Graduate Industrial Organization
Some Notes on Antitrust.

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The purpose of these notes is not to give an introduction to the law of antitrust in any comprehensive way. Instead, the objective is to give a sense of the structure of this body of economic regulation and a taste of the rich and sustaining avenues of research that feed into it...

I Introduction

The Antitrust law is comprised of a range of statutes, including, but not limited to, the Sherman Act, the Clayton Act, the FTC Act, the Hart-Scott-Rodino Act, the National Cooperative Research and Production Act, Antitrust Criminal Penalty Enhancement and Reform Act and the Robinson Patnam Act. The centerpiece of the law, however, is sections 1 and 2 of the Sherman Act. The entire original version of the Act is reproduced below:

> **Transcript of Sherman Anti-Trust Act (1890)**
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> Fifty-first Congress of the United States of America, At the First Session,
>
> Begun and held at the City of Washington on Monday, the second day of December, one thousand eight hundred and eighty-nine.
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> An act to protect trade and commerce against unlawful restraints and monopolies.
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> Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,
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> Sec. 1. Every contract, combination in the form of trust or other- wise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. Every person who shall make any such contract or engage in any such combination or conspiracy, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, at the discretion of the court.

Sec. 2. Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor, and, on conviction thereof; shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

Sec. 3. Every contract, combination in form of trust or otherwise, or conspiracy, in restraint of trade or commerce in any Territory of the United States or of the District of Columbia, or in restraint of trade or commerce between any such Territory and another, or between any such Territory or Territories and any State or States or the District of Columbia, or with foreign nations, or between the District of Columbia and any State or States or foreign nations, is hereby declared illegal. Every person who shall make any such contract or engage in any such combination or conspiracy, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

Sec. 4. The several circuit courts of the United States are hereby invested with jurisdiction to prevent and restrain violations of this act; and it shall be the duty of the several district attorneys of the United States, in their respective districts, under the direction of the Attorney-General, to institute proceedings in equity to prevent and restrain such violations. Such proceedings may be by way of petition setting forth the case and praying that such violation shall be enjoined or otherwise prohibited. When the parties complained of shall have been duly notified of such petition the court shall proceed, as soon as may be, to the hearing and determination of the case; and pending such petition and before final decree, the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises.

Sec. 5. Whenever it shall appear to the court before which any proceeding under section four of this act may be pending, that the ends of justice require that other parties should be brought before the court, the court may cause them to be summoned, whether they reside in the district in which the court is held or not; and subpoenas to that end may be served in any district by the marshal thereof.

Sec. 6. Any property owned under any contract or by any combination, or pursuant to any conspiracy (and being the subject thereof) mentioned in section one of this act, and being in the course of transportation from one State to another, or to a foreign country, shall beforfeited to the United States, and may be seized and condemned by like proceedings as those provided by law for the forfeiture, seizure, and condemnation of property imported into the United States contrary to law.

Sec. 7. Any person who shall be injured in his business or property by any other person or corporation by reason of anything forbidden or declared to be unlawful by this act, may sue therefor in any circuit court of the United States in the district in which the defendant resides or is found, without. respect to the amount in controversy, and shall recover three fold the damages by him sustained, and the costs of suit, including a reasonable attorney's fee.

Sec. 8. That the word "person," or " persons," wherever used in this act shall be deemed to include corporations and associations existing under or authorized by the laws of either the United States, the laws of any of the Territories, the laws of any State, or the laws of any foreign country.

Approved, July 2, 1890.

Needless to say, there have been a few amendments to this statutes over time, the current versions of sections 1 and 2 are:

> §1 Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.
>
> §2 Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.
>
> [see http://uscode.house.gov/download/pls/15C1.txt]

Notice how broad the wording in these sections are. Unsurprisingly, judicial interpretation of these statutes is extensive and sufficiently important that Antritrust Law is often referred to as "Statutory Common Law". That is, the law is developed in the case law. The courts are central to the formulation of the Antitrust Laws.

II Why Antitrust?

