

**STATEMENT OF COMMISSIONERS HARBOUR, LEIBOWITZ AND ROSCH
ON THE ISSUANCE OF THE SECTION 2 REPORT
BY THE DEPARTMENT OF JUSTICE¹**

Today the Department of Justice (“the Department”) issued a Report that, if adopted by the courts, would be a blueprint for radically weakened enforcement of Section 2 of the Sherman Act.² We recognize that, in response to our concerns, today’s Report includes more balanced discussion sections than earlier drafts we reviewed. Nevertheless, the final Report’s descriptions and conclusions respecting how Section 2 is and should be enforced cannot be said to represent the consensus, or even the prevailing, view of the myriad of stakeholders interested in Section 2 enforcement. The Report also goes beyond the holdings of the Supreme Court cases upon which it relies. The Federal Trade Commission (“FTC”) does not endorse the Department’s Report.

We have two overarching concerns with the Department’s Report. First, the U.S. Supreme Court has declared that the welfare of *consumers* is the primary goal of the antitrust laws.³ However, the Department’s Report is chiefly concerned with firms that enjoy monopoly or near-monopoly power, and prescribes a legal regime that places these firms’ interests ahead of the interests of consumers. At almost every turn, the Department would place a thumb on the scales in favor of firms with monopoly or near-monopoly power and against other equally significant stakeholders.

Second, the Report seriously overstates the level of legal, economic, and academic consensus regarding Section 2. For example, the witnesses who participated on the hearing panels were far from unanimous in their opinions about what the settled law was, much less what it should be.⁴ Indeed, in hindsight, we are concerned that the testimony gathered during the hearings was not representative of the views of all Section 2 stakeholders, despite the best efforts of the two agencies to assemble balanced witness panels. In particular, we are concerned that voices representing the interests of consumers were not adequately heard. And insofar as the Report relies on economic

¹ Chairman William E. Kovacic does not join this statement and writes separately.

² U.S. DEP’T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT (2008), *available at* <http://www.usdoj.gov/atr/public/reports/236681.pdf> [hereinafter REPORT]. Section 2 prohibits, among other things, monopolization and attempts to monopolize.

³ *Reiter v. Sonotone Corp.*, 442 U.S. 330, 342 (1979).

⁴ We express our appreciation to Commission and Department staff members who labored long and hard to put together the Section 2 hearings. We are equally appreciative of the time and effort invested by all of the witnesses who testified at the hearings (identified in an Appendix to the Department’s Report), and we join the Department in saluting them for their contributions.

theory, the recent warning of Justice Breyer bears repeating: while economic theory is an important consideration in applying antitrust law, economic theory is not tantamount to the law itself.⁵

We envisioned a Report that would identify outstanding issues in Section 2 enforcement; provide neutral and balanced illustrations of the conflicting positions that have been taken on those issues; and suggest topics for further study to help resolve the debate. Such a Report would carefully distinguish between Supreme Court holdings and *dicta* in terms of their precedential value. Additionally, it would take special care not to imply that the testimony at the hearings was representative of the views of all of the Section 2 stakeholders. Such a Report would have made a significant contribution to Section 2 jurisprudence.

I. The Report's Premises

The Department's descriptions of its Section 2 enforcement intentions are based on four fundamental premises. First, the Report embraces the theory that the promise of monopoly profits drives firms to innovate and compete.⁶ Anticipated financial rewards certainly drive innovation and competition. But this does not guarantee that profits resulting from monopoly power will have the same beneficial market effects as profits resulting from competition. Monopolies have been appropriately criticized because they tend toward inefficiency and have reduced incentives to

⁵ *Leegin Creative Leather Prods. v. PSKS, Inc.*, 127 S. Ct. 2705, 2729 (2007) (Breyer, J., dissenting) (“[A]ntitrust law cannot, and should not, precisely replicate economists’ (sometimes conflicting) views. That is because law, unlike economics, is an administrative system the effects of which depend upon the content of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients.”).

