

The Enforcer Tapes: Colorado

Comments, Questions and Answers, Charles James and Timothy J. Muris, ABA Section of Antitrust Law Post-Annual Meeting, Colorado Springs, August 9, 2001

The following are the edited remarks of Timothy J. Muris, Chairman of the Federal Trade Commission and Charles A. James, Assistant Attorney General of the Antitrust Division of the U.S. Department of Justice, at the ABA Section of Antitrust Law Post-Annual Meeting in Colorado, August 9, 2001.

Roxane Busey, Chair of the ABA Section of Antitrust Law, introduced the two top U.S. antitrust enforcers and invited the audience to ask them probing questions after their remarks.

Comments of Chairman Muris

I will briefly discuss two issues and leave most of the time for questions. One is *California Dental (CDA)* and the issue of truncation; the other is the role of economics.

One point that has surprised me in talking to attorneys in the Bureau of Competition is the looming presence of *California Dental*. As I wrote in an article published last year in the *Supreme Court Economic Review*, given the way the case was tried, the Supreme Court's decision is not surprising. I argued that the case transposed to antitrust a longstanding dispute among the members of the Court about professional advertising that had been previously played out in First Amendment cases. Indeed, *CDA* and the 1995 *Florida Bar* decision had many similarities in the judicial lineups and the issues raised.

For antitrust, *CDA* makes a couple of important points. One, it recognizes once and for all what I thought was obvious, but some others did not, namely that the rule of reason involves a continuum, and that there can be truncation in various cases. Second, *CDA* reinforces that evidence is important. When the Commission tried

the case, it used essentially a per se theory. Ironically, there is abundant evidence about the anticompetitive nature of restraints on advertising and, even more ironically, the FTC itself had produced much of the evidence. For whatever reason, however, the complaint counsel did not choose even to use an economist at trial, and the agency ultimately bore the cost of that ill-fated decision.

In the 1980s, we developed a form of analysis that became known as *Massachusetts Board*. The *Massachusetts Board* analysis derived from a brief that we authored with the Solicitor General on the *NCAA* case. We did not use the word "truncation," but we talked about the possibility of applying the rule of reason in that manner.

As did that analysis, *California Dental* tells us that you have to categorize. There are various levels of analysis under the rule of reason, ranging from preemptory—Areeda's "wink of an eye"—to so-called full-blown rule of reason when market definition would be necessary, absent direct evidence of anticompetitive effect. Surprisingly, some people still want to ignore this fundamental issue of categorization. A prob-

lem with *Massachusetts Board* was it did not really tell you how to categorize. It did have a formula, and, predictably, some of the staff at the Federal Trade Commission found it too easy to allow truncation. In practice, *Massachusetts Board* became too much like the old per-se-versus-rule-of-reason categorization.

Although the concept of truncation and a spectrum is more sophisticated than what it replaced, you still cannot avoid this fundamental issue of the necessity of some form of categorization. As I have written in recent articles, truncation ought to be based on experience. As we gain experience with certain practices, we will need less evidence to condemn them. The classic examples, which everyone recognizes, are naked price fixing and market division. There is also sufficient experience in the economic literature on advertising restraints to treat them in a truncated fashion, and it would not surprise me if that issue finds its way into the courts again from the Federal Trade Commission.

On my second issue—the role of economics—I personally think the Chicago/Post-Chicago discussion is very stale. Although I would not use the word crisis yet, there is an increasing distance between industrial organization economics and its applications to antitrust, which may sound paradoxical given all the money that your clients pay for economists. The problem is that modern industrial organization economics has grown more theoretical and less factual.

If someone asked me to describe myself, I would say “new institutional economics,” not “Chicago” or “Post-Chicago.” The old institutional economics lacked theoretical underpinnings. The new institutional economics now has a formal organization that has been headed by Oliver Williamson, Ronald Coase, and Doug North—the last two are Nobel Prize Laureates. Paul Joskow has written an interesting article, to be published in the *Journal of Law, Economics and Organization*, about transaction cost eco-

nomics, which is a prominent part of this approach.

These economists combine theory with a study of real world institutions. The approach is heavily empirical, in contrast to much of recent industrial organization (IO), which is heavy on theory and light on testing. To start to correct the imbalance, I have asked Dennis Carlton to assemble a group of economists who will meet in the fall to discuss research agenda related to antitrust enforcement.

