

The Elusive Goal of Convergence and The Inevitability of Uncertainty

Thomas B. Leary

One year ago, the European Commission's Directorate-General for Competition published a Discussion Paper on the application of Article 82 to exclusionary practices.¹ The Discussion Paper reflects a significant movement away from formalism and toward a greater reliance on the analysis of economic effects, and it has stimulated extensive discussion and detailed commentary.² This commentary is generally appreciative and respectful in tone but—like most commentary—it does tend to focus more on apparent differences than on similarities, and it is rather obvious that the U.S. commentators still think we do things better over here. There is a pervasive suggestion that the economic approach in the United States is more rigorous and better able to discriminate between pro-consumer and anti-consumer outcomes. Maybe so, but some humility is in order.

This article will not offer a point-by-point examination of current U.S. commentary on the EU's Discussion Paper. The article will simply suggest that antitrust analysis in the United States is still evolving; that it is inherently less rigorous and discriminating than many care to admit; and that, in any event, even common agreement by the United States and the European Union on principles or on actual language will not necessarily lead to common outcomes in any particular case. Counselors for global companies will therefore always have to deal with some uncertainty, and this kind of uncertainty is not unlike uncertainties they have faced in the past, even within a single jurisdiction.

At the outset, it is important to acknowledge that so-called Chicago School economics still dominates antitrust analysis in the United States. People tend to forget what the antitrust world was like roughly 30 years ago, when what was then called "The New Learning" first became widely known outside the academy.³ The idea that antitrust policy should be driven by the economics of consumer welfare was considered heretical by many commentators. Similarly shocking were the ideas that company size could be associated with desirable efficiencies rather than pernicious "competitive advantage," that the intensity of competition is not necessarily correlated inversely with levels of concentration, and that vertical restrictions could be proconsumer.⁴

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¹ DG Competition Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses (Dec. 2005), available at <http://ec.europa.eu/comm/competition/antitrust/others/discpaper2005.pdf>.

² See, e.g., Joint Comments of the ABA Section of Antitrust Law and Section of International Law on the Commission Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses (June 8, 2006), available at <http://www.abanet.org/antitrust/at-comments/2006/06-06/com-article-82.pdf>; Comments of the International Bar Association Antitrust Committee Working Group on Article 82 Enforcement on the DG Competition Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses (June 2006), available at <http://www.ibanet.org/images/downloads/IBA%2082%20final%20.pdf>.

³ The publication of INDUSTRIAL CONCENTRATION: THE NEW LEARNING (Harvey J. Goldschmid et al. eds., 1974), introduced these ideas to the broader legal community.

⁴ See, e.g., William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 71 ANTITRUST L.J. 377 (2003).

All of these once revolutionary ideas are now accepted by virtually all antitrust commentators. The big battle is over, and “[w]e play the antitrust game between the forty-yard lines today.”⁵ But the game does go on, in the United States and around the world. Even though there may be common agreement on methodology, there still can be serious disagreement about the appropriate disposition of individual cases. The persistence of these differences, despite common agreement on methods, is something that judges and agency heads need to understand and that corporate counselors need to deal with every day. It is important for domestic and international bar groups to promote harmony between the approaches in the United States and the approaches in other jurisdictions, but it is also important to have realistic expectations.

People think in pictures, and therefore it may be helpful to illustrate the intellectual evolution of antitrust in this country by recalling the works of three famous 20th century painters. Before the mid-1970s, a lot of business practices were simply declared per se illegal because no one seemed able to articulate a procompetitive explanation. Outside the per se area, the rule of reason analysis lacked coherent structure. Myriad economic and social factors could be received into the record, without any guidance on how they should be weighed.⁶ The finder of fact was somehow supposed to balance the factors in this formless mess. It was rather like the search for a pattern in a painting by Jackson Pollock.

Then came the “New Learning” or “Chicago” revolution. The arguments were compelling and elegant, and it seemed like there was at last a rigorous way to separate procompetitive and anti-competitive behavior. As Robert Bork explained in his famous treatise, a finder of fact must make a binary determination whether particular conduct was explained by “the desire to drive out rivals by improper tactics (which is unlikely) or the desire to create efficiency.”⁷ This clear articulation, combined with a structured approach to rule of reason analysis,⁸ gave rise to an expectation that it would be possible to distinguish clearly between conduct that is inside the lines or outside. Rather like a painting by Piet Mondrian.