⁶ *See, e.g.*, REPORT, Chapter 1 at 7-8; Chapter 2 at 1; Chapter 4 at 49 (low prices); Chapter 7 at 119 (refusals to deal with rivals).

innovate.⁷ Monopolies also have been criticized because monopoly power in one market (even where legitimately acquired or maintained) may be used to leverage power in other markets.⁸

Second, the Report concludes that the risk of over-enforcement of Section 2 is greater than the risk of under-enforcement, contending that fear of liability leads firms to compete less aggressively.⁹ The Report notes that it is often difficult to distinguish between aggressive competition and exclusionary conduct.¹⁰ This may be true in some cases, but that challenge also exists in other areas of antitrust law and is not unique to Section 2. Regardless of the underlying theory of potential liability, antitrust counseling and enforcement decisions require an in-depth, context-specific assessment of the facts. We believe that the federal antitrust enforcement agencies and the private antitrust bar are (and will remain) up to that task, in the Section 2 realm and elsewhere.

At the same time, the Report downplays the risks of under-enforcement. The Report espouses the economic theory that monopoly power is self-destructive and that markets are self-correcting.¹¹ In other words, it is said that a firm with monopoly power (however that power was obtained or maintained) will not have that power forever; thus, the risks of under-enforcement are outweighed by the risks of over-enforcement. Even if correct, however, this hypothesis does not

⁷ Standard Oil Co. v. United States, 221 U.S. 1, 52 (1911) (citing the danger that a monopoly will “fix the price,” impose a “limitation on production,” or cause a “deterioration in the quality of the monopolized product”); United States v. Aluminum Co. of Am., 148 F.2d 416, 427 (2d Cir. 1945) (Hand, J.) (“unchallenged economic power deadens initiative, discourages thrift and depresses energy”); *Federal Trade Commission and Department of Justice Hearings on Section 2 of the Sherman Act: Single-Firm Conduct As Related to Competition*, Sept. 26, 2006 Hr’g Tr., Empirical Perspectives at 13 (Scherer), available at <http://www.ftc.gov/os/sectiontwohearings/docs/transcripts/sept26EmpiricalPerspectivestrans.pdf> (observing that reluctance to “cannibalize the rents that they are earning on the products that they already have marketed” may make monopolists “sluggish innovators”).

⁸ Town of Concord v. Boston Edison Co., 915 F.2d 17, 23-24 (1st. Cir. 1990); *compare* REPORT, Chapter 5 at 77, 90 (declaring that tying is ubiquitous, typically benefits consumers, and is often procompetitive, with no exception for situations where engaged in by a firm with monopoly or near-monopoly power).

⁹ See, e.g., REPORT, Chapter 1 at 14-15; Chapter 3 at 46-47; Chapter 4 at 49, 69 (low prices); Chapter 5 at 88, 90 (tying); Chapter 6, section 1 at 102 (bundled discounts); Chapter 6, section 2 at 116 (loyalty discounts); Chapter 7 at 126, 129 (refusals to deal with rivals).

¹⁰ See, e.g., REPORT, Chapter 1 at 9, 12-13, 18; Chapter 3 at 33-34, 43; Chapter 4 at 49 (predatory pricing); Chapter 5 at 88 (tying); Chapter 6, section 1 at 102, 104-05 (bundled discounts); Chapter 6, section 2 at 116-17 (loyalty discounts); Chapter 7 at 125-26 (refusals to deal with rivals).

¹¹ See, e.g., REPORT, Chapter 2 at 25.

adequately consider the harm consumers will suffer while waiting for the correction to occur. Markets can and do take years, even decades, to correct themselves. For one reason or another, it may take a long time for rivals to surmount entry barriers or other impediments to effective competition. Indeed, the monopolist's own deliberate conduct may further delay a market correction and prolong the duration of consumer harm.

Third, the Department repeatedly cites the “costs of administration” as a factor weighing against enforcement of Section 2.¹² Of course those costs must be considered, by the federal antitrust enforcement agencies as well as by the courts. For example, if it would be impossible to fashion a meaningful remedy for an alleged violation, arguably it is not worth challenging the suspect conduct in the first place. But no one – including the Department – has yet provided a methodology for weighing the costs and benefits of Section 2 enforcement (including potential remedies), or for comparing the relative costs and benefits to businesses versus consumers. Therefore, we do not agree that any category of conduct can be excluded from the scope of Section 2 based on the difficulty of devising an appropriate remedy.

