# What's driving the US antitrust agencies?

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As antitrust veterans know, no matter how much a new administration may want to change how antitrust is enforced, the bulk of the agencies' enforcement agenda remains relatively constant from one administration to the next. Overheated rhetoric notwithstanding, most enforcement decisions are driven by the application of widely shared principles to the facts, with the result that the cases that get brought (or not) usually have more to do with the course of events – what deals are proposed, what misconduct detected – than the agencies' current enforcement agenda.

Over time, however, trends emerge. With two years of Obama administration antitrust enforcement now on display, we have a sufficient record on which to draw some reliable conclusions about what makes this administration's approach to antitrust enforcement different, and what those differences portend for the next few years.

It would be far too simplistic to conclude, based on early rhetoric and the pace of new enforcement announcements, that this administration is motivated by a desire to bring more cases for the sake of statistics, or to appear more aggressive solely for the sake of making antitrust enforcement seem more vigorous. That conclusion would also be unfair to the professionals at both agencies who conduct investigations and make enforcement recommendations. Nonetheless, a close examination of the enforcement records at both the US Department of Justice's antitrust division and the Federal Trade Commission – as reflected in what the agencies have chosen to investigate, how they have resolved those investigations, and what they have said about them – does confirm that the agencies are trying to shift the substance of enforcement in meaningful ways.

We make no effort to present a comprehensive assessment of the record so far, but at least five themes stand out.

### Targeting exclusionary conduct

The first, and likely most obvious, theme has been the agencies' new eagerness to attack conduct that they perceive as "exclusionary," in the sense that its anti-competitive effects, if any, are accomplished indirectly by excluding or impeding rivals. Christine Varney began her tenure as assistant attorney general (AAG) by announcing that the division was withdrawing the Bush administration's report on single-firm conduct – widely known as the Section 2 Report – and planned to reinvigorate enforcement against unilateral conduct of dominant firms. As she declared: her division would not "sit on the sidelines any longer." In place of the Section 2 Report, AAG Varney has offered little guidance other than citation to three cases in which plaintiffs won victories challenging exclusionary conduct: *Microsoft*, *Lorain Journal*, and *Aspen Skiing*.

Section 2 cases – like cases addressing vertical agreements, which can have similar kinds of effects – take time to investigate and develop, so it was not surprising that Varney's antitrust division did not come out of the gates with a barrage of complaints challenging exclusionary conduct. The record of the first two years, however, leaves no doubt that the division has been looking hard for promising cases to amplify the signal that such conduct will be pursued aggressively.

Two of the division's pending lawsuits attack conduct that the division asserts harms competition by diminishing the competitive pressures posed by rivals. Its suit against Blue Cross, Blue Shield of Michigan asserts that the defendant used most-favoured nations clauses in contracts with hospitals to eliminate rival health-care insurers' ability to strike their own better deals with those same hospitals. The division's lawsuit against American Express – and its settlements with Visa and MasterCard – similarly asserts that the defendant used its rules to prevent merchants from promoting rival, and lower cost, payment methods that might compete against AmEx's payment card network. The division is surely looking for more cases of this sort.

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The division's heightened concern about exclusion also shows up in its recent merger enforcement record, most vividly in its challenge to the *Comcast/NBCU* joint venture. Described by AAG Varney as a case about raising rivals costs, the division's complaint against this vertical transaction stems from the conclusion that, following the venture's formation, the two firms would have new incentives to use their market power to disadvantage (and exclude) Comcast's traditional multichannel video programming distribution (MVPD) competitors as well as its budding online rivals. The division's consent decree even includes extensive rules governing when and how *Comcast/NBCU* may include exclusivity provisions in its contracts with third parties.

For its part, the FTC has been no less aggressive, as shown most clearly in its broad-ranging section 5 complaint against Intel. That sweeping challenge to Intel's distribution practices not only

took an extraordinarily strong stance against so-called bundled rebates and loyalty discounts, but also attacked allegedly deceptive marketing and other aspects of a broad "course of conduct" that FTC Commissioner Rosch acknowledged might not be regarded by the courts as a violation of section 2 of the Sherman Act.