The purpose of antitrust laws is to control how firms attain and maintain their market position; presumably for the betterment of consumers, or at least for the benefit of society.

It is tempting to think of this as a weighted average of consumer surplus and total efficiency. However, the law is more subtle and tends to cast things in a more dynamic framework. For instance:

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> **VERIZON COMMUNICATIONS INC., PETITIONER v. LAW OFFICES OF CURTIS V. TRINKO, LLP (Sup. Ct 2004)**
>
> "The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly prices at least for a short period is what attracts business acumen in the first place; it induces risk taking that produces innovation and economic growth. 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.

> Firms may acquire monopoly power by establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing a role for which they are ill-suited. Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion."
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> ...
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> Antitrust analysis must always be attuned to the particular structure and circumstances of the industry at issue.
>
> ...
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> Against the slight benefits of antitrust intervention here, we must weigh a realistic assessment of its costs. Under the best of circumstances, applying the requirements of §2 can be difficult because the means of illicit exclusion, like the means of legitimate competition, are myriad. *United States v. Microsoft Corp., 253 F. 3d 34, 58 (CADC 2001) (en banc) (per curiam).* Mistaken inferences and the resulting false condemnations are especially costly, because they chill the very conduct the antitrust laws are designed to protect. *Matsushita Elec. Industrial Co. v. Zenith Radio Corp., 475 U. S. 574, 594 (1986).* The cost of false positives counsels against an undue expansion of §2 liability. "

That said, much of the mechanics of the economic analysis (as currently practiced) continues to be static, with dynamic considerations being added subsequently (and usually informally).

A justification for Antitrust, of which I am fond (in part because of the Chicago School association) is in Robert Bork's fascinating and provocative book, *The Antitrust Paradox*, at p.311[This is a book that should be read critically, at times the economics is wrong, but always for subtle and interesting reasons].

> "Antitrust is valuable because in some cases it can achieve results more rapidly than can market forces. We need not suffer loses while waiting for the market to erode cartels and monopolistic mergers."

For more on this see Posner's overview of Antitrust in his book (see references)

III What is the scope of regulation?

Before going into specific topics, here is a (incomplete) washing list of the conduct that antitrust has something to say about:

- Monopolization:

  - Predatory conduct
  - Refusal to deal
  - Other exclusionary conduct
- Anticompetitive (horizontal) Agreements:
  - Price fixing
  - Bid rigging
  - Market division schemes and other forms of "non-price" collusion
  - Group boycotts
  - Coordinated refusal to deal
  - Joint ventures
  - Information sharing among competitors
- Anticompetitive Vertical Restraints:
  - Resale Price Maintenance
  - Exclusive Dealing /Exclusive Distributorships
  - Exclusive sales terriories
  - Tying / Full Line Forcing
  - Various quantity limit provisions etc
- Mergers and Aquisitions:
  - Horizontal
  - Vertical
  - Conglomorate
  - Large asset aquisitions e.g. Nortel Patent Portfolio
- Price Discrimination
  - Robinson Patnam Act largely about protecting small business in B2B transactions
- Unfair/Deceptive Methods of Competition (§5 of FTC Act)

- Exemptions
  - Various industries have some sort of exemption from the Antitrust Laws, these include:
  - Agriculture (narrowly construed)
  - Interstate Transport (primarily, the Federal Maritime Commission can approve agreements which are them exempt)
  - Export Trade Associations (you can collude overseas subject to Commerce department saying OK, of course you may have some issues with the overseas jurisdiction...)
  - Bank Mergers (exempt from private enforcement)
  - Insurance (covered by state law not federal)
  - Stock Exchanges (if covered by SEC some ambiguity as to whether limited price fixing OK)
  - Labor Unions
  - Professional Baseball
  - Lobbying Activity
  - Some folks think there is slightly odd applications to "learned" professions...

IV How does enforcement work?