Fourth, the Report emphasizes a need for clear and administrable rules, asserting that this need has motivated courts to fashion “bright line” tests.¹³ While clear rules are desirable in the abstract, the benefits of clarity must be balanced against the benefits of effective and reasonable law enforcement, lest the interests of consumers be compromised.¹⁴ Drawing an analogy to Section 1 enforcement, rules of *per se* illegality largely have been tempered by rule of reason analysis, despite the clear guidance afforded by earlier *per se* rules. Similarly, the Report overstates the extent to which the Supreme Court has embraced bright-line rules of *per se* legality. The only “safe harbors” blessed by the Supreme Court relate to alleged predatory pricing and bidding;¹⁵ they were adopted because of the unique threat to consumer welfare that otherwise might result from challenges to low

¹² See, e.g., REPORT, Chapter 1 at 9, 16; Chapter 2 at 4; Chapter 3 at 45; Chapter 6, section 1 at 102 (bundled discounts); Chapter 7 at 123, 126-27 (refusals to deal with rivals).

¹³ See, e.g., REPORT, Introduction at 2; Chapter 1 at 13-15, 17-18; Chapter 3 at 34-35; Chapter 4 at 49-50, 61, 73 (predatory pricing); Chapter 6, section 1 at 97-98, 105 (bundled discounts); Chapter 6, section 2 at 116 (loyalty discounts); Chapter 8 at 141 (exclusive dealing).

¹⁴ We recognize that businesses are key stakeholders interested in Section 2 enforcement. Firms that enjoy monopoly or near-monopoly power are among these stakeholders, as are their rivals and customers. To the extent the federal antitrust enforcement agencies can provide detailed and transparent guidance to the business community regarding our interpretation of Section 2 and our enforcement priorities – without compromising the interests of consumers – of course we should do so.

¹⁵ *Brooke Group v. Brown & Williamson Tobacco Corp*, 509 U.S. 209 (1993); *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S.Ct. 1069 (2007). The Court has not, however, adopted the “average avoidable cost” safe harbor set forth in the Report. REPORT, Chapter 4 at 65-67.

prices.¹⁶ The Report incorrectly suggests that the Court in *Trinko* adopted a rule of *per se* legality for refusals to deal with rivals, ignoring both the context of the case and the Court’s express language to the contrary.¹⁷

This is not to say that the Department’s premises are entirely without merit. These premises are not totally lacking in support from some of the witnesses at the Section 2 hearings, Supreme Court *dicta* in some cases, and additional scholarship. But these premises do not represent the consensus, or even the prevailing, views of the section 2 stakeholders. They do not reflect the conclusions of those who enacted Section 2 and its counterparts, who decided that, on balance, the negatives associated with the acquisition or maintenance of monopoly power outweigh the positives. Nor do these premises represent the views of the Supreme Court, as those views have been expressed by the Court in its holdings in Section 2 cases. As law enforcement agencies, the Department and the Commission must respect existing law. Of course, the agencies have an equally important obligation to encourage the development of the law – a role that the Commission, in particular, has always taken quite seriously. But with respect to Section 2 enforcement policy, neither the views of the many stakeholders, nor the Supreme Court’s holdings, provide clear guidance regarding whether the drastic changes proposed by the Department are necessary. Therefore, we strongly distance ourselves from the enforcement positions stated in the Report.

II. The Report’s Law Enforcement Standards

The Department’s premises lead it to adopt law enforcement standards that would make it nearly impossible to prosecute a case under Section 2 of the Sherman Act. For example, the Department’s baseline test for Section 2 liability would only condemn conduct if the demonstrable anticompetitive effects are “disproportionately” greater than the procompetitive potential.¹⁸ The disproportionality test distorts the rule of reason standard, which simply asks whether the anticompetitive harm “outweighs” the procompetitive effects. The existing rule of reason standard already poses a significant hurdle to liability, unless care is taken to ensure that a Section 2 plaintiff does not bear a prohibitively high burden of proof.¹⁹

The Department also adopts specific tests for a variety of conduct such as predatory pricing, loyalty discounts, price bundling, tying, refusals to deal with rivals, and exclusive dealing. In almost every case, the Department adopts standards that are tougher – and in some cases much tougher – than existing standards as defined by Section 2 case law.