Today, we recognize that things are sometimes not quite so easy. (The problem was not that Chicago theorists promised too much, but rather that we practitioners may have expected too much.) It is true that, in addition to the traditional category of offenses that are per se illegal, there is a recognized category of business practices that are, in effect, per se legal. Antitrust counselors can clear many practices today that once were suspect, and judges or agency heads seldom have to deal with them. The effects of other practices may be genuinely ambiguous, however, and Chicago economics does not always provide a rigorous way to draw the line. In other words there are broad areas of bright clarity with some fuzziness at the edges. Like a painting by Mark Rothko.

This article will explain, first, why we are living in a Rothko world and why there really is no way out of it.

⁵ Thomas B. Leary, *The Bipartisan Legacy*, 80 TUL. L. REV. 605, 606 (2005).

⁶ See, e.g., *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962); ROBERT H. BORK, *THE ANTITRUST PARADOX* 201 (1978) (discussing the “nine major ideas” that once underlay merger-law enforcement).

⁷ See BORK, *supra* note 6, at 171; see also *id.* at 138.

⁸ See, e.g., *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210 (D.C. Cir. 1986) (preliminary screen to test for the existence of market power).

The Chicago revolution substituted a single lodestar, namely the economic welfare of consumers, for the diffused populist objectives that had previously informed antitrust policy, and it supplied an analytical framework for determining these welfare effects. But this did not mean that cases would necessarily be easier to decide or to handicap. Quite the contrary.

Persistent Sources of Uncertainty

The Chicago revolution substituted a single lodestar, namely the economic welfare of consumers, for the diffused populist objectives that had previously informed antitrust policy, and it supplied an analytical framework for determining these welfare effects. But this did not mean that cases would necessarily be easier to decide or to handicap. Quite the contrary. To the extent that Chicago theorists questioned the inverse correlation between industry concentration and competitive vigor, or supplied likely efficiency justifications for restraints that had previously been deemed per se illegal, the outcome of individual cases may actually have become less predictable. The impact of this uncertainty on corporate counseling will be addressed later; the point here is that common agreement on the appropriate logical approach by various antitrust tribunals does not necessarily mean that there will be agreement on the ultimate outcome. To use a crude analogy, even if the appropriate algebraic equations were universally accepted, different experts might still plug in different numbers.

The Need to Make Predictions. The first and probably most compelling reason for this state of uncertainty is that virtually all antitrust analysis involves predictions. This is obviously true when it is necessary to evaluate the future competitive effects of a pre-notified merger or of a competitive strategy that has just been announced. Predictions are also required, however, when analyzing the competitive effects of past conduct. In this case, of course, there will be evidence of what has already happened in the market place, but it is still necessary to weigh this outcome against a prediction of what would have occurred in an alternative universe without the conduct. There simply is no rigorous way to make predictions about matters that depend so much on human behavior. Economics is not Newtonian physics.

The economics profession has, of course, developed ever more sophisticated measurements and models to help people make predictions. These models can provide directional signals, but anyone with experience in the business world knows that the most sophisticated models cannot replicate the complexity of a competitive marketplace, or even a single organization in the marketplace. Companies are not going to replace CEOs with supercomputers any time soon, and antitrust enforcers or counselors cannot rely on supercomputers either.

Factors that Are Hard to Quantify. The difficulty of making predictions is compounded by the fact that matters of competitive significance often cannot be readily characterized or quantified. For example, antitrust law draws sharp distinctions between unilateral and concerted conduct—and properly so—but it is not always easy to draw the line. In addition, only a relatively small and shrinking segment of U.S. industry deals with fungible products, where comparative prices and output can be fully expressed in numerical terms. A larger and growing segment of U.S. industry deals with combinations of differentiated products, services, and experiences, where comparative prices and outputs cannot be readily captured by statistics.

