



Fordham Competition Law Institute

45TH ANNUAL CONFERENCE ON INTERNATIONAL ANTITRUST LAW AND POLICY

Day 1: 6 September 2018 | 9:15 a.m.-4:40 p.m.
reception immediately following

CLE Course Materials & Speaker Biographies

Fordham Law School
Skadden Conference Center | 150 West 62nd Street
New York City



FORDHAM UNIVERSITY
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Reiko Aoki
Commissioner, Japan Fair Trade Commission

Reiko Aoki is Commissioner of Japan Fair Trade Commission and formerly Executive Vice-President (International, IP and Gender Equality) at Kyushu University. She has conducted research and published on economics of patents, patent pools, standards, innovation and intergenerational political economy in academic journals such as *Journal of Economics, Management and Strategy* and *American Economic Review*. She has been Principle Investigator for research projects funded by Japan Science and Technology Agency and by Japanese Society for Promotion of Science, and Research Institute of Economics, Trade and Industry where she was a Faculty Fellow. She has been actively involved in science, technology and innovation policy as Executive Member of Council for Science and Technology Policy, Japanese Cabinet Office 2009-2014. Previous appointments include Member of Science Council of Japan, Member of Industrial Structure Council (METI), Intellectual Property Committee (JPO), its Patent System Subcommittee and its Expert Working Group, and Information and Communications Council (Ministry of Internal Affairs and Communication) and its subcommittees. She received her Bachelor of Science (Mathematics) from University of Tokyo, Master of Arts (Public Policy) from University of Tsukuba, Master of Science (Statistics) and PhD (Economics) from Stanford University. She has held positions at the Ohio State University, SUNY Stony Brook, University of Auckland and Hitotsubashi University.

Jeffrey C. Bank
Partner, Wilson Sonsini Goodrich & Rosati

Jeff Bank is a partner in Wilson Sonsini Goodrich & Rosati's New York office, where he practices antitrust litigation and counseling, particularly in the pharmaceutical industry.

As an experienced litigator representing both plaintiffs and defendants, Jeff's work has ranged from complex multi-district litigations and global cartel cases to actions against competitors. He has successfully defended pharmaceutical, technology, and media companies against class actions, and has experience in all aspects of litigation, from discovery through appeal.

Prior to joining the firm, Jeff practiced at the Federal Trade Commission's Health Care Division, where he focused on competition issues in the pharmaceutical

and healthcare industry. In his current practice, he regularly counsels clients on merger clearance issues and business practices, and he has represented a diverse range of clients before the FTC, including companies from the medical device, pharmaceutical, and media sectors.

Jeff also serves as the pro bono coordinator for the New York office, and he has worked on numerous immigration and asylum-related matters. He was awarded the John Wilson Award, which is presented annually to individual attorneys who have demonstrated a significant commitment to the firm's pro bono clients. Additionally, Jeff currently serves as board president for Spoons Across America, a New York-based nonprofit.

Jeff received his J.D. from Cornell University Law School.

Jean-Francois Bellis
Managing Partner, Van Bael & Bellis

Jean-François Bellis is a founding partner of Van Bael & Bellis. Before setting up the firm in 1986, he clerked for Lord Mackenzie Stuart, the British judge at the European Court of Justice, and was a partner in the European law department of a major Brussels law firm. Jean-François has several decades of experience in competition and trade law, representing clients in numerous cases before the European Commission and the EU Courts.

Jean-François assists clients on all aspects of competition law with particular expertise in cartels, abuses of dominance and merger control. Jean-François has assisted clients in numerous anti-dumping and anti-subsidy cases in proceedings before the European Commission and in related litigation before the EU Courts and the WTO dispute settlement system. He was appointed by the WTO Director-General as a member of the WTO panel in the *Automotive Leather* dispute between the US and Australia.

Jean-François Bellis teaches a course on EU competition law at the Institute of European Studies of the University of Brussels (ULB) and directs a seminar on competition law at the University of Liège. He also lectures on abuses of dominance at the Brussels School of Competition.

He received his LL.M. from the University of Michigan

and a Master of Laws from the University of Brussels.

Fiona Carlin

Managing Partner, European and Competition Law Practice; Chair, Global and Antitrust Law Practice

Fiona Carlin is a UK qualified barrister and has been practicing EU and competition law in Brussels for more than 20 years. She is the managing partner of Baker McKenzie's EMEA+ region and until July 2018 she was Chair of the Firm's Global Antitrust & Competition Law Practice Group that is ranked in the Top 5 Global Elite by Global Competition Review.

Fiona advises on a wide variety of competition law issues including merger control, State aid grants, sector inquiries and the defence of clients involved in cartel and other investigations, including to appeal stage before the European Courts in Luxembourg. Her practice spans many sectors with a particular focus on pharmaceuticals and industrial and consumer goods. Fiona has been a long-standing advisor to the European pharmaceutical industry association, EFPIA, ever since the EU pharma sector inquiry that was launched 10 years ago.

Isabella de Silva

President, French Competition Authority

Isabelle de Silva is the President of the French Competition Authority. Between 1999 and 2000, she worked at the French Ministry of Culture and Communication. From 2005 to 2008, she was Deputy Reporter at the Conseil constitutionnel (the French constitutional court). As government commissioner, she worked at the court of conflicts (2006-2009) and at the French Council of State (2000-2009). From 2009 to 2011, she was legal director of the French Ministry of ecology, sustainable development, transport and housing. After serving as member of the French regulatory Authority for press distribution (2012), and then as president of the Sixth subsection of the Administrative Jurisdiction Division of the Council of State (2013), she became member of the French Competition Authority in 2014.

Makan Delrahim

Assistant Attorney General, Department of Justice

Makan Delrahim was confirmed on September 27, 2017, as Assistant Attorney General for the Antitrust Division. Mr. Delrahim previously served as Deputy

Assistant to the President and Deputy White House Counsel. Mr. Delrahim's rich antitrust background covers the full range of industries, issues, and institutions touched upon by the work of the Antitrust Division. He is a former partner in the Los Angeles office of a national law firm. He served in the Antitrust Division from 2003 to 2005 as a Deputy Assistant Attorney General, overseeing the Appellate, Foreign Commerce, and Legal Policy sections. During that time, he played an integral role in building the Antitrust Division's engagement with its international counterparts and was involved in civil and criminal matters. He has served on the Attorney General's Task Force on Intellectual Property and as Chairman of the Merger Working Group of the International Competition Network. Mr. Delrahim was also a Commissioner on the Antitrust Modernization Commission from 2004 to 2007. Earlier in his career, Mr. Delrahim served as antitrust counsel, and later as the Staff Director and Chief Counsel of the U.S. Senate Judiciary Committee.

Eleanor M. Fox

Professor of Trade Regulation, New York University School of Law

Eleanor M. Fox is the Walter J. Derenberg Professor of Trade Regulation at New York University School of Law. She is an expert in antitrust and competition policy, and teaches, writes, and advises on competition policy in nations around the world and in international organizations. She has a special interest in developing countries, poverty, and inequality, and explores how opening markets and attacking privilege, corruption, and cronyism can alleviate marginalization and open paths to economic opportunity and inclusive development. Fox received her law degree from NYU School of Law in 1961; she received an inaugural Lifetime Achievement Award in 2011 by the Global Competition Review for "substantial, lasting, and transformational impact on competition policy and practice." She received the inaugural award for outstanding contributions to the international competition law community in 2015 by ASCOLA, the Academic Society for Competition Law. Her book with Mor Bakhoun, *Making Markets Work for Africa*, is in publication by Oxford. She is co-author with Daniel Crane of *Global Issues in Antitrust and Competition Law* (2d ed. West 2017), and with Damien Gerard of *EU Competition Law casebook* (Elgar 2017), and of a casebook on US Antitrust Law (3d ed. West 2012).

Hon. Douglas H. Ginsburg

Senior Circuit Judge, US Court of Appeals for the District of Columbia, Professor of Law, George Mason University Antonin Scalia Law School

Senior Circuit Judge Douglas Ginsburg was appointed to the United States Court of Appeals for the District of Columbia in 1986; he served as Chief Judge from 2001 to 2008. After receiving his BS from Cornell University in 1970, and his JD from the University of Chicago Law School in 1973, he clerked for Judge Carl McGowan on the D.C. Circuit and Justice Thurgood Marshall on the United States Supreme Court.

Thereafter, Judge Ginsburg was a professor at the Harvard Law School, the Deputy Assistant and then Assistant Attorney General for the Antitrust Division of the Department of Justice, as well as the Administrator of the Office of Information and Regulatory Affairs in the Office of Management and Budget. Concurrent with his service on the federal bench, Judge Ginsburg has taught at the University of Chicago Law School and the New York University School of Law. Judge Ginsburg is currently a Professor of Law at the Antonin Scalia Law School, George Mason University, and a visiting professor at the University College London, Faculty of Laws.

Judge Ginsburg is the Chairman of the International Advisory Board of the Global Antitrust Institute at the Antonin Scalia Law School, George Mason University. He also serves on the Advisory Boards of: Competition Policy International; the Harvard Journal of Law and Public Policy; the Journal of Competition Law and Economics; the Journal of Law, Economics and Policy; the Supreme Court Economic Review; the University of Chicago Law Review; The New York University Journal of Law and Liberty; and, at University College London, both the Center for Law, Economics and Society and the Jevons Institute for Competition Law and Economics.

Scott Hemphill

Professor of Law, New York University of Law

Scott Hemphill is a Professor of Law at New York University Law School. He teaches and writes about antitrust, intellectual property, and regulation of industry. His research focuses on the law and economics of competition and innovation, and his scholarship ranges broadly, from drug patents to net neutrality to fashion and intellectual property. Hemphill's recent work examines the antitrust problem

of parallel exclusion in concentrated industries and anticompetitive settlements of patent litigation by drug makers. His scholarship has been cited by the US Supreme Court and the California Supreme Court, among others, and has formed the basis for congressional testimony on matters of regulatory policy. Hemphill's writing has appeared in law reviews, peer-reviewed journals, and the popular press, including the Yale Law Journal, Science, and the Wall Street Journal. He joined NYU from Columbia Law School, where he was a professor of law. Hemphill has also served as antitrust bureau chief for the New York Attorney General and clerked for Judge Richard Posner of the US Court of Appeals for the Seventh Circuit and Justice Antonin Scalia of the Supreme Court.

He holds a JD and PhD in economics from Stanford, an AB from Harvard, and an MSc in economics from the London School of Economics, where he studied as a Fulbright Scholar.

Herbert Hovenkamp

Professor of Law, University of Pennsylvania Law School and The Wharton School

Professor Herbert Hovenkamp is the James G. Dinan University Professor at University of Pennsylvania Law School. He is a recognized expert and prolific author in the areas of Antitrust law and American Legal History. He holds a joint appointment between Penn Law and Wharton Business. Prior to that, Professor Hovenkamp was Professor of Law at the University of Iowa, and before that at the University of California, Hastings College of the Law. He is a fellow of the American Academy of Arts and Sciences.

He has been the Rockefeller Foundation Fellow, Harvard Law School; Fellow of the American Council of Learned Societies, Harvard Law School; Faculty Scholar, University of Iowa; Presidential Lecturer, University of Iowa; and the recipient of the University of Iowa Collegiate Teaching Award.

Professor Hovenkamp holds a B.A. from Calvin College, and a M.A., Ph.D., and J.D. from the University of Texas.

Frédéric Jenny

Chair OECD Competition Committee, Professor ESSEC Business School

Frederic JENNY is professor of Economics at ESSEC Business School in Paris. He is Chairman of the OECD Competition Committee (since 1994), and Co-Director of the European Center for Law and Economics of

ESSEC (since 2008).

He was previously Non Executive Director of the Office of Fair Trading in the United Kingdom (2007-2014), Judge on the French Supreme Court (Cour de cassation, Economic Commercial and Financial Chamber) from 2004 to August 2012, Vice Chair of the French Competition Authority (1993-2004) and President of the WTO Working Group on Trade and Competition (1997-2004).

He was Global Professor of Antitrust in the New York University School of Law's Hauser Global Law School (2014), visiting professor at University College London Law School (2005-2012), Haifa University School of Law in Israel (2012), University of Capetown Business School in South Africa (1991), Keio University Department of economics in Japan (1984), Northwestern University Department of Economics in the United States (1978).

Professor Jenny holds a Ph.D in Economics from Harvard University (1975), a Doctorate in Economics from the University of Paris (1977) and an MBA degree from ESSEC Business School (1966)

James Keyte
Director of Global Development, The Brattle Group (moderator)

James Keyte is the Director of Global Development at The Brattle Group. In this capacity, Mr. Keyte plays a lead role in growing Brattle's antitrust practice and defining a new level of quality for economic consulting.

His extensive practical experience, along with his deep antitrust expertise, gives Brattle a competitive advantage in producing top quality expert work product across all competition subject areas. Mr. Keyte is directly engaged in marketing, training, and quality review across all of Brattle's competition and antitrust engagements both in the U.S. and globally.

Mr. Keyte previously spent more than twenty years as a partner at Skadden, where he handled a wide variety of antitrust litigation, transactions, and advisory matters across numerous industries. He led high-profile antitrust cases involving alleged price-fixing, monopolization, mergers, intellectual property licensing, and sports-related matters, including class actions. He was also involved in a number of high-

profile mergers, several of which involved litigation challenges by the DOJ and FTC.

Mr. Keyte is the Director of the Fordham Competition Law Institute (FCLI), which he will continue to lead, and has published more than 50 articles related to antitrust across a wide range of topics, including on the subject of expert testimony. He is an adjunct professor at Fordham Law School, a former editor of Antitrust Law Journal, and currently serves as editor of Antitrust Magazine. He holds a J.D. from Loyola Law School (Law Review) and a B.A. from Harvard University (cum laude).

Johannes Laitenberger, Director General of DG Competition
Director-General of DG Competition, EU Commission

Johannes Laitenberger is the Director-General of the European Commission's Directorate-General for Competition. He took office on 1 September 2015. Under the political guidance of Commissioner Vestager, he manages the Directorate-General within the framework set by its mission statement and work programme.

He has been Deputy Director-General of the Commission's Legal Service (2014-15), Head of Cabinet of President Barroso (2009-14), Spokesperson of the European Commission (2005-09) and Head of Cabinet of Commissioner Reding (2003-04).

Johannes Laitenberger started his career in the European Institutions in 1996 as an adviser in the General Secretariat of the Council. In 1999, he joined the Commission as a case handler in the Directorate-General for Competition and soon became Member of Commissioner Reding's cabinet (1999-2003).

He studied Philosophy at the Portuguese Catholic University in Lisbon, and law at the Rheinische Friedrich-Wilhelms-Universität, Bonn. He qualified as a German lawyer.

He was born in Hamburg, Germany and grew up in Hamburg and Lisbon, Portugal.

Mario Monti
President, Bocconi University

Mario Monti is President of Bocconi University and Senator for life of the Republic of Italy.

He was Prime Minister of Italy (November 2011-April 2013) and Minister of Economy and Finance (November 2011-July 2012).

He served for ten years as a member of the European Commission, in charge of the Internal Market, Financial Services and Tax Policy (1995-1999), then of Competition (1999-2004).

He is Member of the *Académie des Sciences morales et politiques*, Chairman of the first Advisory Group to Transparency International EU, and Honorary President of Bruegel, the European think-tank he founded in 2005.

From February 2014 to January 2017, he was Chairman of the High-level Group on Own Resources of the European Union, in preparation of the EU Multiannual Financial Framework 2021-2027. Since May 2018, he has Chaired the High-level search committee to find the next president of the European Research Council, which was established by the Commissioner for Research, Science and Innovation Carlos Moedas.

Born in Varese, Italy, in 1943, he graduated from Bocconi University and pursued graduate studies at Yale University.

D. Daniel Sokol
Research Foundation Professor, Levin College of Law, University of Florida, Senior of Counsel, Wilson Sonsini Goodrich & Rosati

Professor D. Daniel Sokol is a University of Florida Research Foundation Professor at Levin College of Law. He focuses his teaching and scholarship on complex business issues from early stage start-ups to large multinational businesses and the issues that businesses face: corporate governance, compliance, innovation, pricing strategies, M&A, collusion, and disparate business regulation around the world.

A highly prolific scholar, Sokol has published his work in law reviews (e.g., *Michigan Law Review*, *Northwestern Law Review*), peer review journals (e.g., *Journal of Law and Economics*), books (e.g., Oxford University Press, Cambridge University Press, Stanford University Press) and the popular press (e.g., *Wall Street Journal*). He is co-editor of the leading two volume Antitrust Economics Handbook as well as the leading Antitrust Compliance Handbook. Sokol is also active in

practitioner circles in the US and abroad. The daily *Global Competition Review* named Sokol its Antitrust Academic of the Year in 2014 at its awards ceremony.

Sokol has taught at a number of other universities including: Northwestern Law School, University of Minnesota Law School, Catholic University of Chile, University of Haifa and the University of Melbourne. He is an Honorary Fellow of the Indian Institute of Corporate Affairs, Fellow of the George Washington Law School Competition Law Center, and a member of the American Law Institute. He also serves as academic advisor to the US Chamber of Commerce.

Professor Sokol received his B.A. from Amherst College, a Master of Studies from the University of Oxford, His J.D. from the University of Chicago and a LL.M. from the University of Wisconsin.

Joseph Stiglitz
Chief Economist, The Roosevelt Institute, University Professor, Columbia University

Joseph E. Stiglitz is an American economist and a professor at Columbia University. He is also the co-chair of the High-Level Expert Group on the Measurement of Economic Performance and Social Progress at the OECD, and the Chief Economist of the Roosevelt Institute. A recipient of the Nobel Memorial Prize in Economic Sciences (2001) and the John Bates Clark Medal (1979), he is a former senior vice president and chief economist of the World Bank and a former member and chairman of the (US president's) Council of Economic Advisers. In 2000, Stiglitz founded the Initiative for Policy Dialogue, a think tank on international development based at Columbia University. He has been a member of the Columbia faculty since 2001 and received that university's highest academic rank (university professor) in 2003. In 2011 Stiglitz was named by Time magazine as one of the 100 most influential people in the world. Known for his pioneering work on asymmetric information, Stiglitz's work focuses on income distribution, risk, corporate governance, public policy, macroeconomics and globalization. He is the author of numerous books, and several bestsellers. His most recent titles are *Globalization and Its Discontents Revisited*, *The Euro*, *Rewriting the Rules of the American Economy* and *The Great Divide*.

Steven C. Sunshine

Partner and Head of Global Antitrust/Competition Group, Skadden, Arps, Slate, Meagher & Glom LLP

Steven C. Sunshine is head of Skadden's Global Antitrust and Competition Group. He represents clients in connection with antitrust aspects of mergers and acquisitions, litigation, counseling and grand jury investigations. He appears before courts in connection with antitrust civil matters and before the U.S. and European antitrust authorities. Mr. Sunshine was formerly deputy assistant attorney general in charge of merger enforcement at the U.S. Department of Justice, Antitrust Division.

Nils Wahl

Advocate General, Court of Justice of the European Union

Born 1961; Doctor of Laws, University of Stockholm (1995); Associate Professor (docent) and holder of the Jean Monnet Chair of European Law (1995); Professor of European Law, University of Stockholm (2001); Managing Director of an educational foundation (1993-2004); Chairman of the Nätverket för europarättslig forskning (Swedish Network for European Legal Research) (2001-06); member of the Rådet för konkurrensfrågor (Council for Competition Law Matters) (2001-06); Judge at the General Court from 7 October 2006 to 28 November 2012; Advocate General at the Court of Justice since 28 November 2012.

Competition and antitrust in the digital age

July 20 2017 | Contributed by **Baker McKenzie**

While the digital economy offers abundant opportunities to customers and retailers alike, it also raises a number of competition concerns, including the impact on bricks-and-mortar businesses, the potential for abuse of market power by major digital platforms and the challenge of fostering online competition while preventing free riding. Competition authorities must evolve and adapt traditional antitrust principles and approaches to meet the challenges of the rapidly changing digital market.

What impact has the rapidly changing digital market had on competition in your jurisdiction and how have legislators and competition authorities responded?

Digital markets are a priority under existing EU competition policy. The fast-paced nature of the market has posed challenges for competition authorities and legislatures alike. However, EU Competition Commissioner Margrethe Vestager has stressed that digitalisation does not require a complete overhaul of competition law or the creation of sector-specific rules, but rather adaptation to the features of digital markets. At the same time, according to the European Commission, fully reaping the benefits of the digital revolution necessitates a consistent regulatory framework. This is why turning the digital single market into a reality has been a European Commission priority since the start of its mandate in 2014.

Digital cartels?

The new digital ecosystem has thus seen the rise of new means of anti-competitive behaviour, transforming what have so far been traditional competition law infringements – for example:

- In *Eturas* (2016) – a case involving an alleged cartel between travel agencies in Lithuania – the European Court of Justice (ECJ) confirmed that price fixing can be achieved not only through human coordination, but also via automated means. In this case, the coordination took place through an e-commerce platform – the Eturas online travel booking system – which sent an electronic message proposing that each agency grant discounts capped at 3%. The ECJ ruled that a travel agency which understood the message communicated and did not distance itself from it would be presumed to participate in a cartel, unless it could demonstrate that it objected to the communication or systematically set prices disregarding the rule.
- In a 2016 UK case, an online seller, Trod Limited, agreed with one of its competitors, GB Posters, not to undercut each other's prices for posters and frames sold on Amazon's UK website. The agreement was implemented by using automated re-pricing software, which the parties configured to give effect to the illegal cartel. Trod was fined a total of £163,371 by the UK national competition authority, while GB Posters received immunity for having reported the cartel.
- Advocate General Szpunar made a brief remark in the *Uber* case that use by competitors of the same algorithm to calculate prices is not in itself unlawful, but might give rise to hub-and-spoke conspiracy concerns. The case concerned whether Uber could be classified as an information services provider or transportation service. To reinforce the argument that Uber should be considered a transportation service, the advocate general noted that the alternative interpretation would classify Uber as a platform which calculated the fees for each of the notionally competing Uber drivers using the platform, so potentially raising competition law risks.

AUTHORS

Agapi Patsa



Aliki Benmayor



- In its contribution to an Organisation for Economic Cooperation and Development discussion on algorithms and collusion, Directorate General for Competition noted two principles underlying the treatment of algorithmic pricing:
 - illegal pricing offline is likely to remain illegal online; and
 - algorithms are under a company's control, thus a company remains liable for its actions.

The European Commission's findings in the e-commerce sector inquiry suggest that this will continue to be an important compliance area. The inquiry noted that the majority of retailers track competitors' prices, with more than two-thirds of those doing so via automated software programs. An overwhelming majority in fact adjust their own prices to those of competitors. In addition, the inquiry noted that collection by marketplaces or direct online sellers of their retailer's pricing information might require safeguards to avoid anti-competitive consequences.

Platforms' use of MFN clauses

With online platforms becoming increasingly popular, most-favoured-nation (MFN) clauses have increasingly captured the attention of both the European Commission and national competition authorities. So far, the focus has been on the markets for hotel accommodation and e-books.

- Between 2012 and 2015 the European Commission supervised the simultaneous actions of several national competition authorities (ie, Austria, France, Germany, Ireland, Italy, Sweden and the United Kingdom) which brought proceedings against hotel booking platforms (ie, Booking.com, HRS and Expedia) for imposing parity clauses on their hotel contractors. The clauses provided that online platforms would automatically benefit from:
 - the same rates and conditions as those granted to their competitors (wide MFN); or
 - those on the hotels' direct online channels (narrow MFN).

Germany's national competition authority prohibited certain MFN clauses. The French, Italian, Swedish, Irish and UK national competition authorities accepted commitments. France and Austria legislated to prohibit online travel agents' price parity clauses.

- In June 2015 the European Commission opened a formal antitrust investigation into some of Amazon's e-books distribution agreements with publishers. The investigation focused on MFN clauses which allegedly granted Amazon the right to be informed of more favourable or alternative terms offered to its competitors, and/or the right to terms and conditions at least as good as those offered to its competitors. The European Commission took the view that these clauses make it more difficult for other e-book platforms to compete with Amazon, by reducing publishers' and competitors' ability and incentives to develop new and innovative e-books and alternative distribution services, while possibly limiting competition between different e-book distributors. In early May 2017, the European Commission accepted Amazon's commitments to no longer enforce or introduce these clauses in agreements. This was not the first time that the e-book sector was under scrutiny. In 2013 the European Commission investigated price parity clauses contained in contracts entered into between Apple and various publishers. This case also resulted in the parties offering commitments to remove price parity clauses from their contracts.

Data as an asset

Competition authorities have become sensitive to the growing importance of Big Data in today's economy. Vestager has emphasised that merely holding a large amount of data may not be problematic, but might need to be factored into the competition law assessment under merger control. Under existing merger rules, the commission and national competition authorities examine mergers that meet certain turnover thresholds.

Following the *Google/DoubleClick* and *Facebook/WhatsApp* cases, several respondents (including the European Data Protection Supervisor) argued that the existing EU merger control regime should be updated to capture proposed concentrations or acquisitions of less established digital companies, which may hold significant quantities of personal data that have yet to be monetised.

The European Commission is examining whether a value-based threshold could be an appropriate proxy for identifying mergers with an EU dimension. The rationale is that the new threshold would

take into account both the future market capitalisation of an IT company and how data acts as a currency with which consumers pay for free services they receive via the Internet. A 'value of transaction' merger threshold has already been adopted in Germany and Austria.

At the same time, the final report of the e-commerce sector inquiry confirmed that competition concerns could arise with regard to data collection and usage. For example, exchanging competitively sensitive data between online marketplaces and third-party sellers or manufacturers with their own shops and retailers may be anti-competitive where the same companies are also direct competitors on a given set of products or services.

Tackling unjustified geo-blocking

With the global economy becoming digitalised at a rapid pace, the European Commission emphasised the need to ensure better access for consumers and businesses to digital goods and services across Europe. E-commerce in the European Union has grown steadily, with the percentage of people ordering goods or services online having grown from 30% in 2007 to 55% in 2016. One of the European Commission's primary goals is to tackle unjustified geo-blocking (ie, commercial practices that prevent online customers from accessing and purchasing a product or a service from a website based in another member state, or which automatically re-route them to a local site). Geo-blocking can also occur when trying to access or purchase online copyright-protected content from another member state.

The European Commission has proposed addressing geo-blocking in the European Union via legislative proposals and the competition law toolbox.

Legislative proposals

- Geo-blocking Regulation – this proposal aims to address the problem of customers being unable to buy products and services from traders located in a different member state, or being discriminated against in accessing prices compared to nationals or residents. The proposal defines specific situations where there can be no justified reason for geo-blocking or other forms of discrimination based on nationality, residence or location.
- Cross-border portability of online content – the European Commission has proposed a regulation that will allow consumers to access their online content subscriptions when they are temporarily outside their member state of residence. The European Parliament, the Council of the European Union and the European Commission reached an agreement on this proposal on May 18 2017.
- Reform of the Satellite and Cable Directive – this proposal aims to address potential consumer demand to access broadcasters' content in member states other than the state of origin, and foster the cross-border distribution of television and radio programmes online by facilitating rights clearance for broadcasters' online services. It also extends the system of compulsory collective management applicable to cable re-transmission to other equivalent digital re-transmissions (eg, internet protocol television).

Competition law

- E-commerce sector inquiry – the European Commission sector inquiry concluded that many retailers still do not sell cross-border for at least one of their product categories. Refusing delivery to customers in other member states and accepting payments from them are classified as the most prominent forms of geo-blocking. Intervention would be considered only if geo-blocking is the result of restrictions in bilateral agreements, not a unilateral business decision of a non-dominant company. In February 2017 the European Commission opened three separate investigations into holiday accommodation, video games and consumer electronics pricing practices that may be problematic under Article 101 of the Treaty on the Functioning of the European Union .
- Antitrust investigation in pay-TV services – this investigation is examining contractual provisions in licensing agreements between six US film studios (Disney, NBC Universal, Paramount Pictures, Sony, Twentieth Century Fox and Warner Bros) and Sky UK, which prevent Sky UK from providing its services across borders (eg, by refusing potential subscribers from other member states or blocking access to films through its online pay-TV services or through its satellite pay-TV services to consumers outside its licensed territory).

Ensuring fair and innovation-friendly platform economy

Complementing enforcement action under competition law, the European Commission is conducting a fact-finding exercise on platform-to-business trading practices. Concerns relate to platforms favouring their own products or services, discriminating between suppliers and sellers and restricting access to and the use of personal and non-personal data. The absence of transparency and redress mechanisms are additional matters raised by stakeholders. The European Commission aims to propose legislation by the end of 2017 to address unfair contractual clauses and trading practices identified in business-to-business relationships.

In terms of market definition, are online services considered to be in the same market as traditional services in your jurisdiction? What impact has this had on competition?

Market definition constitutes the point of departure for an analysis of competitive forces. According to the applicable legal test, the delineation of the relevant market is in essence a matter of substitutability. If traditional and online services can be regarded by consumers as substitutable due to their characteristics or price, they fall within the same product market. Demand substitutability generally consists of the strongest competitive constraint exercised on firms and is considered to carry the heaviest weight in the determination of the relevant market.

The key question is whether a supplier of a traditional service should introduce a 5% to 10% price increase and whether enough customers would be inclined to switch to online (and *vice versa*), making the price rise unprofitable. An affirmative answer may suggest that the market encompasses both traditional and online services.

The question of whether online and offline services are part of the same product market has already been dealt with by the European Commission in a plethora of merger cases. However, no uniform guidance is provided, as the answer is dependent on the service under consideration.

Travel agency services

In *Dnata/Stella, American Express Company/Qatar Holding/GBT, Axa/Permira/Opodo/Go Voyages/Edreams* and *Thomas Cook/Travel Business of co-operative group/Travel Business of Midlands Society*, while leaving the precise market definition open, the European Commission considered a possible sub-segmentation of the market for the distribution of leisure travel agency services into offline travel agencies (package and independent holidays) and online travel agencies (package and independent holidays and leisure flights).

Payments

- Mobile payments versus existing offline payments – in *Telefonica UK/Vodafone UK/Everything Everywhere/JV*, the European Commission examined whether the retail distribution of mobile wallet services (including both offline and online mobile payments) constitutes a separate market from existing offline payment services (near field communication (NFC) enabled credit and debit cards and traditional means of payment, such as credit, debit cards and cash). While it considered that mobile payments are likely to continue to coexist in the foreseeable future with non-mobile means of payment, including NFC and non-NFC-enabled credit and debit cards, the European Commission ultimately left the question open.
- Mobile payments versus existing online payments – in *Telefonica UK/Vodafone UK/Everything Everywhere/JV*, the European Commission further considered that the retail distribution of mobile wallet services (including both offline and online mobile payments) may constitute a market separate from existing online payment services (through credit cards, debit cards and PayPal, online on a static personal computer, tablet or mobile handset). However, the commission once again left the question open.
- Offline versus online mobile wallet services – in the same vein, the European Commission noted in *Telefonica UK/Vodafone UK/Everything Everywhere/JV* that online (eg, Google Wallet) and offline (via NFC-enabled mobile devices) mobile payments are unlikely to be part of the same relevant product market.

In *BNP Paribas Fortis/Belgacom/Belgian Mobile Wallet*, the European Commission equally left the

definition of these potential markets open, primarily due to the rapidly evolving payment landscape which sees new innovative technologies and platforms being developed.

Sale of books

Books are sold to final consumers through a wide range of different channels, including independent book stores, book chains, hypermarkets, book clubs, the Internet, mail orders, credit sales and telemarketing. In *Ahold/Flevo* and *Lagardère/Natexis/VUP*, the European Commission segmented offline and online sales channels, identifying the existence of a distinct 'distant sale' segment within the market for the sale of books to final consumers, comprising book clubs, mail orders and online sales. In *Bertelsmann/Kooperative Förbundet/Bol Nordic*, the European Commission further considered a narrower market for the online sales of books.

However, in *Egmont/Bonnier* the European Commission departed from this direction and identified a single market for all book sales to final consumers, given that the market investigation (covering the Danish market) did not bring forward any element on the basis of which a separate distant sale market might be identified.

Looking further at the upstream market for the acquisition of publishing rights, the market investigation in *Bertelsmann/Pearson/Penguin Random House* revealed strong indications that publishing rights for English language print books and e-books belong to the same product market, as in the majority of cases publishers seem to acquire both rights. On the contrary, results were mixed with regard to the acquisition of publishing rights for audiobooks.

Retail distribution

Although having left open the question of whether all retail sales channels form one product market, the European Commission's investigation in *Otto/Primondo Assets* revealed that the more standardised products within a product category are, the more likely it is that bricks-and-mortar and distance selling (ie, home shopping) could belong to the same relevant product market. This was mainly attributed to the fact that:

- there is a degree of interrelation between the two channels, depending on the product category, in the sense that customers do not necessarily purchase goods in the channel that they first consulted; and
- both channels serve different customers' needs and thus have different advantages and disadvantages from a customer's viewpoint, rendering them complementary rather than substitutable.

Ultimately, the competitive pressure exerted by home shopping and by bricks-and-mortar shops on each other was considered on a member state and sector (non-food retail) level.

What types of conduct constitute abuse of dominance in the online space and what practices are most likely to catch out unwary online players?

Common online business practices may attract abuse claims when engaged in by an allegedly dominant company. Competing to integrate new services or features may draw allegations of tying. Online operators' efforts to gain greater reach through free or 'freemium' models may be allegedly predatory. The race to secure the best online real estate, to leverage a unique set of big data or secure a prime position to offer services to a well-used website's audience may also result in allegations of foreclosure.

- Pre-installation or service integration as a form of product tying – an online player may leverage its market power in one market to foreclose competition in a separate market. In 2009 the European Commission fined Microsoft for tying its Internet Explorer web browser to its Windows operating system. Users could not obtain Windows without also obtaining Internet Explorer. Alternative web browsers could be installed only in addition to Internet Explorer, which would rarely happen because of user inertia. The European Commission is investigating allegations that Google leverages its market power in the market of operating systems by requiring manufacturers to whom it supplies its Android operating system to also pre-install other Google services (eg, Google Chrome).
- Exclusivity obligations in agreements with third parties – this may involve exclusive rights for

an online player with market power to advertise on popular platforms or offer services to popular platforms. In the context of an ongoing investigation against Google, the European Commission is investigating allegations that Google does not allow third-party websites on which Google places ads to also source ads from Google's competitors. The European Commission is also concerned that Google requires third-party websites to reserve the most prominent spaces for Google ads and obtain Google's approval before displaying ads from Google's competitors.

- (Constructive) refusals to deal – where an online player is vertically integrated and has some sort of gatekeeper position in the upstream market, there may be concerns that it uses that position to foreclose competitors' access to users in the downstream market. In 2013 the European Commission investigated a number of large telecommunications operators that provide both internet connectivity with other networks at the wholesale level and internet access services to end users. The European Commission was concerned that the operators charged excessive fees to interconnect with other networks at the wholesale level, which could have the effect of providing an unfair advantage to the operators' own proprietary content services delivered to end users. In addition, the European Commission recently fined Google because it allegedly used algorithms that systematically favoured its own comparison shopping service over those of competitors by giving it top ranking in Google's general search results. In 2017 a UK judge ruled in favour of Google regarding similar complaints made by Streetmap. Streetmap alleged that Google abused its dominant position by prominently placing a clickable image from Google Maps at the top of the search results, whereas the services of Google's competitors appear in the form of links.
- Predatory pricing by means of free products – the emergence of new business models in two-sided markets means that products may be provided to users free of payment. Such free provision may be counterbalanced by data collection and income received from advertisers or by purchases of product versions that offer more functionalities. There have been complaints that the free provision of products amounts to predatory pricing. In 2012 Bottin Cartographes argued before a Paris court that Google abused its alleged dominant position by zero-pricing the Google Maps application program interface. The court sided with Bottin Cartographes, but the judgment was reversed at a higher instance.
- Data collection to lock users in and foreclose competitors – users share data with online players as they use their products. This helps online players to further personalise products. There is a concern that if online players do not share the data that they collect with competitors, users will be less willing to switch between competing products. The German national competition authority is considering this issue in its ongoing investigation against Facebook's alleged abuse of dominant position through the terms and conditions on the use of user data.

What steps are competition authorities in your jurisdiction taking to prevent online retailers and service providers from free riding on the investments of bricks-and-mortar retailers and service providers?

EU competition policy encourages online sales as a means of completing the EU single market. Suppliers must not restrict retailers from advertising or selling products online.

This raises free-riding concerns. Bricks-and-mortar retailers complain that customers benefit from their pre-sale services, but then purchase the products from online retailers. In turn, suppliers are concerned that free-riding may disincentivise bricks-and-mortar retailers from investing in high-quality services (eg, by retaining qualified and trained personnel).

Suppliers find it difficult to address free-riding concerns by bricks-and-mortar retailers. In 2016 Ultra Finishing – a bathroom-fittings manufacturer – was fined almost £800,000 for resale price maintenance in the United Kingdom. Offline retailers warned Ultra Finishing that they would no longer promote its brand because of internet retail outlets butchering prices to the point where it was impossible to compete. In response, Ultra Finishing adopted an 'e-tail' policy recommending online prices not to go 25% below recommended resale prices. The UK national competition authority found that, in reality, this was far from a recommendation. Ultra Finishing monitored online retailers' pricing daily and key accounts reported 'idiot sellers'. Online retailers disregarding the recommendation faced reduced discounts, were prevented from using product images and mere refused orders.

There are indications that there is a growing understanding among enforcers of the need to ensure that physical shops can survive as e-commerce booms. In the EU-wide sector inquiry into e-commerce, aimed at gathering evidence on potential barriers to competition in the online space, the European Commission identified a number of business practices that may limit online sales. But it also acknowledged the legitimacy of free-riding concerns by bricks-and-mortar retailers. Recent public statements made by Vestager also indicate that a shift in attitude may be underway.

As it stands, EU competition rules allow suppliers to take the following steps, among other things, in order to address free-riding concerns and restore the incentives of bricks-and-mortar retailers to increase sales efforts:

- support the sales efforts of a bricks-and-mortar retailer by means of a fixed-fee payment or an additional discount to a bricks-and-mortar retailer to support specific marketing efforts (eg, targeted, in-store or on-site promotions);
- require that retailers sell the products from specific locations or addresses;
- require that retailers sell a certain amount (whether in volume or value) of products via bricks-and-mortar stores;
- set quality standards for online sales that are equivalent to the quality standards imposed for sales in bricks-and-mortar shops (eg, require the online retailer to provide after-sales services);
- exclusively allocate a territory or customer group to a specific retailer – other retailers (including in the online space) may not actively solicit orders from customers residing in that territory or belonging to that customer group. Exceptionally, where establishing a new brand or an existing brand in a new market requires substantial (sunk) investments by the exclusive retailer, the supplier may also require other retailers not to respond to unsolicited requests from customers residing in that territory or belonging to that customer group during the first two years of sale of the products;
- set up a selective distribution system which limits sales of the products to retailers that meet certain criteria, including a requirement for authorised retailers to run at least one bricks-and-mortar shop; and
- charge different prices to hybrid retailers on the one hand and pure online retailers on the other in the absence of dominance – price differentiation is allowed so long as it does not amount to dual pricing (ie, charging different prices to the same retailer, depending on whether the product is sold online or offline).

How can competition authorities best ensure that these steps do not hinder innovation or consumer choice and promote the continued evolution of online services?

EU competition authorities closely examine online sales restrictions imposed by suppliers. Among other things, a supplier may not:

- limit a retailer's ability to advertise or sell online;
- limit the quantity of online sales made by a retailer;
- charge a retailer a higher price for products intended to be resold online than for products intended to be resold offline; and
- restrict the territories or customer groups to which the retailer sells the products online.

Exceptionally, a retailer's ability to actively solicit orders from customers online (eg, by sending out emails or using territory-based banners on third-party websites) may be limited, where those customers reside in territories or belong to customer groups which are exclusively allocated to another retailer. However, in practice, online sales are generally considered to be a passive response by retailers to unsolicited orders placed by customers and cannot therefore be restricted.

There is a risk that EU competition authorities adopt an overly restrictive approach to online sales restrictions, which can have a straightjacket effect on brand owners. It may impede the adjustment of their commercial practices (eg, regarding product presentation and quality) to a retail environment that is changing rapidly, and inhibit them from addressing legitimate concerns (eg, free riding).

There have already been instances where this has happened at the national competition authority level:

- The German national competition authority took the position that restrictions on the use of third-party platforms for online sales may amount to a *per se* infringement of competition. In its final report on the EU-wide sector inquiry into e-commerce, the European Commission took a different position, stating that a restriction on the use of third-party platforms does not necessarily mean an outright prohibition of online sales. Rather, a case-by-case assessment is required. The issue is pending before the ECJ for a preliminary reference ruling in *Coty*.
- The German national competition authority required suppliers to apply the same rebates to bricks-and-mortar distributors as to online distributors (ie, not to make distinctions between different forms of distribution). In its final report on the EU-wide sector inquiry into e-commerce, the European Commission clarified that, whereas a supplier may not charge different prices to the same retailer depending on whether the product is sold online or offline, a supplier may set different (wholesale) prices for the same product to different retailers.

In order to ensure a high level of innovation and consumer choice and promote the continued evolution of online services, EU competition authorities should avoid adopting a hardline approach to online sales restrictions. Moreover, EU competition authorities should coordinate more with one another. Following its EU-wide sector inquiry into e-commerce, the European Commission has vowed to broaden the dialogue with national competition authorities within the European competition network in order to contribute to a consistent application of the EU competition rules as regards e-commerce-related business practices.

For further information on this topic please contact [Agapi Patsa](mailto:agapi.patsa@bakermckenzie.com) or [Alik Benmayor](mailto:aliki.benmayor@bakermckenzie.com) at Baker & McKenzie by telephone (+32 2 639 36 11) or email (agapi.patsa@bakermckenzie.com or aliki.benmayor@bakermckenzie.com). The Baker & McKenzie website can be accessed at www.bakermckenzie.com.

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The case of the European Commission's curious interpretation of the *Intel* judgment

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These days competition law talk resembles central bank talk. While the Mario Draghis and Janet Yellens of this world comment market facts daily before crowds of financial analysts, high-ranking competition officials shae their views on legal developments in conference rooms filled with lawyers, economic consultants and journalists. In the EU, given the European Commissionâ™s ("Commission") role as "guardian of the Treaties", its power to impose multimillion (or even multibillion) Euro fines or competition law infringements, as well as the regrettable slowness of the judicial review process, it is understandable that close attention is paid to pronouncements by

Commission official. In this context, a December 2017 speech of the Director-General of DG Competition entitled "Accuracy and administrability go hand in hand" (the "speech") attracted wide interest from the competition community. Presumably after months of internal discussions, the Director-General disclosed the Commission's interpretation of the Intel judgment, which had been handed down by the Grand Chamber of Court of Justice of the European Union ("CJEU") in September 2017. The speech provides an insight into the implications of the Intel judgment for the Commission's assessment of abuse of dominance cases in general, and of exclusivity rebates cases in particular. The Commission's openness is commendable. For obvious reasons, the Commission seldom discusses cases pending before the EU Courts – the CJEU referred the Intel case back to the General Court ("GC") for a new review – and does so even less on a technical level. As always with such official pronouncements, the speech is an exercise in consensus building. Yet, beyond the big picture, three interpretative positions expressed in the speech deserve a critical assessment.



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ANTITRUST AND THE PULLS OF POPULISM

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I. INTRODUCTION

The populist concern arises when the people feel that the law or the system is not working for them; it is not delivering to them; it is delivering to the elites. In a common expression or perception, the system is making the rich richer; inequality is increasing; outsiders are not getting a fair share of the gains of globalization and trade. We may observe two aspects. First, illiberal populist parties are arising around the world, feeding on the populist discontents. Second, populist discontents target markets and big business. It is perceived that markets are too concentrated and that business firms' strategies exclude challengers and entrench power. "Antitrust should do something." Can it? The two threads may seem unconnected, but are they? They both arise in large part from discontents with markets and big business. Is it possible that, by not addressing economic populism, we fan the flames of political populism?

In this essay I will first but briefly address political populism and emerging antitrust literature that is exposing it. Second, I address economic (market) populism; the claim that markets are not working for the people and antitrust should do something about it. The second part has two subdivisions: 1) The US antitrust debate: There is a frequently used framework: The question is whether we preserve the consumer welfare standard or adopt (dangerous) populism. I contest this framework. 2) The developing country debate, focusing on South Africa, a country

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that persistently excluded the majority of the people from social, political, and economic life of the country. In developing countries I observe a significant overlap between the populist claim that markets, with antitrust, are not delivering for the people, and the pursuit by these countries of an inclusive growth agenda that is efficient for them. Indeed, some Western antitrust standards have become so pro-incumbent that, in countries that use Western standards as the default, there is significant room for a marriage of equity and efficiency.

II. POLITICAL POPULISM

Maciej Bernatt of the University of Warsaw presented a paper at the 2018 annual conference of ASCOLA, the Academic Society of Competition Law, entitled Anti-Institutional Populism and Antitrust: Setting the Scene.¹ The paper describes the rise of populism in countries across Europe and elsewhere, having anti-elitism and national self-interest as slogans, and being triggered by growing inequalities in wealth, automation that undermines the security of workers, and new technologies that grease the wheels of communication with the discontented population and make common cause. He documents risks posed by these new-wave populist governments to merit-based antitrust enforcement. These include preferences for state-owned firms and powerful private firms, protectionist application of competition rules, and loss of independence of the competition authority and the judiciary that make these aberrations happen. Changes have already taken place in Poland, including an amendment to the judiciary statutes that is resulting in replacement of knowledgeable, experienced and neutral judges by Populist Party loyalists. All cases pending before the Supreme Court have been suspended pending formation of a new loyalist tribunal. Meanwhile, the competition authority has waived through, on notice too short

¹ On file with author.

for deliberative antitrust analysis, a complicated merger involving a state-owned electricity firm. The merger significantly increased concentration in an already highly concentrated market and it assures state ownership of all significant firms in the market. Similar examples are given for Hungary. Moreover the fear is expressed that the conditions that nourish populism and its rapid-fire spread across borders are now present in numerous countries, even some that were once thought immune.

III. ECONOMIC POPULISM

A. THE US ANTITRUST DEBATE

A common approach to the subject of antitrust and populism assumes that populism entails loading all public interest goals into the antitrust bucket and to declare: We must defend the consumer welfare standard and reject populism.² I prefer a different framing. The goals of antitrust is a different issue from how to respond to populism. “Consumer welfare” itself is not a self-defining metric but comprises an array of standards. Its scope expands or contracts in accordance with the analyst’s trust or not in business and markets, and conception of economic power, its prevalence and durability. For concerns limited to the functioning of markets and efficiency, there are alternative epithets for goals of antitrust, which include: preserving the market process, providing an environment likely to produce the right incentives to compete and innovate, and helping make markets work. For understanding and confronting the populist critique, a better dichotomy would contrast market values and other values; and would recognize that the other values may or may not be populist and even if populist they may or may not overlap with what a good market law will do.

² See, e.g., <https://truthonthemarket.com/2018/01/26/the-unreasonable-demands-of-antitrust-populism/>.

B. Developing countries: South Africa

A number of developing countries share the following characteristics: They have a huge left-out population and deep systemic poverty. They have weak markets, dominated for years by oligarchs, sometimes in collaboration with a few favored families. The state owns or owned most key businesses, many of which were privatized with entrenched privileges intact. Corruption is excruciatingly high. Markets and competition may have to be created. Stable growth – as well as a just society -- depends on inclusive growth. In South Africa, in addition, apartheid skewed the markets. The end of apartheid was hoped to bring an economic as well as social radical transformation; but while much has been achieved, the economic transformation has not happened. High barriers to entry and expansion on the merits, excessive business concentration, and peoples' vulnerability to exploitation are urgent problems.

I attach an article I wrote on Outsider Antitrust that addresses some of these concerns. To some analysts, the perspective might be called populist and therefore wrongheaded. But in fact every proposal is geared to help make markets work for the people. The proposals are price-lowering, not price-raising; they draw on synergies between clearing paths for outsiders and serving people in their capacity as consumers. One person's populism may be another person's efficiency (with equity). Of course there is much territory beyond the attached proposals that would put populism in tension with robust markets. The paper does not go there.

OUTSIDER ANTITRUST: “MAKING MARKETS WORK FOR PEOPLE” AS A POST-MILLENNIUM DEVELOPMENT GOAL

Eleanor M. Fox*

I. Introduction

In its Declaration on the Right to Development in 1986, the United Nations General Assembly called for nations to “guarantee the meaningful participation of all in development and in the fair distribution of its benefits.”¹

On the run up to 2000, the United Nations promulgated the eight millennium development goals to be achieved in all or part by 2015. The goals ranged from eradicating extreme poverty and hunger to achieving universal primary education to ensuring environmental sustainability. The means for achieving the goals were predominantly identified in terms of money that would flow from the richer to the poorer nations such as providing funds and forgiving debts. Year 2015 has come and gone. Progress was made. But the critical problem of severe poverty persists and the gap between rich and poor widens.² In 2015, the United Nations took stock of the gains and the persisting problems, and it announced post-2015 sustainable development goals (SDGs). There are 17 SDGs.

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This article is based on papers prepared for the OECD Global Forum (2015), UNCTAD Competition Branch, Intergovernmental Experts Conference (2015), and the 4th BRICS International Competition Conference (2015).

¹ Quoted in the synthesis report of the Secretary-General on the post-2015 sustainable development agenda, *The road to dignity by 2030: ending poverty, transforming all lives and protecting the planet*, UN Doc. A/69/700 (Dec. 4, 2014) (“Secretary General’s Report”) 3, available at http://www.un.org/ga/search/view_doc.asp?symbol=A/69/700&Lang=E.

² Poverty rates, *Economist* (May 23, 2015), <http://www.economist.com/news/economic-and-financial-indicators/21651826-poverty-rates>.

This article contributes to the sustainable development literature from an under-appreciated window – markets. It includes control of abusive acts of powerful businesses and States that block the path to markets. The article argues that empowerment to engage in markets, as well as the human benefits of affordable necessities that functioning markets bring, should be a notional eighteenth sustainable development goal. Indeed, empowerment to engage in markets can be more important than development aid because, by its very nature, it eliminates dependency.

This article first describes the few market-related SDGs and the modesty with which they are presented. Second, it highlights and in part critiques common approaches to how competition policy should relate to the SDGs, namely: (1) pleading “not my problem,” (2) urging wide antitrust exemptions so as not to tread on SDGs, and (3) offering as antitrust’s sole contribution enforcement against fixing prices of the necessities of life. Third, the article articulates a robust view of the relationship of competition law and policy to the SDGs. It argues that, in terms of helping the less well-off population, competition and markets are critical. Their value is commonly underplayed and ignored or even blamed for the degradation of the human condition. The exploitative side of markets obscures their human side. The SDG text misses the critical contribution that markets, properly harnessed, can make for the poorer population and for those without connections to wealth and power. This essay presents an empowerment-by-market thesis.

II. The SDGs.

The Sustainable Development Goals are summarized in an integrated set of six essential elements and 17 goals. I include here the stated elements and goals most relevant to markets.

The essential elements include “dignity: to end poverty and fight inequality,” “prosperity: to grow a strong, inclusive and transformative economy” not falling below the poverty line, and commitments on health, planet and the ecosystem, partnerships and global solidarity, and justice and peaceful societies.³

Goal 1 is to end poverty in all its forms. It includes access to basic services including microfinance. Goal 2 would end hunger and promote sustainable agriculture, including by access to markets and ending export subsidies and other trade distortions. Goal 8 would promote inclusive and sustainable economic growth, including job growth and entrepreneurship and growth of small enterprises, and increasing aid for trade support for developing countries. Goal 9 would build resilient infrastructure, promote sustainable industrialization and foster innovation, including integration of small enterprises into value chains and markets. Goal 17 would strengthen the means of implementation and enhance the global partnership for sustainable development by mobilizing and sharing knowledge, expertise, technology and financial resources by debt relief, and by developed countries’ fulfilling their assistance commitments. While some of the goals nod towards markets, and I have stressed those aspects above, the bulk of them entail targets to be reached by financial contributions from developed States. The goals do not identify markets as a source of dignity, empowerment, and sustainable personal and economic development, nor do they identify freeing up markets as a way to reach the goals.⁴ They should.

III. The UN Mandate and the Competition Secretariat Note

³ Secretary General’s Report, *supra* note 1, at 16-19.

⁴ Exceptions are the subgoals to end export trade distortions, and to include small enterprises in value chains. These are important but seem buried in larger equity goals. See Goals 2.b and 9.3, G.A. Res. A/RES/70/1, *Transforming our world: the 2030 Agenda for Sustainable Development*, at 16, 20 (Sep. 25, 2015), available at http://www.un.org/ga/search/view_doc.asp?symbol=A/RES/70/1&Lang=E.

All branches of the United Nations are urged to include the SDGs in their agendas in some meaningful way. Ideally, the progressive agendas would nudge each Member State to ply its oars for the good of the whole in making our world “The World We Want.”⁵

Given the mandate of the UN, the branch on Competition and Consumers responded with a Note of the UNCTAD Secretariat (the Note) on how the discipline of competition law and policy should integrate the SDGs and work towards the goal of promoting sustainable and inclusive growth.⁶ The Note explains the role of competition in providing more and better goods and services and thus promoting consumer welfare. For enforcement, it calls for prioritizing the sectors that matter the most to poorer people and the economy, and it calls for competition advocacy to tear down barriers to entry and market participation, especially for the benefit of poorer people and economic development. But the Note falls into a trap.⁷ It accepts too readily a popular notion that competition law and efficiency trample upon the human values we care about. It choreographs antitrust to back away from its own center stage to make room for the SDGs, without a finer-tuned look at the relationship.

This is not the only approach to the challenge of bringing antitrust into harmony with the SDGs. I have noted above a second response, which I call the silo perspective; namely, the “not my problem” problem.⁸ There is a third perspective, and it is the course I urge. The Secretariat Note provides a useful point of departure. I would first agree with the Note’s stress on the critical

⁵ This is an expressive motto of the SDGs, see BEYOND2015: WORLD WE WANT 2015 WEB PLATFORM, <http://www.beyond2015.org/world-we-want-2015-web-platform>.

⁶ Note by the UNCTAD Secretariat, *The role of competition policy in promoting sustainable and inclusive growth*, UN Doc. TD/RPB/CONF.8/6 (Apr. 27, 2015), available at http://unctad.org/meetings/en/SessionalDocuments/tdrbpconf8d6_en.pdf.

⁷ The trap in fact goes far beyond the Secretariat Note. It stems from the belief that markets are the problem, not a solution. *See infra* note 21.

⁸ *See* Maureen K. Ohlhausen, FTC Commissioner, What Are We Talking About When We Talk About Antitrust?, Remarks at Concurrences Review Dinner (Sept. 22, 2016), available at https://www.ftc.gov/system/files/documents/public_statements/985823/concurrence_dinner_speech_092216.pdf.

importance of anti-cartel law, which lowers prices, and with the need to prioritize pro-poor enforcement and advocacy. But then I would take two different tacks. The first I will call global. This is a call to recognize the power of markets to empower people without economic power and a call for putting markets (Making Markets Work for the People)⁹ on the SDG agenda. Making markets work for the people may, in some jurisdictions, involve resetting the equilibrium of antitrust to recognize it as outsider law, not insider law. The second critique addresses proposed exemptions from antitrust law in the name of the SDGs, and the proposed expansion of antitrust to protect the environment and small business and to achieve fairness. This article challenges the need for exemptions. It argues that the claim of antitrust's conflict with other important values is overblown; that more often the various values we pursue point in the same direction. Moreover, sacrificing antitrust is not costless. The article highlights the qualities of competition and markets that go far towards building a framework for sustainable inclusive development.¹⁰

IV. Making Markets Work for the People

⁹ See also the calls to action by CUTS, the Consumers Unity and Trust Society. For example, Pradeep S, Mehta, Secretary-General, The Role of Competition Policy in Promoting Sustainable & Inclusive Growth & Development, Slide Presentation at the 7th UN Conference to Review the UN Set on Competition Policy, Geneva (July 6, 2015), http://unctad.org/meetings/en/Presentation/CCPB_7RC2015_HLRTCompSusDev_Mehta_en.pdf.

¹⁰ Inclusive development implies an environment hospitable to bringing all people into the economic mainstream. It implies removing obstacles facing people without power to engage in the economic enterprise. It suggests that we should not be satisfied with “enough” firms in the market to, in theory, bring prices down to cost (e.g. four or five typically established players), but that we should be vigilant to remove handicaps that keep outsiders down or out.

Hospitality towards entry of outsiders is an efficient and pro-growth path. See F. M. Scherer, Antitrust, Efficiency and Progress, 62 NYUL Rev. 998, 1012 (1987); Michael E. Porter, Interview, Innovation, Rivalry and Competitive Advantage, 5 Antitrust 5, 7 (1990-1991); Dina Waked, COMPETITION OR CONCENTRATION? OLD DEBATE WITH NEW IMPLICATIONS FOR ANTITRUST ENFORCEMENT IN DEVELOPING COUNTRIES, pp. 10-15 and authorities collected in notes 75-76, while also citing authorities correlating concentration with innovation, and integrating the two perspectives (manuscript on file with author).

Competition law and policy (also called antitrust) help the people in two ways. One way has been much discussed in OECD¹¹ and UNCTAD¹² fora,¹³ particularly when developed country officials are asked: How do competition systems help the poor? One answer is commonly given: Antitrust enforcement lowers prices of goods and services, and competition authorities can and should prioritize cases with a view to targeting goods and services needed by the poorer population. Priorities should include challenging bid rigs that exploit the State as buyer, especially in view of the fact that the poorer population depends disproportionately on services supplied by the State. When the prices of State-procured goods rise, fewer of these goods and services (highways, transportation, health care, schools, children's lunches, housing) are available.

The OECD typically launches discussion projects and its members are invited to make written submissions for discussion at plenary meetings. The OECD has conducted such a project on competition law and poverty. Numerous competition authorities submitted responses, and those submissions, along with the OECD secretariat note accompanying them, are rich in detail on the above points: lowering prices of necessities and prioritization.¹⁴ This is a commendable body of work, and the policy recommendations should be adopted.

But the answer – enforce the law against cartels that involve necessities of life – is incomplete. The larger contribution of competition appears on a much larger canvas that has been overlooked. Competition is about markets, and markets enable the people to participate in the economic enterprise. Markets take people out from under the thumb of cronyistic and

¹¹ The Organization for Economic Cooperation and Development.

¹² The United Nations Conference on Trade and Competition.

¹³ See OECD Policy Roundtable, *Competition and Poverty Reduction*, DAF/COMP/GF(2013)12 (Oct. 4, 2013), available at <http://www.oecd.org/daf/competition/competition-and-poverty-reduction2013.pdf>.

¹⁴ See *id.*

autocratic States. The freedom to participate in the economic enterprise, and not to be swept aside by privilege and power, is not only a personal freedom that enhances dignity but a source of livelihood that lifts people out of poverty by empowering them.¹⁵ We may take lessons from political philosophers and economic observers as diverse as Amartya Sen,¹⁶ Friedrich von Hayek,¹⁷ and Hernando de Soto.¹⁸ Consider the farmers in Benin who must live in a market-compromised world. They are forced to accept overpriced fertilizers (auspices of the notorious Canadian potash cartel).¹⁹ If they could buy their inputs at a competitive price, they could produce a substantial crop and even sell their product for export. Similarly for cotton: If the farmers could produce and sell their product in markets undistorted by the subsidies lavished on Western agribusiness, they could sell their crop at a price that covered their costs. Similarly again, if budding entrepreneurs, though poor and unconnected to sources of power, could enter basic markets free of excessive, incumbent-protecting regulations, they could be a part of the economic enterprise rather than supplicants to it. This freedom and opportunity to enter and rise in the mainstream of economic life empowers people and builds dignity, and reciprocally serves the people as buyers. Not incidentally, as elaborated by Paul Collier in *THE BOTTOM BILLION*²⁰ and before him by Hernando De Soto in *THE OTHER PATH*,²¹ this freedom is a steam valve and a

¹⁵ See Michal S. Gal, *The Social Contract: Should we Recalibrate Competition Law to Limit Inequality?* in *COMPETITION POLICY: BETWEEN EQUITY AND EFFICIENCY* (Ioannis Lianos and Damien M. B. Gerard eds., Cambridge University Press 2017). (identifying growing inequality as a breach of our social contract, noting the ways in which competition law does and does not tend to advance equality values, and suggesting methodologies for bringing competition law closer to equality goals).

¹⁶ Amartya Sen, *DEVELOPMENT AS FREEDOM* (Oxford University Press 1999).

¹⁷ Friedrich A. von Hayek, *THE ROAD TO SERFDOM* (first published 1944, University of Chicago Press 1967).

¹⁸ Hernando De Soto, *THE OTHER PATH: THE ECONOMIC ANSWER TO TERRORISM* (first published 1989, Basic Books 2002).

¹⁹ See Frederick Jenny, *Potash cartels and double standards*, *FIN. TIMES* (Aug. 30, 2010), <https://www.ft.com/content/08aadb2-b490-11df-8208-00144feabdc0>.

²⁰ Paul Collier, *THE BOTTOM BILLION: WHY THE POOREST COUNTRIES ARE FAILING AND WHAT CAN BE DONE ABOUT IT* (Oxford University Press 2007).

²¹ *Supra* note 17.

safety valve; it wards off societal disaffection that seduces young people into gangs of violence and that produces dysfunctional societies.

The competition family knows the value of markets. But a critical mass of devoted individuals who despair of the poverty trap and the inequality gap distrusts markets. They see markets as the enemy that helps the rich exploit the poor, characterizing free markets as the fuel that produces Bernie Madoffs and economic crises. They count markets as the problem.²² This is not surprising in a world in which we see extreme exploitation of people in need of food and medicines, and an antitrust community that says: Not my problem.²³ Antitrust may be seen as complicit with insiders who get rich on market failures that antitrust ignores. Antitrust needs a reset, and the dialogue on the SDGs needs an infusion of understanding the virtues of open markets to ordinary people in achieving the dignity and empowerment goals of The World We Want. The competition agencies and tribunals, on their end, must create a consciousness of making markets work for people without power.

At its birth, antitrust was a discipline and tool for the outsider;²⁴ for people without power. It has been seduced by beautiful, elegant, but unfitting economic assumptions.²⁵ An

²² This is the sentiment of Oxfam's Briefing Paper No. 178, *Working for the Few* (Jan. 20 2014), https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/bp-working-for-few-political-capture-economic-inequality-200114-en_3.pdf. The Briefing Paper also presents many valuable statistics and observations. *But see*, for reliance on the market as the solution, *Promoting Market Access for the Rural Poor in Order to Achieve the Millennium Development Goals*, IFAD Discussion Paper (2003), <https://www.ifad.org/documents/10180/79e82056-a4be-44d2-9362-9cc093b9176d>.

²³ See Harry First, *Excessive Pricing as an Antitrust Violation* (Feb. 2017), manuscript on file with author.

²⁴ Eleanor M. Fox, *The Modernization of Antitrust: A New Equilibrium*, 66 CORNELL L. REV. 1140 (1981).

²⁵ Paul Krugman, *How Did Economists Get it So Wrong?*, N.Y. Times, Sept. 6, 2009, §MM (Magazine), at 36; Joseph Brodley, *Post-Chicago Economics and Workable Legal Policy*, 63 ANTITRUST L.J. 683 (1995). *See* Joseph Stiglitz, *Towards a Broader View of Competition Policy*, chapter in this volume. *See also* Jonathan B. Baker, *Taking the Error Out of "Error Cost" Analysis: What's Wrong with Antitrust's Right?*, 80 ANTITRUST L.J. 1 (2015); Eleanor M. Fox, *The Efficiency Paradox*, in *HOW THE CHICAGO SCHOOL OVERSHOT THE MARK: THE EFFECT OF CONSERVATIVE ECONOMIC ANALYSIS ON U.S. ANTITRUST* (Robert Pitofsky ed., Oxford University Press, 2008) 77; Michal S. Gal, *supra* note 15. *Cf.* Gabriel Kolko, *THE TRIUMPH OF CONSERVATISM: A REINTERPRETATION OF AMERICAN HISTORY, 1900-1916* (1963).

SDG-friendly antitrust would revive antitrust as outsider law, not insider law, and, with the broader advocacy policy that surrounds it, would tear down barriers, empowering people to help themselves.²⁶ In this environment, markets, with antitrust as enabler, can be one of the most powerful tools to lift people out of poverty and reduce severe, persistent inequalities that are symptoms of poverty without mobility.

V. Integrating competition law and policy with the SDGs

Once we understand the critical importance of outsider-friendly antitrust to counter poverty, promote dignity and nurture inclusive development, the claim of conflict between antitrust and SDGs takes a different complexion. Human values are at stake when we suppress markets or stand by while dominant firms do so. In this section, I address proposals for antitrust exemptions and compromises in the name of SDGs, which might be largely wrong-headed.

The UNCTAD Secretariat Note suggests that, to bring competition law into sympathy with the SDGs, fairness should be a major ingredient of competition law and policy, and exemptions from antitrust law should expand. For example, it proposes that exemptions should be granted “for agreements that promote economic progress, environmental protection and green technologies.”²⁷ I will show that exemptions are not needed for economic progress, because economic progress is an efficiency concept embedded in competition analysis, and that applications of competition law seldom conflict with environmental and other SDG values.

This section is, in other words, about compromise of antitrust principles to achieve notionally higher goals that help the poor. There are three perspectives on whether and how SDG

²⁶ What does outsider-friendly antitrust entail? It does not entail protecting inefficient firms from competition. The answer is fact-sensitive. It can best be appreciated in the context of facts. In my essay *The Efficiency Paradox* – *see supra* note 25 – I presented four cases that, I argued, the Court resolved by incorporating incumbent-friendly presumptions into its analysis. If the Court had resolved each dilemma in the other direction, it would have expressed an outsider-friendly antitrust.

²⁷ UNCTAD Secretariat Note, *supra* note 6, at 1.

goals require compromise of antitrust principles. Option one commands the support of much of the antitrust bar in the two most prominent jurisdictions (the US and the EU). The Secretariat Note adopts Option 2. I shall argue for Option 3.

These are the options:

1) Under Option 1, antitrust law is conceptualized as “efficiency” or “consumer welfare” law: It promotes aggregate efficiency or (more honestly, and much more modestly) would step in only to protect consumer surplus from erosion by non-efficiency justified conduct.²⁸ Supporters of this option argue: The SDGs are about equity and non-efficiency goals. Embracing non-efficiency considerations undermines efficiency. As well, it opens the door to unbridled discretion of officials and jurists, inviting politics and cronyism and further undermining efficiency. Antitrust policy-makers should not be seduced into compromises with amorphous notions of equity. Moreover (advocates continue), economic disciplines can be used to solve problems of environmental protection (for example) more efficiently than can antitrust exceptions, as in cap-and-trade pollution permits.

2) According to supporters of Option 2, the SDGs are higher goals or values than efficient markets, and antitrust should give way flexibly, as needed, to serve them.

3) According to Option 3, open markets and access to markets are critically important tools for efficiency, opportunity, mobility, and economic well-being, and for advancing most of the SDG agenda. It is rarely necessary to sacrifice the market goals in order to facilitate SDG goals, and indeed, in view of the value of markets and access to them in aiding and empowering the poorer population, one should be reluctant to sacrifice markets to advance goals best addressed by other means.

²⁸ See Fox, The Efficiency Paradox, *supra* note 25.

I have outlined the tenets of Option 1 in the paragraphs above. I shall focus next on Option 2 and its implications. In doing so, first, I explore the use of exemptions to accommodate antitrust to the SDGs. Second, I explore antitrust flexibility to include fairness, and I explore the claim that “unfairness” should be incorporated as a dimension of anticompetitiveness. Third, I treat the agriculture sector, which is highlighted in the SDGs and the Note, given its place at the epicenter of global poverty. Fourth, I consider other public interests.

Exemptions. A semantic confusion has produced a distorted view of conflicts between antitrust law and the SDGs and thus of the need for more exemptions from antitrust.

There is a threshold issue. A semantic problem has crept into the law that creates an appearance of conflict between antitrust and economic progress where none exists. The problem stems from the wording and structure of the competition law of the European Union, which has been duplicated in the law of many jurisdictions. The wording of the relevant European Treaty article, now TFEU²⁹ Article 101(1), is so broad that, as a first step, the competition prohibition catches all agreements that “distort competition” broadly conceived. Under Article 101(3), Article 101(1) may be declared inapplicable to agreements that promote economic progress where consumers get a fair share of the benefits. Article 101(3) has commonly been referred to as an “exemption” from antitrust, but it is more precisely a mode for completing the analysis of whether the agreement is good or bad for competition and consumers. Since 2004, when the European Union devolved powers of enforcement of the Treaty’s competition law to the Member States, a European Commission “exemption” for 101(3)-compliant agreements has no longer been necessary or even available; but the vocabulary of “exemption” persists.

²⁹ Consolidated Version of the Treaty on the Functioning of the European Union, Oct. 26, 2012, O.J. (C 326) 1.

Perhaps this terminology will live on because history runs deep; Article 101 has had a powerful impact on the world. Many nations have copied its language. This requires an alertness to distinguishing an Article 101(3) exemption (which simply allows agreements that are good for consumers) from an endorsement of anticompetitive, consumer-harming agreements for the sake of non-market goals. This means that we do not need an exemption from antitrust law for agreements that promote economic progress, because antitrust law does not prohibit such agreements. We turn, then, to possible exemptions to advance non-market goals.

An antitrust exemption *is* needed when an agreement or conduct harms competition (including efficiency and innovation) but society wants to endorse it anyway to serve a higher value such as health, the environment, or easing the plight of farmers. When one analyzes carefully to determine whether an agreement is anticompetitive, one finds very little conflict between antitrust and (other) social goals.

But let us suppose that an agreement *is* anticompetitive and the claim is made that the agreement is nonetheless “good” because it will protect the environment. The inquiry in these paragraphs is whether the agreement will really protect the environment, and whether the sacrifice-competition tack is the best tool to address the environmental problem.

We consider two cases. The first is the EU case, CECED.³⁰ The washing machine manufacturers decide that cheaper washing machines are environmentally unsound and the manufacturers agree not to market the cheaper machines. This is a cartel. It is an agreement among competitors to take low-priced machines off the market. It would cause the price of

³⁰ The Commission exempted the agreement in CECED. Commission Decision, Case IV F 1/36.718 CECED, O.J. (L 187) 47 (July 26, 2000). This is an older case and, since its issue, the Commission has been unsympathetic to the claim that non-competition goals, are relevant in the Article 101(3) analysis. *See, e.g. Communication from the Commission – A pro-active Competition Policy for a Competitive Europe*, at 7 (paragraph 3.1), COM (2004) 293 final (Apr. 20, 2004) (indicating a “stronger emphasis on economic analysis,” which “shifts the focus firmly to the economic effects of firm behaviour or of government measures.”)

washing machines to rise. Even the price of the higher-end machines would probably rise, reflecting the new market power of the collaborators (because they gain market power when they act together). Is the price-effect a tolerable by-product of environmental protection? Are we confident that the washing machine manufacturers correctly identified, and took off the market, only environment-harming machines? Are we worried that, given their interest in profits, the manufacturers might have overstated the category of “environmentally unsound” machines? Does the price-level cut made by the manufacturers directly correspond with the environmental harm? In this case, like so many others, there was an alternative course to protect the environment. Manufacturers could have promoted their environment-friendly machines to consumers as a feature consumers may want and be willing to pay for. Also, they – and environmentalists – could have sought legislation that would raise washing machine standards. In this competition case, exceptionally, the European Commission exempted the agreement from antitrust. But CECED is old and weak precedent and not a signal that the Commission would approve such a competitors’ agreement again.

The second example is the Chicken of Tomorrow. The Chicken of Tomorrow was an industry-wide agreement of Dutch suppliers and supermarkets to improve animal welfare and the environment by agreeing to minimum standards for raising chickens – slower breeding (more breeding days), less crowded barns, and more dark hours. The supermarket parties agreed to completely replace all chicken in their bins with the higher-priced product. The Dutch competition authority investigated how much consumers were willing to pay for more animal welfare. It treated the agreement as exemptible if consumers sufficiently valued the gains in animal welfare. It found that consumers did value animal welfare but not sufficiently to pay the

increased costs, and it denied an exemption.³¹ Had consumers been willing to pay for the increased costs of the Chicken of Tomorrow, presumably an exemption would have issued from the national competition authority. (Compatibility with EU law would have remained an issue.)

This agreement, too, was a cartel. It predictably would raise prices – probably above the incremental costs of the enhanced animal welfare, capturing cartel-power profits that would probably become available by the cut-back in output. Presumably, environmentally-conscious chicken breeders could win the loyalty of environmentalist/consumers by advertising the chicken-welfare virtues of their methods – as many breeders do now. If consumers want to pay for better treatment of the chickens they ultimately eat, they can do so without an industry agreement. But the breeders and sellers could force the higher standards on unwilling buyers if they combined – which surely must have been a reason for the agreement. Is the sellers’ agreement a useful and effective way to set good national standards? Should we tolerate the sellers’ conduct in shutting out suppliers of cheaper chickens to poorer consumers? I would answer, No. *Legislation* regulating barnyards in the interests of animal welfare would have more legitimacy, and probably broader coverage, if they were adopted by the people rather than by conflicted market players.³²

³¹ **Johan – can you add a direct cite to the Dutch authority?** See Jan Peter van der Veer, *Valuing Sustainability? The ACM’s analysis of “Chicken of Tomorrow” under Art. 101(3)*, KLUWER COMPETITION LAW BLOG (Feb. 18, 2015), <http://kluwercompetitionlawblog.com/2015/02/18/valuing-sustainability-the-acms-analysis-of-chicken-for-tomorrow-under-art-1013/>.

³² The antitrust objection is not to the industry’s discussing best practices or and even agreeing to best practices. The antitrust objection is to the rivals’ agreement not to deal in the lower-priced product. From a public policy point of view, the industry is not best placed to make the trade-off between more animal welfare and lower prices, nor to enforce this result by agreement. The competitors have a conflict of interest. For a US case disallowing a competitor self-help agreement to take “pirated” fabric and clothing designs off the market, see *Fashion Originators Guild v. FTC*, 312 U.S. 457 (1941). See also *FTC v. Superior Court Trial Lawyers Ass’n*, 493 U.S. 441 (1990).

The Chicken of Tomorrow and CECED are cautionary tales. They suggest caution in relaxing antitrust to save the animals and the environment. Relaxing antitrust is seldom an efficient tool to achieve social goals, while cartels *are* efficient tools for raising prices.

But what if exemptions are necessary to protect the welfare of those people who are least well off or those who have no bargaining power against powerful business? The agricultural industry is an example, which I consider below after a discussion of “fairness.”

Fairness: Fair competition; fair bargaining

Should competition laws embrace a principle of fair competition, and would extension of the scope of competition laws to prohibit unfair competition increase the compatibility of antitrust with the SDGs in a helpful way?

The concept of *fair competition* is often at odds with the hard competition valued by the competition laws. First, we must define terms, for “fair competition” is an ambiguous phrase. If fair competition means that efficient firms must pull their punches so as not to harm their higher-costs rivals, fairness to competitors injures consumers. The disruptive competition of UBER and Airbnb is overwhelmingly perceived as unfair by taxi drivers and hotels, respectively, yet UBER, Airbnb and their likenesses are among the greatest contributors to dynamic competition that helps non-elite buyers and even workers looking for jobs.³³

It is neither necessary nor desirable to embrace an amorphous rule of fairness in order to bring antitrust into sympathy with the SDGs. There are, however, facets of fairness that map onto efficiency and thus instances of no need to relax antitrust to achieve both goals. An example is, as suggested above: an antitrust perspective that gives regard to competition on the merits by

³³ Disparities in coverage of regulation can be unfair. This problem should be addressed by better regulation and deregulation.

people without power (e.g., disallowing use of leverage by dominant firms to close opportunities of outsiders to contest the market). Application of this outsider principle can facilitate efficient inclusive development and thus promote the goals of the SDGs.³⁴

The fact that “fairness” can have meanings that are 180 degrees apart signals the danger in proposing generally that fair competition should be a goal of competition law.

Unfair bargaining. Unfair bargaining is a specific form of unfairness, usually associated with exploitation of buyers or sellers. In developing countries, markets often work poorly, and both suppliers and buyers may be exploited. Massive disparities in bargaining power that predictably result in exploitation may go to the heart of the SDGs, particularly when prices are so high that the poorer people cannot afford the necessities of life.

Most countries follow the European model of competition law against excessive pricing. Yet competition authorities typically do not want to become price regulators; they are trying to free the market, not control it; and there is much debate on the appropriate trigger for an excessive pricing violation. When are prices “excessive”?

If prices are excessive, it can also be said that that sellers have “too much” bargaining power or that sellers are unfairly using their bargaining power; thus the title of this subsection. But despite the language of fairness, we should note that monopoly pricing is a quintessential

³⁴ An aspect of this approach was taken by the South African Competition Tribunal. *See Nationwide Poles v. Sasol (Oil) Pty Ltd.*, case 72/CR/Dec03 (Competition Tribunal 2003) (condemning unjustified price discrimination by a dominant firm that squeezed a small firm out of the market). But this holding was reversed by the Appeal Court. 49CACA April 05 (Competition App. Court 2005) (S. Afr.) (holding that the statutory text did not support the finding of a violation; the favored (big) buyers competed against one another and the disfavored firm did not prove harm to competition).

market harm, not just an “unfairness” harm. High price signals low output, which signals too few resources flowing into the market; thus allocative inefficiency. Efficiency and fairness coincide.

South Africa is one of the prominent jurisdictions working out the standards for when a price is excessive and should be condemned by competition law. When multinational producers of HIV/AIDS drugs sold them in South Africa at the height of the AIDS crisis for a prohibitive price per pill that none but the very rich could afford, a public interest NGO sued the pharmaceutical producers under the South African competition law and won their case by default when the firms refused to open their books to inspection. The pharmaceutical firms settled the case by agreeing to license generic producers.³⁵

Also in South Africa, Mittal, the supra-dominant post-statal steel producer, persisted in selling steel in the domestic market at more than import parity (foreign import price, including the large transportation cost) to its many South African customers that needed steel as an input, while selling the steel for export at the much lower world price. The high domestic price threatened to cripple the competitiveness of a large swath of South African businesses. A South African customer sued. The Competition Tribunal found an abuse of dominance based largely on the skeletal case sketched above plus the availability of a self-executing remedy – prohibiting Mittal from segregating sales for export from sales for the domestic market. This ingenious relief would have meant that more of the domestically-produced steel would naturally be available for the domestic market and the greater domestic supply would push prices down. By this simple template, the Tribunal avoided the quagmire of determining Mittal’s cost and its

³⁵ The *Hazel Tau* case, as recounted in *Generic Pharmaceuticals*, Note by South Africa to the OECD Competition Committee, DAF/COMP/WD(2014)68 (June 5, 2014), at point 2.1, available at [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/WD\(2014\)68&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/WD(2014)68&docLanguage=En).

margin of price above cost. It thus identified a manageable formula for applying the excessive pricing law; simplicity being especially welcome in developing countries where scarcity of resources is an enemy of enforcement. The Competition Appeal Court reversed and remanded, finding the skeletal case insufficient to meet the letter of the South African law.³⁶ We might nonetheless regard the Tribunal's formulation as an inspiration and possible guide to solving challenges in this important area where fairness meets efficiency.

U.S. antitrust does not have an excessive pricing provision. It would leave price levels to contract law and the discipline of the market. Excessive pricing prohibitions are typically treated derogatorily as instruments of wealth distribution, and as inefficient.³⁷ For systems of antitrust that insist on allocative goals only and insist that distributive goals undermine efficient allocations,³⁸ the reach of antitrust to fairness in bargaining is seen as just one more point of conflict between antitrust and the SDGs.

Agriculture

Agriculture is a critical sector. In many of the poorest developing countries, more than 70% of the population live in rural areas and depend on agriculture for their livelihood, and most of this agrarian population lives in deep poverty. If the SDGs are to be addressed, the plight of the small-hold farmers must be on the agenda.³⁹ Agriculture is a prime example of atomized suppliers and concentrated buyers, with huge vertically-integrated multinational agribusiness. The disparate bargaining power and thus extreme vulnerability of small farmers, often in a

³⁶ *Harmony Gold Mining Company Ltd. v. Mittal Steel Corp.*, Case No. 13/CR/Feb 04 (Competition Tribunal 2007), *rev'd*, Case No. 70/CAC/Apr 07 (Competition App. Court 2009) (S. Afr.).

³⁷ But see Harry First, *supra* note 23.

³⁸ This hypothesis has been deeply undermined. See *infra* notes 43-4.

³⁹ See Kofi Annan and Sam Dryden, *Food and the Transformation of Africa: Getting Smallholders Connected*, FOREIGN AFF., Nov./Dec. 2015, at 124.

politicized atmosphere populated by vested interests, is addressed in many jurisdictions by antitrust exemptions.

While the market problems are daunting, the European Union provides an example of a wise approach that marries efficiency and fairness. Rules specify the conditions under which farmers may sell jointly and may jointly set prices within a space exempt from antitrust prohibitions. The conditions for exemption specify that, to gain the benefit of the exemption, the farmers must be cooperating in integrated organizations. They may integrate in many ways; for example, by sharing equipment and storage facilities, procuring inputs jointly, sharing transportation facilities, jointly distributing their product, and jointly assuring quality control. The integrated activities are expected to yield efficiencies. To guard against creation of market power, the volumes marketed by each cooperative may not exceed certain thresholds, thus guaranteeing competition among the cooperatives.⁴⁰

This is an example of an exemption that need not be called an exemption because collaborations within the conditions specified do not undermine competition. The rules steer transactions onto a competitive path. There are sufficient groups of farmers to wage effective competition with one another. The rules are clear, and they give certainty to the farmers as to what they can and cannot do. The cooperative groupings are integrated joint ventures, which produce efficiencies. The competition among the cooperating groups tend to assure competitive

⁴⁰ See speech by Alexander Italianer, then Director-General, European Commission, Co-operating to Compete: The New Agriculture Antitrust Guidelines, Brussels (March 4, 2015), available at http://ec.europa.eu/competition/speeches/text/sp2015_02_en.pdf.

outcomes for consumers. The EU rules are not exemptions to protect inefficient farmers from competition,⁴¹ which would be an entirely different story.

While the agriculture sector is often invoked as a demonstration of needed exemptions, as it is in the Secretariat Note, it may be more constructively invoked as a piece of a positive enforcement agenda. We may ask: What can antitrust law do to protect the agricultural sector from restraints that harm competition in ways that exemplify the SDG concerns? A list quickly emerges: 1) Antitrust can protect the farmers from world input cartels, such as the fertilizer cartel. But there is a hitch. The practical problem is that the farmers in poor countries with under-resourced agencies are generally powerless to protect themselves by antitrust action against the colluding multinational firms, and there is no world antitrust regime to help them even against these admittedly most heinous restraints. 2) Antitrust can protect the farmers from monopsonistic strategies that abusively exploit patent rights and prevent low-cost efficient use of seeds, a strategy once attributed to Monsanto by the U.S. Department of Justice, which dropped charges.⁴² Moreover, the US agencies would protect only Americans, not the larger masses of American firms' victims in developing countries. 3) Antitrust can protect farmers from mergers that significantly increase buying power, as in Bayer's proposed acquisition of Monsanto.⁴³ But,

⁴¹ See Juan David Gutiérrez R., *Agricultural Exemptions to Competition Law*, 6 REV. DERECHO COMPETENCIA. BOGOTÁ 173 (2010) (Colom.).

⁴² See Peter C. Carstensen, *The mixed record of the Obama administration in food competition policy leaves many unresolved issues: "Talking the talk, but not walking the walk,"* 03 Concurrences No. 1 2016, para. 24-28; Tom Philpott, *DOJ Mysteriously Quits Monsanto Antitrust Investigation*, MOTHER JONES (Dec. 1, 2012), <http://www.motherjones.com/tom-philpott/2012/11/dojs-monsantoseed-industry-investigation-ends-thud>.

⁴³ See, e.g. John Kennedy, *Former DOJ Officials Warn Against Bayer-Monsanto Merger*, LAW 360 (Aug. 3, 2016), <http://www.law360.com/articles/824584/former-doj-officials-warn-against-bayer-monsanto-merger>. See, for an example of buying power squeezing farmers in the West African cocoa market, Michael D. Wilcox and Philip C. Abbott, *Market power and structural adjustment: the case of West African cocoa market liberalisation*, paper presented at the American Agricultural Economics Association Annual Meeting (Aug. 1-4, 2004), available at <http://www.agecon.purdue.edu/pdf/Wilcox%20Abbott%20-%20Market%20Power%20and%20Cocoa%20Markets.pdf>. For another, more recent example of concern about increased power in global food chains, see e.g. Ioannis Lianos, Dmitry Katalevsky and Alexey Ivanov *The Global Seed Market, Competition Law and Intellectual Property*

for these mega-mergers that create buying power abroad, Western enforcers typically find no harm to their own consumers, or no harm that cannot be cured by a spin-off; and harm to the upstream suppliers abroad is “not their problem.” Thus, the authorities around the world typically approve mergers that further squeeze even efficient farmers, and the harmed nations and their peoples have no practical power to defend their markets.

The right result, for fairness and efficiency, does not require a bending of antitrust. It requires regard for a poor and powerless constituency that is hurt by antitrust harms. Some would say it requires altruism (allowing victims abroad the right to invoke the predator’s law). Altruism is good but rare. But a remedy for these antitrust harms does not even require altruism. A holistic pro-market solution is efficient for the world.⁴⁴ Yet there is no world antitrust law to protect the vulnerable small suppliers from buying-power-creating mergers, and none is on the horizon. Can we not try harder to embrace the efficient market solutions that advance the SDGs?

Public Interest: Jobs and SMEs

I have reflected on several public interests in the discussion of exemptions. I add here the interest of workers in jobs and the interest of small suppliers in markets. Many jurisdictions allow or mandate consideration of public interest in merger laws. Whether such laws are wise is vigorously debated, but they exist. Antitrust laws of many jurisdictions would never have been enacted without public interest clauses.

Rights: Untying the Gordian Knot, Centre for Law, Economics and Society Working Paper Series, Feb. 2016, University College London, <https://www.ucl.ac.uk/cles/research-paper-series/research-papers/cles-2-2016>.

⁴⁴ See Eleanor M. Fox and Janusz A. Ordover, *The Harmonization of Competition and Trade Law—The Case for Modest Linkages of Law and Limits to Parochial State Action*, 19(2) WORLD COMPETITION 5 (1995).

I observe here two lessons from South Africa, whose antitrust law requires consideration of public interests. First, many mergers entail large layoffs, and a number of South African merger decrees require that the merging parties provide or fund job retraining for the individuals laid off.⁴⁵ The merger has imposed a cost on the society (and indeed a society in which half the young people are jobless), and the merging parties are simply asked to pay a part of the cost they created – ameliorating the plight of vulnerable individuals and helping them to help themselves.

Second, displacement of small suppliers may be a looming issue, as it was in South Africa’s Walmart/Massmart merger. The Tribunal and Appeal Court cleared the merger subject to conditions. The conditionality did not require quotas or buy-national agreements, but required Walmart to provide and stakeholders to administer a large fund for capacity building of the small suppliers. The mandated capacity-building entailed training people and transferring knowledge with a view to grooming the small suppliers to join a global value chain.⁴⁶

Both examples from South Africa merger jurisprudence are market-friendly links to the SDGs. Other public interests are incorporated by a variety of jurisdictions; not always in market-friendly ways and not always for SDG-friendly ends. Those moves and measures are beyond the scope of this essay except as readers may regard the essay as part of the call to consider market-friendly routes.

VI. A Return to Options 1 and 3: Against Technocratic Silos

We return here to Option 1 (“not my problem”) and its tension with Option 3 (adopt outsider antitrust, which may solve the problem in market-friendly ways). This essay contests the

⁴⁵ See, e.g. *Metropolitan Holdings Ltd. v. Momentum Group Ltd.*, Case No: 41/LM/Jul10 (Competition Tribunal 2010) (S. Afr.).

⁴⁶ *In re SACCAWU and Massmart Holdings Ltd.*, Case No. 110/CAC/Jul11 (Competition App. Court 2012) (S. Afr.).

notion of antitrust as a technocratic silo that admits no notion of fairness or better distribution of wealth and opportunity.

I have already argued for outsider antitrust. I do not argue that antitrust so constructed will suddenly lift a billion people out of poverty. But outsider-antitrust does mean that markets hold great potential to empower people with no resources or connections, that market (competition) policy can help ease their way, that antitrust law can control perverse uses of economic power that obstruct their way, and that, in fact, to accomplish these ends, there is no good substitute for markets.

In these paragraphs I have spoken of poverty, equity, inclusiveness, reducing inequality, and forging tighter links between antitrust and the SDGs. Supporters of Option 1 object: Antitrust is about efficiency and SDGs are about equality. The twain do not meet. We cannot pursue equality without diminishing efficiency.⁴⁷ We will end up protecting competitors, not competition, and making us all worse off.

This notion passed as common wisdom for at least 40 years: equity undermines efficiency. The bible was Arthur Okun's book *EQUALITY AND EFFICIENCY: THE BIG TRADE-OFF*, published in 1975. The hypothesized trade-off has been deeply undermined, if not proved wrong, by contemporary scholarship, emanating from the IMF and the World Bank.⁴⁸ Especially in developing countries where masses of the population have been artificially excluded from

⁴⁷ See Ayn Rand, *ATLAS SHRUGGED* (1957) (contradictions do not exist; equity undermines efficiency).

⁴⁸ See Andre G. Berg and Jonathan D. Ostry, *Equality and Efficiency: Is there a trade-off between the two or do they go hand in hand?*, 48(3) *IMF FIN. & DEV* (Sept. 2011), <http://www.imf.org/external/pubs/ft/fandd/2011/09/berg.htm>. See also Federico Cingano, *Trends in Income Inequality and its Impact on Economic Growth*, OECD Social, Employment and Migration Working Papers No. 163, 2014, <http://dx.doi.org/10.1787/5jxrjncwvxv6j-en>.

mainstream economic life, it may be *necessary* to do equity to gain efficiency. There is no efficiency without equity.⁴⁹

Moreover, as time goes on, it becomes increasingly clear that the immutable science that underlay Chicago School economics is neither immutable nor science.⁵⁰ It was based on presumptions that favor incumbents and others who are well enabled. Outsider antitrust would shift presumptions and perspective. It would privilege market entry and inclusion over freedom for firms with economic power. The outsider presumption (protect the market path of outsiders) is surely equally efficient in terms of production and invention in the world.⁵¹ It is likely to be more efficient in terms of the promise of development in developing countries – drawing more effectively on the countries’ human capital. Antitrust *can* nod towards equity and inclusion, and efficiently so. Markets, safeguarded by outsider antitrust, are an engine for the SDGs.

CONCLUSION

Markets empower people to help themselves. Markets and access to markets stand side-by-side food, health, shelter, education, environment, infrastructure, and institutions as critical tools to combat the world’s greatest economic deprivations. Making markets work for people without power is an inherent SDG.

⁴⁹ See Santiago Levy and Michael Walton eds., *NO GROWTH WITHOUT EQUITY: INEQUALITY, INTERESTS, AND COMPETITION IN MEXICO* (The World Bank & Palgrave MacMillan, 2009).

⁵⁰ See Robert Pitofsky ed., *HOW CHICAGO SCHOOL OVERSHOT THE MARK*, (Oxford University Press, 2008) (collecting essays by numerous experts from a range of political policy perspectives uncovering the intrinsic biases of Chicago School economics).

⁵¹ See note 10, *supra*.

IS ANTITRUST'S CONSUMER WELFARE PRINCIPLE IMPERILED?

Herbert Hovenkamp*

Abstract

Antitrust's consumer welfare principle urges that antitrust policy should encourage markets to produce output as high as is consistent with sustainable competition, and prices that are accordingly as low. Such a policy does not protect every interest group. For example, it opposes the interests of cartels or other competition-limiting associations who profit from lower output and higher prices. It also harms less competitive firms that need higher prices in order to survive. Market structure is relevant to antitrust policy, but its importance is contingent rather than absolute – that is, market structure is a concern when it facilitates reduced output or innovation or leads to higher prices.

Antitrust's consumer welfare principle is currently navigating between two hazards, both of which threaten the importance of low prices as an antitrust goal. On the right is a general welfare approach best identified with Robert Bork that would permit efficiency claims as an antitrust defense even when the challenged practice leads to higher prices and causes consumer harm. On the left is an emergent “neo-Brandeisian” approach that often regards low prices as the enemy, at least when they come from large firms at the expense of higher cost rivals.

In both cases, the full story is more complex. The general welfare approach as Robert Bork presented it was built on a strong faith that various practices produced cost savings or other efficiencies, whether provable or not, as well as considerable doubt that a large menu of practices caused genuine competitive harm. In the process it also approved an approach to antitrust that was very difficult to administer and underdeterrent over a wide range of practices.

By contrast, a central claim of the Neo-Brandeis approach is that markets are fragile, threatening monopoly nearly everywhere. Further, antitrust policy should be driven more by political theory rather than economics. While political voices are diverse, making it difficult to identify a single theme, one clear consequence is greater protection for small businesses with higher costs. For example, they point with admiration to one of antitrust's greatest acknowledged disasters, the Robinson-Patman Act. One serious problem facing the neo-Brandeis movement is lack of transparency. The attack on low prices as a central antitrust goal will harm consumers, and vulnerable consumers are most at risk. Politicians who embrace its concerns are likely to be harming their own constituencies, and that could spell political suicide.

Much of the debate about the appropriate role of antitrust in the economy comes down to identifying the driver behind firm size. Why do firms become large? For the neo-Brandeis movement, just as for the progressive critique a century earlier, the driver was politics and lax legal policy, including deficient antitrust enforcement. For more centrist antitrust, the principal driver has been technology and innovations in distribution – although coupled with a certain amount of anticompetitive practice.

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Introduction

Under the consumer welfare principle antitrust policy encourages markets to produce output as high as is consistent with sustainable competition, and prices that are accordingly as low. Such a policy does not protect every interest group. For example, it opposes the interests of cartels or other competition-limiting associations who profit from lower output and higher prices. It also runs contrary to the interest of less competitive firms that need higher prices in order to survive. The consumer welfare principle believes that market structure is relevant to antitrust policy but that its importance is contingent rather than absolute – that is, market structure is a concern when it facilitates reduced output or innovation or leads to higher prices.¹

Antitrust policy under the consumer welfare principle is currently navigating between two hazards. What they share in common is that both denigrate the importance of low prices as an antitrust goal. On the right is a general welfare approach best identified with Robert Bork that would permit efficiency claims as an antitrust defense even when specific efficiencies cannot be proven and the challenged practice leads to higher prices that cause consumer harm. On the left is an emergent “neo-Brandeisian” approach that often regards low prices as the enemy, at least when they come from large firms at the expense of higher cost rivals.

The full story is more complex. Few antitrust outcomes have depended on the choice of a welfare test. Much more significant were the ways in which evidence of competitive harm and offsetting efficiencies were credited. Along with his general welfare approach came Bork’s strong faith that various practices produced cost savings or other efficiencies, whether or not these were provable, as well as considerable doubt that these practices caused genuine competitive harm.² By contrast, a central claim of the Neo-Brandeis approach is that markets are fragile, with the threat of monopoly everywhere. Further, antitrust policy should be driven more by political theory rather than economics. While political voices are diverse, making it difficult to identify a single theme, one clear consequence is greater protection for small business. To date, the strongest claim of the neo-Brandeis movement remains unverified; that is its assumption that individuals in our society are really better off if they lived in a world characterized by smaller firms and higher prices. Everyone in society is a consumer and consumers vote mainly with their purchasing choices. The neo-Brandeisians still face the formidable task of providing evidence these

¹ See discussion *infra*, text at notes __; and Herbert Hovenkamp and Carl Shapiro, *Horizontal Mergers, Markets Structure and Burdens of Proof*, 127 YALE L.J. 1996 (2018).

² See discussion *infra*, text at notes __.

citizens would be better off in some way in a world of higher cost smaller firms, their market behavior notwithstanding. Further, the neo-Brandeis movement at this writing has not provided much in the way of a calculus for determining how these goals should be metered or applied to specific practices, other than highly general ones of the nature that Amazon should be regulated in some fashion.³

The “Welfare Tradeoff”

Forty years ago, Robert H. Bork published *The Antitrust Paradox*, which argued forcefully that antitrust policy should be driven by something he called a “consumer welfare” principle.⁴ However, Bork did not use the term “consumer welfare” in the same way that most people use it today. For Bork, “consumer welfare” referred to the sum of the welfare, or surplus, enjoyed by both consumers and producers, or perhaps even by all of society. Bork referred to consumer welfare as “merely another term for the wealth of the nation.”⁵

When economists speak of “welfare,” they typically mean Pareto efficiency, Kaldor-Hicks efficiency, total surplus, or some closely related concept of “general” welfare.⁶ What these concepts share is that welfare includes the surplus, or wealth net of costs, enjoyed by all those affected, including producers and consumers as well as others. For example, under Kaldor-Hicks efficiency, sometimes called potential Pareto efficiency, a move is efficient if all gainers gain enough to compensate all losers fully, leaving them indifferent.⁷ Actual compensation is not required, but only that the gains be sufficiently large to produce compensation necessary to make everyone either a winner or indifferent. Bork essentially adopted a version of this conception of welfare, except that he misnamed it “consumer welfare.”

Bork’s idiosyncratic and controversial nomenclature launched a significant debate about economic welfare tests as goals of antitrust policy.

³See Lina Khan, *Amazon’s Antitrust Paradox*, 126 YALE L. J. 710, 797-801 (2017). See also discussion *infra*, text at notes ___.

⁴ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 66, 97 (1978).

⁵*Id.* at 90. See also Alan J. Meese, *Debunking the Purchaser Welfare Account of Section 2 of the Sherman Act*, 85 N.Y.U. L. REV. 659, 691 (2010) (observing that Bork equated “consumer welfare” with “society’s total welfare”); Barak Y. Orbach, *The Antitrust Consumer Welfare Paradox*, 7 J. COMPETITION L. & ECON. 133, 148 (2011) (“Bork explicitly equated the term ‘consumer welfare’ with ‘the wealth of the nation,’ a term that economists would understand as ‘social welfare’”)

⁶E.g., GREGORY MANKIW, *PRINCIPLES OF ECONOMICS* 134-155 (8th ed. 2016).

⁷E.g., ALAN DEVLIN, *FUNDAMENTAL PRINCIPLES OF LAW AND ECONOMICS* 29-33 (2015).

On one side are those who espoused a so-called “general welfare” test, which maximizes the aggregate welfare of all of those who are affected by a particular practice.⁸ While such tests come close to Bork’s test they are not quite the same: Bork’s concept of “consumer welfare” included the sum of welfare enjoyed by producers and consumers, but he paid little attention to the welfare effects on third parties.

