simply doesn't exist anymore. Courts in the last three decades have dismantled every per se rule applied to vertical conduct,[60] limited the per se rule in horizontal conspiracies in a variety of ways,[61] made it harder for plaintiffs to infer

---

[58] 1A Areeda & Hovenkamp, *supra* note __, para 241b2, at 293.

[59] Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1 (1984).

[60] Leegin Creative Leather Products, Inc. v. PSKS, Inc., 127 S. Ct. 2705 (2007); State Oil Co. v. Khan, 522 U.S. 3 (1997); Business Electronics Corp. v. Sharp Electronics Corp., 485 U.S. 717 (1988); Illinois Tool Works, Inc. v. Independent Ink, Inc., 547 U.S. 28 (2006); NYNEX Corp. v. Discon, Inc., 525 U.S. 128 (1998).

[61] Texaco, Inc. v. Dagher, 547 U.S. 1 (2006); National Collegiate Athletic Ass'n v. Board of Regents, 468 U.S. 85 (1984); Broadcast Music, Inc. v. Columbia Broadcast Sys., Inc., 441 U.S. 1 (1979); Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co., 472 U.S. 284 (1985).

conspiracies,[62] all but eliminated predatory pricing claims,[63] and substantially restricted the role of monopolization cases.[64] Win rates for antitrust plaintiffs in at least one industry hover below 15%,[65] and court rules make it harder and harder for antitrust plaintiffs to show standing to sue to enforce the laws that remain.[66]

We have no doubt that antitrust at one time was skewed towards overenforcement, but today if there is any bias it is in the opposite direction. The Supreme Court has now decided 16 antitrust cases in a row in favor of defendants,[67] and the *AT&T* case seems poised to be the 17th. It has been 16 years since an antitrust plaintiff won in the Supreme Court. Courts are willing to permit obvious cartels and market division schemes to survive antitrust scrutiny, sometimes

[62] Bell Atlantic Corp. v. Twombly, 127 S. Ct. 1955 (2007); Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574 (1986); Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984).

[63] Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993) (requiring proof of below-cost pricing and probability of recoupment in predatory pricing claims); Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574 (1986) (enhancing pleading requirements in predatory pricing cases); Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 127 S. Ct. 1069 (2007) (holding that stringent standard for predatory pricing also applies to predatory bidding claims).

[64] Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004).

[65] *See* Peter J. Hammer & William M. Sage, *Antitrust, Health Care Quality, and the Courts*, 102 **Colum. L. Rev.** 545, 575 (2002) (study concluding that plaintiffs win only fourteen percent of antitrust cases in the health care industry). While the health care industry may not be representative, it supports a general consensus that plaintiffs rarely win antitrust suits. *But see* Daniel A. Crane, *Rules Versus Standards in Antitrust Adjudication*, 64 **Wash. & Lee L. Rev.** 49, 65 (2008) (contending that rule of reason has become "reinvigorated" in recent years, leading to more wins for plaintiffs).

[66] Atlantic Richfield Co. v. USA Petroleum Co., 495 U.S. 328 (1990) (holding that antitrust plaintiffs must prove "antitrust injury" —i.e., that their injury resulted from harm to the competitive process); Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489 (1977) ("Plaintiffs must prove antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful.").

[67] *See* William Polasky, *Reinvigorating Antitrust Enforcement in the United States: A Proposal*, 22 **Antitrust** 85, 85 (2008) (noting lax antitrust enforcement and pro-defendant bent of the Roberts Court, and listing the cases).

going so far as to call them per se legal,[68] and seem unwilling to restrict anticompetitive behavior by patentees.[69] The Antitrust Division, tasked with enforcing the antitrust laws, permits mergers to monopoly[70] and seems to spend as much time arguing in favor of antitrust defendants as it does suing them.[71] We don't intend to suggest that antitrust law is dead; the agencies continue to prosecute cartels, and private parties continue to file antitrust cases. But for the Supreme Court to say that antitrust is too expansive – that antitrust courts are more likely to wrongly find an

---

[68] In re Tamoxifen Antitrust Litigation, 466 F.3d 187 (2d Cir. 2006) (concluding that "reverse-payment" settlement – in which patent plaintiff pays challenger to drop its validity challenge and stay out of the market – did not violate the antitrust laws); Schering-Plough v. Fed. Trade Comm'n, 402 F.3d 1056, 1076 (11th Cir. 2005) (same); Valley Drug Co. v. Geneva Pharm., Inc., 344 F.3d 1294 (11th Cir. 2003) (same); In re Ciprofloxacin Hydrochloride, 363 F. Supp. 2d 514 (E.D.N.Y. 2005) (same). *But see* In re Cardizem CD Antitrust Litig., 332 F.3d 896, 908 (6th Cir. 2003) (finding reverse payment a *per se* antitrust violation).

[69] *See* Rambus, Inc. v. Federal Trade Commission, 522 F.3d 456 (D.C. Cir. 2008); *cf.* Rambus, Inc. v. Infineon Technologies AG, 318 F.3d 1081 (Fed. Cir. 2003).

[70] *See* Press Release, U.S. Dep't of Justice, *Statement of the Dep't of Justice on its Decision to Close its Investigation of XM Satellite Radio Holdings Inc.'s Merger with Sirius Satellite Radio Inc.* (March 24, 2008) (explaining decision not to challenge merger of the only two satellite radio firms in the United States), at http://www.usdoj.gov/opa/pr/2008/March/08_at_226.html; *see also* Jonathan B. Baker & Carl Shapiro, *Detecting and Reversing the Decline in Horizontal Merger Enforcement*, 22 **Antitrust** 29, 32 & n.17 (2008) (criticizing decision for giving insufficient weight to anticompetitive concerns raised by merger).

[71] Indeed, the DOJ went so far as to file a brief urging the Supreme Court to reject a petition for certiorari filed by its sister agency, the Federal Trade Commission. *See* Brief for the United States as Amicus Curiae, Federal Trade Comm'n v. Schering-Plough Corp., 126 S. Ct. 2929 (2005), 2006 WL 1358441. More generally, the Antitrust Division has filed pro-defendant briefs in *all* of the major antitrust cases before the Supreme Court in the past five years. *See* Brief for the United States as Amicus Curiae, Leegin Creative Leather Prods., Inc. v. PSKS Inc., 127 S. Ct. 2705, 2007 WL 173650 (filed Jan. 22, 2007); Brief of the United States as Amicus Curiae Supporting Vacatur, Credit Suisse Securities (USA) LLC v. Billing, 127 S. Ct. 2803, 2007 WL 173649 (filed Jan. 22, 2007); Brief for the United States as Amicus Curiae Supporting Petitioners, Bell Atlantic Corp. v. Twombly, 127 S. Ct. 1955, 2006 WL 2482696 (filed Aug. 25, 2006); Brief of the United States as Amicus Curiae Supporting Petitioner, Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 127 S. Ct. 1069, 2006 WL 2452373 (filed Aug. 24, 2006); Illinois Tool Works Inc. v. Independent Ink, Inc., 547 U.S. 28, 2005 WL 1864093 (filed Aug 4, 2005).

antitrust violation than to wrongly let one go unpunished – flies in the face of the realities of modern antitrust.

The question then becomes whether there is something about the regulatory environment that causes false positives to be particularly likely. Both *Trinko* and *CreditSuisse* suggest that the answer is yes. *CreditSuisse* suggests that because the antitrust claims at issue in that case, while covering conduct the SEC had itself forbidden, was hard to distinguish from other conduct the SEC had chosen to allow, there was "no practical way to confine antitrust suits so that they challenge only activity of the kind the investors seek to target," suggesting that "antitrust courts are likely to make unusually serious mistakes in this respect."[72] *Trinko* suggests that the conduct at issue there was "the very conduct the antitrust laws are designed to protect," so that mistaken condemnations "are especially costly" and likely to chill legitimate business behavior.[73]

In fact, however, we believe there is less, not more, of a worry about false positives in the presence of regulation, because regulators can easily protect particular types of conduct from antitrust scrutiny by the simple expedient of adopting or requiring it. If the SEC expressly requires certain collaboration or information disclosure by underwriters, for example, antitrust will not condemn that conduct even if it would find that collusion unlawful in an unregulated industry. It is true that antitrust may have a harder task in industries in which a regulatory agency has blessed certain conduct and therefore put it beyond the reach of antitrust law, but the hard task would seem to be effective enforcement, not preventing too much enforcement. So long as antitrust scrutiny is properly focused on private activity rather than regulatory decisions, the presence of regulation is likely to further circumscribe antitrust, not to lead to more false positives.

[72] *CreditSuisse*, 127 S.Ct. at 2395-96.

[73] *Trinko*, 540 U.S. at 414.

Duplication of effort. Finally, the Court suggests in each of these cases that the value of antitrust enforcement is reduced because the administrative agency can perform the same competition-protecting function. If the premise is true, this argument has some force: the incremental value of antitrust enforcement is less if a regulator is already serving the enforcement function. In practice, however, we are skeptical that this will often be the case, or that it will justify abdication of judicial responsibility for antitrust enforcement.

To begin, we note that all of the problems we detailed above make it unlikely that very many administrative agencies will in fact serve as effective guardians of the competition function.[74] Agencies that do not see promoting competition as a core part of their mission, or agencies that have been captured, are unlikely to get competition policy right.[75] Further, even agencies that are willing to take competition into account rarely provide effective mechanisms to enforce competition policy or deter antitrust violations. An agency that stops certain conduct after it begins does not sufficiently deter antitrust violations; an agency that imposes modest fines but lacks the power to stop the conduct at all will be even less effective. And even if there is an effective remedy on the books, agencies are unlikely to have the interest and expertise in antitrust necessary to detect and enforce violations.

"Unlikely" is not "never," of course; there will be situations in which regulatory agencies can play an effective antitrust role in policing purely private conduct, and in those circumstances

[74] *See* 1A Areeda & Hovenkamp, *supra* note __, at 274-75 (arguing that antitrust should apply where "authorized oversight is incomplete or lacking entirely," and that "oversight [is] nearly always incomplete").

[75] The *Trinko* Court is sensitive to the first problem, though not the second. It finds antitrust inappropriate if there is "a regulatory structure designed to deter and remedy anticompetitive harm," but it at least willing to apply antitrust if there is no such structure. *Trinko*, 540 U.S. at 412.

the Court's argument that antitrust law is less important is fair. It is worth noting, however, that that argument has not carried the day in any other area of antitrust law. Federal antitrust law does not preempt state antitrust enforcement, even though states may have different and even occasionally conflicting rules governing remedies and even though the resulting remedies may be cumulative.[76] U.S. antitrust law reaches across national boundaries to stop purely foreign conduct that has an effect on U.S. commerce,[77] even though foreign nations also have antitrust laws and the overlap between them means that mergers and other conduct allowed in the U.S. may nonetheless be banned by foreign antitrust agencies.[78] Federal and state antitrust enforcement co-exists with private rights of action under both state and federal antitrust laws,

---

[76] Areeda & Hovenkamp, *supra* note __, at ¶ 216 p. 345 ("federal and state policy often overlap and address precisely the same practices, often with inconsistent results"); *id.* ¶¶ 2411-2419 (discussing inconsistencies between state and federal law); *see* California v. ARC Am. Corp., 490 U.S. 93 (1989) (holding that federal law did not preempt state antitrust laws allowing indirect purchasers to sue for damages).

[77] United States v. Nippon Paper Indus. Co., 109 F.3d 1 (1st Cir. 1997) ("Section One of the Sherman Act applies to wholly foreign conduct which has an intended and substantial effect on the United States"); *cf.* F. Hoffman-LaRoche Ltd. v. Empagran S.A., 542 U.S. 155 (2004) (clarifying that such antitrust suits can reach only behavior that causes domestic injury, and cannot address conduct that causes independent *foreign* harm).

[78] In 2001, for example, the European Community blocked a merger between General Electric and Honeywell that United States antitrust authorities had allowed, raising the ire of both antitrust authorities and the business community in the U.S. *See* Commission Decision 2004/134, Case COMP/M.2220, General Electric/Honeywell, 2004 O.J. (L 48) 1, *at* http://ec.europa.eu/comm/competition/mergers/cases/decisions/m2220_en.pdf ; *see also* Editorial, *Europe to GE: Go Home*, **Wall St. J.**, June 15, 2001, at A14 ("In the Honeywell case, novel antitrust theories have been dreamed up simply because it would be unthinkable to let a large U.S. company go about its business unmolested."); Remarks of Deborah Platt Majoras, Deputy Assistant Attorney General, Antitrust Division, Before the Antitrust Law Section, State Bar of Georgia, Nov. 29, 2001, at http://www.usdoj.gov/atr/public/speeches/9893.htm#N_2_ ; *see generally* Henry C. Thumann, *Multijurisdictional Regulation of Monopoly in a Global Market*, 2008 **Wisc. L. Rev.** 261, 262-63 (noting that "like the United States," other countries "have reached out and will continue to reach out to regulate conduct that directly lessens competition within their markets, regardless of where the triggering conduct occurs").

even though some have argued that the result is cumulative overdeterrence.[79] And Antitrust Division review of certain mergers under Hart-Scott-Rodino[80] coexists with the review of other specialty agencies. The Department of Transportation must sign off on airline mergers, and the FCC on telecommunications mergers,[81] for example, even though the Antitrust Division and the FTC respectively have concurrent jurisdiction over those mergers. In short, antitrust law does not generally worry about the effects of overlapping enforcement, except when it comes to challenges to the behavior of regulated firms.

---

[79] *See, e.g.*, Jonathan T. Tomlin & Dale J. Giali, *Federalism and the Indirect Purchaser Mess*, **11 George Mason L. Rev**. 157, (2002) (contending that states' recognition of antitrust claims by indirect purchasers "could lead to inconsistent determinations and potentially duplicative damages, … the erosion of the effectiveness of antitrust law, … arbitrary penalties and deterrence and a likelihood of overdeterrence"); Bruce H. Kobayashi, *Antitrust, Agency, and Amnesty: An Economic Analysis of the Criminal Enforcement of the Antitrust Laws Against Corporations*, 69 **Geo. Wash. L. Rev.** 715, 732-33 (2001) (noting risks of overdeterrence); *cf.* Michael K. Block & Joseph Gregory Sidak, *The Cost of Antitrust Deterrence: Why Not Hang a Price Fixer Now and Then?*, 68 **Geo. L.J.** 1131, (1980) (contending that because of error risks, high antitrust sanctions may over-deter and result in suboptimal competition). It is far from clear that this overdeterrence concern is warranted in the modern world, however. *See* Robert H. Lande, *Benefits from Private Antitrust Enforcement: An Analysis of Forty Cases*, 42 **U.S.F.L. Rev.** 879, 907 (2008) (noting that criminal antitrust conduct "occurs far too frequently and is almost certainly significantly underdeterred – even factoring in the effects of the present system of private litigation"); Robert H. Lande, *Why Antitrust Damage Levels Should Be Raised*, 16 **Loyola Consumer L. Rev.** 329, 329 (2004) (contending that, "if the current antitrust damage levels are examined carefully, they do not even total treble damages, and overall are not high enough to deter antitrust violations optimally").

[80] Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18(a).

[81] Indeed, because the agencies have different mandates, their merger approval is often subject to different conditions. *Compare, e.g.*, United States v. AT&T Corp., 65 Fed. Reg. 38,583 (DOJ June 21, 2000), *at* gov/atr/cases/f4800/4841.pdf (D.D.C. 2000) (consent decree approving merger subject to divestiture of certain interests of acquired party), *with In re* Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from MediaOne Group, Inc. to AT&T Corp., *Memorandum and Order*, 15 F.C.C.R. 9816 (2000), *at* http://www.fcc.gov/bureaus/cable/orders/2000/fcc00202.doc (approving merger subject not only to DOJ consent decree regarding divestitures, but also to additional divestiture requirements and a commitment to provide nondiscriminatory access to network by unaffiliated internet service providers).

Our goal in this section is not to argue that regulation never works, much less that antitrust should habitually second-guess decisions made by regulators. Our point is more limited. We worry that the recent trend toward antitrust deference has increasingly blurred the line between deference to regulatory *action* and deference to regulatory *inaction*. Such a trend, if it continued, could lead to complete antitrust immunity in regulated markets. This mutant form of antitrust deference – presumably based on the assumption that regulation is a more efficient way of preventing private anticompetitive conduct than antitrust enforcement – would be fundamentally misguided. Economics counsels against trusting regulators to look for, find, and deter anticompetitive conduct by private actors. It therefore counsels against a broad view of antitrust deference, and in favor of the conflicts-based approach that has long preserved the balance between antitrust laws and industry regulation.