Unilateral effects are particularly revealing of the modern trend in IO, in part because you have economists talking to each other, with the lawyers paying almost no attention other than to the bottom line. Let me give three illustrations of lawyers ignoring this economic approach:

- Judge Hogan did not mention the extensive econometric work in his *Staples* opinion. In fact, he later said he regarded it as a wash.
- *Baby Food* may be an even stronger illustration. There was uncontroverted econometric evidence that the district court judge relied on—although, unfortunately for him, in his opinion he only made passing reference to it. This evidence showed that Heinz and Beech-Nut did not compete; their cross-elasticities were very low. I worked on the case, as some of you know, and I felt that there was other evidence to support that proposition. Although the evidence was uncontroverted—the FTC did not even present a rebuttal witness—it had no impact on the ultimate result.
- The third illustration comes from my personal experience. I have seen thousands of regressions searching for unilateral effects, many involving soft drinks. It is a rare regression that shows both Pepsi and Coke and Diet Pepsi and Diet Coke being strong competitors. One ought to have pause about any regressions that do not show those two propositions.

There are numerous other problems. One is the lack of a good natural experiment—some prod-

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ucts do not allow each other's prices to deviate from each other enough to test the impact of large price changes. Instead, they move closely with each other. One has a problem predicting what would happen with a 5 or 10 percent price change when the underlying data lack significant variability.

Another problem is that some results predict a price change when the variation around the price change includes zero. Most econometricians believe that a result is meaningless if it includes zero within a standard deviation. Finally, the underlying theories are quite restrictive, particularly the so-called Bertrand theory. Some economists state that the models "predict" a price increase. The truth is that many of these models "assume" a price increase.

Comments of Assistant Attorney General James

Last August, Tim, Deb Garza, and I had the occasion to participate in a program at the ABA Annual Meeting on "The Post-Clinton World of Antitrust." As we were sitting there, I never thought for one second that the post-Clinton world would be us. I now find myself in a "be careful what you say" kind of situation.

And then, in late 2000 Ky Ewing (the past Chair of the Section of Antitrust Law) appointed a task force to examine the goals and challenges of antitrust enforcement in the next Administration, and he appointed my former partner, Joe Sims, to head that task force. Joe and I had many discussions about how the antitrust world could be improved. And now I have that Task Force Report pointed at my own head. [<http://www.abanet.org/antitrust/reports2001.html>]

I thought I would take some time this morning to talk about four areas addressed by the Task Force Report. Tim already talked about two. I plan to discuss some of our reactions to these four sets of recommendations, as well as some of the things that the Antitrust Division is trying

to do in response to what was a very thoughtful effort by the Task Force.

One of the first things that the Task Force Report talked about was resources. The fact of the matter is that the legacy of the Bingaman and Klein years is that Congress likes antitrust enforcement and is prepared to support it with resources, provided that we get it from you in the form of Hart-Scott-Rodino filings. But in point of fact, the resource allocations to the agencies—at least to the Department of Justice—are very generous. The markups that are presently pending before the House and Senate provide us with a very good resource base, and hopefully, we will use it wisely.

The report suggests that we need a strong cadre of competent lawyers. One of the things that has happened in the Justice Department is that, by virtue of the very generous salaries many firms are providing to their associates, it is very difficult for us to recruit young lawyers into the antitrust agencies. And then when we do recruit them and they demonstrate any competence at all, you hire them. That leaves us in a situation where we have a constant inflow of young lawyers. We have a group of lawyers who have been there for quite some time, but our real challenge is recruiting and retaining trained, skilled, mid-level attorneys—and everyone knows that any army marches on the strength of its mid-level people.

In that regard, we are devoting a tremendous amount of time to our training efforts. For the very first time, we will have this year a training academy for our new lawyers. We also are encouraging our economists to participate more actively in the training of our lawyers.

One of the other things that we have observed is that the antitrust agencies are so interested in training people in economics and litigation techniques that we have lost a bit of our focus on providing training on some fundamental legal practices—legal research and writing. As a result, we are devoting a fair amount of our time and attention to providing

some basic legal skills training.