In contrast to general welfare tests, consumer welfare looks at only one blade of the scissors. If consumers lose from a practice, then it is counted as inefficient, or anticompetitive, even if the consumer losses are completely offset by producer gains. The consumer welfare model articulates the goal of antitrust as higher output, and thus lower prices. In the classic example, suppose a merger of two large firms creates significant market power, raising prices by \$1,000. This merger also produces savings in production costs of \$1,200. In this case producer gains from productive efficiency exceed consumer losses. This merger would be approved under Bork’s standard because it produces net gains. It would be unlawful under a consumer welfare standard, however, because it produces actual consumer losses and we disregard the producer gains. The most salient characteristic of this merger analyzed under a consumer welfare test is that it reduces output and raises prices.

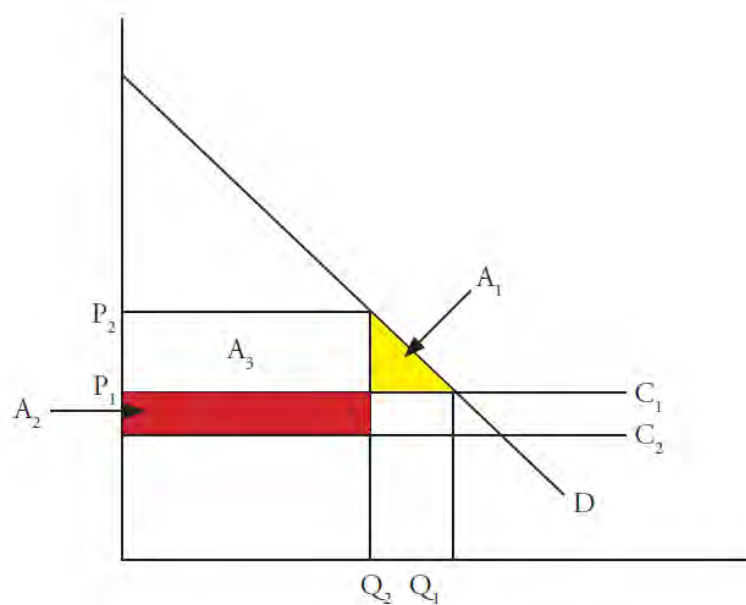
These various welfare tests have become a kind of “holy grail” for mainstream antitrust ideology. One advantage claimed for them is that they promise antitrust solutions that are free of excessive ideology or bias induced by special interests. They perform as a sort of analogue to the competitive market in economics. Nevertheless, very considerable bias can show up in the choice of a welfare test or the way in which it is applied. No welfare test can eliminate the exercise of judgment in competition policy.

One important difference between general welfare and consumer welfare models is that the former are said to require a welfare “tradeoff” between producer gains and consumer losses.⁹ In a highly influential article Oliver E. Williamson presented one of the most reproduced diagrams in the competition policy literature, which illustrated this tradeoff:¹⁰

⁸*E.g.*, Meese, *supra* note __;

⁹While the consumer welfare model does not require such a tradeoff, it may in some circumstances require a kind of balancing to determine whether the resulting price will be higher or lower. This is not a welfare tradeoff, however, and compares only upward and downward pricing pressure.

¹⁰Oliver E. Williamson, *Economies as an Antitrust Defense: the Welfare Tradeoffs*, 58 AM. ECON. REV. 18, 21 (1968).

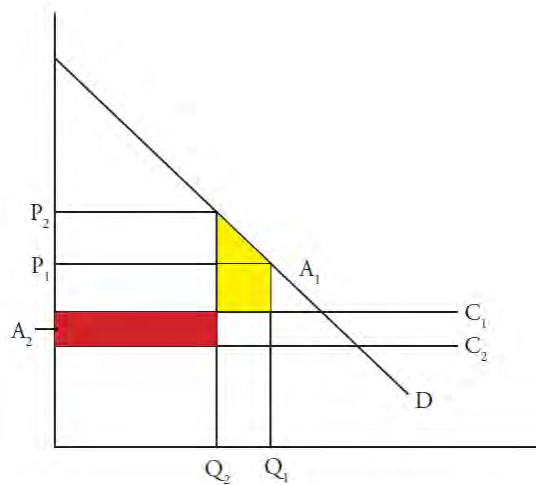


This figure, which is patterned after Williamson's, illustrates a market that was competitive prior to a merger, joint venture, or other antitrust practice that simultaneously produces market power and cost savings. Prior to this event, the market was competitive, with price (P_1) equal to cost (C_1). The merger did two things simultaneously. First, it created market power enabling the firms to raise their price to P_2 . Second, however, it produced efficiency gains facilitating a cost reduction to C_2 . In the figure, the triangle A_1 is the "deadweight loss," or efficiency loss, occasioned by the price increase and corresponding output reduction. Rectangle A_2 , by contrast, represents the gains in productive efficiency. Rectangle A_3 measures the higher prices paid by consumers, but these are a "wash" because they represent losses to consumers that are precisely offset by producer gains. Even though this merger raises prices, it is efficient if rectangle A_2 is larger than triangle A_1 . Williamson surmised that this might often be the case, and that relatively small efficiency gains could offset fairly large price increases, making the exchange welfare positive. Stated in this way, the case for a general-welfare test seems quite appealing.

Upon examination, however, the Williamson model exhibits important shortcomings. First, it presumes a market that was perfectly competitive prior to the merger and monopolized thereafter. The effect of pre-merger perfect competition is to minimize the amount of consumer harm because the lost sales are taken away from marginal consumers who place a very low value on the product. If price-cost margins were significantly higher prior to the merger (shifting Q_2 and Q_1 to the left), then the amount of wealth taken from consumers would be higher and the gains enjoyed by the

producers would be less because they would be spread over lower remaining output.¹¹ A merger or other antitrust practice such as Williamson illustrated, which shifted a market from perfectly competitive to monopolized, would be a very unusual event. In most cases where mergers, joint ventures, or related practices are conducive to the creation of market power, the market already exhibits high price-cost margins. Changing the assumption about pre-merger price-cost margins has an important impact on the relationship between

¹¹ This is illustrated in this figure:



It shows the same market as the first figure, and with a merger or other practice that produces the same per unit cost reduction. In this case, however, the market was already noncompetitive to begin with, reflecting prices (P_1) that were higher than cost (C_1). The yellow area represents two sets of losses. The upper portion is the traditional deadweight loss, which accrues to both consumers and producers. The lower portion is producer profit losses that result from the output reduction. In this case, unlike Williamson's example, output is being taken from consumers whose willingness to pay is higher in relation to the product's cost, and thus was producing greater pre-merger consumers' surplus. The lower portion of the yellow figure represents lost profits to the seller resulting from the output reduction. Second, because output is already lower to begin with, the efficiency gains resulting from a further output reduction are spread over a smaller number of units (the origin to Q_2). Even though the demand curve is identical to the one in the first figure and the per unit amount of the efficiency gains (the height of the rectangle A_2) is the same, it is now no longer clear that the "gain" area covered by the red figure is greater than the "loss" area of consumer deadweight loss + producer profit loss defined by the yellow figure A_1 . In general, the higher are the price-cost margins prior to the merger, the greater the efficiency gains that would be needed in order to offset these losses.

efficiency gains and consumer welfare losses.

Second, the efficiencies that accrue in the Williamson model must take place at lower output levels than prevailed prior to the merger. If the efficiencies are so substantial that they result in higher output, then there is no tradeoff. Consumers and producers would both benefit, and the merger would be approved under both a general-welfare and a consumer welfare test. Tradeoffs occur only in the area of output-reducing mergers. By far the biggest source of merger-generated efficiencies is economies of scale, but these generally occur at higher rather than lower output.

To be sure, some efficiencies can result from practices that reduce output. One example is plant-specialization economies that increase both single-plant scale economies and market power. For instance, prior to a merger Firm A and Firm B might have been producing forty units of Alpha and forty units of Beta in their respective plants, and these output levels may have been inefficiently low. By reorganizing production after the merger, the post-merger Firm AB might produce seventy units of Alpha in one of the plants and seventy units of Beta in the other one. Seventy units might be sufficient to attain productive efficiencies even though that is a lower number than the eighty units that were produced previously. Assuming the post-merger firm had some market power, prices would be higher. We would still have to ascertain whether the increase in productive efficiency resulting from the scale economy outweighed the harm to consumers caused by the ten-unit-output reduction. In any event, the merger alone would not receive this result. The post-merger firm would also have to reorganize its production by switching over portions of each plant. The costs of doing so could range from small to prohibitive depending on the technologies involved.

Other efficiencies may also occur at lower output levels, such as improvements in technology, management, or distribution or procurement, but one must always query whether an output-reducing practice such as a merger is really necessary in order to create such efficiencies. American antitrust merger policy requires that claimed efficiencies be “merger specific,” which means that they could not be attained except via the merger.¹² For other types of practices, such as joint ventures, the equivalent standard is whether there is a reasonably less restrictive alternative that could attain the efficiency but without creating the market power.

A third problem with the Williamson model was the assumption that the merger or joint activity in question created a single-firm monopoly that exercised its power unilaterally while other firms were unaffected. Many mergers and other practices challenged under the antitrust laws do not fall

¹²U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines* §10 (2010), available at <https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf>.

into this category. Rather, they create market power because they are thought to facilitate collusion.¹³ That is, by increasing market concentration or creating a dominant firm, they give rival firms in the market an incentive to reduce their own output or increase their prices as well. In such cases, however, the efficiency gains typically accrue only to the merging firm while the price increase affects the entire market. For example, if two 20% firms should merge into a 40% firm, the result might be that the market is more conducive to collusion or oligopoly price leadership. This would permit firms representing the remaining 60% of the market to raise their prices as well. In that case, however, the market-wide output reductions and resulting consumer injury would be experienced across the entire market, while only 40% experienced the efficiency gains. This would make the tradeoff much less favorable.

Finally is the administrability problem, which is one of the most serious impediments to antitrust general welfare tests. While application of any welfare test poses significant difficulties of measurement, in most close cases estimating consumer welfare effects is far easier than measuring general welfare effects that require a tradeoff.

In order to determine whether efficiency gains to producers exceed losses to consumers, we must measure the areas of rectangle A_2 and triangle A_1 in the picture and net them out. Measuring the efficiency gains requires that we know the size of the cost reduction achieved by this particular practice. That will give us the measurement $C_2 - C_1$, or the height of rectangle A_2 . Then, we must also know the output range, from the origin to Q_2 , over which the efficiencies occur. We will also have to identify what amount of the efficiency gain consists of fixed costs and what amount consists of variable costs; for only the latter will affect the price. For the tradeoff, we would also need to know the size of the post-merger price increase ($P_2 - P_1$), and the output reduction ($Q_2 - Q_1$) over which it would occur. That would give us the two legs of the deadweight loss “triangle.” Demand curves in the real world are never linear, however, meaning that area A_1 is not really a triangle at all. In that case, computing the size of the deadweight-loss area would require computing the location of the actual demand curve, in addition to the size of the two legs.

To the best of my knowledge, no American court has ever based a judgment on an attempt to make these computations and certainly not in any case where the tradeoff is reasonably close.¹⁴ Indeed, Bork himself described

¹³See *id.*, §7.

¹⁴Canadian law, which is more consistent with a general welfare test, provides one controversial decision. See *Comm’r of Competition v. Superior Propane Inc.*, 2003 FCA 53 (Can.); Daniel J. Gifford & Robert T. Kudrle, *Rhetoric and Reality in the Merger Standards of the United States, Canada, and the European Union*, 72

the problem of actual quantification of productive efficiencies in a specific case as “utterly insoluble.”¹⁵ Of course, not every case is close. If the merger or joint venture creates no market power, then there is nothing to trade off, so any efficiency gains whatsoever make the transaction positive. This is why a market power or market structure requirement is essential.¹⁶ The same thing is true in reverse if a merger creates market power but produces no measurable efficiency gains. Many other transactions have positive but small power effects or small production efficiency effects, or vice-versa. In these, computing welfare effects would not be difficult because it would not require much technical measurement at all.

In very sharp contrast, assessing the same transaction under a consumer welfare test is relatively easy. One needs to know whether output (Q_2 to Q_1) has gone down or price (P_1 to P_2) has gone up. That is the only issue to be considered, and the size of the output reduction or price increase does not matter. Further, there is nothing to trade off. Once we know that consumer prices have gone up it does not matter how large are the offsetting efficiency gains. In sum, an antitrust policy guided by output effects as a standard is far easier to administer than a general-welfare alternative.

This is not to say that evaluation of a merger or joint venture under a consumer welfare test is always easy. The hard cases are ones in which a merger or joint venture threatens the exercise of market power, but the defendants claim that the efficiency gains are so substantial that they will fully offset any threatened price increase, producing output that is at least as high as it was prior to the occurrence. This is the standard that the federal antitrust agencies currently apply in evaluating mergers.¹⁷ Nevertheless, the query is simply whether the price is likely to go up or down – much simpler than an inquiry into general welfare effects.

The Importance of the Consumer Welfare Test to Antitrust Policy

In comparison to any general welfare test, the administrative cost savings from a consumer welfare test seem to be substantial. But there may be other advantages as well. One problem with general welfare tests is that they tolerate a significant amount of market power in the economy. There is at least a temporal link between Bork’s more general welfare test and the significant rise of monopoly power in the United States economy. Pretty good evidence exists that since 1980, about the same time that Bork’s book was published and United States antitrust law began a significant rightward

ANTITRUST L.J. 423, 455 (2005); Darwin V. Neher et al., *Lessons from the Superior-ICG Merger*, 12 GEO. MASON L. REV. 289, 290 (2003)

¹⁵BORK, PARADOX, *supra* note __ at 126.

¹⁶See *Merger Guidelines*, *supra* note __, §§4,5.

¹⁷*Id.*, §10.

turn, market power measured by price-cost margins has been on the rise.¹⁸ Accompanying this has been a dramatic rise in firm profits, but stagnant, virtually non-existent growth in wages.¹⁹

There are many causes for this divergence that have little to do with competition policy. Nevertheless, one important component is very likely the considerable weight that the Chicago School generally and Bork in particular placed on the impact of unproven but presumed efficiency gains, and the skepticism they showed about many types of anticompetitive practices, particularly those that involved unilateral conduct or vertical agreements. Williamson concluded that, consistent with his assumptions including pre-merger competition and a common range of elasticities, a cost reduction from efficiencies of 4% would be sufficient to offset a price increase of 20% and still be welfare positive.²⁰ Williamson concluded that

The naive model thus supports the following proposition: a merger which yields non-trivial real economies must produce substantial market power and result in relatively large price increases for the net allocative effects to be negative.²¹

Significantly, Williamson's numbers are thrown completely off if one

¹⁸Jan De Loecker & Jan Eeckhout, *The Rise of Market Power and the Macroeconomic Implications* 9, NBER Working Paper No. 23687 (Aug. 24, 2017), available at <http://www.nber.org/papers/w23687>. For example, the authors concluded that average markups were about 18% in 1980 but 67% in 2017. See also Jonathan B. Baker, *Market Power in the U.S. Economy Today* (Wash. Center for Equitable Growth, March 2017), available at <http://cdn.equitablegrowth.org/wp-content/uploads/2017/03/16154837/032017-baker-antitrust-ib.pdf>. (exploring numerous explanations). The conclusions about European markets are more diverse and less robust. See John P. Weche & Achim Wambach, *The Fall and Rise of Market Power in Europe* (ZEW Discussion Paper #18-003) (2018), available at <https://www.econstor.eu/bitstream/10419/173383/1/1011811367.pdf>. See also Karl Smith, *Markups and Market Power* (Niskanen Center Aug. 23, 2017), available at <https://niskanencenter.org/blog/markups-market-power/> (concluding that the markups are in fact quite skewed, with firms with larger market shares enjoying higher markups). Largely in accord is the Growth Economic Blog, *Rising Markups and Falling Productivity* (Aug. 26, 2017), which observes that the Loecker and Eeckhout data focused on large publicly traded firms, not small business.

¹⁹See, e.g., David Autor, David Dorn, Lawrence F. Katz, Christina Patterson, and John Van Reenen, *The Fall of the Labor Share and the Rise of Superstar Firms* (MIT working paper, May 1, 2017), available at <https://economics.mit.edu/files/12979>; Jose Azar, Ioana Marinescu, and Marshall Steinbaum, *Labor Market Concentration* at 7-8 (NBER Working Paper No. 24147, Dec. 2017), available at <http://www.nber.org/papers/w24147>.

²⁰Williamson, *Welfare Tradeoff*, *supra note* __ at 22-23

²¹*Id.* at 23.

of Williamson's assumptions discussed previously fails to obtain. Williamson assumed a market that was perfectly competitive prior to the merger, with prices equal to marginal cost, and that was monopolized thereafter.²² The result is that an output reduction of a given magnitude reduces consumer welfare by a small amount, because that reduction is coming out of a region where consumers' surplus is small to begin with.²³ This is rarely the case in merger enforcement. For most challenged mergers price-cost margins were high prior to the merger. The Agencies²⁴ and economists generally consider high pre-merger margins to be a danger signal indicating prior oligopoly or collusion, or other competitive concerns.²⁵ Further, in such cases efficiency gains are distributed over a smaller output.²⁶ These differences completely upend the benefit-cost balance that Williamson hypothesized.

The 2010 Merger Guidelines do a much better job of drawing this line. First, unlike Bork, they take the risk of high market concentration seriously, although somewhat less absolutely than economists considered it to be in the 1950s and 1960s.²⁷ Then they draw strong inferences of harm from information about post-merger concentration *and* the increase in concentration caused by the merger. For example, if pre-merger market structure reflects a robust equilibrium²⁸ of prices near marginal cost, few or perhaps no two-firm mergers in that market would be challenged. Finally, once a prima facie case has been made, they require strong evidence of efficiencies that could not be obtained except by the merger and that are of

²²See discussion, *supra* at note __.

²³See the figure in note __ and accompanying discussion.

²⁴See 2010 Horizontal Merger Guidelines, *supra* note __, §§2.2.1, 4.1.3.

²⁵See Carl Shapiro, *The 2010 Horizontal Merger Guidelines: From Hedgehog to Fox in Forty Years*, 77 ANTITRUST L.J. 49, 69-72 (2010); Joseph Farrell & Carl Shapiro, *Recapture, Pass-Through, and Market Definition*, 76 ANTITRUST L.J. 585 (2010); Jonathan B. Baker, *Contemporary Empirical Merger Analysis*, 5 GEO. MASON L. REV. 347 (1997).

²⁶See note __, *supra*.

²⁷See Hovenkamp and Shapiro, *supra* note __; and see U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines (Aug. 19, 2010), available at <https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf>

²⁸That is, the prices would not only have to be at or near marginal cost, the market would also have to be in equilibrium. A two-firm natural monopoly market moving toward the monopoly equilibrium might exhibit marginal cost prices just prior to a merger to monopoly. See Herbert Hovenkamp, *Regulation and the Marginalist Revolution* (Penn L. & Econ. Res. Paper No. 1-14, June 21, 2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3181852.

sufficient magnitude to reverse a predicted price increase.²⁹ These are rarely found.

As noted previously, ever increasing price-cost margins in the economy may have several explanations other than competition policy. One is increasing use of technologies with high fixed costs, which entails higher margins between prices and short-run marginal cost. Another is significantly declining labor participation rates, which has much to do with decades of anti-union legal policy, although it may also reflect an antitrust policy inattentive to labor market monopsony.³⁰ To the extent that wage suppression shows up as retention of profits that would otherwise have been distributed to workers, one can expect price-cost margins to rise. A third possibility is increased monopolistic competition as the market offers a greater variety of goods and services, thus blunting the competition among sellers. Antitrust's role here is controversial.³¹ Product differentiation and monopolistic competition were regarded as significant antitrust issues in the 1970s and early 1980s, leading the Federal Trade Commission to develop some theories that today seem far-fetched. One was "shared" monopoly, mainly in breakfast cereals.³² Another was the FTC's objection to annual style changes for automobiles and some other products.³³ Today we are more likely to think that product differentiation is driven by consumer taste and insistence on variety. In and of itself it is not generally regarded as competitively harmful. Indeed, product differentiation has been one of the mechanisms that has enabled many small businesses to survive – by differentiating their products rather than going head-to-head with larger

²⁹2010 Merger Guidelines, *supra* note __, §10.

³⁰See discussion *infra*, text at notes __; and Ioana Marinescu and Herbert Hovenkamp, *Anticompetitive Mergers in Labor Markets*, __ IND. L.J. __ (2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3124483.

³¹See Herbert Hovenkamp, *Regulation and the Marginalist Revolution* (SSRN, 2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3181852.

³²See, e.g. *In re Kellogg*, 99 F.T.C. 8 (1982) (dismissing complaint – “we should not undertake to restructure an industry under Section 5 of the FTC Act without a clear supportive signal from Congress”); and see Richard Schmalensee, *The New Industrial Organization and the Economic Analysis of Modern Markets*, in *Advances in Economic Theory* 253, 258-65 (W. Hildenbrand ed. 1982); and see Thomas Campbell, *Predation and Competition in Antitrust: the Case of Nonfungible Goods*, 87 COLUM. L. REV. 1625 (1987).

³³See, e.g., Bradford Snell, *Annual Style Change in the Automobile Industry as an Unfair Method of Competition*, 80 YALE L.J. 577 (1971). See Federal Trade Commission, *Report on the Motor Vehicle Industry* 29 (1939), complaining that annual style changes were favoring larger firms and concentrating the industry. See also Harold G. Vatter, *The Closure of Entry in the American Automobile Industry*, 4 OXFORD ECON. PAPERS 213 (1952).

competitors. In addition, the new economy offers a large range of products and services geared to highly individualistic consumer tastes. Less competition purely on product prices is very likely one of the consequences.

It should be clear now that there is much more to this story than the adoption of any particular welfare test. The problem was not merely that the general welfare test trades off presumed harm against presumed benefits. It was that Bork gave the benefit of the doubt to efficiency claims while being extremely skeptical about claims of competitive harm. These views were heavily driven by technical elements of Chicago School industrial organization theory at that time, but some of Bork's individual beliefs went even further. For example, one must add to Williamson's very generous test for merger efficiencies Bork's extreme assumptions about the anticompetitive potential of mergers as well as most other antitrust practices. Bork made no denying of the fact that he disbelieved the theory of oligopoly. As a result, mergers should be considered harmless unless they created a single-firm monopoly.³⁴ He also categorically rejected the idea that merger policy should include any kind of "incipiency" test, even though today the case for such tests seems uncontroversial and required by any theory that identifies price-increasing mergers as harmful.³⁵

In addition, Bork took extremely benign positions on all vertical practices, concluding that the best rule for them should be virtual per se legality except in a small group of cases thought to facilitate collusion.³⁶ He also believed that predatory pricing is so unlikely to succeed that the best rule for it should be per se legality.³⁷ In sum, for practically every practice other than naked price fixing Bork emphasized their efficiencies or harmlessness, while rejecting nearly all theories of competitive harm.

Bork provided little in the way of evidence for either position. Indeed, he attempted to protect his theories from attempts at falsification by arguing that efficiencies were not susceptible to proof or disproof in particular cases.³⁸ "The problem of technical efficiencies alone is likely to be beyond the

³⁴See BORK, ANTITRUST PARADOX, *supra* note __, 221-222. On this debate within the Chicago School, see Herbert Hovenkamp, *Whatever Did Happen to the Antitrust Movement?*, __ NOTRE DAME L. REV. __ (2018) (forthcoming), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3097452.

³⁵See Herbert Hovenkamp, *Prophylactic Merger Policy*, __ HASTINGS L.J. __ (2018) (forthcoming), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3090650.

³⁶BORK, ANTITRUST PARADOX, *supra* note __ at 287-288. See also Hovenkamp, *Whatever Did Happen*, *supra* note __ at __.

³⁷BORK, ANTITRUST PARADOX, *supra* note __ at 144-148.

³⁸*Id.* at 126.

capacities of the law,” he wrote.³⁹ He argued at some length that specific productive efficiencies in a particular case could never be quantified.⁴⁰ For that reason he rejected any notion that antitrust policy should include a case-specific “economies defense.”⁴¹ Rather, it should simply assume that efficiency justifications overwhelmed the explanations of most challenged practices. He also disagreed with Williamson on this point, who had argued for an economies defense in antitrust cases.⁴²

The view toward efficiencies expressed in the 2010 Horizontal Merger Guidelines categorically rejects Bork’s position. The Guidelines unambiguously require an efficiencies defense to a prima facie unlawful merger, with the burden of proof on the defendant.⁴³ Bork’s position is also inconsistent with modern statements of the rule of reason, which require a prima facie case of harm, and then shifts the burden of proof to the defendant to show offsetting defenses.⁴⁴ At least in dicta, that formulation was accepted by all members of the Supreme Court in the 2018 *AMEX* case.⁴⁵ Most generally, it reflects considerable advances in industrial organization theory and econometrics that have occurred since the late 1970s.

One possible explanation for Bork’s very benign attitudes about competitive harm is that, not only does *The Antitrust Paradox* not reflect subsequent advances in economics, it is also very much an “old economy” book. It was published a generation prior to the *Microsoft* litigation⁴⁶ and includes scant mention of intellectual property rights. Bork has a brief discussion of the *International Salt* case and its presumption that a patent creates market power for purposes of tying law,⁴⁷ and another brief discussion

³⁹ *Id.* at 126-127.

⁴⁰ *Id.* at 127-128.

⁴¹ *Ibid.*

⁴² *See id.* at 127.

⁴³ 2010 Merger Guidelines, *supra* note __, §10:

... it is incumbent upon the merging firms to substantiate efficiency claims so that the Agencies can verify by reasonable means the likelihood and magnitude of each asserted efficiency, how and when each would be achieved (and any costs of doing so), how each would enhance the merged firm’s ability and incentive to compete, and why each would be merger-specific.

⁴⁴ *See* 7 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶¶1504-1511 (4th ed. 2017).

⁴⁵ *Ohio v. American Express Co.*, 138 S.Ct. 2274 (2018). *See* Erik Hovenkamp, *Platform Antitrust*, __ J. CORP. L. __ (2019), currently available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3219396.

⁴⁶ *United States v. Microsoft*, 253 F.3d 34 (D.C. Cir. 2001).

⁴⁷ *Id.* at 366-367, discussing *International Salt Co., Inc. v. United States*, 332 U.S. 392 (1947).

of the *Walker Process* case and bad faith patent infringement suits.⁴⁸ Other than that, intellectual property rights and their potential for anticompetitive use go unmentioned.

Instead, most of the cases Bork does discuss involve traditional production or distribution of hard goods or commodities. For these, Bork had been dealt a winning hand – namely, many theories of competitive harm developed from the 1930s through the 1970s were ill conceived, untested, or even fantastic.⁴⁹ The antitrust control of ordinary distribution systems, including the law of RPM, nonprice restraints, tying, and exclusive dealing, were seriously overdeterrent. For example, the old leverage theory of tying⁵⁰ deserved to be rejected, as did the per se rule for intrabrand restraints,⁵¹ but neither of these served to justify Bork’s conclusion that tying arrangements and intrabrand restraints are never anticompetitive. The condemnation of horizontal mergers because they produced cost savings, as in *Brown Shoe*,⁵² was assuredly wrong, as was the view that vertical mergers were bad because they enabled parents to charge their subsidiaries a monopoly price.⁵³ Equally wrong, however, was Bork’s view that all mergers were driven exclusively by efficiency concerns, with no real possibility of competitive harm unless they were mergers to monopoly.

In sum, no particular welfare test answers antitrust’s hard questions. One must also have a substantive theory about when practices are anticompetitive and when they are beneficial, as well as a theory about how harms and benefits are to be proved. The real meaning of Bork’s views lie not so much in the welfare test that he chose, but rather in his extreme generosity toward efficiency claims, to the point of accepting them without proof, and extreme skepticism about claims of competitive harm.

Does adoption of a consumer welfare test require antitrust policy to trade away efficiency for convenience of administration? Perhaps, but not very much and not necessarily any at all. First, as observed previously, it is hard to find even a single case in the United States where the choice of a

⁴⁸*Id.* at 352-355, discussing *Walker Process Equipment, Inc. v. Food Mach. & Chem. Corp.*, 382 U.S. 172 (1965).

⁴⁹On the antitrust treatment of vertical practices at mid-twentieth century, see HERBERT HOVENKAMP, *THE OPENING OF AMERICAN LAW: NEOCLASSICAL LEGAL THOUGHT, 1870-1970*, Ch. 12 (2015).

⁵⁰See 9 PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW* ¶1710 (4th ed. 2018).

⁵¹8 *Id.*, ¶1620 (4th ed. 2017) (resale price maintenance); ¶¶1642-1643 (vertical nonprice restraints).

⁵²*Brown Shoe Co., Inc. v. United States*, 370 U.S. 294 (1962); see BORK, *ANTITRUST PARADOX*, *supra* note ___ at 198-224.

⁵³*Id.* at 225-245.

welfare test has made a difference.⁵⁴ This means that any improvement in efficiency, assuming there is any, would be dwarfed by the savings in administrative costs, because the measurements required by a general welfare test would have to be undertaken in any case that is even moderately close.

Of course, any test can alter incentives. The choice of a consumer welfare test will tend to favor mergers or other antitrust activities that tend toward increased output. For example, structurally challengeable mergers must produce efficiency gains sufficient to offset any predicted price increase. Firms may have to alter their strategies in order to comply with the law, and a few practices that produce only marginal efficiency benefits while threatening competitive harm might be abandoned. Finally, consent decrees can be shaped accordingly. For example, if a merger between two multi-store chains or airlines threatens higher prices in a few markets but not others, then the government may insist on partial divestitures in the markets where consumer harm is predicted.

Finding the “Consumer” in Consumer Welfare

The focal point for identifying consumer welfare is the firm or group of firms accused of an anticompetitive practice, which we call the “defendant.” The consumer welfare principle says that when evaluating a defendant’s activities the policy concern is primarily with the welfare of that entity’s consumers. Of course, other consumers in the same market may be similarly affected, even if they purchase only from the defendant’s competitors. These are frequently called “umbrella” consumers. For example, consumers may pay higher prices to innocent competitors of a cartel that has raised product prices but controls less than the entire market.⁵⁵ Indirect purchasers as well as direct purchasers also qualify as “consumers.” Whether or not they should have a damages action is a relevant question for some purposes, but not for this one.⁵⁶

Clearly, the word “consumer” is under-inclusive. For example, if an office stapler cartel sells a box of staplers to Wal-Mart, which in turn sells a stapler at retail to an end user, the consumer welfare paradigm acknowledges both Wal-Mart and the end user as “consumers,” even though we do not ordinarily think of a commercial intermediary as a consumer. Ironically, under the indirect purchaser rule in United States antitrust law, only Wal-Mart and not the end user, or actual consumer, would have a damages action against the cartel. End use consumers do have standing to sue for damages,

⁵⁴See discussion *supra*, text at notes ___.

⁵⁵On the extent to which so-called “umbrella” purchasers are covered under United States law, see PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶347 (4th ed. 2014).

⁵⁶On this issue, see *id.*, ¶346.

however, if they are direct purchasers.⁵⁷ Further, even indirect purchasers can obtain an injunction.⁵⁸

Another under-inclusion is the supply side of the market. The stapler manufacturer requires both steel and labor as inputs, and it might impose anticompetitive restraints in either of these markets, thus reducing output and suppressing the price that it pays. The harm from monopsony, as opposed to monopoly, has been well recognized in antitrust for decades,⁵⁹ and has recently received renewed attention in the literature, particularly with respect to labor markets.⁶⁰

Clearly suppliers, including suppliers of labor, are not “consumers” in the conventional usage. Nevertheless, the injury that results from the exercise of monopsony power – i.e., buy-side monopoly power – is technically similar to the injury caused by monopoly. In both cases the defendant reduces output. The effect is higher prices to purchasers and lower outlays to suppliers. As a result, all of the reasons for protecting traditional “consumers” under the consumer welfare principle apply to suppliers as well. The only thing that does not fit very well is the label “consumer.”

Some have suggested the term “trading partners” as an alternative to consumers – that is, antitrust should be concerned with “trading partner welfare.”⁶¹ That term has the advantage that it covers both downstream and upstream trades; that is, it applies to entities to whom the defendant sells as well as those from which it buys. Rhetorically, however, the term is certainly not an improvement. Further, it requires an explanation every time one uses it. It is also underinclusive to the extent that it does not encompass people two or three times removed from the violator. For example, if Acme Stapler company sells staplers to Wal-Mart, which in turn sells one to a retail customer, we do not ordinarily think of Acme and the customer as “trading partners,” although that term would apply to the relationship between Acme

⁵⁷Reiter v. Sonotone Corp., 442 U.S. 330 (1979).

⁵⁸2 AREEDA & HOVENKAMP, *supra* note __, ¶346d.

⁵⁹*E.g.*, Mandeville Island Farms v. American Crystal Sugar, Inc., 334 U.S. 219 (1948). On monopsony and its economic effects, *see* ROGER D. BLAIR AND JEFFREY L. HARRISON, *MONOPSONY IN LAW AND ECONOMICS* (rev. ed. 2010).

⁶⁰*See* Ioana Elena Marinescu and Herbert Hovenkamp, *Anticompetitive Mergers in Labor Markets*, __ IND. L.J. (2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3124483; Suresh Naidu, Eric A. Posner & E. Glen Weyl, *Antitrust Remedies for Labor Market Power*, __ HARV. L. REV. __ (2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3129221; C. Scott Hemphill & Nancy L. Rose, *Mergers that Harm Sellers*, 127 YALE L.J. 2078 (2018).

⁶¹*See* Hemphill & Rose, *supra* note __; Herbert Hovenkamp & Carl Shapiro, *Horizontal Mergers, Market Structure, and Burdens of Proof*, 127 YALE L.J. 1996 (2018) (using the term “trading parties”).

and Wal-Mart. The same thing would apply to indirect sellers on the supply side.

What we really want is a name for some class of actors who is injured by either the higher buying price or the lower selling price that attends a monopolistic output reduction. In the case of a traditional consumer the primary cause of this injury is reduced output and higher prices. In the case of a supplier, including a supplier of labor, the primary cause is reduced output and lower selling prices. In both cases there are also injuries to those who are forced out of the market. These include would be consumers who no longer purchase as a result of a monopoly price increase, and suppliers, including labor, who no longer provide their goods or services in response to a price suppression. For administrative reasons it may be important to distinguish those who deal directly with the defendant from those who deal indirectly. But the passed on injury they suffer is the same as that experienced from direct dealers.

I would stick with the word “consumer,” but with the understanding that it is a term of art. Although antitrust policy is clearly concerned with competitive injuries to suppliers, to date supplier injury is the focal point of only a small percentage of the cases.

Measuring Competitive Harm to Suppliers, Including Labor

Supplier welfare issues could represent a significant growth area for antitrust. Although antitrust’s ambit of protection has always covered suppliers, including labor, the problem has received only secondary attention in the case law. Recent literature on labor market concentration and wage suppression suggests that it is time to reconsider that position.

In doing so, however, we must also address some very significant measurement problems. Here the problems are more empirical than conceptual. Monopsony injury is experienced by the seller as lower receipts, but not every lower price paid to a seller is an injury caused by monopsony. Indeed, not even every injury that results when a firm reduces the volume of its purchases is the result of monopsony. Some may result from increased efficiency.

One important disjunction between monopoly and monopsony is the robustness of alternative explanations for these phenomena. When a naked cartel raises its price, we do not ordinarily permit a defense that price-fixing is cheaper than competition. Collusion can eliminate the cost of competitive bidding, which can be high in some markets.⁶² The cost of assembling a bid

⁶² While it can eliminate the cost of competitive bidding it does not always do so. For example, in *United States v. Addyston Pipe & Steel Co.*, 85 F. 271 (6th Cir. 1898), modified and aff’d, 175 U.S. 211 (1899), the pipe cartel employed a very elaborate scheme of internal bidding in order to determine the winner and the cartel

on a complex construction project can be high, but to the best of my knowledge no court has ever held that these costs justified naked collusion as an alternative.⁶³ A cartel might also be a way of allocating a scarce commodity. For example, in the 1960s the U.S. Federal Trade Commission condemned a cartel of pasta manufacturers who responded to a temporary shortage of high quality durum semolina wheat by agreeing to make pasta consisting of 50% farina wheat, which was inferior.⁶⁴

For monopsony the situation is very different. Now the complaint is about low prices, which can result from either monopsonistic output suppression or cost reductions that result from efficiency gains. While antitrust policy wants to condemn the former it has no reason to condemn the latter. The most important theoretical difference between monopsony and efficiency in procurement is the impact on product output. A firm or cartel monopsonizes in the purchasing market by suppressing output. By contrast, cost savings that result from efficiency should result in increased purchases, as well as increased output in the market in which the firm sells.⁶⁵ While that observation is helpful, the distinction is not always easy to prove. We must point to some empirical evidence that indicates either efficiency or monopsony. That can be surprisingly difficult. Nevertheless, there are a few evidentiary signals.

First, when efficiency gains account for the reduction in a firm's expenditures, there is often some observable change in the nature of inputs or the structure of operations that helps explain it. For example, consider the merger of two automobile manufacturers, such as Chrysler and Jeep. One likely consequence is a reduction in the number of dealerships, because a single dealer can now sell and service brands formerly requiring two dealers. This consolidation is not an exercise of monopsony power but simply an efficient reorganization of resources. Further, it should be evidenced by a

price that could easily have been more costly than honest bidding. *Accord* United States v. Romer, 148, 363 F.3d 359 (4th Cir. 1998). The elaborate scheme is described in 11 HERBERT HOVENKAMP, ANTITRUST LAW ¶1905 (4th ed. 2018); HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE §4.1c (5th ed. 2015); GEORGE J. STIGLER, THE THEORY OF PRICE 230-231 (3d ed. 1966).

⁶³See 11 HERBERT HOVENKAMP, ANTITRUST LAW ¶1907c (4th ed. 2018); *see, e.g.,* FTC v. Alliant Techsystems, Inc., 808 F. Supp. 9, 22 (D.D.C. 1992) (refusing to offset higher prices that would result from eliminating competitive bidding against alleged cost savings from elimination of competitive bidders).

⁶⁴*In re* National Macaroni Manufacturers Assn., 65 F.T.C. 583 (1964), enforced, 345 F.2d 421 (7th Cir. 1965).

⁶⁵If the firm is a competitor in the selling market its output will increase as its marginal costs decline. If it has market power in the selling market it will both increase its output and reduce its price.

reduction in the number of dealerships, with the elimination of some personnel that have now become duplicative. In the case of a merger, of course, this will not happen until after the merger has occurred, which serves to make pre-acquisition assessment more difficult. At the same time, accompanying this reduction in dealerships should be an *increase* in the number of units sold. As a firm's costs go down its output increases. For example, a post-merger firm that begins to purchase an input in larger quantities than the two pre-merger partners and obtains a lower price is not likely suppressing its outlay in order to suppress prices.

By contrast, if the labor market is concentrated and the only thing that changes is the bargaining relationship, then an exercise in monopsony power becomes a more serious possibility. Even here, however, there are alternative explanations. For example, the sell side of the labor market may already be exhibiting countervailing power. One thing to look for, although it will not always be helpful, is upward vs. downward pressure on output. Complicating this is the fact that the individual laborer's supply curve behaves in peculiar ways, largely because laborers have utility functions that are more behavioral in nature, rather than strictly neoclassical cost functions. For example, a cut in wages may actually induce laborers to work more in order to maintain subsistence or customary lifestyle levels.⁶⁶ By contrast, an increase in wages may sometimes induce workers to work less because higher wages afford them the opportunity for more leisure. Thus at certain points the labor supply curve might be backward bending.⁶⁷ These issues all serve to make the analysis of labor supply in antitrust cases very difficult. For example, if wages are already near subsistence levels a cartel of employers to suppress wages further may result in more rather than fewer hours of employment.

So it is important to examine other methodologies. For example, buy-side harm can also be inferred indirectly from high concentration, just as it is on the selling side in merger cases. The empirical work that has been done in labor markets suggests correlations between concentration and price that resemble those on the sell side.⁶⁸ Less developed at this writing, but perhaps promising, is the use of the same kind of "upward pricing pressure" techniques that are currently used in product merger analysis to estimate

⁶⁶ See, e.g., Maryke Dessing, Labor Supply, the Family and Poverty: the S-Shaped Labor supply Curve, 49 J. Econ. Behavior & Org. 433 (2002).

⁶⁷ See Giora Hanoch, The "Backward-Bending Supply of Labor, 73 J. Pol. Econ. 502 (1965)

⁶⁸ See Marinescu and Hovenkamp, *supra* note __; Naidu, Posner & Weyl, *supra* note __; Azar, Marinescu, & Steinbaum, *supra* note __. On the correlation between price-cost margins and concentration in product sale markets, see Hovenkamp & Shapiro, *supra* note __.

“unilateral effects” of mergers.⁶⁹

Antitrust’s Left Flank – Reviving Old Debates

Proponents of more general welfare tests come at antitrust’s consumer welfare principle from the right. But another attack originates on the left. This group has been dubbed “hipster antitrust” by some critics, but called the “new Brandeis School” by its followers.⁷⁰ To the extent they have articulated their positions, they say some things that consumer welfarists can agree with, although many that they cannot. Overall, the movement is not enthusiastic about the use of economics in antitrust and appears to believe that economics should either be subordinated to political theory or abandoned entirely.⁷¹

Accompanying this comes very considerable suspicion about markets generally, quite aside from monopoly.⁷² Proponents of the new Brandeis school sometimes write longingly about the nineteenth century when the economy was much simpler and property and contract rules were deemed sufficient to govern markets. For example:

during the first half of the nineteenth century, the citizens of the young United States made themselves free to use their state legislatures to ensure that their markets were open and well regulated and that the incorporations of power necessary to achieve any particular large-scale project were limited in scope and duration. That is, the citizens of the United States ensured that we alone, as a people, would be masters of our own markets and that we alone, as a people, would be masters of our corporations.⁷³

As a matter of history, that view seems naïve. The first half of the

⁶⁹See 4 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶914 (4th ed. 2016). Naidu, Posner & Weyl, *supra* note __ attempt an equivalent methodology which they style “downward wage pressure.”

⁷⁰See Konstantin Medvedovsky, *Hipster Antitrust – A Brief Fling or Something More?*, CPI ANTITRUST CHRONICLE (April, 2018), available at <https://www.competitionpolicyinternational.com/wp-content/uploads/2018/04/CPI-Medvedovsky.pdf>; Daniel A. Crane, *The Tempting of Antitrust: Robert Bork and the Goals of Antitrust Policy*, 79 ANTITRUST L.J. 835 (2014), who also notes some self-comparisons to Jefferson and Madison. See also Lina Khan, *The New Brandeis Movement*, 9 J. EUROPEAN COMP. L. & PRACTICE 131 (2018).

⁷¹*E.g.*, Zephyr Teachout and Lina Khan, *Market Structure and Political Law: A Taxonomy of Power*, 9 DUKE J. CONST. L. & PUB. POLICY 38 (2014).

⁷²See, e.g., K. SABEEL RAHMAN, DEMOCRACY AGAINST DOMINATION 10-13 (2017).

⁷³*E.g.*, BARRY C. LYNN, CORNERED: THE NEW MONOPOLY CAPITALISM AND THE ECONOMICS OF DESTRUCTION 103, 223-224 (2010).

nineteenth century was dominated by major interest group clashes over many aspects of government economic policy, including monopoly, the business corporation, banking, and patent rights.⁷⁴ Not many words in nineteenth century discourse evoked more political heat than “monopoly.”⁷⁵ To be sure, the technological landscape was different, thanks largely to differences in transportation and communication technology, but the conflicts over monopoly and economic power were prominent nonetheless.

While the word “Luddite” is probably too strong, the Neo-Brandeisians exhibit strong ambivalence about innovation, particularly when the firms who engage in it become large.⁷⁶ Along with this comes an aversion to business organizations that result in cost savings. Among these are large technological networks such as Amazon, Google and Facebook,⁷⁷ and hospital group purchasing organizations, which are associations of hospitals that band together in order to procure supplies at lower cost, but in the process exclude some higher cost suppliers from their purchasing.⁷⁸

The political and economic theory underlying the new Brandeis movement largely replicates the “Progressive critique” of history and politics originating during the Gilded Age and stretching well beyond the New Deal.⁷⁹ That writing saw corporations as powerful and largely harmful

⁷⁴See, e.g., MORTON J. HORWITZ, *THE TRANSFORMATION OF AMERICAN LAW, 1780-1860* (1977); HERBERT HOVENKAMP, *ENTERPRISE AND AMERICAN LAW, 1836-1937* (1990); WILLIAM J. NOVAK, *THE PEOPLE’S WELFARE: LAW & REGULATION IN NINETEENTH-CENTURY AMERICA* (1996). On patent law and the debates over intellectual property monopoly, see Herbert Hovenkamp, *The Emergence of Classical Patent Law*, 58 ARIZ. L. REV. 263 (2016).

⁷⁵See, e.g., STEVEN L. PIOTT, *THE ANTI-MONOPOLY PERSUASION: POPULAR RESISTANCE TO THE RISE OF BIG BUSINESS IN THE MIDWEST* (1985). On the Jackson Era, see HARRY L. WATSON, *LIBERTY AND POWER: THE POLITICS OF JACKSONIAN AMERICA* (rev. ed. 2006). On the post-Civil War era, see GRETCHEN RITTER, *GOLDBUGS AND GREENBACKS: THE ANTIMONOPOLY TRADITION AND THE POLITICS OF FINANCE IN AMERICA, 1865-1895* (1999)

⁷⁶LYNN, *CORNERED*, *supra* note __, Ch. 6.

⁷⁷See Lina Khan, *The Separation of Platforms and Commerce*, 119 COL. L. REV. ____ (2019) (forthcoming), abstract available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3180174.

⁷⁸*Id.* at 151-155, relating the account of Retractable Technologies, which was unsuccessful in getting its retractable syringe included in many group purchasing orders. See *Retractable Tech., Inc. v. Becton Dickinson & Co.*, 842 F.3d 883 (5th Cir. 2016) (rejecting antitrust claims).

⁷⁹E.g., CHARLES A. AND MARY R. BEARD, *HISTORY OF THE UNITED STATES* (1921). The leading intellectual history of the earlier part of the period was VERNON L. PARRINGTON, *MAIN CURRENTS IN AMERICAN THOUGHT* (3 vols., 1927-1930). For a good revisionist critique see RICHARD HOFSTADTER, *THE PROGRESSIVE*

forces in American society, viewing large firms as hijacking American business from smaller, independent companies.⁸⁰ The Progressive critique believed that business consolidations, or “trusts,” were invariably harmful.⁸¹ The New Brandeis movement restates concerns that Berle and Means articulated nearly a century ago about the separation of ownership and control in the business corporation.⁸² The Progressive critique and the New Brandeis movement also believe that exclusionary strategies such as predatory pricing are a common device by which firms create dominant positions⁸³ or force

HISTORIANS: TURNER, BEARD, PARRINGTON (1968).

⁸⁰*E.g.*, HERBERT CROLY, *THE PROMISE OF AMERICAN LIFE* 105-135 (1909); HERBERT CROLY, *PROGRESSIVE DEMOCRACY* (1914); BENJAMIN PARKE DE WITT, *THE PROGRESSIVE MOVEMENT: A NON-PARTISAN, COMPREHENSIVE DISCUSSION OF CURRENT TENDENCIES IN AMERICAN POLITICS* (1915) (especially Ch. 7, 113-142, on the business corporation); ADOLF BERLE AND GARDINER MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932) (arguing that separation of ownership and control led to corporate social irresponsibility).

⁸¹See, e.g., JOHN BATES CLARK, *THE CONTROL OF TRUSTS* (1901); JOHN BATES CLARK, *THE PROBLEM OF MONOPOLY: A STUDY OF A GRAVE DANGER AND OF THE NATURAL MODE OF AVERTING IT* (1904); ERNST VON HALLE, *TRUSTS, OR INDUSTRIAL COMBINATIONS AND COALITIONS IN THE UNITED STATES* (1900); WILLIAM M. COLLIER, *THE TRUSTS* (1900); RICHARD T. ELY, *MONOPOLIES AND TRUSTS* (1900); ELLIOT JONES, *THE TRUST PROBLEM IN THE UNITED STATES* (1924). See also Frederic J. Stimson, *Trusts*, 1 HARV. L.REV. 132 (1887); John Bates Clark, *The 'Trust': a New Agent for Doing an Old Work: or Freedom Doing the Work of the Monopoly*, 52 NEW ENGLANDER 223 (1890); MYRON W. WATKINS, *INDUSTRIAL COMBINATIONS AND PUBLIC POLICY* (1927). And see JOHN MAURICE CLARK, *SOCIAL CONTROL OF BUSINESS* 49 (1923). On antitrust during this period, see Richard Hofstadter, “Whatever Happened to the Antitrust Movement,” in *THE PARANOID STYLE IN AMERICAN POLITICS* (1965), reprinted in *THE MAKING OF COMPETITION POLICY: LEGAL AND ECONOMIC SOURCES* 221-251 (Daniel A. Crane & Herbert Hovenkamp, eds., 2013). See also HERBERT HOVENKAMP, *ENTERPRISE AND AMERICAN LAW, 1836-1937*, Chs. 21-22. And see ELLIOT JONES, *THE TRUST PROBLEM IN THE UNITED STATES* 66-72 (1924) (attacking vertical integration as anticompetitive); Myron Watkins and Frank A. Fetter, *Relative Efficiency of Large, Medium-Sized and Small Business* (TNEC Monograph # 13, 1939) (arguing that large firms are less efficient than smaller ones).

⁸²BERLE & MEANS, *supra* note __; cf. LYNN, *CORNERED*, *supra* note __, 230 (speaking of separation of ownership and control as “double socialization,” with the result that no one had the motives of the “real owner” of property).

⁸³*E.g.*, IDA TARBELL, *THE STANDARD OIL COMPANY* 156, 188, 236 (1904); Edward S. Roger, *Predatory Price Cutting as Unfair Trade*, 27 HARV. L. REV. 139 (1913); HERBERT FRANCIS TAGGART, *MINIMUM PRICES UNDER THE NRA* 38 (1936). One of the most influential early attempts to debunk these claims was John S. McGee, *Predatory Price Cutting: the Standard Oil (N.J.) Case*, 1 J. L. & ECON.

targeted firms to merge.⁸⁴ At least up to this writing, the New Brandeis writers simply restate these positions and do little to engage revisionist critics from the 1960s and after.

On predatory pricing, both the earlier literature and the New Brandeisians define it very broadly, even to include market development. So, for example, Amazon is thought to be guilty of predatory pricing, not because it sells a product at a price below its costs, but rather because its investment in product promotion entails that it experiences losses during the early developmental stages.⁸⁵ Just as the Progressive critique, the New Brandeisians adhere to a variety of “leverage” theories – which neo-Brandeisians sometimes term “pincer” monopoly⁸⁶ -- that firms can use power in one market to extend their position into adjacent markets. For example, they might charge monopoly prices in some markets in which they operate in order to subsidize predatory pricing in more competitive markets.⁸⁷ The progressive critique and the New Brandeis movement are both also

137 (1958). See also LAURA PHILLIPS SAWYER, *AMERICAN FAIR TRADE: PROPRIETARY CAPITALISM, CORPORATISM, AND THE “NEW COMPETITION,”* 1890-1940 at 277-279 (2018). See also Butler D. Shaffer, *In Restraint of Trade: Trade Associations and the Emergence of “Self Regulation,”* 20 SW. U. L. REV. 289, 317 (1991).

⁸⁴ Cf. LYNN, *CORNERED*, *supra* note __, 32-42-, 211-218 (using as an example the brewers Luxottica and InBev).

⁸⁵ E.g., Khan, *Amazon’s Antitrust Paradox*, *supra* note __ at 756-761.

⁸⁶ LYNN, *CORNERED*, *supra* note __, 16-22.

⁸⁷ See, e.g., TARBELL, *STANDARD OIL*, *supra* note __ at 398 (Standard’s use of dominance in a pipeline to force capitulation by other shippers). See also Frederic J. Stimson, a Harvard law professor and eventual U.S. ambassador to Argentina, who wrote three years before the Sherman Act was passed:

Take the Philadelphia gas, for instance (and the name is purposely misquoted), a company which owns gas-works in a hundred cities. Say that in two of these are competing works, and that the gas costs the company sixty cents a thousand; a price at which the competing company can also live. The Philadelphia company puts its price in those two cities down to ten cents a thousand, and charges its patrons sixty-one cents in the other ninety-eight cities. The profits of the Philadelphia company remain the same, but its only two remaining rivals are ruined.

Stimson, *Trusts*, *supra* note __ at 134. Of course, the theory assumes that Philadelphia gas was not previously charging its profit-maximizing price in the 98 markets. If it were, a price increase would produce less rather than greater profits. Stimson’s best known legal publication was *POPULAR LAW-MAKING: A STUDY OF THE ORIGIN, HISTORY, AND PRESENT TENDENCIES OF LAW-MAKING BY STATUTE* (1911).

ambivalent or even hostile toward intellectual property rights.⁸⁸ Both hold strong views about the extent of and harm caused by industrial concentration and high entry barriers.⁸⁹ Both the Progressive critique and the New Brandeisians are highly suspicious of vertical integration,⁹⁰ including practices such as tying and exclusive dealing by which suppliers control their dealers.⁹¹

One characteristic of the New Brandeis movement is a belief that centrist antitrust has focused too much on economics and not sufficiently on the political power that is capable of creating monopoly. In the process, it argues, antitrust policy has ignored other values such as fairness or even small business protectionism.⁹² What is far less clear is exactly how these goals should be weighed and balanced against each other. Also missing at this stage is any serious discussion of remedies, except for some very general statements to the effect that perhaps the best fix for Amazon is regulation.⁹³ The movement does not appear to be concerned about high prices. While they are obsessed with what they regard as excessive concerns about efficiency, they do not appear to see efficiency as having much to do with

⁸⁸See discussion *supra*, text at notes __; and see DE WITT, *supra* note __ at 133 (use of patents to “choke off competition and gain control of an industry”). On late nineteenth century hostility toward patents as monopolistic, see HOVENKAMP, OPENING, *supra* note __, Ch. 10.

⁸⁹HENRY CALVERT SIMONS, A POSITIVE PROGRAM FOR LAISSEZ-FAIRE 20-21 (1934). See also ELLIS W. HAWLEY, THE NEW DEAL AND THE PROBLEM OF MONOPOLY 292 (1966, reprint 1995). On Simons and the subsequent evolution of the Chicago School on issues pertaining to industrial concentration, see Robert Van Horn, *Chicago’s Shifting Attitude Toward Concentrations of Business Power* (1934-1962), 34 SEATTLE UNIV. L. REV. 1537 (2011). On the New Brandeis movement and entry barriers, see Khan, *Amazon’s Antitrust Paradox*, *supra* note __ at 719-720, 768-770.

⁹⁰E.g. ARTHUR R. BURNS, THE DECLINE OF COMPETITION (1936) (blaming much of the observed decline in competition on vertical integration); see also SIMONS, POSITIVE PROGRAM, *supra* note __, 20-21 (vertical integration as anticompetitive).

⁹¹On the history of hostility toward vertical integration in mid-twentieth century antitrust policy, see HOVENKAMP, OPENING, *supra* note __, Ch. 12; on the reaction, see Herbert Hovenkamp, *Robert Bork and Vertical Integration: Leverage, Foreclosure, and Efficiency*, 79 ANTITRUST L.J. 983 (2014). Cf. *Carbice Corp. v. Patents Development Corp.*, 283 U.S. 27 (1931) (per Justice Brandeis -- condemning nonforeclosing tie in competitive market under patent misuse doctrine). Cf. LYNN, CORNERED, *supra* note __, 16-22, 27-30, 160-161.

⁹²A good summary of these various arguments is LYNN, CORNERED, *supra*, note

⁹³Khan, *Amazon*, *supra* note __ at 797-801.

lower prices.⁹⁴ Indeed, sometimes its protagonists write as if low prices are the evil to be avoided.

Certainly large firms can wield political power and often do. But cartels of smaller firms do it too. For example, Louis D. Brandeis, the namesake of the neo-Brandeis movement, certainly said many things in opposition to monopoly. However, he also devoted considerable effort to organizing cartels of smaller firms to protect themselves from aggressive price cutters. Beginning around 1912 Brandeis began a campaign to overrule or limit the Supreme Court's *Dr. Miles* decision condemning resale price maintenance (RPM) under a per se rule. This opposition to RPM did not come from those concerned with free riding or other externalities involving point of sale services that might lead to inefficiency.⁹⁵ Rather, it came from small sellers banding together simply to force manufacturers to guarantee them higher margins.⁹⁶ The Fair Trade League and various "open price" associations also campaigned heavily to permit information exchanges intended to blunt "cutthroat" competition.⁹⁷ As a Supreme Court Justice, Brandeis himself wrote a stinging dissent in a decision striking down a statute that attempted to limit the growth of chain stores.⁹⁸ Brandeis' concern was the injury caused by the chains' lower prices. He blamed this phenomenon on the "corporate form" that enabled chain operations⁹⁹ and yearned for the day when retailers were not incorporated or their size was limited.¹⁰⁰ His dissent expressed no concern whatsoever about the adverse impact of higher prices on consumers.

In sum, the neo-Brandeis movement hardly reflects new thinking on these issues. The same themes have appeared and reappeared over antitrust history. They were a prominent feature of Brandeis's campaigns in the 1910s.¹⁰¹ They reappeared in force during the Great Depression, culminating in the Robinson-Patman Act in 1936 – perhaps the most protectionist piece

⁹⁴See LYNN, CORNERED, *supra* note __ at 136-137.

⁹⁵On these rationales for RPM, see HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE §11.3 (5th ed. 2015).

⁹⁶See SAWYER, AMERICAN FAIR TRADE, *supra* note __ at 109-112.

⁹⁷Their champion here was ARTHUR JEROME EDDY, THE NEW COMPETITION: AN EXAMINATION OF THE CONDITIONS UNDERLYING THE RADICAL CHANGE THAT IS TAKING PLACE IN THE COMMERCIAL AND INDUSTRIAL WORLD (1912). See also MILTON NELSON, OPEN PRICE ASSOCIATIONS (1923); FRANKLIN D. JONES, TRADE ASSOCIATION ACTIVITIES AND THE LAW (1922).

⁹⁸*Liggett v. Lee*, 288 U.S. 517 (1933) (striking down a state statute that applied a progressive tax at a higher rate as a chain owned more stores).

⁹⁹Id. at 548-549.

¹⁰⁰Id. at 553-554.

¹⁰¹SAWYER, AMERICAN FAIR TRADE, *supra* note __.

of antitrust legislation ever passed.¹⁰² They were somewhat less successfully promoted in the late 1960s and 1970s, but undermined by Richard Nixon's election¹⁰³ just as the Chicago School was finding its voice in legal antitrust circles.¹⁰⁴ To this day a large portion of antitrust's "state action" doctrine is concerned with state legislation by which interest groups of smaller businesses seek to protect themselves from lower prices or superior technologies offered by others.¹⁰⁵

Moving forward a century, the *eBooks* case returned to some of these issues.¹⁰⁶ Several book publishers fixed the price of ebooks, which Amazon sold, and forced Amazon to raise its retail prices. Notably, both Apple and the publisher cartel members were corporations. Some of the publishers such as Hachette, Harper-Collins, and Simon & Schuster, were in fact quite large, although not as large as Amazon. While Amazon did sell ebooks at low prices, these were responsive to major changes in technology that occurred in the book market. Amazon's price reflected a reality in which the marginal cost of supply was very low, approaching zero except for royalties.¹⁰⁷ Even today books whose copyrights have expired, and are thus royalty-free, are often sold by both Amazon and others at a price of zero.¹⁰⁸

¹⁰² 15 U.S.C. §13. See discussion *infra*, text at notes ___.

¹⁰³ See, for example, the fate of the interventionist Neal Report, which was undermined by the election of Richard Nixon. *Report of the White House Task Force on Antitrust Policy* (May 27, 1969), 115 Cong. Rec. 11, 13890 (1969). See Herbert Hovenkamp, *The Neal Report and the Crisis in Antitrust*, 5 COMPETITION POLICY INT'L 217 (April 30, 2009), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1348707.

¹⁰⁴ E.g., RICHARD POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* (1976); Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U.Pa.L.Rev. 925 (1979). Cf. Frederic M. Scherer, *The Posnerian Harvest: Separating the Wheat from Chaff*, 86 YALE L.J. 974 (1977) (reviewing RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* (1976)).

¹⁰⁵ Most recently in *North Carolina State Board of Dental Examiners v. FTC*, 135 S.Ct. 1101 (2015) (state authorized cartel of dentists excludes teeth whitening by nondentists such as cosmetologists, who charged lower prices).

¹⁰⁶ *United States v. Apple, Inc.*, 992 F. Supp. 2d 263, 266 (S.D.N.Y. 2014), *aff'd*, 787 F.3d 131 (2d Cir. 2015).

¹⁰⁷ For an analysis of the cost changes justifying radical price reductions, see Herbert Hovenkamp, *Antitrust and Information Technologies*, 68 FLA. L. REV. 419, 437-445 (2016).

¹⁰⁸ Examples include JANE AUSTEN, *PRICE AND PREJUDICE*; or ALEXANDRE DUMAS, *THE THREE MUSKETEERS*. All in all, Amazon offers more than 50000 titles at a price of zero. See https://smile.amazon.com/s/ref=nb_sb_noss?url=search-alias%3Ddigital-text&field-keywords=free+kindle+books&rh=n%3A133140011%2Ck%3Afree+kindle+books

Apple organized a cartel of book publishers to impose higher prices on Amazon. There is no conceivable way that this cartel can be thought to be in the best interest of consumers.¹⁰⁹ Amazon did for a time sell some ebooks as a price that “roughly matched the wholesale price of many of its ebooks.”¹¹⁰ The New Brandeis literature suggests that this was predatory pricing.¹¹¹ A far more plausible explanation is that Amazon was engaging in promotional pricing, which is very common by sellers seeking to establish themselves in a market.¹¹² Even these prices fell far short of driving ebook prices down to competitive equilibrium levels.

The New Brandeis writing about Amazon’s alleged predatory pricing confuses predatory pricing with product development. Predatory pricing involves charging a below cost price in order to create a monopoly and earn monopoly profits later.¹¹³ By contrast, development of a new product or line may require a firm to encounter losses at an early stage, but later producing profits. The all important difference is that product development does not depend on exclusion of rivals and subsequent charging of monopoly prices, but only the ability to get one’s own output up to the point of profitability and, if needed, amortize fixed costs. Promotional pricing is often associated with introduction of a new technology or product. For example, a firm that spends a great deal developing a patented drug may require five years of sales in order to recoup its investment. But these five years of losses do not suggest predatory pricing. Rather, many worthwhile investments do not produce instant payoffs. A firm might also require several years of promotional efforts in order to make a new product profitable. Indeed a rule that condemned product investment as predatory would impose unimaginable social costs.

New Brandeisians also speak of harm caused by Amazon’s vertical integration.¹¹⁴ But who is being harmed, and how? Amazon does not make

[&ajr=0](https://www.free-ebooks.net/). Other sources of free ebooks include Free-Ebooks.Net, at <https://www.free-ebooks.net/>; and Gutenberg, at <http://www.gutenberg.org/>.

¹⁰⁹Even members of the New Brandeis movement acknowledge this. See Khan, *Amazon*, *supra* note __ at 758 (noting that the publishers feared that Amazon’s aggressive pricing for ebooks “would permanently drive down the price that consumers were willing to pay for all books.”).

¹¹⁰United States v. Apple, Inc., 952 F.Supp.2d 638, 649 (S.D.N.Y. 2013). In an earlier decision that court undertook a lengthy analysis of the predatory pricing claim and found it unsupported. United States v. Apple, Inc., 889 F.Supp.2d 623, 640-644 (S.D.N.Y. 2012).

¹¹¹Khan, *Amazon*, *supra* note __ at 757 & n. 240.

¹¹²See 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶746 (4th ed. 2015).

¹¹³See *id.*, Ch. 7C.

¹¹⁴Khan, *Amazon’s Antitrust Paradox*, *supra* note __ at 792-797.

very much of anything, so there is certainly not significant vertical integration in the traditional sense. They speak of “fulfillment-by-Amazon” (FBA) as an example of competition-destroying vertical integration.¹¹⁵ FBA is a voluntary service that independent sellers who use the Amazon website can invoke if they want Amazon to ship their products for them and manage sales. Here, not only is there no claim that FBA injures consumers; it does not even injure smaller companies who want to sell through Amazon and take advantage of FBA, which is voluntary. The vast majority of businesses who make online sales feel that they have been benefitted rather than injured by Amazon’s FBA,¹¹⁶ mainly because of FBA’s fulfillment network that gives it uncomparable proximity to customers nationwide.¹¹⁷ In sum, fulfillment-by-Amazon appears to be a practice in search of a victim.

The debate about antitrust’s noneconomic goals is hardly new either, even in response to the Chicago School. Already in the 1970s Chicago School opponents argued that antitrust had an important “political content”¹¹⁸ that could not be ignored, and that antitrust policy must consider “justice” or fairness as important noneconomic goals.¹¹⁹ The more centrist Areeda-Turner treatise, whose first volumes were published in 1978 and 1980, argued that economic analysis should dominate antitrust policy, although they left some room for other values. However, Areeda and Turner rejected “fairness” as a goal of antitrust policy, concluding that it was “a vagrant claim applied to any value that one happens to favor.”¹²⁰ Speaking of populism, they noted its concerns about big business, but also observed that a “large, powerful, and highly visible firm can also be a scapegoat for political demagoguery.”¹²¹ In criticizing their view Louis Schwartz observed that “fairness is so deeply ingrained in the antitrust tradition” that any attempt to reject it in favor of an exclusively economic antitrust jurisprudence “assumes the proportions of

¹¹⁵*Id.* at 775-776.

¹¹⁶See discussion *infra*, text at notes __.

¹¹⁷ See Khan, Amazon, *supra*, note __ at 777-778.

¹¹⁸Robert Pitofsky, *The Political Content of Antitrust*, 127 UNIV. PA. L. REV. 1076 (1979). See also Lawrence Sullivan, *Antitrust, Microeconomics and Politics: Reflections on Some Recent Relationships*, 68 CALIF. L. REV. 1 (1980).

¹¹⁹E.g., Louis B. Schwartz, “Justice” and Other Non-Economic Goals of Antitrust, 127 UNIV. PA. L. REV. 925 (1979). See also Lawrence Sullivan, *Economics and More Humanistic Disciplines: What Are the Sources of Wisdom for Antitrust?*, 125 U. PA. L. REV. 1214 (1977). For a brief retrospective, see Harry First, *Woodstock Antitrust*, CPI ANTITRUST CHRONICLE 1 (April 2018) (dating the era from 1969 to 1979).

¹²⁰1 PHILLIP E. AREEDA & DONALD F. TURNER, ANTITRUST LAW ¶109, at 21 (1978).

¹²¹*Id.* at 22.

radical historical revisionism.”¹²²

Nevertheless, Areeda and Turner also concluded that efficiency and populist goals were “broadly consistent,” because both favored competitive markets rather than concentrations of power:

... the goals of dispersed power and wider business opportunities are served by an antitrust policy which eliminated monopoly not attributable to economies of scale or superior skill, and which prevent those mergers, agreements, or practices which obstruct efficient competition. Populist goals and efficiency goals are consistent over a wide range.¹²³

Is there is a difference between the New Brandeis School and some of these predecessors? One difference is the extent of the hostility toward efficiency. In fact, some of the Open Market postings speak as if low prices are the evil that antitrust should be combatting, rather than the other way around. For example, they complain that the focus on high prices is much greater in later editions of the government’s Merger Guidelines than it was in the initial (1968) Guidelines – as if that were a bad thing.¹²⁴ They argue that a concern with efficiency lacks support in the legislative history.¹²⁵ It is true that the framers did not often articulate efficiency as such as an antitrust goal. Clearly, however, they were concerned about high prices,¹²⁶ and it is essential that the connection not be lost.

This is significant, because under the modern (non-Borkean) consumer welfare principle, low prices are the dog and efficiency is but the tail. Efficiencies are accepted as a defense or an explanation only to the extent that a practice leads to prices that are no higher than they were before the practice was put into place. Or to say this differently, low prices and high output are the true goal of antitrust, and efficiency is merely a means of attaining it.

¹²² Louis B. Schwartz, *On the Uses of Economics: A Review of the Antitrust Treatises*, 128 UNIV. PA. L. REV. 244, 251 (1979), citing HANS THORELLI, *THE FEDERAL ANTITRUST POLICY* 67-68, 91-96 (1955).

¹²³ AREEDA AND TURNER, *ANTITRUST LAW*, *supra* note __, ¶110 at 23.

¹²⁴ See, e.g., Barry Lynn, “The Consumer Welfare Standard in Antitrust: Outdated or a Harbor in a Sea of Doubt?” Testimony before the Senate Committee on the Judiciary: Subcommittee on Antitrust, Competition, and Consumer Rights, December 13, 2017.

<https://www.judiciary.senate.gov/imo/media/doc/12-13-17%20Lynn%20Testimony.pdf> (no page numbers).

¹²⁵ E.g., Khan, *Amazon*, *supra* note __ at 719-722 and *passim*.

¹²⁶ Excellently summarized in Robert Lande, *Wealth Transfers as the Original and Primary concern of Antitrust: the Efficiency Interpretation Challenged*, 50 HASTINGS L.J. 871 (1999) (examining the legislative history).

On the one hand, the neo-Brandeis movement is highly suspicious of government, and particularly of its power over the economy. It observes, quite correctly, that government is prone to corruption and special interest domination and yearns for its vision of the American economy prior to the Civil War.¹²⁷ The real problem, he believes, started with the explosion in the growth of the corporation during the gilded Age.¹²⁸ Just as the progressive critique which he emulates, the argument strongly emphasizes the role of politics in economic change, while paying little attention to changes in technology that provide at least as powerful an explanation. At the same time, however, members of the movement argue for much more heavy-handed regulation, and not in behalf of consumers.

If experience has taught us anything about this expressly political, anti-economic approach to antitrust it is that political approaches have rarely accomplished anything. They have produced a great deal of rhetoric, some remedies that were frequently very badly tailored to the challenged practices and calculated to do more harm than good.¹²⁹ Viewing the monopoly problem as political but without providing a roadmap for analyzing specific practices is a recipe for ineffectiveness and, what is worse, special interest capture. One cannot simply lament that Amazon has grown too large.¹³⁰ We also need specific rules and remedies for identifying what exactly Amazon is doing that should be remedied and what those remedies should look like. Clearly customers are not complaining about monopoly prices. If suppliers are complaining, what are the relevant practices and how are they injured?¹³¹ If there was predatory pricing in the ebook market, what is the evidence? It does not do to describe “harm to the diversity and vibrancy of ideas in the book market” as a rationale for antitrust relief, in the word of one neo-Brandeis critic¹³² -- at least not unless we can supply some metric and

¹²⁷LYNN CORNERED, *supra* note __, 24, 99-102. *See also* Lynn, “Consumer Welfare Standard,” *supra* note __.

¹²⁸ *Id.* at 225.

¹²⁹Arguing this point very forcefully was Richard Hofstadter, *Whatever Happened...*, *supra* note __; and *see* Herbert Hovenkamp, *Whatever Did Happen to the Antitrust Movement*, __ NOTRE DAME L. REV. __ (2018) (forthcoming), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3097452.

¹³⁰*E.g.*, Khan, *Amazon*, *supra* note __.

¹³¹Khan herself acknowledges that customers are happy. *Id.* at 713-716.

¹³²*See id.* at 767

Amazon's conduct would be readily cognizable as a threat under the pre-Chicago School view that predatory pricing laws specifically and antitrust generally promoted a broad set of values. Under the predatory pricing jurisprudence of the early and mid-twentieth century, harm to the diversity and vibrancy of ideas in the book market may have been a primary basis for

insistence on proof of causation. Measured by revenue, book sales in the United States have risen continuously over the past decade.¹³³ The ebook revolution has moved the price of books downward. Everyone seems to be making money. Authors' contracts calling for a strict percentage of sales prices had to be revised but that is underway.¹³⁴ Brick and mortar book sellers have suffered, but their injury has resulted largely from a technology – direct electronic distribution – that has made them superfluous to the ebook segment of the market. It is not antitrust purposes to force distribution channels to maintain institutions that no longer perform a valuable function.¹³⁵

In addition, refocusing antitrust policy so as to make political theory the driver will return us to repeated cycles of special interest capture and protected local monopoly. A good illustration is the way that the neo-Brandeisians treat one of their legislative darlings, the Robinson-Patman Act. Barry Linn describes this statute as “the clearest statement of political intent,” of protecting smaller dealers from price discrimination that favored larger dealers. He continues:

... [T]here are many excellent economic reasons to outlaw or control giant trading firms and retailers. These include their tendency to strip entire systems of their profits and thereby harm the machines, technologies, and people under their power. The authors of Robinson - Patman went out of their way to make sure we understood that although they were aware of this problem, their goal was not economic but political. The point of the law, they wrote, was to “protect the weak [from] the strong.” The “public interest” was best served not by efficiency but by keeping “trade and industry divided

government intervention. The political risks associated with Amazon's market dominance also implicate some of the major concerns that animate antitrust laws. For instance, the risk that Amazon may retaliate against books that it disfavors--either to impose greater pressure on publishers or for other political reasons--raises concerns about media freedom. Given that antitrust authorities previously considered diversity of speech and ideas a factor in their analysis, Amazon's degree of control, too, should warrant concern.

¹³³ <https://www.statista.com/statistics/560733/book-publishing-revenue-usa/>.

Measured by unit they have been flat, indicating that the per copy price has trended upwards. <https://www.statista.com/statistics/240088/total-book-sales-of-the-us-book-market-by-quantity/>.

¹³⁴ See, e.g., June Sproat, *What are the Publishing Standard Royalty Rates?* (July 19, 2017), available at <https://penandthepad.com/publishing-standard-royalty-rates-5019879.html> (noting that ebook royalty rates (25%-50%) are moving higher than for print books (10%-15%)).

¹³⁵ See Hovenkamp, *Technology*, supra note __.

among as many different parties as possible.”¹³⁶

Lina Khan agrees, suggesting that the Act’s “prohibition against price discrimination effectively curbed the power of size.”¹³⁷ In the process she praised the Supreme Court’s *Utah Pie* decision, in which a firm successfully used an earlier version of the statute to protect its local near monopoly position from competitive entry.¹³⁸

The historical record of the Robinson-Patman Act shows a very different reality. The statute was one of the strongest instances of legislative capture by a special interest group in the entire body of antitrust law. It was drafted by H.B. Teegarden, general counsel for the United States Wholesale Grocers Assn., and its principal purpose was to protect small wholesale grocers from A&P company, whose multistore operations threatened the livelihood of many family owned grocery stores.¹³⁹ The purpose did represent a value that the New Brandeisians applaud, which was to keep prices high for the benefit of very small retailers. In fact, however, this jumbled mess of a statute never succeeded in achieving even that highly questionable goal. The aggressively low priced K-Marts, Wal-Marts, and McDonald’s of the world all grew up even as it was being aggressively enforced. Because the statute applied only to “sales,” it undoubtedly fostered a great deal of vertical ownership integration. For example, a manufacturer who feared running afoul of the statute by selling to two independent dealers at different prices could avoid the problem simply by acquiring one or both dealers. Ironically, the statute did not even protect small business effectively. For example, it was used to condemn cooperatives of small firms that were organized so they could purchase goods at a lower price, which would have been a distinctly Brandeisian solution. One court noted that small dealers had “formed the cooperative associations ... for the purpose of achieving a measure of competitive parity with their larger, more aggressive rivals.”¹⁴⁰ It

¹³⁶ 114-115, citing WRIGHT PATMAN, THE ROBINSON PATMAN ACT: WHAT YOU CAN AND CANNOT DO UNDER THIS LAW 3 (1938). In a footnote Lynn laments the decline in RPA enforcement. *Id.* at 271-272 n. 29.

¹³⁷ Khan, *Amazon*, *supra* note ___ at 724.

¹³⁸ *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685 (1967). *Utah Pie* was actually not decided under the Robinson-Patman Act but rather under original §2 of the Clayton Act, which was passed in 1914 and condemned “primary line” price discrimination as a form of predatory pricing.

¹³⁹ See FREDERICK ROSE, PRICE DISCRIMINATION UNDER THE ROBINSON PATMAN ACT 10-13 (1962); Herbert Hovenkamp, *The Robinson-Patman Act and Competition: Unfinished Business*, 68 ANTITRUST L.J. 125 (2000).

¹⁴⁰ *Mid-South Distributors v. FTC*, 287 F.2d 512, 514 (5th Cir.), cert. denied,

condemned its actions under the Robinson-Patman Act nonetheless.

Conclusion: Trading Off Consumer Welfare

Much of the debate about the appropriate role of antitrust in the economy comes down to one question: Why do firms become large? For the neo-Brandeis movement, just as for the progressive critique a century earlier,¹⁴¹ the driver was politics and lax legal policy, including antitrust enforcement. For more centrist antitrust, the principal driver has been technology and innovations in distribution, but coupled with a certain amount of anticompetitive practice.

Of course, if bigness is a consequence of nothing more than politics, then we can reduce the size and reach of business firms with no welfare loss at all whatsoever. Consumer might even benefit. By contrast, if technology and innovation are a significant contributor to bigness, then deconcentration will come at a cost, and perhaps a very large one. The question then becomes whether this cost is one that members of a democratic society will be willing to bear.

One significant advantage that the consumer welfare principle has over alternative approaches focused on general welfare is that it does not require a tradeoff between higher consumer prices and efficiency gains.¹⁴² Rather, if consumer prices are higher, or output lower, we condemn the practice without regard for the welfare gains that result from the efficiency. Factually, of course, the consumer welfare principle can tolerate very large firms. Economies of scale, network economies or other cost savings may create economic preferences for larger firms or collectives, provided that their gains are passed on to consumers. If properly applied, however, the one thing it should not tolerate is ever increasing amounts of market power in the economy.

Just as general welfare proposals, the neo-Brandeisian approach to antitrust also requires a tradeoff – but it would be a far more difficult tradeoff to manage. The neo-Brandeis approach would trade off low prices and high output in favor of a set of goals defined as curbing excessive political power or large firm size, or perhaps values expressed by such things as loss of individual autonomy. The “Curse of Bigness,” as Brandeis himself put it, is an independent value in antitrust policy, to be pursued even if it harms consumers by leading to higher prices.¹⁴³ So far the Neo-Brandeis movement

368 U.S. 838 (1961) (organization of small purchasers of automobile parts); accord *Standard Motor Prod., Inc. v. FTC*, 265 F.2d 674 (2d Cir.), cert. denied, 361 U.S. 826, 80 S.Ct. 73 (1959).

¹⁴¹See discussion *supra*, text at notes __.

¹⁴²See discussion *supra*, text at notes __.

¹⁴³LOUIS D. BRANDEIS, THE CURSE OF BIGNESS: MISCELLANEOUS PAPERS OF

has been characterized by a great deal of ad hoc complaint of the nature that firms such as Amazon and Google are too big. Who the victims are, and exactly how they are injured, remains distressingly unclear.

Assuming for the moment that this goal is defensible, we would still need a metric for applying it. As decades of antitrust litigation has shown, antitrust is not good at balancing. The advantage of the consumer welfare principle is that economics gives us a set of tools for assessing the conditions that are conducive to high output and lower prices, and thus for examining the practices claimed to challenge them. That is not to say that employing these tools is easy, but over the years we have been able to improve their usefulness.

More ominously is the disregard for democratic values that the New Brandeis approach pursues. It rests on the as yet unverified assumption that people have a set of concerns about large firm size that are not expressed in their market behavior. After all, firms such as Amazon grow very large only because people buy there, perhaps even as they verbalize concerns about small retailers. For their part, small retailers who take advantage of online sales generally report a positive rather than a negative impact from firms such as Amazon.¹⁴⁴ We can debate if we want whether opinion polls or markets are more accurate reflectors of preference,¹⁴⁵ but in this case to the best of my knowledge there are not even opinion polls indicating that people who understand the consequences would prefer a world of small but higher priced firms.

While this paper defends the consumer welfare principle, it also acknowledges that antitrust could do better than it has protecting consumer interests. Several practices, such as tacit collusion, predatory pricing law's recoupment requirement, and the status of indirect purchaser plaintiffs, need to be re-examined. Further, anticompetitive practices affecting labor markets

LOUIS D. BRANDEIS (1934).

¹⁴⁴ Small retailers themselves generally report a positive impact from online sales, with more than 80% reporting increases. 68% reported "positively" to the question "How have Amazon and other online retailers impacted your business's sale." Of these, two-thirds sell through their own websites, 24% through Amazon, and 22% through eBay. The numbers add up to more than 100 because several retailers use multiple platforms. See <https://www.insureon.com/resources/research/small-business-online-sales-revenue-poll> (last visited June 12, 2018).

¹⁴⁵ For a thoughtful discussion, pointing out the strengths and weaknesses of both methodologies in political markets, see S. G. Kou and Michael E. Sobel, *Forecasting the Vote: A Theoretical Comparison of Election Markets and Public Opinion Polls*, 12 POLITICAL ANALYSIS 277 (2004).

need to be taken more seriously.¹⁴⁶ While antitrust policy is certainly not the only reason wages fail to keep up with economic growth, its lack of attention in this area is at least a contributor. One place that antitrust under the consumer welfare principle and neo-Brandeisian antitrust policy can agree is that concentration does matter, although they currently disagree about how it should be included in the calculus of competitive harm. The antitrust concern with high concentration is a means to an end – namely, control of higher prices – rather than an end in itself.¹⁴⁷

Antitrust policy should also be more concerned than it currently is with anticompetitive mergers. One area in particular is large tech firm acquisitions of smaller highly innovative rivals. Another is vertical mergers. For example, Amazon's acquisition of Quidsi in 2010 very likely warranted closer scrutiny than it received. Quidsi was a nascent competitor, selling diapers and other household products. When Quidsi initially resisted Amazon's overtures Amazon cut its own price on several products that Quidsi also produced.¹⁴⁸ The use of aggressive pricing to reduce the value of a takeover target or force it to sell out is often alleged to be an anticompetitive strategy, and it is certainly worth a second look.¹⁴⁹

The important point, however, is that established antitrust tools are up to these tasks. More importantly, every story has two sides and the consumer welfare principle is the best mechanism for assessing the harm that they cause. Mergers such as the Amazon acquisition of Quidsi should not be pursued simply because they make Amazon bigger or stretch its activities into new markets. They should be condemned when they enable Amazon to reduce output, diminish quality, or charge higher prices, perhaps by choking off an emergent competitor. In sum, these are fixes that result from proper application of the consumer welfare principle, not from jettisoning it.

Finally is the problem of transparency, which I believe will ultimately prove dispositive. The Neo-Brandeisian attack on low prices as a central antitrust goal is going to hurt consumers, but it is going to hurt vulnerable consumers the most. For example, to the extent that the United States Democratic Party becomes the institution to embrace its concerns, it will be harming its own constituencies the most. As a result, to the extent that is

¹⁴⁶ See discussion *supra*, text at notes __.

¹⁴⁷ See Herbert Hovenkamp & Carl Shapiro, *Horizontal Mergers, Market structure, and Burdens of Proof*, 127 YALE L.J. 1996 (2018).

¹⁴⁸ See Khan, *Amazon*, *supra* note __ at 768-769.

¹⁴⁹ Malcolm R. Burns, *Predatory Pricing and the Acquisition Cost of Competitors*, 94 J. POL. ECON. 266 (1986). On the theory, see Christopher R. Leslie, *Revisiting the Revisionist History of Standard Oil*, 85 S.CAL. L. REV. 573 (2012); Patrick Bolton, Joseph F. Brodley, and Michael H. Riordan, *Predatory Pricing: Strategic theory and Legal Policy*, 88 GEO. L.J. 2239 (2000).

communicated in advance it could spell political suicide. Setting aside economic markets, a neo-Brandeis approach whose goals were honestly communicated could never win in an electoral market, just as it has never won in traditional markets.

Should competition authorities care about fairness and if so how?

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CRESSE 2018

13th International Conference on Competition and Regulation

Heraklion - Crete, Greece

29h June – 1st July 2018

Issues to be discussed

- 1) Unfair practices and competition law
- 2) The crumbling consensus on liberal economic policies
- 3) Globalization and its discontent
- 4) Unfairness and its relationship to competition law enforcement
- 5) The role of unfairness in labour markets
- 6) Unfairness and competition: some tentative conclusions

Three underlying questions

Are unfair **practices** anticompetitive practices ?

Does competition law enforcement make the **process** of competition fair?

Is the **result** of the competitive process fair ?

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Drivers of economic resentment

Economic resentment: Drivers: Economic insecurity, inequality and stagnation

This resentment is driven by **the consequences of globalization on the distribution of jobs, wealth and income** and by the **disruptions that globalization implies in terms of increased competition.**

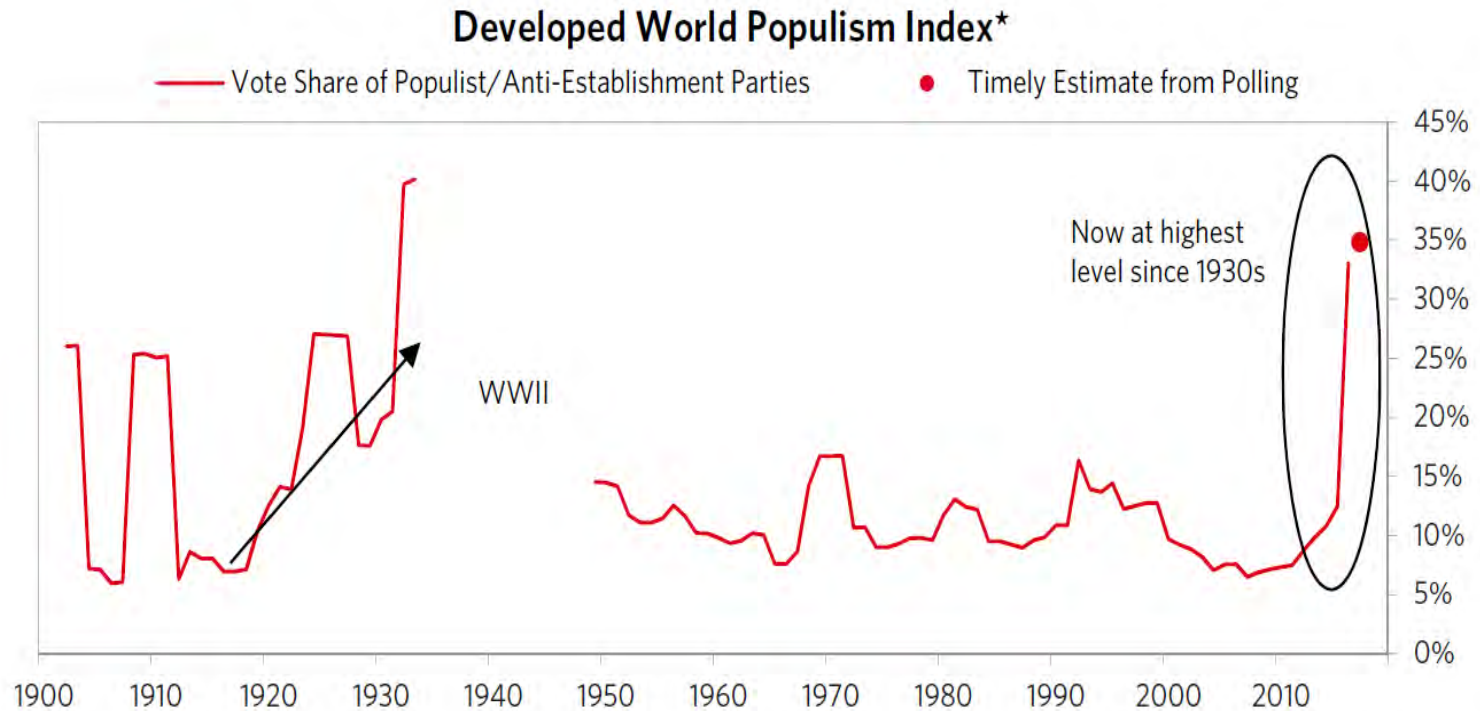
By claiming that economic liberalisation and globalisation benefit society, the elite and the media are considered to be « lying » and « pushing an agenda which works against the people ».

Growing rejection of competition as part of the socio-economic social contract

(...) it seems that at least in some economies **the socio-economic social contract is not working well in practice**. Recent years have envisaged an increased rate of dissatisfaction with market economies.

A growing number of citizens believe that the promises of the competition based market system, which form an important part of the implicit social contract, are not fulfilled and that capitalistic markets are no longer working in their favor. Indeed, statistics indicate that social mobility is low; that wealth is aggregated disproportionately in the hands of the already well-off; that wealth inequality keeps rising; that several large firms dominate the digital economy, thereby blocking at least some of the promises that technological changes were thought to bring about; that technological changes such as robotics create significant disruption effects and have negative implications on the labor market; or that education and social security do not create viable solutions for workers in order to ensure that wide geographic areas or demographic groups are not significantly and irreparably harmed.

Resurgence of populism in the world

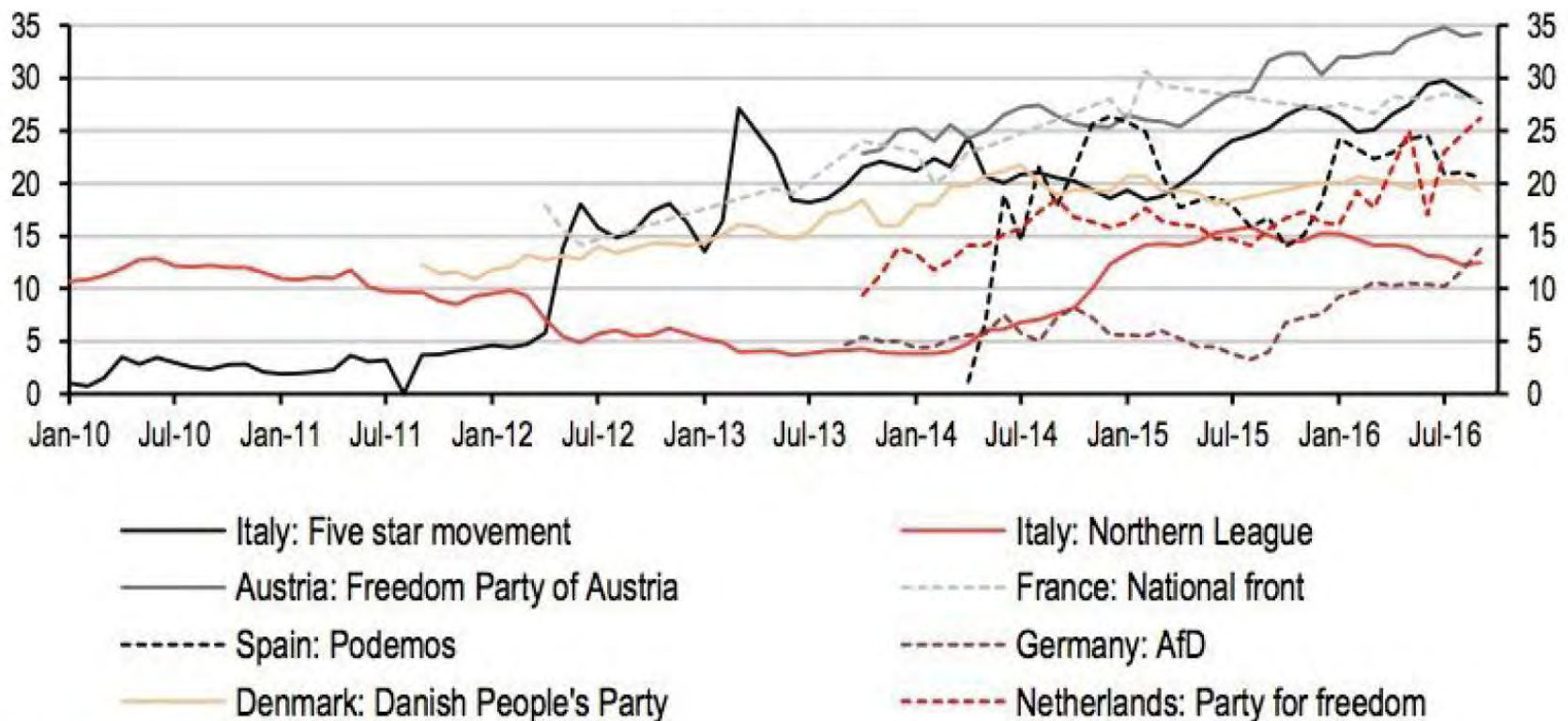


*The latest point includes cases like Trump, UKIP in the UK, AfD in Germany, National Front in France, Podemos in Spain, and Five Star Movement in Italy.

1) Bridgewater Associates, 2007, Ray Dalio Steven Kryger Jason Rogers Gardner Davis

The rise of populist movements in Europe

11. ...which has contributed to the rise of populist and euro-sceptic parties across



Source: Various domestic polls

Right wing and left wing populist platforms in Europe

New York Times, European Populism in the Age of Donald Trump
 JEREMY ASHKENAS and GREGOR AISCH DEC. 5, 2016

Left Wing Populism

		Anti-austerity	Anti-globalization	Anti-eurozone	Anti-establishment	Anti-European Union	Anti-immigration	Anti-Islam
Podemos Spain	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Syriza Greece	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Five Star Movement Italy	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Right Wing Populism

UKIP The United Kingdom	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
National Front France	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
Freedom Party The Netherlands	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
Alternative for Germany Germany	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
Freedom Party Austria	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>



Inequality and the vote for Trump

Table 1: Regression estimate for the determinants of the share of Trump votes relative to the average of the Republican candidate votes in 2004, 2008 and 2012

	Model A	Model B	Model C	Model D
Gini coefficient	0.60** (2.06)	0.64* (1.97)	0.98** (2.38)	0.80** (2.41)
Share of Hispanics	-0.19*** (-3.39)		-0.21*** (-3.65)	-0.22*** (-3.62)
Share of foreign-born population		-0.25** (-2.32)		
Share of population aged 18-44	-0.71** (-2.62)	-0.71** (-2.45)	-0.75*** (-2.76)	-0.49 (-1.51)
Share of population with a high school diploma or less	0.24** (2.13)	0.21 (1.66)	0.26** (2.26)	0.30** (2.45)
Share of male population			1.24 (1.29)	
Share of African-American population				-0.090 (-1.23)
Constant	-0.10 (-0.77)	-0.11 (-0.74)	-0.88 (-1.43)	-0.28 (-1.43)
R-squared	0.49	0.43	0.51	0.51
Observations	51	51	51	51

Inequality and the vote for Brexit

	Model A	Model B	Model C	Model D
Share of population aged 20-34	-0.49 [-4.0]	-0.95 [-6.6]		
Share of population aged 65 and over			0.45 [3.2]	0.69 [3.7]
Share of population with a degree	-0.97 [-11.9]		-1.05 [-13.5]	
Share of population without qualification		0.58 [4.9]		0.64 [5.0]
Disposable income per inhabitant	0.04 [1.9]	-0.08 [-3.2]	0.05 [2.0]	-0.09 [-3.3]
Gini coefficient of income inequality	0.77 [2.6]	0.89 [2.4]	0.93 [3.1]	1.24 [3.1]
Poverty rate	1.00 [3.0]	0.85 [1.9]	1.06 [3.1]	0.95 [2.0]
Unemployment rate	-0.14 [-0.7]	-0.06 [-0.2]	-0.34 [-1.7]	-0.48 [-1.6]
Share of non-UK born population	-0.02 [-0.3]	0.01 [0.1]	-0.05 [-0.6]	-0.12 [-1.2]
Scotland	-19.64 [-17.9]	-19.99 [-14.2]	-19.92 [-18]	-20.73 [-13.7]
Northern Ireland	-14.61 [-6.5]	-17.15 [-6.0]	-14.13 [-6.1]	-17.38 [-5.5]
Wales	-5.30 [-3.9]	-6.82 [-3.9]	-6.00 [-4.3]	-8.39 [-4.5]
London	-8.84 [-2.9]	-11.71 [-3.0]	-9.27 [-3.0]	-12.78 [-3.1]
R2	0.85	0.76	0.85	0.72

Issues to be discussed

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The economic consensus on international trade and competition

A reasonable summary of the consensus around 2000 was:

- (i) **Trade had not been a major contributor to declining manufacturing employment or rising wage inequality in developed countries over the past several decades.**
- (ii) **If displaced by trade, workers employed in regions specializing in import-competing sectors could easily move to other labor markets.**
- (iii) Due to the “law of one price” for skills—meaning that skills, like currency, have the same market value anywhere within a given **country—any adverse effects of trade on low-skilled workers would reduce the wages of this group nationally, rather than primarily affecting the outcomes of trade-exposed workers.**

DAVID H. AUTOR, Trade and labor markets: Lessons from China’s rise, IZA World of Labor, February 2018

Disruptions due to international trade

Economists have long recognized that free trade has the potential to raise countries' living standards.

But what applies to a country as a whole need not apply to all its citizens.

Workers displaced by trade **cannot change jobs costlessly**, and by **reshaping skill demands, trade integration is likely to be permanently harmful to some workers and permanently beneficial to others**. The “China Shock”—denoting China’s rapid market integration in the 1990s and its accession to the World Trade Organization in 2001—has given new, unwelcome empirical relevance to these theoretical insights.

Effect of Chinese imports on affected zones in the US

Over the period 1990 to 2007, (Commuting Zones) that were more exposed to import competition from China experienced substantially greater reductions in manufacturing employment.

Contrary to the established understanding of US labor markets as fluid and flexible, over the course of a decade, trade-induced manufacturing declines in CZs were not offset by sectoral reallocation or labor mobility. Instead, overall CZ employment-to-population rates fell at least equally with manufacturing employment rates, and generally by slightly more. (...) **The fact that these localized effects endure for the span of (at least) a decade suggests that the effects of trade shocks on labor markets are likely amplified by slow and incomplete adjustment. They also reveal that adjustment does not accrue primarily along the wage margin(...); sizable falls are instead found in employment rates within trade-impacted local labor markets.**

Analyses for Denmark, Norway, and Spain, covering periods from the late 1990s to 2007, find results that are consistent with the US evidence, suggesting that the phenomenon is not exclusive to the US

No compensating effect on employment in non-exposed local industries

Considering both those industries that are directly exposed to import competition and those that are indirectly exposed, the analysis finds that import growth from China between 1999 and 2011 led to an employment reduction of 2.4 million workers.

There is little evidence to suggest, however, that employment gains in non-exposed local industries substantially offset these losses. Indeed, the estimated employment decline is actually larger than the 2.0 million job loss estimate when considering only direct and input–output effects.

DAVID H. AUTOR, Trade and labor markets: Lessons from China's rise, IZA World of Labor, February 2018

Do all workers suffer equally ?

In a frictionless labor market where workers move quickly across firms, industries, and regions, wages should adjust uniformly within skill groups in response to a trade shock, even if only a subset of industries or regions is directly exposed. If worker mobility is imperfect across jobs and locations, however, trade shocks can have heterogeneous impacts across workers within the same skill groups.