Unfortunately, the lessons to be drawn from these actions by businesses and their advisors are unsettlingly opaque. Neither agency has been willing to chart any clear lines (or safe harbours) limiting their discretion to pursue exclusionary conduct when and where they perceive it. Rather than numbers of cases, or even their doctrinal foundation, this is the most conspicuous shift in the agencies' enforcement approach. Far less concerned about the potential chilling effect their enforcement may have on pro-competitive behaviour, the agencies now seem to be striving actively and broadly to deter conduct that might diminish the competitive opportunities of rivals.

#### Regulating behaviour when competitive forces are thought inadequate

A corollary to the agencies' stepped-up enforcement against exclusionary unilateral conduct and vertical mergers has been their almost unprecedented willingness to use antitrust decrees to regulate firm behaviour when competitive forces are deemed inadequate.

A prime example is the FTC's settlement of its allegations in the *Intel* case, which imposes an extraordinary array of behavioural limitations on the firm's future marketplace conduct, committing the agency to engage in active monitoring of the firm's activities for years to come. Perhaps this sort of relief is to be expected in a unilateral conduct case, where structural relief is either unavailable or unwarranted in light of the scope of the agency's allegations.

At the division, however, an openness to behavioural remedies has found its way into merger enforcement, in cases such as *Comcast/NBC*, *Ticketmaster/Live Nation*, and *GrafTech/Seadrift Coke*. The *Comcast/NBCU* decree perhaps reflects an extreme example of the division's willingness to allow mergers to go forward based on the parties' agreement to submit their post-merger behaviour to probing and detailed oversight. The proposed decree in that case takes the extraordinary step of regulating the pricing and terms offered by the venture parties by reference to prices and terms offered by third parties (*Comcast/NBCU*'s so-called "peer firms"), restricting their ability to negotiate certain contract terms to those consistent with "common and reasonable industry practice," and establishing an entirely new dispute resolution regime overseen by the division. In another recent decree – *GrafTech/Seadrift Coke* – the division imposed significant restrictions on future contracting behaviour by the merging parties, and in yet another – *L.B. Foster/Portec* – required the parties to report to the division about their ongoing relationships with third parties in markets in which the complaint had not alleged any anti-competitive effects.

To be sure, restrictions on post-merger conduct are not new to antitrust settlements, but this administration has seemed far less reluctant to make use of them. What's driving that trend?

The most obvious explanation is that this sort of behavioural relief is inevitable if the agencies are going to be focusing their efforts on exclusionary conduct, both in monopolisation cases (or analogous claims under section 5) and vertical merger challenges like *Comcast/NBCU* and *GrafTech/Seadrift Coke*. Except perhaps in merger cases, where the agencies have the option of seeking to block the proposed transaction entirely, some sort of conduct-related remedy is likely to be the only way to resolve the kinds of concerns underlying the agencies' challenges.

There is no doubt, though, that the agencies' willingness to impose such remedies also reflects new-found confidence (or hubris?) that their crafting and administration of the behavioural restrictions will draw the right lines around the parties' future conduct, and diminished worries about the adverse effects on competition and consumers if the decrees turn out to bind the parties' hands too tightly.

#### Switching sides in the debate over "innovation effects"

A third key theme of the past two years has been the agencies' changed attitude towards the role of antitrust in rapidly changing markets where innovation provides important consumer benefits.

Both agencies have, as in previous administrations, worked hard to send the message that antitrust enforcement remains relevant and important in the high-tech sectors of the economy. And their case selection demonstrates that, like the previous administration, they will not hesitate to bring cases also challenging conduct or transactions involving the internet economy. Just as the last administration investigated and challenged the proposed Google-Yahoo! search advertising collaboration, so this one attacked Intel's conduct and is carefully scrutinising Google's proposed acquisition of ITA. The high-technology sector is an increasingly important part of the United States' economy, and it is only natural for antitrust scrutiny to follow.