I hope that over a period of years at the Antitrust Division we can address our mid-level situation by having attorneys come to us from the private sector for two- and three-year terms. We think we can do a very good job of training your people because we can expose them to more antitrust than the typical law firm is able to, and I think there would be some mutual benefit to such a program. But it remains for us to work out the details of such an initiative.

We are also giving some considerable thought to our litigation capabilities. I asked our Criminal Deputy, Jim Griffin, to look into how much criminal litigation the Antitrust Division actually did over a period of years. Criminal program litigation is a lot more active than on the civil side. As it turns out, over a period of twelve or thirteen years, the Antitrust Division has tried only sixty criminal cases in total. This includes the period of the great school milk and road-building cases, when there was a perception that trials were pretty active.

We have to find ways to improve our litigation capabilities. Generally, I am not favorably disposed to hiring outside lawyers on a routine basis to handle and lead Division cases. However, in some instances we might experiment with hiring people to provide back-office support to our litigation teams.

The Task Force Report also emphasized the significance of international antitrust and multi-jurisdictional enforcement. As you know, your former leader and my former leader, Mr. James Rill, did a tremendous job of making the world aware of the importance of consultation and coordination among the world's competition agencies.

The GE/Honeywell case notwithstanding, we have a very, very positive bilateral relationship with the European Union and Commissioner Monti and Director Schaub. We are cooperating closely on a number of matters, and I hope that won't get lost in all of the fanfare about GE/Honeywell.

One of the things that I hope you have taken recent notice of is that the European Commission has announced changes to its corporate leniency program. We think it moves their program much closer to ours. Jim Griffin and Scott Hammond of our criminal section engaged in very active consultation with the European Commission on this issue, and it is an example of how our bilateral relationship actually improves convergence.

On the multilateral front, for quite some time we have been engaged in an active dialogue about convergence with other members of the international community. We all view convergence as this fond goal that we hope to achieve somewhere down the road. I think it is about time for us to stop talking about convergence and start converging. To that end, working closely with the Federal Trade Commission, the European Union, Canada and other countries that are vitally interested in this issue, we hope to make some progress along those lines.

The International Competition Network (ICN) is something that is discussed in the Task Force's report. The ICN is not to be confused with the Global Competition Forum, the OECD, or any other organization. It is an effort that we are busily working on and conceptualizing with our counterparts in other governments.

To my way of thinking, we do not need another international debating society. We have plenty of excuses to have French food, and probably do not need another one. What we do need is an appropriate forum or network for government-to-government consultations directed at talking constructively about ways in which we can bring about procedural and substantive convergence. My vision for the ICN is that it be a very project-centered, government-to-government kind of enterprise. When I say "project-centered," I mean something that is not attached to a permanent bureaucracy, but is instead an effort that is focused on a group of projects with timetables and deadlines, has reporting responsibility and task lists, and has

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specific work plans for accomplishing those tasks. The enterprise can then develop reports or findings that can be discussed on a multinational basis with a view toward reaching consensus and achieving implementation through bilateral or multilateral kinds of consultations among governments.

It is important that the ICN institute an appropriate mechanism for private input, but I do not think that private input should come at the cost of having private entities support the ICN financially or participate as equal partners with the government effort. We hope that the private sector would have a very important advisory function in the ICN. But we do not want to create a situation that might diminish the credibility of any government-to-government consultations. We do not want to be perceived as something that is advancing a private agenda—as distinguished from a government agenda—and we do not want to be perceived as setting up a new permanent bureaucracy, because we already have quite a few of those.

Turning now to another important area, the Task Force Report notes the “tension between antitrust law and intellectual property.” That tension is not new, and has existed for quite some time. The fact of the matter is that the significance of the tension has grown, and it has grown, in part, because of the scope and range of intellectual property interests that are now being asserted, because of the importance of intellectual property in many of the New Economy industries, and, quite frankly, because of the very aggressive strategies that companies are employing to extend their intellectual property protections.

Both agencies have had cases in this area, but the Federal Trade Commission deserves some particular credit for its work in the pharmaceutical industry. I think both agencies recognize, however, that we need to expand our knowledge base in this area.