III. An Analytical Framework

So far, we have shown why antitrust law has a continuing role to play in regulated industries. At the same time, we recognize that for regulation to be effective, regulators must have the power to fulfill their statutory mandate without constant oversight from antitrust courts. In this section, we suggest some principles for deciding when antitrust law should apply to behavior in regulated industries, and when courts should defer to regulators.

First, we believe antitrust courts are correct to defer to regulatory decisions themselves. If a regulator sets the price a company must charge, or sets entry conditions that prevent competition that might otherwise have existed, the result is anticompetitive, but the harm to competition results directly from decisions made by regulators who have the specific jurisdiction over the matter.[82] Antitrust law does not trump other laws, but must coexist with them. If the law gives regulators control over a particular decision, antitrust law should not second-guess that decision.[83] Indeed, paradigmatic cases of such state action don't involve private exclusionary behavior at all; it is the regulator, not the party being regulated, that creates whatever competitive harm exists.

Second, regulatory "gaming" that involves efforts to capture regulators or persuade them to limit competition will generally not be actionable so long as the effort to persuade regulators to one's viewpoint is a genuine one and so long as the anticompetitive effects result from the actions of the regulator so persuaded and not from the petitioning effort itself. Deference in this situation follows from the *Noerr-Pennington* doctrine and the First Amendment interests involved, but it also reflects the fact that private behavior that persuades a regulator to limit competition is not really private regulatory gaming at all, but ultimately public action, albeit public action encouraged by an interested private party.

In these petitioning/capture cases, however, deference should not be as absolute as it is in the pure state action cases. There are two circumstances in which private petitioning to obtain anticompetitive government action can run afoul of the antitrust laws. First, the government must in fact be the relevant actor. A government that reflexively blesses whatever prices are set by a private cartel is not in fact exercising its regulatory authority at all. Only if the government

[82] *See* I Areeda & Hovenkamp, *supra* note __, at ¶ 202 p. 166 ("Once a court recognizes the official action as authorized under a valid statute, the antitrust court must recognize that any harm to competition results from government decision rather than from the private action that may have induced official action.").

[83] *See* Town of Concord v. Boston Edison Co., 915 F.2d 17, 28 (1st Cir. 1990) ("At best, permitting judges and juries to speculate in this area would force regulators continually to revisit prior investment-allocation rules and would discourage regulatory efforts to develop (often with a utility's help) a set of economically rational pricing practices – which, after all, is a common objective of antitrust law and regulation."); *see generally* **I Areeda & Hovenkamp, Antitrust Law** .

actually makes the relevant decision and supervises the private party it is regulating should antitrust law defer to that decision. Existing case law in the state action doctrine requires that a government agency clearly articulate its rules and actively their implementation; those rules aren't perfect, but they seem a reasonable basis for drawing the distinction we are discussing here. Second, regulatory deference should not apply in situations in which the private party has effectively abrogated the decisionmaking authority of the regulator by making deliberately false statements that were material to the decisionmaking process.[84] The *Unocal* case, discussed in Part IV below, falls within that category.

Third, antitrust law should *not* defer either to regulatory silence or to private action in the shadow of a regulatory structure. Where the government has not affirmatively decided to pursue an anticompetitive course, or where the cause of competitive harm is not government action at all but private action that takes advantage of a set of regulatory rules, antitrust has an important role to play.

These principles preserve the complementary relationship between antitrust law and regulation. They respect the role of regulators within their jurisdiction, while maintaining antitrust courts as the stewards of competition when regulators are unable or unwilling to serve that function. The need for antitrust oversight becomes particularly acute when the regulatory scheme itself creates opportunities for exclusionary conduct – a phenomenon that we call regulatory gaming.

[84] *See, e.g.*, Armstrong Surgical Center, Inc., v. Armstrong County Memorial Hosp., 185 F.3d 154 (1999); FTC opinion in UnoCal case at 20 ("Misrepresentation … undermines this line of analysis by blurring the distinction between private and governmental conduct. Misrepresentation undermines the government's ability accurately and meaningfully to assess public benefit; it vests control over the outcome in the private purveyor of false information.").

IV. Regulatory Gaming and the Case for Antitrust Intervention

We define regulatory gaming as behavior that abuses a neutral or pro-competitive regulatory structure and wields it as a tool to accomplish exclusionary results. The notion of "abuse" is critical: we are not talking about ordinary government petitions, even those that are motivated by anticompetitive animus. Abuse involves private conduct that distorts the regulatory process, rather than petitioning behavior designed to influence it.[85] In many cases of gaming, regulators either do not have the tools to detect and address the exclusionary behavior at issue, or they can do so only after the fact, through tepid ex post responses that do nothing to deter the next round of games. In comparison, antitrust law offers important advantages: it's flexible, it allows courts to look at the big picture and detect patterns of exclusionary behavior, and the heft of its penalties can deter future misconduct.

In this section, we explore three different forms of regulatory gaming, and consider the role of antitrust law in reviewing the gaming behavior. Each of our examples has two characteristics: first, a regulatory framework that determines certain industry characteristics (such as price or entry); and second, private conduct that usurps the intended function of that framework and converts it into an instrument to suppress competition. In all three cases, we contend that antitrust law has a role to play in evaluating the legality of the defendant's acts. This does not mean that the behavior is always condemned; antitrust law's own internal limits will often bar a successful claim. Indeed, in our third example – the price squeeze – we suggest

[85] This is not to say that petitioning behavior can never qualify as gaming. As the *Unocal* case illustrates, *see infra* text at notes __-__, parties can manipulate a regulatory process by using deception or misrepresentation to achieve exclusionary outcomes, and the law should not immunize such conduct any more than it immunizes sham litigation, *see* California Motor Transport Co. v. Trucking Unlimited, 404 U.S. 508, 512 (1972), or the knowing attempt to enforce a patent procured by fraud, Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172 (1965).

that plaintiffs should rarely prevail. Our point is simply that *antitrust law* should determine the outcome of these cases. It makes no sense to dismiss them merely because a regulator has a finger in the pudding. The persistence of regulatory gaming, its presence across a variety of regulated industries, and the threat it can pose to competition across our economy suggest that the generalized standards of antitrust law have an important role to play in curbing this market-distorting phenomenon.

A. Pharmaceutical product-hopping

The pharmaceutical industry presents a perfect storm for regulatory gaming. The regulator – the Food and Drug Administration ("FDA") – controls product entry through a complex set of regulations that feature lag time, periods of market exclusivity, and patents whose validity and scope are often the subject of lengthy and contentious litigation. And while Congress placed the ultimate goal of generic entry front and center in the FDA's drug approval framework, the agency itself has neither the mandate nor the power to take competition concerns into account in approving particular pharmaceutical products. Each of these regulatory features creates an opportunity for unscrupulous drug manufacturers to game the system in a way that extends their manufacturing exclusivity, to the detriment of competitors and the public. As a result, pharmaceutical gaming has taken many forms over the years.[86] This section explores one of its more recent incarnations – pharmaceutical "product hopping."

Product hopping takes advantage of the lag times inherent in the FDA's generic approval process. Generally, to introduce a new drug to market, a pharmaceutical company must provide

[86] *E.g.*, Valley Drug v. Geneva Pharmaceuticals, Inc., 344 F.3d 1294 (11th Cir. 2003) (rejecting, on substantive antitrust grounds, a challenge to a "reverse settlement agreement," in which a patent-holder paid a generic firm to stay out of its market).

direct evidence of its safety and efficacy;[87] upon approval, it must also provide a listing of any relevant patents in the FDA's "Orange Book."[88] The Hatch-Waxman Act, which Congress passed in 1984, expedites the approval process for generic follow-on drugs.[89] Rather than submitting full safety and efficacy data, a generic manufacturer can obtain FDA approval by filing an Abbreviated New Drug Application ("ANDA"), certifying the bioequivalence between its generic and an existing branded drug.[90] The statute requires the FDA to complete its review within 180 days, but the process often takes longer.[91] Once approved, the generic receives an "AB-rating," which allows pharmacists to substitute the generic when presented with a prescription for the branded product.[92]

---

[87] Between animal testing, clinical trials, and FDA approval, the process for new drug approvals can take up to ten years. *See* Judy Vale, *Note: Expanding Expanded Access: How the Food and Drug Administration Can Achieve Better Access to Experimental Drugs for Seriously Ill Patients*, 96 **Geo. L.J.** 2143, 2169 & n.212 (2008).

[88] 21 U.S.C. § 355(b). The Orange Book (officially entitled "Approved Drug Products with Therapeutic Equivalence Evaluations" but nicknamed for the color of its cover) provides a comprehensive listing of all drugs approved by the FDA. *See* http://www.fda.gov/cder/ob/ (electronic version of Orange Book).

[89] Drug Price Competition and Patent Term Restoration Act, 21 U.S.C. § 355.

[90] 21 U.S.C. § 355(j). Because they lacked the resources to perform clinical trials, small generic drug makers found it difficult to meet the pre-Hatch-Waxman safety and efficacy requirements. Thus, very few generics were available even for drugs whose patents had expired. *See* David A. Balto, *Pharmaceutical Patent Settlements: The Antitrust Risks*, 55 **Food & Drug L.J.** 321, 325 (2000). The Hatch-Waxman Act improved things considerably, leading to a 150% increase in the market share of generics between 1984 and 1998. *See* Congressional Budget Office, *How Increased Competition From Generic Drugs Has Affected Prices and Returns*, The Pharmaceutical Industry 1 (July 1998).

[91] 21 U.S.C. § 355(j)(5)(A); *see* Department of Health & Human Services, *The Food & Drug Administration's Generic Drug Review Process*, *avail. at* http://oig.hhs.gov/oei/reports/oei-04-07-00280.pdf (noting that FDA review process for ANDAs often exceeds the 180-day statutory maximum).

[92] As a general matter, state laws authorize such substitution, and payors (such as insurance companies, HMOs, and government agencies) decide whether to allow or mandate substitution for their covered patients. As the price of branded drugs continues to escalate, more and more insurers and other parties require generic substitution when available. *See* Milt Freudenheim,

While the bioequivalence certification addresses the FDA's safety and efficacy requirements, it does not necessarily qualify the generic to enter the market: the product may be covered by a patent. The Hatch-Waxman Act therefore requires generic manufacturers to identify any patents potentially relevant to their ANDA.[93] If a patent is listed and unexpired, the generic manufacturer must certify either that its product does not infringe the patent, or that the patent is invalid.[94] It must also notify the patentee immediately, after which the patentee has 45 days to sue for infringement.[95] If the patentee sues, it gets an automatic *30-month* stay of the ANDA application.[96] The FDA has no discretion to quicken this stay, nor can a judge shorten it through preliminary relief. According to the statute, only a final court judgment of non-infringement or invalidity can truncate the thirty-month wait.[97] As Lemley and others have pointed out elsewhere, "The effect of this rather remarkable rule is to delay drug price competition for several years even when a patent is clearly invalid, by granting what is akin to an

---

Medicare Plans Affected by Rising Drug Costs, **N.Y. Times**, April 19, 2008, *at* http://www.nytimes.com/2008/04/19/business/19specialtyside.html (noting rising costs of drugs for elderly patients, and the effect on the federal budget).

[93] *Id.* § 355(j)(2)(A)(iv). More specifically, the Hatch-Waxman Act requires certification that the drug falls within one of the following categories: (I) no relevant patent is listed in the Orange Book; (II) the patent listed in the Orange Book is expired; (III) the ANDA only seeks approval after the expiration date of the patent listed in the Orange Book; or (IV) the ANDA does not infringe the patent listed in the Orange Book, or the patent is invalid.

[94] *Id.* § 355(j)(2)(A)(vii). The Hatch-Waxman Act offers a special bonus to the first generic manufacturer to file a Paragraph IV certification for a branded drug. If the first filer succeeds with its paragraph IV application – because of non-infringement, invalidity, or otherwise – it receives a 180-day head start before other generics can enter the market. *Id.*

[95] *Id.* § 355(j)(2)(B), (j)(5)(B)(iii). In its notice to the patentee, the generic must explain in detail the reason that it believes the patent invalid or not infringed.

[96] Indeed, the stay can be longer than 30 months, depending on when the generic files its Paragraph IV certification. *See* Hemphill, *supra* note __, at 1566 n. 50. And a judge does have power to truncate the stay if either party fails to cooperate in the litigation. *See id.*.; 21 U.S.C. § 355(j)(5)(B)(iii).

[97] 21 C.F.R. § 314.107(b)(3).

automatic preliminary injunction whenever a pharmaceutical patent owner files suit against a generic manufacturer."[98]

Creative patent-holders have found several ways to convert this regulatory framework into an exclusionary tool. Before 2004, firms could extend their exclusivity for a product almost indefinitely, by adding new patents to their Orange Book filings and stacking up consecutive 30-month stays.[99] After Congress corrected that particular problem, crafty firms took a different tack: rather than stacking patents, they stacked *products* – making trivial changes to their product formulation and pulling the old drug from the market. This "product-hopping" delays generic competition in two ways. First, like the earlier forms of evergreening, product-hopping can prompt a whole new set of Orange Book filings, ANDA paragraph IV certifications, and litigation-triggered 30-month stays. Second, even without new patent claims, product-hopping delays generic substitution for the new branded product, because the generic firm must file a second ANDA, which faces the same lengthy FDA review as the first one.[100]

---

[98] Herbert Hovenkamp et al., **IP and Antitrust** § 12.4c at 12-43 (2005 Supp.).

[99] In Apotex, Inc. v. Thompson, 347 F.3d 1335 (Fed. Cir. 2003), for example, the drug manufacturer had originally named a single patent in its Orange Book listing for a pioneer drug. In response to a generic's ANDA and Paragraph IV certification, the manufacturer sued for patent infringement, thus triggering an initial 30-month stay. While that lawsuit was pending, the manufacturer obtained additional patents, which it added to its Orange Book listing and used as the basis for yet another lawsuit and stay. Remarkably, while that lawsuit was pending, the firm listed three additional patents in its Orange Book listing for the same drug, thereby triggering yet another round of notice, lawsuit, and 30-month stay. *See also In re* Buspirone Antitrust Litigation, 185 F. Supp. 2d 363 (S.D.N.Y. 2002).

Congress passed legislation in 2003 to eliminate this particular form of patent "evergreening." The new law limits patentees to a single 30-month stay for any given drug, regardless of how many patents it may list in the Orange Book. 21 U.S.C. § 355(j)(5)(b). *See* Hovenkamp et al., *supra* note __, at § 12.4c.

[100] The generic firm may, of course, continue to offer the *first* drug, for which it already gained approval. That means nothing, however, if the branded firm has pulled that drug from pharmacy shelves and convinced doctors to write scripts for its new product. Until the ANDA for that new

The defendant in *Abbott Laboratories v. Teva Pharmaceuticals USA, Inc.*,[101] capitalized on both of these forms of delay. The case involved Abbott's sale and manufacture of fenofibrate, a drug used to treat high triglyceride levels. The saga began in 1998, when Abbott first received approval of its NDA for a capsule form of fenofibrate, which it marketed under the TriCor brand. The next year, Teva filed an ANDA, seeking approval to sell a generic version of TriCor and certifying that its product did not infringe any valid or enforceable patents. Abbott responded with an infringement suit, which triggered the automatic 30-month stay.[102] The judge in the patent suit ultimately agreed with Teva that its product did not infringe, but because Abbott appealed to the Federal Circuit (a losing, but effectively time-consuming, expedition), Teva had to wait almost two years for its final judgment.[103]

In the meantime, Abbott lost little time in devising a strategy to fend off the impending competition from Teva. While the capsule litigation was pending, Abbott submitted an NDA for a *tablet* formulation of the same drug. The "new" product had a different dosage and listed a new indication,[104] but reflected no apparent advances over the capsule version; indeed, Abbott asserted the bioequivalence of the two products in its NDA, and relied on its capsule data to

product is approved (with its AB-rating), state laws limit pharmacists' ability to substitute the "old" generic for the "new" branded drug.

[101] 432 F. Supp. 2d 408 (D. Del. 2006). To the extent it is relevant, Mark Lemley represents Impax, the antitrust plaintiff in this case.

[102] *Id.* at 416.