Government enforcement is shared between the DoJ and the FTC. The DoJ is part of the executive, and as such handles all criminal matters (such as price fixing). The FTC enforces the FTC Act (among other things) and tends to have a primary role in consumer protection. Beyond that the jurisdictions are shared. This leads to a cooperative posture to handling matters, with the matters being allocated to the agency that has the greatest expertise in the industry at issue (in the case of mergers) or the legal issue at hand or just the spare resources to handle it...

Both the DoJ and the FTC have large economics groups staffed by PhD economists. Presenting research in front of this audience is aways fun and

thought provoking. Both agencies also have large groups of lawyers. The dynamic seems tobe that the economists provide analysis that feeds into the ultimate enforcement decisions, which seems made mostly by the lawyers (who have to bring the cases). The process in the FTC and the DoJ differs slightly due to the fact that the FTC, by virtue of being a statutory authority has an administrative law function. One aspect of this is that the commissioners take a quasi-judicial role: they make judgements which have legal standing that can get appealed to the US Court of Appeals. The DoJ does not have this feature.

Private enforcement is also an important part of Antitrust enforcement. That is, individuals can bring actions against those that have caused them to suffer an Antitrust harm. This allows for the recovery of damages and the creation of Class Actions. Hence, the private plaintiffs bar is, at times, quite entrepreneurial in bringing (lucrative) actions.

V Section 2 cases: Monopolization

I'll be brief on this area, although there is interesting work to be done here. The basic statement of principle is:

> If that allegation states an antitrust claim at all, it does so under §2 of the Sherman Act, 15 U. S. C. §2, which declares that a firm shall not monopolize or attempt to monopolize. ... It is settled law that this offense requires, in addition to the possession of monopoly power in the relevant market, the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident. *United States v. Grinnell Corp., 384 U. S. 563, 570571 (1966).*

To construct a case, the complainant needs to establish: 1) definition of a relevant market; 2) existence of market power; 3) some kind of anti-competitive conduct other than the exercise of what might be considered normal business acumen, industry, foresight etc. (see Trinko, above)

What is interesting, and I think fairly open, is the refusal to deal in the context of network industries and emerging technologies. Two cases are illustrative:

> **OTTER TAIL POWER CO. v. UNITED STATES, 410 U.S. 366 (1973)**
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> In this civil antitrust suit brought by appellee against Otter Tail Power Co. (Otter Tail), an electric utility company, the District Court found that Otter Tail had attempted to monopolize

and had monopolized the retail distribution of electric power in its service area in violation of §2 of the Sherman Act, 26 Stat. 209, as amended, 15 U.S.C. §2. The District Court found that Otter Tail had attempted to prevent communities in which its retail distribution franchise had expired from replacing it with a municipal distribution system. The principal means employed were (1) refusals to sell power at wholesale to proposed municipal systems in the communities where it had been retailing power; (2) refusals to "wheel" power to such systems, that is to say, to transfer by direct transmission or displacement electric power from one utility to another over the facilities of an intermediate utility; (3) the institution and support of litigation designed to prevent or delay establishment of those systems; and (4) the invocation of provisions in its transmission contracts with several other power suppliers for the purpose of denying the municipal systems access to other suppliers by means of Otter Tail's transmission systems.

The court found that the conduct was a breach of §2, Trinko, which covers somewhat similar territory, found that refusal to deal was within a ATT's independent discretion (although such a right was not unqualified - See *Aspen Ski* for an example). For related issues in a new technology setting see *Berkey Photo, Inc. v. Eastman Kodak*

The issues raised here encompass what is often referred to as the "essential services doctrine". The courts have been confused (in my view) about how to handle these types of cases, and empirical work, that carefully untagles these issues would be welcome. In addition to being instructive as to how the matter should be weighed in practice.

VI Section 1 cases: Anticompetitive Agreements

Here I want to touch on two areas: Collusion and Resale Price Maintenance. Collusion is an example of a horizontal agreement. RPM is an example of vertical agreement. The purpose of this treatment is to point out open questions and the way the academic literature is shaped by policy and vice versa.