Tim and I have had some substantial discussions about how we might improve our

knowledge base and our understanding of the balancing of antitrust and intellectual property interests. I think this will be an area in which the agencies will be very active, perhaps following upon some of the very fine work that the Pitofsky Commission did in terms of forums and hearings, and bringing the Commerce Department and other government agencies, such as the Patent and Trademark Office, into the debate.

I think it is also an area where the agencies can engage in a fair amount of competition advocacy with the PTO, certain international organizations, and other U.S. regulatory agencies that are involved in licensing and permitting regimes. Hopefully, over a period of time, we will make some progress in increasing understanding in this area.

Last but not least, the Task Force Report addresses the merger process situation. The Division has some ideas that have the potential to improve the process. Of course, that depends upon whether the private bar takes us up on this initiative. We also plan to work with the FTC to identify best practices in the area of second requests and other investigative matters, and hope to achieve progress in this area as well.

The report takes on the subject of clearance, and, quite frankly, our efforts in the merger process area are not going to lead to improvements until we fix the clearance situation. If we are fighting about clearance, then we are not using all of the time under the first thirty days of the Hart-Scott-Rodino process as effectively as we can.

Tim and I have had some discussions about this issue since assuming our respective positions, and we were surprised to find a substantial backlog of fairly contentious clearances. I am proud of the fact that Tim and I were able to resolve these outstanding issues quickly, and I think we are now current on clearances.

We have started to review certain areas of our respective commodity allocations that have become fuzzy over time, and will try to reach

some new accommodations that will improve the process. We are counting on our friendship to help us improve the clearance process and on the clearance process not destroying our friendship. If those two things can occur, that will be a victory as well.

Questions and Answers

Question: *Charles, you spoke about your vision of the role of your agency in the Global Competition Initiative (GCI). Some feel a sense of momentum slide with the GCI over the last six months, and it is probably perfectly understandable.*

You raise some questions. One is the issue of no bureaucracy, and we have heard that from a number of places. The question that arises for me out of that is whether the U.S. agencies and/or the European agencies are going to be prepared to devote some resources themselves, because it does occur to me that to move things forward, actual focused effort needs to be put in place.

I guess the other two subsets of my question are: (1) If there is a momentum issue, have you got a sense of the United States's timing on moving this forward? and (2) With respect to private interests having a role, an advisory-but-not-equal role, are you able at this stage to describe a bit what you think the nature of that advisory role might be for private interests?

James: Tim and I went through a momentum-killing process called Senate confirmation, but I think you will see the momentum increasing now that we are both in place. Tim and I have had quite a few discussions with each other and with our counterparts in other agencies over the last several weeks. I cannot say whether the momentum behind the ICN has reached its former pace, but I think it is moving along at a good speed.

Our intention is that the ICN be launched sometime in the Spring of 2002. The agencies

are prepared to devote resources to this effort, but we think that our resources will not be the only ones that will be deployed. As we contemplate a project-oriented kind of process, we think that the project itself has the potential to dictate the types of resources that are required to execute the project. I envision that at the beginning of a ICN period, whether we call that a year or eighteen months or some other period, the governments would set an agenda of projects that they want to have concluded over a period of time.

In framing the project there would be a work plan. The work plan would dictate certain resource commitments and, depending upon the nature of the project, would involve various types of input, including input from the private sector, government agencies, academia, the business community, and perhaps other organizations.

In terms of considering how the projects were framed, I have always thought that it would be useful to have a business advisory group that would consult with the governments. Obviously, the United States is not in a position to dictate such a vision of the ICN, and so we expect to have consultations in connection with a series of upcoming multinational events and to have a proposed structure for the ICN by the end of the year. If that structure is in place, we can move forward towards a launch in the Spring of 2002.

Muris: I agree that GCI is a useful initiative. Charles's vision is highly useful here. After privacy and non-merger case generation, I am spending more time on international activities than anything else. It is extremely important, and I hope we can make progress.

Question: *I have a comment on the remarks about GCI, and then I have a question, primarily for Tim, about the look-see that Dennis Carlton is going to take into the economic foundations of antitrust policy. Believe it or not, the*

two have a common theme, and the common theme is credible expertise.

There has been a lot of discussion in the context of the GCI of whether the GCI would be totally controlled by the government, steered by the government, and whether private participation would be advisory. I think it is a dreadful mistake if this debate about the composition and control of GCI were a debate about government control versus private control. That is not really the issue. The real issue I think is credible expertise.

