# CAN ECONOMICS BRIDGE THE ATLANTIC?
## Monopolization under Section 2, Dominance under Article 82, and Fouls in Football

by

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Section 2[1] is the hardest part of United States antitrust law. It is analagous to the calls made near the end of American football games. Trailing by 4 points with the ball at the 50 yard line and 30 seconds to go, the quarterback for one team – think of it as a small firm - arches a long pass to the end zone. The receiver and defensive back, who plays for the team you can think of as the dominant firm, jump for the ball and collide. The ball falls to the ground. The referee – think of him as the antitrust authorities or the courts - has to decide whether the defender was or was not within the rules. The decision almost surely determines the outcome of the game.

For visitors from Europe not familiar with American football, similar situations arise in what you and the rest of the world call football. With the score 1-nil in the 89th minute, the striker for one team – again, think of it as the small firm - seems to have a break-away in the box, but the opposing sweeper is able to strip him of the ball with a hard tackle, perhaps from behind. Should the referee award a penalty kick and issue a red card? The cries from the fans who don't like the call – think of them as shareholders, lawyers, or consultants for the losing side - are vociferous; and whether the right call was made can be debated in bars and pubs – think of them as law journals and conferences like this one - for years afterward.

I have chosen these particular sports analogies because the stakes are high; and the question is typically whether a particular practice reflects great skill or a violation of the rules. Given those stakes, I should not go any further without issuing the standard disclaimer. What I say today reflects my views.[2] It does not necessarily reflect the views of the Federal Trade Commission or any of the individual commissioners.

I have been asked to talk today about whether evolving economic principles can be the basis for convergence in general and with respect to monopolization/dominance cases in particular. I will argue that while economics might play this role, it is hardly inevitable that it will. Economics might simply clarify our differences.

An economic approach to a Section 2 case or, for that matter, any antitrust case, means that we state the theory of the case in terms of a model. The discipline of modeling forces us to analyze rigorously and coherently 1) why the practice is profitable and 2) why it is harmful. Answering the second question requires defining exactly what we mean by harm. Given the sophistication of this audience, it might seem inappropriate for me to talk about first principles; but disagreements across the Atlantic might reflect first principles. At the risk of appearing overly simplistic, therefore, the most fundamental issue in monopolization cases is whether they protect competitors or competition. I know of no antitrust practitioner in the United States who admits to thinking that protecting competitors is the proper objective. And yet, even people who profess to have the protection of competition at heart sometimes end up in effect arguing for the protection of competitors. The discipline of modeling can correct this tendency because it forces the

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[1] I refer, of course, to Section 2 of the Sherman Antitrust Act, 15 U.S.C. §2, which makes it illegal to monopolize or attempt to monopolize a market.

[2] I have benefitted from discussions with Mark Frankena, Paul Pautler, and Josh Soven, none of whom are responsible for any errors of fact or judgment.

analyst to be specific about what harm means. When modeled, the principle that antitrust is to protect competition means that "harm" must be an increase in price or, in a more complex setting, a decrease in consumer welfare. It could conceivably mean a decrease in total welfare, although I personally would not endorse such a standard. It cannot mean an increased share for the leading firm or a reduction in the number of competitors. At least that is my view. I am, of course, aware of the argument that in the long run, one must preserve competitors to preserve competition. That is, to put it mildly, an unpopular view in U.S. antitrust circles. My sense is that it is given more credence in Europe. If Europe and the U.S. come out differently on this very fundamental issue, we will not get convergence.

Even if we can agree on the objective function and on the use of economic models to ensure logical consistency to our cases, there is no guarantee of convergence. If we use different models, we will get different results. In a speech I gave two weeks ago in London and Brussels,[3] I asked rhetorically what the antitrust reaction to a Microsoft-Intel merger would be. That hypothetical concerned a merger, not monopolization or abuse, but I cite it here as an example where I am confident that different analysts, choosing different models, would make dramatically different recommendations. The mere use of economics does not guarantee convergence.

Similar issues will arise in analyzing monopolization and abuse of dominance issues. Consider tying, a topic that has occupied a fair amount of my attention in recent years. To have a sensible model of tying, I believe you need to recognize that requiring firms to sell on an unbundled basis imposes costs inherent in a more complex set of product offerings.[4] In my view, if you don't build that assumption into a model of tying, you have simply ignored an essential piece of the basic economics of the decision. Yet, other economists who have modeled tying have left that feature of the cost-benefit analysis out of their models. If I picked up an object and dropped it in front of a group of physicists, I doubt there would be much disagreement over what model would describe the motion of the falling object. Economics has not reached the point where we can expect similar agreement.