One short opinion that illustrates both problems was written by one of the most eloquent spokesmen for Chicago economics on the federal bench, in *Chicago Professional Sports Ltd. Partnership v. NBA*.⁹ This landmark case involved an antitrust challenge to a league rule that would limit the number of basketball games that TV “superstations” may carry. Judge Easterbrook stripped the case down to two dispositive issues. First, was the league acting as a “single entity” when it established the rule, and hence immune under *Copperweld*?¹⁰ A second critical issue was

⁹ 961 F.2d 667 (7th Cir. 1992) (Easterbrook, J.).

¹⁰ *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984).

whether the limitation on the *number* of games on these TV stations could be said to “reduce output.”

On the characterization issue, the court deferred to the district court’s conclusion that the league was acting more like a joint venture than a single entity, but acknowledged that “[c]haracterization is a creative rather than exact endeavor.”¹¹ In a later opinion in the same case,¹² Judge Easterbrook reiterated that this is a “tough question,” and went on to say that the league might be considered a single entity in some contexts and a joint venture in others.

The “output” issue was similarly ambiguous. How do you quantify the “output” of those enterprises that provide consumers with the experience of viewing a basketball game, both live and on TV? The first Easterbrook opinion in *Chicago Professional Sports* cited Supreme Court precedent for measuring output by the number of games that the league rule permitted to be broadcast. But the opinion also implicitly acknowledged that it would not necessarily be inappropriate to adopt other measures of output, such as the total number of people who will enjoy the experience, either live or on TV, or perhaps the effect on overall revenues.¹³ In fact, the enhanced revenues may indicate that various league rules, designed to benefit the weaker teams, have resulted in closer and more exciting contests, which consumers and advertisers deem a superior experience—and hence could be said to increase “output.” Again, however, dedicated supporters of Chicago economics can arrive at different conclusions.¹⁴

Consider also the example, already cited,¹⁵ of an initial market power test to provide structure for the rule of reason analysis. In many, probably most, cases it is easy to decide that a defendant accused of a restrictive practice does not have market power if it has a relatively low market share. But, in order to determine the market share, it is necessary to say what the “market” is, and this can be a complex and controversial task. The economic test for market definition that is set out in the U.S. Horizontal Merger Guidelines requires a prediction of whether a hypothetical monopolist in the product and geographic space under consideration could profitably impose a “small but significant and nontransitory increase in price”—the so-called SSNIP test,¹⁶ over which serious battles have been fought in the international arena. It probably is the best test currently available, but still involves estimates and predictions. Reasonable Chicago-trained minds can therefore arrive at different conclusions.

The Attempt to Quantify Efficiencies. The same problems arise when it comes to measuring the impact of a transaction on efficiencies. A primary contribution of the Chicago revolution was the recognition that efficiencies are important. This is something that is relatively easy to describe, or even illustrate with examples, but actual measurement can be a complex and controversial exercise. The most important sources of efficiency may not be the savings associated with greater scale and scope, but rather intangible improvements in the morale of an organization that are difficult to quantify and impossible to model. Thus, hard as it is to quantify efficiencies, it is much

¹¹ *Chicago Professional Sports*, 961 F.2d at 672.

¹² *Chicago Prof’l Sports Ltd. P’ship v. NBA*, 95 F.3d 593, 599–600 (7th Cir. 1996).

¹³ See *Chicago Professional Sports*, 961 F.2d at 673–74.

¹⁴ For a discussion of similar complexities, see Thomas B. Leary, *The Significance of Variety in Antitrust Analysis*, 68 ANTITRUST L.J. 1007 (2001).

¹⁵ See *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210 (D.C. Cir. 1986).

¹⁶ U.S. Dep’t of Justice & Federal Trade Comm’n, Horizontal Merger Guidelines § 1.0 (1992, revised 1997), available at <http://www.ftc.gov/bc/docs/horizmer.htm>.

much harder to predict that efficiencies will actually be realized. A lot of carefully planned mergers and business strategies fail.

Consider the common example of efficiencies associated with extensive local sales efforts, which provide consumers with amenities like convenient locations, pleasant showrooms with a wide variety of choices, and a knowledgeable sales force. These amenities are expensive, and retailers that provide them are vulnerable to “free riding” by discount retailers that can close the sale once consumers have been educated about their choices in comfortable surroundings elsewhere. Identification of the role that vertical restrictions play in the containment of free-riding has been a major contribution of Chicago theory, and it is now almost universally recognized that these restrictions should be judged under the rule of reason. This victory alone will not eliminate all controversy, however, because it would be extraordinarily difficult actually to balance any adverse effects of the restriction against any adverse effects of the free-riding,¹⁷ and most courts do not even try. Market power screens—or simple assertions that intermodal competition is more important than intramodal competition—are commonly applied instead, but the results can still be indeterminate if the market power issue is not clear-cut or the risks of free riding do not appear substantial.