.
A 2014 study uses longitudinal data from the US Social Security Administration to compare workers with similar demographic characteristics and previous labor market outcomes, but who differ according to the subsequent trade exposure of their 1991 industry of employment.

Those initially employed in subsequently trade-exposed industries accumulate substantially lower earnings over the period 1992–2007. Although workers who become trade-exposed due to initial industry affiliation move among jobs at a higher rate than those who are not trade-exposed, **this trade-induced job mobility is shown to be insufficient to offset the difference in career earnings between more and less trade-exposed workers.**

Are high earners less affected than low earners ?

Although trade shocks affect both high- and low-wage individuals, there are substantial differences between their patterns of adjustment.

Workers whose pre-shock wages are in the top earnings tercile of their age cohort respond primarily by relocating to firms outside the manufacturing sector, and they do not lose earnings relative to their peers who started out in less trade-exposed industries.

By contrast, **workers in the bottom tercile of pre-shock earnings react by relocating primarily within the manufacturing sector, often remaining in industries that are hit by subsequent increases in import competition. These low-wage workers experience substantial differential earnings losses, as they earn less per year both while working at the initial firm and after relocating to new employers.**

DAVID H. AUTOR, Trade and labor markets: Lessons from China's rise, IZA World of Labor, February 2018

Attempts to help reallocation do not work

TAA, the federal government's primary program to help workers who lose their jobs due to foreign competition, offers extended unemployment benefits of up to 18 months, where eligible workers may obtain allowances toward relocation, job search, and health care, as long they remain enrolled in a training **program has a negligible impact on easing local adjustment to trade shocks.**

What do we learn from the trade debate ?

- Competition create winners and losers
- **Labor markets do not adjust as economic theory suggests they do** and exogeneous shocks lead to both higher unemployment and lower wages in competition-exposed markets.
- The **losers of (international) competition are low-skilled wage earners**. Even when they find new jobs, they tend to earn less than they did before competition set in.
- **Capital is definitively on the winning side since it is very mobile**
- **Attempts to help low-skilled labor reallocate do not work well**
- (International) competition, even though it has global advantages is detrimental to the interests of some economic groups and is thus seen by them as unfair.**

Economic globalization has been mismanaged

“I would say **the agenda for globalization has become very imbalanced.**

There are **specific groups that are benefiting handsomely, and there are groups that have lost out.** The challenge is not to reverse or oppose globalization.

I think the **challenge is to rebalance it in a way that will provide broad gains to many groups who feel they have been excluded.**

I do think we've mismanaged this process badly.

The forces that have gained, the right-wing populists, don't have a stake in either liberal democracy or the liberal world economy, and both are at stake right now. But I do think there is a way out.

It's going to require alternatives to the narrative of the right-wing populists, and I'm hoping that will come about.”

1) Interview de Dani Rodrik, Professor of economics at the Kennedy School of Government, Harvard University, « The rise of populism shouldn't have surprised anyone”, Washington Post, August 10 2017

The mismanagement of globalization has led to a questioning of competition

(T)oday fairness is regaining prominence in competition policy discourse. This is in part the result of a broader discontent with globalization and related challenges to the free trade consensus, at least partially in response to the market disruptions caused by international trade, technology and other factors. Within domestic markets, the return of fairness concerns is closely linked to the perceived decrease in the levels of market competition, a general trend observable in particular in the U.S., which manifests itself in three specific forms: (1) evidence of increasing levels of market concentration; (2) decreasing levels of new business entry; and (3) increasing importance of winner-take-all markets as a result of technological change.

As a result of these trends, a surge of fairness claims permeate contemporary competition policy debates where an increasing number of scholars and commentators have advocated stronger incorporation of equity considerations in order to address distributive concerns.

Growing rejection of competition as part of the social contract

(...) it seems that at least in some economies **the socio-economic social contract is not working well in practice**. Recent years have envisaged an increased rate of dissatisfaction with market economies.

A growing number of citizens believe that the promises of the competition based market system, which form an important part of the implicit social contract, are not fulfilled and that capitalistic markets are no longer working in their favor. Indeed, statistics indicate that social mobility is low; that wealth is aggregated disproportionately in the hands of the already well-off; that wealth inequality keeps rising; that several large firms dominate the digital economy, thereby blocking at least some of the promises that technological changes were thought to bring about; that technological changes such as robotics create significant disruption effects and have negative implications on the labor market; or that education and social security do not create viable solutions for workers in order to ensure that wide geographic areas or demographic groups are not significantly and irreparably harmed.

Should we change standards to address inequality ?

The consumer welfare standard also helps address inequality because it does not permit conduct that would harm consumers while benefiting shareholders. In contrast, the aggregate welfare standard can contribute to inequality by permitting conduct that leads to the creation and exercise of market power, if there are also cost savings or other efficiencies associated with the conduct and they are not shared with buyers. Under those circumstances, market power increases producer surplus that accrues primarily to shareholders and top executives, who typically are wealthier than the consumers of the products.

Application of a consumer welfare standard in principle could increase inequality in matters where consumers tend to be wealthy and the sellers are small firms owned by middle-class entrepreneurs, such as hypothetical cartels among worker-owned manufacturers of luxury goods like fine crystal products or yachts. However, we expect those situations are rare. **Overall, therefore, the continued application of a consumer welfare standard likely would lead to less inequality than a change to reliance on an aggregate economic welfare standard.**

Should we change standard to address inequality ?

In our view, although many countries have through time converged toward consumer welfare as the predominant objective of their competition laws – an ascendance that reflects some notions of distributive justice and fairness toward consumers – the normative force of the consumer welfare standard remains fragile.

Despite being usually justified by a distributive justice rationale, we believe that the consumer welfare standard does not vindicate distributional equity concerns for consumers *vis-à-vis* producers, and we believe that such choice of welfare standard does not represent an optimal tool for redistributive goals.

On the contrary, **we view the consumer welfare standard as resulting from a mix of poorly defined distributive concerns and more political economy-oriented explanations.** Under the latter perspective, the ascendance of the consumer welfare standard may be interpreted as a political bargain between self-interested groups of producers (primarily large firms defending the efficiency benefits of economies of scale) and consumers (including final consumers, small buyers, farmers), where **the concept of “consumer welfare” can be seen as a more acceptable form of welfare standard for non-specialist audiences, which would politically allow the advancement of economic goals in the competition policy domain.**

Fairness is the problem, not inequality

“Inequality has been named as a culprit in the populist incursions of 2016 and 2017 (...)what is inequality, and what role does it play in inhibiting or encouraging growth, or in undermining democracy? Does inequality kill, say, by driving people to suicide or to "deaths of despair"? Or is inequality a necessary evil that we must tolerate at certain levels?

These are questions I am often asked. But, truth be told, none of them is particularly helpful, answerable, or even well posed.

Inequality is not so much a cause of economic, political, and social processes as a consequence. Some of these processes are good, some are bad, and some are very bad indeed. Only by sorting the good from the bad (and the very bad) can we understand inequality and what to do about it.

Moreover, **inequality is not the same thing as unfairness; and, to my mind, it is the latter that has incited so much political turmoil in the rich world today.** Some of the processes that generate inequality are widely seen as fair. But others are deeply and obviously unfair, and have become a legitimate source of anger and disaffection”.

Fairness is the problem, not inequality

“There are two different explanations for the divergence between median and top incomes, and it matters a great deal which one is correct. The first attributes it to impersonal and unstoppable processes such as globalisation and technological innovation, which have devalued low-skill labour and favoured the well educated.

The second explanation is more sinister. It holds that median-income stagnation is the direct result of rising incomes and wealth at the top. In this account, the rich are getting richer at the expense of everyone else.

Recent research suggests there is some truth to the second story, at least in the United States. Although globalisation and technological change have disrupted traditional work arrangements, both processes have the potential to benefit everyone. The fact that they have not suggests the wealthy have captured the benefits for themselves.

Angus Deaton

Issues to be discussed

- 1) Unfair practices and competition law
- 2) The crumbling consensus on liberal economic policies
- 3) Globalization and its discontent
- 4) Unfairness and its relation to competition law enforcement**
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What is fairness ?

Implicit in the debate between critics and proponents of fairness, is however an **overly broad, undefined notion of fairness, which in our view fails to advance the debate**. In contrast, we highlight the need to **assess specific dimensions of fairness that are pertinent to the domestic competition policy domain**, which we evaluate in turn.

(...) we identify the following specific notions of fairness that are pertinent to domestic markets:

vertical fairness (between producers and consumers);

horizontal fairness on the demand side (between consumers);

horizontal fairness on the supply side (between producers);

procedural fairness (due process and private enforcement).

Behavioural economics and vertical fairness

The approach of the present study is purely descriptive. Normative status is not claimed for the generalizations that are described as "rules of fairness," and the phrase "it is fair" is simply an abbreviation for "a substantial majority of the population studied thinks it fair."

The paper considers in turn **three determinants of fairness judgments:**

- 1) the **reference transaction**,
- 2) the **outcomes to the firm and to the transactors**, and
- 3) the **occasion for the action of the firm**

Daniel Kahneman, Jack L. Knetsch and Richard Thaler "Fairness as a Constraint on Profit Seeking: Entitlements in the Market, *The American Economic Review*, Vol. 76, No. 4 (Sep., 1986), pp. 728-741

Vertical fairness and reference transaction: the principle of dual entitlement

The main findings of this research can be summarized by a **principle of dual entitlement, which governs community standards of fairness**:

Transactors have an entitlement to the terms of the reference transaction and firms are entitled to their reference profit.

A firm is not allowed to increase its profits by arbitrarily violating the entitlement of its transactors to the reference price, rent or wage (Max Bazerman, 1985; Zajac, forthcoming). When the reference profit of a firm is threatened, however, it may set new terms that protect its profit at transactors' expense.

Vertical fairness and reference transaction: principle of dual entitlement

Example

A small photocopying shop has one employee who has worked in the shop for six months and earns \$9 per hour. Business continues to be satisfactory, but a factory in the area has closed and unemployment has increased. Other small shops have now hired reliable workers at \$7 an hour to perform jobs similar to those done by the photocopy shop employee. The owner of the photocopying shop reduces the employee's wage to \$7.

(N = 98) **Acceptable 17%** **Unfair 83%**

A small photocopying shop has one employee... [as in previous question]... The current employee leaves, and the owner decides to pay a replacement \$7 an hour.

(N = 125) **Acceptable 73%** **Unfair 27%**

Vertical fairness and reference transaction: principle of dual entitlement

Implications

An increase in price by a firm not justified by an increase in cost or by an increase in the price of a competitor is likely to be seen as unfair (even if it is not anticompetitive)

An increase in price following an increase in price by a competitor or an increase in cost is likely to be seen as fair (even if it may be anticompetitive)

Vertical fairness and outcomes to the firm and its transactors

The outcome to the firm is evaluated with respect to the reference profit, and incorporates the effect of exogenous shocks (for example, changes in wholesale prices) which alter the profit of the firm on a transaction at the reference terms.

An action by a firm is more likely to be judged unfair if it causes a loss to its transactor than if it cancels or reduces a possible gain.

Similarly, an action by a firm is more likely to be judged unfair if it achieves a gain to the firm than if it averts a loss. Different standards are applied to actions that are elicited by the threat of losses or by an opportunity to improve on a positive reference profit **-a psychologically important distinction which is usually not represented in economic analysis.**

Judgments of fairness are (...) susceptible to framing effects, in which form appears to overwhelm substance.

Vertical fairness and outcomes to the firm and its transactors

Example

A shortage has developed for a popular model of automobile, and customers must now wait two months for delivery. A dealer has been selling these cars at list price. Now the dealer prices this model at \$200 above list price.

(N = 130) **Acceptable 29%** **Unfair 71%**

Question B..... A dealer has been selling these cars at a discount of \$200 below list price. Now the dealer sells this model only at list price.

(N = 123) **Acceptable 58%** **Unfair 42%**

Daniel Kahneman, Jack L. Knetsch and Richard Thaler "Fairness as a Constraint on Profit Seeking: Entitlements in the Market, *The American Economic Review*, Vol. 76, No. 4 (Sep., 1986), pp. 728-741

Vertical fairness and outcomes to the firm and its transactors

Implications

A cartel to **reduce discounts** is **less likely to be seen as unfair** than a cartel to increase prices.

A cartel to **slow down a decline in price** is **less likely to be seen as unfair** than a cartel to increase price.

A cartel **to pass on an increase in cost** is **less likely to be seen as unfair** than a cartel to increase profits (without cost increase)

A **cartel crisis** among firms losing money is more **less likely to be seen as unfair** than a cartel among profit making firms to increase their profits

Daniel Kahneman, Jack L. Knetsch and Richard Thaler "Fairness as a Constraint on Profit Seeking: Entitlements in the Market, *The American Economic Review*, Vol. 76, No. 4 (Sep., 1986), pp. 728-741

Vertical fairness: occasions in which a firm may reconsider the terms that it sets for exchanges

Three classes of occasions in which a firm may reconsider the terms that it sets for exchanges.

- (i) **Profit reductions**, for example, by rising costs or decreased demand for the product of the firm.
- (ii) **Profit increases**, for example, by **efficiency gains or reduced costs**.
- (iii) **Increases in market power**, for example, by temporary excess demand for goods, accommodations or jobs

Vertical fairness and allocation of gains

Example

1) A small factory produces tables and sells all that it can make at \$200 each. Because of changes in the price of materials, the cost of making each table has recently decreased by \$40. The factory reduces its price for the tables by \$20.

(N = 102) **Acceptable 79%** **Unfair 21%**

2) the cost of making each table has recently decreased by \$20. The factory does not change its price for the tables.

(N = 100) **Acceptable 53%** **Unfair 47%**

Daniel Kahneman, Jack L. Knetsch and Richard Thaler "Fairness as a Constraint on Profit Seeking: Entitlements in the Market, *The American Economic Review*, Vol. 76, No. 4 (Sep., 1986), pp. 728-741

Vertical fairness and allocation of gains

Implications

A cartel to prevent the passing on of a decrease in cost (either through a decline in price or through an increase in discounts) is unlikely to be considered unfair

The fact that two merging firms maintain their price after the merger even though they benefit from efficiencies is unlikely to be considered unfair

Vertical fairness and exploitation of increased market power

Conventional economic analyses assume as a matter of course that excess demand for a good creates an opportunity for suppliers to raise prices, and that such increases will indeed occur. **The profit-seeking adjustments ,that clear the market are in this view as natural as water finding its level-and as ethically neutral.**

The lay public does not share this indifference. **The increase in price to take advantage of a shortage is widely seen as unfair even when close substitutes exist.**

Respondents were nearly unanimous in condemning a store that raises prices when its sole competitor in a community is temporarily forced to close.

Community standards of fairness effectively require the firm to absorb an opportunity cost in the presence of excess demand, by charging less than the clearing price or paying more than the clearing wage.

Daniel Kahneman, Jack L. Knetsch and Richard Thaler "Fairness as a Constraint on Profit Seeking: Entitlements in the Market, *The American Economic Review*, Vol. 76, No. 4 (Sep., 1986), pp. 728-741

Vertical fairness and exploitation of increased market power

Implications

- Monopoly pricing for consumer goods is likely to be seen as unfair.
- Abuse of economic dependency is likely to be seen as unfair
- Price discrimination for consumer goods is likely to be seen as unfair
- Auctions of consumer goods are likely to be seen as unfair
- Monopoly pricing for durable goods which can store value is likely to be seen as fair since consumers can resale the good at an equivalent or higher price

What do we learn about fairness from Kahneman and others ?

Fairness is an argument in the utility function of at least some consumers (a fact usually not taken into consideration by competition authorities). However fairness is a complex concept and needs to be elaborated in any discussion of its impact on human behaviour

Depending on the circumstances profit maximization and pro-competitive behaviour may be perceived to be fair or unfair. Competition law enforcement is not necessarily seen as being fair to consumers and more competition is not necessarily perceived as leading to more vertical fairness.

The refusal of many competition authorities to deal with issues of abuse of dependency or excessive prices or to treat crisis cartels leniently or their use of auctions theory, their treatment of multi-sided markets (see for exemple the recent American Express US Supreme court decision) , as well as their reluctance to be lenient with respect to cartels passing on increases in costs , or their fondnes for auctions may lead the general public to regard their activity as occasionally (vertically) unfair.

Issues to be discussed

- 1) Unfair practices and competition law
- 2) The crumbling consensus on liberal economic policies
- 3) Globalization and its discontent
- 4) Unfairness and its relation to competition law enforcement
- 5) **The role of unfairness in labour markets**
- 6) Unfairness and competition: some tentative conclusions

Consequences of fairness motives on market mechanisms

Almost all economic models assume that all people are exclusively pursuing their material self-interest and do not care about "social" goals per se.

This may be true for some (maybe many) people, but it is certainly not true for everybody.

By now we have substantial evidence suggesting that fairness motives affect the behavior of many people.

The empirical results of Kahneman, Knetsch, and Thaler [1986], for example, indicate that **customers have strong feelings about the fairness of firms' short-run pricing decisions which may explain why some firms do not fully exploit their monopoly power.**

Ernst Fehr and Klaus M. Schmidt "A Theory of Fairness, Competition, and Cooperation, *The Quarterly Journal of Economics*, Vol. 114, No. 3 (Aug., 1999), pp. 817-868

Fairness and labor markets

We conclude that competition renders fairness considerations irrelevant if and only if none of the competing players can punish the monopolist by destroying some of the surplus and enforcing a more equitable outcome.

This suggests that fairness plays a smaller role in most markets for goods than in labor markets.

This follows from the fact that, in addition to the rejection of low wage offers, workers have some discretion over their work effort. By varying their effort, they can exert a direct impact on the relative material payoff of the employer. Consumers, in contrast, have no similar option available. Therefore, a firm may be reluctant to offer a low wage to workers who are competing for a job if the employed worker has the opportunity to respond to a low wage with low effort. **As a consequence, fairness considerations may well give rise to wage rigidity and involuntary unemployment.**

Ernst Fehr and Klaus M. Schmidt "A Theory of Fairness, Competition, and Cooperation, The Quarterly Journal of Economics, Vol. 114, No. 3 (Aug., 1999), pp. 817-868

The antitrust paradox (Bork)

“Consumer welfare is greatest when society’s economic resources are allocated so that consumers are able to satisfy their wants as fully as technological constraints permit. Consumer welfare, in this sense, is merely another term for the wealth of nations. **Antitrust has a built-in preference for material prosperity, but it has nothing to say about the ways prosperity is distributed or used**”.

Commissioner Vestager on fairness

I'm especially glad to join you to look at one of the most fundamental questions in our work. What, exactly, is competition policy for?

(...) the fact is, the **competition rules** aren't there just because we think that competition is a good thing in itself. Like any of the other rules that govern our world, we have competition rules because we believe they make our society a better place to live. That they **make our markets work more fairly for consumers**.

That doesn't mean that we at the Commission see ourselves as superheroes, solving all unfairness, and righting every wrong. It doesn't mean that just because something is unfair, it's automatically also against the competition rules. **All it means is that simply by doing our job – simply by enforcing the competition rules in our Treaty – we do our bit to make Europe a fairer place to live.**

“Fairness and competition, GCLC Annual Conference, Brussels, 25 January 2018”

Issues to be discussed

- 1) Unfair practices and competition law
- 2) The crumbling consensus on liberal economic policies
- 3) Globalization and its discontent
- 4) Unfairness and its relation to competition law enforcement
- 5) The role of unfairness in labour markets
- 6) **Unfairness and competition: some tentative conclusions**

**Thank you very much
frederic.jenny@gmail.com**

“AMERICA FIRST”, POPULISM AND ANTITRUST : TRANSATLANTIC REFLECTIONS

Fordham University's 45th Annual Conference on International Antitrust Law & Policy
New York City, 6-7 September 2018

Mario Monti *

“You are paying more in America than you would in Europe”, warn professors Germàn Gutiérrez and Thomas Philippon of NYU's Stern School in their WorldPost opinion (13 August) showing that US consumers are less well off than their counterparts in the European Union.

“Only two decades ago”, they note, “the United States was effectively the land of free markets and a leader in deregulation and antitrust policy”. Around the turn of the century, however, through “deliberate policy choices [...] European countries created the single market, which took effect in 1993, and deregulated their domestic markets. Today most European Union countries”, the authors say, “score better than the United States in enacting policies that make industries more competitive. Not surprisingly, antitrust enforcement remains active in Europe. Meanwhile in the United States, deregulation and antitrust efforts have nearly ground to a halt”. “If America wants to lead once more in this realm”, they conclude, “it must remember its own history and relearn the lessons it successfully taught the rest of the world”.

Not only does this raise important economic and political issues, but it also begs the question of whether President Trump's motto “America first” can inspire public policies with the brightness of a guiding star or is likely to break down into a nebulous star dust. For example, at least over the short and medium term, certain policies to make “American industry first” may not coincide with policies to make “American consumers first” or “American workers first”. Antitrust is an area where consumers' interests are usually pursued more directly than producers' interests, be they the interests of businesses or of workers.

At the time when, according to Gutiérrez and Philippon, Europe was waking up, I worked, as a European commissioner, first, to make a single market out of the various domestic markets and later to achieve and maintain competition in that single market. During those years the degree of activism of the European Commission began to exceed that of the American Antitrust agencies under President George W. Bush. Yet, we were keen on working together with our American colleagues and were almost always able to avoid open conflicts.

In the area of antitrust policy, or competition policy as we call it in Europe, the last two decades have brought about an impressive convergence between the US and the EU and, more gradually, at the global level. This was greatly helped by work done at the International Competition Network, set up in 2002 at the joint initiative of the US Justice Department, the Federal Trade Commission and the European Commission.

Europe clearly owe to the Americans the historical primacy, ever since the advent of antitrust legislation in the late 19th century. Competition policy in Europe is much more recent, having been developed in the context of EU integration since the 1950's. Yet, the European system has in turn some strong points, relative to an American system which has been somewhat slower in adapting to new challenges.

Concerning the scope of competition policy, the EU embraces in it not just antitrust but also state-aid control and other forms of oversight on national governments conduct in economic and financial markets. Single-market policy, liberalization policy and competition policy have reinforced each other within a coherent vision.

There was, on the other hand, a substantive advantage on the American side, certainly until the early 2000's : the wider and deeper use of economic analysis in antitrust. But the Commission caught up considerably since it set up in 2003 the position of Chief Competition Economist with adequate resources and incisive ways to be heard.

Against this background, observing in particular the activism of Commissioner Margrethe Vestager in cases concerning high tech, big data and digital platforms, many have suggested that the European Union is now well ahead of the United States in terms of pursuing vigorous competition policy. Among these, Gutiérrez and Philippon urge the US not to remain behind. “If the United States is to better serve its middle class, then it must refresh its faith in free markets, bearing in mind three key principles”.

I agree on two of those : 1) “Washington must remember that antitrust and deregulation” should be “a bipartisan affair : it was Democratic President Jimmy Carter who oversaw airline deregulation and Republican President Ronald Reagan, the break-up of AT&T” ; and 2) “Policymakers need to innovate. Regulation needs to evolve and adapt to new technologies. [...] America's harsh response to the European privacy law, known as the General Data Protection Regulation, for example, demonstrates its disregard for innovative regulation”.

I am less convinced by the authors' third principle, calling the courts in the US to “hold regulators to high but not impossible standards”. As formulated, the principle seems obvious. At the same time, it appears to suggest that an important reason of the more vigorous enforcement by the Commission might be that it operates under

an administrative system, where its decisions have direct and immediate legal effects. I do believe that this is a strength, to which Europe should definitely not renounce. But it would be wrong to believe that this in itself induces the Commission to be bolder, as if it did not have to undergo judicial review. The Commission is constantly aware that important decisions are most likely to end up in the Court, as in fact they do.

On the other hand, an important reason of strength of antitrust in Europe, not considered by Gutiérrez and Philippon, is that it is conducted within a rational architecture. Especially after the “Modernization” introduced in 2004, there is an adequate degree of decentralization of cases to the national competition authorities, yet under an orderly system, overseen by the Commission. In America, despite repeated attempts to reconsider the architecture inherited from a remote past, there are two federal antitrust authorities, the DoJ Antitrust Division and the FTC, where the division of competences is not crystal-clear, plus fifty State Attorneys-General.

The system is less coherent than in Europe, both over space (due to the abovementioned structure) and over time (due to the greater proximity of American antitrust authorities to electoral cycles, relative to the more shielded position of the EU Commission). We had a vivid illustration of this in the Microsoft case. The DoJ under President Clinton had decided that a break-up of the company was necessary. Several States sided with it, while several others were against. The Court finally annulled the break-up. Only a few years later, the DoJ under President George W. Bush was satisfied with a very weak settlement, endorsed by the Court.

In the EU, the Microsoft decision was an exclusive competence of the Commission, with the national competition authorities playing only an advisory role. The fine that we imposed, and especially the changes we enjoined to those aspects of Microsoft’s business model that configured the abuse of dominant position, were certainly much less heavy than would have been the break-up that did not go through in the US (incidentally, the EU’s Modernization Regulation has introduced explicitly the power for the Commission to impose a break-up if no other remedy appears possible or effective), but remarkably more demanding than the actual settlement in the US. Yet, we had been offered by the company a settlement which would have been vastly more satisfactory than the American one. But, as I vividly remember from those days of March 2004, although we would have preferred to avoid the risk of a negative judgement in the European Court, we felt that it was important for the industry, as well as for the Commission itself for future cases in that industry, to have a ruling providing legal certainty. As is well known, the Court upheld the Commission’s decision.

The EU’s increased scrutiny of tech giants in recent years under the leadership of Commissioner Vestager has led to the now-common perception among economists and scholars that European enforcers are far ahead of their much more permissive American counterparts when it comes to challenging the threats posed by digital platforms. Former FTC chair William Kovacic said recently that Brussels is now “the capital of the world” when it comes to antitrust enforcement against dominant firms, leaving the Department of Justice and the FTC “in the shade.”

Having listened to Assistant Attorney General for Antitrust Makan Delrahim at a recent conference in Chicago, I expressed the opinion (<https://promarket.org/former-italian-pm-european-competition-commissioner-mario-monti-antitrust-enforcement-vigorous-europe-us/>) that he may be the most potentially vigorous assistant attorney general for Antitrust under a Republican administration that I have seen so far. If this is the case, then the EU and the US may proceed to a reasonably vigorous antitrust enforcement on both side of the Atlantic. That would have two welcome by-products as well. The American administration would feel it necessary to articulate in less dogmatic and more concrete terms the “America first” ambition, in identifying the proper role for antitrust. And, last but not least, containing divergences between US and EU antitrust decisions, especially when they concern US-based companies, would reduce the risk of trade wars triggered by antitrust tensions.

* President of Bocconi University, Milan ; Prime Minister of Italy (2011-2013) ; European Commissioner for Competition (1999-2004) and Single Market (1995-1999). An abridged version of this paper was published in the Washington Post, 17 August 2018 (“Europe promotes competition more than America”)

Europe is now more competitive than America

by Mario Monti

17/08/18

Mario Monti was the prime minister of Italy from 2011 to 2013, the European commissioner for the single market from 1995 to 1999 and the European commissioner for competition from 1999 to 2004.

MILAN — President Trump’s “America First” motto may seem straightforward, but in reality, it’s full of contradictions. America is a nation of competing interests. So which part of it — industry, consumer or worker — does Trump aim to put first?

In the short and medium term, certain policies to put American industry first may clash with policies to put American consumers or workers first. For example, Trump’s “America First” policy does not have a clear answer when it comes to antitrust, an area where consumers’ interests are usually pursued more directly than producers’ interests, whether they are businesses or workers. Trump has not articulated how he will resolve this contradiction. In contrast, Europe has mostly found the right balance between these diverging interests.

When it comes to antitrust legislation, America once set the standard. Competition policy was first introduced in the United States in the late 19th century, while in Europe, it was only developed in the context of European integration starting in the 1950s. But today, the European system is stronger in many ways than the American scheme, which has been somewhat slower to adapt to new challenges. In competition policy, for example, the E.U. embraces not just antitrust but also controls how much aid a state can provide a business and provides other forms of oversight for how national governments intervene in economic and financial markets.

When I was European commissioner, I worked to make a single European market out of the various domestic markets and to promote competition in the resulting EU-wide market. The single market and liberalization and competition policies have reinforced each other within the E.U.’s coherent vision for breaking up monopolies. Against this backdrop, particularly in light of the efforts of Europe’s current commissioner for competition, Margrethe Vestager, to pursue Silicon Valley if necessary, the E.U. appears well ahead of the United States in implementing a vigorous competition policy.

One reason for this is the greater proximity of American antitrust authorities to electoral cycles, relative to the more shielded position of the E.U. The European Commission’s vigorous enforcement operates under an administrative system, where its decisions have direct and immediate legal effects. This is a strength that Europe should certainly maintain. But it would be wrong to believe that this in itself prompts the E.U. to be bolder, as if it did not have to undergo judicial review. Important decisions usually do end up being reviewed in the court.

Another important reason for the strength of antitrust in Europe is that it is conducted within a rational architecture. Especially following the E.U.’s “modernization” of competition laws starting in 2004, cases have been decentralized to national competition authorities. This has happened under an orderly system, overseen by the European Commission. In America, despite repeated attempts to reconsider the framework inherited from a distant past, there are only two federal antitrust authorities, the Department of Justice Antitrust Division and the

Federal Trade Commission (FTC), where the division of competences is not crystal clear, plus 50 state attorneys general.

In other words, the U.S. system is less coherent than the European one. We had a vivid illustration of this in the 2004 Microsoft case. The Justice Department, under former president Bill Clinton, had decided that a breakup of the company was necessary. Several states sided with the department, while several others opposed it. The court eventually annulled the breakup. Only a few years later, the Justice Department, under former president George W. Bush, was satisfied with a very weak settlement endorsed by the court.

In the E.U., the Microsoft decision was the responsibility of the European Commission, with national competition authorities playing only an advisory role. That said, the fine and reforms we imposed on Microsoft were certainly much tamer than what might have been if the breakup had gone through in the United States.

Especially under Vestager's leadership in recent years, Europe has become stricter than American enforcers when it comes to guarding against threats posed by digital platforms. Former FTC chair William Kovacic [said recently](#) that Brussels is now "the capital of the world" when it comes to antitrust enforcement against dominant firms, leaving the Justice Department and the FTC "in the shade."

But Makan Delrahim, the current U.S. assistant attorney general for antitrust, is potentially the most vigorous person to hold that position under a Republican administration that I have seen so far. The E.U. and the United States therefore have an opportunity to proceed to strong antitrust enforcement on both sides of the Atlantic.

That would have two welcome byproducts. The Trump administration would feel called to articulate in less dogmatic and more concrete terms its "America First" ambition and to identify the proper role for antitrust. And containing divergences between U.S. and E.U. antitrust decisions, especially when they concern U.S.-based companies, would reduce the risk of trade wars triggered by antitrust tensions.

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Former Italian PM and European Competition Commissioner Mario Monti: Why Antitrust Enforcement Is “More Vigorous” in Europe Than in the US

Posted on April 23, 2018 by Asher Schechter

Why is Europe so much more vigorous than the US when it comes to antitrust enforcement? In an interview with ProMarket, Monti, who served as the EU’s Competition Commissioner between 1999 and 2004, offers a possible explanation: American antitrust’s sensitivity to election outcomes and industry lobbying.

Europe’s Competition Commissioner Margrethe Vestager announced today that the European Commission has launched an “in-depth investigation” into Apple’s acquisition of the song-recognition app Shazam, based on concerns that the deal would give Apple access to user data that may enable the company to drive customers away from competitors and onto Apple Music.

The Apple/Shazam probe is the latest in a series of aggressive measures undertaken by the EC as it seeks to



Mario Monti. Photo by Zinneke [CC BY-SA 3.0], from Wikimedia Commons

root out
 anticompetitive
 behavior among
 tech giants.
 Nearly two
 years after it
 leveled a 2.4-
billion-euro fine
 on Google for
 abusing its
 market
 dominance to
 favor its
 comparison
 shopping

service in search results, the EC still has two pending antitrust cases against the company and is refusing to rule out the possibility of breaking Google up. In 2016, it ordered Apple to pay 13 billion euros in back taxes to Ireland, and is now suing Ireland for its failure to collect these funds.

The EC's increased scrutiny of tech giants has led to the now-common perception among economists and scholars that European enforcers are far ahead of their much more permissive American counterparts when it comes to challenging the threats posed by digital platforms. In a recent ProMarket piece, former FTC chair William Kovacic wrote that Brussels is now "the capital of the world" when it comes to antitrust enforcement against dominant firms, leaving the Department of Justice and the FTC "in the shade."

Why are European regulators so much more aggressive in their attempt to tame tech giants? One oft-repeated charge is that the European crackdown is driven by protectionism and "anti-American bias." In 2015, then-president Barack Obama weighed in on the issue and accused European competition authorities of being driven by the "commercial interests" of local service providers who "can't compete with ours."

This is not a new dynamic. Similar charges have been made when the European Commission, then led by Mario Monti, decided to block GE's \$42 billion bid to acquire Honeywell and the WorldCom-Sprint merger in the early aughts, and

again when it leveled a then-record fine of 497 million euros against Microsoft for abusing the dominant market position of Windows in 2004.

While persistent, the protectionism charge doesn't necessarily hold up to scrutiny. A recent study by Anu Bradford, Robert Jackson, Jr. and Jonathan Zytnick looked into these accusations, and found no evidence that the EC is protectionist or biased against non-EU or America-based firms.

In a keynote speech during the Stigler Center's annual antitrust conference last week, Monti also categorically denied charges that the EU is acting out of protectionism. "The European Commission, as a competition enforcer, does tend to be more vigorous on average than US antitrust agencies, [but] it is not protectionist," said Monti, the former prime minister of Italy and a lifetime Italian Senator.

ANTITRUST AND COMPETITION CONFERENCE P...



Monti, who served as the EU's Competition Commissioner between 1999 and 2004, is most famous today for his tenure as head of Italy's technocratic government between November 2011 to April 2013. Before then, however, he was known primarily as an antitrust enforcer "most famous for shooting mergers down in flames." His decision to block the GE-Honeywell merger, in the face of intense lobbying and threats of a trade war, led American businessmen to describe him in the pages of The Economist as "the corporate equivalent of Saddam Hussein."

In an interview with ProMarket, Monti explained why, in his view, the protectionism charge remains salient despite evidence to the contrary. "American companies and the American public opinion are obviously impressed by what the EU from time to time does to American companies. Understandably, they follow much less all the other decisions that the Commission takes to enforce competition within the EU," he said. "For Competition Commissioners, the biggest fights are not with American CEOs, but with European governments. For Commissioners, most [of the] arm-twisting activity has to do with the control over state-aid—which is something that does not exist in other parts of the world, but does exist in a supranational structure like the EU—[whereby] the Commissioner has to impose the law not on an American or European company, but on one of its own shareholders.

"For me personally, for example, the toughest fights have not been with [Jack] Welch or [Bill] Gates, but with [then German Chancellor Gerhard] Schröder, because we ordered the elimination of all state guarantees to the public banks in Germany, which was something that would considerably undermine the nexus between politics and finance in Germany."

From early on as the EU's top antitrust enforcer, Monti had been aware of the threats to competition posed by the then-fledgling digital economy. His decision to aggressively pursue the Microsoft case, long after the company reached a settlement with the DOJ, led to what was at the time a record fine against a US tech firm.

While reluctant to comment about pending EC cases, in his interview with ProMarket Monti noted that he does see some resemblances between the European charges against Google and the Microsoft case. "I think the most important underlying commonality is the attempt to leverage the market power acquired in a given market onto proximate markets. That was true for Microsoft tying the Windows operating system and the media player and in different respects, the Google cases also fall within that line, I believe."

When asked how he explains the divergence between antitrust in the EU and the US on digital platforms, Monti offered two explanations: one was that US antitrust is much more sensitive to election outcomes, which makes US antitrust policy less consistent than in Europe. The EU's competition authority is less affected by national election cycles, and even elections to the European Parliament, which take place every five years, have an "absolutely minimal" influence, he explained.

Being shielded from political shifts, he added, allows for a more consistent competition policy. The Microsoft case, he said, provides a useful example. Joel Klein, head of the DOJ's antitrust division under Bill Clinton, wanted to break up Microsoft, but the decision was overturned by the courts. By that point, Klein had already left the DOJ, George W. Bush won the presidency, and the new administration reached a new settlement with Microsoft that, per Monti, was "extremely soft."

The other explanation is that antitrust officials in the US are more vulnerable to lobbying by firms. "Certainly when it comes to lobbying exercised by an American company, I believe that the ability and the effectiveness with which American companies lobby Congress or the administration in the US is greater, in particular in Congress or the White House," he said.

The unique structure of the European Commission, he said, keeps European authorities "a bit more at arms' length" from industry pressures—particularly those of the tech industry. "It's not that the European industry does not lobby Brussels," he said. "But the European industry has known for much longer than the American industry that it's one thing to lobby the legislators in Europe—the European Parliament, which has to approve a proposal for a directive presented by the Commission—and the Commission [is another]. They are much more respectful when it comes to the competition enforcement side, whereas American companies were less familiar with this and maybe in good faith believed that they had to overcome some protectionist bias."

Effectively, he said, European competition officials are able to take decisions “independent from the lobbying exercises—the more far away you are, the less you feel under pressure.” In the US, he said, “permissive changes” in campaign financing laws also lead to more risk of regulatory capture.

In his speech at the antitrust conference, Monti shared an anecdote that epitomized this difference. When the EC was reviewing the GE-Honeywell merger, Jack Welch, GE’s CEO at the time, came to Brussels “with the impression that it was a nice formality that would be greatly appreciated that he pay personal visits to the Commissioner.” This, said Monti, “was very much appreciated... However, after some meetings I had to say to Welch in my office ‘Look, you are putting desperate lobbying pressure on all my colleagues in the Commission and on all the national competition authorities. You must be aware that if you continue like this, you can only worsen your situation.’ And from my office he immediately called Andrew Card, who was the chief of staff for President Bush.”

While critical of the Bush administration’s lax approach to antitrust enforcement, Monti said he was encouraged by Makan Delrahim’s [speech](#) at the Stigler Center conference, in which the Trump administration’s antitrust chief said antitrust enforcers “should be open and receptive to empirical evidence that companies in digital markets may be engaging in predatory pricing or other exclusionary conduct to drive out competition and cause long-run harm to consumers.” Delrahim, said Monti, represents “the most potentially vigorous assistant attorney general for antitrust under a Republican administration that I have seen so far.”

As for the potential for increased convergence on antitrust between the EU and the US, Monti sounded optimistic. “I was very impressed by the depth of [Delrahim’s] speech,” he said. “I saw various signs of opening up prudently more vigorous avenues than we observed during the previous Republican [administration].”

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Antitrust in a time of populism[☆]

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ABSTRACT

This article discusses how to move antitrust enforcement forward in a constructive manner during a time of widespread and growing concern over the political and economic power of large corporations in the United States. Three themes are emphasized. First, a body of economic evidence supports more vigorous merger enforcement in the United States. Tighter merger control can be achieved by utilizing the existing legal presumption against highly concentrating mergers. Second, close antitrust scrutiny is appropriate for today's largest and most powerful firms, including those in the tech sector. Proper antitrust enforcement regarding unilateral conduct by dominant firms should continue to focus on identifying specific conduct that harms customers or disrupts the competitive process. Third, while antitrust enforcement has a vital role to play in keeping markets competitive, antitrust law and antitrust institutions are ill suited to directly address concerns associated with the political power of large corporations or other public policy goals such as income inequality or job creation.

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1. Introduction

Antitrust is sexy again. Where does this take us?

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American politicians are calling on antitrust to solve an array of problems associated with the excessive power of large corporations in the United States. As a recent leading example, in July 2017 Congressional Democrats unveiled “A Better Deal: Cracking Down on Corporate Monopolies and the Abuse of Economic and Political Power.”¹ Their plan calls for much tougher merger enforcement and greater government oversight “to stop abusive conduct and the exploitation of market power where it already exists.”

Not since 1912, when Teddy Roosevelt ran for President emphasizing the need to control corporate power, have antitrust issues had such political salience.² While Roosevelt did not win, Congress passed the Federal Trade Commission Act and the Clayton Act in 1914, significantly strengthening the Sherman Act. Indeed, the Sherman Act itself was passed in 1890 in response to broad concerns about the political and economic power of large corporations in America, as illustrated in this 1889 political cartoon, “The Bosses of the Senate.”



“The Bosses of the Senate,” Puck, 23 January 1889

¹ See <https://democrats.senate.gov/wp-content/uploads/2017/07/A-Better-Deal-on-Competition-and-Costs-1.pdf>.

² Roosevelt’s views are expressed in his famous 1910 “New Nationalism” speech, delivered in Osawatomie, Kansas; see <http://teachingamericanhistory.org/library/document/new-nationalism-speech/>. This passage is especially relevant today: “Combinations in industry are the result of an imperative economic law which cannot be repealed by political legislation. The effort at prohibiting all combination has substantially failed. The way out lies, not in attempting to prevent such combinations, but in completely controlling them in the interest of the public welfare”.

Today's concerns about corporate power, and today's renewed interest in antitrust, represent an opportunity to strengthen competition policy in the United States. This opportunity extends to all three branches of government: the Department of Justice and the Federal Trade Commission can take a tougher line enforcing the antitrust laws, the courts can interpret the very broad antitrust statutes in ways that support more vigorous antitrust enforcement, and Congress could strengthen the antitrust laws. The central purpose of this article is to assess the relevant economic evidence regarding competition in the U.S. economy and then, based on that evidence and on antitrust learning and experience, identify ways to improve and strengthen antitrust.

In [Section 2](#), I document that we truly are at a moment when there is widespread and growing concern among politicians and journalists that the American economy has become significantly less competitive over the past several decades. In [Section 3](#), I then look more deeply at the economic evidence relating to trends in competition in the U.S. economy. I focus on evidence about economic concentration and corporate profits and what it implies about competition. In [Section 4](#), I then discuss competition policy responses to the rising economic concentration and unprecedented corporate profits that we are observing. [Section 5](#) concludes.

Before turning to those topics, I would like to emphasize that the role of antitrust in promoting competition could well be *undermined* if antitrust is called upon or expected to address problems not directly relating to competition. Most notably, antitrust institutions are poorly suited to address problems associated with the excessive political power of large corporations. The courts and the antitrust enforcement agencies know how to assess economic power and the economic effects of mergers or challenged business practices, but there are no reliable methods by which they could assess the *political* power of large firms. Asking the DOJ, the FTC to evaluate mergers and business conduct based on the political power of the firms involved would invite corruption by allowing the executive branch to punish its enemies and reward its allies through the antitrust cases brought, or not brought, by antitrust enforcers. On top of that, asking the courts to approve or block mergers based on the political power of the merging firms would undermine the rule of law while inevitably drawing the judicial branch into deeply political considerations. Let me be clear: the corrupting power of money in politics in the United States is perhaps the gravest threat facing democracy in America.³ But this profound threat to democracy and to equality of opportunity is far better addressed through campaign finance reform, increased transparency, and anti-corruption rules than by antitrust.

³ Much of the problem seems to arise from an overly narrow definition of “corruption” adopted in recent years by the Supreme Court. See Zephyr [Teachout](#) (2014). The inability of Congress to police itself is also a major reason why large companies have so much political power. Of course, economists and political scientists have long recognized the dangers associated with regulatory capture, and legislators are hardly immune to this disease.

Antitrust also is poorly suited to address issues of income inequality. Many other public policies are far superior for this purpose. Tax policy, government programs such as Medicaid, disability insurance, and Social Security, and a whole range of policies relating to education and training spring immediately to mind. So, while stronger antitrust enforcement will modestly help address income inequality, explicitly bringing income distribution into antitrust analysis would be unwise. Baker and Salop (2015) identify a number of ways in which antitrust could help address inequality while staying true to its mission of promoting competition.

2. The new conventional wisdom: competition in America has declined

Until quite recently, few were claiming that there has been a substantial and widespread decline in competition in the United States since 1980. And even fewer were suggesting that such a decline in competition was a major cause of the increased inequality in the United States in recent decades, or the decline in productivity growth observed over the past 20 years.

Yet, somehow, over the past two years, the notion that there has been a substantial and widespread decline in competition throughout the American economy has taken root in the popular press. In some circles, this is now the conventional wisdom, the starting point for policy analysis rather than a bold hypothesis that needs to be tested.

Since 2015, there has been a regular drumbeat in the press reporting on a supposed decline of competition in the United States. In October 2015, the *Wall Street Journal*, hardly an anti-business publication, wrote: “A growing number of industries in the U.S. are dominated by a shrinking number of companies”.⁴ Later that month, the *New York Times* stated: “Markets work best when there is healthy competition among businesses. In too many industries, that competition just doesn’t exist anymore.”⁵ Eduardo Porter of the *New York Times* later connected increasing inequality with a decline of competition, under the title: “With Competition in Tatters, the Rip of Inequality Widens”.⁶

The *Economist*, a highly respected publication regarding economic policy, has been especially sharp and persistent in asserting that there has been a substantial decline in competition in recent years. In March 2016, the *Economist* published a lengthy report stating: “Profits are too high. America needs a giant dose of competition”.⁷ In September

⁴ Theo Francis and Ryan Knutson, “Wave of Megadeal Tests Antitrust Limits in U.S.”, *Wall Street Journal*, 18 October 2015, available at <https://www.wsj.com/articles/wave-of-megadeals-tests-antitrust-limits-in-u-s-1445213306>.

⁵ “How Mergers Damage the Economy”, The Editorial Board, *New York Times*, 1 November 2015, available at https://www.nytimes.com/2015/11/01/opinion/sunday/how-mergers-damage-the-economy.html?_r=0.

⁶ *New York Times*, 12 July 2016, available at <https://www.nytimes.com/2016/07/13/business/economy/antitrust-competition-inequality.html>.

⁷ *Economist*, 26 March 2016, “Too Much of a Good Thing”, available at <https://www.economist.com/news/briefing/21695385-profits-are-too-high-america-needs-giant-dose-competition-too-much-good-thing>.

2016, the *Economist* special report, “The Rise of the Superstars”, highlighted the dangers to competition posed by today’s largest and most successful tech companies.⁸ The magazine’s summary of this report was entitled: “The Superstar Company: A Giant Problem”, along with the subtitle: “The rise of the corporate colossus threatens both competition and the legitimacy of business”.⁹ That summary concluded: “The world needs a healthy dose of competition to keep today’s giants on their toes and to give those in their shadow a chance to grow”. The *Economist* has also expressed grave concerns over passive investment funds, such as index funds, that take large ownership stakes in multiple firms in the same industry. The *Economist* fears that these investments dull competition, calling them a form of “stealth socialism”, asserting that “passive investment funds create headaches for antitrust authorities, and even describing such investments as “a contradiction at the heart of financial capitalism”.¹⁰

The drumbeat continues. *Business Week* recently reported: “Market concentration in the U.S. has reached a three-decade high, while the government has opened fewer antitrust cases”.¹¹

The view that competition has declined in the American economy during recent decades is not confined to the popular press. President Obama’s Council of Economic Advisers added some high-octane fuel to the fire in May 2016 with its release of an issues brief entitled “Benefits of Competition and Indicators of Market Power”. In typical Obama-CEA style, this report was carefully worded with numerous caveats, and it properly cited empirical evidence and the academic economics literature. But overall the CEA report was generally interpreted as embracing the view that the American economy has experienced a decline in competition over the past several decades. After all, the lead paragraph states: “Several indicators suggest that competition may be decreasing in many economic sectors, including the decades-long decline in new business formation and increases in industry-specific measures of concentration”. I discuss the findings of this report below.

A number of progressive think tanks and advocates have issued reports over the past two years documenting the decline in competition in the American economy, linking that decline to increasing inequality, and offering policy proposals to reinvigorate competition policy. The [American Antitrust Institute \(2016\)](#), a respected organization long committed to more effective antitrust enforcement, published a report in June 2016 entitled “A National Competition Policy: Unpacking the Problem of Declining Competition and

⁸ *Economist*, 17 September 2016, available at <https://www.economist.com/news/special-report/21707048-small-group-giant-companiessome-old-some-ware-once-again-dominating-global>.

⁹ *Economist*, 17 September 2016, available at <https://www.economist.com/news/leaders/21707210-rise-corporate-colossus-threatens-both-competition-and-legitimacy-business>.

¹⁰ “Stealth Socialism”, *Economist*, 17 September 2016, available at <https://www.economist.com/news/finance-and-economics/21707191-passive-investment-funds-create-headaches-antitrust-authorities-stealth>.

¹¹ “Here’s How They Play Monopoly in America, and Who Wins”, *Business Week*, 5 April 2017, available at <https://www.bloomberg.com/news/articles/2017-04-05/here-s-how-they-play-monopoly-in-america-and-who-wins>.

Setting Priorities Moving Forward”. This report lists three main symptoms of declining competition: rising concentration, higher profits to a few big firms combined with slowing rates of start-up activity, and widening inequality gaps. The report rather boldly claims (p.7): “There is a growing consensus that inadequate antitrust policy has contributed to the concentration problem and associated inequality effects”.

That same month, the [Center for American Progress \(2016\)](#) issued a report entitled “Reviving Antitrust: Why Our Economy Needs a Progressive Competition Policy”. The introduction and summary to this report states: “there is systematic evidence – ranging from the disconnect of corporate profits and corporate investment to evidence of persistent supra-normal profitability – that points to an increase in rent extraction in the U.S. economy”. These ills are then linked to inadequate antitrust enforcement over the past few decades.

Also in June 2016, the [Roosevelt Institute \(2016\)](#) issued a report, “Untamed: How to Check Corporate, Financial and Monopoly Power”. The first chapter in this report, “Restoring Competition in the U.S. Economy”, opens this way: “Increasing market concentration across the American economy has been a driver of declining economic opportunity and widening inequality in recent decades. In industries ranging from hospitals and airlines to agriculture and cable, markets are now more concentrated and less competitive than at any point since the Gilded Age”.¹² In March 2017, the [Roosevelt Institute \(2016\)](#) released a paper, “Toward a Broader View of Competition Policy”, by none other than Nobel Laureate Joseph Stiglitz. In the abstract, [Stiglitz \(2017\)](#) highlights “the increase in market power across many important sectors of the U.S. economy and persistent higher rates of return to capital than seem consistent with competition”. He adds: “These monopoly rents, may, in turn, play an important role in the country’s growing inequality”.

The Washington Center for Equitable Growth joined the chorus, releasing a paper in March 2017 by antitrust expert Jonathan Baker, “Market Power in the U.S. Economy Today”. [Baker \(2017\)](#) opens his paper with this paragraph: “The U.S. economy has a ‘market power’ problem, notwithstanding our strong and extensive antitrust institutions. The surprising conjunction of the exercise of market power with well-established antitrust norms, precedents, and enforcement institutions is the central paradox of U.S. competition policy today”. In February 2017, Barry Lynn, then the director of the Open Markets program at New America, went so far as to state: “The idea that America has a monopoly problem is now beyond dispute”.¹³

Progressive politicians have also been expressing concerns about declining competition and growing corporate power. Early in the presidential campaign, in October 2015,

¹² See p. 18, with a footnote citing the 26 March 2016 *Economist* article, “Too Much of a Good Thing”, noted above. The authors of this chapter are K. Sabeel Rahman and Lina Khan.

¹³ Barry Lynn, “America’s Monopolies are Holding Back the Economy”, *The Atlantic*, 22 February 2017, available at <https://www.theatlantic.com/business/archive/2017/02/antimonopoly-big-business/514358/>.

Hillary Clinton stated: “Economists, including President Obama’s Council of Economic Advisers, have put their finger on what’s going on: large firms are concentrating their control over markets”.¹⁴ Later in the campaign, her campaign web site promised: “A new commitment to promote competition, address excessive concentration and the abuse of economic power, and strengthen antitrust laws and enforcement”.¹⁵ The 2016 Democratic Party Platform contained a section entitled “Promoting Competition by Stopping Corporate Concentration”, which stated: “Large corporations have concentrated their control over markets to a greater degree than Americans have seen in decades – further evidence that the deck is stacked for those at the top”.¹⁶

Senator Elizabeth Warren has been especially vocal about the decline of competition in America and the need for stronger policies to reign in corporate power. She gave a detailed speech on this topic in June 2016 at New America’s Open Markets Program, in which she stated: “Today in America competition is dying. Consolidation and concentration are on the rise in sector after sector. Concentration threatens our markets, threatens our economy, and threatens our democracy”.¹⁷ The need to control corporate power is an ongoing theme for Senator Warren. In May 2017 she stated: “It’s time for us to do what Teddy Roosevelt did – and pick up the antitrust stick again. Sure, that stick has collected some dust, but the laws are still on the books”.

In July 2017, the Democratic party gave considerable prominence to antitrust issues in the “Better Deal” it put forward to attract voters.¹⁸ Their “Better Deal” plan has three prongs: (1) “new standards to limit large mergers that unfairly consolidate corporate power”, (2) “tough post-merger review”, and (3) “a new consumer competitive advocate”.¹⁹ In September 2017, Senator Klobuchar introduced the “Consolidation Prevention and Competition Promotion Act of 2017”, which would greatly strengthen the ability of the antitrust agencies to block horizontal mergers and to evaluate the effects of mergers that are consummated.²⁰

Perhaps these sentiments are unsurprising, coming from progressive think tanks and politicians during a time of populism. But they are not just coming from that quarter. Concerns about corporate concentration and corporate power are bipartisan, in rhetoric if not in action. During the presidential campaign, candidate Donald Trump stated:

¹⁴ Hillary Clinton, “Being Pro-Business Doesn’t Mean Hanging Consumers Out to Dry”, Quartz, 20 October 2015, available at <https://qz.com/529303/hillary-clinton-being-pro-business-doesnt-mean-hanging-consumers-out-to-dry/>.

¹⁵ <https://www.hillaryclinton.com/briefing/factsheets/2016/10/03/hillary-clintons-vision-for-an-economy-where-our-businesses-our-workers-and-our-consumers-grow-and-prosper-together/>

¹⁶ See <https://www.democrats.org/party-platform>, p. 12.

¹⁷ Senator Elizabeth Warren, “Reigniting Competition in the American Economy”, 29 June 2016, available at https://www.warren.senate.gov/files/documents/2016-6-29_Warren_Antitrust_Speech.pdf.

¹⁸ “Congressional Democrats Promise a ‘Better Deal’ for American Workers, *New York Times*, 24 July 2017, available at <https://www.nytimes.com/2017/07/24/us/politics/congressional-democrats-promise-a-better-deal-for-american-workers.html>.

¹⁹ See https://graphics.axios.com/pdf/better-deal-competition-and-cost.pdf?utm_source=newsletter&utm_medium=email&utm_campaign=newsletter_axiosam&stream=top-stories.

²⁰ See <https://www.klobuchar.senate.gov/public/index.cfm/news-releases?ID=FB9C644A-2F7B-4FB1-9003-0E0C667E1027>.

“It’s not just the political system that’s rigged, it’s the whole economy”.²¹ He vowed to stop AT&T from acquiring Time Warner, calling their merger “an example of the power structure I’m fighting”.²² After the election, Vice-President Elect Pence stated: “The free market has been sorting it out and America’s been losing”, at which point President-Elect Trump chimed in: “Every time, every time”.²³

All of this chatter has even reached the ivory tower. The shifting terms of the debate were impossible to miss at the University of Chicago conference in March 2017, “Is There a Concentration Problem in America”.²⁴ Notably, this conference took place at the home of the Chicago School, which is associated with Milton Friedman and George Stigler. The Chicago School ushered in a far more circumscribed approach to antitrust enforcement around 1980.²⁵ Yet one speaker after another at this conference argued that antitrust enforcement needs to be strengthened. The title of the article in the *Economist* reporting on this conference says it all: “The University of Chicago worries about a lack of competition. Its economists used to champion big firms, but the mood has shifted”.²⁶

3. Taking a closer look at the evidence

In this section, I step back and ask what the empirical evidence actually shows about trends in competition in the United States over the past 30 to 40 years. I consider this an essential predicate to discussion of the various proposals to strengthen U.S. competition policy.

3.1. Trends in market concentration

The starting point for most assertions that there has been a significant and widespread decline in competition in the United States in recent decades is the claim that U.S. markets have systematically become far more *concentrated*. Purely as a factual matter, is this actually true?

²¹ <http://www.politico.com/story/2016/06/transcript-trump-speech-on-the-stakes-of-the-election-224654>.

²² See https://www.washingtonpost.com/news/the-switch/wp/2016/11/11/trump-may-have-a-harder-time-blocking-the-massive-att-time-warner-merger-than-he-thought/?utm_term=.44921a16844e.

²³ <https://www.nytimes.com/2016/12/01/business/economy/trump-carrier-pence-jobs.html>.

²⁴ <https://research.chicagobooth.edu/stigler/events/single-events/march-27-2017>. This conference was sponsored by the Stigler Center for the Study of the Economy and the State and was organized by Luigi Zingales and Guy Rolnik.

²⁵ Many date the shift to the publication of Robert Bork’s book, *The Antitrust Paradox* in 1978. The election of President Reagan and the new antitrust enforcement policies put in place by Assistant Attorney General William Baxter were critical for implementing the ideas in Bork’s book.

²⁶ 12 April 2017, available at <https://www.economist.com/news/business/21720657-its-economists-used-champion-big-firms-mood-has-shifted-university-chicago>.

Before I turn to the data, I would like to state clearly and categorically that I am looking here for *systematic and widespread* evidence of significant increases in concentration in well-defined markets in the United States. Nothing in this section should be taken as questioning or contradicting separate claims regarding changes in concentration in specific markets or sectors, including some markets for airline service, financial services, health care, telecommunications, and information technology. In a number of these sectors, we have far more detailed evidence of increases in concentration and/or declines in competition. In my view, no high-level look at the American economy can substitute for detailed studies of specific markets when it comes to assessing market power. Nonetheless, understanding broad trends is certainly valuable, and, as illustrated above, many are claiming that there has been a systematic and widespread decline in competition in America. Here, I am evaluating those claims, not assessing concentration or competition in specific markets or sectors.

Industrial organization economists have understood for at least 50 years that it is extremely difficult to measure market concentration across the entire economy in a systematic manner that is both consistent and meaningful. Going back to the 1950s, economists seeking to understand the relationship between concentration and profits struggled long and hard with these difficulties, in the end with only limited success. [Schmalensee \(1989\)](#) and [Salinger \(1990\)](#) review this literature. One unavoidable and persistent problem is conceptual: defining relevant markets in which to measure market shares is known to be difficult in individual antitrust cases, and is well-nigh impossible to do consistently on an economy-wide basis. The second problem is very practical and can change over time: what data on sales, prices and costs are actually available on a systematic basis, and how good are those data?

So far as I can tell, recent assertions regarding economy-wide trends market concentration in the American economy have largely ducked both of these problems. This does not mean that the reported results are meaningless, but certainly one should understand the underlying data and their limitations when interpreting those results. That is my limited goal here.

3.1.1. *Measuring changes in concentration over time*

Let me start with the April 2016 report by the Council of Economic Advisers cited above. Below, I reproduce [Table 1](#) from that report. The CEA states flatly: “[Table 1](#) shows that the majority of industries have seen increases in the revenue share enjoyed by the 50 largest firms between 1997 and 2012”. Fair enough – but what are we to make of this fact?

I do not consider the CEA [Table 1](#) to be informative regarding overall trends in concentration in well-defined relevant markets that are used by antitrust economists to assess market power, much less trends in competition in the U.S. economy. My objections to the CEA [Table 1](#) are fundamental: (a) the fifty-firm concentration ratio (CR_{50}) reported

Table 1

Change in market concentration by sector, 1997–2012.

Industry	Revenue earned by 50 largest firms, 2012 (Billion \$)	Revenue share earned by 50 largest firms, 2012	Percentage point change in revenue share earned by 50 largest firms, 1997–2012
Transportation and warehousing	307.9	42.1	11.4
Retail trade	1555.8	36.9	11.2
Finance and insurance	1762.7	48.5	9.9
Wholesale trade	2183.1	27.6	7.3
Real estate rental and leasing	121.6	24.9	5.4
Utilities	367.7	69.1	4.6
Educational services	12.1	22.7	3.1
Professional, scientific and technical services	278.2	18.8	2.6
Administrative/Support	159.2	23.7	1.6
Accommodation and food services	149.8	21.2	0.1
Other services, non-public admin	46.7	10.9	−1.9
Arts, entertainment and recreation	39.5	19.6	−2.2
Health care and assistance	350.2	17.2	−1.6

Source: Economic Census (1997 and 2012), Census Bureau.

Note: Concentration ratio data is displayed for all North American Industry Classification System (NAICS) sectors for which data is available from 1997 to 2012.

in [Table 1](#) is not informative regarding the state of competition. Industrial organization economists generally believe that markets are normally quite competitive with far fewer than fifty firms, so we measure concentration using the Herfindahl Index (HHI) or perhaps the four-firm concentration ratio (CR_4); (b) the two-digit industry groupings in [Table 1](#) are *far too broad* to assess market power, so the trends observed may well reflect nothing more than the expansion of successful, efficient firms into related lines of business, to the benefit of consumers; (c) the revenue shares reported in the CEA [Table 1](#) are calculated on a *national* basis, yet many of the relevant markets are regional or local, so the trends observed may well reflect nothing more than the expansion by successful, efficient firms into new geographic regions, to the benefit of consumers; and (d) shares measured based on overly broad categories are likely to mask some genuinely worrisome increases in concentration in narrower and more meaningful product or geographic markets.

As an illustration of the basic measurement issue, consider what happens to concentration measured at the national level if we begin with a situation in which each of many

local markets has five stores, all locally owned with no cross-ownership across geographies. Then suppose that four national chains arise, and each local market shifts to having a store from each of these four national chains plus one locally-owned store. This shift causes no change at all in concentration at the local level, i.e., in the properly defined relevant markets. Each local HHI is 2000 before and after the rise of the national chains (five stores, each with 20%). Nationally, however, the HHI starts near zero and grows to 1600 (four chains each with 20% nationally). This shift could well go along with lower prices and better service for customers.²⁷

The CEA was no doubt well aware of these problems with its [Table 1](#) when it issued its report. The CEA was careful to qualify its own [Table 1](#), stating: “The statistics presented in [Table 1](#) are national statistics across broad aggregates of industries, and an increase in revenue concentration at the national level is neither a necessary nor sufficient condition to indicate an increase in market power. Instead, antitrust authorities direct their attention to concentration at the relevant market level for each product or service. Those data are not readily available across the economy”.²⁸ Unfortunately, many of those citing the CEA Report as not nearly so careful.

In the end, the CEA [Table 1](#) reflects the growing role of large firms in the American economy, but it tells us little or nothing about trends in concentration in properly-defined relevant markets, and thus it tells us little or nothing about trends in market power. Sheer size and market power are just not the same thing. Sheer size would appear to matter much more for *political* power than for economic power. As noted above, my focus here is on economic power.

Another widely cited source for the proposition that U.S. markets have become systematically more concentrated in recent decades is the *Economist*. In March 2016 the *Economist* published a very useful chart, “A Widespread Effect”, showing the four-firm concentration ratio in some 893 “individual industries”, in the United States in 1997 and 2012.²⁹ I reproduce this chart below.

²⁷ Indeed, small local firms often state that they find it very difficult to compete against large national chains, in large part because the chains have lower costs and thus can charge lower prices. If the competitive process is working properly, and if consumers prefer to shop from locally-owned stores, those preferences would give local stores one competitive advantage over national chains that would to some degree offset their lower costs. Related, antitrust should generally not stand in the way of groups of local stores from different areas working together to obtain the benefits of volume purchasing as a means to compete more effectively with the national chains.

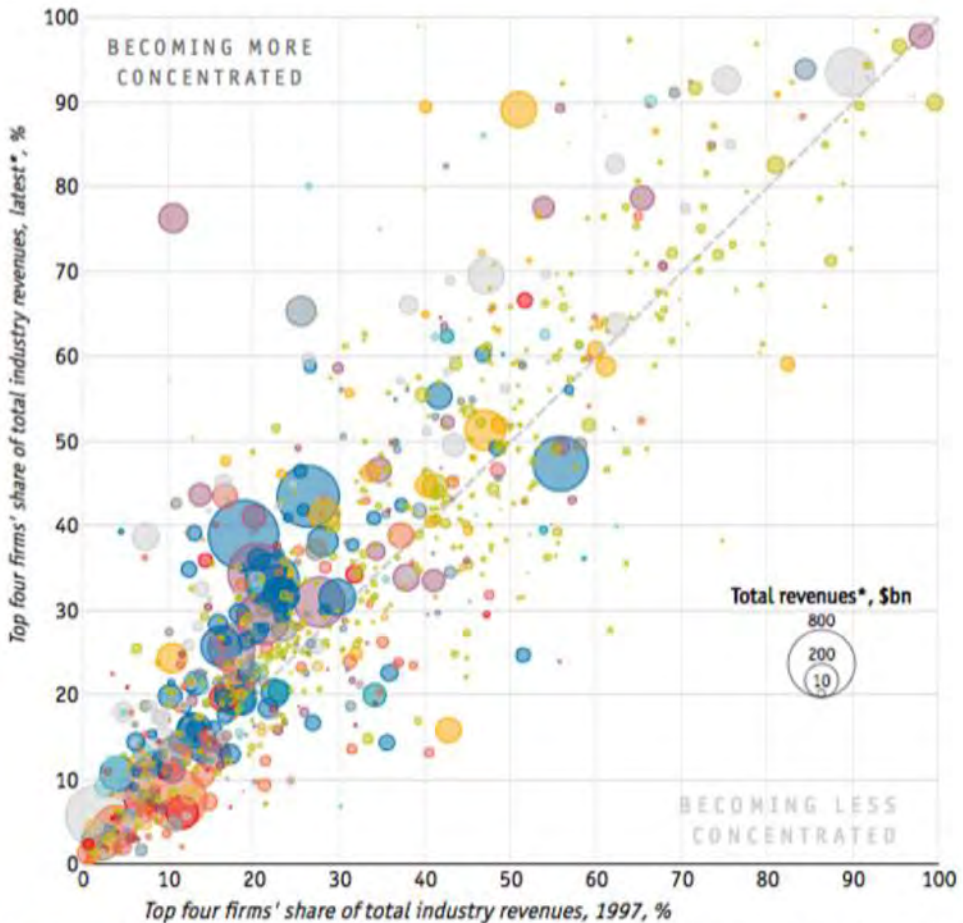
²⁸ Recognizing the limitations of its own [Table 1](#), the CEA cites a number of studies showing rising concentration in specific industries, including bank loans and deposits (1980 to 2010), several agricultural industries (1972 to 2002), hospital markets (early 1990s to 2006), wireless providers (2004 to 2014), and railroad markets. As noted above, I steer clear here of studies of specific industries and focus on systematic evidence across the U.S. economy.

²⁹ See “Corporation Concentration: The Creep of Consolidation Across America’s Corporate Landscape”, available at <https://www.economist.com/blogs/graphicdetail/2016/03/daily-chart-13>, 24 March 2016. This web site is a very handy interactive tool which readers are encouraged to visit and explore.

A widespread effect

Top four firms' share of total industry revenue, %
893 industries, grouped by sector, United States

- Accommodation & food
- Finance
- Other
- Transport & warehousing
- Administration
- Health care
- Professional services
- Utilities
- Arts & entertainment
- IT
- Property
- Wholesale
- Education
- Manufacturing
- Retail



Sources: US Census Bureau; *The Economist*

*Latest available, 2007 or 2012

This chart is based on data from the Economic Census. So far as I can tell, each of the 893 “industries” in the chart corresponds to a four-digit industry under the NAICS classification system used by the Census Bureau. Industries in which the four-firm concentration ratio increased from 1997 to 2007 (or 2012) appear above the 45-degree line. The size of the circle is proportional to revenues in the industry, and the color (or shade) denotes the sector of the economy in which that industry belongs.

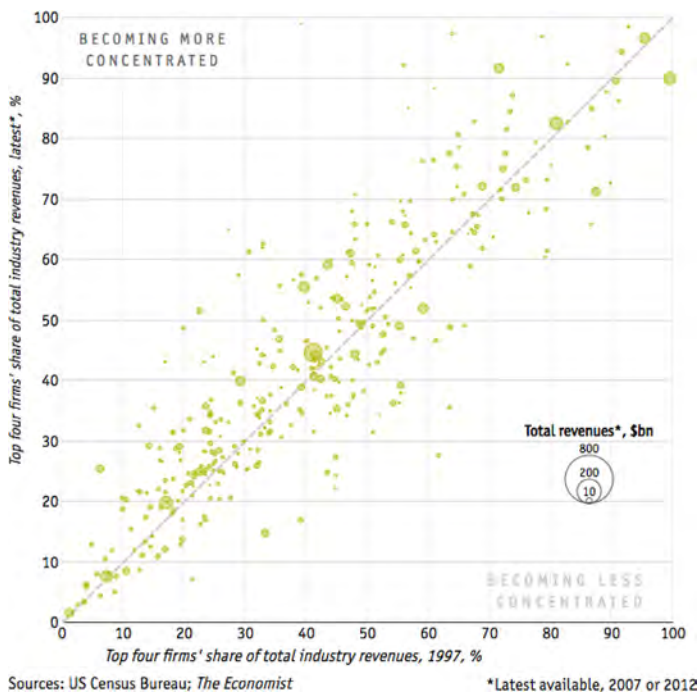
These 893 “industries” are far closer to relevant antitrust product markets than are the two-digit sectors used by the CEA. But still not all that close. Here are a few example of the larger “industries” appearing in the *Economist* chart, with their corresponding revenues and the change in CR4 from 1997 to 2012:

- full-service restaurants (\$224 billion, CR4 up from 8% to 9%);
- direct health and medical insurance carriers (\$647 billion, CR4 up from 20% to 34%)
- general medical and surgical hospitals (\$657 billion, CR4 down from 11% to 8%)
- scheduled passenger air service (\$157 billion, CR4 up from 25% to 65%)
- supermarket and other grocery stores (\$537 billion, CR4 up from 21% to 31%)
- wired telecommunications carriers (\$286 billion, CR4 up from 47% to 51%)

These examples illustrate a major problem with any claim based on these data that concentration has systematically risen in well-defined relevant markets, much less than there has been a decline in competition in these markets: the *geographic* markets for many of these services, including those for full-service restaurants, supermarkets, wired telecommunications services, and hospitals, are *local*, while the measurement exercise is being done at the *national* level.

So, while these data do reflect the fact that large, national firms have captured an increasing share of overall revenue during the past 20 years in many of these 893 “industries”, they do not, in and of themselves, indicate that the relevant *local* markets have become more concentrated. This point is quite important in many of the markets in most of the major sectors reported by the *Economist*: Accommodations and Food, Finance, Health Care, IT, Professional Services, Property, Retail, Transport & Warehousing, Utilities, and Wholesale. The general shift from local firms to national firms is not a cause for concern from the perspective of competition policy if this shift is the result of these national firms providing greater value to consumers. Of course, this shift is a cause for concern if one believes for other reasons that it is important to protect small businesses and entrepreneurs from competition by larger firms.

A distinct problem arises in the manufacturing sector. The following chart illustrates the data from the *Economist* confined to manufacturing:



The *Economist* reports a small increase from 1997 to 2012 in the weighted-average CR4 across these manufacturing “industries”, from about 41% to about 43%, in these Economic Census data. Moreover, it is important to understand, when interpreting this increase in concentration, that the Economic Census data only report production at *domestic* establishments. These data do not include imports of manufactured products, which have grown dramatically over the past 20 years.

Peltzman (2014) looks more deeply at trends in concentration in the manufacturing sector over a longer period of time, 1963 to 2007. He finds no overall increase in concentration from 1963 to 1982, but an increase in concentration following the relaxation of merger enforcement in 1982. He reports that the median HHI in 1982 in the manufacturing industries reported by the Economic Census was 565, and that the median HHI in 2002 for industries with the same definition in both years rose by 97 points, to 662. He finds higher HHI levels and increases for consumer goods than for producer goods.³⁰ Peltzman does not assert that these increases in concentration reflect a decline in manufacturing competition, recognizing that moderate increases in concentration can easily go hand in hand with greater competition due to the presence of economies of scale and efficiency differences across firms.

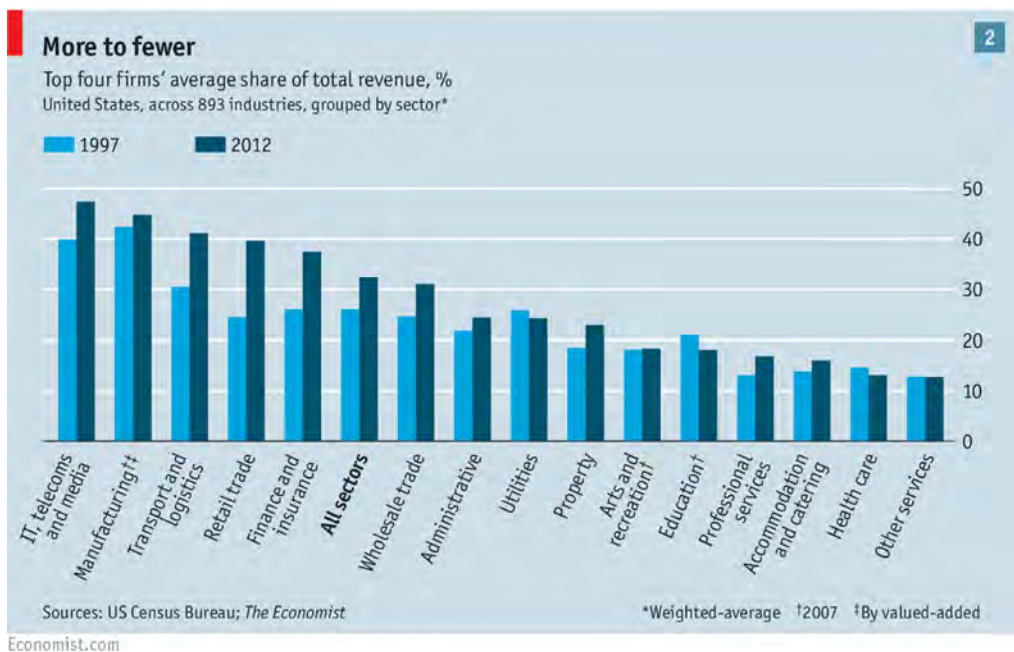
So far as I can determine, all of the various press reports and policy papers raising the alarm about increasing concentration in the U.S. economy ultimately rely on data from the Economic Census. These data convince me that larger firms have systematically

³⁰ See Tables 6 and 7, respectively.

gained business relative to smaller ones, and they no doubt reflect worrisome increases in concentration in *some* narrower markets. But, simply as a matter of measurement, the Economic Census data that are being used to measure trends in concentration do not allow one to measure concentration in relevant antitrust markets, i.e., for the products and locations over which competition actually occurs. As a result, it is far from clear that the reported changes in concentration over time are informative regarding changes in competition over time.

3.1.2. The magnitude of the reported increases in concentration

Let us now set aside these measurement issues and focus on the *magnitude* of the reported increases in concentration. In summarizing the data discussed above covering the 893 four-digit industries, the *Economist* reported, for each broad sector in the economy, the weighted-average increase in the four-firm concentration ratio from 1997 to 2012 as measured across the various “industries” in that sector.³¹ The following chart shows their results.³²



³¹ The weights are based on revenue, except for manufacturing, where the weights are based on value-added.

³² See <https://www.economist.com/news/briefing/21695385-profits-are-too-high-america-needs-giant-dose-competition-too-much-good-thing>.

The *Economist* summarized their findings, stating: “The weighted average share of the top four firms in each sector has risen from 26% to 32%”. See the “All Sectors” bar in the chart.³³

What does the structure of a market with a CR_4 of 32% look like? As an illustration, think about a market with a CR_4 of 32% in which the top four firms have shares of 10%, 8%, 8% and 6%. There must be at least 11 more firms, since the largest any of these other firms can be is 6%, and they comprise 68% of the market. The HHI in this market is between 300 and 700. Industrial organization economists would generally describe this market as being unconcentrated. Since 1982, the Horizontal Merger Guidelines have considered markets with HHIs of less than 1000 to be unconcentrated.

Autor et al. (2017) report similar findings to those in the *Economist*. They too rely on data from the Economic Census, looking at the changes in CR_4 and CR_{20} from 1982 to 2012 at the four-digit industry level, based on sales and based on employment. They then take averages across six broad sectors: manufacturing, retail trade, wholesale trade, services, finance, and utilities and transportation. Below I reproduce their charts illustrating their basic findings regarding concentration in these six sectors:

Autor et al. (2017a) summarize their findings (p. 183) this way:

There is a remarkably consistent upward trend in concentration in each sector. In manufacturing, the sales concentration ratio among the top four increases from 38 percent to 43 percent; in finance, it rises from 24 percent to 35 percent; in services from 11 percent to 15 percent; in utilities from 29 percent to 37 percent; in retail trade from 15 percent to 30 percent; and in wholesale trade from 22 percent to 28 percent.

Autor et al. (2017b) use these same data to report average changes in the HHI by sector from 1982 to 2012. They find an average increase in the HHI in manufacturing from 800 to 875, in finance from 300 to 700, in services from 950 to 1375, in utilities and transportation from 525 to 725, in retail trade from 125 to 625, and in wholesale trade from 325 to 350.

For better or worse, I very much doubt that many antitrust economists would be concerned to learn that a market had experienced these types of increases in the CR_4 or the HHI. Currently, the Horizontal Merger Guidelines consider a market to be unconcentrated if the HHI is below 1500; prior to 2010, the threshold was 1000. The threshold was raised in 2010 to reflect the actual enforcement policies of the DOJ and the FTC and the experience of these antitrust agencies that mergers leading to HHI levels below 1500 typically did not cause competitive problems. Are antitrust economists, who have looked most closely on a case-by-case basis at the relationship between concentration and competition, in literally thousands of cases, completely off base here? Possibly, but I very much doubt it.

³³ We know from the previous chart that these averages mask considerable variation, and that some of the 893 four-digit industries have experienced very large increases in concentration leading to a high CR_4 . I focus here on the averages since we are looking for systematic and widespread changes in concentration.

To summarize, the Economic Census data show a modest average increases in concentration in four-digit NAICS industries. While these four-digit industries often do not line up well with properly defined antitrust markets, these data may reflect increases in concentration in many properly defined antitrust markets over the past 30 or 40 years. Indeed, it would be surprising if that were *not* the case, given the very substantial relaxation of merger enforcement in 1982 for firms with small or modest market shares and in markets with an HHI of less than 1000. The real question is whether those modest increases in concentration have been accompanied by a decline in competition, leading to higher prices or other consumer harms. One cannot answer that question just by looking at measures of concentration, no matter how good the data.

3.1.3. *The relationship between trends in concentration and competition*

Moving past these issues of measurement and magnitude, we come to some deeper questions. How should one interpret changes in concentration over time, and what forces would cause such changes to occur? To sharpen these key questions, consider these two alternative hypotheses:

- *Increase in Concentration Indicates a Decline in Competition:* If we see a market experience an increase in concentration over time, that indicates that this market has become less competitive.
- *Increase in Concentration Reflects the Forces of Competition:* If we see a market experience an increase in concentration over time, that reflects the forces of competition at work, with the firms providing better value to customers gaining market share.

So far as I can determine, the bulk of what has been written in the popular press simply *assumes* that an increase in concentration indicates a decline in competition—even if the resulting level of the four-firm concentration index is only 30% or 40%, meaning that quite a few firms continue to compete. Such an assumption strikes me as unjustified, especially given the forces of globalization and technological change that have transformed many industries in recent decades.

How can we distinguish between the two hypotheses presented above?

First, we need to recognize that markets in the U.S. economy differ vastly: in some markets an increase in concentration over time does indeed indicate a decline in competition, while in other markets the increase in concentration reflects the forces of competition at work. As a result of this heterogeneity, we need to look at individual markets, or at different sectors in the economy, to properly understand and interpret the changes in concentration we observe over time.

Second, and closely related, it is very important to understand the *process* by which concentration has increased over time in any given market. If the increase in concentration resulted from horizontal mergers, that opens up the possibility that inadequate merger enforcement was at fault. Merger retrospectives would be very informative in such markets, to see if the mergers that significantly raised concentrated also harmed customers. Alternatively, if a market has experienced an increase in concentration due to

internal growth by one or a few suppliers, that suggests that these suppliers enjoyed some competitive advantages and gained market share by offering better value to customers, unless these firms engaged in some type of anti-competitive, exclusionary conduct. Identifying those competitive advantages, and the means by which the winners gained market share, would be very informative in this situation.

Several recent empirical studies take on the ambitious task of trying to answer these and related questions for the whole U.S. economy, or at least shed light on them, using concentration measures at the four-digit level based on data from the Economic Census.³⁴ Autor et al. (2017a) and (2017b) ask whether increases in concentration reflect the forces of competition, “so that super-star firms with higher productivity increasingly capture a larger slice of the market”, or “arise from anticompetitive forces whereby dominant firms are able to prevent actual and potential rivals from entering and expanding”.³⁵ Based on their finding that the industries that became more concentrated tended also to be the ones in which productivity increased the most, they conclude: “The findings suggest that a positive productivity-concentration relationship will most likely be a feature of any plausible explanation of rising industry concentration”. Their findings support the view that observed increases in concentration generally reflect the forces of competition at work in manner that has enhanced productivity. Antitrust economists would normally expect this type of competition to benefits customers as well.

Along similar lines, Bessen (2017) finds that an industry’s use of information technology systems (IT) is strongly associated with the level of concentration in that industry and the rise in concentration from 2002 to 2007. Within an industry, use of IT is associated with larger plant size, higher labor productivity, and higher operating profits margins. Focusing on the deployment of proprietary, mission-critical IT systems, he reaches this conclusion: “Successful IT systems appear to play a major role in the increases in industry concentration and in profit margins, moreso than declining concentration”.

3.2. Corporate profits

I now turn my attention to trends in corporate profits. The idea is simple enough: when markets are competitive, supra-normal profits will tend to be transitory. While any single firm may have high and persistent profits simply because it is especially efficient, observing high and persistent profits on a widespread basis tends to suggest that many firms are earning rents associated with market power and that their positions are protected by barriers to entry.

The *Economist* has been especially vocal on this issue, writing: “Profits are an essential part of capitalism. ... But high profits across a whole economy can be a sign of sickness.

³⁴ Gutiérrez and Philippon (2016) and Grullon, Larkin and Michaely (2017) use Compustat data to measure concentration at the three-digit level. For the reasons given above, I am highly skeptical that concentration measures at the three-digit (or two-digit) level are informative regarding competitive conditions in well-defined markets.

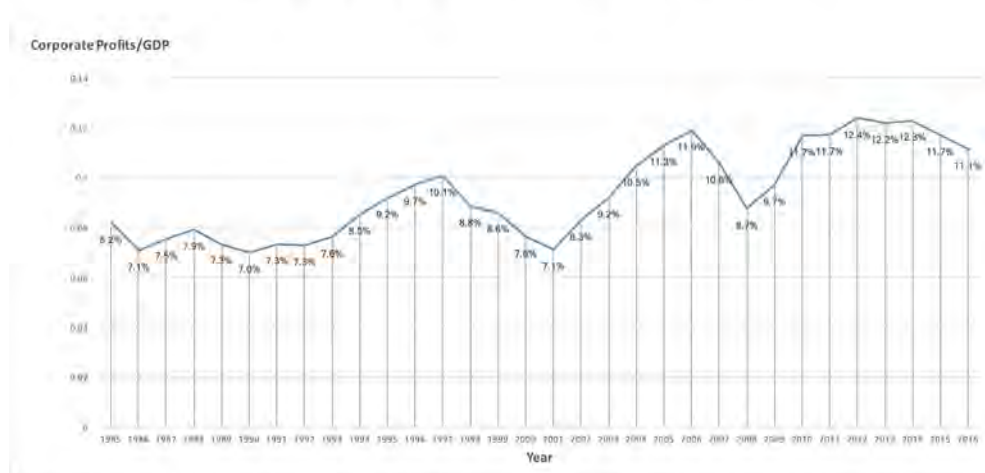
³⁵ Autor, et. al. (2017a), p. 184. Similarly, Barkai (2016) finds a correlation across industries between increases in concentration over time and declines in the labor share of valued-added over time.

They can signal the existence of firms more adept at siphoning wealth off than creating it afresh, such as those that exploit monopolies. If companies capture more profits than they can spend, it can lead to a shortfall of demand. This has been a pressing problem in America”.³⁶

Before turning to the data, it is worth noting that accounting profits often fail to line up with true economic profits. So, some caution is appropriate when looking at economy-wide data on profits. However, the disconnect between accounting profits and economic profits may matter less when looking at *changes* in profits over time than when looking at the *level* of profits, and when looking at a large number of firms.

Here is what the national income accounts show about corporate profits over the past 30 years:

Corporate Profits/GDP: 1985 to 2016



Source: Bureau of Economic Analysis, Table 1.7.5, “Relationship of Gross Domestic Product, Gross National Product, Net National Product, National Income and Personal Income.” Last Revised September 28, 2017, available at <https://bea.gov/iTable/iTable.cfm?reqid=19&step=2#reqid=19&step=3&isuri=1&1910=x&0=-9&1921=survey&1903=43&1904=1977&1905=2017&1906=a&1911=0>.

The Bureau of Economic Analysis (BEA) is seeking to measure “profits from current production”, so this measure of corporate profits excludes dividend income and capital gains and losses.³⁷ The BEA makes adjustments for changes in the value of inventories and depreciation of capital assets. Still, properly measuring corporate profits is a tricky business, not least because of unavoidable gaps between reported accounting profits and

³⁶ *Economist*, 26 March 2016, “Too Much of a Good Thing”, available at <https://www.economist.com/news/briefing/21695385-profits-are-too-high-america-needs-giant-dose-competition-too-much-good-thing>.

³⁷ See “Chapter 13: Corporate Profits”, December 2015, at <https://www.bea.gov/national/pdf/chapter13.pdf>. This measure of corporate profits includes all U.S. corporations and is made before deducting corporate income taxes.

true economic profits. I cannot delve into these important issues here; I confine my attention to high-level trends.

In short: there has been a very substantial increase in corporate profits as a share of GDP over the past thirty years: roughly a 50% increase from 7% to 8% of GDP up to 11% to 12% of GDP.

Interpreting this substantial increase in corporate profits is not straightforward, so my observations here are necessarily tentative. For example, one can ask how much of the growth in corporate profits merely reflects a higher cost of capital, e.g., due to higher interest rates or increased risk taking. I am highly skeptical of this explanation, especially given the historically low interest rates in the United States in recent years, which should cause the return on equity to be lower, not higher. Barkai (2016) firmly rejects this explanation.³⁸ One can also ask whether the increase in corporate profits is due to increased exports by U.S. corporations, which have little to do with increased market power in U.S. markets.³⁹ Plus, of course, it is always possible that some of the reported increase in corporate profits merely reflects accounting issues rather than an increase in true economic profits.

Still, these data strongly suggest that U.S. corporations really are systematically earning far higher profits than they were 25 or 30 years ago. Combined with other evidence that large corporations are accounting for an increasing share of revenue and employment, it certainly appears that many large U.S. corporations are earning substantial incumbency rents, and have been doing so for at least 10 years, apart from during the depths of the Great Recession.

There is also some limited evidence that high levels of profits are persistent at the firm level.⁴⁰ High and persistent profits for any one firm are easy to explain, in theory, based on that firm being more efficient than its rivals. But if high and persistent profits are widespread, any economist will naturally ask why competitive forces are not eroding those supra-normal profits.

This evidence leads quite naturally to the hypothesis that economies of scale are more important, in more markets, than they were 20 or 30 years ago. This could well be the result of technological progress in general, and the increasing role of information technology in particular. On this view, today's large incumbent firms are the survivors

³⁸ Barkai breaks out corporate profits into a required rate of return on capital and extra “profits” or rents. He finds “a large increase in the profit share in the U.S. non-financial corporate sector over the past 30 years.”

³⁹ The share of profits earned by U.S. corporations from exports grew from 14% in 1998 to 18% in 2016. BEA Table 6.17D, “Corporate Profits Before Tax by Industry”, 3 August 2017. So the growth of profits from exports explains a small portion of the overall growth of corporate profits as a share of GDP over the past 20 years.

⁴⁰ The *Economist* article on high profits cited McKinsey for the proposition that there was greater persistence of high profits from 2003 to 2013 than from 1993 to 2003. This question certainly warrants further study. For example, the *Economist* is referring to the persistence of profits at the level of the firm, but from a competition perspective we are more interested in persistence for a firm's participation in a specific market. For more on McKinsey's “economic profit” measure, see Chris Bradley, Angus Dawson, and Sven Smit, “The Strategic Yardstick You Can't Afford to Ignore”, *McKinsey Quarterly*, October 2013, available at <http://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/the-strategic-yardstick-you-cant-afford-to-ignore>.

who have managed to successfully obtain and exploit newly available economies of scale. And these large incumbent firms can persistently earn supra-normal profits if they are protected by entry barriers, i.e., if smaller firms and new entrants find it difficult and risky to make the investments and build the capabilities necessary to challenge them. As discussed in more detail below, in markets where this state of affairs prevails, namely oligopolies protected by barriers to entry, antitrust has a critical role to play to control mergers and acquisitions involving large incumbent firms, and to prevent these firms from engaging in exclusionary conduct.

In the hope of shedding some light on what has caused corporate profits to grow so much, I have broken out the BEA data on corporate profits by sector to learn how the growth of corporate profits over the past 20 years has been distributed across sectors. Here are what these data show:

Corporate Profits by Sector: Share of All Domestic Profits

Sector	1998	2016
Utilities	5.3%	1.1%
Construction	4.2%	5.1%
Manufacturing	29.7%	22.1%
Wholesale Trade	8.1%	7.0%
Retail Trade	9.9%	10.2%
Information	5.3%	7.8%
Finance & Insurance	13.6%	18.3%
Health Care & Social Assistance	2.1%	5.2%
Accommodation & Food Services	1.5%	2.6%

Source: Bureau of Economic Analysis, Table 6.17D, “Corporate Profits Before Tax by Industry,” August 3, 2016. 1998 is the earliest year for which these data are available, and 2016 is the latest year. These data are subject to all of the caveats noted above regarding accounting measures of profits.

Looking at this Table, I would highlight the following observations:

- Profits in the Manufacturing Sector fell sharply as a share of the total. This drop is consistent with the declining share of GDP attributable to manufacturing and with increased import competition. But we know from the literature on labor productivity that manufacturers also lowered their costs through automation. Manufacturing profits were roughly constant as a share of GDP (from 29.7% of 8.8% of GDP, which is 2.6% of GDP in 1998, to 22.1% of 11.1% of GDP, which is 2.5% of GDP in 2016).
- Profits in the Finance & Insurance sector grew sharply, from 13.6% of the total to 18.3% of the total. Since corporate profits as a share of GDP rose by about 50% from 1998 to 2016, this increase in the share of corporate profits to the finance and

insurance sector corresponds nearly to a doubling of these profits as a share of GDP (from 13.6% of 8.8% of GDP, which is 1.2% of GDP in 1998, to 18.3% of 11.1% of GDP, which is 2.0% of GDP in 2016). During the past five years (2012–2016), BEA Table 6.17D shows that corporate profits in Finance & Insurance totaled \$1.6 trillion. This is rather striking in the wake of the bailouts during the Financial Crisis, and quite worrisome given the consolidation that has taken place in this sector.

- Profits in the Health Care & Social Assistance sector have more than doubled as a share of the total. This most likely reflects both growth and consolidation in this sector.
- Profits in the Information Sector, which includes both media and high-tech, have grown as a share of the total, but not as dramatically as one might have thought looking at the enormous stock market values now attached to the largest firms in the tech sector. These sky-high market caps tell us that investors expect high future profits from these firms, suggesting that the share of profits attributable to this sector will continue to grow.

The CEA report looks at how the return to invested capital is distributed across firms, stating: “Returns on invested capital for publicly-traded U.S. non-financial firms have also become increasingly concentrated within a smaller segment of the market. Fig. 1 indicates that the 90th percentile firm sees returns on investments in capital that are more than five times the median. This ratio was close to two just a quarter of a century ago”.⁴¹ This observation is consistent with the findings of Autor et al. (2017b) that a relatively few “superstar” firms have captured a greater share of sales and profits in recent decades.

When interpreting the evidence on trends in corporate profits, it is useful to view that evidence in the context of two other ongoing trends relating to American businesses. First, there has been a long and steady decline in the rate at which new businesses are formed in the United States. Fig. 2 from the CEA Report shows that firm entry rates declined steadily from 1977 through 2013. Decker et al. (2016) discuss this trend in greater depth. Second, the United States has experienced a much-discussed productivity slowdown over the past 15 years, during which time the gap between the most productive and the least productive firms has widened.⁴² This growing gap may well reflect competition at work, as some firms become more efficient than their rivals. However, given the high levels of profits, it is natural to ask whether the growing gap between leaders and laggards also reflects less vigorous competition in oligopolistic markets, as the more efficient firms take their profits in the form of high price/cost margins rather than cutting prices to gain share, which would be more likely to force their less efficient rivals to exit the market.

⁴¹ Council of Economic Advisers (2016), p. 5. These data were compiled by the McKinsey Corporate Analysis tool in a manner that is opaque to me. See Furman and Orszag (2015).

⁴² See, for example, Baily and Montalbano (2016), which reports increasing productivity dispersion across firms and declining rates of new business formation. Andrews, et. al. (2015) show that productivity dispersion is increasing in many OECD countries. For thoughtful commentary on this evidence, see “The Great Divergence”, *Economist*, 12 November 2016, available at <https://www.economist.com/news/business/21709976-group-elite-firms-has-established-sustained-lead-not-good-thing-great>.

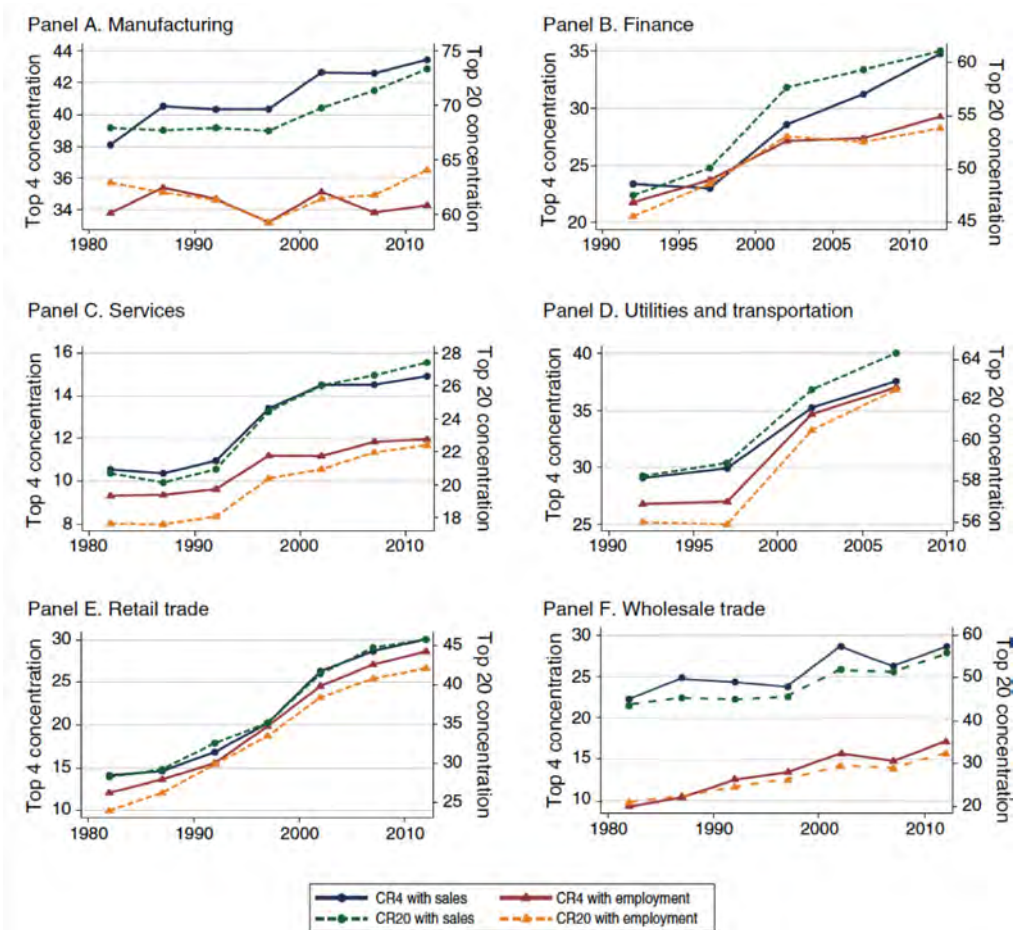


Fig. 1. Average top 4 industry concentration by major industry group.

This question is of great importance, given the findings of Decker et al. (2017) that much of the recent slowdown of productivity growth can be attributed to a weakening of the process by which resources shift toward the more efficient firms within an industry.

These concerns are further enhanced by evidence that high corporate profits are expected to persist into the future. This is most clear in the tech sector, where the platform leaders have breathtaking market caps. But the continued strength of the stock market generally must reflect investors' confidence that high corporate profit flows are durable, together with low interest rates. The *Economist* calls this "the hidden message in American companies' balance-sheet".⁴³

⁴³ "The United States of Debt", *Economist*, 15 July 2017, at <https://www.economist.com/news/business/21725010-hidden-message-american-companies-balance-sheets-united-states-debt>.

In sum, the evidence on corporate profits clearly shows that corporate profits have risen as a share of GDP. This evidence also points to a rise in incumbency rents, i.e., excess profits earned by firms whose positions are protected by high barriers to entry. While any good capitalist is naturally tempted to applaud the success of the large U.S. firms that have seen their profits grow so significantly, perhaps we should hold our applause until we understand better why competitive forces have not (yet?) been more effective at eroding these profits. Profits necessary to induce risky investments are one thing; incumbency rents are quite another.

4. Antitrust and competition policy responses

What does all of this imply for antitrust policy and competition policy going forward?

Antitrust policy can address concerns about rising concentration and high corporate profits (a) by increasing cartel enforcement efforts; (b) by imposing tighter controls on mergers; and (c) by taking a tougher approach to exclusionary conduct by dominant firms. Looking at competition policy more broadly, additional tools can come into play: (d) adopting policies that reduce entry barriers; (e) actively breaking up large firms in concentrated markets; and (f) regulating firms deemed to have substantial market power. I now address these six policy areas in turn.

4.1. *Stricter cartel enforcement*

Detecting and punishing collusion is the most fundamental component of antitrust policy. Cartels are criminal violations in the United States. I believe there is a consensus that antitrust enforcement in this area has become tougher over the past 25 years, both in the United States and especially worldwide. This can be attributed in part to the leniency program adopted and expanded by the DOJ some 25 years ago, and in part to the strengthening of anti-collusion laws and enforcement efforts in many countries and jurisdictions around the world, together with improved international cooperation in cartel investigations. Nonetheless, it is well understood that not all cartel activity is deterred. Indeed, the DOJ seems to uncover a steady stream of major cartels, many of them international in scope. So there is always more to do here.