You find demands for new institutional frameworks in areas where the need for convergence is most prime—for example, in the merger process, which is a problem that has been around for a long time. There are a lot of government-to-government institutions, such as the OECD, that have made stabs at that problem. There are common forum attempts, there are various attempts to harmonize bilateral treaties, and yet the problem persists. What gives rise to demands for a new institution is that occasionally you find hints sneaking through the dialogue, coming out of the existing government institutions, that the message that the lack of convergence imposes very significant burdens on the private sector is still not received.

We are all looking for models for how convergence can be achieved. I think there is consensus that there is a need for convergence. But the models that seem to have worked in the past are not necessarily models based strictly on all-government activity. I think ultimately, because of the nature of merger process review, you have to have statutory reform, regulatory reform. It has to be acceptable to the governments involved. But what gives rise to the basis for government acceptance of a common approach to a complex multi-jurisdictional problem is the application of credible expertise to the problem itself.

It is less a question of government versus private. The question is: what is the best institutional format for getting the best solution?

This relates to the question I have for Tim about the effort to organize some economic thinking about the policy basis for antitrust. This past Monday morning, the ABA Antitrust Section had a session in Chicago involving some very distinguished practitioners, judges, and others. Interestingly, although this group had a fairly broad and deep consensus that antitrust, at least U.S. antitrust, is now about the application of economic analysis to business conduct, one of the major areas of disagreement was what has been the effect of this trend on the economic profession itself. Specifically, the theme was sounded that because antitrust economists are now consultants—they are not litigators, but they are basically at the elbow of the litigators—is the economics profession still available to the antitrust policy world as a source of mutual first-rate objective expertise?

And so the question to you, Tim, is: Have you thought about this issue? Have you thought about how Dennis Carlton is going to organize an effort so that the output, again, appears to be and is the output of people with credible expertise?

Muris: That is an extremely good question. We have asked Dennis to assemble colleagues from the academic world—most of whom also do consulting—to discuss a structured agenda about possible research. I hope, probably more optimistically than I should, that we will have some influence on the academic research agenda, as well as on our own.

Question: I have a question for both of you and it relates to what Tim was talking about—Mass. Board and truncated analysis. In the last administration, we saw a theme that was not only in the horizontal restraints area but also extended to Section 2 analysis. Basically, if there was a restrictive effect of some sort in the activities of a horizontal group or of a monopolist, the initial inquiry was whether there was an efficiency justification of some type that jus-

tified that restrictive effect. If you didn't get over that hurdle, you didn't go on to, for example, market power in the case of horizontal restraints or how much of an exclusionary effect there had been in a Section 2 context. So a tremendous amount of the burden of the analysis was on whether you have the efficiency to justify that level of restraint caused by your conduct. In contrast, certainly in the horizontal restraints area, there is another way of looking at it that says you start with market power, and if there is not a market power issue, then, except for naked restraints, you do not worry about it and nobody has to justify anything.

I would be interested in your views of how you view that relationship between justification and the exclusionary effect in both the Section 2 and horizontal restraint contexts.

James: It is very important to separate out the Section 2 world from the Section 1 world in that respect. One of my partners, Joe Sims, coined the “Can we help you?” school of antitrust enforcement” phrase to talk about situations where agencies looked at a single firm’s situation, looked at the restrictive activities the firm might have engaged in, and then concluded, “If there is not a good economic justification for that, then that must be a Section 2 problem.” I think that, doctrinally, settled law does not permit one to make that intellectual leap and impose a duty on a single firm—regardless of its market power—to help or facilitate the activities of its rivals.

In the Section 1 context, however, I think that is a part of the law that is important. From a government enforcement standpoint, we should not become entangled with cases that do not involve market power and economic harm. I think that the structural framework of the analysis that you described has a lot of support in the case law, and I hope our enforcement activities in the Section 1 area will be very consistent with the case law, and that we will bring relevant cases.

Muris: I agree with what Charles just said. Moreover, it is important to understand where truncation was born. It was in *BMI*, which attempted to avoid rigid categorization. In effect, *BMI* allowed a justification for what many thought was an illegal restraint.