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The Elusive Goal of Convergence. What all this means is that even a common agreement on the analytic principles of Chicago economics will not ensure that the antitrust authorities in the United States and the European Commission will take the same bottom-line view in any particular situation. In fact, the authorities could issue a joint set of guidelines that conformed word-for-word, and still draw different ultimate conclusions. In addition to the issues outlined above, one obvious reason is that competitive effects may be different in different jurisdictions.¹⁸ This observation is not intended to denigrate the efforts of the commentators who seek to close perceived gaps between competition law principles applied in the United States and those applied in the European Union. The message simply is that we should not expect too much too soon. Convergence is a laudable goal but will always remain elusive.

Consider just one illustrative example. The International Bar Association’s comments on the Directorate General’s Discussion Paper on Article 82 recommend specific language to make it clear that the conduct of both dominant and non-dominant companies should not be deemed abusive if it “is likely to produce (‘pro-competitive’) consumer welfare enhancing effects that outweigh any (‘anti-competitive’) market distorting effects.”¹⁹ Assume this recommendation were implemented verbatim. There may be near-universal agreement on how to strike the balance in some cases but, for the reasons stated, there will be other cases in which even the most dedicated Chicago economists would disagree.

Identical outcomes are not assured with identical words, even at the government agencies’ level, and possible outcomes are even more variable when the vagaries of private litigation in the United States—and, perhaps, someday in the European Union—are taken into account. This is a big issue, worthy of extended treatment itself, and something that no corporate counselor can ignore. The risk of private litigation before potentially hostile juries means that corporate coun-

¹⁷ See, e.g., *New York v. Anheuser Busch, Inc.*, 811 F. Supp. 848, 872 (E.D.N.Y. 1993) (“the weighing required by the rule of reason is extremely awkward to apply”).

¹⁸ It is also important to remember that for most people in the European Union, the hypothetical joint guidelines would be written in a foreign language, with unfamiliar or varied overtones.

¹⁹ Comments of the International Bar Association, *supra* note 2, § 4.2.4.

selors in the United States have never been able to rely solely on the standards for decisions outlined in U.S. federal cases and the pronouncements of U.S. federal enforcers. They have had to accommodate uncertainty for a long time.

Some Practical Approaches to Uncertainty

A little history may be instructive. In the early 1980s, the Chicago approach was still highly controversial, the federal agencies were out in front of some courts, and academic opinion was still divided. Some believed that the evolving standards complicated the job of corporate antitrust advisors. I then expressed a contrary view:

Some have complained that rapid evolution, with a possibility of reverter, leads to unpredictability and inhibits antitrust compliance. This is true only if a client is determined to walk close to the cliff edge. The conservative advice of a decade ago is still valid today; in fact, the chances of an antitrust attack against long-standing business practices are considerably reduced. It is therefore easier than ever before for a lawyer to say “yes”; it may sometimes be more difficult to say “no.” This is so, of course, because the “rule of reason” had replaced flat *per se* prohibitions in a number of areas.²⁰

The situation today is in many ways similar. Despite some apparent differences between the approaches of U.S. and EU competition authorities, there obviously has been movement toward greater convergence. The recent Discussion Paper on the application of Article 82 to exclusionary abuses is an extraordinarily ambitious attempt to restate the law in this broad area. There are some comments that observers on this side of the water may think are inconsistent or at variance with EU authority, but that is not unusual when agencies are attempting to find their way in a changing environment. For a domestic example, compare the way that concentration has been discussed in successive iterations of the U.S. Merger Guidelines, and consider the still lingering inconsistency in the latest version—which refers to a market share “presumption” in Section 1.51(c) but goes on to state in Section 2.0 that concentration data provide “only the starting point” for the analysis.²¹ (Experienced counselors in the U.S. understand that the latter statement is more likely to be operative, unless concentration levels will be very high.)