¹⁶ *Brooke Group*, 509 U.S. at 226-27.

¹⁷ *Verizon Comms. Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004).

¹⁸ REPORT, Chapter 3 at 45.

¹⁹ *See, e.g., United States v. Microsoft*, 253 F.3d 34 (D.C. Cir. 2001).

1. Predatory Pricing

With respect to predatory pricing, the Department states that as long as prices are above a firm's "average avoidable costs" (which would not include any costs incurred before the alleged predatory pricing occurs), the firm's pricing is legal.²⁰ The Department adopts this broad rule of legality despite acknowledging that the rule could enable a firm with monopoly or near-monopoly power to exclude a rival who otherwise could constrain the firm's exercise of monopoly power. This would occur, for example, where the firm and its rival must incur large up-front costs but the "avoidable costs" of producing each unit are *de minimis*.²¹ Moreover, in the event that a firm's pricing falls outside this price-cost safe harbor, the Department would allow proof of "efficiencies" as a "defense even in a setting where there is existing monopoly power."²² No Supreme Court decision has embraced either the Department's "average avoidable cost" safe harbor or the proof of "efficiencies" as an extra defense of conduct that could facilitate foreclosure effects.²³ Indeed, the Department acknowledges that the latter defense "received little attention" at the Section 2 hearings.²⁴

2. Loyalty Discounts

Similarly, in the case of loyalty discounts, the Department states that it "would likely apply a standard predatory pricing test."²⁵ That price-cost "safe harbor" would apply even when the loyalty discounts are so-called "first dollar" or "non-linear" discounts.²⁶ The Department again adopts this price-cost "safe harbor" despite recognizing that this legal standard could permit a firm with monopoly or near-monopoly power to foreclose a weaker rival from the minimum viable scale

²⁰ REPORT, Chapter 4 at 65-67.

²¹ *Id.* at 63-64.

²² *Id.* at 71-72.

²³ In *Brooke Group*, the Court stated only that "an appropriate measure of cost" should be used. *Brooke Group*, 509 U.S. at 222-24. The Court did not say it would be "appropriate" to use a price-cost test that could facilitate foreclosure of rivals in a market where monopoly power exists, and the Court has never blessed an additional "efficiencies" defense in those circumstances.

²⁴ REPORT, Chapter 4 at 71.

²⁵ REPORT, Chapter 6, section 2 at 116.

²⁶ "First dollar" or "non-linear" discounts are discounts offered not only on the "contestable" portion of sales made to customers (sales for which the firm and its rival can both compete) but also on "uncontestable" sales (sales for which a rival cannot compete because, for example, the rival lacks the economies of scale or scope to do so). *See* REPORT, Chapter 6, section 2 at 111-12.

it would need to constrain the exercise of monopoly power.²⁷ In an even more striking declaration, the Department says that if a rival “remains in the market” (no matter how crippled the rival may be), the rival’s existence will be treated as evidence that the loyalty discounts are legal, even if the practices fall outside the ambit of the price-cost “safe harbor.”

There is no authority for these law enforcement prescriptions in the holdings of the Supreme Court or, for that matter, the holdings of the “lower court” invoked by the Department.²⁸ Moreover, the Department’s use of the “standard” price-cost “safe harbor” (or any kind of price-cost “safe harbor”), rather than using an exclusive dealing analysis for these kinds of loyalty discounts, is inconsistent with the Report’s recognition that these practices represent a form of exclusive dealing.²⁹