It was predictable—and, indeed, I predicted it when we derived *Mass. Board*—that the staff would try to categorize as much as possible to shift the burden to the parties. Nevertheless, under current law, categorization is inevitable. If we live in a world where you have to categorize, then we should categorize in the most sensible way possible. My impression in reading the “step-wise” discussion is that it did not answer the question of when you truncate. I did not have enough experience with the Justice Department to know whether they were engaged in more burden shifting than was sensible.

As Charles said, we should distinguish the Section 2 case with a monopolist from the Section 1 context. I hope we are sensitive to that issue and that we advance the law in the next few years.

Question: *In the Section 2 context, a particular high point of this theory was Jonathan Baker’s article of a couple of years ago, saying it was just a mode of monopolization analysis—if a monopolist does something that is restrictive, it essentially has to be justified. Do you agree with that in general or is there some threshold quantum of restrictiveness that has to be applied before even a monopolist has to justify what it is doing?*

Muris: Yes. I have written that I disagreed with that approach. Evidence of harm to consumers is necessary, although it need not be quantitative or direct. If a monopolist is going to use an exclusive, however, I am sure that you will counsel it to have good arguments on its behalf. Moreover, post-*Microsoft*, we are not going to find e-mails, at least if you are counseling them, like we found in that case.

Question: *I would like to take the two halves of what you started with, Tim, and sort of show how they meet in relation to what was just said, which is this: When he was on the First Circuit, then-Judge Breyer said, "Economics informs antitrust law, but it is still law." It has to be a system that guides economic actors and we need predictability and we sometimes need simple rules. Yet those of us who have been in the enforcement agencies know that sometimes enforcement decisions are based on exceedingly complex economic models and analyses; they are rarely based on things that actors could predict ex ante.*

To what extent do you think it is appropriate for antitrust enforcement agencies to base their enforcement decisions on different rules than the law provides? A specific example of this might be the truncation issue, where one might say is it perfectly appropriate for an enforcement agency to have its views on how it can properly apply economic analysis, even if the legal standards that a court would apply in a different system in an enforcement process might be very different?

Muris: Again, this is an extremely good and complicated question. To begin to answer, let me raise two points. Charles spoke directly to the first, namely that resource allocation is an important issue, and the government ought to bring cases that will have an impact. Of course, there can be a case when you think the statement of the law itself is important beyond the facts of the case. The second point involves the courts. With mergers, for example, we rarely go to court, and the FTC, in particular, has been extraordinarily difficult to beat in court, outside of hospital mergers.

I am personally uncomfortable with pushing hard on theories that do not have a firm foundation in the law. I also think that the law has a firm foundation in solid economics. Pushed to the extreme, this reasoning could become circular. Particularly in the application of a specific

ic case, people can disagree about how the economics comes out.

James: I think the very first level of inquiry that we go through in the Antitrust Division is whether there is economic harm. Fortunately, in most instances involving true economic harm there is a legal doctrine that will allow us to challenge things. Like Tim, I am very uncomfortable with the view that there are theories that you can pursue for enforcement decision-making purposes that are distinct from the frameworks that exist in the law. I think when you hear that argument, you usually do not hear it before the case is brought. Rather, you hear the case and the whining about why the case was lost. Hopefully, we are not going to do very much whining at the Department while I am there.

Question: *Tim, you have outlined the differences between these two schools of thought on economic thinking and your perspective on each of them. Do you plan to shift the focus of economic analysis at the FTC in the direction of the so-called "institutional economics" that you seem to favor while the research is being undertaken by Dennis's group? And, as a follow-up to that, what are the implications of that, and what kind of economic analysis do you want to see parties presenting to the Commission; what are the types of analysis that perhaps have not been presented recently or are not being presented that you think are more meaningful?*

Muris: Dennis's group is not going to conduct research for us. There are lots of topics for which research would be useful, however. As I mentioned, we will take a hard look at the unilateral effects area, at a minimum to try to make it more relevant. For example, we are considering cases where mergers were approved; where we have models premerger with predictions of what would happen. Such retrospective studies are very useful, and many minds have been changed based on retrospective studies.

I am surprised that more people do not use trade associations to present relevant evidence to us outside of the context of individual cases. There are many, many empirical questions for which better evidence would improve the way we do business. With many trade associations, of course, the members might not agree enough to present evidence on a general issue. ●