[103] *Id.*

[104] Abbott's tablet NDA claimed that the drug could increase levels of "good cholesterol." *Id.* at 416. In support of that claim, however, Abbott submitted data for the *capsule* formulation, and claimed that it was bioequivalent to the new tablets. *Id.* The new indication therefore did not arise from any new utility conferred by the tablets; to the contrary, Abbott's own documents suggested that the capsule form would have supported the same new indication.

support its safety and efficacy claims.[105] As soon as the FDA approved the tablet – and before final resolution of the capsule claim – Abbott launched its TriCor tablets and took extraordinary measures to terminate all possible sales of the capsule form.[106]

Abbott's capsule-tablet switch effectively prevented Teva from penetrating the fenofibrate market. Because pharmacists could not substitute Teva's product for the current version of TriCor – and could not even fill prescriptions for the earlier capsule form – Teva's sales were limited to those doctors who wrote prescriptions specific to Teva's own (Lofibra) brand of the product. Like most generic manufacturers, however, Teva's low-cost business model depended centrally on the ability to substitute for a branded drug, so its sales were, at best, "modest."[107]

The capsule-tablet switch also, predictably, ushered in the next round of the cat-and-mouse game. After Teva filed an ANDA for a generic substitute for the TriCor tablet, Abbott filed new patent infringement suits, which triggered yet another 30-month stay.[108] And while that litigation was pending, Abbott changed its formulation yet again, reducing the tablet dosage,

---

105 *Id.*

106 Abbott not only stopped selling the capsules, but it also bought all existing stock from pharmacies and changed the code for TriCor capsules in the National Drug Data File to "obsolete." "Changing the code to 'obsolete' removed the TriCor capsule drug formulation from the NDDF, which prevented pharmacies from filling TriCor prescriptions with a generic capsule formulation." *Id.*

107 Branded drug companies, of course, view this business model as a form of free riding, because the generic gets the benefit of the branded firm's investment in marketing and promotion. Generic competition, however, does not occur until after the pioneer drug has had several years of exclusivity in the market. And the government has clearly come down on the side of generic substitution, and for good reason: drugs are much cheaper and more widely available today than they were before the passage of the Hatch-Waxman amendments encouraging generic competition. All competition is in some sense "free riding," but that does not mean it is or should be forbidden. *See generally* Mark A. Lemley, *Property, Intellectual Property, and Free Riding*, 83 **Tex. L. Rev.** 1031 (2005).

108 *Abbott*, 432 F. Supp. 3d at 417. This time, Teva responded with an antitrust counterclaim, contending that Abbott's product switches violated Section 2 of the Sherman Act. *Id.*

filing a new NDA, and abandoning the former product as soon as it obtained regulatory approval.[109]

Abbott may have had compelling reasons for its serial product changes beyond the most obvious one of foreclosing competition. If so, then antitrust doctrine requires courts to defer to Abbott's choices, regardless of their competitive effect.[110] If, however – as Teva alleged in its antitrust suit – Abbott made the changes specifically to fend off competition from generics, then it succeeded in harnessing the regulatory framework to preserve its exclusivity for several lucrative years.[111] In light of this obvious anticompetitive harm, the district court in *Abbott Labs* found Teva's antitrust allegations sufficient to survive a motion to dismiss.[112]

---

[109] Just as it did with the capsule/tablet change, Abbott pulled existing stock from shelves and revised the NDDF code to make the old tablet version obsolete. *Id.* at 418. Abbott did identify one arguable difference between the new and old tablets: in its NDA, it sought a label change stating that the new tablets no longer had to be taken with food. Teva alleged, however, that the change was made not to improve product efficacy, but only to prevent generic substitution. *Id.* at 418. And once again Abbott relied on its original safety and efficacy data from the pre-hop formulation, not on new studies, to support the "no food" designation.

[110] As the D.C. Circuit has explained:

> As a general rule, courts are properly very skeptical about claims that competition has been harmed by a dominant firm's product design changes. *See, e.g.*, Foremost Pro Color, Inc. v. Eastman Kodak Co., 703 F.2d 534, 544-45 (9th Cir. 1983). In a competitive market, firms routinely innovate in the hope of appealing to consumers, sometimes in the process making their products incompatible with rivals; the imposition of liability when a monopolist does the same thing will inevitably deter a certain amount of innovation.

United States v. Microsoft Corp., 253 F.3d 34, 65 (D.C. Cir. 2001).

[111] Teva filed its first ANDA in 1999, and as of this writing, the FDA does not list a generic equivalent for the most recent tablet formulation. *See* www.accessdata.fda.gov.

[112] 432 F. Supp. 2d at 422-24. A group of states has also sued Abbott in connection with the TriCor product changes, and the FTC has launched an official investigation into Abbott's behavior. *See* State of Florida et al., v. Abbott Labs., No. __ (D. Del. Complaint Filed March 18, 2008); *see generally* Shirley S. Wang, *TriCor Case May Illuminate Patent Limits*, **Wall St. J.**, June 2, 2008, at B1. The court recently denied Abbott's motions for summary judgment, and the case is now set for trial.

Abbott is not alone in finding exclusionary opportunities in the FDA's drug approval framework. In *FTC v. Warner Chilcott Holdings*,[113] the FTC alleged that Warner Chilcott attempted a similar scheme with its birth control drug, Ovcon. In the months before approval of a generic ANDA, Warner Chilcott's executives hatched a strategy to switch from pill to chewables to prevent generic substitution. When a delay in its NDA approval threatened to spoil its product-hopping plan, Warner Chilcott simply bought off the generic.[114] While the FTC's legal claims focused on this agreement rather than the product-hopping issue, the case shows that product-hopping happens, and that *Abbott Labs* was not an isolated case.

Pharmaceutical product-hopping presents a paradigmatic case of a regulatory game. Without the FDA's product approval framework, generic firms could quickly go to market with competing versions of branded drugs upon expiration of a patent – or even earlier, when they have confidence that their product does not infringe any valid patent on the drug.[115] But the lengthy product approval process – combined with the two-and-a-half year automatic stay that follows any patent suit – acts as a barrier to such competition. While that barrier may, in the ordinary course, be a necessary cost of accommodating patent rights and health and safety concerns,[116] product-hopping exploits it precisely because of its exclusionary effects and

113 2005 WL 3439585 (D.D.C. Complaint Filed Nov. 7, 2005).

114 *Id.* at 9 (noting letter of intent, in which Warner Chilcott would pay Barr (the generic manufacturer) $20 million in exchange for Barr's agreement not to compete in the United States for five years after receiving final FDA approval).

115 The generic in such a case might well face a patent infringement suit, but to obtain an injunction against sale of the drug, the branded manufacturer would have to prove a substantial likelihood of success on its infringement claims. Under the current framework, the "injunction" is automatic, and bears no relation to the merits of the patent claim.

116 We are skeptical that the 30-month automatic stay – with no judicial discretion to override it in lawsuits of questionable merits – is necessary, but our point here is that the stay may serve a legitimate function in some cases but creates an opportunity for abuse in others, and that such abuse should be actionable under antitrust laws.

converts it into a tool for suppressing competition. Making matters worse, the regulators in these cases can do nothing to thwart this obvious abuse of their administrative function. And while Congress, the FDA, or states could theoretically address the problem prospectively by allowing generic substitution across formulations,[117] such an ex post solution would neither compensate for past harm, nor deter new variations of the regulatory game.

From an antitrust perspective, product-hopping to ward off generic competition is precisely the sort of behavior the Sherman Act condemns.[118] While monopolists have no general duty to help their competitors, they do have an obligation to refrain from acts that have no purpose but to exclude competition.[119] And while distinguishing between the two can be tricky, courts have proven themselves up to the task, even in cases involving product design.[120] It

117 *See* Guy V. Amoresano, *Branded Drug Reformulation: The Next Brand vs. Generic Antitrust Battleground*, 62 **Food & Drug L.J**. 249, 256 (2007) ("It may be that a more appropriate approach to the issues raised by reformulation strategies is to leave it to FDA and the state legislatures to determine if some modification of FDA "AB rating" guidelines and state DPS Laws is prudent to address scenarios in which inconsequential reformulations affect the speed of generic drug market entry."). Such an approach would raise challenges of its own, such as how to treat substitutions between products with the same active ingredients but different dosages.

118

> "The offense of monopoly under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historical accident."

United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966).

119 *See id.* (condemning behavior that "was done plainly and explicitly for a single purpose" of driving out competitors); *see also* United States v. Microsoft Corp., 253 F.3d at 65 ("Judicial deference to product innovation … does not mean that a monopolist's product design decisions are per se lawful.").

120 *Microsoft*, 253 F.3d at 65-67 (balancing anticompetitive effect of design choices against business justifications offered by defendant).

makes no sense to immunize patently anticompetitive behavior because of the risk that some cases might prove tough to decide.

The district court in the *Abbott* case – following the analytical structure established in the D.C. Circuit's *Microsoft* opinion – outlined what we view as a reasonable approach to the product-hopping problem.[121] Most significantly for our purposes, the court applied antitrust law to the gaming behavior, rather than washing its hands of the case because of its regulatory context. On the merits, the court applied the rule of reason, first requiring plaintiffs to show that the defendant's product changes had anticompetitive effect.[122] The court held that plaintiffs had met their burden (at least in the context of a motion to dismiss) by alleging that Abbott's change in formula, paired with its abandonment of the old drug, blocked plaintiffs from "their cost-efficient means of competing in the pharmaceutical drug market,"[123] thereby harming both plaintiffs and consumers. The court suggested that defendants could rebut the showing of competitive harm by establishing a valid business reason for the behavior.[124] "[I]f such a justification were offered, the plaintiff could rebut it or, alternatively, establish antitrust liability by demonstrating that 'the anticompetitive harm of the conduct outweighs the procompetitive benefit.'"[125]

---

[121] *Abbott*, 432 F. Supp. 2d at 422 (citing *Microsoft*, 253 F.3d at 66-67).

[122] *Id.* ("Plaintiffs are not required to prove that the new formulations were absolutely no better than the prior version or that the only purpose of the innovation was to eliminate the complementary product of a rival. Rather, as in *Microsoft*, if Plaintiffs show anticompetitive harm from the formulation changes, that harm will be weighed against any benefits presented by Defendants.").

[123] *Id.* at 423.

[124] *Id.* at 422.

[125] *Id.* (quoting *Microsoft*, 253 F.3d at 59, 67). *See generally* Hovenkamp, Janis & Lemley, *supra* note __, at § 12.3; William Kolasky, *Reinvigorating Antitrust Enforcement in the United States: A Proposal*, 22 **Antitrust** 85, 88-89 (2008) (suggesting a "sliding scale" framework for weighing pro-competitive and anti-competitive effects in rule of reason cases).

The *Abbott* opinion leaves open some important questions of antitrust doctrine. The court does not, for example, explain how a fact-finder should go about balancing the pro- and anti-competitive effects of a change in formula. Nor does the court resolve whether a change in formula alone, unaccompanied by the shelf withdrawals and other evidence of exclusionary intent in *Abbott*, would suffice to state a monopolization claim.[126] These questions, we believe, require case-by-case resolution, just as any rule of reason balancing inquiry does. Our goal here is not to settle those questions, or to suggest that they will prove easy in close cases. Our claim is that these are *antitrust* questions, to be addressed as a matter of antitrust law. Product hopping illustrates just how effectively firms can manipulate the FDA's regulatory system, and the extraordinary impact that their behavior can have on competition in drug markets. If a pharmaceutical company designs its products for the sole purpose of dragging out a regulatory process for years and thereby forestalling competition, it has engaged in exclusionary behavior that harms consumers. The fact that it has done so by taking advantage of a loophole in the regulatory scheme does not mean that the FDA has blessed this anticompetitive behavior or that antitrust law must get out of the way to avoid interference in the regulatory scheme. Product hopping is thus one example of a dangerous, market-distorting regulatory game, and a reason that antitrust courts should continue to pay attention to regulated markets.

B. Industry capture of government standard-setting: Unocal

[126] The court in Walgreens v. Astrazeneca Pharmaceuticals L.P., 534 F. Supp. 2d 146 (D.D.C. 2008), rejected a product-hopping antitrust claim based, in part, on the fact that the defendant in that case had not pulled its earlier product from the market after it introduced a new formulation. *See id.* at __ ("here, there is no allegation that AstraZeneca eliminated any consumer choices[; r]ather, AstraZeneca added choices"). Because the defendant continued to sell the old product, the generic in that case could take advantage of generic substitution laws, so the competitive harm alleged in *Abbott* was largely absent in *Walgreens*.

In pharmaceutical product-hopping, the gaming party uses product manipulation to convert neutral product approval rules into tools to exclude entry. Another form of gaming achieves its anticompetitive goals through direct manipulation of the regulatory process – the use of deceit or other misconduct to obtain regulatory outcomes that favor the gaming firm.[127] Like product-hopping, these cases raise tough questions, and require courts to strike a tricky balance between regulatory deference and antitrust intervention. The questions here are tougher than in product-hopping, because the anticompetitive conduct involves the participation (albeit unwitting) of a regulatory agency itself. In particular, the *Noerr-Pennington* doctrine forbids antitrust review of some forms of government petition, even when they may mislead.[128] The doctrine does not, however, require abstention in all cases at all times.[129] In particular, when an agency explicitly relies upon misleading factual submissions by a regulated party, and those

[127] The recent *Discon* case provides another example of this sort of regulatory game. The regulated party in that case engaged in a kickback scheme to deceive regulators into believing that its costs were higher than they really were; the regulators relied on the party's submissions and approved inflated regulated rates; and consumers footed the bill. Nynex Corp. v. Discon, Inc., 525 U.S. 128 (1998). The Supreme Court appeared almost scornful of the idea that the regulatory fraud could form the basis for an antitrust complaint, declaring that "[t]o apply the *per se* rule here – where the buyer's decision, though not made for competitive reasons, composes part of a regulatory fraud – would transform cases involving business behavior that is improper for various reasons, say, cases involving nepotism or personal pique, into treble-damages antitrust cases." *Id.* at 136-37. Because *Discon* involved a very precise legal question, however – the question of whether to apply *per se* analysis to the alleged boycott in that case – the Court's dismissive language does not necessarily preclude a rule of reason claim based on the same set of facts, but with proof of market power or adverse market impact. *See id.* at 135 ("the specific legal question before is us whether an antitrust court considering an agreement by a buyer to purchase goods or services from one supplier rather than another should (after examining the buyer's reasons or justifications) apply the *per se* rule if it finds no legitimate reason for that purchasing decision").

[128] Eastern RR Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127, 136, 140-41 (1961).

[129] *See* BE&K Const. Co. v. N.L.R.B., 536 U.S. 516, 525-26 (2002) ("while genuine petitioning is immune from antitrust liability, sham petitioning is not").

submissions materially affect an agency decision that turns out to have exclusionary effects, antitrust law can and does have something to say.

The *FTC v. Unocal* case epitomizes this form of gaming.[130] *Unocal* involved misrepresentations made to the California Air Resources Board ("CARB"), a state agency charged with reducing fuel emissions. In the late 1990s and early 2000s, CARB conducted a rulemaking process to develop specific, stringent standards for low-emissions gasoline. Unocal participated actively in the rulemaking process, advocating a set of standards that closely resembled the ones ultimately adopted by CARB.[131] In its submissions to the agency, Unocal never mentioned that it owned patent rights over the standards; indeed, it repeatedly touted their "flexibility" and "cost-effectiveness," and suggested that it had relinquished any proprietary interest that it might have once had in the standards.[132] In reliance on these representations, CARB adopted the standards, and refiners invested billions of dollars to comply with them. Only then, according to the FTC, did Unocal disclose its newly-minted patents and demand royalties for the use of the technology.[133]

Like Abbott's product manipulation, Unocal's misrepresentations effectively converted a neutral regulatory process into an exclusionary tool. The purpose of the CARB proceedings was to define a standard that would enable the production of cost-effective, environmentally sensitive fuels – *not* to give market power to one individual party. Yet Unocal's misrepresentations turned

---

[130] *See* Opinion of the Commission, In re Matter of Union Oil Company of California, Docket No. 9305 (opinion issued July 7, 2004), *avail. at* http://www.ftc.gov/os/adjpro/d9305/040706commissionopinion.pdf. For the complete filings and rulings in the case, *see* http://www.ftc.gov/os/adjpro/d9305/index.shtm.