3. Bundled Discounts

The Department acknowledges that bundled discounts can be used by a firm with monopoly or near-monopoly power to foreclose a rival from the scale it needs to constrain the firm’s exercise of monopoly power, especially when the rival cannot offer all of the products in the bundle.³⁰ Yet the Department declares that if the rival can offer all of the products in the bundle, the “standard” price-cost safe harbor will be used.³¹ If the rival cannot do so, the price-cost “safe harbor” will still be used, modified only to attribute the discount at which the bundle is sold to the products sold in common by the firm and the rival.³² Additionally, even if the bundled discount falls outside of these price-cost “safe harbors,” the Department will nevertheless consider it legal, unless a public or private plaintiff demonstrates that the practice has “no procompetitive benefit” or that the harm is “disproportionate” to the benefit.³³

Again, no Supreme Court decision has ever blessed the use of any price-cost rules of legality for any practice except predatory pricing, and the Department is the sole author and authority for

²⁷ *Id.* at 107, 111-12.

²⁸ The Supreme Court has never blessed the use of any price-cost rules of *per se* legality for any practice except predatory pricing. It is not clear that any of the lower court decisions cited in the Report involved “first dollar” or “non-linear” discounts granted by a firm with monopoly or near-monopoly power. In any event, even if such discounts were involved, the lower courts did not address their exclusionary potential.

²⁹ REPORT, Chapter 6, section 2 at 114-15.

³⁰ REPORT, Chapter 6 at 105-06.

³¹ *Id.* at 105.

³² *Id.*

³³ *Id.* at 117.

use of the “disproportionality” safety net.³⁴ Moreover, the Report does not mention the possibility of analyzing bundled discounts as a form of exclusive dealing instead of affording them the protection of price-cost “safe harbors” and requiring proof of “disproportionality,” despite the Department’s recognition of the kinship between bundled discounts and “first dollar” loyalty discounts (the latter having been identified by the Department as a form of exclusive dealing).

4. Tying

The Department declares that tying is ubiquitous.³⁵ Contrary to existing Supreme Court case law,³⁶ the Department says that tying (presumably even by a firm with monopoly or near-monopoly power) “typically benefits consumers” and is “often procompetitive.”³⁷ Tying surely benefits consumers in some instances, but the Department draws no distinction between the use of tying by a firm with monopoly power or near-monopoly power and the use of the practice by other firms.³⁸ Additionally, lest the practice of tying be challenged despite these admonitions, the Department would require public and private plaintiffs to prove that the anticompetitive consequences of a tying scheme are “significantly disproportionate” to any benefits.³⁹ As previously stated, the disproportionality test is of the Department's own making.⁴⁰ The Department’s position enjoys no support in the law, and it is so ill-defined that it will be hard, if not impossible, for any public or private plaintiff to satisfy it.

5. Unilateral Refusals to Deal with Rivals

The Report flatly declares that unilateral refusals to deal with rivals “should not play a meaningful role in antitrust enforcement,” regardless of a firm's monopoly power or the potential for foreclosure.⁴¹ The Department incorrectly implies⁴² that the Commission subscribed to this

³⁴ REPORT, Chapter 3 at 45-46.

³⁵ REPORT, Chapter 5 at 77.

³⁶ Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2 (1984).

³⁷ REPORT, Chapter 5 at 90.

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *See* REPORT, Chapter 3 at 45-46.

⁴¹ REPORT, Chapter 7 at 127, 129.

⁴² *Id.* at 124 and n. 71.

position in the agencies' joint April 2007 report on intellectual property issues ("IP Report").⁴³ The IP Report concluded that "mere unilateral, unconditional refusals to license will not play a meaningful part in the interface between patent rights and antitrust protection."⁴⁴ That statement reflected the agencies' view that the simple act of refusing to license intellectual property may not constitute a violation of the antitrust laws. That view is consistent with the Supreme Court's holding in *Illinois Tool Works* that intellectual property may or may not confer monopoly power.⁴⁵