More concentrated markets are generally regarded as more susceptible to the harms caused by durable, effective cartels and legal, interdependent conduct. Indeed, historically, the central rationale for merger enforcement was to limit market concentration to reduce the incidence of cartels and other forms of coordination among oligopolists. Logically, then, to the extent that U.S. markets have become more concentrated over time, cartel enforcement becomes all the more vital. Devoting additional resources to cartel enforcement is a natural response.

4.2. Stricter merger enforcement

Several types of economic evidence all support moving toward stricter merger enforcement in the United States: evidence that U.S. markets have become more concentrated, evidence that price/cost margins have risen, evidence that entry barriers have become higher, and evidence that corporate profits have risen substantially and are expected to persist.

Merger enforcement is especially important since a wide range of interdependent conduct by oligopolists, i.e., conduct whereby the oligopolists refrain from vigorous competition, is not considered to be illegal if it does not involve an agreement among those oligopolists.

Tightening up on horizontal merger enforcement policy would directly address the rising levels of concentration over the past 20 to 30 years that have received so much attention of late. Merger policy became noticeably more lenient with the adoption of the 1982 Merger Guidelines, which is roughly when concentration levels started to rise, at least in the manufacturing sector.⁴⁴ The 1968 Merger Guidelines stated that the DOJ “will ordinarily challenge” a merger between two firms with 5% market share each, or between a firm with a 20% market share and a firm with a 2% market share.⁴⁵ An even stricter approach was applied in markets with CR4 in excess of 75% and in markets with a trend toward concentration. Under the 1982 Merger Guidelines, only much larger levels and changes in concentration would trigger a presumption by the DOJ that a merger would harm competition.⁴⁶

Antitrust economists have debated for many years where to draw the line for horizontal merger enforcement. This is very much an empirical question. Merger retrospectives are especially valuable in this respect, since they directly address the relevant question: which mergers harm customers by lessening competition? There are a number of convincing merger retrospectives, especially those based on a difference-in-differences analysis, such as [Ashenfelter and Hosken \(2010\)](#). [Blonigen and Pierce \(2016\)](#) also is highly informative. They look at the impact of mergers across a wide range of industries using plant-level data, also taking a difference-in-differences approach. They find that mergers are associated with increases in average markups. They find little evidence that mergers increase efficiency through rationalization of production across plants or through savings in administrative costs. Overall, the evidence from U.S. merger retrospectives supports a shift to a moderately stricter merger enforcement policy.⁴⁷

[Salop and Shapiro \(2017\)](#) and [Hovenkamp and Shapiro \(2018\)](#) advocate a moderately stricter merger control policy. Treating horizontal mergers more strictly is directly

⁴⁴ See [Peltzman \(2014\)](#), op. cit. who makes precisely this argument.

⁴⁵ 1968 Merger Guidelines, at <https://www.justice.gov/sites/default/files/atr/legacy/2007/07/11/11247.pdf>, p. 6.

⁴⁶ 1982 Merger Guidelines, at <https://www.justice.gov/sites/default/files/atr/legacy/2007/07/11/11248.pdf>, p. 14. The 1982 Merger Guidelines also allowed more defenses in cases where the concentration line was crossed.

⁴⁷ See especially [Kwoka \(2015\)](#), with a critique by [Vita and Osinski \(2016\)](#) and response by [Kwoka \(2017a\)](#).

supported by the evidence from merger retrospectives. A shift to stricter merger enforcement is also supported, albeit less directly, by evidence of high and persistent corporate profits, which suggests the presence of meaningful barriers to entry and expansion in many markets. Higher barriers to entry and expansion make it less likely that entry by new firms, or expansion by small ones, will erode any market power that is enhanced by a merger.⁴⁸ In markets where economies of scale are significant, it may well make sense to allow smaller firms to merge to achieve lower costs and thus take on their larger rivals more effectively. But letting the largest firms in such markets merge is more likely to lessen competition, since these firms are each other's strongest rivals. Stricter merger enforcement policy is further supported by the *lack* of evidence that mergers involving industry leaders commonly generate genuine synergies that could not otherwise be achieved,⁴⁹ and by the growing presence of horizontal shareholding.⁵⁰

Stricter merger control policy could involve (a) challenging more mergers, (b) insisting on stronger remedies, and/or (c) including provisions in consent decrees to correct remedial errors.⁵¹ The DOJ and the FTC certainly have sufficient prosecutorial discretion to implement these types of changes. How such a shift would be greeted by the courts is hard to predict, but both the DOJ and the FTC have been quite successful in recent years with their merger challenges, and 50-year old Supreme Court precedent could be cited to support such a shift.⁵²

If the DOJ and FTC were to become more aggressive in challenging mergers, I would expect that would temporarily lead to more merger litigation. If DOJ and FTC were to win these new cases, the case law would evolve in favor of stronger merger enforcement, and the set of proposed mergers would adjust accordingly, so long as the DOJ and FTC stay the course. Alternatively, if the DOJ and FTC were to lose these new cases, they would be forced to pull back. In thinking about this dynamic, it is important to bear in mind that only a small fraction of proposed mergers are challenged by the DOJ and the FTC, and a tiny fraction result in a decision by the court. In the 2016 fiscal year, for example, 1832 merger transactions were reported to the DOJ and the FTC, of which 47, some 2.6%, were challenged, and only a few resulted in a court decision.⁵³

One promising way to tighten up on merger enforcement would be to apply tougher standards to mergers that may lessen competition *in the future*, even if they do not lessen competition right away. In the language of antitrust, these cases involve a loss of *potential*

⁴⁸ Likewise, if one accepts the finding by De Loecker and Eeckhout (2017) that price/cost margins in the U.S. economy rose sharply from 1980 to 2014, that would tend to indirectly support stricter merger enforcement policy.

⁴⁹ For a recent study, see “Mergers and Acquisitions Often Disappoint”, *Economist*, October 7, 2017.

⁵⁰ Horizontal shareholding refers to situations in which an institutional investor owns shares of two or more firms that are rivals in a concentrated product market. Scott Morton and Hovenkamp (2018) discuss the antitrust policy implications of horizontal shareholding. One implication is that horizontal mergers are likely to have anti-competitive effects at lower levels of market concentration than would otherwise be the case.

⁵¹ For more on how this last proposal could work, see Salop (2016).

⁵² See, especially, *United States v. Philadelphia National Bank*, 374 US. 321 (1963). See Hovenkamp and Shapiro (2017) on the legal and economic support for the “structural presumption” established in that case, and Kwoka (2017b) for further analysis supporting the use of the structural presumption.

⁵³ See Federal Trade Commission and U.S. Department of Justice Antitrust Division (2017).

competition. One common fact pattern that can involve a loss of future competition occurs when a large incumbent firm acquires a highly capable firm operating in an adjacent space. This happens frequently in the technology sector. Prominent examples include Google's acquisition of YouTube in 2006 and DoubleClick in 2007, Facebook's acquisition of Instagram in 2012 and of the virtual reality firm Oculus CR in 2014, and Microsoft's acquisition of LinkedIn in 2016. Smaller acquisitions happen on a regular basis, and indeed are an important exit strategy for tech startups.

Acquisitions like these can lessen future competition, even if they have no such immediate impact. To illustrate, suppose that the target firm has no explicit or immediate plans to challenge the incumbent firm on its home turf, but is one of several firms that is best placed to do so in the next several years by developing innovative new products or by improving or modifying its existing products. Not even the target firm knows for sure how its product offerings will evolve. Does it seem so far-fetched that the dominant incumbent firm, whose market capitalization will fall sharply if successful entry occurs, would pay a premium to acquire the target firm in order to avoid the risk of facing this pesky rival in a few years' time? Not to me. Nor does it seem far-fetched that a dominant incumbent firm can reliably identify the firms that are genuine future threats before the antitrust agencies or the courts can do so with confidence.

The problem for merger enforcement is distinguishing this fact pattern from a situation in which the dominant incumbent can and will greatly expand the reach and usage of the target firm's products, e.g., by combining the two products into one, or by using its distribution might to rapidly expand sales of the target firm's products. Making the problem even harder, these fact patterns can occur together for a single proposed merger.

Another classic example of a merger that may lessen competition in the future involves a leading incumbent firm merging with a large supplier, a large customer, or a large firm selling a complementary product, especially if the target firm is contemplating entering the incumbent's market. This was the case when the DOJ challenged the merger between Ticketmaster, which was dominant in providing ticketing services to certain venues, and LiveNation, which was a large customer of Ticketmaster that was developing its own ticketing services.⁵⁴ While such vertical mergers can generate efficiencies, they also can eliminate potential competition.

The DOJ and the FTC have been quite cautious about challenging mergers involving firms that do not currently compete (either much or at all) but which may well become important direct rivals in the foreseeable future. This reticence stems in part from the difficulty of showing that such a merger would significantly increase concentration in a well-defined market, which is normally a key element of the government's case. By showing such an increase in concentration, the government can establish a *prima facie* case that the merger is likely to substantially lessen competition. Furthermore, merger challenges based on the loss of potential competition necessarily rely on the prediction that the two merging firms will become significant competitors in the future. This is

⁵⁴ See <https://www.justice.gov/atr/case/us-et-al-v-ticketmaster-entertainment-inc-et-al>.

inherently a difficult thing to predict, and even harder for the government to prove as the merging firms themselves are trying to convince a court otherwise. And these obstacles are even harder in the high-tech sector, where products and services have overlapping functionality and can change significantly over relatively short periods of time.

Notwithstanding these genuine difficulties, there would be a big payoff in terms of competition and innovation if the DOJ and FTC could selectively prevent mergers that serve to solidify the positions of leading incumbent firms, including dominant technology firms, by eliminating future challengers.⁵⁵ As a general principle, the greater and more durable is the market power of an incumbent firm, the larger is the payoff from preventing that firm from acquiring the smaller firms that, if left to grow on their own, would become its strongest challengers. Sound competition policy would tolerate some false positives – blocking mergers involving targets, only to find that they do not grow to challenge the incumbent – in order to avoid some false negatives – allowing mergers that eliminate targets that would indeed have grown to challenge the dominant incumbent.

4.3. Controlling exclusionary conduct by dominant firms

Many of those calling for stronger antitrust enforcement are especially concerned about what they see as the enormous power of the largest tech firms, notably Amazon, Apple, Facebook, Google, and Microsoft.⁵⁶ The *Economist*, calling these firms “high-tech wizards”, states:

“the superstars are admirable in many ways. They churn out products that improve consumers’ lives, from smarter smartphones to sharper televisions. They provide Americans and Europeans with an estimated \$280 billion-worth of “free” services—such as search or directions—a year. But they have two big faults. They are squashing competition, and they are using the darker arts of management to stay ahead. Neither is easy to solve. But failing to do so risks a backlash which will be bad for everyone”.⁵⁷

⁵⁵ In Shapiro (2011), I explain that mergers between future rivals slow down innovation unless they significantly internalize spillovers associated with R&D or enable merger-specific synergies in conducting R&D. I specifically show that the evidence put forward in the literature that there is an inverse U-shaped function relating competition to innovation is generally either misleading or not relevant for the purpose of merger enforcement.

⁵⁶ Farhad Manjoo at the *New York Times* has taken to calling these firms the “Frightful Five.” See, for example, “Tech’s ‘Frightful 5’ Will Dominate Digital Life for Foreseeable Future”, *New York Times*, 20 January 2016, available at <https://www.nytimes.com/2016/01/21/technology/techs-frightful-5-will-dominate-digital-life-for-foreseeable-future.html>, “Tech’s Frightful Five: They’ve Got Us”, *New York Times*, 10 May 2017, available at <https://www.nytimes.com/2017/05/10/technology/techs-frightful-five-theyve-got-us.html>, and “How the Frightful Five Put Start-Ups in a Lose-Lose Situation”, *New York Times*, 18 October 2017, available at <https://www.nytimes.com/2017/10/18/technology/frightful-five-start-ups.html?rref=collection%2Fsectioncollection%2Fbusiness&action=click&contentCollection=business®ion=rank&module=package&version=highlights&contentPlacement=1&pgtype=sectionfront>.

⁵⁷ “A Giant Problem: The Rise of the Corporate Colossus Threatens Both Competition and the Legitimacy of Business”, *Economist*, 17 September 2016, op. cit.

Some are even calling to break up Amazon, Facebook and Google.⁵⁸

The *Economist* points squarely to antitrust as the solution to the “giant problem” posed by the largest tech firms, stating: “Above all, policymakers need to revamp antitrust policy for a world based on information and networks rather than on selling lumps of stuff”.⁵⁹ When it comes to specifics on just how antitrust policy needs to be revamped, the *Economist* is far more cautious than those calling for breakups, and far more grounded in U.S. antitrust law:

Antitrust authorities need to start setting the agenda by examining the ways that digital companies are using network effects to crowd out potential competitors, or inventing new ways of extracting rents by repackaging other people’s content. But the regulators must also beware of trying to load too much onto the rules: the point of antitrust policy is to promote competition and hence economic efficiency, not to solve problems such as inequality.⁶⁰

As an antitrust economist, my first question relating to exclusionary conduct is whether the dominant firm has engaged in conduct that departs from legitimate competition and maintains or enhances its dominance by excluding or weakening actual or potential rivals.⁶¹ In my experience, this type of inquiry is highly fact-intensive and may necessitate balancing pro-competitive justifications for the conduct being investigated with possible exclusionary effects. In the end, the key question is whether the conduct disrupts the competitive process and either harms customers or is likely to harm them in the future. Critically, the focus of the inquiry is on specific business conduct, not sheer size and just the presence of substantial market power.

The structured inquiry just sketched has long been the approach to monopolization cases taken by the U.S. courts. I believe this approach is sound and has widespread support among industrial organization economists. So I say: let these inquires proceed when suspicious conduct can be identified. But in doing so, let us avoid a “big is bad” mentality and let us truly have the interests of consumers in mind. We learned long ago that proper antitrust enforcement is about protecting consumers, and protecting the competitive process, not about protecting competitors. We must not forget that guiding principle. Indeed, that principle is especially important in markets subject to large economies of scale, whether those scale economies are based on traditional production economies or based on network effects, which are often important in the tech sector.

In this time of populism, many observers appear frustrated that the DOJ and the FTC have brought very few Sherman Act [Section 2](#) monopolization cases over the past

⁵⁸ “Should America’s Tech Giants Be Broken Up?” *Business Week*, 20 July 2017, available at <https://www.bloomberg.com/news/articles/2017-07-20/should-america-s-tech-giants-be-broken-up>. See also [Taplin \(2017\)](#) and Jonathan Taplin, “Is It Time to Break Up Google” *New York Times*, 22 April 2017, available at https://www.nytimes.com/2017/04/22/opinion/sunday/is-it-time-to-break-up-google.html?_r=0.

⁵⁹ “The Rise of the Superstars”, *Economist*, 17 September 2016, p. 16.

⁶⁰ “The Rise of the Superstars”, *Economist*, 17 September 2016, p. 16.

⁶¹ For issues related to *acquisitions* by dominant incumbent firms, in the tech sector or not, see the previous section.

25 years. I have three reactions to this complaint. First, I can say from personal experience that when I was the chief economist at the DOJ during 2009–2011, the Antitrust Division was genuinely interested in developing meritorious [Section 2](#) cases, and we were prepared to devote the resources necessary to investigate complaints and other leads, but we found precious few cases that warranted an enforcement action based on the facts and the case law.

Second, those calling for more monopolization cases must describe the specific conduct that concerns them and explain how that conduct disrupts the competitive process and harms customers. Simply saying that Amazon has grown like a weed, charges very low prices, and has driven many smaller retailers out of business is not sufficient. Where is the consumer harm? I presume that some large firms are engaging in questionable conduct, but I remain agnostic about the extent of such conduct among the giant firms in the tech sector or elsewhere. For better or worse, over the past thirty years the Supreme Court has made it harder for the government (and private plaintiffs) to win [Section 2](#) cases. The DOJ and the FTC could bring cases in an attempt to broaden the reach of the Sherman Act, but precedent in this area moves very slowly and I see no evidence that the current Supreme Court has an interest in greatly expanding the range of conduct that would be found to violate [Section 2](#) of the Sherman Act.⁶²

Third, it seems clear that some conduct that is permitted under the U.S. antitrust laws will be challenged by the European Commission under E.U. law, but I am not convinced that the European approach to evaluating unilateral conduct by dominant firms is superior to the American approach. In any event, the growing divergence between the U.S. and the E.U. in this area does provide a type of “natural experiment”. Researchers can look at conduct challenged by the European Commission, but not challenged by the DOJ or the FTC, as one way of trying to determine whether eliminating that conduct has led to consumer benefits. Simply observing that the EC is “more aggressive” than the DOJ or the FTC does not answer that question.

4.4. Reducing entry barriers and promoting competition

The evidence of high corporate profits, slower productivity growth, and declining rates of new business formation tells me that we should redouble our efforts to generally reduce entry barriers to promote competition, encourage entrepreneurship, and broaden economic opportunities.

There is bipartisan support for many initiatives along these lines, such as reducing occupational licensing requirements where they serve to protect incumbents rather than consumers,⁶³ and eliminating government restrictions that protect incumbents, such as

⁶² Amending the Sherman Act after 125 years is even more daunting, especially given the dysfunction in the U.S. Congress. Plus, it is not clear to me just what new general legislative language would constitute an improvement.

⁶³ See, for example, [Council of Economic Advisers \(2015\)](#).

the rules in many states that prohibit automobile manufacturers from selling their cars directly to consumers.⁶⁴

4.5. *Breaking up large tech firms*

As noted above, some are calling to break up today's tech giants. If these calls are motivated primarily by concerns about *political* power, then focusing attention on the tech sector seems peculiar to me. What about the energy, health care, media, and finance sectors? If these calls are motivated based on concerns about *economic* power, then I would first like to see some showing that breaking these firms up would leave consumers better off in the foreseeable future.

Any call to break up large tech firms based on economic considerations needs to address the concern that dismembering some of our most successful companies will significantly reduce economic efficiency. We know that firms vary greatly in their efficiencies within an industry, and we know that the more efficient firms tend to grow relative to others, at least until they run into diseconomies of scale. On this basis alone, breaking up the largest and most successful firms makes me rather nervous. On top of that, we know that there are substantial economies of scale of various types in the technology sector, including network effects and the economies of scale resulting from the fixed costs associated with developing new products, especially software and content. So these market may drift back toward winner-takes-most anyhow. I vote for strengthening enforcement of the Sherman Act rather than breaking up the largest tech firms.

4.6. *Regulating dominant firms*

Regulation is an alternative way of controlling monopoly power. Historically, price regulation has been reserved for natural monopolies such as the local distribution of electricity or local telephony. Price regulation is notoriously messy, but it can limit the ability of a firm with durable monopoly power to exploit that power. Antitrust is not well suited to preventing the exploitation of monopoly power, especially since "merely" charging a monopoly price is not an antitrust violation in the United States.

While some are calling to regulate today's dominant technology companies, price regulation tends to work rather poorly in industries experiencing technological change. Furthermore, it is well understood that industry-specific regulators are often subject to regulatory capture. For both of these reasons, I suspect there will be relatively little interest in setting up specialized agencies to prevent today's dominant technology companies from exploiting their market power by regulating the prices they can charge. However, regulations relating to privacy, data ownership and portability, or open interfaces and interconnection may attract widespread support. The substantive rules

⁶⁴ See, for example, [Crane \(2016\)](#).

governing such regulations, and the institutions created to implement such regulations, will matter a great deal to their efficacy.

5. Economic populism as an opportunity and a threat

Antitrust was born and then fortified during a period of populism in the United States in the late 19th and early 20th centuries. Likewise, today's populist sentiments—by which I mean the widespread and bipartisan concern that the deck is stacked in favor of large powerful firms—represent an opportunity, indeed a plea, to strengthen antitrust enforcement.

The empirical evidence supports moving in the direction of stronger merger enforcement. The empirical evidence also supports increased vigilance in preventing dominant firms with durable market power from engaging in business practices that exclude their actual and potential rivals. In this article, I have offered a number of constructive proposals along these lines. Rather than repeat those proposals, I close with a word of caution.

Today's populist sentiments pose a threat as well as an opportunity for antitrust. The danger to effective antitrust enforcement is that today's populist sentiments are fueling a “big is bad” mentality, leading to policies that will slow economic growth and harm consumers. The rest of this article is devoted to identifying this threat and discussing how such an error can be avoided.

I take as my starting point the core principle guiding antitrust enforcement in the United States that has served us well for so many years: *antitrust is about protecting the competitive process so consumers receive the full benefits of vigorous competition*. None of the empirical evidence relating to growing concentration and growing corporate profits, which I have discussed at length in this article, provides a basis for abandoning this core principle.

Applying this core principle, we understand quite well how to use antitrust to protect competition and consumers, at least conceptually. This enterprise centers on the economic notion of market power, and relies heavily on industrial organization economics. Of course, there is always room for improvement in practice, and right now that means stricter merger enforcement and vigilance regarding acts of monopolization, as already discussed.

The fundamental danger that 21st century populism poses to antitrust is that populism will cause us to abandon this core principle and thereby undermine economic growth and deprive consumers of many of the benefits of vigorous but fair competition. Economic growth will be undermined if firms are discouraged from competing vigorously for fear that they will be found to have violated the antitrust laws, or for fear they will be broken up if they are too successful.

Populism poses this danger in part because today's populism is in many ways animated more by concerns about the *political* power of large corporations than by concerns about their *economic* power. In this sense, there is a mismatch between 21st century populism and modern antitrust. More specifically if antitrust policy is altered to serve

goals other than the economic goals of promoting competition and protecting consumers, the core principle articulated above would have to be modified or abandoned. Examples of alternative goals for antitrust are the goal of having more small local businesses, the goal of raising wages or employment, and the goal of reducing the political power of large businesses.

I am deeply concerned about the current state of the American political system, and specifically about the political power of large corporations and the cramped definition of corruption that has been adopted by the Supreme Court.⁶⁵ Readers may be interested to learn that the *original* Chicago School, back in the 1920s and 1930s, which was associated with Frank Knight and Henry Simons, was also deeply concerned about the political power of large organizations. Here is what Henry Simons had to say in 1934:

“The representation of laissez faire as a merely do-nothing policy is unfortunate and misleading. It is an obvious responsibility of the state under this policy to maintain the kind of legal and institutional framework within which competition can function effectively as an agency of control. Thus, the state is charged, under this ‘division of labor,’ with heavy responsibilities and large ‘control’ functions: the maintenance of competitive conditions in industry”...⁶⁶

Simons went on (p. 4) to state that “the great enemy of democracy is monopoly, in all its forms”. As a practical matter, I do not see that antitrust can do a great deal to solve the deep problems we face relating to the political power of large corporations and the corruption of our political system. And I fear that assigning those massive tasks to antitrust will be counterproductive.

My hope is that the intense energy of populism will empower stronger antitrust enforcement policy in the United States with the goal of protecting the competitive process and channeling more of the benefits of economic growth to consumers. To protect and preserve this mission, it is important to recognize that antitrust cannot be expected to solve the larger political and social problems facing the United States today. In particular, while antitrust enforcement does tend to reduce income inequality, antitrust cannot and should not be the primary means of addressing income inequality; tax policies and employment policies need to play that role. Nor can antitrust be the primary policy for dealing with the corruption of our political system and the excessive political power of large corporations; that huge problem is better addressed by campaign finance reform, a better-informed citizenry, stronger protections for voting rights, and far tougher laws to combat corruption. Trying to use antitrust to solve problems outside the sphere of competition will not work and could well backfire.

⁶⁵ For an excellent discussion on this vitally important topics, see Teachout (2014).

⁶⁶ Simons (1934), p. 3.

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1

Towards a Broader View of Competition Policy

*Joseph E Stiglitz**

I. Brief History of Competition Policy (Antitrust)

Competition policy (antitrust) began in the United States as a *political* agenda, to limit the market and *political* power of trusts (monopolies and oligopolies). Of course, long before that, economists had recognized that competition was necessary if the market economy was to achieve efficient outcomes,¹ and that firms on their own strive to limit competition. As Adam Smith put it: ‘People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.’²

Market power has, of course, distributive effects as well. The monopolist’s rents come at the expense of consumers: As monopolies raise their prices, their profits increase, while the well-being of consumers and workers decreases. An increase in market power is associated with an increase in inequality.

* University Professor, Columbia University. This is a revised draft of a lecture originally presented at the Fourth BRICS International Competition Conference in Durban, November 2015. I am indebted to Laurence Wilse-Samson for helpful comments on an earlier draft, to Steven Salop and Michael Cragg for discussions over the years on the broader issues of antitrust, and to Eleanor Fox for extremely helpful comments on an earlier version. I am also thankful for research and editorial assistance from Matthieu Teachout and Debarati Ghosh. Financial support to the Ford Foundation Inequality Project at Roosevelt Institute and Columbia University is gratefully acknowledged.

¹ Although it was not until the 1950s, with the work of Arrow and Debreu, that the efficiency of competitive markets was established (K J Arrow and G Debreu, ‘Existence of an Equilibrium for a Competitive Economy’ (1954) 22 *Econometrica* 290). An essential assumption was that every firm and household was a price taker, ie was so small that nothing that it did could affect market prices. In the real world, there are few instances in which this is true. Agriculture is one—but then there is massive government intervention, because markets on their own lead to high volatility in prices and farmers typically couldn’t manage the risks well on their own, and the economy, on its own, didn’t develop the institutions and markets to help individuals do so. And even in agriculture, there is heavy concentration in marketing. Some sectors are characterized by monopolistic competition—many firms, but still, each faces a downward sloping demand curve. (See E Chamberlain, *The Theory of Monopolistic Competition* (Harvard University Press 1933); A Dixit and J E Stiglitz, ‘Monopolistic Competition and Optimum Product Diversity’ (1977) 67(3) *American Economic Review* 308; J E Stiglitz, ‘Technological Change, Sunk Costs, and Competition’ (1987) 3 *Brookings Papers on Economic Activity* 947 (hereafter Stiglitz, ‘Technological Change’).) Antitrust typically has not taken an active role in such sectors.

² A Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (W Strahan and T Cadell 1776) (hereafter Smith, *The Wealth of Nations*).

This is even more the case for monopsony power, that is, when a firm has market power over its ‘suppliers’. This is especially so when a firm has market power in a labour market (eg in a company town). It is costly for workers to move, and thus a monopsonist can lower wages significantly below the competitive level without losing all or even a significant fraction of his workers.

Workers sometimes try to band together to provide some balance of power. Historically, employers have often countered through physical violence. When that is frowned upon, they turn to political action—to try to ban unions (as a ‘conspiracy in restraint of trade’).

Adam Smith talked about these efforts of workers for collective action, the attempt by employers to suppress such efforts, and how appropriate government regulation of the market—as we would put it today, *writing the right rules of the game in the right way*³—can improve matters:

Masters are always and everywhere in a sort of tacit, but constant and uniform, combination, not to raise the wages of labour above their actual rate . . . Masters, too, sometimes enter into particular combinations to sink the wages of labour even below this rate. These are always conducted with the utmost silence and secrecy.⁴

When workers combine, ‘the masters . . . never cease to call aloud for the assistance of the civil magistrate, and the rigorous execution of those laws which have been enacted with so much severity against the combination of servants, labourers, and journey-men’.⁵ ‘When the regulation, therefore, is in support of the workman, it is always just and equitable; but it is sometimes otherwise when in favour of the masters.’⁶

Thus, from the earliest days of capitalism, there has been a political battle over the rules of the game—with employers seeking to make it more difficult for workers to engage in collective bargaining/unionization, but with firms resisting efforts to restrain themselves and their anticompetitive behaviour.

All of this makes it clear that politics and economics cannot be separated. The early ‘trust-busters’ were concerned about the agglomeration of economic power; but they were also concerned about the associated agglomeration of political power. An agglomeration of economic power almost inevitably results in an agglomeration of political power—which can and typically does reinforce the agglomeration of economic power.

A. The Chicago School

In the United States (and elsewhere), courts have been captured by a particular view of the economy, sometimes referred to as the Chicago School (named after the University of Chicago, where many of its prominent members taught). The Chicago School postulates that markets are naturally competitive. In this view, there was in fact relatively little need for government to intervene to ensure competition. The

³ See J E Stiglitz (with N Abernathy, A Hersh, S Holmberg, and M Konczal), *Rewriting the Rules of the American Economy: An Agenda for Growth and Shared Prosperity* (W W Norton 2015).

⁴ Smith, *The Wealth of Nations* (n 3) ch 8.

⁵ *Ibid* ch 8.

⁶ *Ibid* ch 10 (emphasis added).

consequences of the Chicago School were broader: Competition policy shifted to a narrow economic focus, away from the broader societal consequences of concentrations of *power*. And within economics, doctrines that markets were naturally competitive and efficient meant a strong presumption that any observed behaviour, as strange as it might seem, was really efficiency enhancing and supportive of competition. The attractiveness of this shift from the perspective of the judiciary was perhaps understandable: They were given a well-defined question to examine. Was there evidence, in a particular market, of market power? Was there evidence that firms were acting in an anticompetitive way, unfairly using their market power?

Over time, as the influence of the Chicago School grew, so did the presumption that markets were competitive. Even when there was some evidence that there were actions which were anticompetitive, courts looked for offsetting efficiency-enhancing benefits.⁷ While in the United States, there was a 'rule of reason' in balancing the efficiency and anticompetitive effects, there increasingly developed a presumption that firms' actions are efficiency-enhancing. Similarly, in assessing whether a firm was engaged in predatory behaviour, there developed a presumption that it was not: After all, firms were rational, entry barriers were low, and so even if a firm was successful in driving out competitors, there would be new entrants. Thus, no rational firm would engage in selling below costs to drive out others; ergo, predation did not exist. Courts held this view even when there was overwhelming evidence that firms were engaged in loss-making activities in order to establish a more dominant position in the future.⁸

There was also the presumption that distribution does not matter. This presumption is reflected in the use of a total welfare standard, where adverse impacts on consumers could be set against positive benefits to the corporate sector.⁹ Such a perspective is particularly perverse both from an economic and moral point of view in South Africa and other emerging markets. Equally importantly, these perspectives are also increasingly out of sync with developments in modern economics.

B. Developments in modern economics

Modern economic theory (including advances associated with information asymmetries and game theory) has rejected all of the central tenets of Chicago School theory. In particular:

⁷ The competition framework of different countries has evolved differently. Not surprisingly, the Chicago School had less influence in many countries, such as South Africa and the European Union, than it did in the United States. Eleanor Fox notes that: 'The European Union competition law, for example, rejects the Chicago School free market assumptions and privileges openness of markets and access to them by firms without power.' See E Fox, 'The Efficiency Paradox' in R Pitofsky (ed), *How Chicago School Overshot the Mark: The Effect of Conservative Economic Analysis on US Antitrust* (Oxford University Press 2008); and E Fox, 'Monopolization and Abuse of Dominance: Why Europe Is Different' (2014) 59 *Antitrust Bulletin* 152.

⁸ Notice that even if firms did so *irrationally*, with the costs of predation exceeding the benefits, there can be significant anticompetitive effects, eg in discouraging entry.

⁹ As Eleanor Fox has pointed out, 'the US mantra IS that distribution does not matter, but perhaps surprisingly uses a consumer welfare standard and does not consider it distributive. The animus is against distribution to small business'.

- Even competitive markets are not, in general, efficient. As Greenwald and Stiglitz explain,¹⁰ Adam Smith's invisible hand is invisible because it is not there. This is true whenever there are imperfections of information and risk markets, or endogenous knowledge (innovation)—that is, always.
- Markets are not, in general, competitive: Even small deviations from *perfect* competition and *perfect information* matter.¹¹ Recent advances have shown that there is a wide range of mechanisms by which market power is acquired, maintained, and enhanced.
- Inequality matters. Recent studies¹² have shown that distribution does matter for economic performance. Moreover, the Second Welfare Theorem (suggesting that issues of efficiency and distribution can be separated, so that economics should only focus on efficiency) does not in general hold.¹³ In addition, there is increasing evidence that significant parts of inequality are a result of market power.¹⁴

The fact that there are so many instances of anticompetitive behaviour means that the key issue now is selectivity, identifying the most important abuses to prosecute.

II. New Presumptions

The most important implication of this new view is that it changes presumptions. Under the old presumptions, those challenging a seemingly anticompetitive practice had a heavy burden to show that it could not be or was not likely to be or might not be in reality efficiency-enhancing, in which case intervening in the natural workings of the market would lead to a decrease in welfare. Under the new view, there is a much stronger presumption that firms are engaged in some form of exploitive activity—trying to garner for themselves profits at the expense of rivals or consumers.

More successful firms, then, may not be those who are more able to produce products that consumers love and to do so at lower costs; but rather firms that are better

¹⁰ B Greenwald and J E Stiglitz, 'Externalities in Economics with Imperfect Information and Incomplete Markets' (1986) 101 *Quarterly Journal of Economics* 264.

¹¹ P A Diamond, 'A Model of Price Adjustment' (1971) 3(2) *Journal of Economic Theory* 168; M Rothschild and J E Stiglitz, 'Equilibrium in Competitive Insurance Markets: An Essay on the Economics of Imperfect Information' (1976) 90(4) *Quarterly Journal of Economics* 629; Stiglitz, 'Technological Change' (n 2).

¹² OECD, 'Focus on Inequality and Growth' (December 2014), available at <<http://www.oecd.org/social/Focus-Inequality-and-Growth-2014.pdf>> accessed 3 July 2017; J Ostry, A Berg, and C G Tsangarides, 'Redistribution, Inequality, and Growth', IMF Staff Discussion Note (February 2014), available at <<http://www.imf.org/external/pubs/ft/sdn/2014/sdn1402.pdf>> accessed 3 July 2017; J E Stiglitz, *The Price of Inequality: How Today's Divided Society Endangers Our Future* (W W Norton 2012).

¹³ See eg J E Stiglitz, 'Information and the Change in the Paradigm in Economics', abbreviated version of Nobel lecture, (2002) 92 *American Economic Review* 501.

¹⁴ See eg J Furman and P Orszag, 'A Firm-Level Perspective on the Role of Rents in the Rise in Inequality', October, presentation at 'A Just Society', Centennial Event in Honor of Joseph Stiglitz, forthcoming in *Festschrift* (Columbia University Press 2015).

able to create and exploit market power, including taking advantage of consumers. In this view, for instance, Microsoft¹⁵ may have been so successful only to a limited extent because of its technological innovations; more important were its business innovations, which created new barriers to entry and allowed it to entrench its power and fend off emerging competition that threatened its monopoly.¹⁶ Akerlof and Shiller¹⁷ describe the success of firms based on ‘phishing for phools’ and, elsewhere,¹⁸ I have described how globalization opened up a global market place of fools that American financial firms could exploit. This kind of ‘competition’ can be even more distorting than monopoly, because of the efforts/practices aimed at *increasing* market power, with consequences that go well beyond simply raising prices.¹⁹ The intent of these practices is to create entry barriers and to foreclose and reduce competition; the effect is often to stifle innovation and to enhance the ability of the monopolist to exploit its customers and suppliers.²⁰

Competition should be viewed as a process. Open competitive markets provide opportunity. The standard approach undervalues the value of freedom to participate in markets. It typically pays short shrift to the broader societal cost, by which the allegedly efficiency-inducing practices can tie up distribution and routes to market, creating entry barriers and reducing opportunity.

All of this implies that competition authorities should focus *not* just on mergers that reduce competition, or explicit agreements that lead to cartel or cartel-like behaviour or other plain vanilla antitrust violations, but rather on *any* conduct that is likely to prevent, lessen, or distort competition, for instance by: (a) facilitating raising prices (eg by changing elasticities of demand for those setting prices—eg vertical restraints);²¹ (b) creating entry barriers; or (c) raising rivals’ costs.²² Such conduct should be proscribed even if there *might* be some ‘public good’ justification. Use should be made of a public interest test, not just in mergers, but in conduct.

¹⁵ Remarkably, the court alleging that Microsoft used leverage in operating systems (OS) to get dominance in an applications market, browsers, failed. In the interest of full disclosure, I served as an expert witness against Microsoft in antitrust actions undertaken in the United States, Europe, Korea, and Canada.

¹⁶ See below for a brief description of some of these business practices.

¹⁷ G A Akerlof and R J Shiller, *Phishing for Phools: The Economics of Manipulation and Deception* (Princeton University Press 2015).

¹⁸ J E Stiglitz, *Freefall: America, Free Markets, and the Sinking of the Global Economy* (W W Norton 2010) (hereafter Stiglitz, *Freefall*).

¹⁹ See P Rey and J E Stiglitz, ‘Vertical Restraints and Producers’ Competition’ (1988) 32 *European Economic Review* 568 (hereafter Rey and Stiglitz, ‘Vertical Restraints’); P Rey and J E Stiglitz, ‘The Role of Exclusive Territories in Producers’ Competition’ (1995) 26 *Rand Journal of Economics* 451 (hereafter Rey and Stiglitz, ‘Exclusive Territories’).

²⁰ Indeed, Stiglitz showed that in the presence of imperfect information, the major market distortions associated with monopoly were those connected with enhancing its ability to extract rents out of its customers. See J E Stiglitz, ‘Monopoly, Non-Linear Pricing and Imperfect Information: The Insurance Market’ (1977) 44 *Review of Economic Studies* 430. Reprinted in *Selected Works of Joseph E. Stiglitz*, vol I: *Information and Economic Analysis* (Oxford University Press 2009).

²¹ Rey and Stiglitz, ‘Vertical Restraints’ (n 20); Rey and Stiglitz, ‘Exclusive Territories’ (n 20).

²² T G Krattenmaker and S C Salop, ‘Competition and Cooperation in the Market for Exclusionary Rights’ (1986) 76 *American Economic Review* 113; S C Salop and D T Scheffman, ‘Raising Rivals’ Costs’ (1983) 73 *American Economic Review* 271.

More generally, competition policy should be concerned not just with the *existence* of competition, but with the nature of competition. It should work to ensure a competitive market place with reasonable ease of entry. In reality, the market itself creates some barriers to entry (eg in access to credit or technology). Competition authorities should be concerned about any practice that augments these natural barriers, thus increasing the market power that would, in any case, exist. Moreover, there should be a simple test of whether there is market power—the ability to raise prices or lower wages or impose anticompetitive constraints.

III. New Issues Within More Standard Framework

Among the important abuses of market power today are several that are markedly different from those of the past.²³ In particular, there are several instances of monopoly power (eg Amazon, Walmart), where a common test for acceptable behaviour, whether consumers are advantaged, may fail to provide an accurate assessment of the consequences of the policy for societal well-being. In the short run, these monopolists may advantage consumers, driving down the prices they pay and passing on a fraction of those gains. Of course, these gains are at the expense of producers. The gains to consumers are less than the losses of producers. This is a general implication of the fact that market power is distorting, lowering societal welfare.

In the long run, matters may be even worse. Thus, as Amazon drove down what authors received, there was, in effect, a transfer of resources from the creators of intellectual property to the merchants. While intellectual property is designed to encourage such creative activity, the impact of Amazon has been just the opposite.

Network externalities also present a new set of issues. (In such networks, the benefits that one member of the network has from being in the network depend on who else is in the network. A phone network is valuable if and only if there are people on the network that I want to talk to.) Network externalities may arise in an increasingly large number of sectors, such as personal computer operating systems, airline reservation systems, and financial networks. When they exist, they generate new sources of market power, market power that is sustained and enhanced by contract restrictions, such as those that restrict the ability of those participating in the network to pass on charges imposed on them to end-users of the network. For instance, credit card companies charged merchants large fees (called interchange fees, typically 1 to 3 per cent of the value of the transactions), but did not allow merchants to pass on those charges to those who used the credit card—or even to tell their customers how much they were paying in interchange fees. Thus, credit card users had no incentives to use a more efficient payments mechanism. The abuse of this market power

²³ See Council of Economic Advisers, 'Benefits of Competition and Indicators of Market Power' (April 2016), available at <https://www.whitehouse.gov/sites/default/files/page/files/20160414_cea_competition_issue_brief.pdf> accessed 3 July 2017, for an insightful discussion of the increases in market power in the United States, the potential adverse effects, including on inequality, and the new issues confronting antitrust and antitrust enforcement in the United States.

has generated for banks and airline reservation systems billions of dollars in profits, led to inefficiency in choices (eg of payments mechanisms), and stifled innovation.

Of particular concern is the attempt by members of the Chicago School and others to defend the abuses of this market power by their usual argument that markets are naturally competitive and efficient, in this case using the theory of two-sided markets. In that theory, the network operator may lower the price of some participants in the network to induce more to participate, enhancing the value of the network to others. Credit and debit card companies use this argument to justify, for instance, the exorbitant charges imposed on merchants, even when there is no analysis of (a) whether there really exist network externalities on both sides of the market, and (b) whether these network externalities could possibly justify or explain the charges imposed. The contract restrictions are defended as efficiency-enhancing—although I have never seen a persuasive argument that this is so.²⁴

The increasing importance of network externalities, at least in certain industries, implies, to the contrary, that we should be increasingly concerned about abuses of market power: Firms will take advantage of the often inherent market power that results, attempting to amplify and extend its magnitude, durability, and scope.

There are other reasons that competition authorities should be increasingly on guard: As we move to a knowledge economy, fixed, sunk costs become relatively more important, and even small such costs can serve as a large barrier to entry, enabling an incumbent to sustain large profits without the threat of entry (in the knowledge that should there be entry, competition will drive down prices to the point where the entrant will lose money).²⁵ While it may be impossible to eradicate this natural barrier to entry, competition authorities should do what they can to make sure that incumbents do not amplify and extend their market power.

²⁴ In the interests of full disclosure: I have served as an expert witness in several cases (both credit card and airline reservation systems) where these issues have been litigated. For a court ruling that came down strongly with views consistent with those expressed here, see the case against American Express, where the US District Court ruled that the company violated antitrust laws (see <<https://www.justice.gov/opa/pr/us-district-court-rules-american-express-violated-antitrust-laws>> accessed 3 July 2017). The Appellate Court reversed the decision (see ‘DoJ Loses American Express Appeal on Multi-sided Grounds’, Global Competition Review, by Pallavi Guniganti, 27 September 2016), and as at the time of this writing, the Justice Department has not decided on its response. The Appellate Court’s decision showed clearly (in my judgment) the difficulties courts have in dealing with anticompetitive actions in the new digital economy. The court’s decision raised the bar for plaintiffs; if it is sustained, it will force them to address whether a market is a two-sided market, and if it is, to incorporate consumer benefit as an offset to producer harm. It did not itself address the key question of competition among platforms. Other ongoing cases in allegedly two-sided markets (including against American Express) were already addressing all three issues. There has also been a settlement in cases against Visa and Mastercard. In the United States, the Durbin Amendment to Dodd-Frank curtailed the abuses of debit card companies. European and Australian regulatory authorities have also taken actions attempting to limit the restrictive practices. Distributors have also often used similar contract restrictions to enhance their natural market power.

²⁵ See Stiglitz, ‘Technological Change’ (n 2); P Dasgupta and J E Stiglitz, ‘Potential Competition, Actual Competition and Economic Welfare’ (1988) 32 *European Economic Review* 569–77; J E Stiglitz and B Greenwald, *Creating a Learning Society: A New Approach to Growth, Development, and Social Progress* (Columbia University Press 2014).

Similarly, there is a worry that as we move to a service sector economy, many services are local in nature, with reputation for quality an especially important factor in choices. Imperfect information concerning quality can result in important barriers to competition. (More generally, we often underestimate the importance of the non-traded component in the goods we buy. Even if they are tradeable goods, they have to be delivered to the consumer and serviced; the fraction of the lifetime value added arising from these services as a fraction of the total expenditure on the product may be large.) It will be important to understand the ways in which firms in this sector maintain and enhance their market power, and to develop effective remedies.

A. New technique for exercising market power even when naturally acquired

Antitrust has focused on preventing the creation of market power through mergers and anticompetitive practices, and the abuse of market power, however created. But, as the contractual arrangements used by the airline reservation systems and the credit and debit card systems illustrate, there has been innovation in creating, maintaining, and enhancing market power. Moreover, antitrust authorities will have to be increasingly aware of and innovative in responding to these ‘innovations’. Microsoft’s use of Fear, Uncertainty, and Doubt (FUD), threats of lack of interoperability, and bundling of its browser with its operating system—effectively pricing the browser at zero—illustrate advances in anticompetitive practices. The market power created through the use of these anticompetitive practices has persisted,²⁶ presenting antitrust authorities with still another challenge—how best to reverse market power once created, especially when it has been created through anticompetitive practices.

These issues are likely to become even more important as we move to a knowledge-based economy, with intellectual property rights (IPR) playing an increasingly important role. IPR gives firms monopoly power over their knowledge, and changes in IPR have provided corporations with increasing market power. Still, as the example of Microsoft illustrates, even when firms legitimately acquire market power through IPR, they do not have free licence to abuse that market power through the use of anticompetitive practices.

Antitrust authorities should be sensitive to attempts by those in the corporate sector who amplify their market power through changes in our system of IPR. IPR is supposed to balance the dynamic benefits of innovation with the static costs of monopoly and restrictions in the use of knowledge.²⁷ In fact, many in the corporate sector are arguing for strengthening IPR in ways which cannot be defended in

²⁶ The court’s rulings on Microsoft’s rampant anticompetitive practices have been remarkably narrow. The Department of Justice did not win its FUD, bundling, or zero price/predatory pricing counts. The DoJ did not appeal the zero pricing loss in the District Court. It lost in the Appellate Court on the claim that bundling was per se illegal, and the DoJ opted not to retry that part of the case under a rule of reason.

²⁷ J E Stiglitz, ‘The Economic Foundations of Intellectual Property’ (2008) 57 *Duke Law Journal* 1693.

any appropriate balancing of the benefits of innovative incentives versus the costs of monopoly. An obvious example is the extension of the life of copyright. There is no evidence of any innovative benefit of recent extensions (to seventy years beyond the death of the author).

Historically, antitrust authorities have been sensitive to the power of patents to create, amplify, and increase the duration of market power. They forced AT&T to put its patents into a pool, accessible by others. One of the proposals put forward to curb Microsoft's monopoly power was to limit the life of its patents. It was argued that these actions not only increase competition, but also innovation.²⁸

The most egregious abuses perhaps occur in the drug industry, especially in trade agreements. For instance, Big Pharma has attempted to get provisions that allow it to 'evergreen' its patents and to advantage itself at the expense of generics—often obtaining benefits that it could not have obtained in open public debate. (Data exclusivity is an example of one of the mechanisms by which they have attempted to extend the effective life of their patents.) Some of the practices—such as paying off generic firms not to enter—have already been attacked by antitrust authorities; but again, the industry has shown enormous ingenuity in creating market power, often in subtle ways, again often with the assistance of trade ministries. The United States, for instance, has pushed for restrictions on the use of formularies, one way of encouraging competition among drugs with similar benefits. Even worse was the provision in the United States establishing a drug benefit for the elderly (called Medicare Part D), which restricted the ability of the US government to bargain with the drug companies over price. The voice of antitrust authorities needs to be heard more loudly in response to proposed provisions in trade agreements and public legislation.

B. New approaches to antitrust

Over the years, antitrust authorities have developed a set of approaches to establishing antitrust violations. Having such regular procedures provides clarity to firms and seemingly reduces the burden on the judiciary. Plaintiffs alleging an antitrust violation, for instance, have to define a market in which the firm engaged in the alleged market abuse has a critical share. The presumption is that in the absence of a large market share (in some relevant market), it would be impossible for any firm to engage in anticompetitive abuses.

But increasingly, it is being recognized that this standard approach may be inadequate for dealing with some of the important anticompetitive abuses today; for instance, when the relevant market is affected by market-imposed constraints. In the absence of these constraints, for instance, American Express, it might be argued, would not have market power in the credit card market; but with the anticompetitive constraints (eg that its merchants cannot use the price system, passing on some

²⁸ J Furman and J E Stiglitz, 'U.S. versus Microsoft, Declaration as Part of the Tunney Act Proceeding', commissioned by the Computer & Communications Industry Association (28 January 2002) (hereafter Furman and Stiglitz, 'U.S. versus Microsoft').

or all of the costs of different payment systems to its customers), it has enormous market power. That is, it has the ability to raise its price above the competitive level by a significant amount, with a small loss of usage. Indeed, even a firm with a very small market share (like Discover) has market power.²⁹

I would argue that the lesson of these recent examples is that the key issue is actually simpler than that entailed in the standard approach: It is simply whether the firm, with its contract restrictions, has the power to raise prices—and whether it has the power to effectively force firms to agree to anticompetitive contract provisions. The question then is how did it get that market power and is it sustainable. In some cases, that market power resulted from a simple contract restriction, which amplified some natural market power; the prohibition of that contract might, in such circumstances, significantly enhance competition in the market place.

IV. Broadening the Antitrust Agenda

We began this chapter by explaining how the antitrust agenda had been narrowed from a broader concern about *power* to a more narrow focus on certain ‘illegitimate’ ways of creating market power and certain abuses of market power, once obtained. In this section, I want to argue that rather than narrowing the remit of competition policy, we should be broadening it to reflect not only new risks associated with market power, but a broader realization of the limitations on the *natural* forces for competition and the broader uses to which competition policy may be put.

A. New risks associated with market power

There are in fact at least four *new risks associated with market power*, risks that were beyond anything conceivable to the progressives of the era in which antitrust legislation was first passed.

1. Using market power to induce individuals to give up rights of privacy

Some Internet firms provide small discounts to individuals who agree to turn over their data to the firm. It is not clear that the individuals in doing so fully recognize the risks to themselves. Besides, there are societal consequences that go beyond the individual: Putting broad databases together can result in those who control such data having power over individuals, and that power could be abused. There has long been a concern about government intrusion into privacy on precisely such grounds. However, any private sector firm having such data could sell or be forced to turn over

²⁹ The underlying theory is called the theory of insistence. The Appellate Court in the decision referred to in n 26 seems to have rejected the general theory of insistence, which had been supported by the District Court. This is likely to remain an unsettled area for years, unless legislation is passed to clarify that if a firm has the power to raise prices significantly without losing significant sales, it has market power.

that data to the government. While there is no sure way of preventing abuses, not allowing firms to bribe their customers into turning over their data may be helpful. In any case, the collection of such data can give the Internet firm a distinct advantage over rivals, and act as a barrier to entry. Thus, while what is at stake is more than the remit of standard competition authorities, there can be competition effects.³⁰

2. *Using market power to induce individuals to give up rights to use the public legal system for dispute resolution*

This is another example where firms with market power use that market power to enhance their market power; and/or firms are taking advantage of ill-informed consumers to get an advantage over their consumers. Firms with market power can exploit their customers, eg with switch and bait techniques or not performing as promised; but when the customer seeks redress, he is forced to use private arbitration.

Dispute adjudication is a basic public function. There are certain basic rights that individuals should not be able to give up, even for a price. The previous section illustrated one set, rights to privacy. It has long been recognized that an individual should not be allowed either to sell his vote or himself. So too, I believe, for the use of fair courts. By now, there is ample evidence on the lack of fairness of private arbitration.

3. *Too-big-to-fail banks*

These represent a quite different kind of risk of ‘bigness’ than those on which the trust-busters were focused. Too-big-to-fail banks have an incentive to engage in excessive risk taking because they know the government will rescue them. In fact, their plight gives them political power—and it was the abuse of political power with which the progressives were concerned. But the too-big-to-fail banks have proved their political power in another way: It has been virtually impossible to curb their power. As I pointed out,³¹ there was a rough political balance in the United States, between 350 million Americans and ten banks, such that some legislation curbing the worst excesses was passed, but clearly, far less than the vast majority of Americans thought was desirable or necessary.

4. *Inadequate competition in the market place of ideas*

The last illustrates well the limitations of current approaches, where the effect of media concentration is simply measured by market power in often narrowly defined advertising markets. Mergers across media (between television stations

³⁰ Of particular concern is that these Internet providers may already have market power; and they are using that market power to get agreements to transfer information to them, thus enhancing their market power. And this is especially of concern in societies where there is great inequality and large fractions of the population may not be well educated.

³¹ Stiglitz, *Freefall* (n 19).

and newspapers) leading to markedly reduced access to different views have been allowed to go forth, simply because there is competition in the ‘relevant’ market for advertising.

B. Competition policy can and should be broadened further

Until recently, the competitive equilibrium model was the benchmark model used by economists. It was argued, especially by economists from the Chicago School, that competition was the natural state towards which the economy tended, and deviations from this benchmark were limited. It was these limited deviations that were the subject of competition policy. Since the economy tended towards the competitive ideal on its own, only *unnatural* actions—like cartels—should be of concern. But today, there is a growing consensus that the real world entails extensive departures from this competitive benchmark model, with limitations of competition playing a key role in labour, capital, and most product markets. Indeed, there is a growing view that one cannot understand the functioning of most economies today without understanding these *pervasive* limitations in competition; a new benchmark model is emerging, one in which departures from competition are the norm rather than the exception. In this world, antitrust authorities seek not to restore the economy to some perfect competition ideal, but simply seek to prevent excessive and abusive concentrations of market power and the use of anticompetitive practices, particularly when they extend, augment, and deepen market power.

Within most countries, monopoly and monopsony power play an important role in explaining inequality; the growth in monopoly and monopsony power can play an important role in explaining the growth in inequality; and policies aimed at reducing market power can accordingly play some role in the reduction of inequality.³² The extent to which inequality reduction should be an *explicit* objective of competition policy remains a subject of debate.³³ However, in its very nature of checking abuses of power, competition policy is about reducing inequalities in some fundamental sense.³⁴

V. Globalization

The nature and intensity of competition depends on who is in the game. Many have argued with the growth of globalization, there are more firms competing in

³² J E Stiglitz, ‘New Theoretical Perspectives on the Distribution of Income and Wealth Among Individuals: Parts I–IV’, NBER Working Papers 21189–92 (May 2015); J E Stiglitz (with N Abernathy, A Hersh, S Holmberg, and M Konczal), *Rewriting the Rules of the American Economy: An Agenda for Growth and Shared Prosperity* (W W Norton May 2015), available at <<http://www.rewritetherules.org>> accessed 3 July 2017.

³³ See J B Baker and S C Salop, ‘Antitrust, Competition Policy, and Inequality’ mimeo (Georgetown University Law Center 2015).

³⁴ See also E Fox, ‘Making Markets Work for the People’, paper presented to BRICS Competition Conference, Durban (November 2015), published in proceedings in 2016.

any marketplace, and, therefore, there is a stronger presumption in favour of competition (that is, that markets are in fact competitive, so long as trade barriers are kept low). Earlier, we explained that, in fact, even in the case of traded goods, there is often a large non-tradable component, associated with delivery and servicing. Hence, local market power can still matter.

Developing countries face an inherent and historic asymmetry of power. There is a broad philosophical issue: What does 'fair' competition mean, in the context of a developing and emerging market, where small local firms have to compete with foreign behemoths? Is it fair to limit oneself to ensuring that the behemoth does not engage in certain exclusionary practices? Is it true that even some of its competitive advantage arises out of monopsony power in some third market (as described earlier)?

New approaches to development focus on 'helping infant economies grow',³⁵ recognizing the externalities generated by new firms and industries, eg in the manufacturing sector, which in turn imply that a 'free' market solution will not lead to (adequate) development. This provides a legitimate argument for protection—tilting the balance towards domestic firms by, for instance, maintaining a stable, real competitive exchange rate. But it is also an argument for more aggressive enforcement for antitrust. Antitrust policy, like any other policy arena, entails a balancing act, the risks of under and over enforcement. How that balance should play out depends on the circumstances of each individual country.

Thus, just like there should not be a single intellectual property regime for all countries,³⁶ there should not be a single competition policy for all countries. Just as there should be a development-oriented trade regime and a development-oriented intellectual property regime, there should be a developmentally oriented competition regime and antitrust policy.

This is especially so because colonialism and imperialism were based on an asymmetry of political power; and the colonial/imperial countries used that power to entrench themselves economically and to disempower and exploit the countries that they subjugated. In economics, there are often large hysteresis effects: Power, once established, extends and amplifies itself.

The ex-colonial powers were not content to rely simply on market forces to extend and amplify their market power. They embedded within the rules governing the post-colonial era measures that helped perpetuate these imbalances. Thus, escalating tariffs within the World Trade Organization (WTO) rules-based system had the effect of leaving the developing countries to continue exporting low value-added raw materials, and ensuring that the higher value-added activities occurred in the more developed countries.³⁷

³⁵ B Greenwald and J E Stiglitz, 'Helping Infant Economies Grow: Foundations of Trade Policies for Developing Countries' (2006) 96 *American Economic Review* 141 (hereafter Greenwald and Stiglitz, 'Helping Infant Economies Grow'); Stiglitz and Greenwald, *Creating a Learning Society* (n 25).

³⁶ J E Stiglitz, *Making Globalization Work* (W W Norton 2006) and references cited therein; and M Cimoli, D Dosi, K E Maskus et al, *Intellectual Property Rights: Legal and Economic Challenges for Development* (Oxford University Press 2014).

³⁷ See A Charlton and J E Stiglitz, *Fair Trade for All* (Oxford University Press 2005).

Competition policy has an important role to play in *undoing* these historical legacies, enhancing the ability of developing and emerging countries to compete and promote development more broadly.

In international trade agreements—ironically, sometimes under the guise of provisions labelled ‘competition’—developed countries, including both the United States and those in the European Union, have attempted to restrict the ability of developing countries to compete. For instance, they have argued that domestic content regulations are anticompetitive. In other fora, at the International Monetary Fund (IMF) and the World Bank, the advanced countries have discouraged developing countries from using industrial policies (including active exchange rate management) to become more competitive, in spite of the theory and evidence that such policies, when well managed, can be very effective.³⁸ Without industrial policy supporting the development of capabilities and learning by doing and helping firms overcome barriers to entry (such as finance), countries will have low levels of domestic rivalry. Under such circumstances, trade opening can increase the disadvantages of domestic firms and thus decrease effective competition.

The fact that the elimination of *formal* trade barriers does not create a level playing field has finally been recognized in the aid-for-trade movement. Without aid for trade, removing tariffs and other ‘artificial’ trade barriers actually disadvantages developing countries. But the earlier literature on aid-for-trade did not recognize its full implications for the extent of competition within the country.³⁹

At the same time, domestic policies need to be wary of supporting national champions. Dominant firms in many developing countries try to use the ‘national champion’ argument to give them freedom to suppress competition at home and use and abuse their market power.

VI. Market Power, Inequality, and Development

While market power has long been front and centre in competition policy, recent advances have, as we have noted, provided new arguments for the importance of attacking it. It leads to inequality, and inequality leads to poorer economic performance, including lower growth and more instability.

³⁸ See eg Greenwald and Stiglitz, ‘Helping Infant Economies Grow’; and Stiglitz and Greenwald, *Creating a Learning Society* (n 25). More recently, the World Bank has changed its position, and has been actively promoting industrial policies. See J E Stiglitz and Y V Lin, *The Industrial Policy Revolution I: The Role of Government beyond Ideology* (Palgrave Macmillan 2014); and J Y Lin, ‘Industrial Policy Revisited: A New Structural Economics Perspective’ (2014) 22(HS01) *Revue d’économie du développement* 70.

³⁹ See A Charlton and J E Stiglitz, ‘Aid for Trade’ (2006) 5 *International Journal of Development Issues* 41; A Charlton and J E Stiglitz, ‘Aid for Trade’, Keynote Address, *Annual World Bank Conference on Development Economics 2007*, in F Bourguignon and B Pleskovic (eds), *Rethinking Infrastructure for Development* (World Bank 2008); A Charlton and J E Stiglitz, ‘The Right to Trade: Rethinking the Aid for Trade Agenda’ in Mohammad A Razzaque and Dirk Willem te Velde (eds), *Assessing Aid for Trade: Effectiveness, Current Issues and Future Directions* (Commonwealth Secretariat 2013) 386.

Market power is often associated with creating barriers to entry, and inequality means fewer people have resources to enter markets.

These problems can be particularly serious when foreign firms have market power. For them the resulting profits mean that resources are redistributed out of country—depriving the country of needed foreign exchange and undermining demand for domestic non-traded goods, making it more difficult for the country to achieve a competitive market in these goods (including more difficult to achieve economies of scale).

VII. Broadening the Menu of Possible Antitrust Policies

Earlier sections of this chapter have emphasized the importance of broadening the scope of competition policy from the narrow remit to which the Chicago School attempted to condemn it. This section argues that there is, in fact, a broad menu of antitrust policies that competition authorities should employ.⁴⁰

Earlier, we referred to the ‘public interest test’. Within that, there can and should be explicit reference to some of the concerns raised in this chapter: inequality, development, and the marketplace for ideas. We also referred to the necessity of changing *presumptions*.

Of course, those who are engaged in anticompetitive practices, or who believe that markets are naturally competitive, have worked to weaken antitrust enforcement. Therefore, there is a need to increase and focus agency enforcement, with increased antitrust agency budgets. There should be prosecutorial discretion to prioritize cases that benefit less advantaged consumers and to design remedies to benefit less advantaged consumers.⁴¹

Moreover, under the influence of ‘Chicago economics’, there has been a hesitancy to take strong actions. This is seen most clearly in the Microsoft case, where the initial actions failed even to curtail the company from engaging in anticompetitive practices, and subsequent actions did little to curtail the market power that had already been established. There is a need for a rebalance towards more interventionist

⁴⁰ This section has benefitted particularly from Baker and Salop (n 33). A refrain of much of my policy work in development over the past twenty years has been that there was a need for ‘broader goals, more instruments’ than had been suggested by the Washington Consensus, itself largely based on neo-liberal/Chicago School economic perspectives. See J E Stiglitz, ‘More Instruments and Broader Goals: Moving Toward the Post-Washington Consensus’ in G Kochendorfer-Lucius and B Pleskovic (eds), *Development Issues in the 21st Century* (German Foundation for International Development 1999) 11–39; J E Stiglitz, ‘The Economics behind Law in a Market Economy: Alternatives to the Neoliberal Orthodoxy’ in J E Stiglitz and D Kennedy (eds), *Law and Economic Development with Chinese Characteristics: Institutions for the 21st Century* (Oxford University Press 2013a); J E Stiglitz, ‘Creating the Institutional Foundations for a Market Economy’ in *ibid*; J E Stiglitz, ‘The State, the Market, and Development’, WIDER Working Paper 1/2016 (February 2016), originally presented at a conference celebrating WIDER’s 30th anniversary (18 September 2015); and various chapters in *ibid* for a discussion of the relationship between Chicago School economics and the evolution of doctrines related to law and economics.

⁴¹ Thus, under current US law, the Federal Trade Commission (FTC) could conclude that monopoly pricing or price discrimination targeting less advantaged consumers violates the FTC Act.

antitrust and regulatory actions and standards. For instance, one of the proposed actions in the Microsoft case was to limit the term of its intellectual property. While such an action would have both stimulated innovation and curbed market power, this and similarly strong actions were rejected.⁴²

Another example of how antitrust authorities could take stronger actions to promote competition is recognizing excessive pricing by dominant firms as an antitrust offence. EU Competition Law recognizes excessive pricing by a dominant firm as an abuse of dominance (as exploitative conduct). However, there have been very few cases.⁴³ The US Sherman Act is narrower. A monopolist with legitimately obtained and maintained monopoly power is permitted to charge high prices. A ‘conduct element’ is required, such as an agreement or an act of exclusion. (Interestingly, the United States sets prices through antitrust in at least one area—rates for music publishing rights.) The US and other competition authorities could and should adopt the EU approach.⁴⁴

Any jurisdiction will, of course, worry about the dangers and costs of under- versus over-enforcement. But in setting the rules, account should be taken of economies’ different characteristics and histories. Because of sunk costs, history matters. But when that history is coloured by colonialism and oppression, that history cannot be ignored. There is an obligation on competition authorities to take a more proactive stance in rectifying these imbalances.

Among the differences in circumstances facing different economies is size: Smaller economies may face greater problems of entrenched dominant firms. By the same token, natural entry barriers at earlier stages of development imply greater costs associated with exclusionary behaviour, with effects that may be more persistent, outweighing risks of a ‘chilling effect’ of stronger antitrust enforcement.

I would argue that there is a broad role of government to actively encourage competition, recognizing that competition does not simply and naturally arise in the absence of cartels, contrary to the Chicago School presumptions noted earlier. The industrial policies referred to earlier are one important instrument for encouraging entry and competition. A *public option* is another relevant one, at least for some sectors, where the government provides an alternative to the private sector, thereby checking the extent to which it can engage in exploitation. Therefore, the public option in health insurance in the United States might have played an important role in breaking anticompetitive behaviours that were hard to prosecute under existing laws. A public option in annuities might have led to more competitive insurance markets; and the public option in student loans has led to access at a more competitive rate. A public option in the market for conventional mortgages would almost surely bring down the cost of borrowing.

Competition authorities should recognize too that strong competition policy encourages entry. Microsoft’s predatory actions have almost surely had a chilling

⁴² See Furman and Stiglitz, ‘U.S. versus Microsoft’ (n 29).

⁴³ Somewhat disturbing, my understanding is that a recent decision by the Competition Appeal Court in South Africa may make a finding of excessive pricing difficult.

⁴⁴ To implement this standard in the United States, legislation would be needed.

effect on entry in that sector; had there been more confidence that antitrust authorities would have taken actions against those actions, there might have been more entry.

A. Competition and public interest

Earlier, I argued that public interest should be the overriding concern of competition policy. However, this broad mandate may be difficult to incorporate easily within a rules-based competition framework, and the burden imposed on competition policy must take into account the existence of other instruments.

One principle, though, seems clear: Mandates on domestic firms (like lending to underserved communities or participation of historically disadvantage persons) should be imposed on foreign firms, even if it is more difficult for them to fulfil such a mandate. No country should sign trade or investment agreements that make this difficult or impossible.

VIII. Global Perspectives

Competition (when firms are active across borders) is a global public good. As in so many areas within global economics, there is a need for more global cooperation. Globalization implies that what happens in one jurisdiction has effects on those living in others. There is a need for collective action—which is not the same thing as saying that there is the need for the same rules, and especially if those rules are written by the developed countries.

There should be cooperation in international enforcement—in the arena of mergers and cartels, as well as conduct.⁴⁵ The hypocrisy of almost studiously ignoring export cartels (like oil and potash)—which the international community has done—needs to be addressed.

What is clear, though, is that there is a need for a broader regulatory environment for multinationals, including taxation.⁴⁶ Competition policy should be seen as part of establishing this broader global cooperative framework.

Unfortunately, competition policy is increasingly seen as a weapon of national economic policy. Moreover, there are economic as well as political reasons for being easier on domestic firms that engage in anticompetitive practices. Some of the profits they glean are at the expense of citizens and firms in foreign countries. Their exclusionary practices may benefit domestic employment at the expense of foreign employment; and some of the increased profits will rebound to the benefit of the government.

⁴⁵ This does not, however, mean that there should be the same policies in all countries, as noted earlier.

⁴⁶ The failure of the UN conference on Finance for Development (in Addis Abba, July 2015) to establish even the beginnings of such a framework within the United Nations highlights the difficulties. The advanced countries are used to making the rules by themselves, for the benefit of themselves.

Thus, it is perhaps not a surprise that the United States is now accusing Europe of unfairly using competition policy against American firms. The US government is more susceptible to pressure from US firms, and it may well be that the US government sees not only political but economic benefits arising from the success of American firms, even if that success is partially based on anticompetitive practices (or practices of avoiding taxes within Europe). Conversely, Europe worries that companies like Google and Facebook will not only open up the possibility of the misuse of the information that they are gathering, eg by some governmental body, but that these firms will also use their privileged access to information to entrench themselves.

A. BRICS cooperation

Cooperation among BRICS can be an important step in creating that global framework. These countries are working together to understand better and create 'a developmentally oriented competition regime', one of the objectives of which is promoting 'inclusive growth'.

This developmentally oriented competition regime must be based on the recognition that many of the central economic doctrines that have dominated Western competition policy have been discredited, or at least have more limited reach than previously realized.

Cooperation among the BRICS competition authorities can be helpful in sharing insights, and perhaps with more explicit cooperation, in ensuring more competition in areas where in the past competition has been limited.

Implementing this broader agenda that I have laid out here will not be easy. On the contrary, non-implementation of this broader agenda risks losing important opportunities for promoting inclusive development.

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA,)

Plaintiff,)

v.)

AT&T INC., *et al.*,)

Defendants.)

Civil Case No. 17-2511 (RJL)

FILED

JUN 12 2018

Clerk, U.S. District & Bankruptcy
Courts for the District of Columbia


MEMORANDUM OPINION

(June 12, 2018)

If there ever were an antitrust case where the parties had a dramatically different assessment of the current state of the relevant market and a fundamentally different vision of its future development, this is the one. Small wonder it had to go to trial!

On November 20, 2017, the U.S. Department of Justice's Antitrust Division brought this suit, on behalf of the United States of America ("the Government" or "the plaintiff"), to block the merger of AT&T Inc. ("AT&T") and Time Warner Inc. ("Time Warner") as a violation of Section 7 of the Clayton Act, 15 U.S.C. § 18. The Government claims, in essence, that permitting AT&T to acquire Time Warner is likely to substantially lessen competition in the video programming and distribution market nationwide by enabling AT&T to use Time Warner's "must have" television content to either raise its rivals' video programming costs or, by way of a "blackout," drive those same rivals' customers to its subsidiary, DirecTV. Thus, according to the Government, consumers nationwide will be harmed by increased prices for access to Turner networks, notwithstanding the

Government's concession that this vertical merger would result in hundreds of millions of dollars in annual cost savings to AT&T's customers and notwithstanding the fact that (unlike in "horizontal" mergers) no competitor will be eliminated by the merger's proposed vertical integration.

Not surprisingly, the defendants, AT&T, Time Warner, and DirecTV, strongly disagree. Their vision couldn't be more different. The video programming and distribution market, they point out, has been, and is, in the middle of a revolution where high-speed internet access has facilitated a "veritable explosion" of new, innovative video content and advertising offerings over the past five years. Trial Tr. ("Tr.") 1397:1-4 (Montemagno (Charter)). Vertically integrated entities like Netflix, Hulu, and Amazon have achieved remarkable success in creating and providing affordable, on-demand video content directly to viewers over the internet. Meanwhile, web giants Facebook and Google have developed new ways to use data to create effective – and lucrative – digital advertisements tailored to the individual consumer.

As a result of these "tectonic changes" brought on by the proliferation of high-speed internet access, video programmers such as Time Warner and video distributors such as AT&T find themselves facing two stark realities: declining video subscriptions and flatlining television advertising revenues. *Id.* at 3079:18 (Bewkes (Time Warner)). Indeed, cost-conscious consumers increasingly choose to "cut" or "shave" the cord, abandoning their traditional cable- or satellite- TV packages for cheaper content alternatives available over the internet. At the same time, Facebook's and Google's dominant digital advertising platforms have surpassed television advertising in revenue. Watching vertically integrated,

data-informed entities thrive as television subscriptions and advertising revenues declined, AT&T and Time Warner concluded that each had a problem that the other could solve: Time Warner could provide AT&T with the ability to experiment with and develop innovative video content and advertising offerings for AT&T's many video and wireless customers, and AT&T could afford Time Warner access to customer relationships and valuable data about its programming. Together, AT&T and Time Warner concluded that both companies could stop "chasing taillights" and catch up with the competition. 2/16/18 Hr'g Tr. 34:16 [Dkt # 67]. Those were the circumstances that drove AT&T, a distributor of content, and Time Warner, a content creator and programmer, to announce their historic \$108 billion merger in October 2016 (the "proposed merger" or "challenged merger"). Those are the circumstances that cause them to claim today that their merger will increase not only innovation, but competition in this marketplace for years to come.

Section 7 of the Clayton Act assigns this Court the "uncertain task" of weighing the parties' competing visions of the future of the relevant market and the challenged merger's place within it. *United States v. Baker Hughes Inc.*, 908 F.2d 981, 991 (D.C. Cir. 1990). Nothing less than a comprehensive inquiry into future competitive conditions in that market is expected. And the Government has the burden of proof to demonstrate that the merger is likely to lessen competition substantially in that uncertain future.

Since announcing the transaction in late October 2016, defendants have delayed closing on the merger agreement for about 18 months as a result of the Government's investigation and suit. The deal is now set to expire if not consummated on or before June 21, 2018 – a turn of events that would require AT&T to pay Time Warner a "break-up fee"

of \$500 million. The parties have engaged in a highly accelerated discovery schedule to prepare themselves to try this case in March and April of this year. The trial itself lasted nearly six weeks. Both sides put on a case-in-chief and the Government put on a rebuttal case as well. At the conclusion of the trial, I advised the parties I would issue a ruling, if not an opinion, no later than June 12, 2018 so that the losing side would have the agreed-upon time remaining to pursue its appellate rights *before* the merger or the \$500 million break-up fee went into effect.

The following is the Court's Opinion. Initially, I provide context for this suit by reviewing the background of the video programming and distribution industry, the proposed merger, and the procedural history of this case. Thereafter, I discuss the legal standards governing a suit under Section 7 of the Clayton Act, emphasizing in particular the considerations at play in evaluating vertical mergers. With that in place, I next analyze each of the Government's three theories of harm to competition, balancing, as appropriate, the conceded proconsumer benefits of the merger with the consumer harms alleged and the evidence offered to support them. Ultimately, I conclude that the Government has failed to meet its burden to establish that the proposed "transaction is likely to lessen competition substantially." *Baker Hughes*, 908 F.2d at 985.

As such, based on that conclusion, and for all the reasons set forth in greater detail in this Opinion, the Court **DENIES** the Government's request to enjoin the proposed merger.

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BACKGROUND

I. The Video Programming and Distribution Industry¹

The structure of the video programming and distribution industry generally resembles the “three-stage chain of production comprised of manufacturers, wholesalers, and retailers that typifies the distribution of many, if not most, physical goods in the U.S. economy.” Christopher S. Yoo, *Vertical Integration and Media Regulation in the New Economy*, 19 Yale J. Reg. 171, 220 (2002). Here, that three-stage chain of production and distribution involves “content creation, content aggregation, and content distribution.” Proposed Findings of Fact of the United States (“Gov’t PFOF”) ¶ 8 [Dkt. # 128].²

Television content begins at the manufacturing level. Although video programming is often created by studios (such as Time Warner’s Warner Bros.), some networks or distributors “produce content for themselves” or, in the case of live sporting events, license the rights to broadcast the events from the various sports leagues. *See* Tr. 80:12-16 (Fenwick (Cox)). At the second level, programmers (such as Time Warner’s Turner or Home Box Office (“HBO”)) aggregate content into a network or network group and then

¹ For consistency throughout this Opinion, I will use the phrase “video programming and distribution industry” to include creation, packaging, and distribution of professionally produced video content. Of particular relevance here, the Court’s definition of “video programming and distribution industry” encompasses programmers such as Turner; traditional multichannel video programming distributors (“MVPDs”) such as cable and satellite companies; virtual multichannel video programming distributors (“virtual MVPDs” or “vMVPDs”) such as DirecTV Now and DISH’s Sling; and subscription video on demand services (“SVODs”) such as Netflix, Hulu, and Amazon Prime. By contrast, I use the phrase “pay-TV” to refer only to the packaging and delivery of linear – or “live” – television content. That phrase encompasses only MVPDs and virtual MVPDs.

² Many materials before the Court contain confidential business information or other proprietary data; such submissions were typically filed under seal with an accompanying redacted version accessible to the public. The Court has made great effort to refrain from quoting or otherwise including confidential business information in this Opinion, opting instead to refer generally to the exhibits or information filed under seal.

license those networks to video distributors, like AT&T's DirecTV. *See, e.g., id.* at 80:4-9; Plaintiff's Exhibit ("PX") 456-4 to 10. At the third level, distributors bundle and distribute networks to their subscribers. Tr. 80:4-9 (Fenwick (Cox)).

Some subscription-based video programming services are "vertically integrated," meaning, in this context, that those services create or aggregate their content offerings and then distribute those offerings directly to consumers. *Id.* at 3081:18-25 (Bewkes (Time Warner)); *see* Defs.' Proposed Findings of Fact ("Defs.' PFOF") ¶ 12 [Dkt. # 120]. Examples of those services include Netflix, Hulu, and Amazon Prime. Tr. 3155:22-23 (Bewkes (Time Warner)). Traditional video programmers, such as Turner, generally lack such "soup to nuts" integration of content creation and distribution; they are instead reliant upon video distributors to deliver their content offerings to consumers. *Id.* at 3388:6-7 (Stephenson (AT&T)); *see id.* at 485:1-486:6, 612:17-20 (Martin (Turner)). Because the Government's claims center on the proposed combination of Time Warner's video programming with AT&T's video distribution, my background review focuses on those facets of the video programming and distribution industry.

A. Video Programing and Distribution

1. Programmers

Traditional programmers, such as Turner, acquire and aggregate video content. *Id.* at 80:4-16 (Fenwick (Cox)). Generally, programmers do not offer their content directly to consumers. *See, e.g., id.* at 485:1-486:6, 612:1-20 (Martin (Turner)). Instead, they package video content into networks – in Turner's case, networks such as TNT, TBS, and CNN – and then license the rights to display those networks to video distributors. PX459-18; Tr.

80:6-9 (Fenwick (Cox)). As such, Turner and its programming competitors may be thought of as content “wholesaler[s]” in that they are typically reliant upon third-party video distributors to get their offerings to consumers in the downstream market. Tr. 612:3-4, 17-20 (Martin (Turner)).

Most programmers make money in two primary ways, and Turner is no exception. *First*, programmers receive payments from distributors, known as “affiliate fees,” in exchange for granting distributors the rights to display the programmers’ content. *See, e.g., id.* at 604:21-23, 610:20-23. Affiliate fees are memorialized in affiliate agreements, which specify the “net effective rate” a programmer charges for a network on a per-subscriber, per-month basis. *Id.* at 987:5-17 (Breland (Turner)). Rates typically increase year-over-year, pursuant to what are called “escalator” clauses. *Id.* at 91:6-10 (Fenwick (Cox)); *id.* at 2728:19-23 (Katz). Affiliate fees have been “going up” over the past decade industrywide, due at least in part to rising costs of making “higher quality” content. Tr. 2562:9-2563:25 (Carlton); *cf. id.* at 1495:12-16 (Sutton (HBO)) (“So the cost it takes to make shows, shows like the shows we make, has escalated significantly.”). Affiliate fees vary, however, based on the size of the distributor; specifically, in order to incentivize and reward wide distribution, programmers typically provide distributors with “volume discounts” on affiliate fees, meaning that the more subscribers a distributor has, the more a programmer’s net effective rates will decline. *See, e.g., id.* at 987:25-988:13 (Breland (Turner)) (explaining variance in rates between “small,” “medium,” and “large” MVPDs and virtual MVPDs); *id.* at 2911:21-23 (Holanda (RCN)) (describing “volume discounts” of larger distributors); PX127-2 (showing rate differentials).

Second, and as any television viewer can attest, programmers sell advertising slots on their networks to advertisers. *See* Tr. 3179:23-3181:6 (Bewkes (Time Warner)). For decades, television advertising has followed the same playbook. *See id.* at 3086:9-10. During each hour of television, there are roughly eighteen minutes of advertisements. *See id.* at 609:23-610:4 (Martin (Turner)). Distributors sell advertisements for only two of those minutes; the programmer sells ads for the remaining sixteen minutes. *See id.* Advertising fees vary by the channel and the time of day an ad airs. *Id.* at 625:4-11. As with affiliate fees, the broader a program's audience, the more advertising revenue for Turner: as Chairman and CEO John Martin explained with regard to Turner's advertising strategy, "our goal is to have our networks in front of as many eyeballs as possible." *Id.* at 605:7-8.

The classic model of television advertising is limited in two ways. First, in deciding the placement of commercials to be seen by a wide audience, programmers generally must rely on general demographic data, such as age range, about the typical audience for a given program. *See id.* at 625:4-6. Second, and as a result, programmers have no choice but to saturate all viewers of a program with the same, undifferentiated ads – despite knowing that the selected ad will be of little interest to some number of those viewers. *See id.* at 3087:1-8 (Bewkes (Time Warner)).

In the past, Turner's total revenues have been split roughly equally between affiliate fee revenues and advertising revenues. *See id.* at 3088:10-12; PX456-8. For present purposes, however, the key point is this: both the affiliate fee and advertising revenue streams depend upon broad distribution of programmers' networks to consumers. *See, e.g.,*

Tr. 604:17-18 (Martin (Turner)) (“I believe that distribution is the most important variable for success for any programmer.”); *id.* at 3078:17-20 (Bewkes (Time Warner)) (“Q: What are the key drivers of the Turner business? A: Well, the Turner business, first, we need to get it on every distribution platform so that we can have subscriber fees and advertising revenues.”). For that reason, Turner executives aim to “achieve wide distribution” of their networks. Post-Trial Brief of the United States (“Gov’t Post-Tr. Br.”) 6 [Dkt. # 126]; *see also, e.g.*, Tr. 3120:3-7 (Bewkes (Time Warner)); (“So we try everything to stay on all of our channels, Turner, HBO, everything, to keep them on there. And that’s very important to us. If they’re not on there, we’re not only losing the subscriber fees; we’re losing the advertising revenues.”); *cf. id.* at 90:1-2 (Fenwick (Cox)) (“We are dealing with network groups where their goal [is] a hundred percent distribution.”).

2. Distributors

Today, there are three categories of key players in the distribution of professionally produced video content: (1) “traditional” multichannel video programming distributors (“MVPDs”); (2) “virtual” MVPDs; and (3) subscription video on demand services (“SVODs”). *See* Tr. 485:1-487:13 (Martin (Turner)); Gov’t PFOF ¶¶ 9, 14, 19.

First, there are traditional MVPDs. Those distributors include direct broadcast satellite providers, such as DISH or AT&T’s DirecTV; cable television providers, such as Comcast,³ Charter Communications (“Charter”), or Cox Communications (“Cox”);

³ In 2009, Comcast announced its intent to acquire ownership of NBCUniversal (“NBCU”), a media and entertainment company that owns the NBC and Telemundo networks as well as Universal Pictures and Universal Studios. *See* Compl. ¶¶ 16-17, *United States v. Comcast Corp.*, 808 F. Supp. 2d 145 (D.D.C. 2011) (No. 11-cv-106) [Dkt. # 1]. Although the Government, through the Antitrust Division, filed an action

“overbuilders,” such as RCN; or “telcos,” such as AT&T’s U-verse or Verizon Fios. *See* Gov’t PFOF ¶¶ 9, 43-45; Defs.’ PFOF ¶ 34. All of those services offer live – or “linear” – television content as well as libraries of licensed content available for viewing on demand, typically in exchange for a monthly subscription fee. *See* Tr. 81:1-82:8 (Fenwick (Cox)); *id.* at 471:12-16, 638:16-22 (Martin (Turner)); *id.* at 1185:22-1186:1 (Warren (Turner)). Satellite distributors such as DirecTV and DISH operate nationally, whereas cable companies, telcos, and overbuilders distribute video content regionally; in any given local area, however, the incumbent cable operator is typically the dominant MVPD. *See id.* at 408:1-3 (Schlichting (DISH)). Consumers’ choices of traditional MVPDs are therefore dictated by geography. *See id.* at 2187:3-23 (Shapiro); Gov’t PFOF ¶¶ 43-46. Consumers often subscribe to traditional MVPDs as part of a “bundle” of various services, which may include, for example, a single price offering for cable, wireless internet, and home or mobile phone services. *See* Tr. 2784:21-25 (Rossi). Of the approximately 90 million

claiming that the transaction would violate Section 7 of the Clayton Act – an action, as fortune would have it, also assigned to this Court – the Government also urged me to approve the transaction pursuant to a final judgment containing various “remedies” that it represented would “diminish[] Comcast’s ability to use [NBCU’s] programming to harm competition.” Competitive Impact Statement 3, 7, *Comcast Corp.*, 808 F. Supp. 2d 145 [Dkt. # 4]. Those remedies related to procedures set forth in a related FCC order governing the transaction, including, as especially relevant here, requirements that Comcast-NBCU: 1) submit to “baseball style arbitration,” at the distributor’s option, in the event the parties were unable to reach a carriage agreement, 7/27/11 Hr’g Tr. 7:4-7 [Dkt. # 38], and 2) “continue to provide” video programming to the distributor “pursuant to the terms of any existing agreement until the arbitration is completed,” Competitive Impact Statement Ex. A, at 24, *Comcast Corp.*, 808 F. Supp. 2d 145 [Dkt. # 4-1]. At a hearing to discuss the proposed final judgment, counsel for the Government asserted that, “especially in cases of vertical mergers, conduct remedies” such as the ones proposed “can be a very useful tool to address the competitive problems while preserving competition and allowing efficiencies” that “may result from the transaction.” 7/27/11 Hr’g Tr. 15:16-21. Ultimately, I approved the Government’s proposed final judgment with a few modifications to allow me to better monitor the implementation of the remedies imposed as part of the judgment. *See generally Comcast Corp.*, 808 F. Supp. 2d 145. The transaction proceeded and today Comcast-NBCU operates as a “vertically integrated” programmer and distributor. *See* Tr. 882:14-16 (Rigdon (Comcast)).

American households that still receive television content from providers in the pay-TV industry, a substantial majority do so through traditional MVPDs. *See* Gov't PFOF ¶¶ 9, 13. That number is steadily declining, however, as consumers shift towards lower-cost virtual MVPDs or SVODs. *See* Tr. 3450:7-14 (Stephenson (AT&T)); *id.* at 3157:5-13 (Bewkes (Time Warner)).

Second, there are virtual MVPDs, which began to arrive in the marketplace in early 2015. *See id.* at 235:18-22 (Schlichting (DISH)). Like traditional MVPDs, virtual MVPDs distribute linear channels and on-demand content to subscribers for a subscription fee; unlike traditional MVPDs, virtual MVPDs offer their services over the internet, rather than through proprietary infrastructure such as satellite networks or cable lines. Gov't PFOF ¶¶ 14, 15. Because they offer their services over the internet, virtual MVPDs offer service nationwide, either via the web or mobile apps. *See* PX8-18. Examples of virtual MVPDs include DirecTV Now, DISH's Sling, Sony's Playstation Vue, Hulu Live, Google's YouTube TV, FuboTV, and Philo. *See id.* at 18-19; Defs.' PFOF ¶ 8. As their names suggest, some virtual MVPDs are associated with companies that operate traditional MVPDs. Each virtual MVPD competes with traditional MVPDs for subscribers and, increasingly, virtual MVPDs are gaining market share on traditional MVPDs due in part to their ease of use and lower-cost offerings. *See, e.g.,* Tr. 448:24-449:2 (Schlichting (DISH)); *id.* at 607:17-20 (Martin (Turner)); *id.* at 1829:3-12 (Merrill (AT&T)). Therefore, despite their relatively recent vintage, virtual MVPDs already have millions of subscribers. *See id.* at 2019:20-2020:18 (Bond (NBCU)).

Third, there are SVODs, a category that includes Netflix, Hulu, and Amazon Prime. SVODs generally do not offer live, linear programming such as live sporting events or live news. *See id.* at 487:1-16 (Martin (Turner)). Instead, they have large libraries of original and acquired content, accessible by a viewer on demand at any time. *See id.* at 486:12-17. The leading SVODs are vertically integrated and invest *billions* of dollars in creating original programming. *See id.* at 3081:13-25 (Bewkes (Time Warner)); *id.* at 3388:8-9 (Stephenson (AT&T)). By way of example, Netflix *alone* spends more on content than all of Time Warner. *See id.* at 2456:13-14 (Carlton); *see also id.* at 1053:2-7 (Breland (Turner)) (Netflix will spend “almost \$8 billion” on content “[t]his year”). As with virtual MVPDs, SVODs offer low-cost subscription plans as compared to traditional MVPDs and continue to gain market share in the video programming and distribution industry. Indeed, while traditional MVPDs are losing subscribers at a steady clip, Netflix added 2 million subscribers in the last quarter alone. *See id.* at 3450:11-12 (Stephenson (AT&T)).

3. Affiliate Negotiations and “Blackouts”

As previously discussed, the schemes under which programmers extend licensing rights to MVPDs and virtual MVPDs are governed by detailed contracts known as affiliate agreements. *See* PX456-8; Tr. 80:4-9 (Fenwick (Cox)); *id.* at 485:1-486:6 (Martin (Turner)). Those agreements describe the precise rights granted by the programmer, and contain numerous terms and conditions. *See, e.g.*, PX409. Although the “rate” or payment amount is an important feature of any affiliate agreement, Tr. 90:5-10 (Fenwick (Cox)), “these deals are complicated” and “start with a hundred plus open issues,” *id.* at 459:24-25. (Schlichting (DISH)); *see also id.* at 1690:23-25 (York (AT&T)) (“There’s literally

hundreds of items that go on kind of a priority list on what's the right deal.”). Those issues can include digital rights, “windows” (*i.e.*, limitations on when certain content can be aired), “TV Everywhere” rights (*i.e.*, the rights for subscribers to access content away from home on an authorized device), volume discounts, and penetration rate requirements, among others. *See, e.g., id.* at 90:5-14, 101:19-23 (Fenwick (Cox)); Gov’t PFOF ¶¶ 11, 105; PX409-14. At least in the case of Turner, affiliate agreements also include most-favored-nation (“MFN”) clauses, which generally require the programmer to extend to the distributor certain types of terms given to another distributor. *See* Tr. 1024:6-14 (Breland (Turner)) (describing MFNs). Affiliate agreements run “between five and eight years on average.” *Id.* at 87:9-11 (Fenwick (Cox)).

Because wide distribution maximizes programmers’ two income streams – affiliate fees and advertising revenue – programmers like Turner bargain for terms aimed at promoting that distribution. To start, Turner seeks to license “every network” it owns. *Id.* at 606:6-8 (Martin (Turner)).⁴ In addition, Turner negotiates for guarantees of particular “penetration rates” – the percentage of a given distributor’s subscribers who receive a given channel. *Id.* at 1023:10-16 (Breland (Turner)).

Given the duration of the contract and the rights at issue, a single affiliate agreement can dictate the transfer of upwards of a billion dollars between programmer and distributor.

⁴ That said, in the case of DISH’s virtual MVPD, Sling, Turner did license only its “core” networks – CNN, TBS, TNT, and Cartoon Network. *See* Tr. 236:23-24 (Schlichting (DISH)). As Time Warner CEO Jeff Bewkes testified, because 85 to 90% of Turner’s revenue comes from four networks, Turner is well situated to offer skinnier bundles. *See id.* at 3126:22-3127:3 (Bewkes (Time Warner)); *see also id.* at 584:18-24 (Martin (Turner)) (same). By contrast, NBCU’s revenues are spread more evenly across its more than one-dozen networks. *See id.* at 3127:6 (Bewkes (Time Warner)).

See, e.g., PX144-21, 48. It is thus no surprise that witnesses described affiliate agreement negotiations as “very tough” and “intense and aggressive.” Tr. 1022:25-1023:2 (Breland (Turner)); *id.* at 3251:24-25 (Stankey (AT&T)); *see also* Gov’t PFOF ¶ 104. Although the negotiations themselves typically last several months, closing a deal often “come[s] down to the last day and sometimes the last handful of minutes.” Tr. 1093:14-16 (Breland (Turner)); *see also id.* at 87:14-19 (Fenwick (Cox)). Negotiations involving programmers with multiple networks, such as Turner, are particularly “time consuming.” *Id.* at 87:17 (Fenwick (Cox)).

Affiliate negotiations are also idiosyncratic, varying from programmer to programmer and distributor to distributor. The Government’s chief economic expert, Professor Carl Shapiro, recognized as much at trial. Noting that “bargaining is a dark art in many ways,” Professor Shapiro acknowledged that negotiations may turn on myriad “unpredictable factors,” including the “personalities” at the table and other “hairy stuff.” *Id.* at 2213:12, 2294:18-2295:6 (Shapiro). This dynamic flows from the “multitude” of considerations that inform each negotiation. *Id.* at 1690:15 (York (AT&T)). With so many factors and priorities, and with such high stakes, it should be no surprise that terms and conditions vary across affiliate agreements. *See, e.g., id.* at 1681:16-17 (“[W]e do hundreds of deals, and we have hundreds of flavors of most favored nations.”). In short, as Professor Shapiro explained, “the real world is messy and it’s imperfect.” *Id.* at 2210:22-23 (Shapiro).

Sometimes, negotiations between programmers and distributors reach an impasse. If a negotiation is ultimately unsuccessful, the distributor will lose the rights to display the

programmer's content to its customers – a situation known in the industry as a programming “blackout,” or “going dark.” *See id.* at 129:4-9 (Fenwick (Cox)). Blackouts have negative consequences for programmers and distributors alike. On the programming side, a blackout causes a programmer to suffer immediate (and unrecoverable) losses of both advertising and affiliate fee revenue. *See, e.g., id.* at 1094:21-1096:18 (Breland (Turner)). On the distributor side, a blackout may lead a distributor to lose subscribers or may prevent the distributor from attracting new subscribers. *See* Gov't PFOF ¶ 119; *see also, e.g., id.* at 864:12-23 (Rigdon (Comcast)); *id.* at 1348:3-7 (Montemagno (Charter)) (discussing PX373). Because blackouts are almost always negative events for both programmers and distributors, “at the end of the day . . . [t]here's no benefit for anyone to walk away” without an affiliate agreement. *Tr.* 89:23-90:4 (Fenwick (Cox)). Therefore, bargains between programmers and distributors are almost always struck in order to avoid long-term blackouts. *See id.* at 138:13-15; *id.* at 1027:4-7 (Breland (Turner)); *id.* at 1359:14-15 (Montemagno (Charter)); *id.* at 3124:4-7 (Bewkes (Time Warner)).

That is not to say, however, that blackouts are irrelevant to the negotiating dynamic. Rather, in what can best be thought of as an elaborate and stylized Kabuki dance, the evidence shows that “almost every negotiation” involves both programmers and distributors threatening blackouts, especially when one side is seen as demanding terms that are out of line with the market. *Id.* at 1026:17-20 (Breland (Turner)); *cf. id.* at 376:22-377:11 (Schlichting (DISH)). To better understand how to assign the “right value” to a particular deal, programmers and distributors might perform “drop” or “go dark” analyses to estimate the potential impact of a blackout on the programmer's advertising or affiliate

fee revenues or on the distributor's customer base. *Id.* at 1343:11-16 (Montemagno (Charter)); *see also id.* at 1348:3-10 (discussing PX373); *id.* at 862:19-863:3 (Rigdon (Comcast)); *id.* at 1029:10-1030:11 (Breland (Turner)) (discussing PX144).

Nevertheless, given the negative consequences for both sides from a blackout, "the reality" is that "virtually every" bargaining impasse between a programmer and distributor "is resolved after requiring either no blackout or a short-term blackout." *Id.* at 2396:1-5 (Shapiro). Indeed, in recent memory, Turner networks have been blacked out only twice, both for roughly one-month periods. *See id.* at 2357:15-23; Defs.' PFOF ¶¶ 139-143. Permanent blackouts, the evidence shows, are a vanishingly rare occurrence; the record indicates that Turner has *never* engaged in a long-term blackout with a distributor. *See Tr.* 2394:8-11 (Shapiro) (acknowledging that "in the real world there has never been a permanent blackout of the Turner networks").

B. Industry Trends

In recent years, traditional programmers, including Turner, and MVPDs, including DirecTV, have been faced with a number of interrelated industry trends that are particularly relevant to the challenged merger. I will review three of those trends in turn.

1. Rise and Innovation of Over-the-Top, Vertically Integrated Video Content Services

Traditional programmers and distributors are experiencing increased competition from innovative, over-the-top content services, including virtual MVPDs and SVODs. *See infra* p. 24 n.5. Those web-based companies are harnessing the power of the internet and data to provide lower-cost, better-tailored programming content directly to consumers. The

dramatic growth of the leading SVODs in particular, including Netflix, Hulu, and Amazon Prime, can be traced in part to the value conferred by vertical integration – that is, to having content creation and aggregation as well as content distribution under the same roof. *See, e.g.,* Tr. 3080:8-3085:21 (Bewkes (Time Warner)).

As relevant to the video programming and distribution market, vertical integration provides two notable advantages to content services. First, vertical integration reduces the “bargaining friction” inherent in the arm’s-length affiliate negotiations that govern the exchange of rights between traditional programmers and distributors. *See, e.g., id.* at 3104:18-3107:13; *id.* at 1684:25-1685:13 (York (AT&T)). As numerous witnesses discussed, bargaining friction refers to the difficulty inherent in assigning value to and negotiating over new, innovative content rights, like “TV Everywhere,” download rights, and “4K” high resolution. *See id.* at 1685:22-1686:7, 1688:6-13 (York (AT&T)); *id.* at 3104:18-25 (Bewkes (Time Warner)); *id.* at 3222:4-3223:2 (Stankey (AT&T)). AT&T executive Daniel York testified, for example, that DirecTV has attempted, with limited success (and considerable delay), to obtain such rights from programmers through arm’s length-negotiations. *See id.* at 1685:24-1686:22 (York (AT&T)). RCN CEO Jim Holanda joined York in discussing the way in which bargaining friction hindered RCN’s negotiations over TV Everywhere rights. *See id.* at 2968:25-2971:14 (Holanda (RCN)). Further, DirecTV Now’s affiliate agreements require it to restrict the number of viewers who can stream or access programs simultaneously on its platform. *See id.* at 1687:10-14 (York (AT&T)). And when DirecTV floated the concept of “DirecTV mobile” – a pay-TV subscription exclusively for mobile devices – that was “dead on arrival.” *Id.* at

1687:15-25. By contrast, with control over the creation and use of large amounts of original content, SVODs have driven much of the recent innovation in the video programming and distribution industry. *See id.* at 1685:7-13; *id.* at 639:1-8 (Martin (Turner)). These companies have, for example, developed download rights, allowing users to view their content anywhere without wireless access. *See id.* at 1688:16-18 (York (AT&T)).

Second, and relatedly, SVODs' ability to distribute their content directly to consumers over the internet gives them superior access to customer data. SVODs are able to use that customer data to inform their strategy and improve the customer's experience in a number of ways. *See id.* at 3081:21-25 (Bewkes (Time Warner)); *see also id.* at 3388:6-3389:8 (Stephenson (AT&T)). SVODs can use data about viewing habits to determine what programs are popular, and create more of that type of content. *See id.* at 2452:21-2453:3 (Carlton); *id.* at 3245:16-20 (Stankey (AT&T)). In addition, data informs marketing decisions, and allows SVODs to recommend content to users based on their revealed preferences, *i.e.*, the shows they have watched in the past. *See id.* at 3080:19-3081:12 (Bewkes (Time Warner)). Even more, data can inform scheduling choices, and enhance efforts at recapturing consumers who disconnect. *See id.* at 3245:16-20 (Stankey (AT&T)); *id.* at 3081:4-12 (Bewkes (Time Warner)). Finally, and as discussed in more detail below, to the extent SVODs incorporate advertising into their platforms, data allows those ads to be more targeted and thus more lucrative.