Perhaps the most significant thing about the Discussion Paper is its extensive reliance on economic reasoning of a kind that is familiar to practitioners in the United States. The paper does not widen gaps, it narrows them. Counselors who advise multinational clients can survive in this evolving environment just as they did in the comparable environment that existed in the United States some 20 years ago. Now, as then, counselors need to be realistic, flexible, and creative.

Those who are not responsible for day-to-day antitrust advice may not appreciate that corporate counselors frequently have to provide a fast response. Assessment of the legal risks involved in aggressive pricing programs, vertical restraints, or even pursuit of an acquisition opportunity usually cannot await a full file search, canvass of customers, and economic analysis of the possible competitive effects. To the extent that these matters are governed by the rule of reason—which is what Chicago analysis is mostly all about—counselors and their clients have to manage uncertainty.

Consider, for example, the factors that the American Bar Association commentary would include in a definition of “substantial market power” or “dominance”:

²⁰ Thomas B. Leary, *Antitrust Planning in an Era of Uncertainty*, CCH Business Strategies ¶ 2450, at 15,201 (1984).

²¹ For a review of this evolution, see Thomas B. Leary, *The Essential Stability of Merger Policy in the United States*, 70 ANTITRUST L.J. 105, 114–21 (2002).

Many factors in addition to market share may bear on a finding of substantial market power. These include product heterogeneity, entry barriers, the importance and pace of technological innovation, the ability of one competitor to overtake another rapidly through innovation, customer characteristics (sophistication, ability to elicit new supply, etc.) relevant to customer ability to evade or defeat attempted exercises of market power by suppliers, and existence of downstream competition. Some of these factors are identified in paragraph 28 of the Discussion Paper, but the discussion here could usefully be expanded and made more comprehensive.²²

This list may be unassailable in principle, but clients in a hurry are not likely to find it particularly helpful.

In these circumstances, it is useful—indeed, imperative—for counselors to advise clients on the hierarchy of antitrust risks. This advice requires both a deep understanding of the client's business objectives and the courage to suggest alternative strategies that may carry less antitrust risk. There are many examples of this hierarchy. Joint ventures are usually safer than mergers, and long-term contracts are usually safer than joint ventures. Contracts that specify minimum quantities are safer than exclusive dealing arrangements. Incentive discounts based on relative increases in volume purchased are safer than discounts based on total volume, and volume discounts generally are safer than "loyalty" discounts based on the percentage share of the buyer's purchases. In general, strategies that depend on the "pull through" of customer demand through creation of better value are safer than strategies that depend on a "push through" from dealers. Terminations with a soft landing are safer than terminations that are abrupt. The most practical test to apply up front may be to determine whether the proposed strategy seems primarily designed to do something "for" customers or primarily designed to do something "to" a competitor or a maverick dealer. All of these things are true in the United States as well as in the European Union because—regardless of what the cases hold or the antitrust authorities say—the risks of expensive litigation cannot be ignored.

When alternative strategies are subject to the rule of reason, the decision whether various antitrust risks are tolerable is one for business managers. The lawyers' job is to identify and quantify the relative risks, as best they can, including the likelihood of litigation as well as the likelihood of ultimate victory. This is called creative counseling. In addition to purely legal risks, many prudent managers will also weigh the possible adverse political or public relations consequences of particularly aggressive competitive policies. For them, these political and social facts may have real economic consequences, and less restrictive options may be appealing.

Business managements' caution and willingness to consider alternatives may help to explain why some longstanding anomalies in U.S. antitrust law continue to exist. For example, antitrust commentators almost unanimously disfavor the Robinson-Patman Act in its entirety. But even those businesses most directly affected have never been willing to exert the effort needed to effect a repeal or significant modification of the Act. The matter is simply not all that important for them because they have found practical ways to live with the law, just as they have found practical ways to accommodate uncertainties.

Nervous counselors can draw comfort from the fact that many managers prefer to operate in the broad color fields of the Rothko world, rather than in the fuzzy boundaries. For them, subtle differences between outcomes in the United States and the European Union are less likely to be matters of great concern. ●

²² See Comments of the ABA, *supra* note 2, at 5.