[131] *Id.* at 3-5.

[132] *Id.* at 3-4.

[133] *Id.* at 6. The complaint also alleges that Unocal tweaked its patent applications during prosecution to match more closely with the emerging state standard. *Id.*

the regulators into unwilling (and unknowing) participants in a scheme to vest Unocal with just such power. According to the FTC, if CARB had known about Unocal's patent rights, it would have either adopted different standards, or insisted on more favorable terms of access to the standards by competitors.[134] In other words, the misrepresentations reflect "willful acquisition or maintenance" of power in the fuel market – the very definition of an antitrust breach.[135] From a consumer welfare perspective, the behavior caused just the kind of harm that antitrust laws seek to prevent – a structural barrier that will inevitably raise prices and cause inefficiently low production in the relevant market. Indeed, the fact that Unocal's conduct was directed to a state agency made competitive harm all the more likely. Other cases have considered misrepresentations to private standard-setting organizations;[136] those representations can facilitate monopolization of an industry, but only if they end up locking an industry into a standard that turns out to be patented. Market participants in private standard-setting organizations can choose not to adopt the standard. By contrast, no gasoline company can choose to ignore the CARB standard for reformulated gasoline; if Unocal's misrepresentations or omissions in fact caused the adoption of that standard, companies that want to sell gasoline in California had no choice but to pay Unocal whatever they demanded.

Despite these obvious competitive harms, some courts might hesitate to impose liability based on the *Unocal* version of regulatory gaming, for two reasons. First, the *Noerr-Pennington* doctrine, which insulates certain government petitions from antitrust liability, might give courts pause, since Unocal's anticompetitive conduct involved petitioning the government. Second, a

---

[134] *Id.* at 5.

[135] United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966).

[136] Rambus Inc. v. F.T.C., 522 F.3d 456 (D.C. Cir. 2008); Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297 (3d Cir. 2007).

recent decision of the D.C. Circuit casts doubt on the FTC's second theory of harm in *Unocal* – i.e., that an antitrust violation can lie based on misrepresentations that lead to a higher *price* in the market, rather than changing the standard itself. We think the first of these concerns requires careful attention to the facts, but in a case like *Unocal* does not justify antitrust abstention. The second concern is not an argument for abstention at all, but instead a substantive claim that there is no competitive harm in a case like this – a claim of which we are dubious.

1. *Noerr-Pennington* and regulatory games

Under the *Noerr-Pennington* doctrine, "[t]hose who petition the government for redress are generally immune from antitrust liability."[137] The principle applies to all sorts of petitions directed at any branch of government,[138] and derives from two basic tenets: first, that Congress cannot have meant for the Sherman Act to impair citizens' right to participate in our representative democracy;[139] and second, that the First Amendment would, in any event, bar such

[137] Professional Real Estate Investors, Inc. v. Columbia Pictures Indus., 508 U.S. 49, 56 (1993).

[138] *See* Eastern RR Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127, 136, 140-41 (1961) (applying doctrine to bar claim against railroad consortium based on misleading publicity campaign that was aimed to influence legislation); California Motor Transport Co. v. Trucking Unlimited, 404 U.S. 508 (1972) (holding that *Noerr* principle applies generally to petitions to administrative agencies); United Mine Workers v. Pennington, 381 U.S. 657 (1965) (invoking doctrine to petition of executive branch officials and administrative agencies).

[139] *See Noerr*, 365 U.S. at 137 ("In a representative democracy such as this, these branches of government act on behalf of the people and, to a very large extent, the whole concept of representation depends upon the ability of the people to make their wishes known to their representatives. To hold that the government retains the power to act in this representative capacity and yet hold, at the same time, that the people cannot freely inform the government of their wishes would impute to the Sherman Act a purpose to regulate, not business activity, but political activity, a purpose which would have no basis whatever in the legislative history of that Act.").

an interpretation.[140] The doctrine seeks to distinguish between commercial activities – which the Sherman Act addresses – and political activity, which lies beyond its reach.[141]

The doctrine, however, has limits. Even in *Noerr* itself, the Supreme Court cautioned that petitioning behavior could lose its protection if it were a "sham to cover what is actually nothing more than an attempt to interfere directly with the business relationships of a competitor . . . ."[142] Since then, the Supreme Court has applied the exception to misrepresentations made to courts and administrative agencies,[143] including patent infringement suits based on a patent obtained through fraud.[144] The cases following *Noerr* seem to distinguish between attempts to influence a legitimate government process, on the one hand, and behavior that shatters the integrity of the process and effectively converts it into a private affair, on the other.

While a full analysis of the *Noerr-Pennington* exemption falls beyond the scope of this paper,[145] we think the *Noerr-Pennington* doctrine must give way when a defendant has co-opted an administrative process through material misstatements or other fraud. When this happens, the

---

140 *See id.* at 138 ("The right of petition is one of the freedoms protected by the Bill of Rights, and we cannot, of course, lightly impute to Congress an intent to invade these freedoms.").

141 *Id.* at 137; *see id.* at 140-41 ("Insofar as [the Sherman] Act sets up a code of ethics at all, it is a code that condemns trade restraints, not political activity, and … a publicity campaign to influence governmental action falls clearly into the category of political activity.").

142 *Id.* at 144.

143 *See, e.g.*, California Motor Transport Co. v. Trucking Unlimited, 404 U.S. 508, 512 (1972) (finding no immunity when one group of highway carriers "sought to bar … competitors from meaningful access to adjudicatory tribunals and so to usurp that decisionmaking process" by "institute[ing] … proceedings and actions … with or without probable cause, and regardless of the merits of the cases").

144 *See* Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172 (1965).

145 For a thorough analysis of *Noerr* immunity in the context of agency misrepresentations, *see* FTC *Unocal* decision, *at* http://www.ftc.gov/os/adjpro/d9305/040706commissionopinion.pdf. We generally agree with the FTC's view that *Noerr* immunity does not apply to "deliberate misrepresentations that substantially affect the outcome of a proceeding or so infect its core to deprive the proceedings of legitimacy . . . ." FTC *Unocal* decision at 29.

defendant is not merely exercising its rights to influence a legitimate government process; it is effectively converting the process into a private vehicle to exclude competition.[146] As the FTC concluded in *Unocal*, "deliberate misrepresentations that substantially affect the outcome of a proceeding or so infect its core to deprive the proceeding of legitimacy may not, in appropriate circumstances, qualify for *Noerr-Pennington* protection."[147]

2. Evading regulatory limits as antitrust harm

The second open question is whether antitrust injury occurs when a defendant's misrepresentations prevent an agency from placing limits on an exercise of market power, rather than eliminating the market power altogether. In *Rambus v. FTC*,[148] the D.C. Circuit effectively held that where market power resulted from a regulatory decision (there, the grant of a patent), antitrust law could not constrain the price the monopolist charged. *Rambus* involved alleged misrepresentations made in the course of a private standard-setting organization's deliberations. The FTC claimed that Rambus had withheld material information about patent rights that it held over the relevant technology. The FTC alleged that if the SSO had known about Rambus's patents, *either* it would have adopted a different standard, *or* it would have demanded some form of fair and nondiscriminatory licensing terms on Rambus's patents. The D.C. Circuit found the second allegation legally inadequate, concluding that the mere *exercise* of market power (i.e.,

[146] *See* FTC *Unocal* decision at 29 ("Clearly, a proceeding fundamentally tainted by misrepresentation lacks the 'genuine' nature that is the hallmark of what the Supreme Court seeks to protect.").

[147] FTC decision at 29; *see also* Herbert Hovenkamp, *Federalism and Antitrust Reform*, 40 **U.S.F. L. Rev.** 627, 632-33 (2006) ("antitrust need not countenance restraints in which the effective decision makers are the market participants themselves").

[148] Rambus Inc. v. Federal Trade Commission, 522 F.3d 456 (D.C. Cir. 2008).

charging higher prices) does not violate the antitrust laws if the market power itself arose from a valid government grant.[149]

The *Rambus* court relied on *NYNEX v. Discon,*[150] in which the Supreme Court refused to apply the per se rule to a kickback scheme involving a regulated utility. The regulated party in *Discon* awarded a contract for non-regulated services to a company that would charge higher prices that the regulated company could then pass on to consumers through rate regulation. The *NYNEX* Court rejected an antitrust claim alleging that the scheme constituted an unlawful group boycott, absent proof that it harmed competition (not just a competitor) in the *non-regulated* service market. The Court specifically acknowledged that consumers were injured by the conduct, because it resulted in higher prices in the *regulated* market. Because that injury came from the exercise of agency-granted market power, however, the Court deemed it beyond the reach of antitrust law. While *NYNEX* itself involved only the question of whether the *per se* rule applied, *Rambus* read it as going further and immunizing any conduct that owed its origin to a regulatory grant of market power.

Both *NYNEX* and its substantial new extension in *Rambus* are problematic as matters of antitrust law. The harm to competition in *NYNEX* did not stem solely from government-granted market power; it stemmed from the defendant's effort to extend that market power in ways that deceived the regulatory agency and prevented it from controlling NYNEX's behavior. Similarly, the harm to competition in *Rambus* did not stem solely from the government's grant of a patent, but from the combination of that grant with Rambus's deception of a standard-setting organization that would otherwise have restrained the ability of Rambus to charge a

149 *Id.* at 464 ("But an otherwise lawful monopolist's use of deception simply to obtain higher prices normally has no particular tendency to exclude rivals and thus to diminish competition.").

150 525 U.S. 128 (1998).

supracompetitive price for that patent. Both of these cases, in other words, involve deliberate and effective regulatory gaming. By refusing to apply antitrust law to private deceptive conduct that manipulates a regulatory process, or extends or exacerbates the anticompetitive effects of a regulatory decision, *NYNEX* and *Rambus* appear to condone a new and insidious form of implicit antitrust deference to regulation, one in which antitrust law must ignore conduct that exacerbates competitive harm because the company causing that harm wouldn't have been in a position to do so but for regulation.[151]

Whatever one's views of the substantive antitrust issues, the existence of antitrust injury is an antitrust question that should be decided by antitrust courts, and will not (and often cannot) be adequately addressed by regulatory agencies. And neither *NYNEX* nor *Rambus* discredits the notion that abuse of standard-setting processes can, in some circumstances, violate the antitrust laws. In particular, if the facts show that an agency relied upon misrepresentations in choosing a standard – and would have chosen a different standard but for the misrepresentations – then the defendant has caused a structural harm in the market even in the narrow *Rambus* view. In these circumstances, the defendant's misrepresentations are the "but-for" cause of the defendant's

[151] Not all courts have taken the same approach to SSO-related misrepresentations. *See, e.g.*, Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 316 (3d Cir. 2007) (allowing antitrust claim based on allegations that misrepresentations to SSO either influenced the ultimate standard, or prevented SSO from limiting licensing fees).

economic monopoly.[152] While the D.C. Circuit refused to speculate on whether even this could constitute antitrust injury,[153] it strains credulity to imagine any other outcome.

Like product-hopping, then, abuse of government standard-setting processes can cause competitive harm in markets. And like product-hopping, the harm may not be remediable through administrative recourse. The capture of government standard-setting processes offers yet another example of regulatory gaming, and another reason that antitrust courts should continue to play a role in regulated markets.

C. The limits of regulatory gaming – price squeezes

Our final example, the price squeeze, illustrates the limits of antitrust law in addressing gaming behavior. Like the last two examples, a regulatory price squeeze involves manipulation of the regulatory system for anticompetitive ends. But it also often involves behavior which regulators have specifically endorsed, which falls within their core regulatory ambit, and which requires detailed knowledge of both firm and industry economics. In these circumstances, we think the benefits of antitrust intervention begin to fade in comparison with its costs, and courts should tread carefully. While a valid price squeeze claim is theoretically possible, it requires proof of predatory pricing in an unregulated retail market – a showing that is likely to be rare.

---

152 A patent, of course, confers a right to exclude, but does not necessarily confer power over any relevant market. But when a standard-setting body (private or government) settles on a standard that applies across an industry, and one party holds proprietary rights over that standard, the party does have monopoly power. It follows, then, that if a misrepresentation plays a material role in the selection of a patented standard, the misrepresentation has caused the type of harm to competition that the antitrust laws seek to prevent.

153 *See id.* at 463 ("We assume without deciding that avoidance of the first of these possible outcomes was indeed anticompetitive; that is, that if Rambus's more complete disclosure would have caused JEDEC to adopt a different (open, non-proprietary) standard, then its failure to disclose harmed competition and would support a monopolization claim.").

A price squeeze occurs when a vertically integrated firm with a regulated monopoly in an upstream market that faces competition in a downstream market compresses its wholesale and retail prices to make it impossible for others to compete with it in the downstream (retail) market.[154] If the wholesale price is high enough and the retail price low enough, competing retailers simply cannot cover their costs, and will be driven from the market. In *linkLine v. Pacific Bell*, for example, an integrated firm allegedly charged its retail competitors wholesale prices that *exceeded* its own retail rates.[155] A competitor obviously could not stay in the market for long when the cost of a single input is higher than the price it can charge consumers for its overall product.

The economics of price squeezes are the subject of some debate. Advocates of a "one monopoly profit" theory contend that price squeezes can cause no harm, because the upstream monopolist cannot raise the price any more by controlling two levels of production than it could by controlling only the upstream market.[156] Others, however, take issue with the single

[154] *See generally* Areeda & Hovenkamp ¶ 767c; American Bar Association Section of Antitrust Law, **Energy Antitrust Handbook** 121-25 (2002) (discussing price squeeze cases). Judge Learned Hand first recognized price squeezes as an antitrust violation in United States v. Aluminum Co. of Am., 148 F.2d 416, 437-38 (2d Cir. 1945).

[155] linkLine Communications, Inc. v. SBC California, Inc., 503 F.3d 876 (9th Cir. 2007).

[156] *See, e.g.*, J. Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4 **J. Comp. Law & Econ.** 279 (2008) ("If an unregulated, vertically integrated firm truly is a monopolist in the supply of the bottleneck input, and if downstream competitors use that input in fixed proportion to their production of the retail product, then the 'one monopoly profit theory' implies that the vertically integrated firm has no incentive to attempt the price squeeze."). The one monopoly profit theory has led to a general skepticism about applying antitrust law to vertical restraints. As described by Judge Posner:

> Imagine an industry with two levels, production and distribution: if production is monopolized and distribution is competitive, can the monopolist increase his profits by buying out the distributors? … If the producer acquires the distributors and increases the retail markup he will have to decrease the producer markup by the same amount. He cannot maximize his profits by charging a price above the monopoly price…."

monopoly price theory, and contend that monopolists can both increase their profits and insulate their economic power by leveraging their monopoly into related downstream markets.[157]

Whatever the economics of price squeezes more generally, most courts and commentators seem to agree that one form of price squeeze does raise antitrust concerns – a price squeeze involving *predatory* prices at the retail level.[158] In particular, when a monopolist lowers its retail prices to below its relevant measure of costs, it can face claims of predatory pricing like any other established or aspiring monopolist.[159] Predatory pricing alone can be illegal if the monopolist is likely to be able to recoup its costs. But the existence of a price squeeze by a monopolist can help ensure the success of predation as an exclusionary tactic. And

---

Richard A. Posner, **Antitrust Law: An Economic Perspective** 197 (1976); *see also* Phillip Areeda & Louis Kaplow, **Antitrust Analysis** 489 (5th ed. 1997) ("The power already possessed by the … monopolist to control the price and output … effectively controls the price and output of independent" downstream firms); Robert Bork, **The Antitrust Paradox** 229 (2d ed. 1993) ("[A] monopolist has no incentive to gain a second monopoly that is vertically related to the first, because there is no additional monopoly profit to be taken."); *cf.* Charles F. Rule, *Patent-Antitrust Policy: Looking Back and Ahead*, 59 **Antitrust L.J.** 729, 731 ("[T]here is only a single monopoly price for any given product, and you can either sell that product alone or you can combine it with as many complements as you want, but you are only going to be able to earn that one monopoly profit."); GKA Beverage Corp. v. Honickman, 55 F.3d 762, 767 (2d Cir. 1995) ("[A] vertically structured monopoly can take only one monopoly profit…").