2. Declining MVPD Subscriptions Resulting from an Increasingly Competitive Industry Landscape

At trial, witness after witness acknowledged that MVPD subscriptions are on the decline. *See, e.g., id.* at 633:5-15 (Martin (Turner)); *id.* at 891:18-22 (Rigdon (Comcast)); 2229:21-22 (Shapiro); 3369:13-16 (Stankey (AT&T)); *id.* at 3450:15-3451:1 (Stephenson (AT&T)); *see also* PX63-36. Those declines “started faster” than many in the industry anticipated. Tr. 3369:13-16 (Stankey (AT&T)) (discussing the “inflection change” where the “decline of the traditional pay-TV bundle started faster than [AT&T] assumed”). To illustrate, in 2016 AT&T’s traditional MVPDs lost 133,000 customers; last year, DirecTV *alone* lost 1.2 million subscribers. *See id.* at 3004:6-8 (Christopher (AT&T)); *id.* at 3450:7-9 (Stephenson (AT&T)).

The decline in traditional MVPD subscriptions is just one symptom of the increasingly competitive nature of the video programming and distribution industry. Indeed, several witnesses testified that competition in the industry is more intense today than ever before. *See, e.g., id.* at 1398:24-25 (Montemagno (Charter)) (video distribution business is “more competitive now than I’ve ever experienced in my career”); *id.* at 2134:1-3 (Sejen (Cable ONE)) (“Q: In your 31 years in the industry, have you ever seen it more competitive at the distribution level? A: No.”); *id.* at 2950:2-6 (Holanda (RCN)) (“Q: And so in the course of this 30 years that you have been in the business, the video distribution market today is more competitive than at any point that you can recall, true? A: True.”); *id.* at 3213:9 (Stankey (AT&T)) (competition in industry is “at an all-time high”); *id.* at

2476:1-9 (Carlton) (“new entrants” in market such as “Netflix” are “making the market more competitive”).

More specifically, the decline of traditional MVPD subscriptions reflects the growing popularity of virtual MVPDs and SVODs. *See, e.g.*, PX153-3. On that score, two rising trends are worth noting: cord-cutting and cord-shaving. A household “cuts the cord” when it discontinues MVPD services altogether, whether traditional or virtual MVPDs. *See id.* at 605:23-606:4 (Martin (Turner)); *id.* at 2505:10-20 (Carlton). As Professor Carlton relayed, SNL Kagan estimates that roughly twenty percent of American households have cut the cord, discontinuing traditional MVPD services. *Id.* at 2505:12-20. This number, high as it is, continues to grow. *See id.* at 2466:4-10; *see also id.* at 891:18-22 (Rigdon (Comcast)); *cf. id.* at 2948:20-2949:3 (Holanda (RCN)). That said, those households have not exited the entertainment field altogether. *See id.* at 3450:2-6, 12-14 (Stephenson (AT&T)). Instead, many have gravitated to vertically integrated SVODs. *See* PX153-3; *see also* Tr. 3449:12-24, 3450:7-12 (Stephenson (AT&T)). Consumers, particularly young people, find SVODs attractive, with their improved user interfaces, premium content, and lower price points. *See, e.g.*, Tr. 639:1-8 (Martin (Turner)); *id.* at 3449:12-18 (Stankey (AT&T)). On a similar note, a household “shaves the cord” when it departs a traditional MVPD for one of the many virtual MVPDs, which, again, typically carry smaller bundles of networks at lower price points. Gov’t PFOF ¶ 16; Defs.’ PFOF ¶ 21. Many other consumers have shaved the cord, reducing, but not eliminating, their consumption of MVPD services. *See, e.g.*, Tr. 606:2-4 (Martin (Turner)). Consumers intent on shaving the cord have an increasing array of virtual MVPD services

from which to choose – services that operate nationwide over the internet. *See id.* at 2949:15-18 (Holanda (RCN)). Consumers may choose to subscribe to a less expensive, “skinny bundle,” *i.e.*, one with fewer networks, and then supplement that bundle with subscriptions to SVODs like Netflix and Hulu. *Cf. id.* at 2984:13-20 (SEALED); *id.* at 3506:24-3507:2 (Stephenson (AT&T)).

Of course, when a household departs a traditional MVPD, whether for an SVOD or a virtual MVPD, that subscriber loss affects the traditional MVPD in the form of lost margins on subscription fees. *See, e.g.*, PX456-56; Tr. 3450:7-14 (Stephenson (AT&T)); *id.* at 2219:13-21 (Shapiro). Such losses may also affect programmers in the form of declining affiliate fee revenues as well as stagnating or declining viewership. *See, e.g., id.* at 3088:22-3089:1 (Bewkes (Time Warner)) (SVODs and other new competitors are “bleeding away our viewers”); PX153-3. Turner, for example, projects that its domestic subscription revenue growth will decrease to low single digits in each year from 2018 to 2022. *See* Tr. 647:3-11 (Martin (Turner)) (discussing Defendants’ Exhibit (“DX”) 781-21). Increased competition from SVODs also means that more original, high-quality programming is being produced – a trend that increases the costs of securing the talent and rights necessary to make such programming. *See id.* at 1494:15-21, 1495:12-16 (Sutton (HBO)) (“There was a time when very few people were making the kind of shows we make. Now, it seems that almost every week, there’s an announcement of somebody else making it. . . . [A]s I’ve mentioned, Netflix; Hulu makes shows and so does Prime Video. . . . So the cost it takes to make shows, shows like the shows we make, has escalated significantly” because “more people are bidding for the talent involved.”); PX153-6; *cf.*

Tr. 633:16-18 (Martin (Turner)) (“[T]he number of professionally produced television shows in the United States has doubled in the last five years alone.”).⁵

It is therefore no surprise that programmers and distributors alike have noted the competitive threat posed by SVODs. After all, as Nobel laureate Bob Dylan correctly observed: “You don’t need a weatherman to know which way the wind blows.” *Subterranean Homesick Blues*. At trial, numerous witnesses from defendants testified that SVODs present a broad-range of competitive challenges. *See, e.g.*, Tr. 3088:22-3089:25 (Bewkes (Time Warner)) (over-the-top companies are “bleeding away our viewers, because they’re offering competitive video that has these advantages, because they know what to put in front of you individually, and we don’t”); *id.* at 3213:3-9, 3214:8-10 (Stankey (AT&T)) (“The time-and-attention competition now from the likes of Facebook, from the likes of Google, from the likes of Netflix I started asking myself, what should the business do to respond to the changing environment that we’ve heard about in this courtroom, the dawn of these new services coming from the likes [of] Netflix and Google?”). Third-party witnesses from AT&T’s competitor distributors also testified to the role of SVODs in the increasingly competitive industry landscape. *See id.* at 860:24-861:9 (Rigdon (Comcast)) (“[A]n SVOD service like in Netflix provides a wide array of entertainment choices. So people have limited time in the day. So where they’re going to

⁵ Although the Government asserts that “consumers of Multichannel Video Distribution are largely insensitive to price changes” as reflected by their continued payment of increased subscription costs, Gov’t PFOF ¶ 35, at trial there was near-uniform testimony that “consumers are up to here with subscription prices” and that “it’s getting harder and harder” for distributors to pass their increased costs along, Tr. 3089:6-11 (Bewkes (Time Warner)); *id.* at 3446:1-4 (Stephenson (AT&T)). That consumers are at a “gag point” when it comes to traditional MVPD subscription costs is further illustrated by the continued *decline* in subscriptions nationally. *Id.* at 140:13-15 (Fenwick (Cox)); *id.* at 3450:7-9 (Stephenson (AT&T)).

spend their time for entertainment in that respect Netflix competes with traditional TV providers.”); *id.* at 1395:12-21 (Montemagno (Charter)) (Charter’s competitors include “the Googles and the Amazons and the Netflix”); *see also* DX921-35 (DISH “face[s] significant competition” from other companies, including, among others, “Netflix, Hulu, Apple, Amazon, Alphabet . . .”).⁶

3. Shift Toward Targeted, Digital Advertising

Finally, and again as a result of the rising influence of innovative, web-based competitors, the advertising landscape has shifted away from reliance on television advertising offered by programmers to highly-targeted digital advertising. *See* Tr. 3088:3-6 (Bewkes (Time Warner)) (noting that advertisers are shifting their “ad budgets, which

⁶ In the face of all that, the Government continues to insist that SVODs are merely “complement[s]” or “adjunct[s]” to traditional MVPDs, rather than competitors of traditional MVPDs; a few of the Government’s third-party competitor witnesses testified to the same. Gov’t PFOF ¶ 36. I agree with defendants that the Government’s arguments (and the corresponding witness testimony) on that score defy reality, as demonstrated by the evidence adduced at trial. The evidence clearly showed that the leading SVODs – as vertically-integrated entities that produce and distribute their own award-winning content – fiercely compete *both* with programmers such as Turner and HBO *and* with traditional MVPDs and virtual MVPDs. Indeed, industry data reflects that large percentages of MVPD customers have chosen to “cut the cord” and receive content exclusively from SVODs. *See supra* pp. 22-24.

To be sure, the Government contends that, notwithstanding the increasing prevalence of SVODs, “[e]ven programmers believe MVPDs are likely to remain highly profitable in the future.” Gov’t PFOF ¶ 13. That proposition rests on a document from May 2016. *Id.* (citing PX78). As the Court learned at trial, however, the industry has undergone significant changes since mid-2016, diminishing the persuasiveness of that statement and others like it. To take just one example, video programming margins are declining, a fact that presents an obvious threat to future MVPD profitability. Tr. 3853:18-19 (Shapiro) (“I think it is not disputed that the video margins are going down.”). And while the Court accepts that traditional MVPDs continue to have a substantial subscriber base, and indeed may currently constitute a distinct submarket, *see infra* pp. 61-66, it is inescapable that SVODs have played a large role in causing the demand for and continued purchase of traditional MVPD subscriptions to “declin[e] at a rapid pace.” Tr. 3450:7-3451:1 (Stephenson (AT&T)). To ignore those industry trends – trends that are transforming how consumers view video content and blurring the lines between programming, distribution, and web-based competitors – would be to ignore the Supreme Court’s direction to examine this case with an eye toward the “structure, history, and probable future” of this fast-changing industry. *United States v. Gen. Dynamics Corp.*, 415 U.S. 486, 498 (1974) (internal quotation marks omitted). I, of course, cannot do that !

are finite, to the digital platforms at Google and Facebook” and “away from television advertising in general”); PX456-56 (“The advantages of digital advertising . . . have resulted in advertisers shifting more of their advertising budgets from traditional television advertising to digital advertising.”). The share of U.S. spending on digital advertising exceeded spending on television advertising in 2016. *See* DX746A-2; Tr. 3092:15-19 (Bewkes (Time Warner)). Digital advertising revenue is expected to further eclipse television advertising revenue in the coming years. *See* Tr. 3092:22-3093:1 (Bewkes (Time Warner)).

Why the rush from television ads to digital ones? Simply put, digital ads are more efficient. Through their access to and use of consumer data, Google and Facebook are better able to discern the purchasing preferences and interests of individuals viewing particular online content. *See id. at* 623:2-13 (Martin (Turner)); *id. at* 3087:16-3088:2 (Bewkes (Time Warner)); *id. at* 3243:5-10 (Stankey (AT&T)). They can use that information to infer what types of ads would most interest those users. *See id. at* 3087:16-3088:2 (Bewkes (Time Warner)). And they can tailor digital advertisements to those users based on those preferences. *See id. at* 623:8-13 (Martin (Turner)). Best of all from an advertiser’s perspective, Google, Facebook, and other entities engaged in digital advertising have confirmatory data that demonstrates whether particular ads were effective. *See id. at* 623:14-22.

Although traditional programmers like Turner maintain “massive inventories of advertising,” they lack the type of fine-grained data necessary to generate targeted ads. *Id. at* 3392:10-13 (Stephenson (AT&T)). Under the “spray and pray” approach, programmers

instead sell ads based on “broad demographic data” about the viewers of a particular program. *Id.* at 3760:20-24 (Athey). As a result, consumers regularly see ads for things that do not interest them, and advertisers pay to show ads that they know will be ineffective in motivating many in the audience. *See id.* at 3087:1-8 (Bewkes (Time Warner)). As Turner CEO John Martin put it, “there’s been a long saying in the advertising industry where the advertiser would always say, I know I’m wasting half of my money, I just don’t know which half.” *Id.* at 685:20-23 (Martin (Turner)).

The shift toward digital advertising has been extremely profitable for the tech giants – Google and Facebook, in particular. Indeed, those two entities account for roughly 60% of U.S. digital advertising. *See id.* at 3746:16-22 (Athey). And they are growing at a rapid pace: Google’s advertising revenue has “almost tripl[ed]” between 2012 and 2017, while Facebook’s advertising revenue went from \$4 to \$40 billion in the same period. *Id.* at 3097:2-11 (Bewkes (Time Warner)) (discussing DXD122).

By contrast, the rise of digital advertising has been costly to Turner and other programmers that rely on television advertising as a major source of revenue. *See id.* at 3088:3-21; *cf.* PX456-25. In 2017, for example, Turner’s advertising revenue *declined* by 2% relative to the previous year. *See* Defs.’ PFOF ¶ 31 (citing PX456-65); Tr. 3097:14-20 (Bewkes (Time Warner)). In light of the dual-revenue-stream business model of programmers, witnesses testified that declines in television advertising revenue will produce a predictable result: it will place more pressure on affiliate fees, meaning that programmers will increase the fees charged for their content. *See, e.g.,* Tr. 3088:16-21 (Bewkes (Time Warner)). For that reason, Jeff Bewkes, CEO of Time Warner, explained

that the explosion of digital advertising is “actually bad for” video distribution consumers, “because it means that the financial support for all this programming on all these different channels gets pushed over toward subscription prices. And that’s a problem, because we think consumers are up to here with subscription prices.” *Id.* at 3089:6-11.

II. The Parties and Proposed Merger

A. AT&T

AT&T is a “leading provider of communications and digital entertainment services in the United States and the world.” PX455-7. As a distribution company, AT&T is in what its Chairman and CEO Randall Stephenson calls “the connectivity business.” Tr. 3378:23-24 (Stephenson (AT&T)). Although originally known for its “voice telephone” service, AT&T also provides wireless service, broadband service, and pay-TV service to consumers. *See id.* at 3377:23-25, 3379:12-15. AT&T, however, does not create any significant television or movie content. *See id.* at 3245:24-25 (Stankey (AT&T)).

AT&T has two traditional MVPD products: DirecTV and U-verse. Defs.’ PFOF ¶ 34. DirecTV, acquired by AT&T in 2015, is a “satellite-based MVPD service that operates by transmitting programming from satellites to rooftop dishes installed at the customers’ homes.” *Id.*; *see* Tr. 3206:21-22, 3207:21-23 (Stankey (AT&T)); PX455-11 to 12. U-verse, by contrast, is a “telco” MVPD service that operates “[o]ver the same line that [] deliver[s] your telephone service.” *Id.* at 3384:1-2 (Stephenson (AT&T)); Defs.’ PFOF ¶ 34. Between DirecTV and U-verse, AT&T has approximately 25 million video distribution subscribers today, making it the largest provider of traditional MVPD services. *See* PX455-11; Tr. 3384:13-14 (Stephenson (AT&T)).

Despite that substantial traditional MVPD subscriber base, AT&T witnesses testified that they believe the company's future lies in the use of online and mobile wireless connections to access premium video. As John Stankey, the AT&T executive who will be tasked with running Time Warner should the merger proceed, explained, AT&T acquired DirecTV in 2015 not in an effort to double down on the satellite business – a concededly mature and indeed declining asset – but to “pick up a lot of new customers that we could work on migrating” to new, innovative products necessary to compete in the future. Tr. 3207:18-3208:2, 3209:4-7 (Stankey (AT&T)). In late 2016, AT&T launched one such product, DirecTV Now. *See, e.g., id.* at 1824:23-24 (Merrill). DirecTV Now is a virtual MVPD and, as such, carries fewer channels than DirecTV or other traditional MVPDs; is offered at a lower price-point; and is delivered over the internet. *See id.* at 1825:1-3; *id.* at 3385:5-3386:10 (Stephenson (AT&T)). Today, and in large part due to significant promotional efforts and high-level support for the product's launch, DirecTV Now has grown to more than one million subscribers. *See id.* at 3386:2-3 (Stephenson (AT&T)); *id.* at 1825:12-1826:8, 1827:18-1828:2 (Merrill (AT&T)).

AT&T Chairman and CEO Randall Stephenson testified that DirecTV Now plays to AT&T's strong suit, namely its 100-million plus wireless subscriber base. *See id.* at 3379:19-20, 3385:9-14 (Stephenson (AT&T)). With customers increasingly turning to cell phone and mobile devices to access video content, fully “[h]alf of the volume on [AT&T's] network is video.” *Id.* at 3382:5-6. Stankey noted that AT&T welcomes this trend, as it results in users purchasing larger data plans and acquiring more devices. *See id.* at 3254:15-22 (Stankey (AT&T)). AT&T's next major initiative, fifth generation or “5G”

wireless, is calculated to increase video consumption even more. *See id.* at 3383:3-14 (Stephenson (AT&T)). As Stephenson explained to the Court, “[w]hat we’re all working towards is creating [\$]35 and \$15 bundles. And that’s where the world is moving” *Id.* at 3506:23-25. To that end, Stephenson continued, AT&T has plans to launch a new product called AT&T Watch, through which customers will be able to receive “real skinny bundle[s]” of programming for \$15 per month or, in the case of “AT&T wireless unlimited customer[s], . . . for free.” *Id.* at 3434:12-3435:4.

B. Time Warner

Time Warner, by contrast, is in the entertainment business. It has three distinct units: Warner Bros., Turner, and HBO. *See* PX459-18 (Turner), -22 (HBO), -24 (Warner Bros.). Turner operates, among other things, ten linear cable networks that televise scheduled video programming around the clock. *See id.* at 18; Defs.’ PFOF ¶ 7.⁷ HBO is a premium, subscription-based video service that offers movie and television shows, including a significant amount of original content. *See* PX459-22. Unlike Turner, which collects both programming fees and advertising revenue, HBO relies solely on subscription payments to operate. *See id.* at 23; PX456-67; *compare* Tr. 604:21-23 (Martin (Turner)), *with id.* at 1450:12-17, 1493:15-17 (Sutton (HBO)). Warner Bros. operates a studio that creates movies, television programs, and other kinds of video content that are licensed both to Time Warner’s other businesses and to third parties. *See* PX459-24.

⁷ Those networks are TNT, TBS, CNN, CNN Español, CNN International, Cartoon Network/Adult Swim, TruTV, TCM, Boomerang, and HLN. *See* Defs.’ PFOF ¶ 7.

The Government's claims in this case implicate Turner and HBO. Those business units are therefore discussed in more detail below.

1. Turner Networks

The Turner networks are central to the Government's primary theory of harm, and thus warrant the greatest attention here. Turner's business model is simple: distribute its content as broadly as possible in order to maximize the dual income streams of affiliate fees and advertising revenue. *See* Tr. 3078:17-20 (Bewkes (Time Warner)). Historically, Turner has relied on unaffiliated third parties to distribute its content to consumers. *See id.* at 485:1-18, 612:3-4 (Martin (Turner)). Those include traditional MVPDs, such as cable companies and satellite companies. *See id.* at 485:1-18. In recent years, Turner has distributed its content to consumers through virtual MVPDs as well. *See id.* at 485:19-486:6; Gov't Post-Tr. Br. 6.

Industry participants view Turner content as popular and valuable, primarily for Turner's broadcast rights to live sports and for CNN's live news. *See, e.g.,* Tr. 2112:24-2113:12 (Sejen (Cable ONE)) (agreeing that "sports programming" is "[t]he only thing that was unique" to TBS and TNT); *id.* at 245:7-23 (describing TBS and TNT's "important sports" and CNN's "news"). CNN is the second-rated news network, and a top-seven ranked network by viewership. PX8-35; Tr. 717:5-8 (Hinson (Cox)). In the sports domain, Turner has long-term contract rights to show portions of NCAA March Madness, the NBA Playoffs, and certain games of the Major League Baseball Playoffs. *See* PX8-35; Tr. 533:3-12 (Martin (Turner)); *see generally* Gov't PFOF ¶¶ 82-86, 88 (reviewing Turner's sports rights). TBS and TNT are "by far and away" the two most popular Turner networks due

to their sports content. Tr. 471:17-20 (Martin (Turner)). Not surprisingly perhaps, TBS and TNT rank in the top ten most profitable cable networks. *Id.* at 471:21-24; *see also* Gov't PFOF ¶¶ 25, 27.

Reflecting that popularity, Turner enjoyed rate increases from every major MVPD in the last five years. *See* Tr. 998:20-22 (Breland (Turner)); *see also* Gov't PFOF ¶ 97. Turner executives testified that those rate hikes were due in part to a multi-year plan to “catch up” to competitors’ price increases after years of below-market increases. Tr. 644:1-18 (Martin (Turner)). As such, Turner projects that its rate increases will slow to the low single digits from 2018 to 2022. *See id.* at 647:3-11 (discussing DX781). That slowing rate-increase trend is consistent with Turner’s declining viewership numbers. *See id.* at 2458:5-8, 22-24 (Carlton); *see also* PX153-3 to -4; PX456-22. Turner networks account for only 8% of pay-TV viewership, down from 10% in 2011. *See* Tr. 2458:22-24 (Carlton) (discussing DXD109). When internet-based distribution is added to the mix, Turner’s share shrinks to 6% of viewership for 2017. *See id.* at 2458:13-15.

The growth in digital advertising has also posed a particular challenge for Turner. Today, “advanced advertising” makes up less than 5% of Turner’s ad revenue – and it shows. *Id.* at 680:4-7 (Martin (Turner)). Turner’s ad revenues have flatlined. *See* PX456-65. This is because, as a “stuck in the middle wholesaler,” Turner for the most part lacks customer relationships, which supply critical data concerning consumer preferences – data that can be used to tailor advertisements to the end user. *See* Tr. 641:13-25 (Martin (Turner)); *id.* at 3087:16-3088:2 (Bewkes (Time Warner)). Without such data, Turner cannot tailor ads to particular consumers, making its ads less valuable than those carried

on Google or Facebook. *See id.* at 623:5-16 (Martin (Turner)); *cf. id.* at 3771:12-23 (Athey).

At trial, the Court learned that Turner has attempted workarounds to improve its data and sharpen its advertisements. Turner has tried, for example, to purchase data from third parties, but that data was not sufficiently granular. *See, e.g., id.* at 3100:2-4 (Bewkes (Time Warner)). Time Warner also considered buying technology companies, but concluded that the companies' data was insufficient, and came without any guarantee of long-term access. *See id.* 3102:9-3103:6. Finally, Turner has attempted to obtain rights to customer information through affiliate negotiations. *See id.* at 3100:16-22; *cf. id.* at 92:19-24 (Fenwick (Cox)). The record reflects, however, that such efforts generally have been unsuccessful due to the bargaining friction of hotly contested affiliate negotiations and the fact that distributors consider their customer data proprietary. *Id.* at 955:10-18 (SEALED); *cf. id.* at 1022:2-20 (Breland (Turner)); Defs.' PFOF ¶ 16.⁸

In an effort to break out of its "trapped wholesaler" role, Turner has made recent efforts to launch its own direct-to-consumer content offerings. The most notable of those offerings are Film Struck, Boomerang, and Bleacher Report Live. *See Tr.* 588:8-16, 666:10-12 (Martin (Turner)). FilmStruck, which allows viewers to access classic movies as well as independent films, has approximately 100,000 subscribers; Boomerang, which offers a library of children's content and cartoons, has around 150,000 subscribers. Defs.'

⁸ Turner has been able to negotiate for the rights to *limited* data from Hulu's and YouTube's virtual MVPDs. *See Gov't PFOF* ¶ 336. As relevant here, however, that data relates only to the viewing patterns of those who view Time Warner content. That is a limited picture, as such data does not allow Turner to discern what its viewers are watching on competing channels, which could help develop a fuller picture of viewer preferences. *Tr.* 3101:13-22 (Bewkes (Time Warner)).

PFOF ¶ 15. Those figures are of course microscopic in comparison to Netflix’s 125 million subscribers and Amazon’s 100 million Prime subscribers with access to video content. *See* Tr. at 3099:6-12 (Bewkes (Time Warner)); *id.* at 3389:22-25 (Stephenson (AT&T)).⁹

2. HBO

HBO has a different business model than Turner. As a premium network, HBO offers high-quality programming that is supported by subscriber fees rather than advertising. Tr. 1450:12-17 (Sutton (HBO)); *see also* PX456-67. Indeed, HBO has no advertising inventory at all. *Id.* In addition, and unlike the Turner networks, which appear in base cable or satellite packages, HBO is typically an “add-on.” *Id.* at 3073:14-15 (Bewkes (Time Warner)); *see id.* at 1451:16-18 (Sutton (HBO)).¹⁰ HBO offers popular movies and television shows, including a significant amount of original content. *See* PX459-22.

Without advertising, HBO’s business model is even more reliant on broad distribution: “the more, the better,” according to Time Warner CEO Jeff Bewkes. Tr. 3070:3-8 (Bewkes (Time Warner)). HBO content reaches consumers in four ways: (i) through MVPDs; (ii) through virtual MVPDs; (iii) through SVODs; and (iv) through HBO’s proprietary over-the-top product, HBO Now. *Id.* at 1494:1-8, 1451:13-23 (Sutton

⁹ Turner’s Lilliputian direct-to-consumer subscriber numbers, on their face, discredit the Government’s assertion that “Turner is also not the ‘trapped wholesaler’ it claims to be.” Gov’t PFOF ¶ 30.

¹⁰ The Government states that “pay-TV packages include linear TV programming, on-demand content, and typically premium channels *like HBO*.” Gov’t PFOF ¶ 12 (emphasis added). However, no matter how many premium channels “like HBO” may be available on such packages, HBO itself has historically had only a 30% national penetration rate. *See* Tr. 1529:16-17 (Patel (AT&T)); *id.* at 3073:22-23 (Bewkes (Time Warner)).

(HBO)). In each case, the end-customer accesses HBO by way of a distributor – even for HBO Now, which is sold by digital distributors like Apple and Amazon. *See id.* at 1491:6-11. As with Turner, the fact that HBO relies on third parties to distribute its programming means that Time Warner lacks critical data about the preferences and viewing habits of HBO’s subscribers. *See id.* at 3084:14-24, 3098:13-16 (Bewkes (Time Warner)).

HBO faces an array of competitors in the field of premium content creation and programming. There are premium television networks, like Showtime, Starz, and Epix, and online offerings, such as Netflix, Amazon Prime, and Hulu. *See id.* at 1492:20-23 (Sutton (HBO)). What’s more, Disney has launched, and Apple appears poised to launch, a premium, direct-to-consumer service. *See id.* at 1492:22-24; *id.* at 1396:21-25 (Montemagno (Charter)). All of those rivals feature high-quality, premium content, and thus compete directly with HBO. *See, e.g., id.* at 1494:16-23 (Sutton (HBO)). Indeed, Netflix’s programming budget alone is more than twice the size of HBO’s. *Id.* at 3099:13-15 (Bewkes (Time Warner)).

In this highly competitive environment, and lacking direct relationships with its viewers, HBO “[a]bsolutely” depends on MVPD promotions to maximize its distribution. *Id.* at 1496:16-17 (Sutton (HBO)); *cf. id.* at 1528:25-1529:4 (Patel (AT&T)). As HBO President Simon Sutton explained, “our whole business is relying on our affiliates to promote us. If we can’t do that, then our entire business model is destroyed.” *Id.* at 1508:14-16 (Sutton (HBO)). For that reason, HBO seeks to structure its affiliate agreements so as to “incent” distributors to maximize HBO’s distribution. *Id.* at 1456:8-

10. Specifically, as distributors add HBO subscribers. “they generally pay less on the increment.” *Id.* at 1455:18-19.

C. The Proposed Merger

On October 22, 2016, AT&T announced its plan to acquire Time Warner. Answer 18 [Dkt. # 20]. Inclusive of debt, the transaction is valued at approximately \$108 billion. *Id.*

At trial, the evidence showed that defendants view the proposed merger as an essential response to the industry dynamics described above – that is, the increasing importance of web- and mobile-based content offerings; the explosion in targeted, digital advertising; and the limitations attendant with AT&T’s and Time Warner’s respective business models. *See generally* Defs.’ PFOF ¶¶ 49-62 (discussing various proconsumer rationales for the proposed merger). The proposed merger would do so, defendants’ executives asserted, through vertical integration of the companies’ complementary assets: Time Warner’s popular content and significant advertising inventory, and AT&T’s consumer relationships, customer data, and large wireless business.

As a traditional programmer, Time Warner generally lacks access to valuable information about its viewers – it is, as mentioned, akin to a “stuck in the middle wholesaler.” Tr. 641:13-25 (Martin (Turner)). That is because it is the video distributors – not Turner – that own the customer relationships and, therefore, the customer data. *See supra* pp. 20, 25-28. Although Time Warner has “massive inventories of advertising,” it does not “know who the customer is. . . . They don’t know who they are, they don’t know what they’re watching.” *Id.* at 3392:10-13 (Stephenson (AT&T)). Without information

about who its customers are and what their content preferences may be, Time Warner is disadvantaged vis-à-vis SVODs, such as Netflix, Hulu, and Amazon Prime, and web companies, such as Facebook and Google, when it comes to its ability to cater programming or advertisements to viewers. *See supra* pp. 20, 25-28. As AT&T CEO Randall Stephenson explained, without consumer relationships and access to data, Time Warner's "large load of advertising inventory [is] being under utilized." Tr. at 3394:1-2 (Stephenson (AT&T)); *see also id.* at 3771:12-23 (Athey) (confirming that AT&T's digital, data-driven advertising prices are 60% higher than Nielsen-based ads because the former have "finer demographics that are offered for targeting").

As a video distributor, AT&T generally lacks control over the video content it offers. *See id.* at 3219:1-3 (Stankey (AT&T)) ("What we don't have is, we didn't have programming. We didn't have the flexibility to change the product, and that's what the guys on the other side had."). AT&T also has access to only limited advertising inventory. *Cf. id.* at 3393:1-11 (Stephenson (AT&T)); *id.* at 609:23-610:4 (Martin (Turner)). When AT&T seeks to negotiate with programmers for rights to provide or experiment with innovative content offerings, it typically encounters significant bargaining friction that renders those efforts unsuccessful. *See supra* pp. 19-20.

By acquiring Time Warner, AT&T executives testified, the company will immediately gain access to high-quality content and an extensive advertising inventory. *See* Tr. 3408:3-10 (Stephenson (AT&T)). Using its wireless network, AT&T intends to distribute Time Warner content through mobile devices. With such strong industry tailwinds in favor of mobile video consumption, this strategy will increase viewership,

making Time Warner content “worth far more.” *Id.* at 3393:24-25; *cf.* 891:23-25 (Rigdon (Comcast)) (confirming “increasing trend in the consumption of video over mobile devices”). At the same time, AT&T will bring to bear its consumer relationships and data to begin to tailor Time Warner’s advertising and increase its value. *See id.* at 3394:3-18 (Stephenson (AT&T)).

As the Government concedes, that access will inure right away to the benefit of AT&T’s current video distribution subscribers. In particular, the Government’s own expert predicts that, due to a standard benefit of vertical integration, AT&T’s DirecTV and U-verse customers will pay a total of about \$350 million less per year for their video distribution services. *See infra* pp. 66-68. AT&T executives testified about the other efficiencies that would redound to the benefit of AT&T subscribers should the merger be approved. Of most relevance here, with the Time Warner assets, and without the interference of bargaining friction, AT&T will be able to deliver content to its customers in more innovative ways. The merged entity could, for instance, gather and edit individual news clips from CNN throughout the day – all tailored to a given user’s interests – and deliver that news to the wireless customer for viewing on his or her fifteen-minute break. *See* Tr. 3220:21-3221:9 (Stankey (AT&T)). According to AT&T executive John Stankey, that opportunity represents “a new customer at a new moment doing something that wasn’t being done otherwise.” *Id.* at 3221:13-14. Stankey testified that the absence of bargaining friction will also enable AT&T and Time Warner to pursue broader introduction of new technologies, such as “4K” high-resolution programming. *See id.* at 3222:4-22.

AT&T will also, with their customers' permission, use consumer data to develop targeted ads, thereby increasing the value of Time Warner's ad inventory. *See id.* at 3391:12-22, 3393:4-9 (Stephenson (AT&T)). AT&T witnesses testified that, in their view, the Time Warner ad inventory is of sufficient scale to warrant the development of a "programmatic advertising platform" through which AT&T can deploy its data to create a marketplace of data-informed advertising inventory for use by Time Warner and third-party programmers alike. *Id.* at 3243:14-3244:8 (Stankey (AT&T)). At the same time, new, tailored forms of mobile content delivery – like the CNN clips teased above – will create additional advertising opportunities. *See id.* at 3221:10-11. Those opportunities, Time Warner and AT&T witnesses testified, will lead to higher ad revenues that will alleviate pressure on the programming side and lower the price of video distribution to consumers. All of those steps, defendants asserted, will allow AT&T to imitate the highly successful, data-driven entities in the video programming and distribution and advertising markets.

In addition, ownership of Time Warner content will allow AT&T to more efficiently pursue what it sees as the future of the video programming and distribution industry: increased delivery of content via mobile devices, such as cell phones. *See id.* at 3381:24-3382:2, 3393:13-25 (Stephenson (AT&T)). AT&T's vast wireless business – a business that, if taken separately, "would be number 37 in the Fortune 500" – has over 100 million subscribers. *Id.* at 3379:20-24; *see id.* at 3208:21-23 (Stankey (AT&T)). AT&T executives testified about their vision for using those wireless connections to "transform the way we deliver video to customers, [to] make the video far more portable." *Id.* at 3208:20-22

(Stankey (AT&T)); *see id.* at 3393:13-25 (Stephenson (AT&T)). To sum it up, in the words of AT&T Chairman and CEO Randall Stephenson, defendants view the proposed merger as a “vision deal” reflecting a belief “that distribution of [Time Warner’s] content to wireless will drive the value of the content up,” and that “the ability to pair our data with [Time Warner’s] advertising inventory will drive value.” *Id.* at 3402:24-3403:6.

III. Procedural History

A. The Investigation

Following the announcement of the deal in October 2016, the Department of Justice’s Antitrust Division conducted an investigation of the proposed merger’s competitive effects. Defs.’ PFOF ¶ 2. The investigation lasted more than one year. *Id.* During that investigatory phase, the Government took approximately 20 depositions and received roughly 25 million pages of documents. Despite the investigation’s vast scale and obvious importance, defendants had scarce visibility into the process. They could not access the Government’s materials during the course of the investigation. *See* 12/21/18 Hr’g Tr. 12:1-12 [Dkt. # 56]. Nor could they attend, let alone ask questions during, the depositions that took place during the investigation. *See id.*

B. Pretrial Proceedings

1. The Complaint

On November 20, 2017, the Government, acting through the Department of Justice, filed this lawsuit against AT&T, DirecTV, and Time Warner to enjoin the proposed merger under Section 7 of the Clayton Act, 15 U.S.C. § 18. *See* Compl. ¶ 48. Thirty-seven members of the Department of Justice, including Assistant Attorney General for Antitrust

Makan Delrahim, signed the Complaint. *Id.* at 23. In its prayer for relief, the Government asked that defendants AT&T and Time Warner “be permanently enjoined from carrying out the proposed merger and related transactions” or “carrying out any other agreement, understanding, or plan by which AT&T would acquire control over Time Warner or any of its assets; or merging.” *Id.* ¶ 48.

2. Turner’s Arbitration Commitment

About one week after the Government filed its Complaint, Turner sent a letter and an accompanying list of terms and conditions to approximately 1,000 video distributors. *See, e.g.*, PX490; PX491; Tr. 1181:11-16 (Warren (Turner)). In the letter, Turner represented that it was “irrevocably offering to you this agreement to engage in AAA arbitration, subject to the conditions below.” PX490. “This agreement,” the letter continued, “also provides you with the right to continued carriage of the Turner Networks . . . pending the arbitration in the event of a failure to agree upon renewal terms.” *Id.* The agreement specifies that once arbitration is invoked by a distributor, Turner must continue to provide carriage on the same terms and conditions in effect at the expiration of its existing contract with the distributor, subject to the right to receive a “true-up” – make-up payments, in essence – based on the arbitrator’s award. PX491-3 to -4, §§ B.1-.3. In other words, the commitment guarantees that no blackout of Turner content can occur once arbitration is invoked. *See, e.g.*, Tr. 2653:21-23 (Katz). The proposed arbitration agreement incorporates by reference the choice-of-law provisions in the underlying affiliate agreements. PX491-2, ¶ 7.

3. Pre-Discovery Timeline

Defendants filed their answer on November 28, 2017. *See generally* Answer. AT&T and Time Warner also announced that they had agreed to extend the merger agreement through April 22, 2018. *See* PX456-2. Defendants swiftly moved for a trial date and, along with the Government, for a protective order. *See* Defs.’ Mot. to Set Trial Date [Dkt. # 22]; Defs.’ Mot. to Enter Protective Order [Dkt. # 23]; Pl.’s Mot. to Enter Protective Order [Dkt. # 24]. On December 8, 2017, I issued a protective order governing the designation and use of confidential information. *See* Protective Order [Dkt. # 37]. On December 21, 2017, I issued a Case Management Order (“CMO”) [Dkt. # 54] and Scheduling Order [Dkt. # 55], which, among other things, set the trial for March 19, 2018 and stated that there would be no dispositive motions. That same day, to allow for the possibility of the March 19, 2018 trial and the ruling to follow, AT&T and Time Warner extended yet again the drop-dead date of the merger from April 22, 2018 to June 21, 2018. *See* PX456-2. If the deal is not consummated by then, the merger agreement specifies that AT&T will be required to pay Time Warner a break-up fee of \$500 million. *See* PX451-87. In the event of a favorable judgment, defendants agreed “not to consummate or otherwise complete the challenged acquisition until 12:01a.m. on the sixth calendar day following entry of such judgment.” CMO ¶ 3.

4. Discovery

Given the stakes and the June 21, 2018 drop-dead merger deadline, the parties proceeded through discovery on an expedited basis. Fact discovery began in late December, and concluded in mid-February. The Government began producing third-party

documents collected during the investigation to defendants before the New Year. The parties exchanged preliminary fact witness lists in early January, and final fact witness lists one month later. They spent the intervening time on a forced march of depositions. The exchange of initial expert reports took place in early February, with rebuttal reports due at the end of that month. Supplemental discovery closed on February 28, 2018, and expert discovery did so on March 9, 2018. The Scheduling Order set additional deadlines for pre-trial motions, *Daubert* motions, and pre-trial submission of final exhibit lists, just before the March 19 start date for trial.

I provided detailed prescriptions concerning discovery in this compressed time period. The CMO limited each side's final trial witness list to 30 fact witnesses. CMO ¶ 12. The Government and defendants each had a maximum of 15 interrogatories and seven requests for admission. *Id.* ¶ 14(d), (e). The CMO restricted each side to 150 hours of party-depositions, plus 100 hours of non-party depositions. *Id.* ¶ 16. The CMO did not preclude the taking of a deposition of someone already deposed during the investigation phase. *Id.* There were no limits on the number of requests for production. *Id.* ¶ 14(a).

The parties achieved herculean feats during that time. Beyond the 25 million pages of documents produced during the Government's investigation, an additional 7.5 million pages of documents were produced during discovery. 2/2/18 Hr'g Tr. 13:10-13 [Dkt. # 66]. Dozens of third parties received Rule 45 subpoenas. *See* 1/5/18 Hr'g Tr. 7:18-21 [Dkt. # 61]. The Government noticed more than 40 depositions of defendants' witnesses. *Id.* at 9:13-15.

5. Discovery Disputes

Rather than appointing a special master to handle discovery related issues, I relied upon the seasoned counsel on both sides of this case to work together to resolve discovery disputes as they arose. Although counsel generally were successful in doing so, two notable pre-trial issues were brought to this Court for resolution. The first, which arose in mid-January, concerned the disclosure of third-party data collected in prior Government investigations and still in the Government's possession. The second flash point, which took place closer to trial, involved discovery requests in support of defendants' selective prosecution claim.

In a January 18, 2018 letter and during a status hearing held the next day, defendants raised an issue related to the production of historical video programming pricing data in Government files – data that the Government had apparently obtained via prior merger investigations. *See* 1/19/18 Hr'g Tr. 6:14-9:23 [Dkt. # 63]. To that point, the Government had resisted defendants' production requests, arguing that the Antitrust Civil Process Act, 15 U.S.C. § 1313, required it to obtain consent from each of the third parties that originally had produced the information in question. *See id.* at 13:14-15. No third party had given consent, the Government continued; nor did those parties continue to possess some or all of the requested information due to the passage of time since those earlier investigations. *See id.* at 7:12-16, 8:17-20, 15:19-25.

Stuck in a seeming game of document "hot potato," defendants asked this Court to direct the Government to provide copies of the pricing data to the third parties that originally produced it. *Id.* at 16:11, 18:23-25. Such an order would in turn enable

defendants to subpoena the information directly from the third parties. Following oral argument on the issue, I ordered the Government to seek consent from the relevant third parties and to produce the requested information to those third parties by a date certain. 1/22/18 Order [Dkt. # 62]. The Government complied with this Order and defendants apparently were able to obtain the pricing data at issue. 2/2/18 Hr'g Tr. 6:2-5.

The case sailed along until mid-February, when the parties raised an issue related to defendants' contemplated motion for discovery on their "selective enforcement" claim and their attendant inclusion of Assistant Attorney General Makan Delrahim on their trial witness list. The Court held a hearing and heard oral argument on that dispute. *See generally* 2/16/18 Hr'g Tr. [Dkt. # 67]. In that hearing, defendants made an oral motion to compel production of privilege logs relating to their selective enforcement defense. *See id.* at 22:17-23. The Government, for its part, made an oral motion to strike defendants' outstanding discovery and interrogatory requests for logs listing (i) all written communications about the proposed merger between the White House and the Attorney General's Office, (ii) all written communications about the White House's views of the proposed merger between the Attorney General's Office and the Antitrust Division, and (iii) all oral communications about the proposed merger between the White House and the Antitrust Division. *See id.* at 46:8-20, 54:13-55:14. During the hearing, defendants agreed to strike Mr. Delrahim from their witness list subject to the right to call him at trial for good cause. *Id.* at 36:17-37:4. A few days later, after considering the parties' arguments at the hearing, I issued a Memorandum Opinion denying defendants' oral motion to compel and granting the Government's oral motion to strike. 2/20/18 Mem. Op. & Order 6 [Dkt. # 68].

As set out more thoroughly in that opinion, I concluded that defendants had failed to meet the rigorous standard for obtaining discovery on their selective enforcement defense. *See id.* at 4.

6. Evidentiary Disputes

As with most trials featuring large volumes of documentary evidence, evidentiary issues were heavily litigated in this case. Indeed, I set aside the first two days of the trial to address evidentiary issues. Not surprisingly, each side vacillated between arguing for exclusion of documents as prejudicial or irrelevant, on the one hand, or for admission of documents because such concerns are inapplicable in bench trials, on the other. While keenly aware of the principles governing evidentiary rulings in bench trials, in this case, I did not have the luxury of blanketly admitting a mass of documentary evidence and sorting through it after trial.¹¹ The compressed timeline and novel, complicated nature of the case instead necessitated that I make individualized rulings on relevance and admissibility. *Cf.* Manual for Complex Litigation § 12.5.

For this reason, I generally instructed the parties to seek admission of documents through sponsoring witnesses, in order to facilitate determinations of relevancy or to establish the foundation necessary for nonhearsay or hearsay exceptions.¹² Witnesses

¹¹ Nor did defendants broadly stipulate to the admission of the Government's proffered documentary evidence, as defendants seem to have done in recent antitrust cases in our Circuit. The parties also did not introduce their experts' reports into evidence; instead, they rested on the experts' trial testimony.

¹² There was not a uniform rule mandating sponsorship of documents by witnesses. I took judicial notice, for example, of certain statements made by DirecTV and AT&T before the FCC without sponsoring witnesses. *See* Tr. 3966:5-3967:22. In the same way, I was mindful that some documents, such as a slide presentation known at trial as "version 41," would not constitute hearsay, as they were introduced to establish the intent of the parties, rather than for the truth of the matter asserted.

would be able to contextualize and explain the technical and lengthy documents at issue, which might otherwise be misunderstood or selectively cited in post-trial briefs. As such, I instructed the parties to introduce documents through sponsoring witnesses, recognizing that doing so would extend, somewhat, the length of the trial. In the end, the parties agreed to abide by that approach. *See, e.g.*, 3/19/18 Hr’g Tr. 6:17-22 (afternoon session) (Government agrees to “add[] some additional witness and [to] talk[] with the defendants about that with regard to sponsorship issues”).¹³

C. The Trial

The trial began on March 19, 2018 and ended with closing arguments on April 30, 2018.¹⁴ Over that period, there were 23 days of proceedings.

The Government called 20 fact witnesses and two expert witnesses in its case-in-chief. Of the fact witnesses, 11 were employees of defendants, and 9 were employees of third parties. The Government’s chief economic expert was Professor Carl Shapiro. Professor Shapiro is a Ph.D. industrial economist who currently holds a professorship at the University of California, Berkeley. Professor Shapiro has served in various positions in the federal government, including most recently as Deputy Assistant Attorney General

¹³ Negotiations between the parties further winnowed the evidentiary disputes. *See, e.g.*, 3/19/18 Hr’g Tr., PDF at p. 7 (morning session). The parties also heeded warnings from the Court during initial evidentiary hearings as to the likely inadmissibility of certain documents. For instance, after a warning as to the likely admissibility of newspaper clippings, defendants did not seek admission of those documents at trial. *See* 3/20/18 Hr’g Tr. 5:16-20 (afternoon session) (advising defendants that the Court “usually [does not] allow news articles [to be] introduced into evidence. I’ll wait to see what you’ve got . . . but I’m giving you fair notice here”).

¹⁴ On March 9, 2018, the parties each filed a brief, laying out their theories of the case. [Dkt. ## 75, 76, 77]. On March 13, 2018, the parties filed a Statement of Evidentiary Objections under seal. [Dkt. # 86]. The same day, the parties filed a Joint Statement on the Burden of Proof at Trial, which set forth each side’s views of the legal standards and burden of proof applicable to this case. [Dkt. # 87].

for Economics at the Antitrust Division in 2009 through 2011 and as a member of the President's Council of Economic Advisers in 2011 and 2012. He has testified in a number of antitrust matters, including several antitrust trials in our Circuit. The Government also called Professor John Hauser from the Massachusetts Institute of Technology to testify about a survey he designed and performed and on which the Government relies.

For their part, defendants called three expert and three fact witnesses. Chief among their experts was University of Chicago Professor Dennis Carlton, who provided rebuttal testimony to Professor Shapiro. Professor Carlton has served as an economics professor within the University of Chicago since 1976, teaching in the economics department, business school, and the law school. Like Professor Shapiro, Professor Carlton is a seasoned expert witness who himself has served as Deputy Assistant Attorney General for Economics at the Antitrust Division from 2006 to 2008. Defendants also called Professor Michael Katz from the Haas School of Business at the University of California, Berkeley, and Professor Peter Rossi from the UCLA's Anderson School of Management. Defendants called Professor Katz to testify about the effect of arbitration and the FCC's program access rules, and called Professor Rossi to testify about survey methods and to rebut testimony concerning surveys and studies on which the Government relied. As their fact witnesses, defendants called Jeff Bewkes, Chairman and CEO of Time Warner, and Randall Stephenson, Chairman and CEO of AT&T, to testify regarding their decision to merge. Defendants also called John Stankey, a senior executive at AT&T responsible for planning and integration of the proposed merger. Stankey, who will be running Time Warner should

the merger be allowed to occur, testified about the rationale for the merger as well as the synergies and efficiencies that would result from the merger.

The Government's rebuttal case consisted of testimony from three experts. First, the Government called Ronald Quintero, an accounting and financial consultant, to testify as an expert witness on defendants' claims that the challenged merger will result in a number of procompetitive synergies. Next, the Government called Professor Susan Athey, an economics of technology professor at the Stanford Graduate School of Business, to testify regarding defendants' proffered "content intelligence" synergies. Finally, the Government closed out its rebuttal presentation by recalling Professor Shapiro to defend and further explain his case-in-chief testimony in the face of defendants' various criticisms.

To say the trial was well staffed would be an understatement. Thirty-two lawyers entered appearances for the Government, and 14 did so for defendants. Evidentiary disputes were handled on a case-by-case basis as issues arose. In order to accommodate the confidentiality interests of third parties, counsel agreed to craft their questions so as not to elicit sensitive business information, and, on three occasions, I had to close the courtroom to the public following factual proffers by the Government as to the need for doing so.¹⁵ In total, I admitted into evidence over 3,000 pages of documents, broken up into over 120 exhibits. The trial transcript itself exceeds 4,300 pages in length.

¹⁵ The Court explained to the parties that it appreciated both the public's interest in open judicial proceedings, and the importance to the Government's case of third-party testimony and the need to maintain confidentiality. Consistent with these competing interests, and applicable case law, the Court advised the parties that, when seeking to close the courtroom, they would first need to make a proffer explaining the necessity of doing so. *Cf.* 28 C.F.R. § 50.9 (2017) (reciting "the vital public interest in open judicial proceedings" and stating the policy that DOJ counsel "shall not move for or consent to closure of a

On May 3, 2018, a mere one week after the close of evidence, the parties filed their proposed Findings of Fact and Conclusions of Law, totaling nearly 400 pages in length, as well as briefs that synthesized their arguments. On the last day of trial, I advised the parties that it would issue a ruling by June 12, 2018 in order to avoid running afoul of the defendants' merger deadline of June 21, 2018 and to provide the losing party sufficient time to preserve its appellate rights.

IV. Legal Standard

A. The Clayton Act

The Government seeks to enjoin the proposed merger on the basis that it violates Section 7 of the Clayton Act, 15 U.S.C. § 18. *See id.* § 25 (authorizing United States to

proceeding” unless “[n]o reasonable alternative exists for protecting the interests at stake” and “[f]ailure to close the proceedings will produce . . . [a] substantial likelihood of denial of the right . . . to a fair trial”).

In order to accommodate those confidentiality interests, counsel agreed to craft their questions so as not to elicit sensitive business information. *See* Tr. 692:14-16 (“[G]overnment’s counsel has got this choreographed approach here to get this information from you under oath without revealing it to the public.”); *see also, e.g., id.* at 99:12-14 (SEALED). Counsel routinely asked witnesses to point to or confirm for the Court the contents of documents under seal. *See, e.g., id.* at 119:1-21, 124:18-125:13 (Fenwick (Cox)); 535:11-22, 662:7-20 (Martin (Turner)); *id.* at 1095:19-1096:7 (Breland (Turner)); *id.* at 3011:9-21 (Christopher (AT&T)); *id.* at 3529:18-3530:10 (Quintero). Indeed, the Government succeeded in eliciting considerable testimony from a third-party witness – this time from AT&T’s competitor, Cox – by way of a single exhibit. *See, e.g., id.* at 689:18-20 (Hinson (Cox)) (“Your Honor, I’d like to mark Plaintiff’s Exhibit, it’s got some confidential information that Mr. Hinson can point to.”); *see generally id.* at 692:25-708:14; *see also* PX523. In those instances, the Court, but not the public, had access to the referenced documents. In the same way, counsel asked witnesses to describe the contents at an appropriate level of generality. *See id.* at 259:11-13 (Schlichting (DISH)); *id.* at 1278:13-1279:21 (Bewley (Altman Vilandrie)).

Through skillful lines of inquiry and the use of exhibits and demonstratives, this approach resolved most confidentiality-based concerns. For several witnesses, the Government initially raised the possibility of going into closed session, before later declining to seek to do so. *See, e.g.,* Tr. 439:14-16 (SEALED). Other times, the Government elected to establish the factual proffer necessary to close the courtroom. To take one example of the way in which – when it chose to do so – the Government developed the need for closing the courtroom, Government counsel confirmed with NBCU’s Madison Bond in open court that he felt constrained by confidentiality obligations with respect to at least six different items. *See, e.g., id.* at 1992:2-1992:8; *id.* at 1993:24-1994:6 (Bond (NBCU)).

seek equitable relief to restrain a pending acquisition that violates Clayton Act). As relevant here, Section 7 “prohibits acquisitions, including mergers, ‘where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition.’” *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 713 (D.C. Cir. 2001) (quoting 15 U.S.C. § 18). The Government “has the ultimate burden of proving a Section 7 violation by a preponderance of the evidence.” *United States v. H & R Block, Inc.*, 833 F. Supp. 2d 36, 49 (D.D.C. 2011) (internal quotation marks omitted); *see also* Proposed Conclusions of Law of the United States (“Gov’t PCOL”) ¶ 24 [Dkt. # 127]. Accordingly, the Government’s “failure of proof in any respect will mean the transaction should not be enjoined.” *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 116 (D.D.C. 2004).

By using “the words ‘may be substantially to lessen competition’” in Section 7, Congress indicated “that its concern was with probabilities, not certainties.” *FTC v. Whole Foods Mkt., Inc.*, 548 F.3d 1028, 1042 (D.C. Cir. 2008) (emphasis omitted) (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962)). Although certainty of harm is not necessary to prove a Section 7 violation, neither is the “mere possibility” of harm sufficient. *Heinz*, 246 F.3d at 713 (quoting S. Rep. No. 1775, at 6 (1950)); *see also Baker Hughes*, 908 F.2d at 984 (“Section 7 involves *probabilities*, not certainties or possibilities.”). Rather, to grant injunctive relief under the Clayton Act, the Court *must* conclude that the Government has introduced evidence sufficient to show that the challenged “transaction is

likely to lessen competition substantially.” *Baker Hughes*, 908 F.2d at 985.¹⁶ As part of satisfying that burden, Section 7 “demand[s] that a plaintiff demonstrate that the substantial lessening of competition will be ‘sufficiently probable and imminent’ to warrant relief.” *Arch Coal*, 329 F. Supp. 2d at 115 (quoting *United States v. Marine Bancorporation*, 418 U.S. 602, 623 n.22 (1974)).

In assessing the Government’s Section 7 case, the court must engage in a “‘comprehensive inquiry’ into the ‘future competitive conditions in a given market,’” keeping in mind that “the Clayton Act protects ‘competition,’ rather than any particular

¹⁶ It is undisputed that the Government has the burden of proving a Section 7 violation. The Government’s view on what measure of proof that burden requires, however, has been somewhat of a moving target. In some instances, the Government mirrors defendants’ position that Section 7 requires a showing that the challenged transaction is “likely” to harm competition; in others, the Government states that it must show a “reasonable probability” or “appreciable danger” of harm to prevail. Compare Compl. ¶ 44 (“The effect of the proposed merger would be likely to lessen competition substantially” in the relevant markets.), and Gov’t PFOF 20 (“The proposed merger would likely substantially lessen competition” in the relevant markets.) (capitalization altered), with Gov’t Post-Tr. Br. 13 (disputing that the “United States must show that harm is ‘likely’”), and Gov’t PCOL ¶ 5 & n.1 (reciting a purportedly more lenient “reasonable probability” standard). In the final analysis, each alternative formulation appears aimed at clarifying the central point that Section 7 does not require “certain” harm, but instead permits courts to use predictive judgment to “arrest anticompetitive tendencies in their ‘incipiency.’” *United States v. Penn-Olin Chem. Co.*, 378 U.S. 158, 171 (1964) (quoting *United States v. Philadelphia Nat’l Bank*, 374 U.S. 321, 362 (1963) (internal quotation marks omitted)). Thus, it is not surprising that courts have used these terms interchangeably. See, e.g., *Hosp. Corp. of Am. v. FTC*, 807 F.2d 1381, 1389 (7th Cir. 1986) (noting that Section 7 requires “an appreciable danger” of anticompetitive consequences and concluding in same paragraph that Commission had adequately demonstrated that the “challenged acquisitions are likely to foster collusive practices, harmful to consumers”); *Anthem*, 236 F. Supp. 3d at 215 (citing with approval other court’s use of “reasonably likely” formulation, later concluding that “[p]laintiffs have carried their burden to establish that the merger is likely to harm competition”).

For present purposes, I need not further toil over discerning or articulating the daylight, if any, between “appreciable danger,” “probable,” “reasonably probable,” and “likely” as used in the Section 7 context. That is because even assuming that the “reasonable probability” or “appreciable danger” formulations govern here and require more than a “mere possibility,” but less than a “more likely than not” showing of harm, *but see Baker Hughes*, 908 F.2d at 991 (describing “the ultimate issue” in a Section 7 case as “whether [the proposed] transaction is *likely* to lessen competition substantially” (emphasis added)); *Anthem*, 236 F. Supp. 3d at 215 (“merger is likely to harm competition”); *United States v. Aetna, Inc.*, 240 F. Supp. 3d 1, 9 (D.D.C. 2017) (“the proposed merger is likely to substantially lessen competition”); *FTC v. Staples, Inc.*, 190 F. Supp. 3d 100, 110 (D.D.C. 2016) (“proposed merger is likely to reduce competition”), my conclusions regarding the Government’s failure of proof would remain unchanged for all of the reasons discussed below.

competitor.” *United States v. Aetna*, 240 F. Supp. 3d 1, 18 (D.D.C. 2017) (quoting *Baker Hughes*, 908 F.2d at 988, 991 n.12). “[O]nly . . . examination of the particular market – its structure, history and probable future – can provide the appropriate setting for judging the probable anticompetitive effect of the merger.” *United States v. General Dynamics Corp.*, 415 U.S. 486, 498 (1974) (quoting *Brown Shoe*, 370 U.S. at 322 n.38). “Hence, antitrust theory and speculation cannot trump facts”; the Government must make its case “on the basis of the record evidence relating to the market and its probable future.” *Arch Coal*, 329 F. Supp. 2d at 116-117.

B. *Baker Hughes* Burden Shifting Framework

As the above discussion displays, Section 7 vests courts with the “uncertain task” of “making a prediction about the future.” *Baker Hughes*, 908 F.2d at 991; *United States v. Anthem, Inc.*, 236 F. Supp. 3d 171, 191 (D.D.C. 2017). To say the least: that is no easy assignment! In such a setting, and in the absence of a crystal ball, “allocation of the burdens of proof assumes particular importance.” *Baker Hughes*, 908 F.2d at 991. To further assist courts in this prospective inquiry, our Circuit has set forth a burden shifting framework for use in determining whether a proposed transaction violates the Clayton Act. *See, e.g., id.* at 982-83.

Under that framework, the Government must first establish its prima facie case by 1) identifying the relevant product and geographic market and 2) showing that the proposed merger is likely to “substantially lessen competition” in that market. *Id.* at 982, 991; *see also Arch Coal*, 329 F. Supp. 2d at 117; Gov’t PCOL ¶ 24. If the Government satisfies its prima facie burden, the burden then shifts to defendants to “provide sufficient evidence

that the prima facie case ‘inaccurately predicts the relevant transaction’s probable effect on future competition.’” *United States v. Anthem, Inc.*, 855 F.3d 345, 349 (D.C. Cir. 2017) (quoting *Baker Hughes*, 908 F.2d at 991). One way defendants may do so is to offer evidence that “post-merger efficiencies will outweigh the merger’s anticompetitive effects.” *Heinz*, 246 F.3d at 721. If the defendants put forward sufficient evidence to rebut plaintiff’s prima facie case, “the burden of producing additional evidence of anticompetitive effect shifts to the [government], and merges with the ultimate burden of persuasion, which remains with the [government] at all times.” *Anthem*, 855 F.3d at 350 (quoting *Baker Hughes*, 908 F.2d at 983).¹⁷

¹⁷ Defendants assert that the burden-shifting framework is inapplicable to vertical merger cases, where no market-concentration-based presumption of harm attaches. As such, defendants argue that the Government has the burden to account for all of defendants’ proffered efficiencies as part of making its prima facie case. I am skeptical of this position, both as a matter of law and logic. *Cf. Heinz*, 246 F.3d at 720 (discussing “efficiencies defense” as a component of the defendants’ case); 4A Areeda & Hovenkamp, *Antitrust Law* ¶ 970c. But given that the “ultimate burden” of proving a Section 7 violation rests with the plaintiff, *H & R Block, Inc.*, 833 F. Supp. 2d at 49, any debate over burden shifting “may be somewhat academic,” as defense counsel conceded, 3/20/18 Hr’g Tr. 67:6-7 (morning session); *cf. Baker Hughes*, 908 F.2d at 991 (deeming “the distinction between” the “burden of production” and “the ultimate burden of persuasion” as “always an elusive distinction in practice”). That is especially so here, where, as will become evident, the Court’s ruling does *not* turn on the efficiencies offered by defendants in their affirmative case, but rather on its conclusion that the *Government’s* evidence, as “undermined and “discredit[ed]” by defendants’ attacks, is insufficient to “show[] a probability of substantially lessened competition,” and thus that the Government has “failed to carry its ultimate burden of persuasion.” *Baker Hughes*, 908 F.2d at 983, 990-91.

I will nevertheless pause to mention briefly why I am confident that defendants will achieve considerable efficiencies beyond those conceded by the Government. At trial, defendants presented the Court with documentary and testimonial evidence concerning efficiencies likely to flow from the proposed merger. The efficiencies, defendants explain, come both on the “cost” side, and on the “revenue” side. By defendants’ calculations, cost synergies will total \$1.5 billion and revenue synergies \$1 billion on an annual basis. *See* Tr. 3234:17-3235:14 (Stankey (AT&T)). On the cost side, AT&T’s John Stankey testified that the marriage of AT&T and Time Warner will lead to the elimination of redundant positions in each company, achievement of certain economies of scale, and insourcing of services that the acquired entity currently acquires from vendors. *See id.* at 3235:22-3240:1. And on the revenue side, AT&T and Time Warner expect to see the gains in innovation – particularly by way of a new programmatic advertising platform – that motivated the merger in the first place. *See id.* at 3229:20-25, 3240:2-3246:9.

Putting aside the revenue synergies, which, by their nature, are more uncertain, I have a high degree of confidence that defendants will generate most, if not all, of the predicted \$1.5 billion in annual cost

C. Antitrust Analysis of Vertical Mergers

In the typical horizontal merger case under Section 7, the Government's path to carrying its prima facie burden is clear: by putting forward statistics to show that the proposed "merger would produce a firm controlling an undue percentage share of the relevant market, and would result in a significant increase in the concentration of firms in that market," the Government triggers a "'presumption' that the merger will substantially lessen competition." *Heinz*, 246 F.3d at 715 (internal quotation marks and alterations omitted) (quoting *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 363 (1963)); *see also, e.g., Anthem*, 236 F. Supp. 3d at 209; *Aetna*, 240 F. Supp. 3d at 43; *H & R Block, Inc.*, 833 F. Supp. 2d at 72.

In this case, however, the "familiar" horizontal merger playbook is of little use. *Baker Hughes*, 908 F.2d at 982. That is, of course, because the proposed transaction between AT&T and Time Warner is a vertical merger – *i.e.*, one that involves "firms that do not operate in the same market" and thus "produce[s] no immediate change in the level of concentration in any relevant market." Dept. of Justice & Fed. Trade Comm'n, Non-Horizontal Merger Guidelines § 4.0 (June 14, 1984) ("Non-Horizontal Merger

savings by 2021. *See id.* at 3234:13-20. AT&T derives its prediction through the same rigorous analytical process applied in each of its mergers. *See id.* at 3226:1-3229:3; *see also* DX658. Most recently, in the acquisition of DirecTV, AT&T exceeded cost synergy predictions, which now total \$2 billion annually. Tr. 3229:4-8, 3369:21-3370:4 (Stankey (AT&T)). Indeed, it is uncontested that AT&T has a strong record of meeting similar cost synergy estimates in past mergers. *See id.* at 3229:2-3, 3229:9; *see also id.* at 3226:3-5. That "analogous past experience" serves to "substantiat[e]" defendants' "efficiency claims," leaving this Court with little doubt that AT&T will stay on its projected track. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 10 (Aug. 19, 2010). Thus, while not necessary to my final judgment in this case, defendants have presented persuasive, probative evidence that the merger will produce even more efficiencies than those accounted for in this Opinion. As such, no further "troll[ing] the Internet" by Mr. Quintero would likely convince the Court otherwise! Tr. 3605:25 (Quintero).

Guidelines”).¹⁸ The parties therefore agree that in this case “there is no short-cut way to establish anticompetitive effects, as there is with horizontal mergers.” Joint Statement on the Burden of Proof at Trial (“Joint Statement”) 3 [Dkt. # 87]; *see* 4A Areeda & Hovenkamp, *Antitrust Law* ¶ 1000a (“[T]he basic economic reason for limiting horizontal mergers is well-founded and rather generally accepted: horizontal mergers increase market concentration, and high market concentration can substantially lessen competition among rivals, particularly with respect to price. Unfortunately, there is no comparable theoretical basis for dealing with vertical mergers.”).

With no presumption of harm in play, the Government concedes that, to satisfy its burden here, it must make a “fact-specific” showing that the effect of the proposed merger “is likely to be anticompetitive.” Joint Statement 3-4. Such a showing is “necessarily both highly complex” and “institution specific.” David T. Scheffman & Richard S. Higgins, *Vertical Mergers: Theory and Policy*, 12 *Geo. Mason L. Rev.* 967, 967 (2004); *see also* Gov’t PCOL ¶ 25 (collecting sources for proposition that “vertical mergers are judged on a case-by-case basis” based on consideration of “case-specific evidence of a danger of future competitive harm”). Of particular relevance here, the Government states that a vertical merger may “act as a clog on competition” by giving the merged firm “control of a competitively significant supplier.” Gov’t PCOL ¶ 46 (quoting *Brown Shoe*, 370 U.S. at 324). Such a situation would occur, the Government continues, if the merged firm were to

¹⁸ Although the Guidelines are not binding on this Court, our Circuit has noted that they are “a helpful tool, in view of the many years of thoughtful analysis they represent, for analyzing proposed mergers.” *Anthem*, 855 F. 3d at 349 (citing *Baker Hughes*, 908 F.2d at 985-86). As the Non-Horizontal Merger Guidelines make reference to concepts contained within the Horizontal Merger Guidelines, I will cite to both as appropriate.

withhold a source of supply from its rivals or otherwise foreclose access to the source “on competitive terms,” such as by causing its rivals to “pay[] more to procure necessary inputs,” which in turn could “harm[] competition and consumers.” *Id.* ¶¶ 46, 57-58 (emphasis omitted) (quoting *Yankee Entm’t & Sports Network, LLC v. Cablevision Sys. Corp.*, 224 F. Supp. 2d 657, 673 (S.D.N.Y. 2002); *Sprint Nextel Corp. v. AT&T, Inc.*, 821 F. Supp. 2d 308, 330 (D.D.C. 2011)).

Further complicating the Government’s challenge is the recognition among academics, courts, and antitrust enforcement authorities alike that “many vertical mergers create vertical integration efficiencies between purchasers and sellers.” Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 Antitrust L.J. 513, 519 (1995).¹⁹ The proposed merger reflects that principle: the Government’s chief economic expert, Professor Shapiro, predicts that the merger, if consummated, would lead to \$352 million in annual cost savings on the part of AT&T’s customers. *See* Tr. 2252:19-21 (Shapiro); *infra* pp. 66-68; *see also* Gov’t PFOF ¶¶ 222-223 (EDM effect is “generally accepted as a potential procompetitive benefit resulting from vertical mergers”).

As the Government also notes, the “principal objective of antitrust policy is to maximize consumer welfare by encouraging firms to behave competitively.” Gov’t PCOL

¹⁹ *See also* Robert H. Bork, *The Antitrust Paradox* 227 (2d ed. 1993) (“Vertical mergers may cut sales and distribution costs, facilitate the flow of information between levels of the industry . . . [.] create economies of scale in management, and so on.”); Ernest Gellhorn et al., *Antitrust Law and Economics* 411 (5th ed. 2004) (discussing the “[v]arious efficiency rationales” that “can motivate vertical mergers”); *cf.* *National Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831, 840 (D.C. Cir. 2006) (“[V]ertical integration creates efficiencies for consumers.”).

¶ 4 (quoting *Anthem*, 855 F.3d at 366 (emphasis and internal quotation marks omitted)); *see id.* (“Section 7 proscribes mergers with the potential to harm the competitive process, and thereby result in harm to consumers, including higher prices”). As such, any proper assessment of a proposed merger, Professor Shapiro testified, must consider both the positive and negative “impact[s] on consumers” by “balancing” the proconsumer, “positive elements” of the merger against the asserted anticompetitive harms. *See* Tr. 2182:12-20, 2253:4-5 (Shapiro); *see also id.* at 2461:22-2462:5 (Carlton) (“Well, Professor Shapiro is looking at the [e]ffects on consumer prices. That seems the right thing to do. . . .[W]e want to see what’s going to be the result on the end price that consumers pay.”); *cf.* Gov’t PFOF ¶ 223 (discussing fact that Professor Shapiro accounted for EDM effects). In view of that “somewhat different” analysis applicable to vertical mergers, Tr. 2182:16-18 (Shapiro), it is perhaps little surprise that the Department of Justice’s Non-Horizontal Merger Guidelines recognize that vertical mergers “are less likely than horizontal mergers to create competitive problems,” Non-Horizontal Merger Guidelines § 4.

Given all of the competing considerations at play, “the analysis of vertical mergers” has been described as “much more complex than the analysis of horizontal mergers.” Scheffman & Higgins, *Vertical Mergers*, 12 *Geo. Mason L. Rev.* at 967. Things are made more difficult still by the lack of modern judicial precedent involving vertical merger challenges – a dearth of authority that is unsurprising, considering that the Antitrust Division apparently has not tried a vertical merger case to decision in *four* decades! *See*

Defs.' Proposed Conclusions of Law ("Defs.' PCOL") ¶ 32 [Dkt. # 120]; 2/16/18 Hr'g Tr. 13:24-14:1.

To sum up, the Court accepts that vertical mergers "are not invariably innocuous," but instead can generate competitive harm "[i]n certain circumstances." Non-Horizontal Merger Guidelines §§ 4, 4.2; Gov't PCOL ¶ 22.²⁰ The case at hand therefore turns on whether, notwithstanding the proposed merger's conceded procompetitive effects, the Government has met its burden of proof of establishing, through "case-specific evidence," that the merger of AT&T and Time Warner, at this time and in this remarkably dynamic industry, is likely to substantially lessen competition in the manner it predicts. Gov't PCOL ¶ 25. Unfortunately for the Government, for the following reasons, it did not meet its burden.

ANALYSIS

The challenged vertical merger here would unite Time Warner, a creator and supplier of popular video content, with AT&T, a large downstream purchaser and distributor of video content. The Government concedes that the challenged merger, like most vertical mergers, will result in significant benefits to customers of the merged

²⁰ The Court therefore declines defendants' invitation to adopt either a per se rule or a presumption that would apply to most vertical mergers. See Pre-Tr. Br. of Defs. 29 [Dkt. # 77]. To be sure, the standard for which defendants advocate aligns with the views of a number of authorities, including judges from this Circuit. See, e.g., Robert Bork, *The Antitrust Paradox* 245 ("[I]n the absence of a most unlikely proved predatory power and purpose, antitrust should never object to the verticality of any merger."); *Comcast Cable Comms., LLC v. FCC*, 717 F.3d 982, 990 (D.C. Cir. 2013) (Kavanaugh, J., concurring) ("[A]bsent market power, vertical integration and vertical contracts are *procompetitive*." (citing Douglas H. Ginsburg, *Vertical Restraints: De Facto Legality Under the Rule of Reason*, 60 *Antitrust L.J.* 67, 76 (1991))). Tempting though it may be to agree with my appellate brethren, I need not, and will not, go that far to resolve this case.

company. Specifically, the Government's lead expert, Professor Carl Shapiro, estimates that the merger will cause AT&T to lower the price of DirecTV, resulting in \$352 million in annual savings for DirecTV's customers. *See* Tr. 2252:19-20 (Shapiro).

Notwithstanding those conceded consumer benefits, the Government contends that the challenged merger is "likely to lessen competition substantially," *Baker Hughes*, 908 F.2d at 985, and thus should be enjoined under Section 7, *see* Compl. ¶ 10. The challenged merger would likely result in a substantial lessening of competition, according to the Government, in three "mutually reinforcing" ways. Gov't Post-Tr. Br. 7.

First and foremost, the Government argues that the challenged merger would enable Turner to charge AT&T's rival distributors – and ultimately consumers – higher prices for its content on account of its post-merger relationship with AT&T. *See, e.g.* Compl. ¶¶ 36-38; Gov't PFOF ¶¶ 226, 231-32; Gov't Post-Tr. Br. 1-2. *Second*, the Government contends that the challenged merger will substantially lessen competition by creating an increased risk that the merged firm will act, either unilaterally or in coordination with Comcast-NBCU, to thwart the rise of the lower-cost, consumer-friendly virtual MVPDs that are threatening the traditional pay-TV model. *See* Compl. ¶¶ 40-41; Gov't PFOF ¶ 278. *Finally*, the Government alleges that the merged entity could harm competition by preventing AT&T's rival distributors from using HBO as a promotional tool to attract and retain customers. *See* Compl. ¶ 39; Gov't PFOF ¶ 234.

In the remainder of this section, I will analyze each of those theories of harm to competition. Initially, I will set forth the relevant market definition, which incorporates the Government's proposed product and geographic markets. Next, I will discuss the

conceded consumer benefits associated with the proposed merger. Mindful of those conceded benefits, and the need to balance them against the Government's allegations of consumer harm, I will then evaluate whether the Government has carried its burden to show a likelihood that the challenged merger will result in a substantial lessening of competition. For the reasons discussed in detail below, I have concluded that the answer to that question is no !

I. Market Definition

Typically, “[m]erger analysis starts with defining the relevant market” in which to assess the alleged anticompetitive harms. *FTC v. Sysco Corp.*, 113 F. Supp. 3d 1, 24 (D.D.C. 2015) (citing *United States v. Marine Bancorporation*, 418 U.S. 602, 618 (1974)). The relevant market comprises two parts: a product market and a geographic market. *Anthem*, 236 F. Supp. 3d at 193. Here, the Government defines the primary relevant product market as the “Multichannel Video Distribution” market, and the relevant geographic markets as the approximately 1,200 local markets in which residents have access to video offerings from the same set of multichannel video programming distributors. Gov’t PFOF ¶¶ 31, 38-41. Both of those proposed markets find support, the Government contends, in Professor Shapiro’s expert analysis, *see* Tr. 2184:22-2188:4 (discussing hypothetical monopolist test, among other things), as well as the *Brown Shoe* “practical indicia,” *see* 370 U.S. at 325 (listing “industry or public recognition of the submarket,” “the product’s peculiar characteristics and uses,” and “distinct customers” and “distinct prices” of the product as relevant to product market determination); Gov’t PFOF ¶¶ 32-36.

Horizontal merger cases often “to a great extent . . . hinge[] on” market definition because such definition affects the ultimate market concentration statistics associated with a proposed transaction. *FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1073 (D.D.C. 1997). For that reason, market definition is often heavily contested in horizontal merger cases, turning on fine-grained economic analyses of “SSNIPs” and cross-elasticity of demand. *See, e.g., Anthem*, 236 F. Supp. 3d at 193-198; *FTC v. Staples, Inc.*, 190 F. Supp. 3d 100, 116-127 (D.D.C. 2016); *Sysco Corp.*, 113 F. Supp. 3d at 24-48. Happily, I need not delve deeply into those concepts here. The proposed vertical merger, as discussed, does not “involve an increase in market concentration,” and defendants, for all of their objections to the Government’s case, have not meaningfully challenged the Government’s proposed product or geographic markets. Joint Statement 3; *see* Tr. 2186:25-2187:2, 2188:2-4 (Shapiro). I will thus accept the Government’s proposed product and geographic markets for purposes of this case, and briefly discuss the basics of those markets – as well as the role of the product market as it relates to my analysis of the Government’s claims of harm – below.

Product Market. The Government’s *primary* product market is the market for multichannel video distribution. Multichannel video distribution, as defined by the Government, involves the distribution of live, or “linear,” video programming networks, as well as on-demand content, to subscribing consumers. Gov’t PFOF ¶ 31; Trial Br. of the United States (“Gov’t Pre-Tr. Br.”) 22 [Dkt. # 76]. As relevant here, the sellers in that product market are: 1) MVPDs, including cable television providers, such as Comcast, Cox, and Charter; direct broadcast satellite providers, such as DirecTV and DISH, which operate nationally; telecommunications providers, or “telcos,” such as Verizon Fios and

AT&T's U-verse; and overbuilders, such as RCN; and 2) virtual MVPDs, including Sony's Playstation Vue, Hulu Live, Google's YouTube TV, DirecTV Now, and DISH's Sling. As discussed, virtual MVPDs provide the same live-TV services as do traditional MVPDs, but do so over the internet rather than by way of a dedicated transmission path that they control. *See* Gov't PFOF ¶ 15. Although the majority of U.S. households (approximately 90 million) currently receive linear video programming through traditional MVPDs, *id.*, and a majority are likely to continue to do so, there is no debating that the number of MVPD subscribers is "declining unequivocally" as consumers increasingly turn to virtual MVPDs and SVODs for their video content needs. Tr. 3451:22-23 (Stephenson (AT&T)); *see id.* at 3449:12–3451:1 ("DirecTV lost 1.2 million subscribers in 2017. The whole system, pay TV, cable, satellite, lost 3 million."); *see also id.* at 2948:11-24 (Holanda (RCN)); PX455-136 to -137.

As the above discussion indicates, the Government's proposed product market focuses on the downstream distribution of live-TV content to consumers—a focus that excludes both the upstream programming market and the market for SVODs such as Netflix, Hulu, and Amazon Prime. *See, e.g., id.* at 2184:22-2185:5 (Shapiro); *cf.* Gov't PCOL ¶ 38 (disputing need to "define an 'upstream' programming market").²¹ That product market definition appears to reflect the Government's (and Professor Shapiro's) projections regarding where the challenged merger's ultimate "net harm" to consumers –

²¹ The Government also asserts that a broader market of "All Video Distribution" – which includes SVODs in addition to MVPDs and virtual MVPDs – constitutes a relevant product market. *See* Gov't PFOF ¶ 37 (citing Tr. 2184:18-2185:17) (Shapiro). For simplicity's sake, this discussion mirrors the Government's focus on the multichannel video distribution market. *Cf.* Gov't Pre-Trial Br. 22.

i.e., the predicted increased costs to “multichannel video subscribers” – will result. *Cf.* Gov’t PFOF ¶ 231. Importantly, however, accepting the Government’s proposed product market does not mean that Turner’s position in the upstream programming market is irrelevant to evaluating the Government’s theories of harm in this case. Nor does it require this Court to ignore the rising role of SVODs in the broader multichannel video programming and distribution market. That is because the Government’s proffered increased-leverage theory, not to mention its other theories of harm, incorporates those factors in at least three different ways.

First, as will become clear in the ensuing discussion, examining the importance of Turner’s content to distributors in the upstream programming market is a necessary (but not sufficient) step in evaluating the Government’s increased-leverage theory. *Cf.* Gov’t PFOF ¶¶ 69-102 (proposing findings of fact to support assertion that the “merger would enable AT&T to harm competition because MVPDs and virtual MPVDs need Turner content to compete effectively”). *Second*, the bargaining model from which the Government’s measures of consumer harm are derived itself accounts for the increasing role of SVODs and “cord cutting” in the market, as those trends affect the amount of benefits that AT&T could expect to receive under the Government’s increased-leverage theory. *See, e.g.*, Tr. 2242:2-18 (Shapiro) (discussing role of “cord cutting” in calculating the bargaining model’s “diversion rate” input); *id.* at 2504:11-2506:24 (Carlton) (explaining why cord cutting “matters a lot” to bargaining model). *Third* and finally, the Government has argued that certain documents reflect an intent on the part of defendants to use the proposed merger to act consistently with the Government’s increased-leverage

theory of harm, among other theories. *See* Gov't PCOL ¶ 51 (stating, in relation to "[d]efendants' internal documents," that "[e]vidence of anticompetitive intent can also form the basis of a court's prediction of harm"). To appropriately evaluate the strength of such evidence, however, I must be able to put it in the context of other documents and statements related to the various rationales for the proposed merger including, of most relevance here, defendants' asserted desire to compete with SVODs and other technology companies amid "the ongoing revolution in video programming and distribution." Defs.' PFOF ¶ 6; *see also* Tr. 3079:18-3080:2 (Bewkes (Time Warner)). Therefore, although the Government is of course correct that the refrain "we are getting killed by new competition in different markets" is no "defense to an illegal merger," Gov't Post-Tr. Br. 21, I simply cannot evaluate the Government's theories and predictions of harm, as presented by the Government at trial, without factoring in the dramatic changes that are transforming how consumers view video content.

Geographic Markets. The Government has identified over 1,100 local multichannel video distribution markets as the relevant geographic markets. *See* Gov't PFOF ¶ 41. These local markets, which the Government calls "Local Footprint Overlap Zones," represent each local geographic area in which "residents have access to video offerings from the same set of MVPD competitors." *Id.*; *see* Tr. 2187:3-25 (Shapiro). The localized geographic markets reflect the reality that, due to limitations of the physical transmission paths maintained by many of the providers in the multichannel video distribution market, the mix of MVPDs and virtual MVPDs available to a consumer varies based upon where that consumer lives. *See* Gov't PFOF ¶ 40. As such, the Government

contends that the asserted “effects of the proposed merger” will vary depending “on the market shares of the various MVPDs and virtual MVPDs in [a] region,” and that analyzing the local markets is therefore appropriate. *Id.* The Government has not relied upon harm in any particular local market as the basis for enjoining the merger, however. Instead, the Government’s expert “aggregated” all of the alleged harms in the local markets in order to derive a total measure of nationwide economic harm. Gov’t PFOF 13 (“Relevant downstream geographic markets are local, but they can be aggregated for analytical convenience.”); *see* Tr. 2255:1-2256:15 (Shapiro) (providing aggregate estimates of consumer harm nationwide).

II. Conceded Consumer Benefits of Proposed Merger

Vertical mergers often generate efficiencies and other procompetitive effects. *See supra* pp. 53-57 & nn. 17, 19. The proposed merger is no exception. Indeed, the Government concedes that this case implicates one “standard benefit” associated with vertical mergers: the elimination of double marginalization (“EDM”). Tr. 2438:6 (Carlton); Gov’t PFOF ¶ 222.

As relevant here (and at the risk of oversimplifying things), double marginalization refers to the situation in which two different firms in the same industry, but at different levels in the supply chain, each apply their own markups (reflecting their own margins) in pricing their products. *See* Tr. 2251:15-25 (Shapiro). Those “stacked” margins are both incorporated into the final price that consumers have to pay for the end product. *Id.* at 2251:24. By vertically integrating two such firms into one, the merged company is able to

“shrink that total margin so there’s one instead of two,” leading to lower prices for consumers. *Id.* at 2252:1-3. EDM is, therefore, procompetitive.

In the context of a Time Warner and AT&T combination, EDM will play out as follows. Prior to the merger, AT&T must pay Time Warner a certain price to display Turner content to its DirecTV customers. *Id.* at 2251:19-25. The price that AT&T pays includes Time Warner’s profit margin, that is, an amount over and above the marginal cost of the programming. *Id.* After the vertical integration of AT&T and Time Warner, however, AT&T will no longer need to pay Turner’s profit margin to display Turner content. *See id.* at 2252:1-3; *id.* at 2438:9-15 (Carlton). In effect, that means that AT&T’s marginal cost of licensing Turner content will be lower, which in turn renders distribution of Turner to its DirecTV customers more profitable. *Id.* at 2438:13-15 (Carlton). With its profits increased, AT&T would have the “incentive to get more customers and in particular AT&T’s price, the DirecTV price will go down to consumers.” *Id.* at 2438:16-18.

According to the Government’s expert, Professor Shapiro, EDM would result in AT&T lowering the price for DirecTV by a “significant” amount: \$1.20 per-subscriber, per-month. *Id.* at 2252:6-7 (Shapiro). All told, those savings to AT&T’s customers add up to \$352 million annually. *See id.* at 2252:19-21. Those savings, moreover, would begin flowing to AT&T’s customers “pretty quickly” after consummation of the merger. *Id.* at 2446:4-5 (Carlton).

All sides agree that any proper antitrust analysis of the proposed merger must account for those “positive elements of the merger in terms of DirecTV, having lower costs.” *Id.* at 2182:12-13 (Shapiro); *cf.* Gov’t PFOF ¶¶ 222-23. In other words, to

understand whether the proposed merger will harm consumers, Professor Shapiro explained, it is necessary to “balance” whether the Government’s asserted harms outweigh the merger’s conceded consumer benefits. Tr. 2180:24, 2181:1-6 (Shapiro); *see id.* at 2182:11-21 (“So I’m going to need to trade those off. This is somewhat different than horizontal merger analysis. We’re talking about vertical merger analysis here.”). With that important principle in mind, I will now examine whether the Government has met its burden under Section 7.

III. The Government Has Failed to Meet Its Burden to Show That the Proposed Merger Is Likely to Substantially Lessen Competition by Increasing Turner’s Bargaining Leverage in Affiliate Negotiations

The Government’s primary theory of harm to competition focuses on the challenged merger’s integration of Turner’s important video content – content that includes, among other things, the networks CNN, TNT, and TBS – with AT&T’s video distributors, U-verse and DirecTV.²² Specifically, the Government contends that, should the challenged merger proceed, Turner’s relationship with AT&T will enable Turner to extract greater prices from AT&T’s rival distributors for its “must-have” content than it could without the merger. *See, e.g.*, Compl. ¶¶ 31-38. The Government argues that distributors would then pass on those price increases to their subscribers, resulting in an increase of hundreds of millions of dollars in annual consumer payments. *Id.* ¶ 39; Gov’t PFOF ¶¶ 231-232.

According to the Government, it carried its burden to support its increased-leverage theory of harm to competition by offering what it refers to as “real-world objective

²² For purposes of this section, the Court at times refers to AT&T’s collective distribution offerings as “DirecTV.”

evidence” – namely, statements contained within defendants’ prior regulatory filings and internal business documents as well as testimony from third-party competitor witnesses. Gov’t PCOL ¶ 21. To further corroborate its increased-leverage theory and predict the consumer harm that would be generated, the Government also relied on testimony and economic modeling proffered by Professor Carl Shapiro. Professor Shapiro opined that a post-merger Turner would be able to extract greater affiliate fees from distributors due to increased bargaining leverage Turner would gain on account of its relationship with AT&T. Citing the results of his economic models, Professor Shapiro predicts that such increased leverage would lead to total, annual consumer harms that outweigh the conceded \$352 million in annual cost savings that the proposed merger would generate for AT&T’s customers. *See, e.g.*, Tr. 2253:4-15 (Shapiro).

Not surprisingly, the defendants vigorously disagree with the Government’s increased-leverage theory of harm. To start, defendants argue that the Government has failed to put forward any “meaningful real-world evidence” to support the premise that a post-merger Turner would benefit from increased bargaining leverage with distributors on account of its relationship with AT&T. Defs.’ PFOF ¶ 81. If anything, defendants argue, analysis of real-world pricing data demonstrates that prior instances of vertical integration in this industry have not produced the increased-leverage effects that the Government predicts. *Id.* ¶¶ 95-102. Defendants also challenge Professor Shapiro’s testimony, arguing that it lacks sufficient basis in the facts of this industry and reflects results based on a model riddled with improper inputs and faulty assumptions. *Id.* ¶¶ 86-94, 105, 111-13, 188, 204.

In evaluating these competing contentions, the Court unfortunately does not have the luxury of looking to judicial precedents applying the increased-leverage theory in the context of a Section 7 challenge to a vertical merger. Indeed, the Government has not pointed to *any* prior trials in federal district court in which the Antitrust Division has successfully used this increased-leverage theory to block a proposed vertical merger as violative of Section 7. *Cf.* Tr. 2390:2-4 (Shapiro) (noting, with respect to proffered economic bargaining model, that “[w]hat’s less common is to use it to evaluate a merger or a vertical merger especially”); Defs.’ PCOL ¶ 32. Thus, in this matter of first impression, I must determine whether the evidence adduced at trial is sufficient to support the Government’s assertion that Turner will likely gain increased bargaining leverage in affiliate negotiations on account of the proposed merger and, if so, whether any increased distributor or consumer costs stemming from the increased bargaining leverage will result in a substantial lessening of competition under Section 7.

Having heard and considered the evidence adduced at trial, I conclude that the Government has failed to clear the first hurdle of showing that the proposed merger is likely to increase Turner’s bargaining leverage in affiliate negotiations; I thus need not consider the separate legal question of whether any effects associated with the Government’s increased-leverage theory would result in a substantial lessening of competition for purposes of the Clayton Act’s prohibitions.²³ Before explaining that conclusion, I need to

²³ On that score, defendants argue that “even taken at face value, the Government’s projected price effects do not state a claim under the Clayton Act.” Defs.’ PCOL 159 (capitalization altered); *see also id.* ¶¶ 31-33. In particular, defendants point out that the miniscule per-consumer price increases of approximately 27-cents per month relied on by the Government would not prevent AT&T’s rival distributors from competing in the marketplace or otherwise “impair[] their ability to discipline” AT&T’s

briefly review the basics of affiliate negotiations and the Government’s increased-leverage theory of harm. With that background established, I will examine the evidence put forward by the Government to support its argument that the challenged merger would likely increase Turner’s bargaining leverage with distributors and thereby enable it to secure greater affiliate fees than it could without the merger. Ultimately, as I will explain, the Government’s proof at trial falls *far* short of establishing the validity of its increased-leverage theory.

A. Background of Increased-Leverage Theory of Harm

As previously discussed, the terms under which distributors may license and display programmers’ content are set through a “very tough” series of affiliate negotiations. Tr. 1023:2 (Breland (Turner)); *see supra* pp. 14-18. As with any type of bargaining, each party to an affiliate negotiation attempts to take advantage of its points of leverage, and “reaching a deal in the end can come down to a battle of the competing bargaining leverages.” Tr. 1025:20-22 (Breland (Turner)); Gov’t PFOF ¶ 154. In the event an affiliate negotiation is unsuccessful, the distributor will lose the rights to display the programmer’s content to its

prices; indeed, they claim that competition would be promoted by the challenged merger’s conceded vertical integration effect of lowering AT&T’s prices to its projected consumers. *Id.* ¶¶ 31-32; *cf. Comcast Cable Comms., LLC v. FCC*, 717 F.3d 982, 990 (D.C. Cir. 2013) (Kavanaugh, J., concurring) (“Vertical integration and vertical contracts become potentially problematic only when a firm has market power in the relevant market.”).

For the reasons given by defendants, the Court harbors serious doubts that the Government’s proffered affiliate fee increases to AT&T’s rivals or the resulting 27-cent per-month subscriber cost increases would, if proven, constitute a “substantial lessening of competition” for purposes of Section 7. 15 U.S.C. § 18. As just noted, however, I need not rest this opinion on that legal conclusion. That is because, for all of the reasons provided in the section that follows, the Government has failed to carry its burden to put forward adequate evidence to show that there are likely to be *any* price increases (much less price increases that outweigh the conceded EDM benefits to consumers) either to AT&T’s rival distributors or their subscribers under its increased-leverage theory.

customers. Such a situation is known in the industry as a programming “blackout,” or “going dark.” Tr. 129:4-9 (Fenwick (Cox)).

Blackouts have significant, if not “catastrophic,” negative consequences for programmers – in the form of lost advertising and affiliate fee revenues. *Id.* at 1128:7-12 (Breland (Turner)); Defs.’ PFOF ¶¶ 76-77. Distributors, for their part, may lose subscribers. *See generally, e.g.*, Tr. 2197:4-2198:2 (Shapiro). In “almost every negotiation,” therefore, programmers and distributors threaten blackouts in an attempt to gain concessions. *Id.* at 1026:17-1027:3 (Breland (Turner)); *cf. id.* at 367:1-22, 376:22-377:11 (Schlichting (DISH)). Given that blackouts are negative events for both programmers and distributors, however, deals between programmers and distributors are invariably struck in order to avoid long-term blackouts. *See id.* at 138:13-15 (Fenwick (Cox)); *id.* at 1027:4-7 (Breland (Turner)); *id.* at 1359:14-15 (Montemagno (Charter)); *id.* at 3124:4-7 (Bewkes (Time Warner)). Indeed, when it comes to Turner, the record shows that there has *never* been a long-term blackout of the Turner networks. *See id.* at 2357:12-14 (Shapiro) (“Q: But to be sure there’s never been a long-term blackout of Turner, right? A: No”); Defs.’ PFOF ¶ 94. That fact is by no means lost on either side.

That background brings us to the Government’s increased-leverage theory. Notably, under that theory, the Government does *not* allege that a post-merger Turner would be incentivized to start *actually* engaging in long-term blackouts with distributors. That is so, as Professor Shapiro concedes, because withholding Turner content would not be “profitable” to the merged entity given the attendant losses in significant advertising and affiliate fee revenues. *See* Tr. 2293:9-17 (Shapiro). In other words, and in contrast to

a prevalent theory of vertical merger antitrust harm, Turner will not “foreclose” downstream distributors from accessing Turner content. *See id.* at 2218:15-16 (“This is not a foreclosure-withholding story.”); *cf. Brown Shoe*, 370 U.S. at 323-24 (stating that “[t]he primary vice of a vertical merger or other arrangement tying a customer to a supplier is that, by foreclosing the competitors of either party from a segment of the market otherwise open to them, the arrangement may act as a clog on competition” (internal quotation marks omitted)).

Instead, the Government’s increased-leverage theory of harm posits that Turner’s bargaining position in affiliate negotiations would improve after the merger due to its relationship with AT&T. That is so, the Government argues, because Turner and its distributor counterparties would recognize that, should Turner fail to strike a deal and engage in a long-term blackout with a distributor, Turner would no longer face the mere downside of losing affiliate fees and advertising revenues. *See, e.g., Gov’t Post-Tr. Br.* 1-2. Rather, some of those losses would be offset, according to the Government, by new benefits to AT&T’s video distribution companies via the following chain of events: 1) some of the rival distributor’s customers would depart or fail to join the distributor due to the missing Turner content; 2) some portion of those lost customers would choose to sign up with AT&T’s video distributors (which would have Turner); and 3) AT&T would profit from those gained subscribers. *See generally Tr.* 2197:15-2198:12 (Shapiro). As a result, the Government predicts that Turner’s downside position in the event of a blackout would improve as a result of the proposed merger. That improved downside position, according to the Government, would in turn enable Turner to demand higher prices for its content in

post-merger affiliate fee negotiations with distributors – price increases that would ultimately be passed on to consumers. *See* Compl. ¶ 38.

At trial, the Government relied on two primary categories of evidence to support its increased-leverage theory of harm. First, it offered so-called “real-world objective evidence” – namely, statements contained within defendants’ prior regulatory filings and internal business documents as well as testimony from third-party competitor witnesses. Gov’t PCOL 21. Second, the Government called an expert, Professor Carl Shapiro, to testify about its increased-leverage theory, which is based on an economic theory of bargaining known as the Nash bargaining theory, and to estimate the consumer harm associated with the increased-leverage theory. Gov’t PFOF ¶ 201. For the following reasons, neither category of evidence was effective in proving the Government’s increased-leverage theory. Accordingly, as to this theory, the Government has failed to meet its burden of proof to show that the merger is likely to result in a substantial lessening of competition.

**B. The Government’s So-Called “Real-World Objective Evidence”
Is Insufficient to Support Its Increased-Leverage Theory of Harm**

To support its increased-leverage theory of harm, the Government first points to various pieces of the so-called “real-world objective evidence” it offered at trial. Gov’t PCOL 21. That evidence primarily consisted of defendants’ ordinary course-of-business documents and excerpts of regulatory filings submitted by defendants in prior administrative proceedings, as well as the testimony of third-party witnesses from AT&T’s rival distribution companies. Of particular importance here, the Government’s so-called

real-world evidence was directed at explaining and establishing two main concepts. First, the Government sought to establish the importance of Turner content to distributors and the resulting leverage Turner enjoys in affiliate fee negotiations. Second, the Government relied on this so-called “real-world objective evidence” to substantiate its prediction that Turner’s leverage with distributors would *increase* as a result of Turner’s post-merger relationship with AT&T. Neither, however, provided persuasive support for the Government’s increased-leverage theory of harm. How so?

1. Evidence Regarding the Popularity of Turner Content Is of Limited Probative Value in Evaluating the Contention That Turner Will Gain Increased Leverage Due to the Proposed Merger

At trial, much time was spent debating the “must-have” status of Turner’s programming content. According to the Government, distributors literally ““must have”” Turner’s content in order “to compete effectively” in the video distribution industry. Gov’t Post-Tr. Br. 4; *see also id.* at 6 (“Distributors don’t just want this specific input to compete effectively, they truly need it.”); Gov’t PFOF 23 (similar). Defendants countered that the term “must have” is simply a marketing phrase used to mean “popular” and, similarly, that Turner content is not actually necessary to allow distributors to operate their businesses successfully. *See* Defs.’ PFOF ¶ 179.

Based on the evidence, I agree with defendants that Turner’s content is not *literally* “must have” in the sense that distributors cannot effectively compete without it. The evidence showed that distributors have successfully operated, and continue to operate, without the Turner networks or similar programming. *Cf.* Tr. 351:5-25 (Schlichting

(DISH)) (discussing fact that DISH’s virtual MVPD, Sling, offers packages without broadcast stations and CBS); PX144-121 (listing “[p]ast [n]etwork [d]rops” by distributors). Indeed, Stefan Bewley, a consultant who generated a slide deck with recommendations for Charter’s use in evaluating its relationships with programmers, indicated that “Charter would be better off and would save a lot of money [by] canceling Turner.” Tr. 1336:10-12 (Bewley (Altman Vilandrie)). Sling President Warren Schlichting acknowledged DISH founder and chairman Charlie Ergen made similar statements to the investment community. *See, e.g., id.* at 365:17-366:1 (Schlichting (DISH)) (conceding that Ergen stated in investor call that a Turner blackout would be “slightly cash positive for us from a cash-flow perspective”).