Such disagreements over how to model a problem lead to disagreements on substance. I confess to being puzzled by what I see to be continued interest in Europe in tying and bundling of products sold to final consumers.[5] Tying and bundling are practices that are completely prevalent in competitive markets, which is compelling empirical support for the proposition that they can be efficient. Moroever, the economics models that suggest that they might be problematic seem to rest on highly specialized assumptions. I don't know what we would look to in a particular case to conclude that the practice in fact

[3] Michael A. Salinger, "Is it Live or is it Memorex: Models of Vertical Mergers and Antitrust Policy," Association of Competition Economics Seminars on Non-horizontal Mergers, London, September 7, 2005 and Brussels, September 8, 2005, available at http://www.ftc.gov/speeches/salinger/050927isitlive.pdf.
[4] See David E. Evans & Michael Salinger, "Why Do Firms Bundle and Tie? Evidence from Competitive Markets and Implications for Tying Law," *Yale Journal on Regulation*, vol. 22, 2005, pp. 37-89.
[5] I distinguish bundling and tying to end consumers from the bundled discounts that were at issue in LePage's, Inc. v. 3M, 324 F.3d 141 (3d Cir. Pa., 2003), cert. denied 124 S. Ct. 2932 (2004) and Virgin Atlantic Airways Ltd. v. British Airways, PLC, 257 F.3d 256 (2d Cir. 2001).

leverages or preserves market power. To use terms associated with commentators on either side of the Atlantic, antitrust concerns with bundling and tying seem to be based on what Frank Fisher termed "exemplifying theory,"[6] not, to use John Sutton's phrase, "robust theory."[7] My understanding and hope is that the U.S. Supreme Court will in the not too distant future overturn the per se treatment of tying under Section 1. Without that artificial legal inducement to tack a Section 1 claim to monopolization cases, I do not see tying of products sold to final consumers playing a prominent role in Section 2 enforcement. If the concern with bundling and tying continues in Europe, I do not think we will see convergence.

An area of monopolization/dominance law where I am more optimistic about convergence is vertical foreclosure. I do not mean to suggest that such cases are easy. A striking feature of the modern economic landscape that is different from earlier periods of antitrust history is how vertically disintegrated firms with large market shares are. The business historian Alfred Chandler put forth the hypothesis that vertical integration was a key aspect of the strategy for the companies that came to dominate their markets in the early part of the 20th century.[8] He argued that explicit control of the flow from raw material to the final consumer was needed to support new scales of operation. That simply is not true anymore.[9] We should not be surprised to see firms at different stages of production enter into complicated contracts, and the contractual terms between a dominant firm at one stage and either its upstream suppliers or downstream distributors can give rise to complaints of monopolization or abuse. The Dentsply[10] decision in the United States provides a case in point. Dentsply was the dominant supplier of artificial teeth. It sold through dental suppliers, which also sold other kinds of dental supplies. According to the decision of the court of appeals, this form of distribution provides convenience for dental laboratories, as they can purchase multiple supplies from a single firm. Dentsply's contracts with dental distributors required exclusivity, leaving competing producers of artificial teeth with direct distribution as their best alternative. As I said, I do not think such cases are easy. Exclusive contracts are common in competitive settings and with good reason. To take a simple example, some universities do not let their professors teach courses at other universities without permission, as they are concerned that competing universities will free ride on their brand name. In my opinion, the concern with exclusivity is that it can, to use a phrase coined by one of my predecessors as Bureau Director, raise rivals' costs.[11] In the case of professors and

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[6] See Franklin M. Fisher, "Games Economists Play: A Noncooperative View," *The Rand Journal of Economics*, vol. 20, 1989, pp. 113-24.

[7] See John Sutton, *Sunk costs and Market Structure: Price Competition, Advertising, and the Evolution of Concentration* (Cambridge, Massachusetts: MIT Press) 1991.

[8] See Alfred D Chandler Jr, *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, Massachusetts: Belknap Press) 1977.

[9] See Naomi R. Lamoreaux, Daniel M.G. Raff, & Peter Temin, "Beyond Markets and Hierarchies: Toward a New Synthesis of American Business History," NBER Working Paper 9029, June 2002.

[10] U.S. v. Dentsply ("Dentsply") 277 F. Supp. 2d 387 (D.C. Del. 2003), r'vsd and remanded, 399 F.3d 181 (3rd Circ. 2005).

[11] Steven C. Salop & David T. Scheffman, "Raising Rivals' Costs," *American Economic Review*, vol. 73, 1983, pp. 267-71.

universities, there are many people capable of teaching college courses and many universities vying for their services, so the effect of exclusivity on rivals' costs cannot be great. If a dominant firm at one stage insists on exclusivity at another, however, then it may tie up that entire stage. That cannot by itself be illegal, as there might be efficiency justifications for the contracts. Still, raising rivals' costs provides an economically sound basis for distinguishing anticompetitive actions that should be condemned by the monpolization and abuse statutes from competitive actions that the antitrust laws are intended to promote.

To conclude, therefore, with as succinct an answer as I can give to the question I was asked to address, simply using economic tools will not be sufficient to bring about convergence. Economics will lead to convergence if we agree on the types of models that are useful for different types of cases. If, on the other hand, we choose different models embodying perhaps different objectives, then, as with football, we may use the same name for the game we are playing; and we may have similarly heated debates about how certain calls should come out; but the competition policy game we will be playing will be fundamentally different.