157 *See, e.g.*, Pietro Crocioni, *Leveraging of Market Power in Emerging Markets: A Review of Cases, Literature, and a Suggested Framework*, 4 **J. Competition L. & Econ.** 449, 458-69 (2008) (summarizing arguments for and against one monopoly profit theory); *cf.* Roger D. Blair & David L. Kaserman, **Law and Economics of Vertical Integration and Control** 124. Then-Judge Breyer laid out the economic arguments for an against price squeezes in Town of Concord v. Boston Edison Co., 915 F.2d 17, 27-29 (1st Cir. 1990); *see also* Statement of the Federal Trade Commission, Petition for a Writ of Certiorari in Pacific Tel Co. d/b/a AT&T California v. linkLine Comms., Inc. (No. 07-512), *avail. at* http://www.ftc.gov/os/2008/05/P072104stmt.pdf.

158 Not all commentators view even predatory price squeezes as problematic. *See, e.g.*, Sidak, *supra* note __.

159 *See, e.g.*, Covad Communications Co. v. BellSouth Corp., 374 F.3d 1044, 1050 (11th Cir. 2004) (holding that price squeezing complaint states an antitrust claim if "the two basic prerequisites for a showing of price predation under § 2 of the Sherman Act are met"); Covad Communications Co. v. Bell Atlantic Co., 407 F.3d 1220, 1222 (D.C. Cir. 2005) (rejecting price squeeze claim, but noting that such a claim may lie if the plaintiff had alleged predatory pricing at the retail level).

if the monopolist is compensated for its regulated wholesale prices, the fact of regulation can also help the monopolist recoup its losses.

Price squeezes can, depending on the circumstances, involve a regulatory game. Price squeezes can occur in fully regulated markets (with regulated prices at both wholesale and retail levels), partially regulated markets (with regulated wholesale prices, but no regulation at retail), and unregulated markets. And while their use in fully regulated markets probably lies beyond antitrust courts' jurisdiction,[160] partially regulated price squeezes raise thornier questions. If, for example, a partially regulated firm convinces regulators to approve an unreasonably high wholesale price for an input that it controls, it can easily undercut its retail rivals, who must pay the wholesale price as a part of their cost of production. If the cost-cutting is predatory, the regulated party can effectively drive out its retail competition, which perverts the entire purpose of the wholesale price regulation – ensuring meaningful access to the input for competitors.

Yet even this form of predatory price squeeze raises difficult questions that lie at the very intersection between regulatory deference and substantive antitrust law. In particular, because predatory pricing claims require proof that a defendant priced below its costs, courts must consider the relationship between the regulated wholesale prices and the "appropriate measure" of a defendant's costs.[161] Should courts treat the regulated prices as an accurate measure of the cost of the regulated input, and assume that retail prices that fall below them are by definition predatory? Should courts instead treat the regulated wholesale price as irrelevant, and require direct evidence of the integrated firm's overall costs? Or, at the other extreme, should courts

[160] For reasons discussed more fully below, antitrust courts should not ordinarily second-guess decisions affirmatively made by regulators within their core area of expertise. For fully regulated industries, the fact that the regulator has specifically approved both levels of prices counsels against antitrust intervention.

[161] *See* Brooke Groupe Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222-23 (1993).

decide that antitrust laws have no role to play because of the existence of regulation at one level of production?

We can see good reasons to support either of the first two approaches to predatory price squeeze claims. While it seems reasonable to hold producers to what they tell regulators about their accurate measure of cost, the wholesale rates do not necessarily reflect the producer's cost of utilizing the wholesale input internally; it may well cost more to provide it to third parties.[162] On the other hand, courts may find the regulated rate useful as a benchmark to evaluate the credibility of cost evidence provided by the parties.[163]

The third option, however – complete abdication of antitrust law's role in a partially regulated industry – makes no sense as a matter of law or economic policy. In the (probably rare) case in which an integrated firm engages in true predatory pricing, its behavior can undermine competition in the retail market just like other forms of predatory conduct. Indeed, as with standard-setting, the fact of regulation may make the conduct more problematic than it would be in the absence of regulation, since the monopolist can rely on a government-approved wholesale price to compel payment by retail competitors and therefore to create the price squeeze. And the regulators in these cases have no power to address the exclusionary behavior, because their jurisdiction is limited to the wholesale – rather than the retail – price.

Of course, a predatory pricing claim requires proof of other elements as well – evidence of actual or potential monopoly power in the relevant (in this case, retail) market, as well as a likelihood of recoupment should the scheme succeed in driving competitors from the market. As

[162] Indeed, this is the main justification for vertical integration more generally: it often costs less to integrate different operational layers into a single enterprise.

[163] *Cf.* Covad Communications Co. v. BellSouth Corp., 374 F.3d 1044, 1051 (11th Cir. 2004) (holding that relationship between wholesale and retail prices "is a factual matter for the district court to determine at a later stage of proceedings").

a result, we think successful predatory price squeeze claims – like predatory pricing claims more generally – are likely to be rare. Their rarity, however, appropriately owes itself to stringent standards of substantive antitrust law, rather than absolute deference to regulators in even partially regulated markets.

The Supreme Court will have an opportunity to reflect on some of these issues this term in *Pacific Bell Telephone Co. v. linkLine Communications, Inc.*[164] *LinkLine* involves an alleged price squeeze in the DSL Internet services market, a partially regulated industry. According to linkLine, Pacific Bell not only compressed its wholesale and retail prices, but for a period, it charged other DSL providers wholesale prices that *exceeded* the fees charged to retail customers. If true, such a price structure would obviously make it impossible for competitors to buy DSL line access and resell it in competition with Pacific Bell. The Ninth Circuit held these allegations sufficient to state a claim for monopolization. The opinion hedged on a variety of points, including whether predation was necessary to state a price squeezing antitrust claim,[165] and whether unlawful price squeezes could occur in fully regulated markets.[166] The Ninth Circuit suggested, without holding, that a valid price squeeze claim might lie even when regulators approved prices at both levels.[167]

---

[164] 128 S. Ct. 2957 (2008, granting cert.).

[165] *E.g.*, linkLine Communications, Inc. v. SBC California, Inc., 503 F.3d 876 (9th Cir. 2007) ("We do not preclude the district court, however, from re-examining the viability of this claim on summary judgment after the record is more fully developed and it is clear whether the complained of behavior took place at the regulated wholesale level, the unregulated retail level, or some combination of the two, and to what extent, if any, the responsible agencies have devoted attention to or had involvement in the complained of conduct.").

[166] *Id.* at 883-84 (concluding that viability of price squeeze claim in fully regulated industry turns on the "particular industry and factual setting").

[167] The court cited an earlier Ninth Circuit opinion finding price squeeze claims possible in fully regulated markets, depending on the industry setting. *See id.*

The Supreme Court could resolve the *linkLine* case in a number of different ways. It could hold, as a matter of antitrust law, that the allegations in the case were insufficient to state a predatory pricing claim.[168] It could go further, and hold (as the defendant urges) that price squeeze claims of any stripe are implausible after *Trinko*.[169] It could surprise us all and uphold the price squeeze claim based on its (implicit) allegation of predatory retail pricing. Whatever it does, our argument is that the Court should do it as a matter of antitrust law and not blind regulatory deference. The Court will have an opportunity to clarify the relationship between antitrust law and regulation, and we hope it does so in a way that respects the continuing role of antitrust law in regulated industries. That does not mean the plaintiff should win the case; price squeeze claims, like other forms of predatory pricing, are rarely successful. But it does mean that the Court should not avoid the substantive issue altogether by wrongly assuming that the regulated agency can or will solve the problem.

V. Conclusion

Regulators cannot, should not, and do not substitute for antitrust courts in ensuring vibrant competitive markets. Indeed, as we have explained in this article, the existence of regulation can sometimes exacerbate, rather than alleviating, the risk of exclusionary behavior in

[168] Judge Gould, in his dissenting opinion, contended that the predatory pricing claim failed to allege several critical facts, including the ability to influence prices in the retail market and below-cost pricing. *See id.* at 886 ("if plaintiffs in good faith cannot allege market power, below cost sales and probable potential for recoupment in the retail market, then the case should not proceed").

[169] This argument begins with the premise that *Trinko* effectively abolished antitrust claims based on unilateral refusals to deal. If a company has (as a matter of antitrust law, anyway) an absolute right to deal or not deal with its competitors, then it has an absolute right to determine the conditions of those deals.

regulated markets. When parties game a regulatory system to achieve anticompetitive results, antitrust law should apply.

We emphasize that saying antitrust law should scrutinize some forms of private regulatory gaming does not necessarily mean that antitrust law should condemn every type of regulatory gaming. Antitrust law properly balances anticompetitive harm against precompetitive benefits, and it properly balances the risk of false negatives against the risk of false positives. In particular cases, regulatory gaming may implicate precompetitive concerns such as encouraging innovation.[170] In other cases, regulatory gaming may resemble conduct that is neutral or procompetitive, raising the risk that antitrust enforcement will create false positives. But substantive antitrust law is sensitive – even, perhaps, overly sensitive – to these concerns. They may provide a reason for antitrust courts to tread cautiously in finding defendants liable, but they do not offer a reason for antitrust courts not to ask the hard questions at all.

[170] Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263 (2d Cir. 1979); 1 Hovenkamp et al, IP & Antitrust, *supra* note __, at sec. 12.5.

Mr. JOHNSON. Thank you, Professor Lemley, and also thank you for your submission of corrective language.

Dr. Cooper?

TESTIMONY OF MARK COOPER, DIRECTOR OF RESEARCH, CONSUMER FEDERATION OF AMERICA, WASHINGTON, DC

Mr. COOPER. Thank you, Mr. Chairman, Members of the Committee.

Former Federal Trade Commission Chairman Robert Pitofsky edited a recent volume on antitrust practice in the last couple decades entitled, "How the Chicago School Overshot the Marks: The Effect of Conservative Economic Analysis on U.S. Antitrust." The *Trinko* and *Credit Suisse* rulings demonstrate that under the influence of conservative economics the Supreme Court has not simply overshot the mark, it has gone off the deep end.

These cases establish regulation as the barrier to antitrust oversight without requiring the courts to examine the effectiveness of regulation in controlling behaviors that are repugnant to both regulation and antitrust. This is particularly ironic since conservative economics generally takes a dim view of the ability of regulators to promote the public interest. If anything, conservative economic theories should have led the Court to give antitrust a wider berth, not a narrower berth.

Trinko, in particular, presumes antitrust has high costs and low benefits without demanding a careful accounting of the costs and benefits. It assumes false positives are plentiful, more likely, and more costly than false negatives without any empirical evidence to support that claim. It is the ultimate triumph of economic theory over fact in the antitrust space that favors corporations and regulation at the expense of competition and antitrust.

After a decade in which we have watched large corporations inflict huge losses on the economy and society—Worldcom, Enron, Lehman Brothers, Goldman Sachs, and BP—the notion that large corporations acting on their private interests can be expected to behave in economically efficient and socially responsible ways or that regulation can be presumed to be effective in protecting the public interest seems rather silly.

We need every regulatory cop on the beat and antitrust is one of the most important weapons policymakers have to protect the public from anticompetitive, anti-consumer business practices. To preemptively sideline antitrust in industries where it is needed most—those with the greatest market power—destroys the balance between regulation and antitrust that has worked well over the course of a century.

Regulation is a second best, to be sure, but better than unfettered exercise of market power where market structure does not support vigorous competition, and I testified here on that issue in relationship to the antitrust modernization process.

The antitrust laws are simultaneously applied to regulated industries to constantly probe for areas where competition can improve the public welfare. Regulators are not particularly adept at this role because it is not their core competence and they have a tendency to be captured by the industries they regulate. The greatest value of the balance between regulation and antitrust exists where the market structure is least certain, where there is a transition between regulation and competition or where there are a mix of competitive and monopoly elements in the market.

Much of a 21st century economy resides in this middle range, and the telecommunications sector, which was the target of the *Trinko* case, is a perfect example. Congress was seeking to move telecommunications to a greater reliance on competition after a century of reliance on monopoly. The incumbent telephone companies would determine to prevent the loss of their market power. Under their litigious, obstinate foot-dragging, the effort to open the network collapsed.

Both antitrust and regulation were aiming at the same goal, and the transition would have benefited from close antitrust scrutiny. The *Trinko* decision not only prevented this scrutiny in that case, but it severely restricted the likelihood of scrutiny in future cases.

Trinko was a stretch of the antitrust laws that the Court could have easily brushed aside if it was so inclined without changing the terrain of antitrust laws. That was the easy and prudent thing to do, especially when citing the regulatory scheme of a statute that expressly stated Congress was not intending to restrict the applicability of the antitrust laws. Instead, the Supreme Court engaged in an extreme form of judicial activism using a weak case to make a major change in antitrust practice.

The Court could remedy the situation in future cases by making it clear that the *Trinko* decision applies only to private antitrust suits and its application to private antitrust actions rests on the unique regulatory obligations and oversight embodied in the 1996 Telecommunications Act. Unfortunately, given the extremist ideology that underlies the decisions I am doubtful that the Court will be inclined to fix the problem any time soon.

Congress should act swiftly to restore the balance between antitrust and regulation that worked so well in the 20th century. Thank you.

[The prepared statement of Mr. Cooper follows:]

PREPARED STATEMENT OF MARK COOPER

Consumer Federation of America

Testimony of Dr. Mark Cooper
Director of Research

On

Is There Life After *Trinko* and *Credit Suisse?*
The Role of Antitrust in Regulated Industries

Subcommittee on Courts and Competition Policy
Committee on the Judiciary
U.S. House of Representatives

June 15, 2010

Mr. Chairman and Members of the Committee,

My name is Dr. Mark Cooper. I am Director of Research of the Consumer Federation of America. I appreciate the opportunity to appear before you today to offer the consumer view of a recent turn in antitrust jurisprudence that poses a severe threat to competition and consumers.

Judiciary Committee hearings about antitrust principles are invariably stacked with lawyers who argue about whether the principle or practice at hand is good law, especially when viewed through the lens of past antitrust practice because precedent plays a prominent place in antitrust cases. That is certainly true in the case of the *Trinko* and *Credit Suisse* rulings being discussed today, but I believe that this issue can and should be approached in a more direct fashion. The courts and congress should move swiftly to reverse this ruling because it is bad policy based on faulty economic reasoning.

These cases establish regulation as a barrier to antitrust oversight, without requiring the court to examine the effectiveness of regulation in controlling behaviors that are repugnant to both regulation and antitrust. Trinko in particular presumes antitrust has high cost and low benefits without demanding a careful accounting of the costs and benefits. It assumes false positives are plentiful, more likely and more costly than false negatives without any empirical evidence to support that claim. It is the ultimate triumph of economic theory over fact in the antitrust space. These decisions favor corporations and regulation at the expense of competition and antitrust to such an extent that, as Howard Shelanaski has shown,[1] many of the landmark cases in U.S. antitrust history would never have made it through the courts.

After a decade in which we have watched large corporation inflict huge losses on the economy and society – Worldcom, Enron, Lehman Brothers, Goldman Sachs, and BP – the notion that large corporations can be expected to behave in economically efficient and socially responsible ways because there is a convergence between their private interest and the public interest or that regulation can be presumed to be effective in protecting the public interest seems rather silly. We need every regulatory cop on the beat and antitrust is one of the most important weapons policymakers have to protect the public from anticompetitive, anti-consumer business practices. To preemptively sideline antitrust policy in the industries where is it needed most – those with the greatest market power – is a huge mistake.

The Flawed Economic Theory Underlying *Tinko/Credit Suisse*

In 2008, Robert Pitofsky, former Chairman of the Federal Trade Commission, edited a thoughtful volume on the development of antitrust practice in the past couple of decades entitled *How the Chicago School Overshot the Mark: The Effect of Conservative Economic Analysis on U.S. Antitrust.*[2] Published just before the financial meltdown, the book seems a little timid, since many leading economists, Chicago Schoolers, like Allen Greenspan, there was a flaw in the theory.

---

[1] Howard Shelanski, "The Case for Re-balancing Antitrust and Regulation," *SSRN*, March 18, 2010.

[2] Robert Pitofsky (Ed.), *How the Chicago School Overshot the Mark* (Oxford: Oxford University Press, 2008).

"Those of us who looked to the self-interest of lending institutions to protect shareholders' equity, myself included, are in a state of shocked disbelief. Such counterparty surveillance is a central pillar of our financial markets state of balance…

"If it fails, as occurred this year, market stability is undermined…

"I made a mistake in presuming that the self-interests of organizations, specifically banks and others, were such that they were best capable of protecting their own shareholders and their equity in the firms.