I therefore give little credit to blanket statements by third-party competitor witnesses indicating that the entire “viability of [their] video model” could depend on whether they offer Turner programming. *Id.* at 128:21 (Fenwick (Cox)); *see also id.* at 697:2-19 (Hinson (Cox)) (claiming that, without Turner, Cox would lack “the ability to compete” and that their customers would “go somewhere else”). Such statements were largely unaccompanied by any sort of factual analyses or, worse, contradicted by real-world examples from the witnesses themselves. *See, e.g., id.* at 128:22-129:20 (Fenwick (Cox)) (neither she nor others at Cox had done analysis of potential subscriber losses in Turner blackout); *id.* at 2947:1-13 (Holanda (RCN)) (“Q: And so today, you’re not offering this Court any empirical data or any real-world evidence of subscriber losses if RCN didn’t have Turner, right? A: No, not our company.”). *Compare id.* at 242:14-15, 352:5-7 (Schlichting (DISH)) (“[I]f you don’t have March Madness” games, half of which are

carried by Turner, “you’re not in the pay-TV business.”), *and id.* at 245:14-15 (“Q: How about CNN, why is CNN must have? A: Well, imagine coming around to midterm elections without CNN, right.”), *and id.* at 242:16-243:1 (“ABC, NBC, CBS, Fox and Time Warner are the five groups that you, you just, it’s very hard to have a pay-TV service without them.”), *with id.* at 352:1-19 (conceding that DISH’s Sling does not carry CBS, which offers the other half of the March Madness games), *and id.* at 360:18-24, 388:10-389:5 (acknowledging that DISH went dark with CNN at time of 2014 midterm elections and suffered only negligible subscriber loss), *and id.* at 351:11-21 (admitting that Sling Orange package lacks all of the “broadcast stations [and] CBS”).²⁴

Nor does those witnesses’ (or, for that matter, defendants’) use of the term “must have” to describe Turner content change things. Indeed, the evidence indicated that the term “must have” is a marketing phrase used by virtually every programmer to suggest that its content is popular with viewers. *See, e.g., id.* at 549:19-20 (Martin (Turner)) (“‘Must have’ is another way of saying, we have popular programming.”); *id.* at 899:13-16 (Rigdon (Comcast)) (agreeing that “must have is just a term of art that means something is popular”); *id.* at 1092:18-24 (Breland (Turner)) (“[M]ust have means it’s popular I

²⁴ The “must have” status of Turner content also varies based on whether the content is available for viewing through other means, such as over the internet. Former Cable ONE negotiator Randy Sejen testified, for example, that subscriber losses from a blackout of Turner’s live baseball content were mitigated by the fact that “consumers were able to wire around” the blackout by “accessing mlb.com if they needed to see a particular playoff game.” Tr. 2117:21-2118:20 (Sejen (CABLE ONE)). Along those same lines, Sejen testified that the online availability of March Madness basketball games could potentially “address the sort of must-have nature” of that content. *See id.* at 2121:11-16, 2123:1-5. I received similar evidence indicating that the availability of HBO’s content through online, direct-to-consumer platforms has lowered the value of HBO programming – and thus its leverage – in the eyes of distributors. *See, e.g., DX709.*

don't in a literal sense mean that I must have this content or I can't be successful."); *id.* at 2130:23-2131:6 (Sejen (Cable ONE)) (agreeing that he would "expect to hear" all programmers pitch their content as "must-have" and that he would "kind of take that with a grain of salt").

That said, I do nonetheless accept the Government's contention that Turner has popular content – especially live sporting events and live news – and, as a result, enjoys bargaining leverage with distributors. *See* Gov't PFOF ¶¶ 70-102 (summarizing evidence regarding Turner's importance to distributors); *id.* ¶¶ 103-177 (summarizing evidence supporting proposition that "Turner's valuable content gives it leverage in negotiations" with distributors). Importantly, however, accepting that straightforward proposition – *i.e.*, that popular programmers such as Turner are able to demand more for their content than less popular programmers – does not prove that the challenged *merger* would harm competition pursuant to the Government's increased-leverage theory of harm. To prove its increased-leverage theory, in other words, it is not sufficient for the Government to put forward evidence that Turner has important content and thus bargaining leverage – that fact is true today, pre-merger. Rather, the Government's increased-leverage theory posits that Turner's pre-merger bargaining leverage would materially increase as a result of its post-merger relationship with AT&T and that, as a result, distributors would cede greater affiliate fees than they would absent the merger.

To support that contention at trial, the Government primarily relied on defendants' own statements and documents as well as testimony of third-party competitor witnesses, most (but not all) of whom expressed concern regarding the challenged merger's potential

effects on their businesses. Neither category of evidence, however, is persuasive in proving that Turner's post-merger negotiating position would materially increase based on its ownership by AT&T.

2. Defendants' Own Statements and Documents Provide Little Support for the Contention That Turner Will Gain Increased Leverage Due to the Proposed Merger

According to the Government, defendants' own prior statements and ordinary course business documents "recognize that vertical integration poses a threat to competition" and, thus, provide convincing support for the Government's bargaining leverage claim. *See* Gov't PFOF ¶¶ 47-58. The Government points to statements made by defendants in the context of prior regulatory proceedings, and statements contained in internal documents such as slide decks and emails created by various individuals within the defendant companies. Neither category, however, was of any particular probative value. How so?

As a general matter, the Government is undoubtedly correct that "ordinary course-of-business documents, including those generated by the defendants," can be probative of whether a proposed merger is likely to result in competitive harm. Gov't PCOL ¶ 49. But as with any other piece of documentary evidence, assessing the probative value of defendants' own documents and statements requires an examination of the context, circumstances, and foundation of the proffered evidence. As such, with few exceptions, the Court denied the Government's requests to admit into evidence and cite in post-trial briefing a number of company documents for which there was no accompanying

background or foundation testimony. *See supra* pp. 46-47 & nn. 11-13. With the benefit of foundational testimony, I have considered all of the documentary and testimonial evidence from defendants' files and witnesses upon which the Government relied at trial. Having done so, I nonetheless conclude that the proffered statements and documents admitted are of such marginal probative value that they cannot bear the weight the Government seeks to place on them.²⁵

First, the Government argues that defendants' statements "made in external filings with governmental authorities" are evidence of defendants' "understanding of the anticompetitive effects that result from this transaction." Gov't PCOL ¶ 52. The statements in particular upon which the Government relies were made, either in comments or supporting expert reports filed by AT&T or DirecTV, in the course of the following FCC proceedings: 1) the 2010 review of the Comcast-NBCU merger, *see* PX1 (DirecTV); PX441 (DirecTV); 2) the 2012 proceeding to determine, *inter alia*, whether to allow one

²⁵ Before proceeding further, the Court notes a bit of confusion in the Government's position about the role of defendants' alleged "anticompetitive intent" in assessing the likely harms associated with the challenged merger. Gov't PCOL ¶ 51. In opening arguments, counsel for the Government stated, in reference to the predictive exercised called for by Section 7, that "courts don't focus on intent. What they focus on is effects, effects in the market." Tr. 10:15-16. But the Government's post-trial brief cites cases for the proposition that "[e]vidence of anticompetitive intent can also form the basis of a court's prediction of harm," while at the same time noting that "absence of evidence demonstrating anticompetitive intent . . . suggests nothing." Gov't PCOL ¶ 51 & n.12.

The Court need not toil to reconcile those positions or parse the state of our Circuit's current case law on the issue. *Compare Whole Foods Mkt.*, 548 F.3d at 1047 (Tatel, J., concurring in the judgment) ("[T]he Supreme Court has clearly said that 'evidence indicating the purpose of the merging parties, where available, is an aid in predicting the probable future conduct of the parties and thus the probable effects of the merger.'" (emphasis and internal quotation marks omitted) (quoting *Brown Shoe*, 370 U.S. at 329 n.48)), *with id.* at 1057 (Kavanaugh, J., dissenting) ("[I]ntent is not an element of a § 7 claim. . . ." (citing *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1402 (7th Cir. 1989)) ("Firms need not like their competitors; they need not cheer them on to success; a desire to extinguish one's rivals is entirely consistent with, often is the motive behind, competition.")). That is because, as discussed below, here there is nothing akin to the direct, anticompetitive intent evidence of the other cases cited by the Government in its post-trial brief.

of the FCC's program access rules to sunset, *see* PX2 (AT&T); PX442 (AT&T); PX443 (DirecTV); 3) the 2014 annual video competition proceeding, *see* PX444 (AT&T); and 4) the 2014 review of the AT&T-DirecTV merger, *see* PX467 (AT&T and DirecTV).²⁶ Not surprisingly, the Government contends that these prior statements show that defendants have previously recognized the validity of applying its increased-leverage theory to affiliate fee negotiations. *See, e.g.*, Gov't Post-Tr. Br. 2. But with that said: so what? Although I agree that a few of the proffered statements might be somewhat probative of the Government's increased-leverage theory, that limited probative value cannot, and does not, overcome the numerous insufficiencies with the Government's case discussed below.

In particular, in examining defendants' prior regulatory filing statements, I am mindful of the considerations discussed in the context of the third-party competitor testimony. *See infra* pp. 91-99. When AT&T and DirecTV made many of the proffered regulatory filings, they acted as competitors to (or customers of) distributors whose

²⁶ Just prior to the close of evidence, when the Government moved the Court to take judicial notice of certain enumerated regulatory filings, I noted that the materials filled a notebook that is about "4 inches thick of paper." Tr. 3942:4-5. Given the complex analyses and arguments contained within the voluminous filings, I noted that the Government was "at an absolute minimum . . . going to have to isolate and identify as to each document which statement or statements" it thought were relevant to the case for purposes of clearing Federal Rule of Evidence ("FRE") 403. *Id.* at 3943:23-3944:3. In response, counsel for the Government stated that the "memorandum that I handed up isolates and lists the specific statements, and I'm happy to limit to those that are identified on page 3 and 4." *Id.* at 3945:11-13. In its post-trial papers, the Government nonetheless appears to argue that the *entire* expert reports appended to the prior regulatory filings are admissible under FRE 801(d)(2) as adoptions of defendants. *See* Gov't PCOL ¶ 54 & n.13. That is largely beside the point, however. That is because the Court declines to admit those portions of the proffered expert reports and filings not "identified on page 3 and 4" of the Government's motion under FRE 403. *Id.* at 3945:11-13. In my judgment, evaluating the complicated, fact-specific arguments and analyses contained with those filings and reports would essentially require a trial within a trial (recall that not even the expert reports in *this case* were offered into evidence by the parties), the result of which would produce evidence that is only marginally probative for all of the reasons discussed below.

competitive positions would be affected by FCC review. For that reason alone, I am hesitant to assign any significant evidentiary value to those prior regulatory filings.

Finally, with respect to this particular categories of statements, I particularly decline to place much stock in the statements related to the sunseting of the FCC's ban on exclusive contracting between certain programmers and distributors. *See, e.g.*, PX2, PX442. Many of those statements relate to the issue of withholding content – something the Government's own expert concedes would *not* occur as a result of the proposed merger. *Compare* PX2-4 (“[V]ertically integrated programmers continue to have the incentive and ability to use (and indeed have used whenever and wherever they can) that control as a weapon to hinder competition to their down-stream cable affiliates *by withholding popular programming from competing MVPDs.*”) (emphasis added), *with* Tr. 2218:13-17 (Shapiro) (“I’m not saying that after the merger, Turner will deny its content to the other distributors. *This is not a foreclosure-withholding story.*”) (emphasis added). Generic statements about “mushroom[ing]” bargaining power of all programmers are similarly unhelpful to evaluating the Government's particular claims in this case. PX444-3 to -4.

That brings us to select statements made by DirecTV or AT&T that relate to vertically integrated programmers' ability to raise content prices and the use of the Nash bargaining model to estimate increased affiliate fees. *See, e.g.*, PX1-17, -83 (“[V]ertical integration of programming and distribution can, if left unchecked, give the integrated entity the incentive and ability to gain an unfair advantage over its rivals.”); PX441-5 (noting “voluminous economic and other evidence that the proposed transaction would enable Comcast to raise the prices paid by its MVPD rivals for NBCU programming”);

PX443-79 (“[V]ertically integrated MVPDs have an incentive to charge higher license fees for programming that is particularly effective in gaining MVPD subscribers than do non-vertically integrated MVPDs.”). According to the Government, those statements show that defendants recognize the validity of applying *this* bargaining model to estimate the impact of AT&T and Time Warner’s vertical integration on affiliate fee negotiations. Please !

Generic statements that vertical integration “*can*” allow the integrated entity to gain an “unfair advantage over its rivals,” PX1-17 (emphasis added), do not come close to answering the question before the Court in relation to the Government’s increased-leverage theory: whether the Government has carried its Section 7 burden to show, through proof at trial, that Time Warner will gain increased bargaining leverage in affiliate negotiations on account of the proposed merger and, if so, whether that increased bargaining leverage would result in increased distributor or consumer costs that would constitute a substantial lessening of competition under Section 7. *Cf. In re Applications of Comcast Corp.*, 26 FCC Rcd. 4238 ¶ 24 (2011) (noting differences in FCC’s “public interest” review and DOJ’s burden for “block[ing] a transaction” under Section 7). Similarly, the arguments that the Comcast-NBCU merger would harm distributors or consumers (as well the projections of harm) were, of course, informed by the state of the market at the time of the proceeding and the particular inputs to the models presented to the FCC. *See, e.g., id.* app. B (Technical Appendix) (setting out various formulae and inputs used to model potential economic harm). Given all that, defendants’ specific predictions regarding the ability of a merged Comcast-NBCU to leverage price increases by threatening to withhold the particular programming at issue is not particularly probative of whether a merged AT&T-

Time Warner could do the same with its programming in today's more competitive marketplace. *Compare id.* ¶ 41 (“We do not determine at this time whether online video competes with MVPD services.”), *with* Gov't PFOF ¶¶ 14-18 (detailing role of virtual MVPDs in “distribut[ing] linear channels and on demand content to subscribers over the internet”). Moreover, as discussed in more detail below, defendants' expert Professor Carlton concluded in an econometric analysis of content pricing following the Comcast-NBCU merger that, contrary to the predictions offered by competitors in the regulatory filings, the merger did *not* cause content prices to increase. *See infra* pp. 100-105.

That said, the Court agrees with the Government that the fact that defendants previously submitted expert reports or commentary sponsoring the use of the Nash bargaining model in the context of affiliate fee negotiations counts as a mark (albeit a faint one) against defendants' attempts to disavow the applicability of the Nash bargaining theory in this case. Unfortunately for the Government, however, my conclusion that the Government has failed to provide sufficient evidentiary support to show the Nash bargaining theory accurately reflects post-merger affiliate negotiations or the proffered bargaining model in this case does not turn on defendants' protestations that the theory is “preposterous,” “ridiculous,” or “absurd.” Gov't PFOF ¶ 47 (quoting Tr. 50:18 (Defs.' Opening); *id.* at 3119:19-24 (Bewkes (Time Warner)); *id.* at 3430:1-11 (Stephenson (AT&T))). It rests instead on my evaluation of the shortcomings in the proffered third-party competitor testimony, *see infra* pp. 91-99; the testimony about the complex nature of these negotiations and the low likelihood of a long-term Turner blackout, *see infra* pp. 14-18, 115-117 & nn.34-36; and the fact that real-world pricing data and the experiences of

individuals who have negotiated on behalf of vertically integrated entities all fail to support the Government's increased-leverage theory, *see infra* pp. 99-108. Therefore, even assigning *some* probative weight to the statements made by defendants in prior regulatory proceedings, those statements do not come close to providing a sufficient evidentiary basis to prove the viability of the Government's increased-leverage theory in this case.²⁷

Second, to prove its increased-leverage theory, the Government relies upon random statements from defendants' "ordinary course" business documents, including employees'

²⁷ The Government takes its regulatory filings argument one step further in its post-trial briefing, asserting, for the first time, that defendants' prior regulatory statements should result in them being *judicially estopped* from denying basic predicates of the increased-leverage theory of harm. Gov't PCOL ¶¶ 74-75. To say the least, that argument is a stretch. As the Supreme Court has explained, the "equitable doctrine" of judicial estoppel may be "invoked by a court at its discretion" to guard against a party's "improper use of judicial machinery" to gain an "unfair advantage." *New Hampshire v. Maine*, 532 U.S. 742, 750-51 (2001) (internal quotation marks omitted). To appropriately apply judicial estoppel against a party, the "party's later position must be 'clearly inconsistent' with its earlier position"; courts also consider whether the party has "succeeded in persuading a court to accept that party's earlier position" or would "derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped." *Id.* (internal quotation marks omitted).

Applying those factors, I easily conclude that estoppel is not appropriate here. To start, the cited prior regulatory comments are not "clearly inconsistent" with defendants' current positions: predicting that a different vertical transaction, made at an earlier time period and in a less-competitive market, will shift bargaining outcomes is *not* inconsistent with arguing that the Government has failed to carry its burden of proof to show at trial that a different transaction, proposed in the context of an even more competitive market, is likely to similarly shift outcomes (much less substantially lessen competition). *Maine*, 532 U.S. at 750; *Jankovic v. Int'l Crisis Grp.*, 822 F.3d 576, 586 (D.C. Cir. 2016) (declining to apply estoppel when party's position was not inconsistent). Although that consideration alone is fatal to the Government's estoppel argument, the Court further notes that the equities also weigh against applying estoppel here. The Government investigated the proposed merger for approximately one year before filing its suit. Disputes regarding the applicability of an increased-leverage theory as applied to the transaction have been front and center in the litigation, and were fully aired at trial. Given all that, I am hard pressed to understand how the Government would suffer an "unfair detriment" if defendants are not estopped; if anything, it would seem manifestly unfair to defendants to accept the Government's post-trial estoppel argument that much of the trial evidence can be ignored and indeed substituted with decades-old regulatory filings. Thus, even assuming that estoppel can be applied based on statements contained within *third-party* regulatory comments to prior administrative proceedings, *but see Abtew v. U.S. Dep't of Homeland Sec.*, 808 F.3d 895, 899-900 (D.C. Cir. 2015) ("[T]he rule of judicial estoppel 'generally prevents a party from prevailing in *one phase of a case* on an argument and then relying on a contradictory argument to prevail in *another phase*.'" (emphasis added) (quoting *Maine*, 532 U.S. at 749)), the Court declines the Government's last-minute invitation to estop defendants here.

emails and internal slide decks. Indeed, the Government even featured many such statements (or, more accurately, snippets of such statements) in its Complaint and pre-trial filings. However, as became clear at trial, when live witnesses take the stand a trial by slide deck leaves much to be desired !

Exemplary of this problem is a series of Government exhibits containing emails and drafts of slide decks generated prior to a merger integration meeting in 2017. *See* PX31; PX184; PX189; PX363. The Government has emphasized statements excerpted from those slide decks, contending before, during, and after trial that they highlight AT&T’s “core belief” that the merger would help it preserve the role of “[t]raditional Pay-TV” as a “cash cow business to AT&T for many years to come” by ensuring “stability through the slow, structural decline of the industry.” PX363-12 to -13; *see, e.g.*, Compl. ¶ 3 (“As AT&T/DirecTV’s strategic merger documents state, after the merger, disruption need not occur immediately – the merged firm ‘can operate [its] pay-TV business as a ‘cash cow’ while slowly pivoting to new models.’”); Gov’t Pre-Tr. Br. 2-3 (same).

At trial, however, we learned that those statements were drafted by a lower-level AT&T employee who had nothing to do with the substance of the decision to acquire Time Warner, *see* Tr. 1777:16-1778:3 (Manty (AT&T)), and in any event, were contained in a preliminary draft and were subsequently removed or changed, *see id.* at 1732:25-1733:25. To be sure, Government counsel endeavored to characterize that subsequent change as a nefarious “sanitization” by lawyers; but testimony indicated that the “whole deck changed” as a result of the parlor room process and its attendant legal review. *See id.* at 1738:7-13, 1744:8-13. *Compare* PX363 (Apr. 8, 2017), *and* PX31 (Apr. 9, 2017), *with* PX189 (Apr.

18, 2017). In the final analysis, no upper-level AT&T witness testified to ever having viewed or otherwise relied on the draft statements. To say the least, their probative value was minimal.

As it turned out, much of the Government's proffered "ordinary course" evidence went the way of those draft slide deck statements. *Compare* Tr. 1713:20-23, 1714:3-6 (Gibson (AT&T)) (confirming that internal AT&T documents stated that "NBCU could become a more formidable negotiating power" and that "[c]ontent costs could increase" as a result of the expiration of the Comcast-NBCU consent decree) (internal quotation marks omitted), *with id.* at 1712:14, 25, 1714:1-2, 9-10 (testifying that the document in question represents a "draft understanding of some pretty complicated merger conditions" designed to "brainstorm the what-ifs" of what Comcast-NBCU "may be able to do" that the team "hadn't finished"), *and id.* at 1715:20-21, 1717:17-18 (email chain, PX11, contains "first very rough understanding of" Comcast-NBCU merger conditions by "individual who reported to me regarding merger conditions for the first time"). *See also id.* at 1770:25-1771:12, 1772:16-25 (Manty (AT&T)) (showing that PX184, although sent to two AT&T senior vice presidents in July 2016, was generated in 2014 by team of lower-level AT&T employees and consulting firm members). I need not recount all of the examples here. Suffice it to say that I find that the Government frequently "overemphasized the importance and relevance" of the excerpts from defendants' documents, given that many of them, the testimony revealed, contained "informal speculation" about "rationales for the merger" or were generated by individuals "who had no decision-making role or authority in relation to the merger." *H & R Block*, 833 F. Supp. 2d at 77 n.30; *cf.* Dep't of Justice & Fed. Trade

Comm'n, Horizontal Merger Guidelines § 2.2.1 (Aug. 19, 2010) (“Horizontal Merger Guidelines”) (“The Agencies give careful consideration to the views of individuals whose responsibilities, expertise, and experience relating to the issues in question provide particular indicia of reliability.”).

In a few instances, however, the Government sought to draw evidentiary support from some of AT&T CEO Randall Stephenson’s own statements and notes. The Government pointed, for example, to an email that Stephenson sent upon being informed by Time Warner CEO Jeff Bewkes that “Time Warner had ‘taken a 10% stake in Hulu’ and that Hulu was going to launch a virtual MVPD.” Gov’t PFOF ¶ 51 (alteration omitted) (quoting PX47). In response to Bewkes’ statement that he did not think the announcement would impact AT&T’s relationship with Time Warner, Stephenson stated that it was “hard to imagine how it won’t impact all of our relationships,” continuing that AT&T is “trying to figure out how we navigate a very new world where you folks are going around us while trying to preserve the old revenue streams and business models from us.” PX47. At trial, Stephenson testified that his email indicated his concern that DirecTV Now, the new virtual MVPD AT&T was “standing . . . up” at around that same time, would get the “same access” as one of its virtual competitors, Hulu. Tr. 3475:21-22, 3477:6-7. In this Court’s view, expressing concern about how a rival virtual MVPD’s relationship with Time Warner could affect AT&T’s nascent DirecTV Now platform does little to prove how AT&T would likely behave in the event of a vertical integration.

The Government also relies on notes that Stephenson drafted to himself in preparation for an AT&T Board of Directors Meeting to discuss the merger. *See* Gov’t

PFOF ¶ 52. In those notes, Stephenson listed the following as a discussion point: “How can you advantage your own distribution (TV, BB, Wireless) without harming TW position as a wide distributor of content to other SVOD, cable networks, and broadcast networks.” DX609-8. The Government argues that this bullet point reflects “exactly the theory of the government’s case: use content to advantage distribution.” Tr. 3980:4-5 (Gov’t Closing); *see also* Gov’t PFOF ¶¶ 52-53. Not so. At trial, Stephenson testified credibly that the point of that note was to frame a discussion with his Board “that if there is a thought process that says we’re going to use this content to enhance the distribution business, that means you’re going to have to limit the distribution” and that “is counter is how you create value in one of these businesses.” Tr. 3407:16-21. That testimony mirrors the contents of a letter sent by Stephenson to all AT&T officers shortly after the announcement of the proposed merger. In that letter, known among those in defendant companies as the “Magna Carta” of the merger, Stephenson writes “[t]o Time Warner employees: We will continue to distribute Time Warner content broadly across the industry. In fact, we want to extend its distribution deeper into mobile so all wireless companies become distribution points for Time Warner content.” DX625-1; *see also* Tr. 3408:16-22 (Stephenson (AT&T)).

To be sure, the Government impugns Stephenson’s explanation, calling it “curious” and credulity “strain[ing]” in light of the testimony given about the other notes on the same page. *See* Gov’t PFOF ¶ 53; Tr. 3980:21, 3981:9 (Gov’t Closing). But even should I fail to credit Stephenson’s explanation about that particular pre-Board-meeting bullet point, the contents of that bullet point fail to meaningfully advance the Government’s case. To start, as we learned at trial, there are a number of ways in which AT&T could “advantage [its]

own distribution” through use of Time Warner content without acting in accordance with the Government’s increased-leverage theory of anticompetitive harm. *See, e.g.*, Tr. 3220:21-3221:20 (re-stacking and re-editing personalized sets of CNN news clips for access on mobile devices); *id.* at 3222:4-22 (shooting, producing, and broadcasting live sporting events in 4K resolution); *id.* at 3223:13-3224:4 (integration of social media and multi-screen functionality with content).

In short, despite the Government’s efforts to paint a contrary picture, this is not a case containing direct, probative evidence of anticompetitive intent on the part of high-level executives within the merging company. *Cf., e.g., Whole Foods Mkt.*, 548 F.3d at 1044-45 (Tatel, J., concurring in the judgment) (discussing “Project Goldmine,” as well as other merger-related documents, in which Whole Foods CEO stated, among other things, that company to be acquired is the “only existing . . . springboard for another player to get into this space” and that “[e]liminating” the company “means eliminating this threat forever, or almost forever”). Stephenson’s statements and the Government’s other proffered documentary evidence instead suggest, at the very most, that AT&T (or its third-party consultants) recognized that one *possibility* of uniting content and distribution would be to withhold or otherwise limit content from other distributors in an attempt to benefit AT&T’s distribution platforms. But evidence indicating defendants’ recognition that it could be possible to act in accordance with the Government’s theories of harm is a far cry from evidence that the merged company is likely to do so (much less succeed in generating anticompetitive harms as a result). *Cf. Baker Hughes*, 908 F.2d at 984 (“Section 7 involves *probabilities*, not certainties or possibilities.”). That is especially true when the

Government's documentary evidence is weighed against the considerable contrary evidence – including other evidence related to the motivation for the challenged merger – that came out at trial. *See, e.g.*, Defs.' PFOF ¶¶ 49-62 (collecting evidence regarding the proposed merger's ability to "enable the combined company to respond to the challenges posed by the current transformation of the video marketplace and, in so doing, bring better products and better value to consumers"); *see also supra* pp. 36-40. Thus, taking such documentary evidence for all it's worth, that evidence is only marginally probative of the viability of the Government's increased-leverage theory of harm.

3. Third-Party Competitor Witness Testimony Provides Little Support for the Contention That Turner Will Gain Increased Leverage Due to the Proposed Merger

In further support of its bargaining leverage claim, the Government called a number of third-party witnesses from AT&T's competitor video distribution companies to the stand. Although such companies are "customers" that purchase Turner content, Tr. 18:15 (Gov't Opening), all of them are also competitors of AT&T's video distribution services. *See, e.g.*, Tr. 82:7-8 (Fenwick (Cox)); *id.* at 263:19-24 (Schlichting (DISH)). Not surprisingly, most of the third-party competitor witnesses testified that they oppose the challenged merger for a number of reasons. According to the Government, that "direct industry evidence" supports its bargaining claim by describing "how the merger would increase Time Warner's leverage over distributors." Gov't Post-Tr. Br. 8. I disagree. For the reasons discussed below, the third-party competitor witness testimony fails to provide meaningful, reliable support for the Government's increased-leverage theory.

As has been observed in the context of other merger cases, I start by noting the difficulty of determining just how much weight to give the proffered third-party competitors' concerns about the challenged merger. On the one hand, such testimony can provide the Court with insight into the nature of the industry and a proposed transaction's potential effects in the market. *See* Gov't PCOL ¶¶ 48-49. On the other hand – and particularly in the context of a vertical merger case where, as here, upstream customers are downstream competitors – there is a threat that such testimony reflects self-interest rather than genuine concerns about harm to competition. *Cf. Arch Coal*, 329 F. Supp. 2d at 145 (citing 2A Areeda & Hovenkamp, *Antitrust Law* ¶ 538b, at 239 (“‘subjective’ testimony by customers” is “often unreliable”)); Horizontal Merger Guidelines § 2.2.2 (noting possibility that customers may voice opposition to merger “for reasons unrelated to the antitrust issues raised by that merger”); Tr. 2462:14-23 (Carlton) (noting that a “rival doesn’t want to see a transaction that makes it[s] competitor more efficient,” even though such a result may be “good for consumer[s]”). As in any Section 7 case, however, the central issue here is whether the Government has proffered sufficient support for the anticompetitive effects it asserts; it is not about protecting AT&T’s rivals from any and all competitive pressures they would experience should the merger go through. *Cf. Aetna*, 240 F. Supp. 3d at 18 (“[T]he Clayton Act protects ‘competition,’ rather than any particular competitor.”) (citing *Baker Hughes*, 908 F.2d at 988, 991 n.12). Caution is therefore necessary in evaluating the probative value of the proffered third-party competitor testimony. *Cf. Ken Heyer, Predicting the Competitive Effects of Mergers by Listening to Customers*, 74 *Antitrust L.J.* 87, 127 (2007) (“In evaluating the likely competitive

consequences of proposed mergers, competition authorities and courts properly weigh the totality of the evidence, refusing to take the views expressed by customers at face value and insisting that customer testimony be combined with economic evidence providing objective support for those views . . .”).

For starters, I would note that *not* all third-party witnesses provided testimony supportive of the Government’s predictions that Turner’s post-merger bargaining leverage would increase as a result of its relationship with AT&T. For example, when Comcast lead negotiator Gregory Rigdon was asked whether he believed the merger would increase Turner’s bargaining leverage, he answered in the negative, noting that he didn’t “have any reason to believe that it will impact my negotiations with Turner or HBO.” Tr. 884:5-6 (Rigdon (Comcast)). Thus, the evidence indicates that AT&T’s largest video distribution competitor – and thus a significant source of harm in Professor Shapiro’s model, *see, e.g., id.* at 2665:3-7 (Katz) – does not anticipate changing its negotiating strategy with respect to a post-merger Turner. Along those same lines, Randy Sejen, a recently-retired negotiator from Cable ONE, testified that when negotiating with a programmer, “it doesn’t matter to us who owns the network.” *Id.* at 2102:6-7 (Sejen (Cable ONE)). In short, the Government’s third-party competitor witnesses were not consistently concerned regarding Turner’s ability to demand increased affiliate fees post-merger.

It is the case, however, that other third-party competitor witnesses expressed “concern about the increased” bargaining leverage or other competitive gains on the part of Turner “that will result from the proposed transaction.” *Arch Coal*, 329 F. Supp. 2d at 145. Their testimony, however, suffered from shortcomings that, when viewed in light of

my fundamental concerns with crediting the “subjective views of customers in the market,” *id.*, undermine the probative value of their evidence in supporting the Government’s predictions of Turner’s increased-bargaining leverage.

Much of the third-party competitor testimony I heard consisted of speculative concerns regarding how the witnesses thought Turner might act in negotiations after the merger. Some witnesses simply accepted key assumptions of the Government’s increased-leverage theory without any supporting analysis or data. For example, testimony from the Government’s lead-off witness, Cox negotiator Suzanne Fenwick, helps to illustrate both of those problems. When asked on direct examination about her views of the proposed merger, Fenwick stated that she is “very concerned” that, post-merger, Cox would be presented by Turner with “a horribly ugly deal and that when faced with that deal, we have to think about that if we do go dark, they have a benefit in picking up Cox customers” via DirecTV. Tr. 107:18-21 (Fenwick (Cox)). Fenwick continued that, as a result of that “benefit that is created in this merger that isn’t there today,” the negotiating “leverage changes” and that AT&T “has a different incentive now than they had before” – namely, the incentive to “pick up customers” lost by Cox in a Turner blackout. *Id.* at 107:12-14, 108:7-9, 148:1-2.

Fenwick’s speculation about how Turner might act relies on certain key assumptions for which she had no factual basis. Indeed, the amount of customers that distributors would lose as a result of a Turner blackout (not to mention the resulting “benefit” to AT&T), is one of the central disputes in this case. Without offering any supporting analysis, Fenwick

simply assumes those figures to be in line with the Government's predictions, a point highlighted by the following exchange during cross-examination:

Q: So let's talk about that. How many customers are going to leave [Cox] even with the reduction in your price to your cable subscribers, how many?

A: We don't know.

Q: Have you tried to compute it?

A: I have not.

Q: You have no idea?

A: We believe that it's a large number.

Q: I know you believe that, but do you have any evidence, any information, any hard facts?

A: I don't have a churn analysis for you, no.

...

Q: Do you think you had an obligation in giving testimony to oppose a merger of this importance that you would do some homework and run some numbers?

A: No, we felt like our job was to point out how the leverage changes.

Q: So you think you could just come in here and give your opinion that the leverage is going to change and you're going to lose all of these customers even though you have no idea how many customers you're going to lose and you've never done a single bit of quantitative analysis; is that true?

A: Sure.

Id. at 141:1-142:5; *see also id.* at 147:22-148:10.

Testimony from other third-party witnesses suffered from similar problems. DISH Sling president Warren Schlichting testified that the merger would "kind of throw[] the card table up in the air" by placing Turner in a "win win" situation where they "can raise

prices and make more money and make us less competitive, or they can raise, they can present onerous terms that we can't accept." *Id.* at 261:24-25, 262:8-22 (Schlichting (DISH)). That was so, according to Schlichting, because DISH would lose "a lot of subs" in the event of a Turner blackout and most of those lost subscribers "would accrue to [DirecTV's] benefit." *Id.* at 262:19-21. RCN CEO Jim Holanda testified that he feared his company would lose access to certain Time Warner programming rights, even though he had no "empirical data or any real-world evidence of subscriber losses if RCN didn't have Turner." *Id.* at 2947:10-13 (Holanda (RCN)). Just as with Fenwick's testimony, Schlichting's and Holanda's contentions about Turner's post-merger position – including the amount of subscribers they would lose and AT&T would gain – assume away many of the disputed issues in this case. *Cf. id.* at 404:22-405:3 (Schlichting (DISH)) ("Q: You don't have any calculations about how many subs DISH would lose or Sling would lose if there were a blackout let's say today. . . . A: No.").

Some third-party competitor testimony even contradicted the testimony of the Government's lead expert, Professor Carl Shapiro. *Cf. Staples*, 970 F. Supp. at 1085 (declining to "give . . . much weight" to party's testimony that was "contradicted by other evidence" submitted by the party). For example, Schlichting's testimony regarding Turner's increased post-merger leverage *assumes* that Turner would profit from, or at the very least would be willing to accept, a long-term blackout of DISH. *See, e.g.*, Tr. 263:10-12 (Schlichting (DISH)) (stating that Turner may be incentivized to blackout DISH because "it's always, it's more lucrative to take subs than it is to, you know, collect programming, programming fees"); *id.* at 264:6-8 ("Q: So you would expect to be more likely to go dark

[with Turner] if the merger goes through? A: I would.”). Tom Montemagno, a lead negotiator for Charter, testified similarly. He noted that his concern with the challenged merger is “mainly around what’s going to happen with excessive price, pricing increases.” and specifically, whether Charter will “lose access to critically important content that AT&T make take exclusive away from our customers and make it harder for [Charter] to compete.” *Id.* at 1350:12-15, 1352:1-3 (Montemagno (Charter)). The assumptions reflected by that testimony – namely, that a post-merger Turner could and would go dark with DISH or Charter – run directly contrary to Professor Shapiro’s testimony that a post-merger Turner would *not* be incentivized to blackout or otherwise withhold its content from distributors. *See id.* at 2293:3-4, 14-15 (Shapiro) (Turner will “continue to license Turner content” to distributors after the merger); *id.* at 2218:13-21 (“I’m not saying that after the merger, Turner will deny its content to the other distributors.”). Indeed, when asked whether he was “aware” of Professor Shapiro’s opinion that “it would not be profitable for the merged company to withhold the Turner Networks from DISH and other distributors,” Schlichting admitted that he was not. *Id.* at 417:13-17, 418:15-16 (Schlichting (DISH)).

Other concerns raised by the third-party competitors were not particularly germane to the Government’s Section 7 allegations in this case. Charter’s Montemagno, for example, noted his concerns that the merger would harm Charter’s competitive position due to the bundling of the Turner networks and the ability of DirecTV to use advertising to appeal to Charter’s customers. *See id.* at 1405:13-18 (Montemagno (Charter)). On cross-examination, however, Montemagno conceded that “none of those issues are a result of this merger,” but instead “all exist in the marketplace today.” *Id.* at 1407:12-18; *see*

also id. at 1407:19-23 (“Q: And AT&T, DirecTV, if it wanted to buy ads on Turner or anybody else in order to try to lure your customers away, they could do that today, they could do that yesterday, couldn’t they? A: They can buy them yes.”). Holanda grounded RCN’s concerns about the challenged merger in a prior experience with Comcast-NBCU and negotiations over RCN’s “broadcast basic” package. *Id.* at 2920:6-23, 2921:2-6 (Holanda (RCN)). But that experience is not especially probative of the Government’s increased-leverage theory, given that the Turner networks do not include major broadcast programming and, in any event, that penetration rates exist in the pre-merger market. *See id.* at 2955:9-12.

Finally – and perhaps unsurprisingly given that a post-merger Turner, like a pre-merger Turner, would stand to suffer large losses in affiliate fee and advertising revenues in the event of a blackout – the record is barren of any contentions by the third-party competitors that they would actually give in to any price increases demanded by Turner as a result of its purported increase in post-merger leverage. Schlichting never testified, for instance, that DISH would in fact pay more to Turner for its content as a result of the merger, noting instead that “I don’t think we’ve quite figured out what we would do” during post-merger negotiations with Turner. *Id.* at 264:11-12 (Schlichting (DISH)). The lack of real-world evidence that Turner would likely be successful in obtaining increased fees from virtually every distributor (as Professor Shapiro’s model projects) due to its relationship with AT&T is yet another strike against the Government’s increased-leverage theory of competitive harm. *Cf. Anthem*, 855 F.3d at 360 (describing as “farfetched” the assumption that contractual negotiations will lead to the same outcome “in every instance,”

especially in light of the fact that contracts at issue were “customized relationship-driven contracts” (internal quotation marks and alteration omitted)).

In the final analysis, the bulk of the third-party competitor testimony proffered by the Government was speculative, based on unproven assumptions, or unsupported – or even contradicted – by the Government’s own evidence. Especially in view of the fact that the third-party competitor witnesses have an incentive to oppose a merger that would allow AT&T to increase innovation while lowering costs, such testimony falls far short of persuasively “show[ing] that this merger threatens” to harm competition by allowing Turner to wield increased bargaining leverage. Gov’t Post-Tr. Br. 8.

4. Real-World Evidence Indicating That Prior Vertical Integration of Programmers and Distributors Has Not Affected Affiliate Fee Negotiations Undermines the Government’s Increased-Leverage Theory of Harm

For the reasons discussed above, the Court is not convinced that the “real-world objective evidence” offered by the Government provides sufficient support for its increased-bargaining leverage claim. That conclusion is further bolstered by evidence relating to three prior instances of vertical integration in the video programming and distribution industry: 1) News Corp., a programmer, acquiring part of DirecTV in 2003 and then spinning it off in 2008; 2) the 2009 split of Time Warner, a programmer, from Time Warner Cable, a MVPD; and 3) the 2011 combination of Comcast, a distributor, and NBCU, a programmer. *See* Defs.’ PFOF ¶ 96; Tr. 2440:4-8 (Carlton). According to defendants, the econometric analysis of their chief economic expert, Professor Dennis Carlton, and witness testimony both provide significant, real-world evidence indicating

that, contrary to the Government's increased-leverage theory, those prior instances of vertical integration did not affect affiliate fee negotiations or content prices. For the following reasons, the Court agrees with defendants.

a. Professor Carlton's Econometric Analyses of Prior Vertical Transactions Found No Statistically Significant Effects on Content Pricing

When it comes to evaluating the antitrust implications of proposed mergers, both Professor Shapiro and Professor Carlton recognize that empirical analysis of prior, similar transactions can be “convincing evidence.” Tr. 2526:13 (Carlton); *see id.* at 3885:25-3886:20 (Shapiro) (agreeing with the “general thrust” of statement that “compar[ing] the observed changes from completed mergers against premerger predictions” is the “most direct way” to gauge the “reliability of different methods of evaluating proposed mergers”); *cf.* Horizontal Merger Guidelines § 2.1.2 (“The Agencies look for historical events, or ‘natural experiments,’ that are informative regarding the competitive effects of the merger. For example, the Agencies may examine the impact of recent mergers, entry, expansion, or exit in the relevant market.”). In this case, however, neither the Government nor Professor Shapiro presented original analysis of any prior vertical transactions in this industry. *See* Tr. 2337:11-13 (Shapiro) (“I did not end up doing my own separate analysis” of transactions analyzed by Professor Carlton.); *id.* at 2473:22-25 (Carlton) (“Professor Shapiro did no econometric analysis of any of the data as far as I can tell.”); *see also* Defs.’ PFOF ¶¶ 96, 99.²⁸

²⁸ Indeed, when asked in discovery whether it had a position on whether these transactions affected content prices, the Government cited to one FCC study related to the News Corp.-DirecTV transaction and

Defendants, by contrast, did seek to analyze the available pricing data resulting from prior instances of vertical integration. Although they initially had trouble obtaining some of the relevant pricing data from the Government or third-parties, *see supra* pp. 44-45, they were eventually able to obtain the data after seeking relief from this Court, *see id.*; 1/22/18 Order. Defendants' lead economic expert, Professor Dennis Carlton, then analyzed that third-party pricing data, among other proprietary and public-source data in his possession, to test whether it is "true that content prices are higher on a network when it's sold by someone who's vertically integrated." Tr. 2470:10-12 (Carlton). Specifically, Professor Carlton performed a "regression analysis or an econometric analysis, which is a statistical attempt to answer the question precisely." *Id.* at 2473:1-2. In running his regressions, Professor Carlton used different "statistical techniques to analyze the problem in a variety of ways." *Id.* at 2473:7-8.

All of that analysis, Professor Carlton testified, generated "completely consistent" results across all three examples he considered: "There's absolutely no statistical basis to support the government's claim that vertical integration in this industry leads to higher content prices." *Id.* at 2473:13, 2440:13-15; *see id.* at 2470:13-17, 2476:22-24. The "bulk of the results," Professor Carlton explained, "show no statistically significant result at all," although "many do show a *decrease*" in content prices. *Id.* at 2477:7-12 (emphasis added). Moreover, Professor Carlton noted that his results are particularly "compelling" in light of

stated that, beyond that study, "the United States does not, at this time, have a position as to whether any prior vertical integration between a programmer and a distributor resulted in higher video programming fees" or "higher prices for consumers" than "would have prevailed absent the integration." DX893-28 to -29.

the fact that the industry, as reaffirmed by numerous witnesses at trial, is “more competitive” today than at the time of the prior transactions he analyzed. *Id.* at 2476:6-9; *see also id.* at 1398:24-25 (Montemagno (Charter)) (video distribution business is “more competitive now than I’ve ever experienced in my career”); *id.* at 2134:1-3 (Sejen (Cable ONE)) (“Q: In your 31 years in the industry, have you ever seen it more competitive at the distribution level? A: No.”); *id.* at 2950:2-6 (Holanda (RCN)) (“Q: And so in the course of this 30 years that you have been in the business, the video distribution market today is more competitive than at any point that you can recall, true? A: True.”); *id.* at 3213:9 (Stankey (AT&T)) (competition in industry is “at an all-time high”). In short, based on his analysis, Professor Carlton stated that there has been “nothing like” the price increases predicted by Professor Shapiro following prior instances of vertical integration of programmers and distributors. *Id.* at 2470:19-20 (Carlton).

Although the Government and Professor Shapiro sought to undermine the basis for Professor Carlton’s conclusions at trial, those efforts were unavailing. Professor Shapiro, for his part, critiqued Professor Carlton for relying on faulty data and attempting to draw conclusions from prior transactions that are not comparable to the challenged merger. Focusing on Professor Carlton’s reliance on SNL Kagan data, Professor Shapiro stated that such data is “pretty poor” because it relies on “public sources” and reports content costs “to all of the distributors on average.” *Id.* at 3831:11-18 (Shapiro). Of course, Professor Carlton testified that he relied not only on SNL Kagan data, but also on data from third parties such as DirecTV, DISH, and Charter – all of which, when analyzed, showed no statistical pricing effects associated with the relevant prior instances of vertical integration.

Id. at 2470:4-12 (Carlton). Taking Professor Shapiro’s critiques of the SNL Kagan data on their own terms, however, those critiques miss the mark. For one thing, even Professor Shapiro acknowledged that SNL Kagan data is “commonly used” by individuals in the industry. *Id.* at 3889:3 (Shapiro); *see also, e.g., id.* at 1073:20-1074:4 (Breland (Turner)).²⁹ Moreover, it was SNL Kagan data that formed the basis of the only study of prior harm cited by the Government and Professor Shapiro. *Id.* at 3889:4-9 (Shapiro) (agreeing that FCC study that he “relied on” in his expert report was “based on Kagan data”); Gov’t Post-Tr. Br. 16 (citing same FCC study); DX893-28 (Gov’t answer to interrogatory, citing same FCC study); *see also* Tr. 2467:21-2468:9 (Carlton). For those reasons, Professor Shapiro’s criticisms of defendants’ prior transaction data does not, in this Court’s view, detract from Professor Carlton’s expert opinion that defendants’ evidence related to the prior transactions is “especially probative” when considering the Government’s claims of harm. *Id.* at 2475:21-22 (Carlton); *see id.* at 2441:13-20 (“Ignoring that evidence is a big mistake.”).

Professor Shapiro and the Government also denounced Professor Carlton’s analysis on the basis that the prior vertical transactions are not sufficiently similar to the challenged merger. They pointed out, for example, that two of the prior transactions involved regional cable distributors (Comcast and Time Warner Cable), whereas the challenged merger involves DirecTV, which operates nationally. Regional operation means, Professor Shapiro testified, that one would “not expect[] to see evidence of post-merger price

²⁹ One more witness testified to this fact in sealed testimony. Tr. 930:17-18 (SEALED).

increases beyond the overall industry increases” because “most of the MVPDs . . . don’t compete with Comcast,” for example. *Id.* at 2338:8-13 (Shapiro); *cf. id.* at 2558:18-2559:15 (Carlton). Professor Carlton explained, however, that the regional versus national distinction is “irrelevant” when it comes to his analysis of DirecTV and DISH prices; that is so, Professor Carlton stated, because those two satellite companies compete “everywhere” the regional cable companies operate and it is the “national share” that matters to Professor Shapiro’s bargaining model. *Id.* at 2474:11-17, 2560:5-11 (Carlton). To the extent the Government is now arguing that one would not expect to see *any* increased-leverage harm due to Comcast’s status as a regional distributor, I simply note that the Government argued to the contrary prior to this case. *See, generally, e.g., Compl., Comcast Corp.*, 808 F. Supp. 2d 145 (No. 11-cv-106).

Finally, the Government and Professor Shapiro note that the prior vertical transactions all were “remediated” by regulatory or court-ordered conditions – conditions that will not apply to the challenged merger. Tr. 3830:20 (Shapiro). Professor Carlton agrees that, in theory, his study’s conclusions would be affected if the conditions associated with the prior transactions were not “sufficiently similar” to those at issue here. *Id.* at 2558:12-15 (Carlton). I will thus briefly address Turner’s 2017 arbitration offer and its relation to the conditions on the Comcast-NBCU transaction.

The arbitration proceedings envisioned by Turner’s offer are similar in many of “the fundamental ways” to those blessed by the FCC, DOJ, and this Court in the Comcast-NBCU merger. Defs.’ PFOF ¶ 214 (citing Tr. 2680:1-9 (Katz)); *see also id.* ¶ 225. Most notably, both arbitration arrangements are “baseball-style”: each party puts forward a final

offer before knowing about its counterparty's offer, and the arbitrator chooses between those two. Tr. 2680:1-9 (Katz). In addition, both sets of arbitration arrangements contain "standstill provisions," which prevent the blackout of content while the arbitration is pending. *Id.* They also both set out "fair market value" as the standard, and have similar discovery procedures. *Id.* at 2680:1-13. As Professor Katz testified, "the objective is the same. The overall structure the same. So they are similar overall." *Id.*; *see also id.* at 2958:12-16 (Holanda (RCN)). Given all of these similarities, I conclude that Professor Carlton's econometric analysis of the pricing effects of the Comcast-NBCU combination can be afforded probative weight in predicting the potential pricing effects of the challenged merger.³⁰

To sum it up, neither the Government nor Professor Shapiro has given this Court an adequate basis to decline to credit Professor Carlton's econometric analysis. And that analysis, according to Professor Carlton, definitively shows that prior instances of vertical integration in the video programming and distribution industry have had no statistically significant effect on content prices.

³⁰ The parties spent a good deal of the trial debating the finer points of Turner's November 2017 arbitration offer, made shortly after the filing of the Complaint in this case. The Government asserts that the arbitration commitment must be ignored or, at the very least, must be proven binding and effective by defendants, while defendants describe its absence from Professor Shapiro's model as a critical weakness in the model's design and the Government's prima facie case. *Compare* Gov't Post-Tr. Br. 21-22, *with* Post-Trial Br. of Defs. ("Defs.' Post-Tr. Br.") 14. For purposes of this discussion, as explained below, I have confidence that Turner's arbitration offer will have real-world effect and, thus, that it is appropriate to consider Professor Carlton's econometric analysis of the Comcast-NBCU transaction. *See infra* n.51.

*b. Executives from Vertically Integrated Programmers and Distributors
Testified That Vertical Integration Does Not Affect Affiliate Fee
Negotiations*

Professor Carlton's analysis of prior vertical integration is further reinforced, defendants contend, by the consistent testimony of Comcast-NBCU and Time Warner executives that the integration of programming and distribution does not affect affiliate negotiations. I agree.

Defendants first point to the testimony from Madison Bond, who has served as a lead negotiator for NBCU during the past seven years when the company has been vertically integrated with Comcast. When questioned by defense counsel about his prior negotiations on behalf of NBCU, Bond testified that he "never once took into account the interest of Comcast cable in trying to negotiate a carriage agreement." Tr. 2014:22-24 (Bond (NBCU)). Consideration of potential Comcast gains during an NBCU blackout "doesn't factor at all" into his negotiations, Bond continued, nor has anyone from Comcast "ever asked" him "to think about that." *Id.* at 2015:1, 2015:10-12. Bond's statements were similar to testimony given by Comcast's chief negotiator, Greg Rigdon, who testified that he has never suggested, or seen a Comcast document suggesting, that NBC "should go dark on one of [Comcast's] competitors because then [Comcast] might pick up some subscribers" or that NBCU should "hold out for a little bit more in affiliate fees because that will harm" Comcast's competitors. *Id.* at 882:22-24, 883:1-11 (Rigdon (Comcast)).³¹

³¹ In response, the Government asks this Court to ignore the import of that testimony from the Comcast and NBCU witnesses on the basis that the conditions governing the Comcast-NBCU transaction would have prevented any coordination between the programming and distribution components and thus rendered such conversations between the two pointless. *See* Gov't Post-Tr. Br. 19 n.14. Please! The Comcast and NBCU witnesses' testimony aligns with testimony from witnesses not subject to the FCC

Time Warner executives testified similarly about their time at the company when it was vertically integrated with Time Warner Cable. Recalling that period, Time Warner CEO Jeff Bewkes testified that he was not aware of any Time Warner negotiator “articulating this theory of added incentive or added ability to leverage a price increase” because Time Warner was “vertically integrated with Time Warner Cable.” *Id.* at 3121:22-3122:8 (Bewkes (Time Warner)). Turner CEO John Martin, who served as CFO of Time Warner Cable at the time it was vertically integrated with Time Warner, testified along the same lines, as did Turner lead negotiators Coleman Breland and Richard Warren. *See id.* at 601:10-602:15 (Martin (Turner)) (“Q: Did you ever hear anyone say that Turner would have more leverage because Time Warner Cable and Turner were in the same family? A: No, I did not.”); *id.* at 1129:6-12 (Breland (Turner)) (“I’ve been in Turner when we were a vertically integrated company and had a sister company called Time Warner Cable. And I can tell you at no time during my tenure there did anyone ask me to consider in my negotiations and how I dealt with other distributors the outcome and impact at Time Warner Cable”); *id.* at 1190:14-15 (Warren (Turner)) (noting, when asked about Government’s increased-leverage theory, that “[w]e didn’t do that when we were part of Time Warner Cable”). Martin also testified that Time Warner’s content prices did not

order’s conditions and is also entirely consistent, as subsequently discussed, *see infra* pp. 114-117, with the goal of companywide profit maximization. *See* Tr. 601:10-602:15 (Martin (Turner)); *id.* at 1129:6-12 (Breland (Turner)); *id.* at 1190:14-15 (Warren (Turner)); *cf. id.* at 2102:6-11 (Sejen (Cable ONE)) (“I mean, it doesn’t matter to us who owns the network It really doesn’t matter.”). For that reason, among others, *see infra* nn. 34, 36, I decline the Government’s invitation to disregard the Comcast and NBCU witnesses’ testimony referenced in this section.

decrease following the spin-off of Time Warner Cable. *See id.* at 603:24-604:1 (Martin (Turner)).

The Government seems to believe that any “post-merger” testimony given by Time Warner executives should be “discount[ed]” as potentially biased because it was given by interested employees of a defendant company. Gov’t PCOL ¶ 56. Poppycock ! The testimony at issue does not involve promises or speculations about the employees’ future, post-merger behavior. Rather, it is testimony about what these executives previously experienced when working within a vertically integrated company. That testimony regarding executives’ prior experiences in the industry is uniform among all testifying witnesses and unrebutted by the Government; moreover, it finds independent support in the analysis performed by Professor Carlton. For those reasons, I decline the Government’s request to discount it.

To be sure, neither Professor Carlton’s econometric analysis nor the testimony discussed above provides “perfect evidence” of what will happen as a result of the challenged merger. Tr. 2475:15-17 (Carlton). But when weighed against the relatively weak documentary and third-party testimonial evidence proffered by the Government in support of its increased-leverage theory, the real-world evidence indicating that vertical integration has not affected content prices or affiliate negotiations further undermines the persuasiveness of the Government’s proof.

C. The Government's Expert Testimony Is Also Insufficient to Support Its Increased-Leverage Theory of Harm

In addition to offering the so-called “real-world objective evidence” set out above, the Government called noted antitrust economist, Professor Carl Shapiro, to testify in support of its increased-leverage theory. Professor Shapiro first discussed the academic underpinnings of the theory, explaining that it was grounded in an economic concept known as the Nash bargaining theory. Thereafter, Professor Shapiro opined that Turner’s post-merger leverage would increase pursuant to those economic principles. In order to predict the increased distributor costs and consumer harms that would result from Turner’s increased post-merger leverage, Professor Shapiro constructed economic models. Acknowledging that proper antitrust analysis of a proposed vertical merger requires balancing the merger’s proconsumer benefits with its harms, *see supra* pp. 52-54, Professor Shapiro testified that the challenged merger would result in annual consumer cost increases that would far outweigh the \$350 million in annual EDM savings he conceded the merger would generate. He thus concluded, based on his economic modeling, that the merger was likely to cause a substantial lessening of competition by increasing consumer costs as a result of Turner’s increased bargaining leverage.

At trial, defendants mounted a series of attacks on Professor Shapiro’s analysis. They challenged Professor Shapiro’s threshold contention that the economic theory of Nash bargaining can accurately predict the dynamics and final fee structure of complex affiliate fee negotiations. They also asserted that the theory, as applied here, rests on improper assumptions – including the notion that Turner could gain increased leverage

from threatening a long-term blackout – that negate its usefulness in evaluating the real-world effects of the proposed merger. Finally, defendants, both through their own experts and their examinations of industry witnesses, argue that Professor Shapiro’s inputs are faulty, and note further that use of the proper inputs would cause the model to predict that the merger will have a net benefit to consumers rather than a net harm. As will become clear in the section that follows, I largely agree with defendants’ various critiques of Professor Shapiro’s testimony.

For starters, I couldn’t help but notice that the more and more questions were raised during the trial about the reliability of Professor Shapiro’s theory and model, the more the Government appeared to be minimizing the importance of his analysis. *Cf.* Defs.’ Post-Tr. Br. 10 (noting Government’s attempt to “retreat from the model” in its closing argument). Indeed, during its closing argument, the Government touched on Professor Shapiro’s model relatively briefly, arguing that it simply “confirmed what the industry witnesses had already explained.” Tr. 4000:5-6 (Gov’t Closing). And the Government’s post-trial filings, for their part, all but ask the Court to overlook any failings of the model, arguing that “Section 7 does not require any quantification of harm from a price increase” and that “it would be perverse to penalize a plaintiff that does provide a quantification of the potential price increase.” Gov’t PCOL ¶ 20; *see also* Gov’t Post-Tr. Br. 15 (“[D]efendants’ critique of Professor Shapiro’s model misses the bigger picture: the model is but one part of Professor

Shapiro's opinion, and his opinion is one part of the United States' evidence."').³² Go figure !

With that, I will now turn to my own evaluation of Professor Shapiro's expert testimony. First, I will explain why the evidence is insufficient to support Professor Shapiro's conclusion that this Nash bargaining theory will accurately predict an increase of Turner's post-merger bargaining leverage in affiliate fee negotiations with distributors. Second, I will examine Professor Shapiro's economic bargaining model, concluding that the evidence is also insufficient to support the input values upon which he relied to generate his predictions of harm.

1. The Evidence Is Insufficient to Support Professor Shapiro's Conclusion That the Merger Will Increase Turner's Bargaining Leverage and, in Turn, Affiliate Fees

Relying on a particular economic bargaining theory, Professor Shapiro opines that, due to its post-merger relationship with AT&T, Turner's leverage in affiliate negotiations

³² To the extent the Government's increased-leverage theory now leans more heavily for support on the industry witness testimony and defendants' documents, as "framed" by Professor Shapiro's analysis more generally, Gov't Post-Tr. Br. 8, that shift in emphasis fails to salvage its claim given the independent problems with that so-called "real-world objective evidence" set out in the section above. *See supra* pp. 75-109; *cf.* Defs.' Post-Tr. Br. 10 ("But adding zero to zero is hardly a sound way to prove a price increase.'). In the Court's view, however, it is worth noting that the Government's retreat from Professor Shapiro's model cannot be squared with Professor Shapiro's testimony (seemingly approved by the Government) that to perform a valid "vertical merger analysis" under the applicable "consumer welfare" standard, it is necessary to "balance" or "tradeoff" the merger's proconsumer benefits with any predicted consumer harms. *See* Tr. 2180:8-2181:8, 2182:7-21, 2253:4-5 (Shapiro). At trial, that "somewhat different" "balancing" analysis of the challenged vertical merger was enabled not by the testimony of the third-party competitors or defendants' documents and statements, but by the cost-benefit predictions Professor Shapiro generated through use of his models. *See id.* at 2182:17-18, 2252:19-2253:15. For that reason, asking the Government to provide sufficient support for the proffered bargaining model is not, as the Government seems to argue, penalizing them for failure to quantify the "specific *magnitude* of the potential harm," Gov't PCOL ¶ 16, but instead is simply part and parcel of what Professor Shapiro testified is necessary to determining *whether* the proposed vertical merger will harm consumers overall.

will increase due to a reduction in financial exposure in the event of a long-term blackout. Professor Shapiro in turn opines that, as such, a post-merger Turner would be able to secure greater affiliate fees from distributors.

It is beyond dispute that, to be probative in a particular case, expert testimony must incorporate assumptions that are “reasonable” in light of the record evidence. Joint Statement 8; *cf. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 242 (1993) (“When an expert opinion is not supported by sufficient facts to validate it in the eyes of the law, or when indisputable record facts contradict or otherwise render the opinion unreasonable, it cannot support a jury’s verdict.”). Hewing to that rule is especially important in Section 7 cases, where the Supreme Court’s observation that “only” an “examination of the particular market – its structure, history and probable future – can provide the appropriate setting for judging the probable anticompetitive effect of the merger” dictates that the disputes “must be resolved on the basis of record evidence relating to the market and its probable future.” *General Dynamics*, 415 U.S. at 498 (internal quotation marks omitted); *Arch Coal*, 329 F. Supp. 2d at 116-117. “Hence,” to borrow a line from one of my able colleagues, “antitrust theory and speculation cannot trump facts.” *Arch Coal*, 329 F. Supp. 2d at 116; *accord* Gov’t PCOL ¶ 22 n.6 (quoting Steven C. Salop, *Invigorating Vertical Merger Enforcement*, 127 Yale L.J. 1962, 2018 (2018) (“[T]he direction of the net competitive effect is a question of fact, not theory. . . .”). That is true no matter whether the testimony relates to a theory that is considered “mainstream” or has been deemed applicable to different factual or economic scenarios in other proceedings.

Gov't PFOF ¶ 202; *cf.* Gov't Post-Tr. Br. 9.³³ Unfortunately for Professor Shapiro, the facts adduced at trial regarding the real-world operation of affiliate negotiations demonstrated that his testimony “rests on assumptions” that are “implausible and inconsistent with record evidence.” *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 n.19 (1986).

To start, various industry witnesses testified that the identity of a programmer's owner does not affect the negotiating dynamic. Indeed, this opinion by Professor Shapiro runs contrary to all of the real-world testimony during the trial from those who have actually negotiated on behalf of vertically integrated companies. While I need not repeat their testimony here, I would simply note that the witnesses consistently testified that they had *never* considered the identity of the programmer's owner in the course of affiliate fee negotiations. *See, e.g.*, Tr. 2014:22-2015:14 (Bond (NBCU)); *id.* at 882:22-24, 883:1-11 (Rigdon (Comcast)); *id.* at 3121:22-3122:8 (Bewkes (Time Warner)); *id.* at 601:10-602:15 (Martin (Turner)); *id.* at 1129:6-12 (Breland (Turner)); *id.* at 1190:14-15 (Warren

³³ On that score, it is notable that, although the Government states that its proffered bargaining model is “a standard model that is in economics textbooks and widely used by economists,” Gov't PFOF ¶ 202, Professor Shapiro acknowledged that, with respect to the model, “[w]hat's less common is to use it to evaluate a merger or a vertical merger especially,” Tr. 2390:2-3 (Shapiro).

To support Professor Shapiro's testimony regarding economic bargaining theory and his model, the Government contends that defendants' experts “endorsed” application of the model generally, but quibbled with the model's inputs. Gov't Post-Tr. Br. 2. That characterization is questionable, especially given Professor Carlton's extensive testimony about his conclusion that “the evidence provides no statistical support for the government's claim that prices will rise in this transaction” – statistical evidence that he considers more probative in analyzing the Government's increased-leverage theory than Professor's Shapiro's “quite . . . complicated economic model.” Tr. 2439:19-25, 2441:25 (Carlton); *see id.* at 2439:22-2441:25. Nonetheless, it is of course the Government's burden – not defendants' – to sufficiently link its proffered expert testimony to the underlying facts in the industry. It is therefore no surprise that Professor Carlton spent most of his limited time on the stand discussing the econometric studies he performed, rather than cataloguing whether the facts adduced at trial support Professor Shapiro's testimony.

(Turner)). One was left to wonder why Professor Shapiro turned a blind eye to such extensive real-world experience? When I asked Professor Shapiro about the effect of that testimony on his analysis, the following exchange ensued:

[A]: No, I am aware of that testimony. And so I think there's a very serious tension between that testimony and the working assumption for antitrust economists that Professor Carlton and I share; that the company after the merger will be run to maximize their joint profits.

...

[A]: So what I'm saying is that it will be in AT&T's interests to play this – to use this leverage in the negotiations. It will be in their interest –

The Court: So that's an assumption that you're making?

[A]: Yes, it is. Okay.

The Court: But you don't have an independent basis of evidence for that?

[A]: That is fair.

The Court: That's an economist assumption?

[A]: That is true. That is true.

...

[A]: Look, I think if you accept that, which, from my point of view, would not be in the combined interests of the new company. They would be leaving money on the table.

The Court: Okay.

[A]: If you accept that, then this bargaining leverage would not come into play.

Id. at 2199:22-2200:2, 2200:22-2201:7, 2202:6-12 (Shapiro).

The Court accepts Professor Shapiro's (and the Government's) argument that, generally, "a firm with multiple divisions will act to maximize profits across them." Gov't

Post-Tr. Br. 19; *see also* Tr. 2525:22-25 (Carlton). That profit-maximization premise is *not* inconsistent, however, with the witness testimony that the identity of a programmer's owner has not affected affiliate negotiations in real-world instances of vertical integration. Rather, as those witnesses indicated, vertically integrated corporations have previously determined that the best way to increase company wide profits is for the programming and distribution components to separately maximize their respective revenues. *See, e.g.*, Tr. 2015:16-19 (Bond (NBCU)) ("Q: And, in fact, what you were doing is trying to maximize the revenue of NBC as a programmer in those negotiations, correct? A: Yes, sir."); *see also id.* at 1129:17-18 (Breland (Turner)). In the case of programmers, that means pursuing deals "to be on all the platforms," rather than undertaking a "series of risks" to threaten a long-term blackout. *Id.* at 1129:17-22 (Breland (Turner)); *id.* at 3120:22 (Bewkes (Time Warner)). So understood, the consistent and, in this Court's judgment, credible, trial testimony is not in fact in "serious tension" with "economic logic" – just with Professor Shapiro's opinion that the identity of a programmer's owner influences negotiations ! *Id.* at 2199:22-2200:2 (Shapiro); Gov't Post-Tr. Br. 19.

Next, Professor Shapiro's opinion that Turner's post-merger relationship with AT&T will enable Turner to more credibly threaten a distributor with a long-term blackout in order to extract greater affiliate fees was severely undermined by defendants' evidence that such a blackout would be infeasible. *See id.* at 2195:4-7 (Shapiro) ("Q: Explain to His Honor why blackouts are relevant here for this discussion today. A: Well, even though they don't happen very much, that's the key to leverage, okay?"); *see also id.* at 2442:13-17 (Carlton). Indeed, the evidence showed that there has never been, and is likely never

going to be, an actual long-term blackout of Turner content. *See id.* at 2218:13-23, 2357:12-14 (Shapiro). Numerous witnesses explained,³⁴ and Professor Shapiro acknowledged, that a long-term blackout of Turner content, even post-merger, would cause Turner to lose more in affiliate fee and advertising revenues than the merged entity would gain. *Cf. id.* at 2293:2-17. Given that, there is an insufficient evidentiary basis to support Professor Shapiro’s contention that a post-merger Turner would, or even could, drive up prices by *threatening* distributors with long-term blackouts.³⁵

³⁴ Witness after witness confirmed that blackouts – and the attendant loss of distribution – have “massive implications” for Turner. Tr. 1189:13-16 (Warren (Turner)); *see also, e.g., id.* at 659:22 (Martin (Turner)) (“[I]t’s very bad for business to go dark.”); *id.* at 1128:7-1129:4 (Breland (Turner)) (“I lose money the minute I go dark. It can be catastrophic to my business”); *id.* at 3119:22-3120:22 (Bewkes (Time Warner)) (“So if our channels, any of them, are not in some distribution offering, that’s catastrophic for us. We lose a lot of money. . . . Due to the size of most of our distributors, hundreds of millions of dollars.”). During Turner’s one-month blackout with DISH in 2014, for example, Turner lost “[n]orth of 30 million dollars” in subscriber fees and advertising revenue. *Id.* at 1115:2 (Breland (Turner)). In order to end the blackout, Turner agreed to a temporary affiliate agreement extension that released DISH from any obligation to pay \$120 million in audit monies that Turner believed it was owed. *Id.* at 1118:15-19. Turner agreed to cede those funds, Turner executive Coleman Breland testified, because Turner was “bleeding” and “losing a tremendous amount of money” during the blackout. *Id.* at 1118:23-24. Given all that, it is perhaps unsurprising that, for all of the testimony about the “very intense and aggressive” nature of affiliate negotiations, *id.* at 3251:24-25 (Stankey (AT&T)), Professor Shapiro testified that Turner has *never* experienced a long-term blackout with a distributor, *see id.* at 2357:12-14 (Shapiro).

³⁵ To understand why, note that Professor Shapiro’s opinion incorporates the “key” recognition that each side’s bargaining leverage “is based on what would happen if there were no deal.” Tr. 2193:16-18 (Shapiro). Simply stated, if a party’s alternative to striking a deal improves, that party is more willing and able to push harder for a better deal because it faces less downside risk if the deal implodes. Professor Shapiro gave an example of negotiations between a seller and buyer of a used car; he noted that if the seller’s next-best offer improves, he will be able to extract a higher price from the original buyer. *See id.* at 2213:2-10. The bargaining concept the example demonstrates, Professor Shapiro explained, is that “you have more leverage now because you have a better offer. And you will be more . . . willing to apply that leverage. And some of them are willing to walk away, if necessary. . . . [B]etter outside offers make one party stronger in those negotiations.” *Id.* at 2213:13-20. Unlike the car seller, who might be “willing to walk away” and accept his alternative offer to sell the car for a gain, however, *id.* at 2213:15-16, the evidence at trial indicated that Turner would *not be willing* to accept the “catastrophic” affiliate fee and advertising losses associated with a long-term blackout, *id.* at 1128:10 (Breland (Turner)); *see supra* pp. 14-18.

It is worth emphasizing again that Professor Shapiro does *not* contend that Turner’s economics are going to somehow flip after the merger – he acknowledged, for example, that Turner would lose over \$100 million per month during a post-merger blackout with a large distributor. *Id.* at 2314:4-15; *see also id.* at 2293:3-15 (agreeing with defense counsel that Turner will “continue to license Turner content” to distributors because it would be “profitable” to do so). As a result, Professor Shapiro testified that Turner would not be incentivized to *actually* engage in a long-term blackout with a distributor:

I should say – I think we skipped over it. I’m not saying that after the merger, Turner will deny its content to the other distributors. This is not a foreclosure-withholding story. . . . I considered whether there would be withholding. And that has been a concern in some private – prior vertical mergers. And I did not think that would happen.

Id. at 2218:13-21; *see id.* at 2443:12-15 (Carlton).

In view of that evidence on the prospects of a long-term blackout, the lynchpin of Professor Shapiro’s testimony (and, accordingly the Government’s increased-leverage theory) is the *assumption* that a post-merger Turner would gain increased leverage by wielding a blackout threat that will only be somewhat less incredible. That does not make sense as a matter of logic and, more importantly, that has not been supported by sufficient real-world evidence.³⁶

³⁶ The Court finds Time Warner CEO Jeff Bewkes’ response to a question regarding the increased-leverage theory to be particularly persuasive: “And the way I – I think it’s best the way to understand it, is if we have a risk that a thousand-pound weight might fall on us – we hope it doesn’t, but if that’s always there, then if you said to me, well, don’t worry; it might be a 950-pound weight instead of a thousand pounds, are you going to think about it differently, feel differently? Are you going to take more risk that any of that might happen to you? Absolutely not.” Tr. 3120:23-3121:7 (Bewkes (Time Warner)). Although not controlling, the Court notes that some of Turner’s lead negotiators credibly testified to similar effect. *See, e.g., id.* at 1128:7-12 (Breland (Turner)) (“The concept that Turner would push” as though “going dark is good for us, I believe I’ve given examples today of why it’s just the opposite. I lose money the minute I

2. The Evidence Is Insufficient to Support the Inputs and Assumptions Incorporated into Professor Shapiro's Bargaining Model

In order to measure the increased distributor and consumer costs associated with his prediction that Turner's post-merger bargaining leverage would increase, Professor Shapiro constructed a rather complex economic bargaining model.³⁷ That model seeks to quantify the benefits that AT&T would gain as a result of a long-term, post-merger blackout of the Turner content on AT&T's rival distributors. According to Professor Shapiro, those benefits correspond to the increased affiliate fees that AT&T's rival distributors will pay as a result of Turner's increased post-merger bargaining leverage.

go dark. . ."); *id.* at 1190:14-17 (Warren (Turner)) (answering, when asked whether could gain leverage by "threatening to blackout distributors," that "I don't think that's a realistic perspective.").

On the stand, Professor Shapiro attempted to support his increased-leverage proposition by noting that programmers and distributors "think about what'll happen if there's a blackout" when formulating their negotiating strategy. *See id.* at 2193:23-2194:13 (Shapiro). The Government does the same in its post-trial filings. *See, e.g.*, Gov't PFOF ¶¶ 124-153 (collecting evidence to support proposition that "MVPDs have estimated their likely subscriber losses to inform their negotiating strategy"). The evidence showed that distributors engage in that exercise "with varying degrees of sophistication." *Id.* ¶ 124. With respect to companies that perform "go dark" analyses of the potential consequences of a blackout, the bulk of the evidence showed that negotiators relied on those analyses to get a general sense of "the value" of a programmer's content by measuring how many customers they would lose in the event of a blackout – customer losses that, notably, are not going to change as a result of the merger. *See Tr.* 935:12-16, 936:23 (SEALED); *see id.* at 1349:15-19 (Montemagno (Charter)) (reviewed the "high points" of the Altman Vilandrie go-dark analysis "[v]ery briefly"); *id.* at 1094:21-1095:1 (Breland (Turner)) (although "you never want to go dark if you are a programmer," preparing for a go dark scenario is "just prudent math"). Contrary to Professor Shapiro and the Government's arguments, such high-level evidence does not provide support for the more specific prediction that a marginal improvement in Turner's (still unprofitable) position in a blackout would meaningfully alter Turner's bargaining leverage.

In a similar way, the Government seeks to rely on the testimony of Turner executive Coleman Breland for the proposition that "Turner bargains over price down to hundredths of a penny," Gov't PFOF ¶ 108, and that Turner "almost went dark with Time Warner Cable over a single penny increase on one channel in 2012," *id.* ¶ 158. That account of Breland's testimony is "misleading at best." Defs.' PFOF 38 n.5. For the reasons set out in Defendants' proposed findings of fact, *see id.*, Breland's testimony does not bolster Professor Shapiro's model.

³⁷ Technically, Professor Shapiro used two models. He first used an economic bargaining model to generate predicted affiliate fee increases to distributors; then, he plugged those distributor cost increases into a separate merger simulation model to generate his estimates for consumer cost increases. *See Tr.* 2314:17-25 (Shapiro). As defendants' arguments focus on the design of Professor Shapiro's bargaining model rather than the merger simulation model, I will refer only to the bargaining model.

As Professor Shapiro explained at trial, his model relies on three primary inputs: 1) a figure for long-term subscriber loss, which is the total loss of subscribers a distributor would experience in the event of a long-term blackout of Turner content; 2) the diversion rate, which estimates the percentage of a distributor's lost subscribers that would sign up for AT&T's distribution services; and 3) AT&T margin data, from which Professor Shapiro calculates a measure of profits that AT&T would derive from subscribers it gains or maintains as a result of the hypothesized long-term Turner blackout. *See* Tr. 2217:15-24 (Shapiro). After selecting and entering values for those inputs and running his bargaining model, Professor Shapiro predicts that the challenged merger would lead to annual, net consumer harm ranging from \$286.5 million to \$561 million for the year 2016, with that range increasing in subsequent years. *See id.* at 2255:14-15, 3920:6-10; *id.* at 2256:16-20 (predicting \$436 million in net consumer harm for the year 2017 and \$571 million in net consumer harm for the year 2021). The low and high end of the ranges result from using different values – 9% and 14%, respectively – for the subscriber loss rate. *See id.* at 2239:3-7.

Of course, both 2016 and 2017 have passed with no merger. Thus, as Professor Shapiro concedes, his bargaining model does not “literally predict[] the price increases that will occur in negotiations in the real world.” *Id.* at 2294:18-2295:1. Rather, Professor Shapiro testified that his model is designed to “evaluate the fundamental incentives and changes in the market created by the merger.” *Id.* at 2209:11-12. For that reason, he stated that his model does not account for the existence of Turner's current affiliate agreements with distributors, which will “expire in time.” *Id.* at 2209:13-14.

Defendants attack Professor Shapiro’s bargaining model from all directions. Noting that models are “only as good as the inputs,” *id.* at 2315:11, defendants argue that each of Professor Shapiro’s three “very important” inputs lacks a sufficient basis in the trial evidence, *id.* at 2315:12. Defendants also argue that Professor Shapiro’s model improperly assumes away Turner’s current affiliate agreements – agreements that will serve to significantly constrain Turner’s post-merger bargaining leverage for years to come.³⁸ I agree with defendants, for the most part, that the inputs and assumptions of Professor Shapiro’s model are not sufficiently grounded in the evidence – a fact that “undermine[s]” my “confidence in the reliability and factual credibility” of his projections. *Anthem*, 855 F.3d at 363. How so?

a. The Evidence Is Insufficient to Support Professor Shapiro’s Long-Term Subscriber Loss Rate

In order for AT&T to benefit from a long-term Turner blackout with a rival distributor under the increased-leverage theory, a sufficient number of customers must

³⁸ Correcting for those faults, defendants argue, would cause Professor Shapiro’s model to predict a net *benefit* to consumers on account of the merger. Specifically, Professor Carlton testified that when one updates or accounts for those four factors – the long-term subscriber loss rate, the diversion rate, the margin data, and the presence of contracts – Professor Shapiro’s model generates an average 52-cent per-month, per-consumer benefit rather than an average 27-cent per-month, per-consumer harm. *See* Tr. 2516:2-6 (Carlton); *see also id.* at 2255:9-25 (Shapiro) (testifying about the “[p]redicted Turner monthly fee increases for consumers” reflected by PDX11, slide 11).

The large effects on the predicted net harm created by minor changes to Professor Shapiro’s inputs raises a separate question regarding the model’s sensitivity. As Professor Carlton noted, Professor Shapiro performed no “statistical tests” to demonstrate that the “tiny percentage” increases in harm predicted by his model are “any different from zero” statistically speaking. *Id.* at 2450:16-2451:12 (Carlton). Without such statistical testing, Professor Carlton testified, the predicted harms could fall within the range of zero “just because of normal fluctuations in how we estimate models in the perimeters [sic] of the model.” *Id.* The fact that Professor Shapiro’s model “cannot be proven to any statistical significance” provides this Court with additional cause to reject the model’s conclusions as “persuasive” evidence. *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 161 (D.D.C. 2000).

actually depart or decline to join the rival distributor due to its failure to offer Turner content. Professor Shapiro refers to that measure of lost customers as the “long-term subscriber loss rate.” At trial, Professor Shapiro testified that his model incorporates a low-end long-term subscriber loss rate of 9%, a number representing the combined percentage of current and potential subscribers who would either leave or decide not to sign up with a distributor in the event of a hypothetical long-term blackout of Turner content. *See* Tr. 2239:3-5 (Shapiro). Whether viewed as a measure of Turner’s “market power” in the programming market or not, *id.* at 2239:18, that measure of customer loss – deemed the “long-term subscriber loss” rate by Professor Shapiro – is critical to Professor Shapiro’s bargaining model and the predicted consumer harm it generates.

Of course, there has never been a long-term blackout of Turner content; Professor Shapiro thus had no “real-world” evidence on which to base his projected subscriber loss rate. *Id.* at 2394:8-11. Instead, as a basis for his chosen 9% value, Professor Shapiro relied on three principal pieces of evidence: (1) a third-party consultant slide deck commissioned by Charter in late 2016; (2) his own analyses of long-term blackouts of a different programmer, Viacom, with cable distributors Suddenlink and Cable ONE; and (3) the results of an internet survey conducted by another of the Government’s testifying experts, Professor John Hauser. *See id.* at 2225:17-2226:7. The evidence indicates, however, that each of Professor Shapiro’s sources is significantly flawed. Thus, even taken together, they fail to establish the reliability of Professor Shapiro’s long-term subscriber loss rate and the conclusions generated by his model.

1) Charter's Third-Party Consultant Slide Deck

According to Professor Shapiro, a slide deck, commissioned by AT&T's competitor Charter in late 2016 and authored by consultants at a San Francisco-based firm called Altman, Vilandrie & Company ("Altman Vilandrie"), was the "single best document and analysis" he found in coming up with a measure for the long-term subscriber loss rate. *Id.* at 2235:11-14. That was so, according to Professor Shapiro, because the slide deck, in contrast to the other available pieces of evidence, addressed "exactly" the question of interest to his analysis: the subscriber-loss effects of a long-term Turner blackout with a major distributor, as measured in *both* lost current customers and lost potential customers. *Id.* at 2235:19-20, 2236:20-2237:3. But although the slide deck may have analyzed the questions in which Professor Shapiro was interested (perhaps not so fortuitously, *see infra* pp. 127-128), the evidence shows that it did so via methodologies that were significantly flawed.

Before explaining further, it is necessary to review the basics of the slide deck's analysis. Altman Vilandrie director Stefan Bewley, who was responsible for supervising the project, explained that the slide deck was designed to examine "the value of content programming." *Id.* at 1271:23 (Bewley (Altman Vilandrie)). The slide deck, entitled "Content Valuation Project," contains charts predicting Charter's subscriber losses in the event of permanent blackouts with various programming networks. *See id.* at 1249:18-21; *see also* PX79. To generate those loss predictions, Altman Vilandrie used three different methods: (1) an internet survey, (2) set top box data, and (3) the so-called "hybrid" method, which made slight adjustments to the set top box analysis. *See* Tr. 2792:10-11, 2801:1-5.

2808:6-20 (Rossi); *id.* at 1271:24-1272:6 (Bewley (Altman Vilandrie)). Although Professor Shapiro praised that analysis for its apparent rigor, *see id.* at 2235:18-19 (Shapiro), he later conceded, despite professing that he usually does not accept data without “look[ing] into it more and figur[ing] out how reliable it is,” *id.* at 3848:10-13, that he did not take steps to evaluate the reliability of the Altman Vilandrie data before he relied on it, *id.* at 3863:21-23 (“Q. So we can establish that all you did was read the report, right? A. I relied on the report. I didn’t dig behind it.”). Rather, Professor Shapiro simply incorporated the final figure included in the slide deck’s table of results. *See* PX79-6.

Defendants’ survey and statistics expert, Professor Peter Rossi, did however examine the methods that Altman Vilandrie used to predict the reported subscriber loss rates. And in testimony that largely went unrebutted,³⁹ Rossi explained his conclusion that “[a]ll three are invalid.” Tr. 2792:5 (Rossi). Those conclusions, which I accept, are outlined below.

First, Altman Vilandrie relied on an internet survey. That survey, as Professor Rossi explained, combines three different types of internet surveys – a “conjoint,” a “channel chooser,” and a “Max Diff.” *Id.* at 2792:13-17. In the conjoint survey, respondents view eight to ten screens and are presented with different options and pricing for bundles of video programming, broadband, and telephone services; the survey seeks to infer the respondent’s willingness to trade off different service features. The channel chooser survey, for its part, tries to ascertain how much priority respondents give to a particular

³⁹ The Government did not recall any Altman Vilandrie witnesses on rebuttal to answer to Professor Rossi’s critiques.

cable network. And the Max Diff survey allows the respondent to rank the different networks. Based on its internet survey's combination of those approaches, Altman Vilandrie calculated one set of subscriber loss figures for current and prospective video customers. *See* PX 79-18.

Professor Rossi testified that the internet survey method was plagued by considerable flaws, both in the way the questions were designed and in the way the answers to those questions were used to project subscriber loss. He noted, for example, that the conjoint survey's presentation of 12 networks included only one network – CNN – owned by Turner. Tr. 2794:7-9 (Rossi). Although Professor Rossi testified to the common-sense proposition that it is “impossible” to infer the value of all of the remaining Turner networks just from CNN, apparently that is what Altman Vilandrie did with the results of the conjoint survey. *See id.* at 2793:11-14, 2800:6-11. With respect to the Max Diff survey's process for ranking channels, Professor Rossi testified that such a ranking can give a sense of relative importance, but cannot measure how much more or less important one network is than another; of particular relevance here, moreover, the ranking methodology does not define what “important” means to a respondent, and thus says “[a]bsolutely nothing” about “whether a subscriber to Charter would leave if there was a Turner blackout.” *Id.* at 2795:9-16. Finally, although Altman Vilandrie purported to combine the conjoint and Max Diff methodologies to bolster its analysis, Professor Rossi testified that such methodologies “fundamentally cannot be combined” as a matter of statistical practice. *See id.* at 2796:18-2797:4; *see id.* at 2800:16-17 (“It’s literally an impossibility, and there is absolutely no

way to combine these two.”).⁴⁰ For those reasons, Professor Rossi’s “bottom line conclusion” about the survey methodology was that it is “completely invalid.” *Id.* at 2800:22-24.

Second, Altman Vilandrie utilized a set top box methodology. Set top box data, as should now be familiar, shows the amount of time a particular cable set top box is tuned to specific channels. *See id.* at 1274:16-18 (Bewley (Altman Vilandrie)); *id.* at 2801:5-12 (Rossi). As Bewley acknowledged, set top box data does not necessarily reflect actual viewership or correlate to a particular network’s value. *See id.* at 1275:17-22 (Bewley (Altman Vilandrie)). Professor Rossi testified similarly, noting that such data, without more, “cannot possibly answer the question about the effect of removing any channel or group of channels.” *Id.* at 2802:7-8 (Rossi). In addition, because set top box data is generated by Charter’s current customers, it provides no information about “prospective customers for Charter.” *Id.* at 2801:19-24. Notwithstanding those limitations, the Altman Vilandrie slide deck purported to derive current and prospective subscriber loss figures from the set top box data by assigning differing “churn propensity” values – that is, values reflecting the likelihood that a viewer will leave a distributor – to different levels of viewing concentration. *Id.* at 2802:9-2804:14; *see* PX79-18, -68.

Professor Rossi testified, however, that the churn propensity values, and their correlation with set top box data, are “not based on data of any kind” and instead reflect

⁴⁰ Although Professor Rossi explained that Altman Vilandrie relied in part on the Sawtooth Software, which incorporates some of his own innovations in survey methodology, the combination procedure took place “outside of Sawtooth Software.” Tr. 2855:20-2856:6 (Rossi).

“purely assumed numbers.” Tr. 2804:12-13 (Rossi). Although the lack of empirical support is reason enough to disregard the slide deck’s analysis of the set top box data, that flaw is compounded by the particular values assigned in the churn propensity schedule. In particular, based on the schedule, Altman Vilandrie predicts that the loss of a network with a specified viewing concentration or greater will *always* cause a distributor’s customers to leave. *Id.* at 2807:13-20; PX79-68; DX0681-73. I agree with Professor Rossi that the upper-threshold assumption, and indeed the entire set-top box methodology, lacks a sufficient basis in evidence and is unreliable. *See* Tr. 2807:13-22.

Third, and most importantly for purposes of Professor Shapiro’s analysis, Altman Vilandrie implemented what it refers to as a “hybrid” methodology. Ultimately, the April 27, 2017 slide deck upon which Professor Shapiro relied indicates that the hybrid methodology produces a video subscriber loss rate of 9% for current customers and 10% for prospective customers. Tr. 2388:1-11, 3868:1-20 (Shapiro). Professor Shapiro testified that the 9% long-term subscriber loss rate that he incorporated into his model “reflect[s]” those results. *Id.* at 2237:4-8, 2388:1-11; *see* PX79-6, -18.

A key problem with the design of the hybrid methodology, as Professor Rossi testified, is that it blends two methods only in the sense that it alters the set top box method’s lower churn propensity threshold “based to some extent on some of the survey data.” Tr. 2808:14-18 (Rossi). In other words, the hybrid methodology can be thought of as “just a revision or alteration, minor alteration to the set-top box method.” *Id.* at 2808:19-20. The hybrid methodology is thus plagued by the same problems as is the set top box methodology, including the fact that it “can’t say anything about prospective customers.”

Id. at 2808:19-22. As a result, the hybrid methodology – and its associated 9% and 10% subscriber loss predictions for current and prospective customers – falters on the same grounds as the set top box methodology.

Moreover, evidence regarding the evolution of Altman Vilandrie’s slide deck casts further doubt on the reliability of the figures associated with the hybrid methodology. Specifically, the evidence shows that a “final read out” version of the slide deck sent to Charter on April 21, 2017 reported that the hybrid method produced a 5% and 6% subscriber loss rate for current and prospective customers, respectively. *See id.* at 1302:4-20 (Bewley (Altman Vilandrie)); 3068:1-12 (Shapiro). Almost immediately after a meeting with Charter representatives a few days later, however, Altman Vilandrie, with the “permission” of Charter, altered the results of the hybrid methodology for “just” Turner and no other programmer. *Id.* at 1310:14-1311:15 (Bewley (Altman Vilandrie)). Those alterations led to the 9% and 10% current and prospective subscriber loss rates upon which Professor Shapiro’s analysis relied. *See id.* at 3868:1-12 (Shapiro); *compare* DX681-23, *with* PX79-18.

That Turner-centric turn of events is enough alone to give me pause before accepting Professor Shapiro’s reliance on the slide deck, notwithstanding the Government’s presentation of a more benign view of the slide deck’s evolution. *See, e.g.*, Tr. 1327:16-1332:4 (Bewley (Altman Vilandrie)) (testifying, among other things, that it was Altman Vilandrie that “proposed making an exception for Turner” based on the results of the hybrid methodology as compared to the results of other methodologies). In my view, moreover, the most troubling aspect of the testimony regarding the contested changes to the slide deck

was that Professor Shapiro was entirely unaware of those changes when he “first relied on the document” to perform his analysis. *Id.* at 2365:8-10 (Shapiro); *see also id.* at 2366:4-7. At trial, Professor Shapiro admitted that he was not aware of the alterations made to the Altman Vilandrie slide deck until his pre-trial deposition by defendants. *Id.* at 2365:1-3. He nonetheless defended his reliance on the slide deck for the long-term subscriber loss figures, in no small part based on his insistence that although the current subscriber loss figure had been altered, the prospective subscriber loss figure “was not changed here.” *Id.* at 2388:1-6; *see id.* at 2366:9-11 (“If I used the five percent instead, I would get a long-term subscriber loss rate of 8.5 percent instead of nine in my calculations.”). Given that, Professor Shapiro continued, the altered current subscriber loss figure was “a lot less significant” because “it’s just one of the two components that affects the long-term subscriber rate.” *Id.* at 2388:11-15. Based on that assumption, Professor Shapiro testified that, even if one accepted the original 5% existing-customer subscriber loss figure, “[i]t’s not as though my number would go from . . . nine to five percent if you made that change. It would go from nine to 8.5” percent. *Id.* at 2388:8-10.

But Professor Shapiro “made a mistake” in so testifying, a fact he was later forced to concede on rebuttal. *Id.* at 3868:17-20. When confronted on rebuttal with the two versions of the slide deck, Professor Shapiro acknowledged that the prospective subscriber loss figure *had* indeed been changed from an original value of 6% to the 10% value upon which he relied. *Id.* at 3868:1-20. He also testified, moreover, that using the original 5% existing customer subscriber loss figure and 6% prospective subscriber loss figure would

yield a departure rate of about 5 or 6%, which in turn would “largely eliminate[] the net MVPD cost increase” he projects. *Id.* at 3870:22-3871:3.

For all of these reasons, I conclude that Professor Shapiro’s reliance on the projected long-term subscriber loss rates contained in the Altman Vilandrie slide deck was misplaced. Given Professor Shapiro’s testimony that the slide deck was the “single most important document” to him in calculating the long-term subscriber loss rate incorporated into the bargaining model, *id.* at 2360:25-2361:3, that conclusion *alone* is all but fatal to Professor Shapiro’s analysis. To the extent, however, that Professor Shapiro relied upon two other categories of evidence, such evidence also fails to support his chosen long-term subscriber loss rate.

2) Long-Term Viacom Blackouts with Suddenlink and Cable ONE

In generating his long-term subscriber loss rate, Professor Shapiro also relied on his own analysis of the effects of long-term blackouts of Viacom programming – which includes networks such as MTV and Nickelodeon – with two MVPDs, Suddenlink and Cable ONE. In particular, Professor Shapiro opined that the Viacom blackout caused Suddenlink to lose 9.4% of its video subscribers and Cable ONE to lose 16% of its video subscribers. Gov’t PFOF ¶ 208. The Court need not spill much ink addressing those figures because even a cursory review of the evidence shows that they are unreliable.

With respect to Professor Shapiro’s 9.4% figure for Suddenlink, it is notable that *Suddenlink itself* represented to the public that it suffered only a 2 to 2.5% subscriber loss as a result of the blackout with Viacom. *See* Tr. 2480:21-22 (Carlton). Given the unusual

nature of a long-term blackout, Charter, Comcast, and Wall Street power Citi also studied the event, the latter two concluding that Suddenlink's subscriber loss percentage was in the "low single digits." *Id.* at 2483:1-2; Defs.' PFOF ¶ 150. Altman Vilandrie's study for Charter produced similar results. *See* PX79-6. I heard from defendants' expert Professor Carlton that Professor Shapiro's estimates were inflated when compared to those other reported figures due to his failure to account for the fact that the rate of subscriber loss in the video distribution industry started to increase in 2016. *See* Tr. 2483:16-2484:2 (Carlton); *see also id.* at 2490:8-10.⁴¹ When Professor Carlton corrected Professor Shapiro's analysis to control for that trend, he generated a 4.8% subscriber loss rate for the Suddenlink-Viacom blackout, a number much more in line with industry estimates. *See id.* at 2484:3-8.⁴²

Professor Shapiro's 16% subscriber loss estimate for the Cable ONE long-term blackout of Viacom is even more unreliable. On that score, it is sufficient to note that Randy Sejen, Cable ONE's chief negotiator, testified that "[t]he losses attributable to Viacom are very, very small . . . and were not significant." *Id.* at 2123:21-2124:12 (Sejen

⁴¹ Professor Shapiro omitted from his analysis of industry trends December 2016 data that showed an even steeper decline in industry subscribership. When first questioned about the decision not to include this data in his analysis, Professor Shapiro did not recall that any data was omitted, and could not provide an explanation for that omission. *See* Tr. 3879:1-14 (Shapiro). When called back to the stand days later, Professor Shapiro recalled that he had noticed something "peculiar" about the omitted numbers. *Id.* at 3915:9. Professor Shapiro's testimony concerning the 2016 data was not the only time that he demonstrated a lack of familiarity with the materials he presented to the Court. *See infra* pp. 127-129, 139-140. To be clear, although both call into question his analysis, Professor Shapiro's lack of familiarity with the contents of his report and with his own data analysis presents a credibility problem separate from the problems with key inputs generated by outside sources like Altman Vilandrie.

⁴² Pursuant to the parties' representations and agreements during an April 26, 2018 bench conference related to the Suddenlink analysis, the Court will strike the following lines of trial testimony from Professor Shapiro: Tr. 3926:12-13; Tr. 3917:5-7; Tr. 3878:9-10; Tr. 3877:20-21; Tr. 3806:10-12.

(Cable ONE)). Specifically, Sejen noted that the Viacom blackout was “felt and absorbed” within four to six months and caused a subscriber loss of just 2%. *See id.* at 2130:1-4, 2123:21-24. Given Sejen’s testimony that Cable ONE lost only 2% of subscribers, the Court has no reliable basis to accept Professor Shapiro’s calculation of a subscriber loss figure eight times that amount – and therefore rejects it in toto.

To be sure, I heard evidence that, in relative terms, Turner programming is more valuable than Viacom programming. But that fact *alone* cannot make up for Professor Shapiro’s baseline failure to establish any reliable measure of subscriber losses associated with the long-term Viacom blackouts. Having concluded that Professor Shapiro’s Viacom analysis lacks an adequate basis, I will now turn to the last main piece of evidence he cited in support of his long-term subscriber loss figure.

3) Professor Hauser’s Internet Survey

The last piece of evidence upon which Professor Shapiro based his long-term subscriber loss rate is an internet survey. The internet survey was conducted by another of the Government’s testifying experts, Professor John Hauser, who heads the marketing department at the Massachusetts Institute of Technology. Tr. 756:9-14 (Hauser). The survey generated a long-term Turner blackout subscriber loss percentage of 12% and a 30-day Turner blackout subscriber loss percentage of a whopping 8.2%. *Id.* at 761:7, 803:24-804:3.

Although once at the forefront of the Government’s presentation, *see, e.g.*, Gov’t Pre-Trial Br. 29, Professor Hauser’s survey now finds itself in the background, with even Professor Shapiro minimizing his reliance on it, *see* Tr. 2360:22-24 (Shapiro) (“[Hauser’s]

twelve percent is corroborative. If I didn't rely on that, if we decided that was unreliable, it wouldn't change my opinions.”). Professor Shapiro however had good reason to unhitch his analysis from Professor Hauser's internet survey wagon: cross-examination and real-world evidence alike revealed that the survey was inherently unreliable and produced inflated results !

Before explaining that conclusion, a brief review of Professor Hauser's survey might be helpful. The survey had roughly 1,600 participants. *Id.* at 765:11 (Hauser). Those participants were drawn from an internet panel and then broken into four groups of approximately 400 participants each: three “test” groups and one “control” group. *See id.* at 775:10-14, 761:21-762:5 (Hauser). The test groups were presented with an online survey, in which they were presented with questions about their potential responses to Turner blackouts of varying lengths, including a permanent blackout, a one-month blackout, and a one-week blackout. *See id.* at 775:22-776:6. The control group was not presented with any information about a blackout. *See id.* at 776:14-18; *id.* at 2768:8-11 (Rossi).

Defendants' survey expert, Professor Rossi, testified that Professor Hauser's survey is “unreliable” for any number of reasons. *Id.* at 2768:15 (Rossi). For purposes of the analysis here, I need only discuss two.⁴³ First, Professor Rossi testified that the survey was drawn in a biased and misleading way, with the effect of overstating the importance of

⁴³ Professor Rossi also criticized Professor Hauser for failing: 1) to establish that his group of survey participants constituted a representative sample of the population of interest, and 2) to provide a margin of error – that is, a measure of reliability – for his survey's results. *See* Tr. 2771:22-2773:21, 2775:2-6 (Rossi). Although the Court agrees that those problems are notable, it sees no need to pile on by addressing them further in light of the two significant design flaws discussed below.

Turner content. Second, Professor Rossi testified that the survey's centerpiece, the intent-to-switch scale, was confusing and skewed. *See id.* at 2768:12-2769:8. After considering the expert testimony as well as other evidence calling into question the results of Professor Hauser's survey, I agree with Professor Rossi's conclusions.

First, Professor Rossi faulted Professor Hauser's survey as building in bias at the "priming" stage. *Id.* at 2786:17. Professor Hauser testified that many television viewers think about video programming in terms of specific shows or genres, not channels. *See id.* at 817:17-818:5. Professor Hauser therefore began his survey by "priming" survey respondents to connect genres of programming to specific channels through the use of network logos. *See id.* at 817:25-818:17; *see also id.* at 824:15-825:6 (sports); *id.* at 821:4-12 (special events). According to Professor Rossi, however, Professor Hauser's use of logos was problematic. In particular, Rossi noted that the internet survey "tend[ed] to visually overemphasize Turner content" relative to other content by, for example, enumerating the Turner channels in large font or inaccurately over representing the Turner networks relative to other programming. *Id.* at 2783:12, 15-17 (Rossi); *see also id.* at 2787:9-2788:25 (discussing DX915B).⁴⁴ At one point, the survey presented respondents in the test group with large Turner logos for six straight slides, despite not showing those slides to the control group. *See id.* at 838:23-839:3 (Hauser); *id.* at 2789:25-2790:8, 24-25

⁴⁴ This is not the first time Professor Hauser's "graphic effects and presentation methods" have been called into question on this basis. *See Apple, Inc. v. Samsung Elecs. Co.*, No. 11-CV-01846-LHK, 2014 WL 976898, at *10-*16 (N.D. Cal. Mar. 6, 2014).