In rapidly evolving "new economy" markets, innovation has long played an important role in the agencies' analysis of competitive effects. Safeguarding the benefits of innovation is a central theme of the reports on intellectual property and antitrust issued by prior administrations, as well as numerous speeches by agency officials.

The new administration cares deeply about innovation as well, but there have been two notable shifts in approach. First, the agencies' enforcement record and rhetoric show them to be much more confident in their judgement about the sources of innovation that antitrust policy should work hardest to protect. Whereas prior administrations were hesitant to use antitrust to regulate the behaviour of firms that had achieved success through path-breaking innovation, this administration has been far more willing to intervene to ensure opportunities for the next generation of firms to compete for consumer attention through innovation, even if doing so requires the dominant firm to pull its punches to facilitate those efforts.

This shift is nowhere clearer than the 180 degree reversal in the division's views about "net neutrality" regulation. In 2007, the division counselled caution, lest regulation reduce the incentives for broadband network owners to invest. In 2011, the division has affirmatively embraced net neutrality regulation by requiring *Comcast/NBCU* to comply with the FCC's new net neutrality regulations even if they are overturned by the courts. More generally, the FTC's suit against Intel and the division's against *Comcast/NBCU* illustrate the agencies' new bias toward protecting the potential benefits from innovation by firms challenging the strong market position of market incumbents, rather than preserving the incentives for firms to strive to become dominant through innovation.

Second, perhaps related to their new openness to behavioural remedies, the agencies seem far more willing to stake decisions to bring cases on predictions about the likely evolution of fast-changing markets. We doubt that agency staffs are any better able to predict the future than they were in the past. Rather, the agencies seem philosophically more prepared to err on the side of using antitrust to provide new opportunities for smaller firms and less inclined to think that markets might evolve favourably without their intervention or worry that firms may be less inclined to innovate out of fear that antitrust will force them to play fair with rivals if they achieve great success. Reflecting this attitude, the division explained in *Comcast/*

*NBCU* that the joint venture's potential post-formation conduct was "extremely troubling given the nascent stage of [online video distributors'] development".

**Making market definition matter less – the ascendant role of unilateral effect analysis and direct evidence of anti-competitive effects**

It is old news that, particularly in the merger arena, the agencies have placed greater emphasis on unilateral effects analysis, which in turn has led them to place greater weight on direct evidence of likely anti-competitive effects. Unilateral effect theories underlay many of the merger challenges in the last administration and also animated many of the non-merger investigations and challenges as well.

With the appointment of Joe Farrell and Carl Shapiro as chief economists at the two agencies, however, the agencies are more inclined than ever to leap straight to a conclusion about competitive effects without passing through any formal analysis of market power in any defined antitrust market. The revised discussion of unilateral effects analysis in the new Horizontal Merger Guidelines stakes out this position in no uncertain terms, putting courts on notice that they should be more sympathetic to agency challenges founded upon economic analysis of the effects a proposed transaction will have on the post-merger competitive incentives and decision-making of the combined firm.

A wide array of agency challenges over the past few years (and before) show that unilateral effects theories are driving much of the agencies' enforcement agenda. The division's analysis in *Comcast/NBCU* of the joint venture's post-transaction incentives to use its control over NBCU content to disadvantage Comcast's rivals, the FTC's attack on the *Wholefoods/Wild Oats* merger, and many of the agencies' less-publicised challenges (such as the division's in *Baker Hughes/BJ Services* and *Bemis/Alcan Packaging Foods Americas* and the FTC's in *Panasonic/Sanyo* and *Danaher/MDS*, to name just a few) highlight the trend. In view of the merger guidelines' explicit endorsement of this approach, this trend will certainly continue.