Buried, if not dead, beneath the rubble of the financial market collapse, lies the efficient market hypothesis, the single most important cornerstone of conservative economics. Once you admit A *Failure of Capitalism*,[3] you must re-examine all of the policies pursued in the name of a flawed economic theory. The conclusion to Pitofsky's introductory essay in the volume characterizes damage well, a characterization that fits Trinko and *Credit Suisse* cases to a tee.

"Specific concerns include preferences for economic models over facts, the tendency to assume that the free market mechanisms will cure all market imperfections, the belief that only efficiency matters, outright mistakes in matters of doctrine, but most of all, lack of support for rigorous enforcement and willingness of enforcers to approve questionable transactions if there is even a whiff of a defense.[4]

Exhibit 1 identifies dozens of ways in which conservative economic theory led to lax antitrust enforcement that severely underestimates the harm that anticompetitive practices impose on the economy under the claims of under invest in antitrust. The Exhibit also notes the flaws in economic thinking in the conservative approach to antitrust that afflict the *Trinko and Credit Suisse* rulings. Indeed, the *Trinko* and Credit *Suisse* decisions take the errors of conservative economics to a whole new level. Left to stand, they would institutionalize a bias against antitrust analysis that is totally unjustified by a century of antitrust practice or the contemporary record of antitrust analysis. Simply put, the *Trinko/Credit Suisse* decisions indicate that under the influence of conservative economics, the Supreme Court has not simply overshot the mark; it has gone off the deep end.

[3] From Richard Posner, *A Failure of Capitalism* (Cambridge: Harvard University Press, 2009), on the right to Joseph Stiglitz, *FreeFall* (New York, W.W. Norton, 2010), on the left, the critical weakness of market fundamentalism has been acknowledged. The efficient market hypothesis als come in for particular criticism (Frank Portnoy, *Infectious Greed* (New York, Henry Holt, 2003); George Cooper: *The Origin of Financial Crises: Central Banks, Credit Bubbles and the Efficient Market Hypothesis* (New York: Vintage, 2008; Justin Fox, *The Myth of the Rational Market* (New York: Harper, 2009); John Cassidy, *How Markets Fail*, (New York: Farrar, Straus and Giroux, 2009).

[4] Pitofsky, p. 5.

EXHIBIT 1:
CRITIQUE OF MARKET FUNDAMENTALISM IN ANTITRUST ENFORCEMENT*
UNDERLINED FLAWS REFLECTED IN TRINKO RULING

Fundamental Flaws
Over-reliance on the market to cure everything (4, 5)
Over-emphasis on efficiency to excuse everything (5)
Over-estimation of ease of entry and expansion of output (42, 236)
Failure to recognize wealth transfers as a cause of consumer harm (90)

Faulty analytic approach
Over-reliance on economic models, that privilege theory over fact (5, 42, 57, 82)
Over-concern about false positives rather than false negatives (52, 123)
Failure to require empirical evidence leads to over-estimation of efficiency gains (18, 42)
Failure to require demonstration of mechanism for pass through of efficiency gains (263)
Defines markets too broadly, resulting in underestimation of market power (243)
Failure to recognize non-economic impacts and causes (42)
Places burden on the wrong party and imposes impossibly high standards of proof (164, 260)
Ignores subjective evidence and customer views (165, 243)

Substantive Weaknesses
Underestimation of horizontal impacts
Overbroad claims of importance of monopoly rents as inducement to competition (85)
Overbroad claims of importance of intellectual property monopoly to innovation and R&D (6, 3, 183)
Downplaying ability of leading firm to raise rival's costs and engage in predatory practices including pricing, boycott, tying, bundling, retaliation, (27, 57, 80, 126)
Non-cooperative gaming ability to raise prices (6, 56), divide markets (6)
Importance of anticompetitive impacts of network effects (56)

Failure to recognize the anticompetitive potential of vertical leverage (52, 127, 141)
Over-reliance on single monopoly profit to absolve harm of maker power (40)
Overstated defense and incomplete analysis of vertical restraints (19, 186)
Potential effects of vertical leverage by (1) creating market power in tied product, (2) maintaining market power in tying product, (3) facilitating collusion and parallelism, (4) evading regulation
Enhanced tools of monopolization through (1) raising rivals cost, (2) refusal to deal (3) increases barriers to entry

Policy outcomes that harm competition and consumers
Under appreciation of the importance of concentration allows merger to domination (6, 236)
Under enforcement and tendency to do nothing (6, 36, 37)
Failure to use structural solution (29, 122, 126)
Over-protection of autonomy of leading or dominant firms (86, 127, 165)
Under-emphasis on dynamic efficiency and competitive rivalry (79, 80)
Lack of appreciation for the role of mavericks (81)

*Pages references are to Robert Pitofsky (Ed.), *How the Chicago School Overshot the Mark* (Oxford: Oxford University Press, 2008). Earlier discussions of this critique of conservative economics can be found in: Mark Cooper, "Comments of the Consumer Federation of America on the Proposed Horizontal Merger Guidelines," *Federal Trade Commission*, FTC File No. PO92700, June 4, 2010; "The Analysis of Market Failure After the Collapse of Market Fundamentalism: The Implications of the Defeat of the Chicago School for Antitrust and Regulation in the U.S. Energy Sector," *10th Annual energy Roundtable: Major Developments in Energy Markets*, American Antitrust Institute, March 2, 2010, presents a discussion of the critique for energy markets; "Testimony of Mark Cooper, on Consumers Competition and Consolidation in the Video Broadband Market," *Commerce Committee, U.S. Senate*, March 11, 2010 pp. 7-9 presents this critique as applied to the Comcast-NBCU merger.

The *Trinko/Credit Suisse* court places regulation above antitrust, without allowing an examination of the effectiveness of the regulation, an approach that is particularly ironic since conservative economics generally takes a dim view of the ability of regulators to promote the public interest. If anything, the theory should have led the court to give antitrust a wider berth, not a narrower one.

The reason the court turned in the wrong direction is that it was influenced by a series of the most fundamental flaws in conservative economics identified in Pitofsky's volume, excessive deference to theoretical models and efficiency claims, excessive concern about false positives, protection of dominant corporations, and a failure to recognize the importance of wealth transfers.

All of these flaws were neatly summarized in the remarkable claim that "monopoly profits" are the wellspring of economic progress. To be sure, supra normal profits are the carrot, but competition is the stick. Rewards to innovation yield supranormal profits, which may be associated with gains in market share, but they should not be equated with "monopoly profits" in the sense that the term is typically used. In a dynamic economy, innovation rents are quickly should be quickly dissipated by competition. In the case at hand, if the court had bothered to look, it would have been quite clear that any supranormal profits had nothing to do with innovation and everything to do with using market power to frustrate competitive entry and raising the competitors' costs. The whiff of efficiency was provided by the theoretical possibility that there might be a drop of innovation rent or efficiency gain in an ocean of anticompetitive rent seeking.

The Importance of Balance Between Regulation and Antitrust

The simultaneous jurisdiction of antitrust and regulation was created over a century ago, during the Progressive era, when policy makers realized that the modern industrial economy was creating huge corporate enterprises that could easily amass market power that robbed the economy and the public of the benefits of competition.[5] There are industries in which market power is so pervasive that prudential regulation is necessary on an ongoing basis. Although competition is preferable, regulation is a second best, better than the unfettered exercise of market power. The decision to regulate does not cancel the preference for competition and the antitrust laws are simultaneously applied to constantly probe for areas where competition can improve the public welfare. Regulators are not particularly adept at this role because it is not their core competence and they have a tendency to be captured by the industries they regulate.

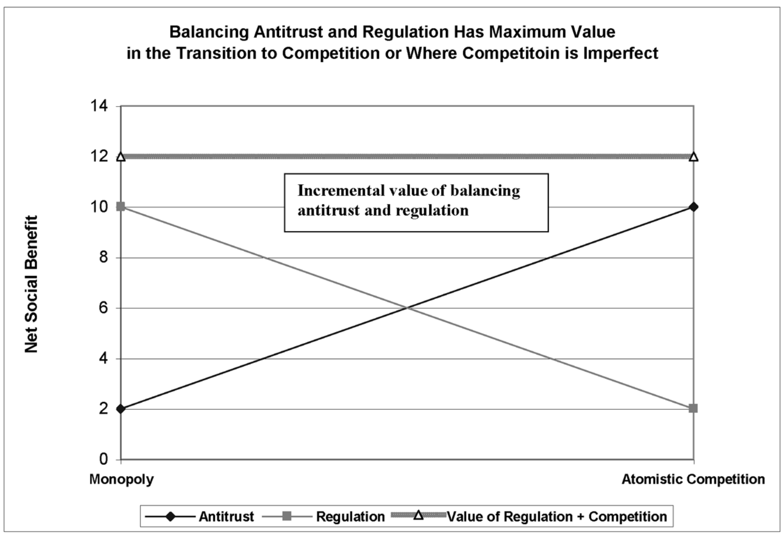
These principles were reaffirmed in the New Deal, as prudential regulation was layered atop aggressive antitrust enforcement to repair the damage that irresponsible market behavior and lax antitrust enforcement had done to the economy in the 1920s. For fifty years, vigorous enforcement of the antitrust laws combined with effective oversight of market power through regulation to produce a remarkable record of economic growth and progress. Antitrust and regulation worked hand in had to prevent the accumulation of market power, where markets should support vigorous competition, and to regulate market power where they cannot. Balance is the key to creating a dynamic, progressive capitalist economy.

[5] The Sherman Act of 1890 was passed three years after the Interstate Commerce Act or 1887.

That balance was destroyed by the *Trinko/Credit Suisse* decisions.

The balance was destroyed at a moment when, and in an area where the value of antitrust was highest. As Shelanski has argued, the greatest value of the balance between regulation and antitrust exists where the market structure is least certain – where there is a transition between regulation and competition or where there are a mix of competitive and monopoly aspects to the market. Exhibit 2 presents a graphic representation of the idea.

EXHIBIT 2:



When underlying characteristics dictate that monopoly is the efficient outcome, there will be little cost to under enforcement of antitrust, since there are few gains to be made by imposing competitive solutions. When atomistic competition is sustainable, regulation will impose inefficiencies on the industry. But these pure types of markets are few and far between. Much of a 21st century economy resides in the middle range. The telecom sector was seeking to move to a greater reliance on competition after a century of reliance on monopoly. The incumbent telephone companies were determined to prevent that progress. Under their litigious, obstinate foot dragging, the effort to open the network collapsed. The transition would have benefited from careful antitrust scrutiny. The Trinko decision not only prevented that scrutiny in this case, but it severely restricted the likelihood of such scrutiny in the future.

Conclusion

The expression "hard cases make bad law" has risen to the status of a proverb, with a history stretching back well over a century, but this is an instance where an easy case was used as an excuse to make bad policy.[6] *Trinko* was a stretch of the antitrust laws that the court could have easily brushed aside, if it was so inclined, without changing the terrain of antitrust law. That was the easy and prudent thing to do, especially when citing the regulatory scheme of a statute that expressly stated that it was not Congress' intention to restrict the applicability of the antitrust laws. Instead, the court used a weak case to make a major change in antitrust practice applying a theory that had been increasingly discredited in recent years.

The court could take steps to remedy the situation in future cases by making it clear that the *Trinko* decision applies only to private antitrust suits and its application to private antitrust actions rests on the unique regulatory obligations and oversight embodied in the 1996 Act. Given the extremist ideology that underlies the decision, we are doubtful that the court will be inclined to fix the problem any time soon. Therefore, Congress should act swiftly to restore the balance between antitrust and regulation that worked well in the 20th century.

[6] "Hard cases make bad law, no doubt, and maybe bad policy, *Spectator* 21 July 2001, http://www.answers.com/topic/hard-cases-make-bad-law

---

Mr. JOHNSON. Thank you, Dr. Cooper.

And now we will begin with questions.

Mr. Thorne, is it not true that the issue in *Trinko* that went up to the Supreme Court was whether the conduct by the telecom company violated the antitrust law?

Mr. THORNE. Mr. Chairman, that is exactly correct. The question in *Trinko* was whether Verizon, in providing access to its facilities, had done it in a way that was consistent with the antitrust laws.

Mr. JOHNSON. And the Court used dictum to suggest that in general the benefits of applying antitrust law in a privately-brought case was few. In other words, there weren't very many benefits to be had for the bringing of a private action in a regulated industry context. Is that correct?

Mr. THORNE. Mr. Chairman, with all respect, I have read the case differently. I read it as having two parts, and give me a second, I will explain: First, the Court asked——

Mr. JOHNSON. And I think you did during your testimony.

Mr. THORNE [continuing]. That the dicta that you are referring to was not on the question of whether Verizon had violated the existing antitrust laws. The additional question—the second part of the decision—because the antitrust laws are somewhat plastic—it is a very brief statute—don't restrain competition, don't monopolize—the Court has the ability if it wants to to expand antitrust into places it has never gone before.

And on the question of—the second question, not whether existing antitrust laws were violated—the Court found clearly they were not—but on the second question, should we take this occasion to expand antitrust into a new place, in that circumstance the Court thought for a whole list of reasons it would be a bad idea. And one of the things the Court listed was the fact that regulators were already policing the very conduct.

Mr. JOHNSON. Okay. Well, let me get Professor Lemley's opinion about that.

Mr. LEMLEY. So I think Mr. Thorne is correct to say the Court expressly considered should antitrust law not apply here at all, and they rejected that conclusion because of the savings clause. But I think it is also correct to say that the Court went out of its way to express skepticism of the value and role of antitrust in an area that was subject already to regulation. And the Court in particular said antitrust can do less good here because regulators are already policing the risk to competition and it has a greater potential for harm. And so I think the Court was, in fact, going beyond its brief to decide the question that Mr. Thorne's case presented——

Mr. JOHNSON. Do you——

Mr. LEMLEY [continuing]. Conduct violated the antitrust laws.

Mr. JOHNSON. All right. Thank you.

Do you agree, Mr. Shelanski?

Mr. SHELANSKI. Mr. Chairman, I think that the Court tried to draw two lines that will be very difficult to implement in practice. On one hand, as Professor Lemley said, the Court did not say that antitrust law, as clearly established, doesn't apply. It wasn't able to say that in light of the savings clause.

It did, however, say that claims that would be an extension of the outer boundaries of antitrust law could not be brought where there is a regulatory structure in place. There are two problems with that statement: Under the fact-intensive analysis of Section 2 of the Sherman Act, which tends to occur under the rule of reason and involve a balancing of pro-versus anticompetitive effects, every case is going to be different on its facts, and identifying the outer boundary is not nearly as clear or straightforward an exercise as the Court represents.

And so lower courts could look at a case, say, "Well, we have never seen exactly this case before. It must be beyond the outer boundary. It must be foreclosed in the presence of a regulatory structure," which brings me to the second problem of the decision: The Court does not establish clear standards for the regulatory structure that must be in place before it precludes an antitrust claim. Does it have to be as elaborate, detailed, and competently and actively enforced as the Telecommunications Act of 1996? If so, as I suggested in my testimony, we may worry less about the displacement of antitrust.

But what about a regulatory scheme that does not directly address the competitive harm at issue but addresses some competitive harm, or it is within the authority of an agency but not enforced? The Court doesn't tell us whether or not that kind of regulatory structure is adequate, and our profound concern at the Federal Trade Commission is that lower courts could interpret such a weak regulatory structure to defeat antitrust claims, and not just outer boundary antitrust claims, good antitrust claims that could be brought under existing precedence.

Mr. JOHNSON. Well, let me ask Dr. Cooper, do you feel that the ruling in *Trinko* taken together with—or ruling in *Credit Suisse* taken together with *Trinko* actually act to impose a presumption that actions brought by plaintiffs, both public and private, in a regulated setting are—in other words, the burden of proof has been shifted to the plaintiff on these kinds of cases to establish that the antitrust laws do apply?

Mr. COOPER. Actually, I think the example that—the end point where Mr. Thorne wants to end up shows us the great danger. Of course, the argument he makes is that, if I never dealt voluntarily I never have to deal. And this is an industry in which it controlled access to its networks for a century never voluntarily making it available, and Congress said it is now time to make it available.

For me, the critical question will be, if you allow that to happen in our—especially in our technology industries, you will have a lockdown of all of the functionalities on which a broad swath of economic activity relies. That is the implication of this case, and he drew it. That implication is disastrous; it needs to be rebutted, I think, precisely by containing the damage that this case can do. So the proposition which we can ask is whether the refusal-to-deal has severe negative economic and social effects.