(Rossi). As Professor Rossi explained, that priming tended to bias respondents in favor of indicating an intent to switch in the event of a Turner blackout. *Id.* at 2790:16-17 (Rossi).

Second, Professor Rossi testified that Professor Hauser’s survey asked respondents to report their answers using a scale that was confusing and, again, likely to cause respondents to overestimate their likelihood of switching distributors in the event of a Turner blackout. Professor Hauser’s survey did not squarely ask respondents whether they would switch providers in the event of a Turner blackout. Instead, the internet survey presented respondents with, as it is known in the industry, a “Juster scale” by which they answered the question, “How likely are you to switch your TV provider, on a scale from 1 to 99?” DX915-152; *see* Tr. 788:12-18, 814:1-4 (Hauser). The scale included percentages – 10%, 20%, 30%, etc. – and accompanying descriptors such as “very slight possibility,” “slight possibility,” “some possibility,” and “fair possibility.” *See* Tr. 813:15-814:19 (Hauser); DX915-152. The results of the Juster scale were translated directly into a subscriber loss rate. Thus, if each respondent rated his or her likelihood of switching at a “very slight possibility,” corresponding to 10% on the Juster scale, Professor Hauser’s survey would spin out a subscriber loss rate of 10%. *See* Tr. 815:20-816:18 (Hauser).

Professor Hauser’s Juster scale had two critical flaws: first, its text descriptions were “out of w[h]ack with the numbers,” Tr. 2778:17-21 (Rossi), and, second, Juster scales are particularly unreliable in quantifying consumer choices of this kind, *see id.* at 2779:1-2782:19. Professor Rossi put it in plain terms:

Now if I told you that I thought there was a very slight possibility that I would get into a car accident driving from Washington to Baltimore on the Baltimore Washington Parkway this evening, I don’t think you would say

that was one out of every ten times I attempted that. You might say one out of every thousand or more. So the text description is out of whack with the numbers. And that's true throughout the scale.

Id. at 2778:12-19. Professor Rossi also testified that the survey's text was bound to present skewed results because it "minimiz[ed] or neglect[ed] many aspects of switching costs" – that is, the various costs associated with switching distributors. *Id.* at 2783:13-14 (Rossi); *see also id.* at 2783:19-2786:16 (detailing different kinds of switching costs, including search costs, transactional costs, bundle-derived costs, and psychological costs, and concluding that Professor Hauser's survey failed to adequately account for those costs). That problem casts further doubt on the reliability of the survey. *Cf. H & R Block*, 833 F. Supp. 2d at 66-68 (declining to rely on "customer survey[]" results in part because survey "failed to assign" adequate "pricing" data to some of participants' response options).

More fundamentally, Professor Rossi explained, Juster scales are notoriously inaccurate when used "as an exact quantification" of the likelihood that a customer will engage in some future behavior. Tr. 2779:16-21, 2782:2-13 (Rossi). Academic literature cited by both Professors Rossi and Hauser establishes that the average correlation for predictions of this kind falls between .3 and .6. *See id.* at 2779:16-2780:5. Professor Hauser's scale, nonetheless, purports to assign a correlation value of 1.0, that is, a *perfect* linear association where intent predicts behavior virtually every time. *See id.* 2872:15-2781:2, 2872:1-4. And even that unsupported correlation "basically disappears" when respondents are asked to predict their behavior with respect to new products or situations – such as a permanent Turner blackout. *See id.* at 2780:15-24.

Given the significant questions raised about the design of Professor Hauser's survey, it should come as no surprise that the survey's results were puzzling to expert and fact witnesses alike. Gregory Rigdon, Comcast's chief negotiator, responded to Professor Hauser's one-month blackout loss estimate of 8% by noting, "[T]hat seems like a big number in one month." *Id.* at 897:2-3 (Rigdon (Comcast)). He gave the same answer when asked about the survey's long-term 12% loss estimate. *See id.* at 898:3-5 ("Q: But in terms of nay group you've ever seen dropped, have you ever seen anything approaching a 12 percent – A. That seems like a big number."). Turner CEO John Martin put things a bit more strongly, calling the survey's 8% one-month blackout subscriber loss prediction "absurd." *See id.* at 660:9-11 (Martin (Turner)). Defendants' expert Professor Carlton, for his part, said that the 8% departure rate for one month "strikes me as way too high" and is "nothing like" the Cable ONE estimate of 1.1% to 1.2% for the actual temporary Turner drop. *Id.* at 2491:4-15 (Carlton). Finally, even Professor Shapiro himself noted that Professor Hauser's one-month subscriber loss estimate of 8% "seems high." *Id.* at 2360:18.

Of course, if Professor Hauser's survey generated inflated one-month subscriber loss estimates as compared to real-world evidence, that fact "cast[s] doubt on what Professor Hauser is doing" with the survey design generally. *Id.* at 2491:4-15 (Carlton). It is therefore small wonder why both the Government and Professor Shapiro have deemphasized the role of the Hauser internet survey. All in all, I can't help but conclude that the internet survey's methods are unreliable and that its results fly in the face of real-world evidence regarding the effect of programming blackouts.

For all of the reasons discussed above, the evidence is not sufficient to support the 9% long-term subscriber loss figure that Professor Shapiro utilized in his model.⁴⁵ Because the Government has the burden of proof as well as the responsibility to demonstrate that its proffered expert testimony has an adequate grounding in evidence, the lack of evidentiary support for Professor Shapiro's input is fatal to the model's probative value in predicting the asserted harm associated with the Government's increased-leverage theory.⁴⁶

b. The Evidence Is Insufficient to Support Professor Shapiro's Diversion Rate

To evaluate the number of customers that AT&T stands to gain from a long-term Turner blackout with a rival distributor, it is necessary to estimate how many of that rival's customers "will end up as DirecTV subscribers, either by moving to DirecTV or by staying at DirecTV and not going to" the rival. Tr. 2240:9-11 (Shapiro). In Professor Shapiro's

⁴⁵ The miniscule nature of subscriber losses resulting from the two actual instances of Turner blackouts perhaps should have alerted Professor Shapiro that something was awry with his sources. The evidence showed that there have been two short-term blackouts of Turner content with distributors: 1) a thirty-day blackout with Cable ONE in October 2013, which resulted in "fairly insignificant" subscriber losses in the range of about .6%, Tr. 2116:10-13, 2127:21-2128:2 (Sejen (Cable ONE)); and 2) a thirty-day blackout with DISH in November 2014, in which some Turner networks – including CNN, but not TBS or TNT – were blacked out, resulting in a loss of less than 1% of DISH subscribers, *see id.* at 388:10-389:5 (Schlichting (DISH)). Those subscriber loss figures simply cannot be squared with some of the figures represented in the sources upon which Professor Shapiro relied.

⁴⁶ Because the evidence does not support use of Professor Shapiro's 9% "low end" long-term subscriber loss rate, it stands to reason that the larger 14% long-term subscriber loss rate he used to generate the high end of his predicted harm range is also unsupported. Tr. 3851:21-3852:8 (Shapiro). The same goes for the higher 12% and 16% long-term subscriber loss rates he used, rather curiously and contrary to the Altman Vilandrie slide deck upon which he claimed to rely, to generate the predicted harms for a 2017 and 2021 market configuration. *See* Tr. 2493:9-2495:18 (Carlton). Professor Shapiro's appeal to the fact that he predicted a range of harm is therefore unavailing: He is not "suffering the consequences of being conservative" in his estimates, Tr. 3852:1-2 (Shapiro), the consequences arise because even his conservative estimate lacks sufficient evidentiary support and reliability. The same can be said for the Government's post-trial submissions regarding the "conservative[]" nature of Professor Shapiro's analysis. Gov't Post-Tr. Br. 14.

model, that figure is known as the “diversion rate.” *Id.* at 2240:13. The diversion rates Professor Shapiro uses differ based on geography. Specifically, Professor Shapiro calculated a diversion rate for each of the local geographic markets based on an assumption that subscribers “move to the other [distributors], in each local market, to the other distributors proportional[ly] to their marketshare.” *Id.* at 2240:23-2241:1-3, 2241:15-20.

The parties’ main dispute related to diversion rate pertains to “cord cutting,” also referred to in this context as the “outside good.” *Id.* at 3871:8-9; *see id.* at 2604:13-17 (Carlton). As is likely familiar by now, an individual “cuts the cord” by discontinuing his MVPD subscription and opting instead to receive television programming through an internet-based SVOD like Netflix or Hulu. *See supra* pp. 22-23. Professor Shapiro acknowledges that, as a result of cord cutting, “[d]iversion to AT&T will be reduced to some extent because some current subscribers of a rival MVPD that would leave that MVPD due to a loss of Turner content will cancel their pay-TV service altogether” rather than “switch to AT&T or another MVPD that carries Turner.” Gov’t PFOF ¶ 215; *see Tr.* 2241:22-2242:18 (Shapiro). To account for that effect, Professor Shapiro assigns a value to cord cutting of approximately 10%. *See Tr.* 3871:8-15 (Shapiro).

According to defendants, Professor Shapiro’s 10% figure understates the rate of cord-cutting and, accordingly, results in an inflated diversion rate. *See Defs.’ PFOF* ¶¶ 182-187; *see also Tr.* 2515:16-20 (Carlton). Defendants insist that the proper cord-cutting rate is closer to 20%. *See Defs.’ PFOF* ¶ 185; *see also Tr.* 2505:10-20 (Carlton). Plugging that 20% cord-cutting rate into Professor Shapiro’s model, defendants’ lead expert Professor Carlton testified, would result in a predicted net consumer *benefit*. *See*

Tr. 2515:16-20 (Carlton) (if one uses 20% cord-cutting rate in Professor Shapiro's model, then "Professor Shapiro's 27-cent price increase on average becomes [a] 6-cent benefit, decrease"). After evaluating the evidence and the parties' arguments on cord cutting, I conclude that there is insufficient evidence to support the 10% cord-cutting figure utilized by Professor Shapiro.

The basis for Professor Shapiro's 10% figure was the (by now discredited) Altman Vilandrie slide deck, created for Charter. *See id.* at 2372:8-10 (Shapiro) ("A: Well, you relied on Altman Vilandrie for what you called the outside good, correct? A: For that part, yes, that's correct."). What I learned about the slide deck's cord-cutting figure, however, was that it was derived from the results of Altman Vilandrie's "conjoint survey." *Id.* at 2821:7-15 (Rossi). Specifically, as explained by defendants' survey expert Peter Rossi, Altman Vilandrie first looked to the measure of people who answered that they would not "take any" MVPD service in the event of a blackout with Charter. *Id.* at 2821:9-14 (Rossi); *id.* at 2242:11-15 (Shapiro). Altman Vilandrie then took those estimates, Rossi testified, and "multiplied all of those coefficients by .6 without justification" – meaning, in layman's terms, that they "cam[e] up with a figure and then reduc[ed] it by 40 percent." *Id.* at 2821:14-18 (Rossi); *id.* at 3871:16-19 (Shapiro). That reduction, in turn, produced Altman Vilandrie's cord cutting estimate of 16.8%, which Professor Shapiro used to derive his ultimate cord cutting estimate of 10%. *Id.* at 2372:19-2373:4, 3871:11-19 (Shapiro); *id.* at 2821:16-21 (Rossi); *see* PX79-38.

Although Professor Shapiro testified that he was "aware" of Altman Vilandrie's 40% reduction methodology, he could not recall whether he was aware of it at the time he

relied upon Altman Vilandrie's cord-cutting figure, or just as a result of Professor Rossi's trial testimony. Tr. 3871:16-23 (Shapiro). Moreover, Professor Shapiro was unable to explain Altman Vilandrie's choice to reduce the cord-cutting figure, stating only that his "understanding is Mr. Bewley explained he did that based on evidence that reflected market conditions in Altman Vilandrie, as part of their analysis." *Id.* at 3872:4-8. The Court, however, has been unable to locate that alleged testimony in the trial record, or in the Government's post-trial filings for that matter. *Cf.* Gov't PFOF ¶¶ 214-216 (discussing Altman Vilandrie's cord-cutting figure with no reference to Bewley testimony).

If that were not enough alone to give pause before accepting Professor Shapiro's 10% cord-cutting estimate, defendants cast additional doubt on that figure by citing to SNL Kagan data as well as to real-world evidence regarding the prevalence of cord cutting in the industry. With respect to SNL Kagan data, Professor Carlton testified that the data shows that "[a]round 20 percent" of "total TV households" are "cord cutters." Tr. 2505:12-18 (Carlton).⁴⁷ SNL Kagan's 20% figure, defendants state, aligns with other industry evidence about the extent of cord cutting. *See* Defs.' PFOF ¶¶ 183, 185. AT&T surveys of departing customers, for example, indicate that "25 to 30 percent" of those customers report that they are "going to cord cutting." Tr. 2506:19-24 (Carlton). RCN CEO Jim

⁴⁷ To be sure, the Government, through the rebuttal testimony of Professor Shapiro, attempted to rebuff Professor Carlton's 20% cord-cutting rate. Professor Shapiro pointed out that, in the context of examining the consequences of a Turner blackout, it is "pretty likely" that a departing customer would "want to go somewhere else where you can get the Turner content." Tr. 3808:11-12 (Shapiro). Thus, Professor Shapiro continued, stating that "20 percent of American households don't have pay-TV service" overall is "beside the point." *Id.* at 3808:5-6, 15. Were it defendants' obligation to provide sufficient support for the departure rate in Professor Shapiro's model, rather than Professor Shapiro's, that rebuff would perhaps be persuasive. But even accepting Professor Shapiro's point about defendants' proposed rate, that point does not prove that the departure rate *he* proffered had adequate evidentiary support.

Holanda testified that similar surveys by his company report that “at least half of the customers who leave RCN’s video services are leaving for OTT providers” – a number that Holanda predicts is “likely to grow in the future as Millennials become more and more prominent in the marketplace.” *Id.* at 2948:20-2949:3 (Holanda (RCN)). That evidence about the *increasing* presence of cord cutting in the market, in the Court’s view, undercuts yet another aspect of Professor Shapiro’s measures of cord cutting – namely, that they apparently “declin[e] over time” because of a particular “feature of his model.” *Id.* at 2448:7-9 (Carlton).

In the final analysis, it is the Government’s burden to adequately support its proffered model’s harm – and, necessarily, the model’s inputs – through the testimony of its expert or related evidence. The utter lack of explanation regarding Altman Vilandrie’s methodology for generating the cord-cutting projection upon which Professor Shapiro relied, coupled with defendants’ real-world evidence regarding the prevalence of cord cutting in the industry, leaves me with little confidence in the accuracy of Professor Shapiro’s 10% cord-cutting figure. As with the long-term subscriber loss estimates, I therefore conclude that the Government has also failed to provide adequate support for Professor Shapiro’s diversion rate estimate and thus the model’s predicted net consumer harm.

c. The Evidence Is Insufficient to Support Professor Shapiro’s Profit Margin Figure

Finally, Professor Shapiro’s last input to his model is AT&T’s monthly profit margins for its video customers. *See id.* at 2245:7-9, 2315:12-17 (Shapiro). To calculate

those monthly video margins, Professor Shapiro relied on internal AT&T figures measuring new customers' "lifetime value" to AT&T, or "LTVs." *Id.* at 2344:12-16; *id.* at 2577:13-14 (Carlton). In particular, Professor Shapiro averaged AT&T's reported LTVs for a three-month period ending in June 2016. *See id.* at 2344:12-20, 3843:13-18 (Shapiro). That average generated a profit margin of \$1,324, which Professor Shapiro used in his model to estimate the monetary benefits that AT&T would gain in the event of a long-term Turner blackout. *Id.* at 3843:21-3844:4.

Defendants argue that Professor Shapiro's 2016 LTV data is "outdated and thus not a reliable input into Professor Shapiro's model." Defs.' PFOF ¶ 188. Defendants assert that Professor Shapiro instead should have used the "latest" available LTV figure from June of 2017, or \$821. Tr. 2508:3 (Carlton); *id.* at 3844:9 (Shapiro). That \$821 figure – disclosed by an AT&T witness and Professor Carlton after Professor Shapiro's initial expert report and the close of fact discovery, but before Professor Shapiro's rebuttal report and the start of trial – is approximately 40% lower than the 2016 margin figure used by Professor Shapiro to generate his original estimates of net consumer harm. *See id.* at 2448:17-2449:1 (Carlton). Defendants argue that using the \$821 figure from 2017, rather than the \$1,324 figure from 2016, significantly reduces the net consumer harm predicted by Professor Shapiro's model. *See id.* at 2507:20-22 ("[I]f margins go down, Professor Shapiro will predict lower increases in Turner content, even in his own model."); *id.* at 2508:17-21 (using "the more up-to-date" profit margin figures "eliminates a large fraction of all [of Professor Shapiro's predicted] harms").

At trial, each side spent much time attempting to justify, or impugn, Professor Shapiro's reliance on the 2016 versus 2017 LTV data. The Government, for its part, raised questions about the genesis and legitimacy of the late-breaking 2017 margin data; on that score, it requested, and was granted, the opportunity to depose the AT&T executive responsible for compiling and producing the data. Defendants, on the other hand, questioned Professor Shapiro extensively about his continued reliance on the 2016 LTV data in the face of deposition testimony⁴⁸ and Professor Carlton's report, both of which disclosed updated 2017 LTV figures.

While I have no reason to doubt Professor Shapiro's good faith in continuing to rely upon the 2016 LTV data during his direct testimony, for present purposes, the important point is this: the trial evidence indicates that Professor Shapiro's 2016 LTV figures, and thus his measure of AT&T's margins, are outdated and too high. That is true whether they are compared against the "most current finalized" June 2017 LTV figure (\$821) cited by Professor Carlton, *id.* at 3844:18, 3849:14-23 (Shapiro), or instead against an average of all three of the 2017 LTVs that had been finalized at the time of trial, *id.* at 2585:13-22 (Carlton).

At trial, AT&T witness David Christopher testified about AT&T's method for generating the 2017 LTV data; he also confirmed the values of the finalized LTVs for

⁴⁸ Specifically, David Christopher testified to the June 2017 LTV figure during his deposition on February 14, 2018. *See* Tr. 3002:16-25. Although Professor Shapiro's report cites Christopher's deposition, on the stand Professor Shapiro admitted that he did not read that deposition transcript and did not in fact know David Christopher's role in the case. *See id.* at 2345:17-2346:3 (Shapiro) ("Q: If I told you that you cited to [Christopher's] deposition in your report, does that ring a bell? A: No. Q: Well, did you read his deposition? A: I did not.").

January, April, and June 2017. *See id.* at 3001:9-17, 3011:11-17 (Christopher (AT&T)). Although the Government rightly points out that such LTV numbers can (and, in the case of the 2017 LTVs, do) fluctuate from month to month, *see id.* at 3015:10-24, the overall “downward trend is the same,” *id.* at 3016:4; *see also id.* at 3003:15-3004:15 (discussing downward pressures on LTVs). The declining state of AT&T’s 2017 LTVs, moreover, aligns with the testimony of numerous witnesses regarding the continued decrease of video margins in the distribution industry. *See, e.g., id.* at 3852:22-25 (Shapiro) (“Q: And you are aware, sir, of the testimony of pretty much every other competitor witness in this case who has testified that their video margin are going down, right? A: Yes.”).

Given that evidence, it is perhaps unsurprising that even Professor Shapiro conceded during his rebuttal testimony that he “think[s] there’s some validity to using the 2017 margin instead of the 2016 margins.” *Id.* at 3810:10-11; *see also id.* at 3843:17-18 (“[I]t would be reasonable to use the 2017 margins if one did it in the context of the rest of my analysis.”); *id.* at 3849:5-8 (“Then when I’m given more data later and now we’ve had the trial, I understand that more; that’s why I said this time around, I could see using the 2017 data.”). Professor Shapiro also confirmed that using an average of all finalized 2017 LTVs would generate a 2016 net increase in MVPD costs of \$98 million per year – a number “significantly lower” than his original estimate of \$235 million in MVPD costs. *See id.* at 3849:24-3851:3. Those lower MVPD costs, in turn, would decrease the predicted harm to consumers from the \$.27 per-subscriber-per-month figure Professor Shapiro testified about to a figure of approximately \$.13 per-subscriber-per-month. *See id.* at 3851:6-14.

In view of the above evidence, I agree with defendants that the 2016 margin data utilized by Professor Shapiro is outdated and inflated.⁴⁹ Whether one substitutes that figure for the June 2017 LTV data or an average of all of the finalized 2017 LTV data in Professor Shapiro's model, the result is a significant decrease in the predicted amount of net consumer harm. Although that decrease, standing alone, does not eliminate all of the harms generated by Professor Shapiro's model (just the bulk of them), it provides yet another reason to reject the predictions offered by Professor Shapiro at trial.

⁴⁹ With his model's original reliance on the 2016 LTVs under attack, Professor Shapiro's rebuttal testimony doubled down on an argument relating to the value of AT&T's existing customers. The argument proceeds as follows. In addition to calculating LTVs for newly acquired video customers, AT&T assigns margin values to its existing video subscribers. Those values, known as active customer values ("ACVs"), are generally higher than LTVs because they do not account for "subscriber acquisition costs." Tr. 3854:22-3855:4 (Shapiro). Professor Shapiro's long-term subscriber loss rate includes a measure of the existing customers that AT&T will retain as a result of a long-term Turner blackout on its distribution rivals. The value of those maintained customers, Professor Shapiro opines, is likely "50 percent higher" than the margin value for new-customers. *Id.* at 2244:13-21. Professor Shapiro did not, however attempt to generate or otherwise assign a "measure of the margin on the retained subscribers." *Id.* at 2244:9-10. Instead, his model only incorporates the margin value associated with new subscribers. *Id.* at 2244:22. As a result, Professor Shapiro states that his "margin figure is definitely understated and substantially understated because I don't have the proper data on the value of the retained customers." *Id.* at 2244:14-17.

Therein lies the problem. Although opining about the importance of the value of retained customers to AT&T, Professor Shapiro undertook no analysis to incorporate that overall effect into his model. That should come as little surprise, given that this "larger point" appeared only in footnote 414 of the ninth appendix to Professor Shapiro's 300-page expert report; nonetheless, it renders his reliance on the existing-versus-new customer distinction unconvincing. *Id.* at 3809:18, 3855:5-3856:5. That footnote, Professor Shapiro testified, indicates that "the value of existing subscribers [is] between 150 and 225 percent as large as new subscribers." *Id.* at 3813:13-17. Beyond footnote 414's general observation, Professor Shapiro did not attempt to quantify the total dollar value of existing customers' margins versus new customer margins, much less incorporate a figure for existing customer margins into his model. *Id.* at 2244:22-2245:1 ("But, again, the data I have available, I'm using those gross add margins."). On rebuttal, Professor Shapiro nonetheless cited that "higher number" as "what gives me a higher end of my range" of projected harm. *Id.* at 3819:25-3820:7. That does not appear to be the case: elsewhere, Professor Shapiro testified that the "higher end" of the range derives from his use of a higher long-term subscriber loss rate of 14% (as compared to the 9% rate he chose to present to the Court during his direct testimony), rather than any alterations to other inputs, such as the margin data. *Id.* at 2259:4-8 ("I realize there are ranges here. These are based on, we're starting from the low end, 9 percent subscriber loss rate, and projecting that. So if we started with the 14 percent, we'd have higher numbers."); *see also id.* at 2239:3-7. Professor Shapiro's belated attempts to link his point regarding the increased margins for existing customers to the high-end projections he reported, or to present those increased margins as if they were quantified and incorporated into his model, are thus unavailing and further undermine the credibility of his presentation.

d. The Model's Failure to Account for the Real-World Effects of Turner's Long-Term Contracts Further Undermines Its Probative Value

Turner is currently party to long-term affiliate agreements with nearly all of its distributors. See Tr. 2316:3-18 (Shapiro); *id.* at 2444:10-23 (Carlton); *see also, e.g.*, PX211; PX410; PX422.⁵⁰ Those agreements, Professor Shapiro concedes, will “prevent [Turner] from raising the fees for some number of years” and thus “temporarily constrain[]” his predicted effects of the merger in the real- orld. Tr. 2209:8-9, 16 (Shapiro). In running his model and rendering his predictions, however, Professor Shapiro curiously chose to ignore Turner’s current affiliate agreements. At trial, Professor Shapiro explained – and anticipated cross-examination on – that choice by noting that his model is designed to “evaluate the fundamental incentives and changes in the market created by the merger.” *Id.* at 2208:21-25, 2209:4-19. In other words, Professor Shapiro’s predictive exercise requires assessing “the longer term impact of a new market structure”; factoring in Turner’s current affiliate agreements, he noted, would be counterproductive because those agreements are “temporar[y]” and will “expire in time.” *Id.* at 2209:11-19, 2320:24-2321:10.

The evidence in this case, however, shows that the real-world effect of Turner’s present affiliate agreements will be rather “significant” until at least 2021. *Id.* at 2316:14-18. Indeed, Professor Shapiro conceded that by simply factoring in the presence of one such affiliate agreement with a large distributor (which the Court will not name for

⁵⁰ The primary exception is Charter, which has been displaying Turner content pursuant to temporary, short-term extensions of the companies’ affiliate agreement, which initially expired in 2016. See Tr. 1353:21-1354:3 (Montemagno (Charter)).

confidentiality purposes), the total MVPD price increase predicted by his model decreases by “about one-third” – a decrease that “take[s] away the vast majority the net effect” on MVPD monthly costs. *See id.* at 2317:25-2318:6, 2319:10-16; *see also id.* at 2617:12-2618:13 (Carlton) (factoring in that “one contract” reduces MVPD harm projection to “roughly a 5-cent projected price increase instead of a 27-cent price increase”). Not surprisingly, Professor Carlton testified that simply by accounting for all current affiliate agreements and making no other changes to Professor Shapiro’s model, the model would generate a predicted net *benefit* to consumers rather than a net harm for the years 2016 and 2017. *See id.* at 2513:1-9 (2017) (discussing DXD116); *id.* at 2515:25-2516:1 (2016) (discussing DXD116).

In other words, given Turner’s existing contracts, the level of post-merger harms predicted by Professor Shapiro’s existing model would not begin to phase in until at least 2021. But even Professor Shapiro concedes that 2021 is “getting out there a ways” and that “it gets harder” to predict actual harm that far down the line. *Id.* at 2258:1-2, 2316:15-2317:4-5 (Shapiro). That recognition reflects the testimony of industry witnesses, many of whom testified that the landscape of the video distribution industry is continually changing and will continue to change as new entrants join the market. *See, e.g., id.* at 2456:7-11 (Carlton) (“So we have Netflix, we have Google coming in, you have Amazon Prime. These are all big firms, Apple and Facebook we know are coming in. . . .”); *id.* at 2948:20-2949:3 (Holanda (RCN)) (agreeing that migration to “OTT providers” is “likely to grow in the future as Millennials become more and more prominent in the marketplace”); *cf. id.* at 3853:18-19 (Shapiro) (“I think it is not disputed that the video margins are going down.”).

I am thus left with projections of harm for the years 2016, 2017, and 2021 that all concede have not and will not occur in the real world due to Turner's actual affiliate agreements. *See, e.g., id.* at 2317:6-15 (Shapiro) (“Q: So let’s be clear about this when . . . you said \$586,000,000 of annual price increase[s] to all of the MVPDs and a couple of virtual [MVPDs] in there, right? A: That’s the number there. Q: So just to be clear, that isn’t going to happen. This isn’t going to happen let’s say in the year after the merger, right? That can’t happen. A: That is true.”). As such, I have no choice but to agree with Professor Carlton that Professor Shapiro’s model is “overestimating how quickly” the predicted harms “are going to start occurring.” *Id.* at 2444:15-23 (Carlton). To the extent, moreover, that the model projects “actual effects [that] will only occur gradually” after the largest of those agreements expires in 2021, even Professor Shapiro admits that it “gets harder” to project what the industry – and thus actual, real-world harm – will look like that far down the road. *Id.* at 2209:17-19, 2316:19-2317:5 (Shapiro); *cf. id.* at 235:18-19 (Schlichting (DISH)) (Sling launched as the first virtual MVPD in February 2015). For those reasons, even putting aside the various problems with the model previously discussed, I conclude that the model’s predictions of harm are not “sufficiently probable and imminent” to be probative in view of the facts of this case, especially “in the context” of the ever-increasing competitiveness of this “particular industry.” *Arch Coal*, 329 F. Supp. 2d at 115 (quoting *Marine Bancorporation*, 418 U.S. at 623 n.22); *Aetna*, 240 F. Supp. 3d at 79 (quoting *Brown Shoe*, 370 U.S. at 321-22).

* * *

After hearing Professor Shapiro's bargaining model described in open Court, I wondered on the record whether its complexity made it seem like a Rube Goldberg contraption. Professor Carlton agreed at the trial that that was a fair description. *See* Tr. 2447:2-7 (Carlton). But in fairness to Mr. Goldberg, at least his contraptions would normally move a pea from one side of a room to another. By contrast, the evidence at trial showed that Professor Shapiro's model lacks both "reliability and factual credibility," and thus fails to generate probative predictions of future harm associated with the Government's increased-leverage theory. *Anthem*, 855 F.3d at 363. Accordingly, neither Professor Shapiro's model, nor his testimony based on it, provides me with an adequate basis to conclude that the challenged merger will lead to *any* raised costs on the part of distributors *or* consumers – much less consumer harms that outweigh the conceded \$350 million in annual cost savings to AT&T's customers.⁵¹

⁵¹ Although they amount to "extra icing on a cake already frosted," there are even more reasons to be skeptical of the Government's increased-leverage theory of competitive harm. *Yates v. United States*, 135 S. Ct. 1074, 1093 (2015) (Kagan, J., dissenting).

First, the Court has reason to believe that, post-merger, AT&T will honor Turner's commitment to arbitrate, counterparties will agree to the terms of that commitment, and the prospect of arbitration will influence affiliate negotiations. In short, the commitment, made by Turner shortly after the filing of this suit, will have real-world effects. For starters, the proposed arbitration agreement is similar "in many of the fundamental ways" to the arrangement blessed by the DOJ, FCC, and this Court in the Comcast-NBCU merger. Tr. 2680:1-9 (Katz); *see also* 7/27/2011 Hr'g Tr. 7:4-7, 13:6-10, Comcast Corp., 808 F. Supp. 2d 145. Record evidence confirmed the real-world impact of an arbitration provision of this kind, giving the Court confidence both that arbitration offer will have import to negotiations and would be accepted by Turner's counterparties. *See supra* pp. 100-105 (reviewing econometric analysis of affiliate-agreement prices after the Comcast-NBCU merger); *see also* Tr. 1388:18-22 (Montemagno (Charter)) (testifying to effects of arbitration in NBCU negotiations); *id.* at 2017:12-15 (Bond (NBCU)) (similar); *id.* at 121:14-122:9 (Fenwick (Cox)) (confirming that Cox had proposed arbitration "[j]ust like in Comcast case" as condition to this merger); *id.* at 464:17-20 (Schlichting (DISH)) (similar). Given its trial presentation, I am hard-pressed to conclude that AT&T would (much less could) retreat from the commitment in light of the apparent reputational costs of doing so – costs that would imperil future negotiations in a marketplace with repeat players. *See, e.g., id.* at 3261:23-3262:3 (Stankey (AT&T)); *cf. id.* at 2622:4-2624:1 (Carlton).

IV. The Government Has Failed to Meet Its Burden to Show That the Proposed Merger Is Likely to Substantially Lessen Competition on the Theory That AT&T Will Act to Harm Virtual MVPDS Through Its Ownership of Time Warner Content

The Government's second theory of competitive harm relates to virtual MVPDs. Virtual MVPDs, like traditional MVPDs, offer consumers linear (or "live") television programming in exchange for a subscription fee. *See supra* pp. 11-13. Unlike traditional MVPDs, however, virtual MVPDs transmit their video content over the internet. *Id.* Compared to traditional MVPDs, virtual MVPDs generally offer lower-cost programming packages to consumers; those packages, known in the industry as "skinny bundles," contain fewer networks than do the larger bundles offered by MVPDs. *Id.* Although virtual MVPDs are of recent vintage, they are quickly gaining market share in the video

Contrary to the Government's insinuations about the reasons for the arbitration offer, moreover, the Court does not view the offer as akin to an admission by defendants that the proposed merger would lead to the anticompetitive harms that the Government posits. *Cf. id.* at 39:1-5 (Gov't Opening). Instead, the Court credits John Stankey's and Randall Stephenson's testimony that the commitment was intended to "put our money where our mouth is" in showing that the proposed merger, far from being aimed at "do[ing] any of the things that the government allege[s]," is instead a "vision deal" being pursued to achieve "lower prices, improved quality, enhanced service, [and] new products." *Id.* at 3261:16-3262:3 (Stankey (AT&T)); *id.* at 3402:3 (Stephenson (AT&T)); *see also id.* at 3467:18-3468:9 (Stankey (AT&T)); *id.* at 3395:23-25 (Stephenson (AT&T)); *supra* pp. 36-40.

Second, the Court observes that the Government's increased-leverage theory fails to account for another feature of the market, namely the FCC's program access rules. As defendants' expert, Professor Katz, testified, those rules are calculated to prevent precisely the kind of harm predicted by the Government: a vertically integrated entity discriminatorily increasing programming prices on its distributor-rivals. *See* Tr. 2693:14-2694:5 (Katz) ("They wanted to make sure that somehow control of the programmer wasn't used to harm competition."); 47 U.S.C. § 548(b), (j); 47 C.F.R. § 76.1001(b)(1)(i)-(ii); *see* 47 U.S.C. § 548(c)(2). Those regulations are a proper subject of antitrust analysis, *see Verizon Comms Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 411-12 (2004), and appear to be squarely on-point, at least according to the unrebutted testimony of Professor Katz. *See* Tr. 2693:19-2694:1 (Katz) ("[T]here are two broad categories. One category . . . prohibits discrimination against different distributors. And the other broad category prohibits the distributor from having undue influence on the decisions of the programmer. So, again, the idea of you don't want the distributor telling the programmer to go do things to harm other distributors."). Nevertheless, the Government all but wishes them away – and does so with little explanation or, more importantly, record evidence.

programming and distribution industry. *See* Tr. 448:24-449:2 (Schlichting (DISH)). Examples of virtual MVPDs include AT&T’s DirecTV Now, DISH’s Sling TV, Sony’s Playstation Vue, Hulu Live, Google’s YouTube TV, FuboTV, and Philo. Gov’t PFOF ¶ 14; Defs.’ PFOF ¶ 8.

According to the Government, the challenged merger would give AT&T the “ability to harm competition by slowing the growth of emerging, innovative online distributors” – that is, virtual MVPDs. Gov’t PFOF 104. AT&T could do so, the Government asserts, either acting on its own (under the “unilateral theory”) or in coordination with Comcast-NBCU (under the “coordination theory”). *See* Gov’t PCOL ¶ 63.⁵² Defendants counter that the evidence does not support the Government’s virtual MVPD theories. Far from showing that AT&T is trying to marginalize virtual MVPDs, defendants claim that the trial demonstrated that AT&T is embracing those providers – even launching and supporting a successful virtual MVPD, DirecTV Now. With respect to the supposed incentive to coordinate with Comcast, defendants argue that the Government’s theory ignores critical differences between the positions of AT&T and those of Comcast vis-à-vis virtual MVPDs as well as key limitations on the companies’ abilities to coordinate successfully. For the following reasons, I agree with the defendants that the Government has failed to show a

⁵² It will come as no surprise that a basic premise of the virtual claims – as for the Government’s increased-leverage theory – is the literal “must have” nature of Turner programming. For all the reasons stated earlier in this opinion, the Court is skeptical that, in the Government’s words, virtual MVPDs are “dependent on programmers” like Turner. Gov’t PFOF ¶ 17. For instance, Sling, the most successful virtual MVPD, offers a package without broadcast stations and does not offer CBS at all. *See* Tr. 351:12-25 (Schlichting (DISH)). As Sling President Warren Schlichting explained, the whole point of virtual MVPDs like Sling, in fact, is to carry *fewer* channels. *See id.* at 236:2-6 (“Q. Do you carry all the same channels as other pay-TV services? A. Certainly not all of them. One of the places that we tried to innovate is to carry fewer channels, many fewer channels.”).

likelihood that the merger would substantially lessen competition by empowering the merged company to act, either unilaterally or in coordination with Comcast-NBCU, to harm virtual MVPDs.

Unilateral Theory. The Government first claims that AT&T has an incentive to harm innovative virtual MVPDs and could act unilaterally on that incentive by foreclosing or restricting virtual MVPDs' access to "must-have" Turner content. *See* Gov't Post-Tr. Br. 11. That is a curious claim, to say the least, in light of Professor Shapiro's testimony that, in his view, "standing alone, acting unilaterally, the – AT&T *will* still want to license the Turner content to virtual MVPDs." Tr. 2260:19-21 (Shapiro) (emphasis added); *see id.* at 2291:8-11 ("Q: Now with respect to coordination, you've made no claim that AT&T post merger would have a unilateral incentive to withhold Turner content from virtual MVPDs, correct? A: Correct."); *id.* at 2293:9-13 ("Q: And you're not contending and you've rendered no opinion that they will withhold Turner content from MVPD[s], correct? A: That's correct. Q: Or as we said unilaterally from virtual MVPDs, correct? A: Also correct."). That is so, according to Professor Shapiro, because as with traditional MVPDs, it would be "profitable" for the merged entity to continue to license Time Warner content to virtual MVPDs. *Id.* at 2293:14-17.

If citing Professor Shapiro's testimony weren't enough to dispel the Government's unilateral virtual MVPD theory, defendants put forward additional evidence that AT&T would have incentive to *license* Time Warner content to virtual MVPDs after the merger. For starters, given Turner's imperative of broad distribution, *see supra* pp. 10-11, Turner executives testified that it is important for Turner's content to be included on virtual

MVPDs as they continue to grow in relevance. With consumers choosing to cut or shave the cord, Turner has “embrac[ed] virtual MVPDs,” Turner CEO John Martin testified, “because, again, we need to be distributed to as full distribution as possible.” *Id.* at 607:13-16 (Martin (Turner)); *see also id.* at 3157:22-3158:7 (Bewkes (Time Warner)) (explaining that virtual MVPDs are a favorable trend because they are “another place where we could put our networks in front of consumers”); *id.* at 1064:25-1065:3 (Breland (Turner)) (“Q. . . . [W]hat was your strategy with respect to negotiating with the new entrant virtual MVPDs? A. I want to be on every platform that comes.”); *cf. id.* at 3126:8-16 (Bewkes (Time Warner)) (stating that the Government’s coordination theory “makes no sense” because “[w]e want to be on all the virtual MVPDs”).

The entire premise of the proposed merger – allowing AT&T to go mobile with video content – provides yet another reason to reject the Government’s unilateral merger theory. *See id.* at 3393:24-25 (describing plans to deploy Time Warner video content over AT&T’s wireless network in order to make that content “worth far more”); *see also* PX456-3 (discussing merger strategy and AT&T “strategy of ensuring that its content is available to consumers on a wide range of distribution platforms”). AT&T’s largest business is its wireless business, where it has more than 100 million subscribers. *Id.* at 3208:19-24 (Stankey (AT&T)); *id.* at 3379:19-20 (Stephenson (AT&T)). On its own, if separated from the rest of the corporation, AT&T’s wireless business would be “number 37 on the Fortune 500” – approximately the size of Proctor & Gamble. *Id.* at 3379:20-3380:1 (Stephenson (AT&T)).

Within its wireless business, AT&T Chairman and CEO Randall Stephenson explained, “getting video delivered onto the mobile device” is one of AT&T’s “big focus areas.” *Id.* at 3381:24-25; *see id.* at 3208:20-22 (testifying about AT&T’s goal of “transform[ing] the way we deliver video to customers, [to] make the video far more portable”). Increased video consumption is lucrative for AT&T because viewers consume more data on the wireless network. This leads AT&T customers to “buy up” on data plans, get more devices, or connect more devices to the network – all “good for [AT&T’s] business.” *Id.* at 3254:19-22 (Stankey (AT&T)). Indeed, “over half of all of the traffic on [AT&T’s] network today is video, delivering video.” *Id.* at 3382:4-5 (Stephenson (AT&T)).

Industry trend-lines point toward increased video consumption in the future – and AT&T aims to ride these tailwinds. *See id.* at 3505:21-3507:2. Right now, AT&T is working to develop fifth-generation wireless, which will drive video consumption even more. *Id.* at 3382:7-3383:5. And AT&T views mobile consumption of video, including through virtual MVPDs, as a critical part of its post-merger future. *See id.* at 3506:23-25 (“What we’re all working towards is creating [\$]35 and \$15 bundles. And that’s where the world is moving.”). Notably, the benefits associated with AT&T customers accessing virtual MVPD content continue to accrue even when they use DirecTV Now’s competitors like Sling and YouTube TV. *See id.* at 3432:16-20 (“With AT&T, we’re in a unique position. We like over-the-top. Over-the-top generally means, in this day and age, wireless. People are using their wireless devices to watch video, whether it’s our video or not, we’re somewhat ambivalent.”). All of this gives the combined entity even more reason to

distribute Time Warner content as broadly as possible in order to encourage the proliferation of virtual MVPDs. As Randall Stephenson put it, the proposed merger is a “vision deal” reflecting a belief “that distribution of [Time Warner] content to wireless will drive the value of the content up” and that “the ability to pair our data with [Time Warner’s] advertising inventory” for digital ads delivered over the internet “will drive value.” *Id.* at 3402:24-3403:6.

Against that evidence, the Government cites a handful of AT&T documents and statements related to virtual MVPDs – documents the Government says show AT&T has the incentive to slow the rise of virtual MVPDs. *See, e.g.*, PX42; PX228; PX40; PX47; PX48. For multiple reasons, however, I do not consider the fact that AT&T executives may have previously expressed displeasure with Turner’s relationships with its competitor virtual MVPDs to be probative of AT&T’s post-merger economic incentive to license Turner content to virtual MVPDs. First, these statements shed no light on the post-merger incentive AT&T would have to maximize distribution of Turner content. As the reader now knows, wide distribution is the *sine qua non* of the programming industry, driving both subscription and advertising revenue. Indeed, because of these “[gains] from trade” associated with licensing Turner content as broadly as possible, Professor Shapiro himself refused to countenance the Government’s unilateral virtual MVPD theory. Tr. 2293:12-17. Second, these statements do not explain why AT&T would discard the profits associated with increased video consumption by its 100 million-plus wireless subscribers

accessing virtual MVPD offerings. In short, the Government’s evidence on its unilateral withholding theory is fatally anemic.⁵³

Second, from the other direction, the Government advances an alternative unilateral claim: that AT&T would have the ability to break the “skinny bundle” models of virtual MVPDs by forcing those distributors to take *too many* Turner networks. Citing the testimony of Sling’s President, Warren Schlichting, the Government argues that a post-merger requirement that Sling “take eight Turner networks instead of four would ‘break [Sling’s] model’” and, indeed, would have a snowball effect with other programmers. Gov’t PFOF ¶ 288 (quoting Tr. 265:17-266:8, 268:9-23 (Schlichting (DISH))).

That argument, however, ignores that Turner has less of an imperative to risk a deal with Sling (or other virtual MVPDs) by insisting on carriage of all of its networks. That is so, the evidence indicates, because Turner has a highly “concentrated portfolio of networks,” Tr. 558:1 (Martin (Turner)), with 85 to 90% of Turner’s revenues deriving from only four networks, *see* Defs.’ PCOL ¶ 51 n.39; *accord* Gov’t PFOF ¶ 75. That fact, as

⁵³ To the extent the Government seeks to recycle these statements for purposes of its coordination theory, this evidence is unpersuasive on that count, too. The combined entity would stand to gain much from wide distribution of Time Warner content to virtual MVPDs, and stand to lose much by refusing to do so. The Government’s remaining fact evidence similarly fails to establish any incentive to act, unilaterally or coordination, to stifle virtual MVPDs. To the extent the Government seeks to recycle the slide deck, PX184, PX543, or Schlichting’s testimony for its virtual claims, that evidence remains of limited probative value for the reasons stated above. *See supra* pp. 86-88 (PX184, PX543); *see supra* pp. 75-78 (Schlichting testimony). Nor does additional speculation of third parties, *see* Gov’t PFOF ¶¶ 291-292, or testimony as to the “importan[ce]” of Turner content to virtual MVPDs, *see id.* ¶¶ 293-294 – even if presented for the first time in this section – move the needle. Altogether, the best the Government could marshal was a statement from AT&T’s John Stankey that “we kind of expected [Sling] might be concerned about” AT&T attacking their skinny bundle. *See* Tr. 3256:3-15. Such evidence, on its own or in combination, simply cannot countermand the prime directive of programming – broad distribution – not to mention AT&T’s independent incentive to grow video consumption on its wireless network, *see supra* pp. 153-155.

Time Warner CEO Jeff Bewkes noted – means Turner is “better placed” to succeed in the skinny bundle model. Tr. 3126:22. The Government’s skinny bundle point also overlooks the fact that Turner – like other programmers – already fights tooth and nail to get all of its networks into all of the packages of every distributor. *See id.* at 433:18-21 (Schlichting (DISH)); *id.* at 606:5-11 (Martin (Turner)). Simply put, the Government has not produced sufficient evidence to show that the challenged merger is likely to make a meaningful difference to that dynamic.⁵⁴ For all of the above reasons, I conclude that the Government has failed to meet its burden on its claims arising from AT&T’s asserted potential to unilaterally harm virtual MVPDs through its post-merger control of Turner content.

Coordination Theory. The Government posits that the challenged merger would also create a likelihood that AT&T would coordinate with Comcast-NBCU to harm virtual MVPDs. In contrast to the unilateral withholding claim just discussed, the Government did at least attempt to provide some expert support for this coordination claim. *See id.* at 2261:14-20 (Shapiro). Unfortunately for the Government, however, neither that expert testimony nor its other evidence is even close to sufficient to support its coordination claim.

How so?

⁵⁴ In support of the notion that virtual MVPDs need Turner networks (again, in the most literal sense), the Government points to a statement by John Martin, Turner’s Chairman and CEO, that Sling would be “shit without Turner.” Gov’t PFOF ¶ 156 (quoting PX4). This statement does not accomplish the work that the Government thinks it does. For starters, as discussed above, the very “skinny bundle” concept embraces fewer networks – even fewer popular ones – with the knowledge that some consumers will welcome the trade of fewer networks for a lower subscription fee. And second, it should come as no surprise that – even in colorful language – executives would be avid boosters for their companies’ products. In the final analysis, the Government’s repeated use of this John Martin quote, *see* Tr. 12:3-7 (Gov’t Opening), 17-18 (Gov’t Closing), calls to the mind one Court’s admonition “rummage[ing] through business records” for “tidbits that will sound impressive (or aggressive)” undermines efforts to ensure “accuracy of decisions.” *A.A. Poultry Farms, Inc.*, 881 F.2d at 1402.

A proposed merger may violate Section 7 by “enabling or encouraging post-merger coordinated interaction among firms in the relevant market that harms [consumers].” Gov’t PCOL ¶ 67 (quoting *FTC v. OSF Healthcare Sys.*, 852 F. Supp. 2d 1069, 1086 (N.D. Ill. 2012)). Such coordinated conduct need not constitute an illegal agreement under Section 1 of the Sherman Act, but instead can comprise instances of tacit coordination. *Cf. Heinz*, 246 F.3d at 715 (coordinated effects can occur “either by overt collusion or implicit understanding”). In order to assess whether a merger will lead to an unacceptable risk of competition-stifling coordination, courts evaluate various “market conditions, on the whole.” *H & R Block*, 833 F. Supp. 2d at 77 (citation omitted). In short, that analysis involves consideration of whether would-be coordinators could wield anticompetitive power “by recognizing their shared economic interests and their interdependence with respect to price and output decisions.” *Brooke Grp.*, 509 U.S. at 227. Not so here !

As it does for its other claims, the Government relies on a key assumption when pressing its theory of coordinated effects. Here, the Government assumes that, “[a]s the only two vertically integrated traditional MVPDs, Comcast and AT&T would share an incentive to slow the entry and growth of virtual MVPDs.” Gov’t PFOF ¶ 299. To act on that incentive, the Government further asserts, the companies could “mutually forbear” from licensing their programming content “without any communication between them.” *Id.* (quoting Tr. 2265:5-2265:6 (Shapiro)). Not only is that theory overly speculative, it ignores key differences between AT&T and Comcast that undermine the Government’s argument.

First, the Government has failed to put forward sufficient evidence to show more than a theoretical “possibility” of coordination. *Cf. Baker Hughes*, 908 F.2d at 984 (“Section 7 involves *probabilities*, not certainties or possibilities.”). Indeed, the Court need look no further than the testimony of Professor Shapiro in that regard. When questioned at trial about the Government’s coordinated effects theory, Professor Shapiro conceded that he had no “way of accessing [sic] the probability” of coordination and thus had not attempted to “quantif[y] any risk whatsoever” that the predicted coordination “could occur.” *See* Tr. 2291:25-2292:13 (Shapiro).⁵⁵ Accordingly, Professor Shapiro confirmed that he was “not in a position to say” that coordination is “more likely to happen than not,” and indeed was not even prepared to say that there’s a “one percent chance that coordination will happen” as a result of the challenged merger. *Id.* at 2292:6-13. Given that testimony, and the lack of “a detailed theory” with respect to coordination, I can

⁵⁵ The Government insists that it need not introduce quantitative evidence in support of the coordinated effects theory. *See* Gov’t PCOL ¶ 71. The suggestion, of course, is that the Court should steer clear of imposing a requirement that the Government make a numbers-based showing on coordinated effects. Let me be clear. The Government here has failed to carry its burden on the coordination theory not because there is some *per se* requirement of quantitative analysis. Rather, the Government has failed to carry its burden because it has not put forward persuasive evidence – in any form – that AT&T and Comcast have the incentive or, given market constraints, the ability to coordinate in the manner predicted.

There is one more point. The cases cited by the Government *do* involve quantitative showings. In each one, the Court made or adopted a threshold quantitative assessment as to market concentration. *See H & R Block*, 833 F. Supp. 2d at 71-72 (applying Herfindahl-Hirschmann Index to determine market concentration); *OSF Healthcare*, 852 F. Supp. 2d at 1078-80 (same); *see also Hosp. Corp.*, 807 F.2d at 1384 (accepting “FTC’s figures” as to “highly concentrated market”). That determination, in turn, triggered the “‘ordinary presumption of collusion’ that attaches to a merger in a highly concentrated market.” *H & R Block*, 833 F. Supp. 2d at 77 (quoting *Heinz*, 246 F.3d at 725). And with that presumption in place, the burden shifted to defendants to rebut the case by “produc[ing] evidence of ‘structural market barriers to collusion’ specific to [the relevant] industry that would defeat” the presumption. *Id.* (quoting *Heinz*, 246 F.3d at 725). Thus, the Government’s insinuation that past coordinated-effects challenges were tried without resort to quantitative analysis is simply misleading. In short, the Government cannot evade its burden of proof on the “ultimate issue [of] whether the challenged acquisition is likely to facilitate collusion,” *Hosp. Corp.*, 807 F.2d at 1384; Gov’t PCOL ¶ 71, by simply stating that it “does not need to quantify the potential harm,” Gov’t PCOL ¶ 71.

sympathize with Professor Carlton's reaction: "I'm not quite sure what I'm supposed to rebut on [t]his." *Id.* at 2454:1-10 (Carlton).

Second, the Government's argument regarding the incentive of AT&T and Comcast to coordinate to harm virtual MVPDs ignores that both stand to lose large amounts of affiliate fee and advertising revenues by withholding their content from virtual MVPDs. *See supra* pp. 10-11; Tr. 3126:8-16 (Bewkes (Time Warner)) (stating that the Government's coordination theory "makes no sense" because "[w]e want to be on all the virtual MVPDs"); *id.* at 2020:5-18 (Bond (NBCU)) ("Q: Why have you decided to license your networks to each of those virtual MVPDs? A: Well, simply we're interested in getting the most amount of distribution that we can get, and they represent an important new pathway of distribution. As I said, they now have well over three million subscribers in total. . . . [I]f we were not on those platforms we would have, you know, three million less subs, fewer subs."). Unsurprisingly, NBCU has licensed its content to each virtual MVPD. *See id.* at 2019:15-2020:2 (Bond (NBCU)). The Government has not explained why either company would be willing to forgo those affiliate fees and advertising revenues from virtual MVPDs. Nor has the Government proffered any expert analysis, for example, of how those economics could, or would, change assuming a coordinated blackout of both Turner and NBCU.

Third, and critically, the Government's argument also ignores key differences between the two companies – differences that AT&T executives believe give AT&T a competitive advantage over Comcast moving forward in this new era of rising virtual MVPD prevalence. AT&T's John Stankey, who will be responsible for running Time

Warner should the challenged merger proceed, emphatically (and credibly) stated at trial that he could not “even imagine” aligning with Comcast given the companies’ history of dealings, adding, “I’m not going to cooperate with somebody I don’t like.” *Id.* at 3255:2-3256:2 (Stankey (AT&T)). AT&T CEO Randall Stephenson testified similarly, responding to a question about the Government’s coordination theory as follows: “You probably have to live in this industry every day like I do to appreciate what a stretch that is. We compete with Comcast in the marketplace. The individual that runs communication company, he wakes up every day trying to think, how do I win in the marketplace against Comcast?” *Id.* at 3431:25-3432:5 (Stephenson (AT&T)).

The most obvious “advantage” AT&T has over Comcast when it comes to virtual MVPDs is that, unlike Comcast, and as discussed at length above, AT&T has a vast wireless business with over 100 million customers. *Id.* at 3432:2-7; *id.* at 3208:19-24 (Stankey (AT&T)); *see also id.* at 3432:17-22 (Stephenson (AT&T)) (“Over-the-top generally means, in this day and age, wireless. People are using their wireless devices to watch video, whether it’s our video or not, we’re somewhat ambivalent. We’d rather it be our video; but either way, it serves our interests for people to watch video over our wireless network.”); *see also supra* pp. 153-155. The reasons to encourage, not quash, virtual MVPDs unilaterally become even more compelling in the context of a coordination claim with Comcast – a competitor that is much more beholden to legacy cable infrastructure and the traditional MVPD business model. *See id.* at 3432:2-12 (Stephenson (AT&T)); *cf. id.* at 3255:18-22 (Stankey (AT&T)) (“We don’t want to cooperate with Comcast to play their game. We want to figure out how we use our mobile devices and our mobile network to

change the game”); *id.* at 3208:19-24 (“[O]ne of the clear objectives [for AT&T in acquiring DirecTV] was to start to transform the way we deliver video to customers [to] make the video far more portable, start to emphasize the fact that we could use our 100 million wireless subscribers to be able to do things differently, which is dramatically different than Comcast.”).

The Government does not dispute that AT&T’s wireless business confers strong incentives to maximize distribution to virtual MVPDs. Nor can it be questioned that AT&T’s strong positioning in the world of mobile content distribution gives it a powerful disincentive to work with Comcast to stifle those mobile providers of video. AT&T has plainly positioned itself to ride industry tailwinds in support of mobile consumption of video. As John Stankey explained, AT&T acquired DirecTV in 2015 not in order to double down on the satellite business, a concededly mature and declining asset, but to “pick up a lot of new customers that we could work on migrating” to new products. *Id.* at 3207:18-20 (Stankey (AT&T)); *see also id.* at 3207:21-3208:2. Indeed, as soon as the merger closed, AT&T began renegotiating DirecTV’s contracts to allow for a mobile, direct-to-consumer option, DirecTV Now. AT&T knew that it was “in a foot race to basically start to change the product to be able to catch the next wave, whatever that next wave was going to be. And we didn’t expect that we were going to continue to see traditional pay-TV subscribers” increasing. *Id.* at 3209:12-16. Nowhere does the Government explain why AT&T would deploy valuable Time Warner content to prop up a rival’s business model, while harming its own. Go figure !

This fundamental problem of incentives and profitability buries the Government's claim. It is beyond dispute that neither the proffered concentration in the MVPD market (which, by the way, will be the same post-merger), *see* Gov't PFOF ¶ 306, nor the importance of Turner and NBCU content, *see id.* ¶ 307, nor some transparency in "key information," *see id.* ¶¶ 308-310, nor any other of the Government's evidence on the coordination theory (alone or in combination), can establish a "risk of coordination" unless the parties have an incentive or interest to collude in the first place.

Even assuming, contrary to the evidence, that AT&T would want to coordinate with Comcast under the Government's theory, the staggered, lengthy industry contracts would make that coordination strategy extremely risky. *See id.* at 643:20-644:2 (Martin (Turner)) (testifying that "because of the length of these contracts, because they're typically years in length," a strategy set "in 2013" would "begin to show up in '15, '16 and '17"); *id.* at 87:9-11 (Fenwick (Cox)) (testifying that affiliate agreements run "between five and eight years on average"). Under the Government's coordination theory, one party – AT&T or Comcast – would have to "jump first," giving up valuable programming rights on the hope that the other, in some years' time, would elect to do the same. Indeed, this barrier to coordination is so great as to put to rest the notion not only that AT&T and Comcast would have the *incentive* to coordinate, but that the post-merger marketplace would afford them the *ability* to do so. Whether by way of tacit coordination or an illegal agreement, putting such blind faith in one's chief competitor strikes this Court as exceedingly implausible ! Indeed, the decision to "not to renew [a] license or not to license to a new virtual MVPD and wait and see if the other did it," as Professor Shapiro proposes, would *enhance* the other party's

position in its next round of negotiations with the virtual MVPD at issue. Tr. 2264:14-2265:13 (Shapiro). As Charter's Tom Montemagno explained, if a distributor goes dark with one network group, that distributor is in "a vulnerable spot, and I feel like I sort of have to do the deal" when another network group threatens a blackout. *Id.* at 1404:13-15. The result would be forgone revenue for a period of years, with AT&T's chief competitor gaining outsized profits in the next round of negotiations. The Government puts forward no persuasive reason why AT&T and Comcast would engage in such conduct.

The fundamental difference in incentives between AT&T and Comcast vis-à-vis virtual MVPDs, the barrier to coordination in the form of long-term contracts, coupled with the fact that the Government has provided no evidence to show how the benefits of a coordinated blackout would outweigh the companies' resulting losses of affiliate fee and advertising revenues, leave me completely unable to accept the Government's coordinated effects theory.⁵⁶

⁵⁶ In support of its coordination theory, the Government points to past communication between Dan York of AT&T and counterparts at other distributors in the Los Angeles market concerning the Sportsnet LA network. *See* Gov't PFOF ¶¶ 311-312; Tr. 2081:9-2081:16 (York (AT&T)); PX462. These instances are only weakly probative of future coordination, involving, as they do, a different market, distinctive factual setting, and different distributors. In all respects, this evidence cannot overcome AT&T's strong disincentives to coordinate with Comcast detailed in this section. *Cf. H & R Block*, 833 F. Supp. 2d at 77-78 (detailing "highly persuasive historical act of cooperation" between the same two parties at the center of post-merger coordination allegations). The same goes for inquiries by York concerning Verizon Fios packages or evidence regarding John Harran's conversations with his counterpart and "good friend" at NBCU. *See* Defs.' PFOF ¶ 291; Gov't PFOF ¶ 313.

V. The Government Has Failed to Meet Its Burden to Show That the Proposed Merger Is Likely to Substantially Lessen Competition on the Theory That AT&T Will Restrict Distributors' Use of HBO as a Promotional Tool

The Government's final theory centers on HBO. On this score, the Government alleges that the combined entity will have the "incentive and ability" to prevent rival distributors from using HBO as a promotional tool to attract and retain customers. *See* Gov't Post-Tr. Br. 9-10; Compl. ¶ 39.⁵⁷ Under this theory, the combined entity would

⁵⁷ In its proposed conclusions of law, the Government describes its theory that the merged entity might "restrict the use of HBO as a competitive tool." Gov't PCOL ¶ 61; *see also* Tr. 3993:7-10 (Gov't Closing) ("It means that if this merger goes forward, then the combined firm could limit the use of HBO as a competitive tool, if that competition threatens to impact AT&T."). Under this theory, HBO is a "competitive tool" insofar as it is used by distributors for discounts, promotions, marketing, and ad campaigns. *See* Gov't PCOL ¶ 61 (predicting that AT&T will have an incentive "to restrict the use of HBO as a competitive tool, and *thereby impair the competitive process and deny consumers the benefits of discounted HBO and other promotions*" (emphasis added)); *see also* Gov't PFOF ¶ 234 ("Overall, HBO is a highly valuable brand, which currently engages in significant promotional activities with MVPDs, both AT&T and its rivals."). This is consistent with the way in which Professor Shapiro viewed the theory. *See* Tr. 2290:25-2291:3 (Shapiro) ("Q. The only theory of harm that you considered relating to HBO is this issue that perhaps some promotional, some promotion of HBO might be curtailed, right? A. That's fair."). It is also consistent with the way in which the Government's Complaint and Pre-Trial Brief characterized the theory. *See* Compl. ¶ 39 ("MVPDs . . . today use HBO as a tool to entice new customers and to dissuade unhappy customers from leaving and switching to a rival MVPD. . . . After the merger, however, the merged firm would have the incentive and ability, through contractual restrictions, to impede rival MVPDs from using HBO to compete against AT&T/DirecTV."); Gov't Pre-Trial Br. 39 ("HBO could limit approvals for the use of HBO in marketing and promotions by DirecTV's rivals in a number of ways, including forms of subtle or targeted obstruction.").

The Government's proposed findings of fact, like its closing argument, appear to advance a considerably broader theory on the ways in which HBO could limit the terms of its distribution post-merger. Such a theory would go well beyond restricting promotion-related terms. *See* Gov't PFOF ¶ 267 (listing ways in which HBO could restrict distributors' offerings of HBO to customers); Tr. 3975:11-19 (Gov't Closing) (same). Most troubling is the Government's suggestion, based solely on the testimony of Martin Hinson of Cox, that the combined entity could "withhold[] HBO entirely." Gov't PFOF ¶ 267 (citing Tr. 703:25-704:18 (Hinson (Cox))). Professor Shapiro himself disavowed this very theory of withholding HBO content: "Q. You don't claim that post-merger HBO will be withheld from any MVPD, correct? A. Correct." Tr. 2290:15-18 (Shapiro). Professor Shapiro similarly disavowed any claim that HBO's price would increase on account of the merger. *See id.* at 2290:21-23.

For the reasons discussed in this Part, the Government has failed to prove that the merged entity has an incentive to restrict rival distributors' use of HBO for promotions. To the extent that the Government suggests that AT&T will withhold HBO content altogether, will delay access to HBO content, will increase penetration rate requirements, or will engage in any other potentially anticompetitive conduct that falls outside the proffered promotion-withholding scheme, the Court holds that, in light of the sparse supporting

“foreclos[e] competitors of the purchasing firm in the merger from access to a potential source of supply, or from access on competitive terms.” Gov’t PCOL ¶ 61 (quoting *Yankees Entm’t & Sports Network*, 224 F. Supp. 2d at 673). The basic idea, the Government tells us, is that rival distributors’ use of HBO in promotions will tend to draw potential customers to those MVPDs and away from AT&T, thereby giving AT&T reason to withhold or restrict its consent to use HBO in marketing, discounts, and bundles. See Gov’t PFOF ¶ 234. At the risk of stating the obvious, this is a gossamer thin claim.

The Government has failed to meet its burden of proof on this theory for two independent reasons. *First*, the Government has failed to show that the merged entity would have *any* incentive to foreclose rivals’ access to HBO-based promotions. This is because the Government’s promotion-withholding theory conflicts with HBO’s business model, which remains “heavily dependent” on promotion by distributors. Tr. 3074:5-6 (Bewkes (Time Warner)). HBO does not run ads, leaving subscription fees as its overwhelming source of revenue. See *id.* at 3070:3-5; PX456-67. This makes HBO a volume-based business, in which more subscribers means more revenue. See Tr. 3070:3-8, 3072:7-9 (Bewkes (Time Warner)). And because HBO continues to rely on distributors to reach the end-user, witnesses testified that HBO needs MVPD promotions in order to achieve this volume. See, e.g., *id.* at 3128:16-3129:8; *id.* at 1496:10-17 (Sutton (HBO)); see also *id.* at 1508:14-16 (“[O]ur whole business is relying on our affiliates to promote us. If we can’t do that, then our entire business model is destroyed.”); *cf. id.* at 1528:25-1529:4

evidence and Professor Shapiro’s disavowal of those theories, the Government has failed to meet its burden of proof that such conduct would likely result from the proposed merger.

(Patel (AT&T)). The Government simply fails to explain why AT&T would jeopardize – much less jettison – the promotional model on which HBO “absolutely” depends.⁵⁸ *Id.* at 1496:16-17 (Sutton (HBO)).

Second, the Government fails to establish that HBO promotions are so valuable that withholding or restricting them will drive customers to AT&T.⁵⁹ Put differently, the Government has failed to show that the marketplace substitutes for HBO are “inferior, inadequate, or more costly.” Gov’t PCOL ¶ 62 (internal quotation marks omitted). Third-party distributor witnesses testified that, for example, their companies had reduced the use of HBO in promotions, *see* Tr. 950:22-951:7 (SEALED); *id.* at 2135:17-22, 2135:24-2136:1 (Sejen (Cable ONE)). An executive from RCN said that his employer used HBO for promotions only because of the “economic incentives” offered by HBO to do so. *See id.* at 2971:16-23 (Holanda (RCN)); *cf. id.* at 2136:15-19 (Sejen (Cable ONE)). A Comcast executive confirmed that Netflix is a “substitute” for HBO that Comcast has incorporated into its set top box and includes in marketing. *See id.* 886:8-22 (Rigdon (Comcast)). This is all consistent with other evidence adduced at trial, which showed that distributors’ choice of which premium content provider to use for promotions may vary based on a number of

⁵⁸ As an add-on, HBO is low-hanging fruit for customers looking to shave monthly cable bills. *Cf.* Tr. 2137:3-6 (Sejen (Cable ONE)). This results in high “churn,” making HBO that much more reliant on promotions to maintain subscriptions. *See id.* at 2316:10-12; *id.* at 2972:20-24 (Holanda (RCN)). In these promotions, HBO depends on distributors because “the distributor . . . owns the relationship with the customer.” *Id.* at 1528:22-1529:4 (Patel (AT&T)).

⁵⁹ The Court is aware that, in the most technical sense, HBO has the “ability” to withhold certain promotions by way of its contract-based approval process, under which HBO must bless distributors’ use of HBO trademarks and talent for us in promotions. This fact alone, however, does not establish that AT&T would be able to “impair the competitive process.” Gov’t PCOL ¶ 61. For its theory, the Government must also show that HBO has an incentive to act anticompetitively and that only “inferior, inadequate, or more costly” substitutes for HBO promotions exist in the marketplace, *id.* ¶ 62 (citation omitted). The Government has failed to make these showings.

factors. *See id.* at 1526:17-25 (Patel (AT&T)).⁶⁰ Indeed, the evidence at trial further showed that MVPDs are hardly limited to premium content providers like HBO, Showtime, and Netflix in their choice of promotional tools; to the contrary, distributors have been known to bundle services with gift cards, price discounts, higher broadband speeds, additional telephone lines, video on demand films, devices such as iPads, and free installations or equipment. *Id.* at 717:15-25 (Hinson (Cox)); *id.* at 2972:1-6 (Holanda (RCN)); *id.* at 1497:5-10 (Sutton (HBO)).

Although this promotion-withholding theory made only a very brief appearance at trial, the Government asserts that this theory of harm constitutes an independent basis for blocking the merger. Gov't PCOL ¶¶ 61-62; Gov't Pre-Trial Br. 40.⁶¹ But in support of this theory, the Government has brought to bear little evidence indeed. As with its primary,

⁶⁰ After a trial replete with evidence on evolving, hyper-competitive marketplace conditions, the notion that Netflix is an adequate substitute for HBO should come as no surprise. "There was a time," HBO President Simon Sutton explained, "when very few people were making the kinds of shows we make [at HBO]. Now, it seems like almost every week, there's an announcement of somebody else making it." Tr. 1494:13-21. Netflix now has a programming budget that more than doubles HBO's, *id.* at 3099:13-15 (Bewkes (Time Warner)), and Netflix and HBO openly compete "in many different ways," including for "the talent to make the same shows," *id.* at 1493:18-1494:3 (Sutton (HBO)). And when measured by number of subscribers, both Netflix and Amazon are "eclipsing HBO." DX709-3. Indeed, one of the Government's experts, in an improper communication sent to Government attorneys during the course of his testimony in violation of the Court's witnesses rule, forwarded a YouTube video describing Netflix as one of the "top-ten . . . monopolists you've never heard of." *See* Tr. 3602:17-3603:7, 3604:7-25 (Quintero). Put simply, HBO is in the fight of its life!

⁶¹ The Government appears to suggest that incentive to engage in anticompetitive conduct – without any demonstration as to the probability of acting on that incentive – is sufficient reason to block a proposed merger. *See* Gov't PCOL ¶ 61 ("In this action, the effect of the merger may be to lessen competition substantially by incentivizing the merged firm to restrict the use of HBO as a competitive tool, and thereby impair the competitive process and deny consumers the benefits of discounted HBO and other promotions."). This proposition seems impossible to square with the legal standards governing Section 7 actions, which require a probability of anticompetitive effects. *See supra* pp. 50-52 & n.16. Because the Government has failed to establish that the merged entity will have any incentive to withhold HBO promotional rights, the Court need not answer the question whether the existence of such an incentive, without more, would be sufficient to show that the proposed merger would substantially lessen competition for purposes of Section 7.

increased-leverage claim of harm, the Antitrust Division decided to spill most of its ink developing undisputed facts – HBO is popular, *see* Gov’t PFOF ¶¶ 28, 235-242, valuable, *see id.* ¶¶ 28, 235, 243-252, and an effective promotional tool for MVPDs, *see id.* ¶¶ 253-258. The Government also relays the undisputed fact that HBO, as a matter of contract, retains significant control over the way in which its “trademarks or . . . talent” are used in those promotions. Tr. 1458:10-13 (Sutton (HBO)); *see* Gov’t PFOF ¶¶ 269-270 (discussing approval process for use of HBO in promotions). It did not, however, come to Court with economic evidence of any kind, *see* Tr. 2291:4-7 (Shapiro), and proffered only bare conjecture about how there may be “like a thumb on the scale” in favor of the Government’s promotion-withholding stratagem, *id.* at 2267:8-21; *see also id.* at 2267:3-7. As such, the Government’s evidence is too thin a reed for this Court to find that AT&T has, in that well-worn turn-of-phrase, either the “incentive” or the “ability” to withhold HBO promotional rights in order to “lessen competition substantially.” Gov’t PCOL ¶ 61. For these reasons, it is small wonder that Professor Shapiro himself refused to endorse the theory, testifying that, in his view as an economist, such a ploy “[o]n its own . . . would not have such a big impact, that it would substantially lessen competition.” Tr. 2275:24-2276:13 (Shapiro).

For these two, independent reasons, the Government has failed to provide sufficient evidence to support its final theory in this case. Accordingly, I reject outright the assertion that the combined entity would likely restrict HBO as a promotional tool in order to harm AT&T’s distribution rivals and thereby lessen competition in the marketplace.

CONCLUSION

The parties have waged an epic battle, under extremely restricted deadlines, to litigate and try this historic vertical merger case. Each side's evidence and theories have been subjected to cross-examination and the rigors of the Rules of Evidence and Civil Procedure. It has been a herculean task for all the parties and the Court.⁶² Each side has had its proverbial day in Court. The Court has now spoken and the defendants have won. But, the process is not quite over yet !

There is a grave and understandable fear on the part of the defendants that the Government will now seek to do *indirectly* what it couldn't accomplish directly by seeking a stay of this Court's order pending an appeal to our Circuit Court.

The consequences of receiving such a stay would cause irreparable harm to the defendants in general and AT&T in specific. First, it would effectively prevent the consummation of the merger by the June 21, 2018 break-up date for the deal. Second, it would cause AT&T to have to pay the \$500 million break-up fee it will owe to Time Warner if the deal is not consummated by that date. Those two consequences, of course, would occur regardless of whether this Court's decision were later upheld following appellate review. In this Court's judgment, a stay pending appeal would be a manifestly unjust outcome in this case.

The Government has had this merger on hold now since October of 2016 when it launched its investigation. In that 18-plus month period, the companies have twice

⁶² See, e.g., WDH & RSC at W.R. 6326.

extended the break-up date to accommodate the Government's litigation of this case. During that same period, the video programming and distribution industry has continued to evolve at a breakneck pace. The cost to the defendants and the Government to investigate, litigate, and try this case has undoubtedly been staggering – easily in the tens of millions of dollars.

If the Government were to ask me to stay this Court's ruling, I would, under the law, have to weigh whether the Government has a strong likelihood of success on the merits and would suffer irreparable harm should the stay be denied, among other things. Well, suffice it to say – as my 170-plus page opinion makes clear – I do not believe that the Government has a likelihood of success on the merits of an appeal. And in my judgment, given that our Circuit Court has never hesitated to unwind an unblocked merger if the law and facts warrant doing so, there would be no irreparable harm to the Government – only to the defendants – if my ruling were stayed. As such, I could not, and would not, grant such a stay in the first instance.

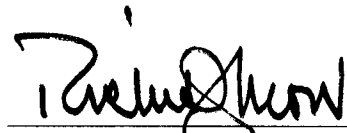
That of course is not to suggest in any way that the Government should not consider seeking appellate review of the merits of this Court's decision. That is, by any standard, fair game. But the temptation by some to view this decision as being something more than a resolution of this specific case should be resisted by one and all !

The Government here has taken its best shot to block the merger based on the law and facts, and within the time allowed. The defendants did their best to oppose it. The Court has spoken. To use a stay to accomplish *indirectly* what could not be done directly – especially when it would cause certain irreparable harm to the defendants – simply would

be unjust. I hope and trust that the Government will have the good judgment, wisdom, and courage to avoid such a manifest injustice. To do otherwise, I fear, would undermine the faith in our system of justice of not only the defendants, but their millions of shareholders and the business community at large.

* * *

Thus, for all of the foregoing reasons, the Government's request to enjoin the proposed merger is **DENIED**.



RICHARD J. LEON
United States District Judge

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OPTIMIZING PRIVATE ANTITRUST ENFORCEMENT IN HEALTH CARE

ANNE MARIE HELM*

ABSTRACT

Americans are paying too much for health care services and insurance, in large part due to insufficiently competitive markets. Waves of consolidation have fortified providers and insurers with market power, resulting in higher prices and lower quality for consumers. As antidotes, advocates have proposed various legislative, regulatory, and enforcement solutions. Yet, unlike public antitrust enforcement, private antitrust enforcement is either not mentioned or criticized as sour grapes from competitors or a money grab by consumers. Instead of ignoring or bashing private litigation, those looking to address the health care pricing crisis in the United States should be looking to optimize it. Effective private enforcement can restore competition, deter antitrust violations, and compensate victims in the markets for health care services and insurance. For plaintiffs, the key to optimizing private antitrust enforcement is overcoming the unavoidable challenges in litigating these cases—from satisfying pleading standards and establishing standing, to defining relevant markets. This article explains the key obstacles involved in these cases and tracks recent and current plaintiffs whose experiences provide insight.

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I. INTRODUCTION

Americans are paying too much for health care services and insurance, in large part due to insufficient competition among providers and payors.¹ Waves of consolidation in these markets have fortified providers and insurers with market power, resulting in higher prices and lower quality for consumers.² As antidotes, health economists and other policy advocates have proposed various legislative, regulatory, and enforcement solutions.³ Yet private antitrust enforcement is rarely recommended to remedy health care market dysfunction. Whereas *public* antitrust enforcement is generally touted as indispensable,⁴ *private* antitrust enforcement is often disregarded as baseless, self-serving litigation that only strains judicial resources and may even raise costs.⁵ But the notion that private litigation is important should not be controversial.⁶ Private

1. MARTIN GAYNOR ET AL., MAKING HEALTH CARE MARKETS WORK: COMPETITION POLICY FOR HEALTH CARE 1 (Apr. 2017), <https://www.brookings.edu/wp-content/uploads/2017/04/gaynor-et-al-final-report-v11.pdf>.

2. See Robert Berenson, *Acknowledging the Elephant: Moving Market Power and Prices to the Center of Health Policy*, HEALTH AFF. BLOG (June 3, 2014), <http://healthaffairs.org/blog/2014/06/03/acknowledgingthe-elephant-moving-market-power-and-prices-to-the-center-of-health-policy/>; WILLIAM B. VOGT & ROBERT TOWN, ROBERT WOOD JOHNSON FOUND., HOW HAS HOSPITAL CONSOLIDATION AFFECTED THE PRICE AND QUALITY OF HOSPITAL CARE? 1, 8 (Feb. 2006), http://www.rwjf.org/content/dam/farm/reports/issue_briefs/2006/rwjf12056/subassets/rwjf12056_1; MARTIN GAYNOR & ROBERT TOWN, ROBERT WOOD JOHNSON FOUND., THE IMPACT OF HOSPITAL CONSOLIDATION—UPDATE 1–3 (June 2012), <http://www.rwjf.org/en/library/research/2012/06/the-impact-of-hospital-consolidation.html>; MARTIN GAYNOR ET AL., MAKING HEALTH CARE MARKETS WORK: COMPETITION POLICY FOR HEALTH CARE 1 (Apr. 2017), <https://www.brookings.edu/wp-content/uploads/2017/04/gaynor-et-al-final-report-v11.pdf>; Leemore Dafny et al., *Paying a Premium on Your Premium? Consolidation in the US Health Insurance Industry*, 102 AM. ECON. REV. 1161, 1163 (2012) (finding that health insurance consolidation between 1998 and 2006 led to a seven percent increase in large group health insurance premiums); José R. Guardado et al., *The Price Effects of a Large Merger of Health Insurers: A Case Study of UnitedHealth-Sierra*, HEALTH MGMT., POL'Y & INNOVATION 8 (2013) (finding the UnitedHealth Group and Sierra Health Services merger increased the post-merger premiums in the Nevada markets by 13.7 percent, suggesting that the merging parties exploited the market power gained from the merger); PAUL B. GINSBURG, CTR. FOR STUDYING HEALTH SYS. CHANGE, WIDE VARIATION IN HOSPITAL AND PHYSICIAN PAYMENT RATES EVIDENCE OF PROVIDER MARKET POWER (Nov. 2010).

3. See, e.g., GAYNOR ET AL., *supra* note 1, at 17, 23, 28–29 (recommending: (1) changes to laws on information sharing, certificate of need laws, and certificates of public advantage; (2) new legislation banning anti-competitive contract clauses; and (3) increased federal and state antitrust enforcement).

4. See, e.g., Edith Ramirez, *Antitrust Enforcement in Health Care—Controlling Costs, Improving Quality*, 371 NEW ENG. J. MED. 2245, 2245 (2014).

5. See, e.g., Gregory J. Werden et al., *Deterrence and Detection of Cartels: Using All the Tools and Sanctions*, 56 ANTITRUST BULL. 207, 227–34 (2011) (disputing Lande & Davis's findings).

6. See Robert H. Lande & Joshua P. Davis, *Comparative Deterrence from Private Enforcement and Criminal Enforcement of the U.S. Antitrust Laws*, 2011 BYU L. REV. 315, 315

antitrust enforcement can restore competition, deter antitrust violations, and compensate victims in the markets for health care services and insurance, and, accordingly, the United States should be looking for ways to optimize it.

When passed, the antitrust statutes envisioned private cases as a fundamental part of an overall enforcement scheme.⁷ Indeed, the treble damages remedy was meant to spur private litigation.⁸ The Supreme Court has acknowledged as much: “By offering potential litigants the prospect of a recovery in three times the amount of their damages, Congress encouraged these persons to serve as ‘private attorneys general.’”⁹ The Court later elaborated, “The treble-damages provision wielded by the private litigant is a chief tool in the antitrust enforcement scheme, posing a crucial deterrent to potential violators.”¹⁰ Over the last century, private cases have greatly outnumbered public enforcement actions.¹¹ Recently, however, “private actions have caught up in the well-

(2011) [hereinafter Lande & Davis, *Comparative Deterrence*] (arguing that private antitrust litigation is more effective than Department of Justice (DOJ) criminal enforcement at deterring cartels); Robert H. Lande & Joshua P. Davis, *The Extraordinary Deterrence of Private Antitrust Enforcement: A Reply to Werden, Hammond, and Barnett* 58 ANTITRUST BULL. 173, 185–86 (2013) [hereinafter Lande & Davis, *Extraordinary Deterrence*].

7. The private right of action under the antitrust laws is (are) contained in Sections 4 and 16 of the Clayton Act, which apply respectively to actual and threatened injuries. 15 U.S.C. §§ 15, 26 (2012). Section 4 provides: “[A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States.” 15 U.S.C. § 15(a) (2012). Under both provisions, the “antitrust laws” include the Sherman and Clayton Acts. 15 U.S.C. § 12(a) (2012). However, the “antitrust laws” do not include Section 3 of the Robinson-Patman Act. 15 U.S.C. § 12(a) (2012). This is distinct from the legal framework in most other countries, as the United States provides some of the broadest access to private parties in antitrust. See Kenneth Ewing, *Private Anti-Trust Remedies Under US Law*, 1 PLC CROSS-BORDER COMPETITION HANDBOOK 87, 87 (2006–2007), <https://www.steptoe.com/assets/attachments/2804.pdf>. Many countries limit enforcement to governmental entities, and, where private remedies are available, those remedies are typically more limited in scope. See Ewing, *supra*, at 87, 91; see also Nicholas Heaton & Benjamin Holt, *Know-How: Private Litigation*, GCR, <http://globalcompetitionreview.com/know-how/topics/1000309/private-litigation-2017> (last visited Nov. 12, 2017) (providing a database of comparative international competition laws) (last visited Dec. 12, 2017).

8. By statute, plaintiffs are entitled to the treble damages remedy, which provides for recovery of “threefold the damages by [the plaintiff] sustained, and the cost of suit, including a reasonable attorney’s fee.” 15 U.S.C. § 15(a) (2012).

9. *Hawaii v. Std. Oil Co.*, 405 U.S. 251, 262 (1972); accord *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 635 (1985) (“A claim under the antitrust laws is not merely a private matter.”) (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.* 723 F.2d 155, 168 (1st Cir. 1983); *American Safety Equipment Corp. v. J.P. Maguire & Co., Inc.* 391 F.2d 821, 826 (2d Cir. 1968)).

10. *Mitsubishi Motors Corp.*, 473 U.S. at 635.

11. Paul E. Godek, *Does the Tail Wag the Dog?: Sixty Years of Government and Private Antitrust in the Federal Courts*, THE ANTITRUST SOURCE 1, 1–3 (Dec. 2009), https://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Dec09_Godek12_17f.authcheckdam.pdf; see also Peter J. Hammer & William M. Sage, *Antitrust, Health Care Quality, and the Courts*, 102

orchestrated, ideologically driven ‘tort reform’ movement” and have been characterized as “legalized blackmail” as opposed to a vital component of our statutory antitrust scheme.¹² Private antitrust enforcement does not deserve this characterization and indeed is a much needed means to address health care pricing.

Antitrust law is premised on the notion that competition leads to lower costs, higher-quality products and services, and encourages investment and innovation. In health care, as former Federal Trade Commission (FTC) Chair Edith Ramirez stated, “The success of health care reform in the United States depends on the proper functioning of our market-based health care system.”¹³ Although highly regulated and somewhat complicated by the buyer and seller relationships among patients, providers, and payors, health care in the United States is nonetheless market-based. As such, the sector depends on competition to drive prices down and quality up, even after the at-risk Patient Protection and Affordable Care Act.¹⁴ There is a real need for more antitrust enforcement in health care. As to hospital mergers, a named top public enforcement priority,¹⁵ the FTC has only challenged *one percent* of mergers over the past decade.¹⁶ And, even with both the FTC and the Department of Justice (DOJ) enforcing the federal antitrust laws, the lower-priority cases challenging anti-competitive conduct are even more scant, and criminal cases are rarer still.¹⁷

COLUM. L. REV. 545, 585 (2002) (describing empirical study of antitrust cases in health care between 1985 and 1999: “Of the 542 opinions in our sample, only 31 (representing 22 disputes) involved cases brought by the DOJ (10 disputes), the FTC (11 disputes), or state attorneys general (1 dispute)”).

12. Robert H. Lande & Joshua P. Davis, Am. Antitrust Inst., *Restoring the Legitimacy of Private Enforcement*, in A REPORT TO THE 45TH PRESIDENT (forthcoming 2017) (manuscript at 1), https://scholarworks.law.ubalt.edu/cgi/viewcontent.cgi?article=2017&context=all_fac.

13. Ramirez, *supra* note 4, at 2245.

14. *The State of Competition in the Health Care Marketplace: The Patient Protection and Affordable Care Act’s Impact on Competition: Hearing on Serial No. 114-46 Before the Subcomm. on Regulatory Reform, Commercial and Antitrust Law*, 114th Cong. 1, 3 (Sept. 10, 2015) (statement of Thomas L. Greaney, Professor) (noting that the ACA “relies on (1) competitive bargaining between payers and providers and (2) rivalry within each sector to drive price and quality to levels that best serve the public”).

15. See Julie Brill, Comm’r, Fed. Trade Comm’n, Keynote Address at Hal White Antitrust Conf. 1, 3–4 (June 9, 2014), https://www.ftc.gov/system/files/documents/public_statements/314861/140609halwhite.pdf (exclusively discussing hospital merger enforcement in a speech on health care and competition, including a historical discussion and specific discussion of recent Federal Trade Commission (FTC) hospital merger victories).

16. Deborah L. Feinstein, Dir., Bureau of Competition, Fed. Trade Comm’n, American Antitrust Institute Health Care Roundtable: Competition & Health Care—Enforcement & Policy Priorities 18 (Feb. 22, 2017), https://www.ftc.gov/system/files/documents/public_statements/1120623/feinstein_aai_speech_2-22-17.pdf.

17. See *id.*; DEP’T OF JUSTICE, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE (Aug. 1996), <https://www.justice.gov/sites/default/files/atr/legacy/2007/08/14/0000.pdf>.

In this void, private antitrust enforcement is essential to address market power in health care, and one that assumes a role that public enforcement cannot—or does not—presently fill.¹⁸

The insufficiency of public enforcement to address antitrust concerns in health care will likely only be exacerbated by the new presidential administration, under which at least one commentator has noted that “it is fair to expect some tempering of the level of activity that characterized the Obama administration.”¹⁹ Generally, Republican administrations are less likely to intervene in transactions and challenge the conduct of businesses, and despite some campaign rhetoric to the contrary, President Trump’s appointments seem to indicate an approach more in line with the party than with a new populism.²⁰ Of course, political influence is not limited to the federal realm; in states, the political priorities of elected attorneys general influence antitrust policy as well. Nevertheless, even the most aggressive public enforcement scheme would be incapable of addressing antitrust issues in health care without its private cousin.

What can private antitrust enforcement accomplish? Effective enforcement achieves deterrence, compensates victims,²¹ and maintains or restores competition in health care markets. Private enforcement allows health care entities to police their own markets and consumers to seek relief from anti-competitive acts. But it is often said that antitrust laws are meant to protect competition and consumers, not competitors.²² The concern is that entities, acting in their own self-interest, will use the antitrust laws to try to modify contracts, redress various business torts, stifle competition, and extort settlements from rivals.²³ Despite criticisms that private suits are self-interested and therefore anti-competitive, a lawsuit can be both self-interested and pro-

18. See *Palmyra Park Hosp. Inc. v. Phoebe Putney Memorial Hosp.*, 604 F.3d 1291, 1305 (11th Cir. 2010) (noting that due to limited resources, the government is not necessarily a better plaintiff than a competitor).

19. Maria Raptis, *Skadden Discusses Antitrust Enforcement in the Trump Administration*, THE CLS BLUE SKY BLOG (Apr. 19, 2017), <http://clsbluesky.law.columbia.edu/2017/04/19/skadden-discusses-antitrust-enforcement-in-the-trump-administration/> (last visited Oct. 27, 2017).

20. See *id.*

21. See Lande & Davis, *Comparative Deterrence*, *supra* note 6, at 315–18 (arguing that private antitrust litigation is more effective than DOJ criminal enforcement at deterring cartels); Lande & Davis, *Extraordinary Deterrence*, *supra* note 6, at 174.

22. Marivin Ammori, *Monopolies: Antitrust Law Protects Consumers, Not Competitors*, WIRED (Oct. 16, 2012, 3:00 PM), <https://www.wired.com/2012/10/antitrust-is-supposed-to-protect-consumers-not-competitors/>.

23. R. Preston McAfee et al., *Private Antitrust Litigation: Procompetitive or Anticompetitive?*, ANTITRUST DOCUMENTS GROUP 2–5 (Dec. 1, 2005), <https://www.justice.gov/atr/private-antitrust-litigation-procompetitive-or-anticompetitive>.

competitive.²⁴ Indeed, the antitrust laws were written to take advantage of private plaintiffs' incentives and information to bring suits that benefit both themselves and consumers.

Moreover, to limit the likelihood of abuse, courts have narrowed the per se doctrine, increased standing requirements,²⁵ and augmented the pleading standards; all of which deter frivolous, self-serving suits. In any event, studies have shown that antitrust actions by competitors in more concentrated markets, like health care markets, are more likely to be pro-competitive than they would be in more dispersed industries.²⁶ Some would argue that these measures even overdeter and overscreen.²⁷

How can private antitrust enforcement in health care be optimized? For plaintiffs, the key is overcoming the challenges in pursuing antitrust cases in health care. Those challenges fall into two groups: (1) those resulting from policies designed to decrease the incidence of self-serving and/or frivolous suits, and (2) those forming the essence of antitrust matters in health care. Understanding both sets is essential to optimizing private antitrust enforcement in health care. The first set requires plaintiffs to plead facts in light of new, more demanding standards to demonstrate antitrust injury and to attempt to certify classes of plaintiffs. The second set includes defining relevant markets and selecting claims for a lawsuit. Understanding the sources of these obstacles and how other recent plaintiffs have (or have failed to) overcome them is essential to optimizing private enforcement's role in addressing the competition problems in health care.

This article contains three parts. Part II describes how plaintiffs typically use private enforcement in health care services and insurance markets. Part III addresses the common challenges involved in private antitrust actions in health care and suggests strategies based on recent cases.

II. HOW PLAINTIFFS USE PRIVATE ANTITRUST ENFORCEMENT IN HEALTH CARE SERVICES AND INSURANCE MARKETS

Some practitioners and scholars have termed antitrust a "judicial enforcement (or 'law enforcement') model" because "the Sherman and Clayton Acts . . . creat[e] a species of common law, the meaning of which can evolve with changing conditions, which gives the federal courts a critical role in

24. See, e.g., *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-cv-1509-Orl-37DAB, 2015 WL 275806, at *7–8, *10 (M.D. Fla. Jan. 22, 2015) (holding that plaintiff whose interests overlapped with the public interest in competition among health care providers had standing).

25. See William Kolasky, *Antitrust Litigation: What's Changed in Twenty-Five Years?*, 27 ANTITRUST 9, 9–10, 12–13 (2012) (noting that the Supreme Court's changes to the antitrust standing requirement with the *Brunswick Corp. v. Pueblo Bowl-o-Mat* decision in 1977 put an end to the increase in number of antitrust suits (after a quadrupling in the decade prior)).

26. McAfee et al., *supra* note 23, at 12.

27. See Lande & Davis, *supra* note 12, at 1–2.

fashioning our competition laws.”²⁸ Accordingly, the development of antitrust law is a dynamic process that takes into account changing conditions for which the role of the federal courts cannot be understated.²⁹ Health care markets are certainly an area in which market conditions have changed over time, and courts and litigants have responded. Under these conditions, plaintiffs have evolved into litigants who prototype claims and analyses, not always certain how their experiments will turn out. The large majority of cases in this realm are brought under the Sherman Act, challenging either unilateral or concerted conduct,³⁰ or under Clayton Act Section 3, which proscribes exclusive dealing.³¹ Notwithstanding, some private litigants have brought merger challenges under Clayton Act Section 7, although informational asymmetries and injunctive remedies based on potential—as opposed to actual—damages discourage most plaintiffs from bringing these cases.³² Occasionally, a Clayton Act claim of an impermissible merger is just one claim of many in a private suit alleging a

28. Mark S. Popofsky & Douglas H. Halward-Driemeier, *Antitrust and the Roberts Court*, 28 ANTITRUST, Summer 2014, at 26, 26. Plaintiffs typically sue under the Sherman Antitrust Act, 15 U.S.C. §§ 1–7 (2012), and the Clayton Act, *id.* §§ 12–27; 29 U.S.C. §§ 52–53 (2012). In addition, most states (all but Pennsylvania) have antitrust statutes that are largely coextensive with federal law. See Dan Packer, *Pa. Sen. Proposes Antitrust Law as State Lags Behind Others*, LAW360 (Mar. 15, 2013, 5:15 PM), <https://www.law360.com/articles/424213/pa-sen-proposes-antitrust-law-as-state-lags-behind-others> (last visited Feb. 2, 2018). Further, many state antitrust statutes include a provision providing that federal antitrust precedents should be used as a guide in interpreting the state’s antitrust laws. See, e.g., VA. CODE ANN. § 59.1-9.17 (1974) (Construction of Chapter) (“This chapter shall be applied and construed to effectuate its general purposes in harmony with judicial interpretation of comparable federal statutory provisions.”).

29. Popofsky & Halward-Driemeier, *supra* note 28, at 26.

30. 15 U.S.C. §§ 1–2 (2012).

31. *Id.* § 14.

32. The government typically has more information about upcoming mergers in light of the federal merger pre-notification program created in 1976 by the Hart-Scott-Rodino Antitrust Improvements Act, 15 U.S.C. § 18(a) (2012). Parties planning mergers of a certain size must notify the FTC and the DOJ (the antitrust agencies) in advance of proposed deals. Lisl Dunlop & Shoshana Speiser, *Merger Control in the United States: Overview*, THOMSON REUTERS PRACTICAL LAW (June 1, 2017), [https://content.next.westlaw.com/Document/Ieb49d8761cb511e38578f7ccc38dcbec/View/FullText.html?contextData=\(sc.Default\)&transitionType=Default&firstPage=true&bhcp=1](https://content.next.westlaw.com/Document/Ieb49d8761cb511e38578f7ccc38dcbec/View/FullText.html?contextData=(sc.Default)&transitionType=Default&firstPage=true&bhcp=1). After filing the required pre-merger notification forms, the entities may not complete the deal until the waiting period expires, the antitrust agencies terminate the waiting period early, or until they participate in a more extensive review following a “Second Request” for more information. *Id.* However, occasionally private plaintiffs file merger challenges and the FTC or DOJ follows. See *Saint Alphonsus Med. Ctr.-Nampa, Inc. v. St. Luke’s Health Sys., Ltd.*, 778 F.3d 775, 782 (9th Cir. 2015), *aff’g* 2014 WL 407446 (D. Idaho 2014); Bruce D. Sokler et al., *Hospital Wins First Round Against Largest Rival in Antitrust Suit Alleging Illegal Exclusive Dealing Agreements with Insurers*, HEALTH CARE ANTITRUST ALERT (Mar. 30, 2015), <https://www.mintz.com/newsletter/2015/Advisories/4811-0315-NAT-AFR-HC/> (“It will likely be a historical footnote that the FTC’s seminal *St. Luke’s* case began as private litigation brought by a rival hospital before the FTC or the Idaho Attorney General ever showed up.”).

scheme of monopolization and exclusive dealing arrangements in provider-insurer contracts.³³

In light of the breadth and flexibility of the antitrust statutes, the same facts that give rise to an antitrust lawsuit often give rise to other claims. For example, a hospital suing another hospital and insurer based on provisions contained in the defendants' contracts might bring the suit as a conspiracy in restraint of trade under Sherman Act Section 1, which may involve allegations of exclusive dealing arrangements, tying, a group boycott or concerted refusal to deal, and/or as a monopolization or conspiracy to monopolize case that describes the same conduct. The recent fact patterns of several cases in this area are described below:

A. Providers as Plaintiffs

- A surgical hospital sues a larger hospital(s) and/or insurer, and/or managed care organization alleging the defendants acted to keep it out of the market for surgical services by conspiring or illegally contracting with other providers and/or insurers.³⁴
- Physician groups sue a health care corporation comprised of hospital and insurance plan alleging the health care giant used its market power, gained in part from anti-competitive mergers, to obtain exclusive referral arrangements aimed at eliminating competitors.³⁵
- A specialty practice sues a hospital and an insurer for forming a Health Maintenance Organization (HMO) and excluding the specialty practice from the HMO's network.³⁶
- Providers and insurance subscribers sue a large insurance company alleging horizontal market allocation.³⁷
- A large hospital sues a competitor hospital alleging that the competitor, the only local provider of essential services, used its status as a "must-

33. See Third Amended Complaint at 64, 66, 70, 73, 77, 80, 84, 88, 92, *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-CV-01509-RBD-DAB (M.D. Fla. May 22, 2014).

34. See, e.g., *Med. Ctr. at Elizabeth Place, LLC v. Atrium Health Sys.*, 817 F.3d 934, 936 (6th Cir. 2016); *Arapahoe Surgery Ctr., LLC v. Cigna Healthcare, Inc.*, 80 F. Supp. 3d 1257, 1260–61 (D. Colo. 2015); *Heartland Surgical Specialty Hosp., LLC v. Midwest Div., Inc.*, 527 F. Supp. 2d 1257, 1263–64 (D. Kan. 2007); *Surgical Care Ctr. of Hammond, L.C. v. Hosp. Serv. Dist. No. 1 of Tangipahoa Par.*, 309 F.3d 836, 838 (5th Cir. 2002); *Marion HealthCare LLC v. S. Ill. Healthcare*, 2013 WL 4510168, at *1–2 (S.D. Ill. Aug. 26, 2013).

35. *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-CV-1509-ORL-37DAB, 2015 WL 275806, at *1 (M.D. Fla. Jan. 22, 2015); *N.M. Oncology and Hematology Consultants v. Presbyterian Healthcare Servs.*, 54 F. Supp. 3d 1189, 1197 (D.N.M. 2014).

36. *Little Rock Cardiology Clinic v. Baptist Health*, 591 F.3d 591, 594 (8th Cir. 2009).