But there is also an emerging subplot. There appears to be a tendency for the agencies, and especially the FTC, to conclude that conduct is anti-competitive whenever there appears to be evidence that prices are higher as a result of the conduct, even if it is not so clear that higher prices stem from any adverse impact on the competitive process. This reasoning is apparent in such cases as the FTC's section 5 challenge to N-Data's decision to demand high patent royalties; its challenge to Fresenius' acquisition of a drug from Daiichi Sankyo, where the concern was the evasion of Medicare price-control regulation; and the controversial comments by Commissioner Rosch suggesting that FTC staff should have challenged the sale by Merck of several of its drugs to Ovation, which freed Ovation to increase prices radically because it lacked Merck's reputational inhibitions. This reasoning also shows up in the division's challenge to Keyspan's hedging contract, which gave it an incentive to demand higher prices for its electric capacity.

A desire to circumvent analysis of how particular conduct might harm competition also shows up in the FTC's expansion, in the recent *Realcomp* decision, of the "inherently suspect" framework of analysis, which allows condemnation of conduct without any analysis of the defendant's market power or the actual effects of the conduct in any relevant market.

**Aggressively pursuing practices that might make collusion more likely**

At the same time, the agencies have sought to loosen the standards for challenging conduct that may facilitate collusion among competing firms. The new merger guidelines, for example, do away with any suggestion that the agencies must prove precisely how a transaction will enable firms to reach terms of coordination or police compliance with those terms. It is now enough for the agencies merely to conclude that they have a credible basis for thinking that a merger may enhance a market's vulnerability to coordinated interaction.

In their non-merger civil enforcement programmes, moreover, both agencies have been paying particularly keen attention to practices that may facilitate collusion, even if they do not rise to the level of an anti-competitive agreement. In *GrafTech/Seadrift Coke*, for example, the division challenged a merger that integrated a producer of graphite electrodes with one of its key suppliers (of petroleum coke), because the combined firm would inherit a supply relationship with another key supplier of the same input, and might use its contractual most-favoured nation rights to facilitate coordination among coke producers. This concern could just as easily arise outside the merger setting, when vertically integrated firms interact with a customer or suppler that is also a competitor.

In a similar vein, both the FTC and DoJ have aggressively investigated (and the FTC recently challenged in the *U-Haul/AMERCO* matter) public statements made in the context of public earnings statements – and related conference calls with securities analysts – that the agencies have perceived as designed to invite coordination by the competitors monitoring the remarks.

**What do these trends portend for the coming years?**

Although the cases the agencies investigate and bring in the coming years will continue to depend critically on the mergers that are proposed and the conduct the agencies detect – in part through complaints from customers and competitors – these trends will shape the agencies' case selection, litigation strategies and settlement approach. We can confidently predict that:

The agencies – especially the division – will be looking hard for more merger and non-merger cases targeting exclusionary conduct. The door has for some time been open to competitors with complaints about the conduct of their dominant rivals. The agencies will remain open to hearing these kinds of stories and will continue to sift these complaints for potential cases warranting enforcement attention.

Both agencies will be very active in industries – especially in the high-tech field – where they see a role for antitrust in protecting the opportunities of smaller firms to innovate. They will tend to emphasise the benefits of providing smaller firms with freer access to markets in which dominant firms compete while downplaying the potential long-run costs occasioned by an enforcement climate that reduces the rewards available to firms that succeed though innovation.

Both agencies will continue to pursue creative theories of competitive harm flowing both from unilateral incentive effects as well as from the facilitation of coordination, both tacit and explicit.

And the agencies will focus their limited resources on certain sectors of the economy where they see antitrust enforcement as mattering most. Among the key areas of focus will be health care, which has attracted so much of the FTC's attention of late and also continues to garner the division's attention in such cases as Blue Cross Blue Shield of Michigan; the technology sector, where both agencies have been active; as well as industries that are the focus of the administration's broader economic policies: financial services, energy and agriculture.