If a patent does confer monopoly power, however, then denial of access to the patented technology may not be a "mere" unilateral refusal to license intellectual property. A firm with monopoly power or near-monopoly power may violate Section 2 if it refuses to license to, or otherwise refuses to deal with, a rival. The Commission has never itself, or in conjunction with the Department, said otherwise. Indeed, the Supreme Court repeatedly has held, as it stated long ago in its *Colgate* decision, that when there is a "purpose to create or maintain a monopoly" there may be a duty to deal with a rival.⁴⁶ Although the Court held in *Trinko*⁴⁷ that a firm with monopoly power had no duty to deal with rivals when the public was protected by regulation of the firm's practices, the Court declared in *Trinko* that the right to refuse to deal with rivals is not unqualified.⁴⁸ The Department acknowledges this aspect of *Trinko* in its Report but fails to apply such a standard to the conclusions in this chapter.⁴⁹

6. Exclusive Dealing

Finally, with respect to exclusive dealing, the Department adopts another "safe harbor," declaring that the practice is legal if no more than thirty percent of the market is foreclosed to a

⁴³ U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION (Apr. 2007), available at <http://www.ftc.gov/reports/innovation/P040101PromotingInnovationandCompetitionrpt0704.pdf>.

⁴⁴ *Id.* at 6, 32.

⁴⁵ *Illinois Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006).

⁴⁶ *United States v. Colgate & Co.*, 250 U.S. 300 (1919) (*dictum*); *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 602 (1985); *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 466-467 (1992).

⁴⁷ *Trinko*, 540 U.S. 398.

⁴⁸ *Id.* at 408 (citing *Aspen Skiing*, 472 U.S. at 601).

⁴⁹ REPORT, Chapter 7 at 122, 125.

rival.⁵⁰ According to the Report, that rule applies despite the Department’s acknowledgment that a rival may need greater access to the market in order to achieve sufficient scope and scale to constrain the exercise of monopoly power.⁵¹ The Department further declares that exclusive dealing will be considered legal, even if outside the “safe harbor,” unless the public or private plaintiff can establish that the conduct has no procompetitive effects or that its anticompetitive effects are “disproportionate” to its benefits under the Department’s newly-created “disproportionality” requirement.⁵²

III. Conclusion

The Department’s Report does not consider all of the exclusionary practices that may be used to obtain or maintain monopoly power and cause harm to consumers.⁵³

The Department embraces a series of “safe harbors” applicable to individual practices, even though each of these practices has substantial potential to lead to anticompetitive foreclosure if employed by a firm with monopoly power or near-monopoly power. In other words, each practice might be used by a firm with monopoly power or near-monopoly power to foreclose a rival from making sales the rival needs to compete effectively. As a result, the dominant firm might be sheltered from competition that otherwise would constrain its exercise of monopoly power.

Even for practices that fall outside the “safe harbors,” the Department would impose rigorous burdens of proof on both public and private plaintiffs. These burdens of proof will be difficult, if not impossible, for plaintiffs to meet.

In short, the Department’s Report erects a multi-layered protective screen for firms with monopoly or near-monopoly power. As an inevitable consequence, dominant firms would be able to engage in these practices with impunity, regardless of potential foreclosure effects and impact on consumers. Indeed, it appears that the Department intends for this screen to apply even when a firm uses two or more of these practices collectively, instead of just one practice individually.

⁵⁰ REPORT, Chapter 8 at 141.

⁵¹ *Id.* at 137.

⁵² *Id.* at 140.

⁵³ As one notable example, except for a passing reference, the Report ignores forms of “cheap exclusion;” that is, virtually costless forms of exclusionary conduct, which may be employed by a firm with monopoly or near-monopoly power. See Susan A. Creighton, D. Bruce Hoffman, Thomas G. Krattenmaker & Ernest A. Nagata, *Cheap Exclusion*, 72 ANTITRUST L.J. 975 (2005) (citing, as examples, the Commission’s *Unocal* case and the Commission’s Orange Book exclusion payment cases).

This Commission stands ready to fill any Sherman Act enforcement void that might be created if the Department actually implements the policy decisions expressed in its Report. We will continue to be vigilant in investigating and, where necessary, prosecuting Section 2 violations.

The Department's Report undoubtedly will spark lively discussion and spur additional Section 2 scholarship, and we look forward to being a part of that process. In addition, we will continually seek to strengthen our relationships with our foreign counterparts, as we look around the world for additional perspectives on dominant firm conduct and other competition issues.