Mr. JOHNSON. Thank you, Dr. Cooper.

I will now turn to the Ranking Member, Mr. Howard Coble.

Mr. COBLE. Thank you, Mr. Chairman.

Gentlemen, thank you for your appearance today.

Mr. Shelanski, you expressed concern that the FTC and DOJ could be precluded from bringing some antitrust cases in regulated industries as a result of these two cases. Do you have some suggestion for how Congress could legislatively repeal these cases for DOJ and FTC, A, and B, is this concern based on how *Trinko* and *CSFB* have been actually interpreted by district courts and courts of appeal, or are you concerned mainly as to how they may be interpreted?

Mr. SHELANSKI. Thank you, sir.

Let me start with your second question first. I think our principal concern is, given the relatively few number of years that have occurred since *Credit Suisse* and given the long cycle that our investigations in cases can occur over, that we are thinking about how these cases may affect our enforcement. We are always thinking in every action about these cases, about whether they impose some impediments.

And we have current cases in which we are very attuned to the possibility that *Credit Suisse* and the *Trinko* issues could arise. So at this point, given the relatively short time that has passed, our concern is mostly current and prospective than with particular decisions that have occurred.

As to what could be done to protect the jurisdiction of the Federal Trade Commission—I am obviously not here to speak on behalf of the Justice Department, but I will speak broadly about public enforcement—our concern is that public enforcers who have an ability to coordinate with regulatory authorities, to identify the gaps in regulation, to work interactively with regulatory authorities to identify places where antitrust can be a useful complement, that we not be prevented by interpretations of *Credit Suisse* and *Trinko* from undertaking that independent policy judgment about whether antitrust would be more beneficial than costly in any particular setting where we are investigating a regulated firm.

And so the particular kind of language is not something that I would be prepared to provide you right off the top of my head, but a general thrust would be something that protects that jurisdiction that expressly says, "Nothing in the antitrust laws as heretofore developed would prevent the public antitrust agencies from exercising their independent judgment about the value of an antitrust case."

Mr. COBLE. Thank you, Mr. Shelanski.

Mr. Thorne, you stated in your testimony that *Trinko* would not have prevented the government from bringing its case at AT&T. One thing that has been suggested here is that the antitrust enforcement agencies—notably DOJ and FTC—be exempted from the *Trinko* and *CSFB* decisions. Would such an exemption underline the regulatory clarity that you wanted to bring to bear with the *Trinko* case? Or in other word, would you favor a statutory exemption from *Trinko* for DOJ and FTC?

Mr. THORNE. Mr. Ranking Member, first of all—and I have to say this—my experience with both the Justice Department and FTC has been one of absolute admiration. The enforcers at the Justice Department and the Federal Trade Commission are first-rate; they are the best antitrust enforcers on the planet. So I am not going to say anything bad about their ability to enforce the antitrust laws.

But the idea of breaking apart public enforcement and private enforcement under two different regimes is a new idea. It is the first time in over 100 years under the Sherman Act that we have had a different enforcement regime for the two areas. So it started to raise questions in my mind like, if you are going to separate the private cases from the public cases does that mean that the private cases can no longer tag along with the public cases? And it seems like there are a series of questions.

Right now the Justice Department is viewed as only a law enforcer; it doesn't set out separate policies or make laws, it just enforces the laws as they are written. Would this change that relationship that the Justice and the Federal Trade Commission have?

So I am interested in the proposal. It is novel, and it seems to raise for me a series of questions that ought to be thought through.

Mr. COBLE. And I didn't mean to imply, Mr. Thorne, that you are accusatory. I didn't mean to suggest that at all.

Mr. Lemley, let me start with you and then open it up to the others. Professor, how can Congress effectively communicate its intent to have antitrust laws and telecommunication laws operate side by side?

Mr. LEMLEY. Well, I do think it is a problem because of the presence of savings clauses in the very statutes that have been interpreted, and that is why I think the best approach is actually to modify the antitrust law itself to say that you should not assume or imply repeal from the antitrust law unless Congress expressly grants an immunity. I think that if done in the context of a hearing like this and with legislative history that made it clear that this was directed at cases like *Credit Suisse*, I think the message would be received by the courts that this was not, in fact, an area in which antitrust deference was appropriate merely because there was a regulatory system. And I have suggested in my written testimony some language that—quite brief language—that might achieve that end.

Mr. COBLE. Mr. Chairman, a red light appeared, but may others respond to my question?

Mr. JOHNSON. Certainly.

Mr. COBLE. Doctor, do you want to start?

Mr. COOPER. The goal that Professor Lemley outlined is precisely the place we need to get to, where the full force of the antitrust laws apply. And if the argument is going to be that somehow or another regulation has done the job then that burden ought to be on the defendant in the case. That is, we need the antitrust laws to have full effect.

The savings clauses tend to get thrown in at the last minute. They don't have a lot of legislative history. If there is any possibility that the Congress was carving out some sort of exemption they are not well documented in the record, and I think that is a mistake. This is a moment, and this is a sector, where we desperately need to make sure that we can get down that path to a more competitive environment, so——

Mr. COBLE. Thank you, sir.

Mr. COOPER [continuing]. Changing the—switching the burden would be the critical point here. The presumption should be in favor of antitrust and rebuttable if there is specific regulatory language that one can cite and demonstrate effective regulation is actually in place, not just in theory.

Mr. COBLE. Thank you.

Mr. Thorne, do you and Mr. Shelanski want to weigh in?

Mr. THORNE. No, thank you, Mr. Ranking Member.

Mr. SHELANSKI. I have nothing to add.

Mr. COBLE. Thank you.

I yield back. Thank you, Mr. Chairman.

Mr. JOHNSON. Thank you, sir.

Next we will recognize Mr. Conyers for questions.

Mr. CONYERS. Thank you very much.

Just for the record, Dr. Cooper, are you a lawyer?

Mr. COOPER. I am not a lawyer.

Mr. CONYERS. Okay. You seem to advise a lot of lawyers, though.

Mr. COOPER. I have been an expert witness about 400 times, so you spend a lot of time with lawyers.

Mr. CONYERS. Okay. I have never recommended law school to a person your age, but there are honorary degrees, probably, floating around in the profession.

Anybody want to comment on their thinking about the pattern of the history of antitrust law in America—Sherman Act 1890, Clayton Act 1914, Robinson-Patman Act 1936, Hart-Scott-Rodino 1976? Where we started off with—while we were protecting people originally in the 19th century from consumer fraud, conspiracies, collusion, it was anti-monopolistic, price-fixing. Then Clayton came in with private—the rights of private lawsuits to enforce antitrust law in America; Hart-Scott-Rodino mergers, Robinson-Patman fair pricing considerations.

Is this an era that is gone—we sort of dealt with it? We had a rash of cases—big cases—that we study in law school. But now it seems like the pendulum is swinging the other way, that we are trying to scale back and even to me sometimes strange interpretations of savings clauses, that if you don't put a savings clause in it maybe means that antitrust isn't being contemplated.

What do you think, Cooper, Lemley, Thorne, Shelanski?

Mr. COOPER. I would offer two observations. It is interesting, you gave me the following key dates in the antitrust history: 1890, 1914, 1936, and 1976. I would point out that the Interstate Commerce Act is 1887; the Mann Act, which extended the Interstate Commerce Act to telecom, is 1910; and the Federal Communications Act—the Federal Power Act—are all the early 1930's.

So the interesting thing is that the notion that we needed both regulation and antitrust is deeply embedded in that century of legislative history, so the idea that the Court finds it repugnant to have dual jurisdiction just is inconsistent with that history, and I think it is really important, as I mentioned in my testimony, that Congress legislated both at almost exactly the same time very consciously understanding it needed both. That is, to me, the most important lesson.

The second point I would make is that the essential facilities doctrine, in an age where digital networks become the center of economic and communications and social activities, the access to that essential facilities—that network—becomes more important than ever. And of course, that is the issue that the Court was whacking away at in this case.

So we are going in the wrong direction on both counts. We are claiming that we ought not have dual jurisdiction when that is clearly a part of our history, and we are restricting the access to essential facilities when it is more important than ever to have access to those facilities.

Mr. LEMLEY. I do think antitrust has a—antitrust history has a pendulum problem. We started out with the antitrust laws to correct excesses of private behavior and we succeeded, but in some sense we succeeded too well and antitrust laws started to reach too far into the regulation of private behavior. That pendulum has been swinging back for 30 years now and I think it may well have swung too far in the opposite direction.

It is absolutely desirable to have economic analysis and sophistication in thinking about antitrust. I guess I would like to see us not push the pendulum back the other way but see if we can get it not to swing so far in either direction and to center itself somewhere where we focus on economic analysis, we make the right decisions, but we are not simply saying we have to cut back antitrust or we have to expand antitrust at all costs.

Mr. CONYERS. Professor, what cases were you thinking of when you mentioned the pendulum had swung too far?

Mr. LEMLEY. Well, if you look at the history until a couple of weeks ago when the Supreme Court decided the American Needle case antitrust plaintiffs, both governmental and private, have been on a losing streak in the United States Supreme Court that had run 18 years and 18 cases without a single antitrust plaintiff's victory until American Needle.

And I do think—I think the concerns that were expressed in the early 1980's about not simply reacting to any private behavior by saying, "There must be an antitrust problem here," were real, but I think the opposite concern is equally powerful. You cannot simply say, "Well, if there is any plausible justification that we can come up with for why private behavior might be acceptable we should automatically defer to that behavior.

Mr. CONYERS. I quite agree with your analysis with the numbers, but name me a case.

Mr. LEMLEY. Well, so some of the ones—I think the *Credit Suisse* case that we are talking about here is problematic. I think the—I think some of the decisions that make it essentially impossible to prove certain types of antitrust cases—predatory pricing cases, for example—are problematic. Predatory pricing is often over-claimed, but that doesn't mean it doesn't happen. So the legal standards that we have created in cases like Brooke Group may be too strict.

Mr. CONYERS. Mr. Thorne?

Mr. THORNE. Two quick observations, Mr. Chairman. First, listening to your summary of the dates, it just—it is amazing to me how durable these very simple antitrust laws have been, and I think everybody on the panel agrees how important. Justice Marshall was not going too far in talking about the Sherman Act as a Magna Carta for free enterprise, almost on the par of the First Amendment guaranteeing speech and political participation. It is very important and there is no—it is wonderful to see how durable it has been.

As a small second note on Brooke Group and on cases like it, these are the new cases that probably add up to the 18 that Professor Lemley talks about. If you think that it is important to have antitrust that is fair, efficient, and predictable, you need some clarity for businesses that are going to go out—like Verizon or other private enterprises—go out and then actually behave in the marketplace. So if Verizon is going to price a product it needs to know at what point can we go in cutting prices to benefit consumers—at what point can we go before we will be in some liability, we will be hailed before a one-time lay jury and then told we have priced too low, we have hurt our rivals, and now you pay triple damages in a class action.

The predictability comes from having a test like, don't price below your costs. That is something businesses understand. There is sometimes a debate about where, you know, this measure of cost or another measure of a cost—but the concept, don't price below your costs and you will be okay——

Mr. CONYERS. But there is no law against that.

Mr. THORNE. Well, that is what Brooke Group held, but if Brooke Group could be repealed then businesses would not have the predictability of knowing. For example, if I lower my prices today and hurt some small rivals I have benefited consumers right away but the rivals may not be able to keep up with price cuts.

So there is a theme in the recent cases of saying a successful firm is allowed to do things that benefit consumers. A successful firm can cut price down to cost. A successful firm can innovate or invest just like a smaller rival can do. These are things that are good for consumers, and these are decisions that I think——

Mr. CONYERS. Your recommendation is good if the company has market power—in other words, if it is big and powerful. If it isn't you can price wherever you want—and I will be corrected on this; I have got a number of lawyers that are researching it now.

Attorney Thorne, do you think you should have won your case?

Mr. THORNE. The *Trinko* decision? I thought I should have won it in the Second Circuit and I am pleased that we won it without dissent in the Supreme Court, and I think it is good law and not a mistaken law. Thank you, Mr. Chairman.

Mr. CONYERS. Well, why didn't you win? [Laughter.]

Mr. THORNE. The Second Circuit has, in a series of cases, expressed skepticism not about the particular legal standards that apply but the procedural posture of the case. So the way the case came up to the Second Circuit and then the Supreme Court was on a motion to dismiss. *Trinko* had not been allowed to take discovery, and we had not been allowed to take discovery of *Trinko*.

So it was on—it was a—complaint with a lot of details which gave you the information necessary to decide if there was a complaint there. But the Second Circuit is historically reluctant to decide things on a motion to dismiss; they prefer to see a little discovery. And the phrase of Judge Sack, who was on the Second Circuit panel of writing, he quoted—I think it was Dickens, it was with some miscreant in Oliver Twist "—Let's see what happens; maybe something will turn up." Discovery was and summary judgment, was just the preferred procedure, and I think that is why we lost in the Second Circuit.

Mr. CONYERS. And it reminded me of the sports metaphor—"We was robbed."

Thank you, Mr. Chairman.

Mr. JOHNSON. Thank you, Mr. Chairman.

Next we will hear from Mr. Chaffetz for questions.

Mr. CHAFFETZ. Thank you.

And thank you all for being here.

Mr. Shelanski, I would like to start with you if I could. Recently Congress passed a massive health care reform bill, and the FTC has historically pursued numerous antitrust actions in the health care field. Are there any concerns that what was passed in March will prevent the FTC from bringing price-fixing cases in the health care industry?

Mr. SHELANSKI. Thank you. That is an excellent question.

We at the commission do a lot of enforcement, as you noticed, in the health care sector. It has been historically one of the major regulated industries in which we have operated and continue to operate. And the health care bill, having been recently passed, is something that we are, of course, studying with a great eye to the extent to which there may be regulatory provisions that affect our ability to continue——

Mr. CHAFFETZ. I am not an attorney, by the way, Mr. Chairman. I just want to know for the record. If you have got one of those honorary degrees you are handing out let me know, though. That would be great.

Mr. CONYERS. Well, I am sure the law schools are already deciding among themselves which ones will confer you with an honor by next summer.

Mr. CHAFFETZ. Thank you.

To continue on, Mr. Shelanski, if the FTC and the Department of Justice are given different substantive legal standards for bringing antitrust cases how would you deal with all the private class action cases that would want to follow in their wake? Would trial bar lawyers, class actions, triple damages be allowed to piggyback on the government cases? How is that going to work?

Mr. SHELANSKI. Well, that is obviously going to be an extremely important area for policy. And to the extent that what the Supreme Court was primarily concerned about were what has been called the toxic combination of triple damages and class action—how to preserve the good aspects of antitrust without the high error costs, where—and not all such cases are inappropriate, I want to be very clear about that; but those that are have to be prevented from following on the heels.

I would make two remarks about that, though. One is that when the public agencies win a case that demonstrates that there is merit to the claim of anticompetitive conduct, and so to the extent that a firm may have further civil damages that flow from proven anticompetitive conduct, that is what the antitrust laws are there to prevent and to compensate the damage of plaintiffs for.

But I would also add that where the Federal agencies enforce there may be ways for them to resolve claims without precedential effects. The Federal Trade Commission Act brings all of its competition law cases technically under Section 5—that is of not the Sherman Act, not the Clayton Act, but the Federal Trade Commission Act. It does not provide for private rights of—automatic private rights of action. It does not provide for triple damages; and which also provides, under the Supreme Court's very decision in a number of other cases for—antitrust law, but clearer that private plaintiffs can follow on with those actions.

Mr. CHAFFETZ. Let me continue on here regarding *Trinko* here. You argued that "The Second Circuit's erroneous construction of Section 2 would fundamentally transform the Sherman Act so as to require monopolists to pull their competitive punches, assist their competitors, convert themselves from retailers into wholesalers, and share monopoly profits on demand." Are you repudiating your earlier findings in the Supreme Court, and why, and what has changed?

Mr. SHELANSKI. Okay, I just want to be clear—I am not sure I wrote those words——

Mr. CHAFFETZ. Okay, assuming that it is not a quote, but generally the spirit of what I said there—I am happy to repeat it, but I believe I am pulling from a direct quote here that was in the brief, at least——

Mr. SHELANSKI. Okay. Okay. I thought you were quoting the testimony. I am sorry.

Mr. CHAFFETZ. My apologies. From the brief——

Mr. SHELANSKI. The public antitrust agencies are just as concerned with sound antitrust enforcement as the Supreme Court is, and the public agencies would, I think—what they were expressing in that brief—and I want to be clear that I was neither an author of the brief nor am I authorized to speak on behalf of those that were—but my personal interpretation of what was written in that brief was a concern that refusals-to-deal not be too automatically punished because, as Mr. Thorne has argued, when you have successfully developed a product and successfully innovated in an area there should—it would be harmful, as the FTC has often stated, for American consumers if you automatically had to turn over that innovation, that invention, that product to a rival. That could harm competition rather than help competition.

And I think what was being expressed in the brief was a concern that we not have a rule that, as we were talking about pendulums, that goes too far in telling successful innovators that as successful competitors you have to confer your advantage on your rivals. As Justice Scalia said in the *Trinko* case, that could harm competition, not help it, and I don't think we disagree with that.

The question is, as my colleague, Professor Lemley said, where that pendulum is set. The Court may have gone too far in *Trinko*.

Mr. CHAFFETZ. Thank you, Mr. Chair.

Mr. JOHNSON. Thank you.

Next we will hear from Mr. Polis with questions.

Mr. POLIS. I join my colleague from Utah as a non-attorney on the Committee. A basic question maybe one of you can help me with is the concept—legal term—regulated industry binary and clear, or is it a continuum of what a regulated industry is or isn't?

Mr. LEMLEY. I think the answer is it is clearly—it is a continuum and that is a significant part of the problem. In some sense all industries are regulated, they are all subject to health and welfare regulation, environmental oversight and that sort of thing, and so one of the worries is that if we defer in—if antitrust law defers to any area in which there is regulation in the modern economy that may be almost on to everyone. Now, obviously some industries are more heavily regulated——

Mr. POLIS. If we take an example—if we can comment on the publishing industry as an example. This would be an industry that has some regulation, especially regarding, you know, sale of books and pricing and so forth that could be viewed within the antitrust realm. Is that one that falls somewhere on the continuum between—if anybody is familiar already with that industry—between regulated and unregulated?

Mr. LEMLEY. I think it is probably a less regulated industry than most, but—and it is certainly the case that we wouldn't want antitrust to step away from actions in the book publishing industry. There were, in the last 10 years, significant antitrust cases brought against price-fixing behavior among publishers, and we don't want to give cover to antitrust violations as private defendant have sometimes suggested in other industries merely because there is a regulatory component.

Mr. POLIS. And some of the regulated industries on that end are, in fact, regulated for other reasons, and indeed, for primary reasons unrelated to competition policies. Is that correct as well?

Mr. LEMLEY. Absolutely. Absolutely.

Mr. POLIS. Do you have any examples of that you can give, what you might consider a regulated industry where the primary thrust of the regulatory structure is not necessarily around the same types of concerns that antitrust law address?

Mr. LEMLEY. Well, I mean, so I think one example is securities regulation, right, where our interests are in—they are in some sense bound up with the working of the marketplace, but they are not with competition in the same sense antitrust law thinks about it. But environmental regulation obviously fits into that category as well. If we are restricting the way in which you run a coal mine we are not doing it in order to encourage competition; we are doing it because we are worried about the environmental consequences——

Mr. POLIS. And in your opinion there is not any legislative legal language in the regulatory structure that is created for many of these regulated industries that specifically was designed by Congress to exempt them from antitrust?

Mr. LEMLEY. I think that is right, and I think that is right precisely because the assumption, until 6 or 7 years ago, was that we didn't need legislative language to solve this problem because courts wouldn't impliedly repeal the antitrust laws merely because there was regulation. And it is that assumption that has been called into question.

Mr. POLIS. Right. So an answer—a legislative answer—could take two forms. One would be modifying the Antitrust Act to explicitly not exempt regulated industries; the others would be to amend the relevant regulations for the respective industries to make it clear that nothing contained in those acts exempt them from antitrust.

Mr. LEMLEY. Right. And I will just mention in the latter category that there are an awful lot of regulations out there. The former seems the simpler approach.

Mr. POLIS. I should ask, clearly the former is the simpler approach, also, perhaps, you know, difficult—so would it, in fact, be legally constructive going forward when we look at industry regulation to include boilerplate language not exempting them from antitrust, or could that be taken as a point of evidence that, in fact, the ones that don't contain that language it wasn't contemplated? Would you recommend that—would you consider recommending that course of action to us going forward in the industries who regulate?

Mr. LEMLEY. So I think it is a worry, right, because one of the cannons of construction the courts use is, "Well, you said it here, you didn't say it here, so in the second category you must not have meant it to apply," which is why I think that the general approach within the antitrust laws is the proper one.

Mr. POLIS. Yes. Thank you. Just as a—and this would obviously—the counterargument would be as a reaction to a precedent that didn't exist when the other laws were set up. You are correct, obviously, legislatively in terms of opening up all the various industries that are regulated not the most likely political occurrence. But certainly going forward, absent an ability to modify the Antitrust Act itself, it certainly is a possibility that we could explore at the same time as we started to explore a clarification within the Antitrust Act.

I appreciate your answers and I yield back.

Mr. JOHNSON. Thank you, Mr. Polis.

Next, Mr. Goodlatte?

Mr. GOODLATTE. Well, thank you, Mr. Chairman. I appreciate your holding this hearing and I appreciate this very interesting discussion by our panelists.

To follow up on the comments of the gentleman from Colorado, you could also take it a step further and in writing revisions to our antitrust laws say that when those laws are applied under circumstances specified in the law they would supersede the regulatory effect.

My concern here is this: I am very much a supporter of our antitrust laws, and I do not think we apply them as often as we should, and I share some of the concerns that have been expressed here. But quite frankly, I think antitrust has a more positive effect on our economy when it tells an entity, you can't do a certain thing because of its anticompetitive effect. But that still incentivizes that business to find a different way to deliver those services to their customers that they were told they couldn't deliver in that fashion because it had an unfair effect on their competition. Whereas with regulation my fear is that the regulatory process is, you will do this but you will do it this specific way, and that often has a very negative impact upon the incentive of businesses to be innovative in their process. So the clashing of those two ideas here is one that I respect, quite frankly, the Court's concerns.

And Professor Lemley, let me ask you in that regard: You are talking about reversing the presumption. Help me juxtapose that with the Supreme Court's decision in *Credit Suisse* in which they have set forth this four-factor test which seems to me would put some burden on the defendant in those cases to first say, hey, there are regulations here, number one. Number two, the regulatory agency, whether it is FTC or somebody else, is indeed exercising their authority under those regulatory powers. Thirdly, that there would be a conflict that would exist between those regulations and the exercise of the antitrust decision. And then finally, whether the practices would be subject to conflicting requirements lie within the heart of the securities laws. Obviously this decision could well be read to only apply to the securities industry.

But that seems to be a pretty good test. What is your response to that?

Mr. LEMLEY. Well, so I think my first response is that test in the—articulated in the abstract is not a bad test. As applied in the actual *Credit Suisse* case it didn't work because the very conduct—the conduct that was in question, I think, was pretty clearly anti-competitive, and the regulatory decision to which the Court chose to defer was not an affirmative decision to require the conduct or even to bless the conduct; it was merely regulatory in action, the fact that the FCC hadn't brought an action against this particular conduct.

Mr. GOODLATTE. So good test but bad decision?

Mr. LEMLEY. Yes, I think that is right.

Now, so I think the—so my worry, then, is, you know, what is the—how are lower courts who are reading this decision as applied in this context going to take terms like, "Is there a conflict between the two?" If there is a real conflict—if the regulation affirmatively says you have to do it this way—then yes, you shouldn't hold people liable for violating the antitrust laws for doing what the regulators told them they had to do. That would be unfair.

I agree with you, on the other hand, that if we have a choice between and antitrust regime that says, don't engage in anticompetitive conduct but feel free to compete otherwise, we are better off choosing that over a regulatory system that tells people how they have to compete. And so my instinct would be to say we ought to limit the circumstances in which we think there is a real conflict between regulation and the antitrust laws as much as possible.

Mr. GOODLATTE. How does your "reversing the presumption" differ from this test? I mean, what would you add to that or how would you differ from that in terms of attempting to reinstate some antitrust authority here without creating too many of these conflicts between the antitrust enforcement and regulatory enforcement?

Mr. LEMLEY. Well, I think the focus should, in fact, be on conflict. That is, I think if we simply had a rule that said, the antitrust laws apply here, they haven't been repealed, they can nonetheless—they should nonetheless be—antitrust should defer to actual actions by the regulators and they ought to defer in circumstances in which there really is a conflict so that the behavior by the defendant is compelled by the regulators and so it can't be an antitrust violation as a result. You can't put a private company in the position of having to violate one law or the other.

But short of that, if the government hasn't acted and if the government's regulatory scheme doesn't put people in the position that they are going to run afoul of one regime or the other, unless there is an express immunity that Congress has adopted, I don't think the courts should be creating one by implication.

Mr. GOODLATTE. Mr. Chairman, my time is expired. I wonder if I might ask Mr. Thorne if he—I know he didn't profess to be an expert on the *Credit Suisse* decision, but he might visualize how this discussion that we have just had might impact his company and his point of view about this.

Mr. THORNE. Well, my company is probably not affected by *Credit Suisse* because in——

Mr. GOODLATTE. You are not in the securities industry, but——

Mr. THORNE. The telecom statute has a very strong, explicit savings clause, so antitrust is fully preserved for telecom. But, you know, I have read the *Credit Suisse* decision. I noticed how deeply context-specific it was. It didn't seem like a blanket rule was going to work. It was something that depended on the rules, depended on the facts.

The Securities Exchange Commission there was an advocate for immunity. The Justice Department came in on the other side and said, no, we think we have got a way to make antitrust work despite your concerns about needing all the cooperation of the firms to aggregate capital. So it sounds like something where you would want the advice of the SEC in crafting something that will change how the SEC-related rules were immunizing against antitrust conduct.

Mr. GOODLATTE. And if I might also ask Mr. Shelanski to talk about that very point, you had a conflict between two government agencies—not yours, but the SEC and the Justice Department—the court of appeals, the Department of Justice, and the SEC had decidedly different positions on the question of whether security law is preemptive in the antitrust laws. Can you explain the position that the agencies took before the Supreme Court and the extent to which the Court adopted the government's position? Would the FTC take the same position today?

Mr. SHELANSKI. I can't speak to whether the FCC would take the same position today——

Mr. GOODLATTE. I said the FTC.

Mr. SHELANSKI. Oh, the FTC. I think that our position would be very much along the—I can't speak for the agency, but our testimony today suggests that our testimony would be very much along the lines, or our position would be very much along the lines of the position that the Department of Justice took.

We as a public agency can make a reasoned judgment about whether the conduct we are attacking is reached or not by regulation and whether or not we can frame the issue crisply enough that a court can separate the antitrust conduct from regulated conduct.

There is a profound irony that the *Credit Suisse* court did not address. The very courts that they are saying are incapable of avoiding confusion between the securities laws and separate non-regulated antitrust conduct are the same courts they are saying will have to apply the four-part test whenever a conflict comes up. I find that to be a little bit strange.

And just to address your other point, I agree fully that fixed rules that say you must do something in a particular way are less desirable than more targeted and more flexible antitrust enforcement. There is a risk after *Credit Suisse* and after *Trinko* that regulatory agencies will feel they have to be more rather than less aggressive because of fear that antitrust cannot play its backup role. That was a concern of the Justice Department in the *Credit Suisse* case and I think it is a concern that we at the commission would have today.

Mr. GOODLATTE. Thank you, Mr. Chairman.

Mr. JOHNSON. Thank you.

I have one additional question. What is the cumulative effect on public and private enforcement of antitrust laws of the Supreme Court's decisions in *Trinko* and *Credit Suisse*? What is the cumulative effect?

And I would like to get a response from you all.

Mr. SHELANSKI. Well, I will begin with addressing the public enforcement side of your question and I will try to say a word about private enforcement as well. Certainly at the FTC we do a substantial amount of enforcement in regulated industries—health care and electricity, just to name two, would be a couple of areas——

We have to think very carefully in our enforcement decisions going forward about whether or not we will, in a given case, run into a *Credit Suisse* or a *Trinko* problem, so it certainly imposes a burden and a litigation of risk on the agency. And as I said in response to Mr. Chaffetz, this is something that is, going forward, going to be a serious concern for us in health care, energy, other industries.

On private enforcement, the only thing I can say is it must—I think both of these cases will, over time, and perhaps have already, although we can't observe cases that have soon happened because counsel said we can't bring the case, but I would imagine that it is a—the effects have been to reduce private enforcement.

Mr. THORNE. Mr. Chairman, as a private enforcer, *Trinko* and *Credit Suisse* have not cooled our ardor at all in seeking to fully enforce the antitrust laws. As I mentioned in my written testimony, after *Trinko* we brought a case in a highly regulated industry. We felt no deterrent from the *Trinko* decision. We think *Trinko* lines up squarely with the prior precedents and didn't change anything.

And again, I am not an expert, but as I read *Credit Suisse* that is a case that is specific to the SEC context, and I don't see that precluding private enforcement. And if you look at the good work that the Justice Department and the FTC have done in this Administration so far I don't see these cases cooling their ardor at all either.

Mr. JOHNSON. Thank you, Mr. Thorne. Very careful analysis.

Professor?

Mr. LEMLEY. I think the cases have emboldened the companies that are regulated to look for ways that they can game the system, because if they can engage in conduct that is within or find shelter in regulation they are more confident that they will escape antitrust scrutiny, and I think that is a bad thing.

Mr. COOPER. That is my concern and I have expressed it already—the dynamic of establishing the principle that if you never deal you never have to deal. In industries where we have deeply interconnected networks and essential facilities is leading us to a place where you get people with the ability to really frustrate the entry of competition.

Mr. JOHNSON. Thank you.

And are there any other questions from Members of the Committee?

With that, I will conclude this hearing. I would like to thank all of the witnesses for their testimony, and without objection Members will have 5 legislative days to submit any additional written questions which we will forward to the witnesses and ask that you answer as promptly as you can to made a part—to be made a part of the record. Without objection the record will remain open for 5 legislative days for the submission of any other additional materials.

Today's hearing has raised troubling questions regarding the Supreme Court's attitude toward antitrust laws and the ability of the lower courts to enforce them. I remain concerned that this is part of a larger disregard held by this Court toward the will of Congress.

And with that, this hearing of the Subcommittee on Courts and Competition Policy is adjourned.

[Whereupon, at 11:48 a.m., the Subcommittee was adjourned.]

APPENDIX

Material Submitted for the Hearing Record

Prepared Statement of the Honorable Howard Coble, a Representative in Congress from the State of North Carolina, and Ranking Member, Subcommittee on Courts and Competition Policy

Mr. Chairman, thank you for calling this hearing of the Courts and Competition Policy Subcommittee.

Today's hearing could have profound implications for the jurisdiction of this subcommittee. It deals with two Supreme Court cases that, if the critics are correct, could severely limit the reach of antitrust laws in regulated industries.

I am of two minds on today's hearing. On the one hand, I am a strong supporter of our federal antitrust laws. They are critical to ensuring that customers receive the benefits of competition, namely, lower prices and greater choices.

So, to the extent that these decisions can be read as blanket exemptions from the antitrust laws, I am skeptical of their reach.

On the other hand, I am wary of over-regulating businesses or, what is worse, giving businesses conflicting regulatory demands.

So, to the extent that these decisions can be read as merely clarifying the regulatory burden borne by businesses, I am supportive.

The fact that these decisions can be read two different ways really complicates matters. For example, is *Trinko* merely a limit on the extent that antitrust law can compel a dominant firm to deal with its rivals? Or is it a blanket antitrust exemption for the telecommunications industry, despite an antitrust savings clause in the 1996 Telecommunications Act?

These are very complicated and weighty issues in antitrust law and I am glad that we have such a diverse panel of experts to help us understand the reach of these decisions.

These questions are hardly just academic. Currently, Members of both the House and Senate are meeting to reconcile the financial services regulatory bill. Both versions of that legislation contain antitrust savings clauses. Depending on what we learn here today, we may need to revisit that language to ensure that courts will honor Congressional intent with respect to the role that antitrust will play in the financial services industry going forward.

With that, I look forward to hearing from all of our witnesses on this important topic.

I yield back the balance of my time.

○