37. *In re Blue Cross Blue Shield Antitrust Litig.*, No. 2:13-CV-20000-RDP, 2017 WL 2797267, at *2, *6 (N.D. Ala. 2017).

have” participating provider to obtain exclusive dealing arrangements with commercial health insurers.³⁸

- A hospital sues a competitor hospital alleging the competitor “leveraged a state-granted monopoly in certain medical services” to exclude the hospital from local insurance companies’ provider networks by tying favorable insurance reimbursement rates for monopolized services to a refusal to include the plaintiff hospital in the insurance companies’ networks.³⁹
- A large hospital with its own health plan sues a large insurance company alleging the insurance company attempted to block both the hospital’s acquisition of a general acute care community hospital and its entry into the insurance market.⁴⁰

B. Payors as Plaintiffs

- An insurance company sues a competitor insurance company for using most favored nations clauses in insurer-provider contracts alleging that the exclusionary clauses drove up health care costs and inhibited competition.⁴¹
- Self-funded payors sue a large hospital alleging it overpaid for health insurance because of contracts with insurance entities that contained anti-competitive provisions.⁴²

C. Consumers as Plaintiffs

- Purchasers of commercial health insurance sue a large hospital alleging the hospital overpaid for health insurance because of provider-insurer contracts that contained anti-competitive provisions that require the

38. *Methodist Health Servs. Corp. v. OSF Healthcare Sys.*, 859 F.3d 408, 409–10 (7th Cir. 2017); Complaint at 1–2, *Marion HealthCare, LLC v. S. Ill. Healthcare*, No. 3:12-cv-00871-JPG-PMF (S.D. Ill. Aug. 3, 2012).

39. *Palmyra Park Hosp., Inc. v. Phoebe Putney Mem’l Hosp.*, 604 F.3d 1291, 1294 (11th Cir. 2010).

40. *Steward Health Care Sys., LLC v. Blue Cross Blue Shield of R.I.*, 997 F. Supp. 2d 142, 148–49 (D.R.I. 2014).

41. *Aetna, Inc. v. Blue Cross Blue Shield of Mich.*, No. 11–15346, 2012 WL 2184568, at *1 (E.D. Mich. June 14, 2012). This lawsuit was a “follow-on” case to the government case of *United States v. Blue Cross Blue Shield of Michigan*, which the government voluntarily dismissed after the Michigan state legislature passed a law banning most favored nations clauses in provider-insurer contracts. See Press Release, U.S. Department of Justice, Justice Department Files Motion to Dismiss Antitrust Lawsuit Against Blue Cross Blue Shield of Michigan After Michigan Passes Law to Prohibit Health Insurers from Using Most Favored Nation Clauses in Provider Contracts (Mar. 25, 2013), <https://www.justice.gov/opa/pr/justice-department-files-motion-dismiss-antitrust-law-suit-against-blue-cross-blue-shield> (last visited Nov. 11, 2017).

42. *UFCW & Emp’rs Benefit Tr. v. Sutter Health*, 194 Cal. Rptr. 3d 190, 193 (Cal. Ct. App. 2015).

insurer to buy all or none of the hospital's services and/or prevent insurer from steering patients to lower-priced providers.⁴³

- Individual and small-employer customers sue a large insurance company alleging horizontal market allocation.⁴⁴

These lawsuits, which seek to combat the effects of market power in health care services and insurance markets, have sprung up in response to the growing consolidation in those markets, and, accordingly, are a relatively recent phenomenon. As a consequence, there is no set structure for a complaint; rather, each plaintiff tends to select claims based on case-specific facts and litigation strategy. Nonetheless, all plaintiffs must deal with the following key challenges in litigating their cases.

III. KEY CHALLENGES

A. Policy-Driven Challenges

The first key set of challenges plaintiffs face in private antitrust suits are those which result from “tort reform,” a term that generally refers to changes to the civil justice system to reduce the number of cases filed by plaintiffs, the number of cases that survive past the earliest stages of litigation, and/or the amount of damages plaintiffs receive.⁴⁵ Though not based on tort statutes, courts in private antitrust cases have imposed the same types of limiting mechanisms that ostensibly seek to deter or dispense frivolous lawsuits. In antitrust cases, tort reform changes began in the late 1970s when, after early enthusiasm by Congress and the courts over private litigants' role as “private attorneys general,”⁴⁶ the Supreme Court issued a series of decisions that reined in private antitrust suits by narrowing the per se doctrine and tightening standing requirements.⁴⁷ After years of abridgment, today the per se rule only extends to “‘naked’ price fixing and market division agreements, a small subset of boycotts, or concerted refusals to deal, and—by a very thin thread—some tying

43. *Sidibe v. Sutter Health*, 51 F. Supp. 3d 870, 872–75 (N.D. Cal. 2014), *rev'd*, 667 F. App'x 641 (9th Cir. 2016); Complaint at 2, *DiCesare v. Charlotte-Mecklenburg Hosp. Auth.*, 2017 WL 1359599 (N.C. Super. Ct. Apr. 11, 2017) (No. 2016 CVS 16404).

44. *In re Blue Cross Blue Shield Antitrust Litig.*, 2017 WL 2797267 (N.D. Ala. 2017); *In re Blue Cross Blue Shield Antitrust Litig.*, 26 F. Supp. 3d 1172, 1179–81 (N.D. Ala. 2014).

45. *See, e.g., Tort Reform*, BLACK'S LAW DICTIONARY (10th ed. 2014).

46. *Hawaii v. Standard Oil Co. of Cal.*, 405 U.S. 251, 262 (1972); *accord Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 635 (1985) (“A claim under the antitrust laws is not merely a private matter.”) (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.* 723 F.2d 155, 168 (1st Cir. 1983); *Am. Safety Equip. Corp. v. J.P. Maguire & Co., Inc.* 391 F.2d 821, 826 (2d Cir. 1968)).

47. *See, e.g., Brunswick Corp. v. Pueblo Bowl-o-Mat, Inc.*, 429 U.S. 477, 489 (1977). Around that time, the Supreme Court also began to limit the per se doctrine, which gives a stronger presumption of unreasonableness to certain restraints on trade. *See William Kolasky, Antitrust Litigation: What's Changed in Twenty-Five Years*, 27 ANTITRUST 9, 11 (2012).

arrangements.”⁴⁸ More recently, in the early 2000s, in response to perceived abuses by the plaintiffs’ bar in the form of large class actions, the Supreme Court revised antitrust pleading requirements and then all federal pleading requirements to prevent meritless cases from proceeding to discovery.⁴⁹ As a result, all plaintiffs in health care antitrust cases face certain procedural obstacles as they navigate a system designed to winnow out cases at the earliest stages.

1. Per se versus Rule of Reason

The per se rule is the judicially created concept that some antitrust violations are so inherently illegal that plaintiffs need to plead and prove only that the conduct occurred;⁵⁰ the anti-competitive effects are implied. After a high point in the mid-twentieth century, when numerous antitrust offenses received per se treatment, the doctrine has been increasingly limited, either by express overruling or increased dubiousness.⁵¹ Instead, the rule of reason, “which requires the plaintiff to plead and prove that defendants with market power have engaged in anticompetitive conduct,”⁵² has become the dominant rubric of judicial analysis. Under the rule of reason, the court conducts a balancing inquiry that determines whether the alleged restraint is reasonable, and, if so, it passes antitrust scrutiny.⁵³ Matters are further complicated for litigants by the fact that it is not always clear whether a case will receive per se or rule of reason treatment until close to its resolution. A plaintiff who arrives at summary judgment having declined to prove a case under the rule of reason takes a significant risk⁵⁴ because the court could ultimately decide not to apply per se treatment at summary judgment:

[I]f there is any reasonable chance that the court will ultimately require the rule of reason, the plaintiff has no choice but to proceed through discovery under that rule even if the chance is small. This means that the value of the per se rule is lost in a significant number of cases, because the plaintiff must do all of the things that rule of reason analysis requires, including developing expert testimony on questions about relevant market, market power, and anticompetitive effects, even though the case may ultimately be decided under the per se rule. At least prior to trial, the greatest cost in litigating a rule of reason

48. Herbert J. Hovenkamp, *The Rule of Reason*, PENN L.: LEGAL SCHOLARSHIP REPOSITORY 1, 2 (July 2017), http://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2780&context=faculty_scholarship (last visited Nov. 11, 2017).

49. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 556, 559 (2007); *Ashcroft v. Iqbal*, 556 U.S. 662, 678–79, 684 (2009).

50. *See N. Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958).

51. Hovenkamp, *supra* note 48, at 41.

52. *Id.* at 2.

53. *See* PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION* 380–81 (3d ed. 2010).

54. *See* Hovenkamp, *supra* note 48, at 9.

case is the cost of developing a record, so most of the cost savings that the per se rule promises will have been lost.⁵⁵

In recognition of this predicament, most plaintiffs err on the side of putting together a case that anticipates rule of reason analysis.

In health care, some plaintiffs who have recently pursued exclusively per se cases have failed to convince the court of this course, warning future plaintiffs of the risks of such a strategy. For example, in one of the cases related to most favored nations clauses in provider-insurer contracts in Michigan, the plaintiff lost a motion to dismiss after committing to a per se pleading strategy.⁵⁶ A number of other district courts have likewise made clear that vertical arrangements, including contracts and agreements between hospitals and insurers that are often the subject of lawsuits in this arena, receive rule of reason treatment.⁵⁷ More recently, in *Medical Center at Elizabeth Place v. Premier Health Partners*, a hospital plaintiff, MCEP, that sued the partners of competitor hospital group's joint venture, claiming the joint venture was a conspiracy to orchestrate a group boycott (a "non-venture") to exclude the plaintiff from managed care contracts, physicians, and funding, lost at summary judgment because of its per se case.⁵⁸ The district court declined to offer per se treatment to the allegations noting that the Supreme Court had a presumption of rule of reason analysis particularly with regard to vertical restraints in antitrust cases and quoted the Supreme Court's admonition that "easy labels do not always supply ready answers."⁵⁹ As part of its lengthy analysis, the district court seemed somewhat swayed by the fact that one of the main restraints at issue in the case the "panel limitations" clause in contracts between the joint venture member

55. *Id.* at 10.

56. *City of Pontiac v. Blue Cross Blue Shield of Mich.*, No. 11-10276, 2012 WL 1079895, at *8 (E.D. Mich. Mar. 30, 2012).

57. *Marion Healthcare, LLC v. S. Ill. Healthcare*, No. 12-CV-00871-DRH-PMF, 2013 WL 4510168, at *9 (S.D. Ill. Aug. 26, 2013) (agreeing with the defendant that rule of reason is appropriate for a case challenging allegedly exclusionary contracts between defendant hospital and insurer); *Methodist Health Servs. Corp. v. OSF Healthcare Sys.*, No. 1:13-cv-01054-SLD-JEH, 2015 WL 1399229, at *4, *8 (C.D. Ill. Mar. 25, 2015) (deciding ultimately on foreclosure grounds under a rule of reason analysis at summary judgment); *see also Prime Healthcare Servs., Inc. v. Serv. Emps. Int'l Union*, No. 11-cv-2652-GPC-RBB, 2013 WL 3873074, at *11 (S.D. Cal. July 25, 2013), *aff'd*, 642 F. App'x 665 (9th Cir. 2016); *Rheumatology Diagnostics Lab., Inc. v. Aetna, Inc.*, No. 12-cv-05847-JST, 2013 WL 3242245, at *9 (N.D. Cal. June 25, 2013).

58. *Med. Ctr. at Elizabeth Place, LLC v. Premier Health Partners*, No. 3:12-cv-26, 2017 WL 3433131, at *1 (S.D. Ohio Aug. 9, 2017).

59. *Id.* at *2 (citing *Broadcast Music, Inc. v. Columbia Broadcast Sys., Inc.*, 441 U.S. 1, 8 (1979)). This case's loss was particularly tragic for the plaintiff because, after winning on appeal to the Sixth Circuit Court of Appeals, which overturned the district court's ruling on summary judgment that the defendants were a single entity and therefore incapable of a conspiracy, they returned to district court, only to lose because their case was brought under the per se rule instead of the rule of reason. *See id.* at *1, *6.

hospital defendants and their contracted insurers was a vertical, as opposed to horizontal, restraint.⁶⁰ That clause provided that if the insurer were to add other hospitals to its provider network, the hospital would have the option to terminate the contract or renegotiate its rates for health care services.⁶¹ Plaintiff MCEP argued that the restraint deserved per se treatment because the restraint's operation excluded the plaintiff, a *horizontal* competitor, from the market, which the court concluded was too far of a logical leap.⁶²

The obvious takeaway is that even for a conspiracy case among horizontal competitors, like the group boycott and especially one that involves provider-insurer contracts, as so many of these cases do, the plan should be to plead and prove the case under a rule of reason rubric. Thus, even when pleading these cases as conspiracies (as is often the case),⁶³ plaintiffs should be prepared to establish all facets of a rule of reason case.⁶⁴ Because, as the court pointed out in *Elizabeth Place*, the restraints at issue are often *vertical*, even when an alleged horizontal conspiracy is involved (e.g., competitor hospital alleges that rival hospitals conspired to exclude it from the market by obtaining exclusivity from all local insurers), the likelihood of obtaining per se treatment is low.⁶⁵ Given the importance of surviving beyond the pleading stage of private litigation, this strategy is even more salient.

2. *Twiqbal*

Despite developing after the antitrust standing doctrine, new pleading standards affect all elements of a plaintiff's case, including standing; this article will discuss them first. In 2007, and again in 2009, the Supreme Court overhauled the federal civil pleading standards for the first time in sixty years, raising the bar considerably for surviving a motion to dismiss for failure to state a claim.⁶⁶ Prior to 2007, the federal pleading standard under Rule 8(a) of the Federal Rules of Civil Procedure (FRCP Rule 8) required a "short and plain statement of the claim showing that the pleader is entitled to relief."⁶⁷ The Supreme Court's longstanding interpretation of FRCP Rule 8 was that it required

60. *Id.* at *14.

61. *Id.*

62. *Med. Ctr. at Elizabeth Place*, 2017 WL 3433131, at *14.

63. *See, e.g., id.* at *4; *Arapahoe Surgery Ctr., LLC v. Cigna Healthcare, Inc.*, 80 F. Supp. 3d 1257, 1261 (D. Colo. 2015); *Heartland Surgical Specialty Hosp., LLC v. Midwest Div., Inc.*, 527 F. Supp. 2d 1257, 1263 (D. Kan. 2007).

64. Plaintiffs must establish the following: (1) the defendants conspired; (2) the conspiracy produced anti-competitive effects in the relevant product and geographic markets; (3) the conduct was illegal; and (4) the scheme was the proximate cause of the plaintiff's antitrust injury. *Med. Ctr. at Elizabeth Place*, 2017 WL 3433131, at *3.

65. *Id.* at *15.

66. *See Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 555–56 (2007); *Ashcroft v. Iqbal*, 556 U.S. 662, 678, 684 (2009).

67. FED. R. CIV. P. 8(a)(2) (2016).

“notice pleading”—i.e., “a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove *no set of facts* in support of his claim which would entitle him to relief.”⁶⁸ The deferential “no set of facts” standard—in place from 1957 to 2007—gave the benefit of the doubt to the plaintiff, who, as a matter of policy, was presumed to bring a legally viable claim unless such claim was essentially inconceivable under the facts alleged in the complaint.

This changed in 2007 in *Bell Atlantic Corp. v. Twombly* when the Supreme Court ruled that to plead a Sherman Act Section 1 conspiracy claim, a plaintiff must give the court “*plausible* grounds to infer an agreement” by filing “a complaint with enough factual matter (taken as true) to suggest that an agreement was made.”⁶⁹ At first, the new plausibility standard was limited to antitrust conspiracy claims under the Sherman Act. Then, two years later in *Ashcroft v. Iqbal*, the Court extended the plausibility standard to *all* federal claims brought under Rule 8 in federal court and provided further guidance for applying the new standard.⁷⁰ The cases are often discussed and cited together and have even been given the moniker *Twiqbal* as a shorthand.

The policy behind the *Twombly* decision was to rein in the perceived misuse of the courts by private litigants, especially through class action attorneys, filing baseless lawsuits aimed at lucrative damages awards or, more commonly, settlements.⁷¹ *Twombly* was part of a larger effort by the Supreme Court to discourage the proliferation of large class action suits based on thinly pled allegations. The Court cited repeatedly to its decision of two years prior in *Dura Pharmaceuticals, Inc. v. Broudo* in which it required a higher showing of causation at the pleading stage in securities fraud cases, and *Twombly* made sense in that context.⁷² The Court’s extension of *Twombly*’s new rule to all federal claims two years later in *Iqbal* was both much more expansive and more fraught with controversy. For starters, unlike *Twombly*, *Iqbal* was not a class action nor an antitrust case nor even a case involving allegations of corporate malfeasance; instead, it was a *Bivens* action, which is an individual’s suit against

68. *Conley v. Gibson*, 355 U.S. 41, 45–47 (1957) (emphasis added), *abrogated by* *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007).

69. *Twombly*, 550 U.S. at 556 (emphasis added).

70. *Iqbal*, 556 U.S. at 684.

71. *Twombly*, 550 U.S. at 557–59 (“[T]he threat of discovery expense will push cost-conscious defendants to settle even anemic cases before reaching those proceedings. Probably, then, it is only by taking care to require allegations that reach the level suggesting conspiracy that we can hope to avoid the potentially enormous expense of discovery in cases with no ‘reasonably founded hope that the [discovery] process will reveal relevant evidence’ to support a § 1 claim.”) (alteration in *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 347 (2005)) (quoting *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 741 (1975)).

72. *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 346–47 (2005); *Twombly*, 550 U.S. at 557, 557–59, 562 (citing *Dura Pharm.*, 544 U.S. at 346, 347).

a federal officer alleged to have violated the plaintiff's constitutional rights.⁷³ In other words, whereas *Twombly* fit the mold of the type of case criticized as an instance of opportunistic plaintiffs' lawyers suing deep-pocketed corporate defendants hoping for a settlement, *Iqbal* most certainly did not. The plaintiff-respondent *Iqbal* had been detained in connection with investigations into the September 11, 2001, attacks and had filed suit against multiple federal officials.⁷⁴ In addition, the Supreme Court held that *Twombly* applied to *all* federal pleadings, and "facts" that were nothing more than legal conclusions would no longer suffice in federal pleading; instead, "only a complaint that states a *plausible* claim for relief survives a motion to dismiss."⁷⁵ The Court then explained the new process lower courts should use: "Determining whether a complaint states a plausible claim for relief will . . . be a context-specific task that requires the reviewing court to draw on its judicial experience and common sense."⁷⁶ In other words, the new plausibility standard was both flexible and subjective. Critics argued that the purpose of the FRCP, enacted almost seventy years earlier, was to increase ordinary citizens' access to the federal courts by simplifying the historically more technical code pleading, which *Iqbal* directly contravened.⁷⁷

Opinions about the actual effects of the new plausibility standards on federal cases are varied. A major study conducted by the Federal Judicial Center in 2011 concluded that on the whole "*Twombly* and *Iqbal* have had a modest effect on the resolution of Rule 12(b)(6) motions."⁷⁸ Other studies likewise have found no statistically significant effect on dismissal rates.⁷⁹ However, studies focused on dismissal rates may ignore "selection effects," meaning the deterrent effects on plaintiffs who may decide not to file a case at all in light of the new

73. *Iqbal*, 556 U.S. at 668, 676.

74. *Id.* at 668 (naming as defendants: John Ashcroft, the former Attorney General of the United States, and Robert Mueller, then Director of the Federal Bureau of Investigation).

75. *Id.* at 679 (emphasis added).

76. *Id.* (citing the decision on appeal from the Court of Appeals for the Second Circuit, *Iqbal v. Hasty*, 490 F.3d 143, 157–58 (2007)).

77. See, e.g., Arthur R. Miller, *From Conley to Twombly to Iqbal: A Double Play on the Federal Rules of Civil Procedure*, 60 DUKE L.J. 1, 9–10 (2010) ("Federal civil procedure has been politicized and subjected to ideological pressures. Thus, the Supreme Court's recent decisions in *Bell Atlantic Corp. v. Twombly* and *Ashcroft v. Iqbal* should be seen as the latest steps in a long-term trend that has favored increasingly early case disposition in the name of efficiency, economy, and avoidance of abusive and meritless lawsuits. It also marks a continued retreat from the principles of citizen access, private enforcement of public policies, and equality of litigant treatment in favor of corporate interests and concentrated wealth. To a significant degree, the liberal-procedure ethos of 1938 has given way to a restrictive one.") (footnotes omitted).

78. Kevin R. Reich, *Five Years After Twombly: Where Are We Now?*, 10 ABA ANTITRUST SEC. JOINT CONDUCT COMMITTEE E-BULL. no. 1, 2012, at 2.

79. William H. J. Hubbard, *The Effects of Twombly and Iqbal*, 14 J. EMPIRICAL LEGAL STUD. 474, 475 (2017).

plausibility requirement.⁸⁰ And aggregate effects aside, plaintiffs are required to plead their cases in light of the new standard, which comes up in courts' standing analyses as well as substantive considerations like market definition, discussed in Part III.

3. Antitrust Standing

Antitrust standing, a creature of the common law, imposes a more onerous showing than its older cousin, constitutional standing.⁸¹ Of course, plaintiffs in antitrust suits also must have Article III standing to bring their cases,⁸² but the inquiry is usually collapsed into one "antitrust standing" analysis, whose requirements are often distilled into two prongs: A plaintiff must show (1) he has suffered *antitrust* injury and (2) that he is an efficient enforcer, i.e., the appropriate plaintiff to bring suit.⁸³ First, the antitrust injury requirement ensures both that the defendant harmed *competition or markets* (and not just the plaintiff, in a more tort-like sense) and that the plaintiff was injured in fact either as a direct market participant or as being "inextricably intertwined" with the harm resulting from the anti-competitive scheme.⁸⁴ Next, the efficient enforcer requirement ensures that the plaintiff be not too remote, i.e., has suffered directly from the defendant's conduct,⁸⁵ and is therefore the best plaintiff to bring suit; otherwise the best plaintiff might try to sue later on (potentially after damages have been awarded to the inferior plaintiff).

80. *Id.* at 476.

81. See generally *Brunswick Corp. v. Pueblo Bowl-o-Mat, Inc.*, 429 U.S. 477, 489 (1977); see also John J. Miles, *HEALTH CARE AND ANTITRUST LAW*, § 9:7 n.4 (2017) (collecting cases).

82. See Jonathan M. Jacobson & Tracy Greer, *Twenty-One Years of Antitrust Injury: Down the Alley with Brunswick v. Pueblo Bowl-o-Mat*, 66 *ANTITRUST L.J.* 273, 288 n.104 (1998) (citing *Sanner v. Chicago Bd. of Trade*, 62 F.3d 918, 922–27 (7th Cir. 1995); *Malamud v. Sinclair Oil Corp.*, 521 F.2d 1142, 1152 (6th Cir. 1975)).

83. *Associated Gen. Contractors of Cal., Inc. v. Cal. State Council of Carpenters*, 459 U.S. 519, 535 n.31 (1983); Miles, *supra* note 81, at § 9:7 n.4.

84. *Blue Shield of Va. v. McCready*, 457 U.S. 465, 483–84 (1982) (noting that although the plaintiff was not a competitor or customer of the defendant, the plaintiff's injury was "inextricably intertwined" with the injury the defendants intended to inflict on the market and others, i.e., it "flow[ed] from that which makes defendants' acts unlawful" within the meaning of *Brunswick*, and [fell] squarely within the area of congressional concern").

85. See Jacobson & Greer, *supra* note 82, at 288. The danger of allowing recovery by a remote plaintiff is that a more directly injured plaintiff would later sue, and the defendant would be put at risk of another set of damages. Examples of ill-suited antitrust plaintiffs who typically cannot meet the standing requirement "include officers, employees, shareholders, prospective shareholders, creditors, guarantors, distributors, brokers, sales representatives, and suppliers of businesses injured by the violation." Miles, *supra* note 81, at § 9:7.

a. Antitrust Injury

Following an uptick in antitrust cases filed by competitors in the mid-twentieth century, courts became concerned that businesses were using the antitrust statutes as federal business tort statutes unrelated to competition or consumers. In response, in 1977, the Supreme Court clarified in *Brunswick Corp. v. Pueblo Bowl-o-Mat, Inc.* that to use the Clayton Act's private right of action, a plaintiff must show "antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation."⁸⁶ In *Brunswick*, the Court echoed the seminal *Brown Shoe Co. v. United States*, explaining: "The antitrust laws, however, were enacted for 'the protection of competition, not competitors.'"⁸⁷ The Supreme Court further clarified in 1990 that antitrust injury required some showing of public harm.⁸⁸ The issues of relative injury to the plaintiff and competition have come up in two recent antitrust cases brought by hospitals. In *Methodist Health Services Corp. vs. OSF Healthcare System*, the Seventh Circuit affirmed the district court's grant of summary judgment for the defendant, expressing doubt over the plaintiff's contention that it had brought its case to restore competition on behalf of multiple injured parties, none of whom were party to the lawsuit, and concluded that the plaintiff was "simply an unsuccessful competitor."⁸⁹ On the other hand, in another recently settled district court case, *Omni Healthcare, Inc. v. Health First, Inc.*, the district court in Florida made clear it would redress injuries that were more personal to the plaintiff so long as those injuries coincided with an injury to competition and also resulted from the same conduct of the defendant.⁹⁰ Plaintiffs also must show that they suffered direct harm; such harm is presumed for competitors and direct customers but not for those who are not participants in the relevant antitrust market.⁹¹ Some courts include this analysis when considering a plaintiff's remoteness in the antitrust injury prong, determining whether the plaintiff was "inextricably intertwined" with the harm resulting from the defendant's conduct, whereas other courts do an almost identical analysis under the "efficient enforcer" prong, discussed below.

86. *Brunswick Corp. v. Pueblo Bowl-o-Mat, Inc.*, 429 U.S. 477, 489 (1977). *Brunswick* was a Clayton Act case, but subsequent Supreme Court cases made clear that the *Brunswick* rule applied equally to cases under the Sherman Act. See *Blue Shield of Va.*, 457 U.S. at 482 (applying the antitrust injury rule to a claim brought under Sherman I); *Atl. Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 334–335 (1990) (holding that antitrust injury is an essential element of every private antitrust case, irrespective of the substantive theory of liability); see also Jacobson & Greer, *supra* note 82, at 282.

87. *Brunswick Corp.*, 429 U.S. at 488 (citing *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962)). This definition of "antitrust injury" was extended to Section 16 cases for injunctive

b. Efficient Enforcer

For the purpose of antitrust standing analysis, the law favors direct consumers or customers as plaintiffs.⁹² Notwithstanding that preference, in determining whether the plaintiff is an efficient enforcer of the antitrust laws, courts in the health care cases at issue vary in their rigidity of applying a presumption in favor of a customer or competitor in light of the particular characteristics and constituents of those health care markets. As described in Part II, recent cases in this arena have seen plaintiffs as the following: hospitals, ambulatory surgery centers, physician groups, insurance companies, insurance subscribers, and patients. One recent district court clarified that “[t]here is no ‘bright-line rule’ for determining whether a plaintiff is an efficient enforcer,” and instead of strictly assessing the role played by the plaintiff in the market at issue, “the ‘efficient enforcer’ requirement ensures that the ‘particular plaintiff will efficiently vindicate the goals of the antitrust laws.’”⁹³ Moreover, in cases where a plaintiff is not a customer or competitor precisely because of being excluded from the market by the defendant’s anti-competitive conduct, courts are cognizant that to deny standing on that basis would be inconsistent with the policy behind the antitrust laws.⁹⁴ Finally, courts have demonstrated awareness of “efficient enforcer” issues that are inherent in the structure of health care markets, where patients may be customers of insurance companies but not of providers, who receive payment directly from insurers instead of patients and, in such a scenario, have recognized the antitrust standing of insurance plan

relief in 1986. *Cargill, Inc. v. Monfort of Colo., Inc.*, 479 U.S. 104, 122 (1986); see also CHRISTINE L. WHITE ET AL., ANTITRUST AND HEALTHCARE: A COMPREHENSIVE GUIDE 61 (2013).

88. *Atl. Richfield Co.*, 495 U.S. at 334; see also Jacobson & Greer, *supra* note 82, at 284.

89. *Methodist Health Servs. Corp. v. OSF Healthcare Sys.*, 859 F.3d 408, 411 (7th Cir. 2017).

90. *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-CV-1509-ORL-37DAB, 2015 WL 275806, at *8 (M.D. Fla. Jan. 22, 2015) (citing *Todorov v. DCH Healthcare Auth.*, 921 F.2d 1438, 1450 (11th Cir. 1991)).

91. *Blue Shield of Va.*, 457 U.S. at 472, 480, 483–84 (noting that although the plaintiff was not a competitor or customer of the defendant, the plaintiff’s injury was “inextricably intertwined” with the injury the defendants intended to inflict on the market and others, i.e., it “flow[ed] from that which makes defendants’ acts unlawful’ within the meaning of *Brunswick*, and [fell] squarely within the area of congressional concern”).

92. See, e.g., *Associated Gen. Contractors of Cal., Inc. v. Cal. State Council of Carpenters*, 459 U.S. 519, 544–545 (1983); Miles, *supra* note 81, at § 9:7 n.4.

93. *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-CV-1509-ORL-37DAB, 2015 WL 275806, at *7 (M.D. Fla. Jan. 22, 2015) (quoting *Todorov v. DCH Healthcare Auth.*, 921 F.2d 1438, 1452 (11th Cir. 1991)).

94. See, e.g., *Steward Health Care Sys., LLC v. Blue Cross & Blue Shield of R.I.*, 997 F. Supp. 2d 142, 160 (D.R.I. 2014) (“To permit the defendant in an unlawful exclusion case to hide behind the presumptive disfavoring of non-market participants would subject plaintiffs in such cases to an insurmountable Catch–22. Were courts to observe a blanket prohibition on claims brought by those excluded from the market by alleged anticompetitive conduct, those firms responsible for the exclusion might never be held accountable.”).

subscribers to sue a provider who contracts with their insurance company.⁹⁵ Defendants have largely been unsuccessful in using the Indirect Purchaser Rule, or *Illinois Brick Co. v. Illinois* Doctrine, which states that only direct purchasers may sue for antitrust violations in these cases.⁹⁶

In the recent case *Palmyra Park Hospital, Inc. v. Phoebe Putney Memorial Hospital*, the Eleventh Circuit Court of Appeals overruled the district court's dismissal on the grounds that the plaintiff hospital was not an "efficient enforcer," and therefore the plaintiff lacked standing.⁹⁷ In that case between two competing Georgia hospitals, Palmyra alleged that Phoebe Putney had used its monopoly power (state-granted by way of a certificate of need) to demand that Blue Cross and other insurers exclude Palmyra from their provider networks.⁹⁸ Specifically, Palmyra claimed that Phoebe Putney tied favorable reimbursement rates to a refusal to include Palmyra in those networks so that insurers who included Palmyra in their networks would have to pay Phoebe Putney more for the same health care services.⁹⁹ The Eleventh Circuit's analysis focused on the particular features of health care markets, which led to the holding that Palmyra is not only an efficient enforcer but also an ideal plaintiff to bring this suit.¹⁰⁰ Whereas the district court had concluded that "[t]he most direct affect [sic] of Defendants' alleged anticompetitive conduct would be felt by the allegedly coerced insurers who pay higher reimbursement rates and the patients who ultimately pay higher premiums and co-pays for medical services,"¹⁰¹ the appellate court, after analyzing the incentives at play, concluded that those insurers had suffered little harm and therefore were unlikely plaintiffs.¹⁰² In fact, once the tie was in place (i.e., Blue Cross and others agreed to exclude Palmyra from its networks in exchange for better reimbursement rates),¹⁰³ it is unclear that the insurers would be paying higher rates at all, and to the extent they were, the cost could easily be passed on to their subscribers. Thus, the insurers had

95. See, e.g., *Sidibe v. Sutter Health*, 4 F. Supp. 3d 1160, 1173 n.7, 1181 (N.D. Cal. 2013) (dismissing second amended complaint on other grounds).

96. See, e.g., *id.* at 1173 n.7 (noting that patients who sued hospital based on its allegedly competitive contracts with the insurers whose health plans plaintiffs subscribed to had standing); cf. *Med. Sav. Ins. Co. v. HCA, Inc.*, No. 2:04CV156FTM-29DNF, 2005 WL 1528666, at *2, *8 (M.D. Fla. June 24, 2005) (involving an insurance company that had no contracts with hospitals and just paid amounts of charges it deemed "reasonable" that sued hospitals for conspiracy to boycott; citing *Ill. Brick Co. v. Illinois*, 431 U.S. 720, 735 (1977), the court said patients were the more efficient enforcer), *aff'd*, 186 Fed. App'x 919 (11th Cir. 2006).

97. *Palmyra Park Hosp., Inc. v. Phoebe Putney Mem'l Hosp.*, 604 F.3d 1291, 1294 (11th Cir. 2010).

98. *Id.*

99. *Id.* at 1296.

100. *Id.* at 1306.

101. *Id.* at 1303–04 (quoting lower court opinion).

102. *Palmyra Park Hosp., Inc.*, 604 F.3d at 1305.

103. *Id.* at 1302–03.

questionable damages and little incentive to sue, and their subscribers likewise may or may not have had damages in the form of increased premiums—and organizing and determining this harm would be difficult and likely prohibitive to filing suit.¹⁰⁴ The most significant effect of the arrangement between Phoebe Putney and the insurers was an incentive change for patients: Patients had the incentive to go to in-network hospital Phoebe Putney and not out-of-network Palmyra because of how insurance companies reimburse for hospital charges.¹⁰⁵ No patient would be willing to pay out of pocket for similar treatment at an out-of-network hospital, so the contracting arrangement took away demand from Palmyra—so much so that the hospital experienced a drop in revenue from twenty-four million dollars to six million dollars.¹⁰⁶ Indeed, the Third Circuit held that “[a]s Phoebe Putney’s chief competitor, Palmyra is undoubtedly well suited to vindicate these harms.”¹⁰⁷

c. Special Considerations in Health Care

In some recent health care antitrust cases, defendants accused of harming competition through arrangements that artificially depress prices have argued that lower prices benefit, as opposed to harm, consumers.¹⁰⁸ This argument fails generally because antitrust injury includes harms that result from conspiracies to lower prices in contravention of fair and open competition.¹⁰⁹ But in health care cases, courts have also specifically pointed out that diminishment of quality and limitation of access are key in the health care analysis, as patient decisions are not made based on price to the same extent that they are in other markets for goods and services.¹¹⁰ For example, in the Third Circuit’s reversal in *West Penn Allegheny Health System, Inc. v. UPCM*, provider West Penn sued competitor provider UPMC and insurer Highmark for various antitrust violations, including those related to UPMC and Highmark’s agreement that Highmark, who also had a business relationship with plaintiff West Penn, was “not to do anything to benefit West Penn financially.”¹¹¹ Pursuant to that agreement, the complaint alleged that West Penn had asked Highmark to renegotiate and raise its rates. It

104. *See id.* at 1305.

105. *See id.* at 1304.

106. *Id.* at 1302–03.

107. *Palmyra Park Hosp., Inc.*, 604 F.3d at 1305 (the court also noting that contrary to the district court’s suggestion, the government was not necessarily the best plaintiff in light of limited resources).

108. *See, e.g.*, *W. Penn Allegheny Health Sys., Inc. v. UPMC*, 627 F.3d 85, 104 (3d Cir. 2010); *N.Y. Medscan LLC v. N.Y. Univ. Sch. of Med.*, 430 F. Supp. 2d 140, 147 (S.D.N.Y. 2006).

109. *E.g.*, *Knevelbaard Dairies v. Kraft Foods, Inc.*, 232 F.3d 979, 988 (9th Cir. 2000) (“[T]he central purpose of the antitrust laws . . . is to preserve competition. It is competition—not the collusive fixing of prices at levels either low or high—that these statutes recognize as vital to the public interest.”).

110. *See, e.g.*, *W. Penn Allegheny Health Sys., Inc.*, 627 F.3d at 104.

111. *Id.* at 103.

further alleged that although Highmark acknowledged that the rates were too low (i.e., below market), Highmark nonetheless refused to raise the rates in light of its agreement with UPMC.¹¹² West Penn asserted that it had suffered antitrust injury as a result of those depressed rates, and Highmark countered that the depressed rates allowed the insurer to offer lower premiums to subscribers and to find antitrust injury in this situation would frustrate the purpose of the antitrust laws, which is to promote consumer welfare.¹¹³ The court rejected Highmark's argument, finding instead that Highmark had not, in fact, passed those savings on to subscribers, and doing so likely would have "diminish[ed] the quality and availability of hospital services."¹¹⁴ Similarly, in a district court case in which the plaintiff alleged that the defendant had engaged in anti-competitive conduct in the market for Positron Emission Tomography and Computed Tomography medical scanning equipment, the court was not swayed by the defendant's argument that consumers, and therefore competition, had not suffered because prices had not gone up.¹¹⁵ Finding that the plaintiffs had adequately pled antitrust injury, the court stated: "Indeed, in the context of the provision of health care services for cancer patients, the quality of care is likely to be at least as important to patients as the price."¹¹⁶ Lastly, a district court in New Mexico recently found antitrust injury by recognizing that an insurer payment of below-market reimbursement rates to a provider indicated that insurer's market power in the relevant market, explaining that a monopsonist (seller) with market power is every bit as capable of causing antitrust injury as is a monopolist (buyer).¹¹⁷ Accordingly, in health care, diminution in quality should be considered in any discussion of antitrust standing.

d. *Twiqbal*

The standing inquiry in antitrust cases has been further complicated by the muddling of standards by lower courts in response to *Twombly* and *Iqbal*.¹¹⁸ Understanding both the development of the antitrust standing rules as well as how courts are applying them in health care cases particularly since *Twiqbal* is essential to filing an effective complaint. Outside of health care, some courts,

112. *Id.* at 100.

113. *Id.* at 104.

114. *W. Penn Allegheny Health Sys., Inc.*, 627 F.3d at 104.

115. *N.Y. Medscan LLC v. N.Y. Univ. Sch. of Med.*, 430 F. Supp. 2d, 140, 147–48 (S.D.N.Y. 2006).

116. *Id.*

117. *N.M. Oncology & Hematology Consultants, Ltd. v. Presbyterian Healthcare Servs.*, 54 F. Supp. 3d 1189, 1205–06 (D.N.M. 2014).

118. See Jacobson & Greer, *supra* note 82, at 288; see also *Somers v. Apple, Inc.*, 729 F.3d 953, 965 (9th Cir. 2013); *Prime Healthcare Servs., Inc. v. Servs. Emps. Int'l Union*, No. 11–cv–2652–GPC–RBB, 2013 WL 3873074, at *12 (S.D. Cal. July 25, 2013), *aff'd*, 642 F. App'x 665 (9th Cir. 2016).

including the Court of Appeals for the Ninth Circuit, have expressly mingled antitrust injury and the plausibility standard for pleading claims by citing *Twombly* and *Iqbal* to support the proposition that “to state a plausible antitrust injury, [the plaintiff] must allege facts that rise beyond mere conceivability or possibility.”¹¹⁹ Likewise, in health care, some lower courts are mingling *Twombly* with antitrust injury.¹²⁰ Be that as it may, the *Twombly* growing pains have not necessarily resulted in a stricter standing requirements for plaintiffs. For example, in 2010, the Court of Appeals for the Third Circuit reversed the district court’s dismissal of a health care provider’s suit against another provider and insurer on the grounds that the district court’s application of *Twombly* overshot the requirements of that case, including as to antitrust standing.¹²¹ That early district court decision, written in response to a renewed motion to dismiss based on the Supreme Court’s rulings in *Twombly* and *Iqbal*, was guided by the defendant’s insistence that the plausibility “requirement includes pleading facts sufficient to satisfy the antitrust injury requirement.”¹²² The court applied a strict version of plausibility to all facets of the complaint. The Third Circuit acknowledged the new standard but clarified that it applied equally to all federal claims and did not impose heightened pleading requirements for antitrust cases.¹²³

4. Class Certification

Although private antitrust litigation immediately conjures thoughts of large class action cases, most cases involving health care services and insurance premiums are individual actions by competitors, unlike the larger consumer cases against pharmaceutical companies. The scarcity of class actions in this arena is likely due to the individualized nature of damages in health care,¹²⁴

119. *Somers*, 729 F.3d at 695 (citing *Ashcroft v. Iqbal*, 556 U.S. 662, 678–79 (2009); *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007)).

120. See, e.g., *Prime Healthcare Servs., Inc.*, 2013 WL 3873074, at *12. In *Prime Healthcare Services, Inc. v. Service Employees International Union*, the district court cited *Twombly* for the proposition that the plaintiff must plead sufficient facts to allege antitrust injury simply by misquoting *Twombly* to read that the plaintiff’s “allegations must ‘raise a reasonable expectation that discovery will reveal evidence of’ an injury to competition,” *id.*, whereas *Twombly* says “raise a reasonable expectation that discovery will reveal evidence of *illegal agreement*,” *Twombly*, 550 U.S. at 556 (emphasis added).

121. *W. Penn Allegheny Health Sys., Inc. v. UPMC*, 627 F.3d 85, 98 (3d Cir. 2010) (“We conclude that it is inappropriate to apply *Twombly*’s plausibility standard with extra bite in antitrust and other complex cases.”).

122. *W. Penn Allegheny Health Sys., Inc. v. UPMC*, No. 09CV0480, 2009 WL 3601600, at *19 (W.D. Pa. Oct. 29, 2009), *rev’d*, 627 F.3d 85 (3d Cir. 2010).

123. *W. Penn Allegheny Health Sys., Inc.*, 627 F.3d at 98 (“We conclude that it is inappropriate to apply *Twombly*’s plausibility standard with extra bite in antitrust and other complex cases.”).

124. See *Palmyra Park Hosp., Inc. v. Phoebe Putney Mem’l Hosp.*, 604 F.3d 1291, 1305 (11th Cir. 2010) (explaining why a patient class might not be the most efficient enforcer).

which may deter plaintiffs from trying to satisfy the FRCP 23(b)(3) requirement that issues common to the class will predominate over issues specific to individual class members in the case.¹²⁵ Nonetheless, a few notable class actions have been filed with some classes certified in this sphere.

Most famous among the class actions in this area may indeed be the most unlikely: *Messner v. Northshore University HealthSystem*, a merger challenge to the consummated merger of two hospitals in the Chicago area.¹²⁶ Challenges to mergers by the government, of course, are common, and indeed this private challenge followed a merger challenge from the FTC. But private plaintiffs rarely challenge mergers because of timing issues (mergers are typically challenged when they are still in the planning stages, a time when plaintiffs often have little information about the deal) and because the typical remedy in a merger challenge is an injunction. Although the class was certified after being remanded to the district court in 2013, it still feels like somewhat of a one-off—plaintiffs have not followed suit en masse to challenge mergers in federal court either as follow-on cases to FTC merger challenges. Still, the *Messner* case contains valuable language for would-be challengers. Given that after a careful examination of the markets for health care services at issue, including that the calculation of damages would be affected by factors including “(1) health service provider contract negotiation, (2) multi-year contract terms, (3) hospital location, reputation, and quality, and (4) prevalent improvements in the technology behind certain services,” the court nonetheless concluded that predominance issues did not preclude class certification.¹²⁷ The court explained, “Individual questions need not be absent. The text of FRCP 23(b)(3) itself contemplates that such individual questions will be present. The rule requires only that those questions not predominate over the common questions affecting the class as a whole.”¹²⁸

Even though *Messner* has not given rise to a wave of follow-on Clayton Act-based merger challenges over the past five years, its language was recently relied upon by a *state* court in certifying a class in a challenge to hospital contracting provisions brought by self-funded payors in California.¹²⁹ The court cited the Seventh Circuit’s suggestion in *Messner* that “even in the ‘market for hospital services [which] seems to be particularly complex,’ certification may be

125. FED. R. CIV. P. 23(b)(3).

126. *Messner v. Northshore Univ. HealthSystem*, 669 F.3d 802, 808 (7th Cir. 2012).

127. Justin Boley, *Seventh Circuit Vacates Northshore Hospital Antitrust Class Certification Denial*, WEXLER WALLACE LLP (Jan. 17, 2012), <https://www.wexlerwallace.com/seventh-circuit-vacates-messner-antitrust-class-certification-denial/> (last visited Nov. 1, 2017).

128. *Messner*, 669 F.3d at 815.

129. Order Granting in Part Motion to Strike, Granting Class Certification, and Setting Case Management Conference at 9, *UFCW & Emp’rs Benefit Tr. v. Sutter Health*, Cal. App. Dep’t Super. Ct (Aug. 14, 2017) (No. CGC 14-538451) (quoting *Messner*, 669 F.3d at 816).

proper.”¹³⁰ That case, *UFCW & Employers Benefit Trust v. Sutter Health*, contains similar allegations to *Sidibe v. Sutter Health*, which is back in district court after the Ninth Circuit reversed the lower court’s dismissal for failure to state a claim but has not yet reached class certification.¹³¹ *Sidibe* will be the first case in federal court to seek certification for a class of patients (insurance subscribers) suing for damages from overcharges related to a hospital’s anti-competitive clauses in insurer contracts and related tying arrangements (as part of a monopolization scheme)—facts similar to those present in several suits brought by competitors against hospitals over the past several years.¹³² Interestingly, another putative class of plaintiffs has filed a case similar to *UFCW* in state court in North Carolina.¹³³ That case, which is still pre-class certification, is distinct in that the plaintiffs chose to file in state court, even though the suit was a follow-on to a DOJ matter.¹³⁴

Also currently pending, and in pre-class certification, are two large tracks (provider plaintiffs and subscriber plaintiffs, respectively) of antitrust class actions against Blue Cross Blue Shield (BCBS) entities in multi-district litigation in the Northern District of Alabama.¹³⁵ The plaintiffs alleged that BCBS plans and their association used their market power, derived from being the dominant insurer in multiple markets, to engage in and profit from the anti-competitive scheme.¹³⁶ In the alleged scheme, the individual BCBS plans and their national association conspired to carve up insurance markets among the insurers across the country in a nationwide market allocation scheme under which BCBS plans were allocated a particular market and then would agree not to compete with other neighboring BCBS plans in at least seventeen states.¹³⁷ The two-tracked litigation presents “a unique case where one class (providers)

130. *Id.*

131. Current Docket, *Sidibe v. Sutter Health*, 51 F. Supp. 3d 870 (N.D. Cal. 2014).

132. *See, e.g.*, *Palmyra Park Hosp., Inc. v. Phoebe Putney Mem’l Hosp.*, 604 F.3d 1291, 1294, 1298 (11th Cir. 2010); *Methodist Health Servs. Corp. v. OSF Healthcare Sys.*, 859 F.3d 408, 409 (7th Cir. 2017); *Marion HealthCare LLC v. S. Ill. Healthcare*, 12–CV–00871–DRH–PMF, 2013 WL 4510168, at *1 (S.D. Ill. Aug. 26, 2013); *Arapahoe Surgery Ctr., LLC v. Cigna Healthcare, Inc.*, 80 F. Supp. 3d 1257, 1262 (D. Colo. 2015).

133. *DiCesare v. Charlotte-Mecklenburg Hosp. Auth.*, No. 16 CVS 16404, 2017 WL 1359599, at *1 (N.C. Super. Ct. Apr. 11, 2017), *cert. denied*, 804 S.E.2d 541 (N.C. 2017) (mem.).

134. *United States v. Charlotte-Mecklenburg Hosp. Auth.*, 248 F. Supp. 3d 720 (W.D.N.C. 2017).

135. *In re Blue Cross Blue Shield Antitrust Litig.*, 2:13–CV–20000–RDP, 2017 WL 2797267 (N.D. Ala. June 28, 2017).

136. Corrected Consolidated Second Amended Provider Complaint, *In re Blue Cross Blue Shield Antitrust Litig.*, 26 F. Supp. 3d 1172 (N.D. Ala. 2014) (No. 2:12–cv–02532–RDP).

137. *Id.* at 131; *see also* Irina Rodriguez, Moderator, Office of the New York Attorney General, *Blue Cross Blue Shield Antitrust Litigation: Update on the Issues*, (May 4, 2016), A.B.A. Antitrust Sec. L. Rep., at Slide 11, https://www.americanbar.org/content/dam/aba/publications/antitrust_law/20160504_at160504_materials.authcheckdam.pdf.

asserts an antitrust injury (low reimbursement rates) which tends to benefit the other class (subscribers who may have paid lower premiums as a result),” such that “[e]ach class will be putting forth evidence that the other class wasn’t injured.”¹³⁸ It is unclear how this potential conflict and other factors will play in the class certification motions, which will be filed soon.

B. Substantive Antitrust Challenges

1. Market Definition

As venerated antitrust scholar Professor Hovenkamp observed, “Markets do not define themselves.”¹³⁹ Litigants define markets, and doing so accurately is an exercise not only in economics but also in advocacy. As former FTC Chairman Robert Pitofsky stated in 1990, “[A]ntitrust practitioners have long known that the most important single issue in most enforcement actions—because so much depends on it—is market definition.”¹⁴⁰ Indeed, market definition is not only important to public antitrust, but it is also an essential element and one of the main stumbling blocks in private cases. To plead most antitrust claims, the plaintiff must define the relevant market in the complaint along with the reasoning behind the proposed definition.¹⁴¹ Defining relevant markets is a highly fact-specific inquiry,¹⁴² which makes doing so in a private complaint, before the benefit of discovery, particularly challenging. And defendants may, and often do, move to dismiss a case for failure to state a claim based on the proposed market definition included in the complaint.¹⁴³ Indeed, market definition is central to most antitrust analyses because “[w]ithout a definition of [the relevant] market there is no way to measure [a defendant’s] ability to lessen or destroy competition.”¹⁴⁴

Defining a relevant market is the first step towards convincing the fact finder that a defendant possesses the legally essential *market power* over a product or

138. Rodriguez, *supra* note 137, at Slide 13.

139. HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE 111 (5th ed. 2016).

140. Robert Pitofsky, *New Definitions of Relevant Market and the Assault on Antitrust*, 90 COLUM. L. REV. 1805, 1807 (1990).

141. HOVENKAMP, *supra* note 139, at 111 n.19.

142. EDWIN S. ROCKEFELLER, THE ANTITRUST RELIGION 41 (2007).

143. See, e.g., Sidibe v. Sutter Health, 51 F. Supp. 3d 870, 872 (N.D. Cal. 2014), *rev'd*, 667 F. App’x 641 (9th Cir. 2016); Omni Healthcare, Inc. v. Health First, Inc., No. 6:13-cv-1509-Orl-37DAB, 2015 WL 275806, at *1 (M.D. Fla. Jan. 22, 2015); Steward Health Care Sys., LLC v. Blue Cross & Blue Shield of R.I., 997 F. Supp. 2d 142, 149 (D.R.I. 2014); Marion HealthCare, LLC v. S. Ill. Healthcare & Health Servs. Corp., No. 12-cv-871-SMY-PMF, 2015 WL 3466585, at *1 (S.D. Ill. May 29, 2015).

144. Total Renal Care, Inc. v. W. Nephrology & Metabolic Bone Disease, P.C., No. 08-cv-00513-CMA-KMT, 2009 WL 2596493, at *6 (quoting Walker Process Equip., Inc. v. Food Mach. & Chem. Corp., 382 U.S. 172, 177 (1965)).

a geographic area. This exercise is required to prove claims under the rule of reason, which is the presumptive judicial rubric for most antitrust claims.¹⁴⁵ Once a market is defined, the plaintiff demonstrates the defendant's market share therein—a high share signaling likely market power. Market power is defined as “the power to raise prices above competitive levels without losing so many sales that the price increase is unprofitable.”¹⁴⁶ Firms that acquire market power often engage in anti-competitive conduct beyond just raising prices, including, e.g., demanding exclusivity provisions in contracts, using market power in one market to demand better pricing and terms in another market, and/or tying the sale of other, unwanted products to the sale of a product over which they have market power.¹⁴⁷ Plaintiffs may sue based on each of these types of conduct, and market power is a prerequisite for each.¹⁴⁸

Determining the “relevant market” in an antitrust case is a two-part calculation that “is a collection of products and geographic locations, delineated as part of an inquiry aimed at making inferences about market power and anticompetitive effect.”¹⁴⁹ The terms “relevant market” and “antitrust market” are used “to distinguish these markets from what business executives and consultants might define for other purposes.”¹⁵⁰ The determination of relevant market is two-part in that it requires one to define both (1) a product market and (2) a geographic market,¹⁵¹ which are distinct, yet intertwined. The product market is bounded by “the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it.”¹⁵² Once determined, the product market serves to define the geographic market, which “extends to the area of effective competition where buyers can turn for alternative sources of supply” of the product at issue.¹⁵³ Or as one court explained, “The relevant product market identifies the products or services that compete with each other, and the relevant geographic market identifies the area

145. Hovenkamp, *supra* note 48, at 2.

146. HOVENKAMP, *supra* note 139, at 106.

147. See Richard D. Cudahy & Alan Devlin, *Anticompetitive Effect*, 95 MINN. L. REV. 59, 72 (2010).

148. See HOVENKAMP, *supra* note 139, at 106–07. Moreover, market power is an essential element of many antitrust claims, and, to complicate matters, the *degree* of market power required to prove those claims varies. *Id.* at 107. For example, monopolization requires a high degree of market power, attempted monopolization requires less market power, and a pre-merger challenge requires showing a “dangerous probability of acquiring market power” in the future. *Id.*

149. Jonathan B. Baker, *Market Definition: An Analytical Overview*, 74 ANTITRUST L.J. 129, 130 (2007).

150. *Id.*

151. See *id.*

152. *Sidibe v. Sutter Health*, 51 F. Supp. 3d 870, 883 (N.D. Cal. 2014) (quoting *Brown Shoe Co., Inc. v. United States*, 370 U.S. 294, 325 (1962)), *rev'd*, 667 F. App'x 641 (9th Cir. 2016).

153. *Id.* (quoting *Tanaka v. Univ. of S. Cal.*, 252 F.3d 1059, 1063 (9th Cir. 2001)).

where the competition in the relevant product market takes place.”¹⁵⁴ Or as an economist might explain, the inquiry looks at consumer substitution patterns to determine the metes and bounds of both product and geographic markets.

The FTC and DOJ’s jointly issued *Horizontal Merger Guidelines* are the source for one of the main tests used in relevant market definition. The test, first included in the 1982 version of the Guidelines, aids in product as well as geographic market definition, where it continues to play a role in the new workshopped models discussed herein. Thus, it is explained here prior to the other aspects of the development of market definition models. The test aims to determine consumer substitution patterns, which are the basis for market definition. Essentially the test asks whether a monopolist in a given market could raise its prices above the competitive level without losing customers.¹⁵⁵ In economic terms, the test determines “the smallest grouping of sales for which the elasticity of demand and supply are sufficiently low that a ‘hypothetical monopolist’ with 100% of that grouping could profitably reduce output and increase price substantially above marginal cost.”¹⁵⁶ Put more simply, it checks whether consumers will substitute for another product in response to a price hike of a certain size. The test uses the “small but significant non transitory increase in price” test (“SSNIP”) as its key metric, which is imposed, hypothetically, to arrive at the smallest relevant market.¹⁵⁷ The size of the price increase used for the test is small; it is not so small as to not matter at all to consumers but not so large that it causes buyers to leave or for other sellers to enter the market.¹⁵⁸ Once the smallest grouping is determined, the entity’s market share in that market is considered to determine whether it has market power.¹⁵⁹ In sum, the process aims to “find the smallest group of products or firms for which there are no close substitutes, thus allowing such a hypothetical monopolist to exert market power.”¹⁶⁰

a. Market Definition in Health Care

Defining relevant markets is crucial to antitrust analysis regardless of industry; however, the process presents unique challenges in health care due to the role of health insurers, the non-price reasons for consumer behavior, and the differentiation in health care services. Whereas most industries present obvious consumers, in light of the various and overlapping players in health care markets,

154. *Id.* at 883.

155. HOVENKAMP, *supra* note 139, at 112.

156. *Id.*

157. *Id.*

158. *Id.*

159. *Id.* at 111–12.

160. Martin Gaynor et al., *A Structural Approach to Market Definition with an Application to the Hospital Industry* 6 (Nat’l Bureau of Econ. Research, Working Paper No. 16656, 2011), <http://www.nber.org/papers/w16656>.

who the buyers and sellers are is much less clear.¹⁶¹ The role of the payor, as well as the distinctions between private and public payors, has become crucial to a proper market definition. In addition, a patient's decision to purchase a particular health care service is influenced by non-price factors, including the recommendations of her physician, the network of her health plan or managed care organization, and the plans offered by her employer.¹⁶² On top of that, a patient is typically more willing to travel for a non-emergency or elective service, like a knee replacement, than for an acute one, like an appendectomy, or may have no choice but to travel for a specialty service that is only available in a few locations, like an organ transplant.

b. Lessons from Public Enforcement

Market definition, unlike the other challenges discussed in this article, is an area where the lessons from public enforcement, especially hospital merger cases, are instructive. As one legal expert presciently put it two decades ago: "The antitrust treatment of horizontal mergers by the Justice Department and the Federal Trade Commission is one of the most well developed and closely scrutinized areas of antitrust law."¹⁶³ However, at the time of this statement about merger analysis, the FTC may have been experts in most industries but was losing hospital merger challenges. After losing a series of provider merger challenges in the mid- and late-1990s, often involving highly concentrated markets, the FTC undertook to study whether those mergers subsequently resulted in higher prices, and whether the FTC's market definition methodology used to challenge the transactions was to blame.¹⁶⁴ The FTC's study, aided by top academic economists who wrote several related papers on the issue, concluded that those mergers resulted in higher health care prices and the market definition analyses relied on by the Commission, and often, by the courts, was faulty.¹⁶⁵ Thereafter, the FTC worked with economists to revise its market

161. ABA SECTION OF ANTITRUST LAW, MARKET DEFINITION IN ANTITRUST: THEORY AND CASE STUDIES 277 (2012).

162. See *id.* at 277-78.

163. Carl Shapiro, *Mergers with Differentiated Products*, ANTITRUST, Spring 1996, at 23.

164. Brill, *supra* note 15, at 1 n.2 (citing the following FTC losses: Fed. Trade Comm'n v. Hosp. Bd. of Dirs. of Lee Cty., 38 F.3d 1184, 1186 (11th Cir. 1994); Fed. Trade Comm'n v. Freeman Hosp., 69 F.3d 260, 273 (8th Cir. 1995); Fed. Trade Comm'n v. Butterworth Health Corp., 946 F. Supp. 1285, 1303 (W.D. Mich. 1996), *aff'd*, 121 F.3d 708 (6th Cir. 1997); United States v. Mercy Health Servs., 902 F. Supp. 968, 989 (N.D. Iowa 1995), *vacated as moot*, 107 F.3d 632 (8th Cir. 1997); United States v. Long Island Jewish Med. Ctr., 983 F. Supp. 121, 149 (E.D.N.Y. 1997); Fed. Trade Comm'n v. Tenet Health Care Corp., 186 F.3d 1045, 1047 (8th Cir. 1999); California v. Sutter Health Sys., 84 F. Supp. 2d 1057, 1085 (N.D. Cal. 2000), *aff'd*, 217 F.3d 846 (9th Cir. 2000), *and amended by* 130 F. Supp. 2d 1137 (N.D. Cal. 2001)).

165. Brill, *supra* note 15, at 2, 2 n.5, 2-3 n.6 (citing the following papers: Steven Tenn, *The Price Effects of Hospital Mergers: A Case Study of the Sutter-Summit Transaction* 22 (Fed. Trade Comm'n Bureau of Econ., Working Paper No. 293, 2009), <http://www.ftc.gov/be/workpapers/wp>

definition analyses for provider mergers and developed new models that have been the basis of the market definitions used in a string of victories by the FTC.¹⁶⁶

The key feature of the new ways to define health care markets is that they consider the roles of the various players in health care markets. Importantly, they take into account the key distinction between health care and other types of markets: the role of the health insurer. As explained by economist Gregory Vistnes in a seminal article in 2000, “Hospital competition is modeled as a two-stage game. In the first stage, hospitals compete to be included in a plan’s hospital network. In the second stage, hospitals compete for a plan’s individual enrollees, with that competition affected by whether a hospital is in the plan’s network.”¹⁶⁷ In health care, from the consumer perspective, “patients commit to a network of medical providers at the time they purchase their health insurance,

293.pdf; Patrick S. Romano & David J. Balan, *A Retrospective Analysis of Clinical Quality Effects of the Acquisition of Highland Park Hospital by Evanston Northwestern Healthcare*, 18 INT’L J. ECON. BUS. 45, 61 (2011); Deborah Haas-Wilson & Christopher Garmon, *Hospital Mergers and Competitive Effects: Two Retrospective Analyses*, 18 INT’L J. ECON. BUS. 17, 30 (2011); Aileen Thompson, *The Effect of Hospital Mergers on Inpatient Prices: A Case Study of the New Hanover-Cape Fear Transaction*, 18 INT’L J. ECON. BUS. 91, 99 (2011); Orley Ashenfelter et al., *Retrospective Analysis of Hospital Mergers*, 18 INT’L J. ECON. BUS. 5, 14 (2011); Cory S. Capps et al., *Antitrust Policy and Hospital Mergers: Recommendations for a New Approach*, 47 ANTITRUST BULL. 677, 713 (2002); Cory S. Capps et al., *The Silent Majority Fallacy of the Elzinga-Hogarty Criteria: A Critique and New Approach to Analyzing Hospital Mergers* 27–28 (Northwestern Univ. Ctr. for the Study of Indus. Org., Working Paper No. 0017, 2001); Cory S. Capps, *From Rockford to Joplin and Back Again: The Impact of Economics on Hospital Merger Enforcement*, 59 ANTITRUST BULL. 443, 476 (2014); Cory S. Capps, *Economic Analysis of Hospital Mergers in the 21st Century: A New Economic Toolkit for Assessing Hospital Mergers at the American Bar Association Antitrust Law Section Conference on Antitrust in Healthcare* (May 4, 2012)).

166. Brill, *supra* note 15, at 3, 3–4 n.9 (citing the following FTC victories: In the Matter of Inova Health Sys. Found. & Prince William Health Sys., Inc., No. 9326, 2008 WL 2556051, at *1 (Fed. Trade Comm’n June 17, 2008) (dismissing FTC complaint after the parties abandoned the merger); In the Matter of Reading Health Sys. & Surgical Inst. of Reading, No. 9353, 2012 WL 6188557, at *1 (Fed. Trade Comm’n Dec. 7, 2012) (dismissing FTC complaint after the parties abandoned the merger); Fed. Trade Comm’n v. OSF Healthcare Sys., 852 F. Supp. 2d 1069, 1071, 1095 (N.D. Ill. 2012) (granting FTC preliminary injunction); Fed. Trade Comm’n v. Phoebe Putney Health Sys., Inc., 133 U.S. 1003, 1016 (2013); Fed. Trade Comm’n v. Phoebe Putney Health Sys., Inc., No. 1:11-CV-00058-WLS, at 1 (M.D. Ga. June 5, 2013), <http://www.ftc.gov/sites/default/files/documents/cases/2013/06/130606phoebestip.pdf>; *Statement of FTC Competition Director Richard Feinstein on Today’s Announcement by Capella Healthcare that It Will Abandon Its Plan to Acquire Mercy Hot Springs*, FED. TRADE COMM’N (June 27, 2013), <https://www.ftc.gov/news-events/press-releases/2013/06/statement-ftc-competition-director-richard-feinstein-todays> (last visited Nov. 12, 2017)).

167. Gregory Vistnes, *Hospitals, Mergers, and Two-Stage Competition*, 67 ANTITRUST L.J. 671, 672 (2000).

but before they know their specific medical needs.”¹⁶⁸ This shift in thinking, which led analysts to focus on insurer-provider negotiations and consumer preferences as they related to networks, was instrumental in developing more accurate ways to define health care markets. Before that, the two main methods of defining hospital markets in merger enforcement challenges, Elzinga-Hogarty and Critical Loss Analysis, had been overestimating the size of geographic markets, causing courts to find lower market shares and lower risks of resulting market power than they should have.¹⁶⁹ Dissatisfied with the results of the older analyses, economists developed new market definition models. Some economists distinguish these models as “structural” in comparison to the previously used “quantitative” models,¹⁷⁰ which essentially means that they take into account the role of the health insurer in determining health care prices.¹⁷¹

As another economist explains, health insurers, which typically charge the patient only a small portion of the provider’s price, cause patients to be unresponsive to the true prices of the services they consume, and therefore any accurate model must take them into account.¹⁷² But that does not mean that competition does not play a role in determining health care markets.¹⁷³ However, instead of doing so exclusively through consumer choice, competition in health care markets “does this through the selective contracting practices of insurance plans, which construct networks that attempt to optimize the tradeoff between comprehensiveness and costliness.”¹⁷⁴ The substitution analysis then focuses on the networks, i.e., “[w]hether an insurer includes attractive providers in the network, and at what price, depends upon the availability of substitutable providers.”¹⁷⁵ The newer analyses then also consider other stages of

168. Cory Capps et al., *Competition and Market Power in Option Demand Markets*, 34 RAND J. ECON. 737, 737–74 (2003).

169. Martin S. Gaynor et al., *A Structural Approach to Market Definition with an Application to the Hospital Industry*, 61 J. INDUS. ECON. 243, 248 (2013).

170. *Id.* at 245, 249, 256.

171. The new models included an analysis called “Willingness-to-Pay,” which is uniquely tailored to the health care industry based on a bargaining model of the negotiation between insurance companies and hospitals, a “Bertrand model,” and a market power measure for hospitals called the “Logit Competition Index.” See Christopher Garmon, *The Accuracy of Hospital Merger Screening Methods* 6 (Fed. Trade Comm’n Bureau of Econ., Working Paper No. 326, 2015) (citing Robert Town & Gregory Vistnes, *Hospital Competition in HMO Networks*, 20 J. HEALTH ECON., 733, 733–53 (2001); Cory Capps et al., *Competition and Market Power in Option Demand Markets*, 34 RAND J. ECON. 737, 737–63 (2003)); see also David Dranove & Andrew Sfekas, *The Revolution in Health Care Antitrust: New Methods and Provocative Implications*, 87 MILBANK Q. 607, 614 (2009).

172. Brett W. Wendling & Nathan E. Wilson, *The Importance of Substitution in Assessing Health Care Provider Mergers*, 59 ANTITRUST BULL. 515, 516 (2014).

173. See *id.* at 516–17.

174. *Id.* at 517.

175. *Id.*

competition, including hospitals' subsequent competition for patients or insurers' competition for inclusion in plans offered to employees.¹⁷⁶

Plaintiffs and, correspondingly, courts have been borrowing from these analyses in defining markets in recent private cases—e.g., in the multi-district antitrust litigation against BCBS. Paraphrasing Vistnes' article from 2000, the court recently explained, "Healthcare providers participate in what is known as two-stage competition; first they compete for inclusion in the provider networks of insurers' plans, and then they compete for patients within a plan."¹⁷⁷ The related-but-distinct concept of a "two-sided market" recently received considerable attention following the Second Circuit's ruling in *United States v. American Express Co.* There, the court reversed the district court's ruling in favor of DOJ that American Express's "non-discrimination provisions" in its contracts with merchants, which prevented the merchants from steering consumers to use credit cards with lower fees (to be paid by the merchants), were anti-competitive.¹⁷⁸ In so ruling, the Second Circuit made clear that market definition in such markets should not be limited to one side of the market; instead the analysis must look at the anti-competitive effects on the consumer and not just the merchant. The admonition that antitrust protects competition (and consumers) as opposed to competitors is not new, but competitor plaintiffs must make certain to clarify that their interests align with those of consumers by showing that the anti-competitive effects extend to consumers in the form of higher prices or diminished quality. For example, in *Methodist*, where the plaintiff hospital argued that exclusive dealing by its competitor with insurers destroyed competition in the relevant tri-county health care services market, both the district court and Seventh Circuit were unconvinced that harm extended beyond the hospital-insurer stage of the market to the hospital-patient stage.¹⁷⁹ Accordingly, the court concluded that the only "victim" was the plaintiff who had the opportunity to improve and compete against competitor hospitals for contracts with insurers.¹⁸⁰

Specifically as to product markets, the FTC has long been using "cluster markets" in which groups of health services are grouped together—a tactic that

176. Petitioner's Response to Defendant's Motion for Judgment on the Pleadings at 9–10, *Methodist Health Servs. Corp. v. OSF Healthcare Corp.* 2014 WL 1612838 (No. 13-cv-1054) (citing Gregory Vistnes, *Hospitals, Mergers, and Two-Stage Competition*, 67 ANTITRUST L.J. 671, 672 (2000)).

177. *In re Blue Cross Blue Shield Antitrust Litig.*, No. 2:13-CV-20000-RDP, 2017 WL 2797267, at *5 (N.D. Ala. June 28, 2017). This concept of a "two-sided market" recently received considerable attention following the Second Circuit's reversal in *United States v. American Express Co.* *United States v. American Express Co.*, 838 F.3d 179, 185–86 (2d Cir. 2016) (noting that credit card companies compete for merchants as well as for consumers), *cert. granted*, 138 S. Ct. 355 (2017) (mem.).

178. *American Express Co.*, 838 F.3d at 184–86, 206.

179. *Methodist Health Servs. Corp.*, 859 F.3d at 410–11.

180. *Id.* at 411.

has become popular in private cases.¹⁸¹ Of course, due to dissimilarities among most health care services, the most accurate product markets might be defined as singular services.¹⁸² No one would argue that bypass surgery and hip replacement are the same offering. Nonetheless, the procedures both have features that make them comparable for antitrust analysis, e.g., they are inpatient procedures typically covered by both Medicare and commercial insurance plans. Moreover, cases are often about how a defendant's conduct and market position affects the prices of multiple types of health care services, and defining a distinct market for each would be cumbersome and confusing. And unlike in most industries where "cluster markets are most often used as a convenience and not because they are analytically rigorous,"¹⁸³ the existence of networks means that goods are already clustered. Cluster markets make considerable sense in an industry characterized by network effects, i.e., as the number and type of health care providers included in the network increases, the more valuable the network is to consumers.¹⁸⁴

c. Market Definition at the Pleading Stage

Private enforcement differs from public enforcement in the degree to which defining markets at the pleading stage matters. As explained above, when the FTC files a challenge to a hospital merger, it typically does so with the benefit of pre-merger discovery and after having had a chance to do a full economic analysis of the merger's potential effects on competition. In contrast, in a private case, the plaintiff usually has insufficient information about anti-competitive effects until the post-pleading discovery process begins. Accordingly, surviving a motion to dismiss is crucial. And because pleading standards have become more difficult to satisfy, this is no simple task.

d. The *Twiqbal* Effect on Market Definition

Defining relevant markets is a highly fact-specific inquiry, which makes doing so in a complaint, before the benefit of discovery, particularly challenging. And because market definition is a factual as opposed to a legal issue, it cannot be resolved at the pleading stage.¹⁸⁵ Yet, in light of *Twombly* and *Iqbal*'s higher pleading standards, plaintiffs treat market definition as a discovery-phase fact issue at their peril. *Twiqbal*'s plausibility standard has crept (albeit

181. See *Fed. Trade Comm'n v. Advocate Health Care Network*, 841 F.3d 460, 467–68 (7th Cir. 2016) (collecting hospital merger cases); *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-CV-1509-ORL, 2015 WL 275806, at *11 (M.D. Fla. Jan. 22, 2015); *In re Blue Cross Blue Shield Antitrust Litig.*, 2017 WL 2797267, at *5.

182. See ABA SECTION OF ANTITRUST LAW, *supra* note 161, at 280–81.

183. *Id.* at 280.

184. See SHEARMAN & STERLING LLP, 2017 ANNUAL REPORT: 23 MAJOR TRENDS IN ANTITRUST LAW 84 (2017) (discussing the network effects associated with the credit card industry).

185. See *Eastman Kodak Co. v. Image Tech. Servs. Inc.*, 504 U.S. 451, 482 (1992).

inconsistently) into courts' evaluations of relevant market definitions at the early stages of cases over the past several years. Even before the *Twiqbal* holdings, some courts already used a plausibility standard to evaluate market definition at the pleading stage.¹⁸⁶ Back then, many courts used "plausible" and "viable" interchangeably to describe the standard for relevant market definition at pleading.¹⁸⁷ Now with *Twiqbal* in effect, some commentators have noted the more express application of the "plausibility" standard to the non-conspiracy elements of antitrust claims, including market definition.¹⁸⁸

In reality post-*Twiqbal* courts have required varying degrees of plausibility in regard to market definition in health care cases. Some courts have demanded *Twiqbal*-style allegations of plausible relevant markets,¹⁸⁹ while others apply more forgiving standards.¹⁹⁰ There are three main categories of such cases: (1) cases in which courts expressly require that plaintiffs plead "plausibility" under *Twiqbal*,¹⁹¹ (2) cases that more generally cite to the *Twiqbal* standard as applying to all of the claims, but not expressly to market definition (and even in some cases citing to pre-*Twiqbal* cases in the market definition analysis),¹⁹² and (3) cases in which the plaintiff seems to luck out by drawing a judge whose standard for market definition appears closer to notice pleading than either pre-*Twiqbal* analyses that call for "plausibility" or "viability," or post-*Twiqbal*

186. *E.g.*, *Ferguson Med. Grp., L.P. v. Mo. Delta Med. Ctr.*, No. 1:06 CV 8 CDP, 2006 WL 2225454, at *3, *5 (E.D. Mo. Aug. 2, 2006).

187. *E. & G. Gabriel v. Gabriel Bros.*, No. 93 CIV. 0894 (PKL), 1994 WL 369147, at *2–3 (S.D.N.Y. July 13, 1994). *Theatre Party Assocs., Inc. v. Shubert Org., Inc.*, 695 F. Supp. 150, 154, 156 (S.D.N.Y. 1988) (granting defendant's motion to dismiss where plaintiff failed to allege "viable" or "plausible" relevant market).

188. Stephen P. Safranski, "*Plausibility and the Non-Conspiracy Elements of Antitrust Claims*," ROBINS KAPLAN, LLP (June 5, 2014), <http://www.robinskaplan.com/resources/articles/plausibility-and-the-non-conspiracy-elements-of-antitrust-claims> (last visited Nov. 30, 2017).

189. *E.g.*, *Sidibe v. Sutter Health*, 51 F. Supp. 3d 870, 883 (N.D. Cal. 2014), *rev'd*, 667 F. App'x 641 (9th Cir. 2016); *see also* Safranski, *supra* note 188 ("Sidibe embodies the level of precision that federal courts may now demand in antitrust litigation under the *Twombly* plausibility standard when it comes to pleading the existence of a relevant market.").

190. *See, e.g.*, *Steward Health Care Sys., LLC v. Blue Cross & Blue Shield of R.I.*, 997 F. Supp. 2d 142, 163 (D.R.I. 2014) ("Geographic markets need not be alleged or proven with 'scientific precision,' nor be defined 'by metes and bounds as a surveyor would lay off a plot of ground.' The complaint need only present sufficient information to plausibly suggest the contours of the relevant geographic market.") (quoting *United States v. Blue Cross Blue Shield of Mich.*, 809 F. Supp. 2d 665, 673 (E.D. Mich. 2011)).

191. *E.g.*, *Sidibe*, 51 F. Supp. 3d at 882; *Little Rock Cardiology Clinic PA v. Baptist Health*, 591 F.3d 591, 596 (8th Cir. 2009); *N.M. Oncology & Hematology Consultants, Ltd. v. Presbyterian Healthcare Servs.*, 54 F. Supp. 3d 1189, 1199 (D.N.M. 2014).

192. *E.g.*, *Steward Health Care Sys., LLC*, 997 F. Supp. 2d at 151, 160; *Powderly v. Blue Cross & Blue Shield of N.C.*, No. 3:08-CV-00109-W, 2008 WL 4129767, at *1–2 (W.D.N.C. Sept. 4, 2008).

“plausibility” tests.¹⁹³ Under the circumstances, plaintiffs should assume a court will use greater scrutiny to examine pleading stage relevant market definitions. In one notable recent district court case, *Sidibe*, the court’s dismissal of the plaintiffs’ claims on a motion to dismiss the third amended complaint was based entirely their failure to allege *plausible* relevant geographic markets under *Twiqbal*.¹⁹⁴ That case was reversed and remanded to district court when the Ninth Circuit Court of Appeals decided, based on a 2008 case contemporaneous to *Twombly* but pre-*Iqbal* Ninth Circuit case, that fewer facts were required of plaintiffs in market definition at the pleading stage.¹⁹⁵ However, the Ninth Circuit’s opinion was unpublished and may be cold comfort for plaintiffs who opt to avoid *Twiqbal* plausibility when pleading relevant markets.

e. Recent Trends in Product Market Definition

Product market can be a subject of greater contention in private enforcement cases in health care than in public hospital merger challenges because the FTC and merging hospitals so often agree on the relevant product market (and conflict on geographic market).¹⁹⁶ Yet, like in public enforcement cases, product market is less contentious than the more often dispositive issue of geographic markets, and fewer cases tend to be dismissed on this issue early on in litigation.¹⁹⁷ Like the FTC and DOJ, most plaintiffs also distinguish health services paid for with government insurance from those paid for with commercial insurance in defining product markets,¹⁹⁸ but this issue has come up in some recent cases. For example, in *Marion HealthCare, LLC v. Southern Illinois HealthCare*, the

193. *E.g.*, *Am. Med. Ass’n v. United Healthcare Corp.*, 588 F. Supp. 2d 432, 447 (S.D.N.Y. 2008); *Deborah Heart & Lung Ctr. v. Penn Presbyterian Med. Ctr.*, No. CIV. 11-1290 RMB KMW, 2011 WL 6935276, at *4 (D.N.J. Dec. 30, 2011); *Omni Healthcare, Inc. v. Health First, Inc.*, No. 6:13-cv-1509-Orl-37DAB, 2015 WL 275806, at *11-12 (M.D. Fla. Jan. 22, 2015).

194. *Sidibe*, 51 F. Supp. 3d at 883, 886-87 (noting that the district court explained it was “not requiring heightened pleading”).

195. *Sidibe v. Sutter Health*, 667 F. App’x 641, 643 (9th Cir. 2016).

196. *Gaynor et al.*, *supra* note 160, at 3, 3 n.6, but see *Promedica Health System, Inc. v. Fed. Trade Comm’n*, 749 F.3d 559, 565 (6th Cir. 2014), a case in which the product market was a subject of contention.

197. Recent cases where defendants have challenged a product market in health care as too narrow include a case where the court found the product market should extend to all medical services provided to inmates in all locked facilities, not just prisons, *Colonial Med. Grp., Inc. v. Catholic Health Care W.*, 444 Fed. App’x 937, 938 (9th Cir. 2011), and a case in which the district court conflated the product market with the geographic market, demanding that the “product market” should extend to similar products in other geographic areas, *Rocky Mountain Med. Mgmt., LLC v. LHP Hosp. Grp., Inc.*, No. 4:13-cv-00064-EJL, 2013 WL 5469890, at *14 (D. Idaho Sept. 30, 2013).

198. *See, e.g.*, *Methodist Health Servs. Corp. v. OSF Healthcare Sys.*, No. 1:13-cv-01054-SLD-JEH, 2015 WL 1399229, at *2 (C.D. Ill. Mar. 25, 2015); *In re Blue Cross Blue Shield Antitrust Litig.*, No. 2:13-CV-20000-RDP2017, 2017 WL 2797267, at *5 (N.D. Ala. June 28, 2017).

plaintiff's product market definition included only hospital services paid for by commercial insurers but not government payors.¹⁹⁹ The district court granted the defendant's motion to dismiss, finding that a product market that included only hospital services paid for by commercial insurance, but not those same services when paid for by Medicare or Medicaid, was implausibly narrow.²⁰⁰ In doing so, the court relied on the Eighth Circuit's 2009 decision in *Little Rock Cardiology Clinic PA v. Baptist Health*, a case that declined to distinguish health care services markets based on payors, reasoning that, from the doctor's perspective, the consumer's method of payment was irrelevant and therefore could not be the basis of a market definition.²⁰¹ Those cases appear to be the exception, however, and other courts in contemporaneous cases have limited product markets to health care services purchased by commercial payors despite defendants' arguments for all payors' inclusion.²⁰²

Plaintiffs have also been successful in using the cluster market approach in health care. For example, the court accepted this strategy in the recently settled case of *Omni Healthcare* in which physician groups sued a health care corporation comprised of a hospital and an insurance plan, alleging the health care giant used its market power, gained in part from anti-competitive mergers, to obtain exclusive referral arrangements aimed at eliminating competitors.²⁰³ In declining to exclude the plaintiff's expert economist's report, which clustered health services into product markets, the court explained that "[t]he Supreme Court has also recognized that there is 'no barrier to combining in a single market a number of different products or services where that combination reflects commercial realities.'"²⁰⁴ Even more recently, a court in the antitrust

199. *Marion HealthCare, LLC v. S. Ill. HealthCare*, No. 12–CV–00871–DRH–PMF, 2013 WL 4510168, at *2 (S.D. Ill. Aug. 26, 2013). The court dismissed the complaint without prejudice, *id.* at *11–12, and after refiled the case with a product market definition broadened to include all payors, several counts of the complaint survived a subsequent motion to dismiss, *Marion HealthCare, LLC v. S. Ill. Healthcare & Health Servs. Corp.*, No. 12–cv–871–SMY–PMF, 2015 WL 3466585, at *8 (S.D. Ill. May 29, 2015).

200. *Marion HealthCare, LLC*, 2013 WL 4510168, at *10–11.

201. *Little Rock Cardiology Clinic PA v. Baptist Health*, 591 F.3d 591, 597–98 (8th Cir. 2009).

202. *See, e.g.*, *Methodist Health Services Corporation's Opposition in Response in Opposition* at 9–10, *Methodist Health Servs. Corp. v. OSF Healthcare Sys.*, No. 13-cv-1054 (C.D. Ill. Apr. 11, 2014) (relying on Economist Gregory Vistnes's work and *In re ProMedica Health System, Inc.* to argue that exclusion of government payors resulted in the most accurate product market definition because the prices government payors pay for medical services do not significantly constrain those paid by commercial insurers, who negotiate their rates with providers separately and individually); *In re Blue Cross Blue Shield Antitrust Litig.*, 2017 WL 2797267, at *9; *Steward Health Care Sys., LLC v. Blue Cross Blue Shield of R.I.*, 997 F. Supp. 2d 142, 161 (D.R.I. 2014) (finding that a product market with only commercial payors was plausible because of lack of interchangeability with Medicare- and Medicaid-purchased health care services).

203. *Omni Healthcare Inc. v. Health First, Inc.*, No. 613CV1509ORL37DAB, 2016 WL 4272164, at *2, *22 (M.D. Fla. Aug. 13, 2016).

204. *Id.* at *8 (quoting *United States v. Grinnell Corp.*, 384 U.S. 563, 572 (1966)).

litigation against BCBS noted that a “cluster market” is “a concept widely accepted in healthcare antitrust cases and scholarly economic analyses.”²⁰⁵ Because of the existence of networks in health care, this clustering finds a natural fit in health care product markets. In this sense, cluster markets are more a market reality than a litigant’s convenience and are likely to continue to gain traction as the plaintiff’s preferred methodology for product market definition.

f. Recent Trends in Geographic Market Definition

Recent antitrust health care cases also highlight the aspects of geographic market definition that courts appear to be most focused on at the pleading stage. Of course, courts demand good faith and are inclined to dismiss a complaint when they determine that a plaintiff’s proposed geographic market definition is more a gerrymandered, results-driven presentation of the facts rather than an accurate picture of the market at issue.²⁰⁶ Beyond that, plaintiffs must frame their geographic market definition, just as with product market definition,²⁰⁷ in terms of substitutes available to the buyer. This distinction is not new, and the notion of available substitutes was articulated in the seminal (but non-health care) case of *Brown Shoe* in 1962.²⁰⁸ Once the product market is determined, it serves to define the geographic market, which “extends to the area of effective competition where buyers can turn for alternative sources of supply” of the product at issue.²⁰⁹

In a number of private antitrust cases over the past several years, court decisions have favored plaintiffs’ geographic market definitions that described where customers *could* receive health care services over those that described where patients *actually* received services. In a 2002 monopolization and tying case before the Fifth Circuit, the court explained that the plaintiff’s expert had defined the defendant hospital’s service area as coextensive with its geographic market instead of “where people could practicably go for inpatient services.”²¹⁰ This defect was fatal, as the court explained, “‘trade area is not necessarily the relevant geographic market for purposes of antitrust analysis’ because

205. *In re Blue Cross Blue Shield Antitrust Litig.*, 2017 WL 2797267, at *5.

206. *See, e.g.*, *Ferguson Med. Grp., L.P. v. Mo. Delta Med. Ctr.*, No. 1:06CV8 CDP, 2006 WL 2225454, at *3 (E.D. Mo. Aug. 2, 2006); *Little Rock Cardiology Clinic PA*, 591 F.3d at 599.

207. U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES 8 (2010), <https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf>. Recall that product market definition involves “demand substitution factors,” or “customers’ ability and willingness to substitute away from one product to another in response to a price increase or a corresponding non-price change such as a reduction in product quality or service.” *Id.* at 7.

208. *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962).

209. *Sidibe v. Sutter Health*, 51 F. Supp. 3d 870, 883 (N.D. Cal. 2014) (quoting *Tanaka v. Univ. of S. Cal.*, 252 F.3d 1059, 1063 (9th Cir. 2001)), *rev’d*, 667 F. App’x 641 (9th Cir. 2016).

210. *Surgical Care Ctr. of Hammond, L.C. v. Hosp. Serv. Dist. No. 1 of Tangipahoa Par.*, 309 F.3d 836, 840 (5th Cir. 2002).

geographic market evidence must take into account ‘where consumers could practicably go, not on where they actually go.’”²¹¹ In 2014, the district court in *Sidibe* articulated the same reason for dismissing the plaintiffs’ geographic market definition—the Dartmouth Atlas’ hospital service areas (routinely used in the health care insurance industry)—saying the definition did not work “for antitrust purposes” because the relevant geographic market should encompass the area where patients *could go*, not just where they typically already did go.²¹² But that case was reversed on appeal by the Ninth Circuit.²¹³ And in the BCBS multi-district litigation, a court recently accepted Dartmouth Atlas Hospital Referral Regions and Dartmouth Atlas Hospital Service Areas as relevant geographic markets “for the product market defined as the purchase of goods and services from healthcare facilities by commercial buyers.”²¹⁴ Accordingly, the notion of where a plaintiff *could go* versus *does go* may be evolving as courts continue to consider how the role of the insurer affects how health care markets function. In other words, the network controls the geographic scope of markets more so than in other antitrust cases where consumers could act on preferences without such constraints. Plaintiffs who focus on the geographic boundaries related to how the network directs patients may therefore be the most successful in defining markets.

2. Claim Selection

Determining which claims to include in one of these cases based on cases already filed is not exactly a scientific exercise. For one, the number of cases filed is small. And of the cases filed, many settle before their claims are litigated.²¹⁵ It is often easier to identify losing strategies than winning ones, but even then all that can be learned from a lower court opinion is how one district court judge saw the issue. For example, many of the cases involving providers and insurers involve similar facts: smaller provider sues larger provider(s) (and often one or more insurer) for keeping it from competing in the market for certain health care services in a given location. Such a case could be styled as a conspiracy to boycott under Sherman Act Section 1, an exclusive dealing arrangement under Sherman Act Section 1 or Section 2 or Clayton Act Section 3, and/or monopolization or a conspiracy to monopolize under Sherman Act

211. *Id.* (quoting *Minn. Ass’n of Nurse Anesthetists v. Unity Hosp.*, 208 F.3d 655, 662 (8th Cir. 2000)).

212. *Sidibe*, 51 F. Supp. 3d at 884.

213. *Sidibe v. Sutter Health*, 667 F. App’x 641, 642 (9th Cir. 2016).

214. *In re Blue Cross Blue Shield Antitrust Litig.*, No. 2:13-CV-20000-RDP, 2017 WL 2797267, at *6 (N.D. Ala. June 28, 2017).

215. *See, e.g.*, *Joint Stipulation of Final Dismissal, Arapahoe Surgery Center, LLC v. Cigna Healthcare, Inc.*, 80 F. Supp. 3d 1257 (D. Colo. 2016) (No. 1:13-CV-03422); *Order of Dismissal with Prejudice, Omni Healthcare, Inc. v. Health First, Inc.*, 2015 WL 275806 (M.D. Fla. Jan. 22, 2015) (No. 6:13-cv-1509-Orl-37DAB).

Section 2, as well as anti-competitive under the relevant state antitrust statutes, and so on. The plaintiff's selections determine whether the case will be examined under the per se doctrine or the rule of reason, what effects must be shown including whether the plaintiff must show it was foreclosed from dealing in the relevant market, and more. Of course, each case has its own specific facts (e.g., a plaintiff may have evidence of an outright conspiracy in one case, whereas another plaintiff may only have the option of suing based on the contracts at issue), as well as other unique circumstances like the political environment involved and the judge assigned. Furthermore, a plaintiff's attempts to choose claims more favorable to the plaintiff's case than the court believes the facts provide for can be fatal, as was the case in *Elizabeth Place*, where the court essentially held that the plaintiffs had tried to shoehorn a case about vertical restraints (restrictions on agreements between providers and payors, which would require more evidence of anti-competitive effects through a rule of reason analysis) into a horizontal conspiracy claim, that they might stand to win under per se treatment.²¹⁶ Accordingly, plaintiffs are ultimately left to determine which claims most accurately reflect the facts of their cases, including the realities of the markets in which they buy or sell health care services or insurance. As courts continue to develop a more sophisticated understanding of how these markets work, plaintiffs will likely be rewarded for such a strategy.

IV. CONCLUSION

Private antitrust enforcement is an indispensable tool in the fight against market power and high prices in health care. Unlike public enforcement, private enforcement allows health care entities to police their own markets and consumers to seek redress from the effects of market power among providers and insurers. Besides, public enforcement is incapable of doing the entire job due to limited resources and or a lack of political will. Despite criticisms that private suits are self-interested and therefore anti-competitive, these lawsuits can be both self-interested *and* pro-competitive. The antitrust laws were written to take advantage of private plaintiffs' incentives and information. Properly optimized, private antitrust enforcement has the potential to provide a truly effective complement to public antitrust enforcement as a means to addressing health care prices.

216. *Medical Ctr. at Elizabeth Place, LLC v. Atrium Health Sys.*, 817 F.3d 934, 946 (6th Cir. 2016).

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THE ANTI-COMPETITIVE POTENTIAL OF CROSS-MARKET MERGERS IN HEALTH CARE

JAIME S. KING* AND ERIN C. FUSE BROWN**

ABSTRACT

Health care consolidation in the United States has been widespread at all levels and across all entities. This consolidation has extended beyond horizontal mergers of hospitals or other providers to include out-of-market mergers, or cross-market mergers. Cross-market mergers include the merger or acquisition of any health care entity that does not directly compete with the acquiring entity in the same product or geographic market. Antitrust enforcers have historically had little in the way of market theory, economic models, or empirical data to inform their analyses on the potential impacts of cross-market mergers on competition. However, recent developments in economic theory and empirical studies now offer evidence that cross-market mergers can, in some instances, harm competition and drive price increases in health care markets when a common insurer exists across those markets. This article aims to start a discussion among the health policy and antitrust communities about the potential for cross-market acquisitions to harm competition, whether existing antitrust laws could theoretically support a challenge to a cross-market acquisition, and the practical challenges to doing so. This article will argue that health policy analysts, antitrust enforcers, and academics should begin to consider the anti-competitive potential of cross-market acquisitions and develop a means to analyze them both legally and economically.

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INTRODUCTION

Over the last several decades, the U.S. health care system has experienced unprecedented provider, insurer, and pharmaceutical company consolidation.¹ This consolidation generated significant concerns among consumers, employers, health services researchers, and government entities, especially in light of ever-rising prices in all facets of health care.² Unfortunately, these concerns proved warranted: The U.S. health care pricing problem is largely a provider market power problem.³ Within the same geographic area, prices for health care services can vary up to 60% for inpatient services and up to 100% for outpatient services between the highest- and lowest-priced hospitals.⁴ Further, health services research demonstrates that provider market power drives these variations in price, rather than differences in quality, payor mix, demographics, or health of the patient population.⁵ In other words, higher-price providers rarely

1. Martin Gaynor et al., *Making Health Care Markets Work: Competition Policy for Health Care*, 317 JAMA 1313, 1313–14 (2017).

2. See ERIN C. FUSE BROWN, NAT'L ACAD. FOR STATE HEALTH POLICY, STATE STRATEGIES TO ADDRESS RISING PRICES CAUSED BY HEALTH CARE CONSOLIDATIONS 1 (Sept. 2017), <http://www.nashp.org/wp-content/uploads/2017/09/Consolidation-Report.pdf>; see also Robert Berenson, *Acknowledging the Elephant: Moving Market Power and Prices to the Center of Health Policy*, HEALTH AFF. BLOG: FOLLOWING THE ACA (June 3, 2014), <http://healthaffairs.org/blog/2014/06/03/acknowledging-the-elephant-moving-market-power-and-prices-to-the-center-of-health-policy/>; *Health Care Market Consolidations: Impacts on Costs, Quality and Access*, 2015-2016 Leg., 413th Sess. 1–2 (Cal. 2016) (statement of Paul B. Ginsburg), <https://www.brookings.edu/wp-content/uploads/2016/07/Ginsburg-California-Senate-Health-Mar-16-1.pdf>.

3. See, e.g., PAUL B. GINSBURG, CTR. FOR STUDYING HEALTH SYS. CHANGE, WIDE VARIATION IN HOSPITAL AND PHYSICIAN PAYMENT RATES EVIDENCE OF PROVIDER MARKET POWER 6–7 (Nov. 2010), <http://www.hschange.org/CONTENT/1162/1162.pdf>; CHAPIN WHITE ET AL., CTR. FOR STUDYING HEALTH SYS. CHANGE, HIGH AND VARYING PRICES FOR PRIVATELY INSURED PATIENTS UNDERSCORE HOSPITAL MARKET POWER 1 (Sept. 2013), <http://www.hschange.org/CONTENT/1375/1375.pdf>; Robert A. Berenson et al., *The Growing Power of Some Providers to Win Steep Payment Increases from Insurers Suggests Policy Remedies May Be Needed*, 31 HEALTH AFF. 973, 973 (2012); Berenson, *supra* note 2; see also FUSE BROWN, *supra* note 2, at 2.

4. WHITE ET AL., *supra* note 3, at 2.

5. See, e.g., MARTHA COAKLEY, MASS. OFFICE OF ATTORNEY GEN., EXAMINATION OF HEALTH CARE COST TRENDS AND COST DRIVERS: REPORT FOR ANNUAL PUBLIC HEARING 2 (2011), <http://www.mass.gov/ago/docs/healthcare/2011-hcctd-full.pdf>; Joseph P. Newhouse & Alan M. Garber, *Geographic Variation in Health Care Spending in the United States: Insights from an Institute of Medicine Report*, 310 JAMA 1227, 1227–28 (2013) (“[P]rice variation is responsible for an estimated 70% of the total geographic variation in spending among privately insured persons. Variation in wage levels and variation in the quantity of services delivered are almost equally responsible for the remaining estimated 30% of spending variation.”); Zack Cooper et al., *The Price Ain't Right? Hospital Prices and Health Spending on the Privately Insured* 3, 33 (Nat'l Bureau of Econ. Research, Working Paper No. 21815, 2015), <http://www.nber.org/papers/w21815> (concluding that hospital market structure, that is, the degree of competition in the market, is strongly associated with hospital prices); GINSBURG, *supra* note 3, at 7.

provide better care or treat patients with more complicated diagnoses; they simply have more market leverage.⁶

Health care consolidation has been widespread at all levels and across all entities. Initially, hospitals, individual physicians, and provider groups merged horizontally with direct competitors.⁷ Next, hospital systems formed and began acquiring additional hospitals, while physician practice groups began to form larger group practices.⁸ In more recent years, consolidation has extended beyond horizontal mergers of hospitals or physician organizations to include non-horizontal, or “cross-market mergers.”⁹ Cross-market mergers include the merger or acquisition of any health care entity that does not directly compete with the acquiring entity in the same product or geographic market.¹⁰ Cross-market mergers can include the acquisition of a physician organization by a hospital system (commonly referred to as vertical health care integration), the purchase of a local community hospital in a rural or suburban area by a hospital system in a major city, or the acquisition of a single-specialty physician group by a larger provider organization in a different market.¹¹ This article will focus on geographic cross-market mergers in which a merger occurs between health care entities in different geographic markets.

Modern health care mergers often involve horizontal, vertical, and cross-market integration of providers, and in some instances the integration of an insurance entity as well.¹² This multifaceted combination of competitors and market complements greatly complicates antitrust analysis. Unfortunately, antitrust enforcers have had little in the way of market theory, economic models, or empirical data to inform their analyses on the potential impacts of geographic

6. See, e.g., COAKLEY, *supra* note 5; GINSBURG, *supra* note 3, at 2–3.

7. See GINSBURG, *supra* note 3, at 7; Kelly J. Devers et al., *Hospitals' Negotiating Leverage with Health Plans: How and Why Has It Changed?* 38 HEALTH SERVS. RES. 419, 427 (2003).

8. See GINSBURG, *supra* note 3, at 7.

9. See Leemore Dafny, Kate Ho & Robin S. Lee, *The Price Effects of Cross-Market Hospital Mergers* 29–30 (Nat'l Bureau of Econ. Research, Working Paper No. 22106, 2016), <http://www.nber.org/papers/w22106> (revised June 2017).

10. See, e.g., Gregory S. Vistnes & Yianis Sarafidis, *Cross-Market Hospital Mergers: A Holistic Approach*, 79 ANTITRUST L.J. 253, 254, 289 (2013); Joe Cantlupe, *New Scrutiny for Hospital Mergers*, NEW ENG. J. MED. CATALYST (Nov. 29, 2016), <https://catalyst.nejm.org/scrutiny-hospital-cross-market-mergers/> (last visited Oct. 16, 2017).

11. See David A. Argue & Scott D. Stein, *Cross-Market Health Care Provider Mergers: The Next Enforcement Frontier* 30 ANTITRUST 25, 25 (2015).

12. Prior to the 1982 Merger Guidelines and their 1984 revisions, courts divided non-horizontal mergers into vertical and conglomerate (which this article refers to as cross-market) mergers. ROBERT S. SCHLOSSBERG, *MERGERS AND ACQUISITIONS: UNDERSTANDING THE ANTITRUST ISSUES* 475–76 (Am. Bar Ass'n, 3d ed. 2008). The Supreme Court has defined a conglomerate merger as “one in which there are no economic relationships between the acquiring and acquired firm,” while lower courts and commentators often label non-horizontal and non-vertical mergers as conglomerates. *Id.* at 475 (quoting *Fed. Trade Comm'n v. Proctor & Gamble Co.*, 386 U.S. 568, 577 n.2 (1967)).

cross-market mergers on competition in health care. In antitrust circles, the assumption has always been that geographic cross-market mergers, by definition, were not anti-competitive because the merging entities did not compete against one another.¹³ However, recent developments in economic theory and empirical studies now offer evidence that geographic cross-market mergers can harm competition and drive price increases in health care markets under certain circumstances.¹⁴ While these findings, accompanied by anecdotal reports from insurance companies claiming that cross-market provider mergers were contributing to higher reimbursement rates, have piqued the interest of the Department of Justice (DOJ) and the Federal Trade Commission (FTC), antitrust enforcers have yet to challenge a cross-market health care merger.¹⁵

This article aims to start a discussion among the health policy and antitrust communities about the potential for cross-market acquisitions to harm competition, whether existing antitrust laws could theoretically support a challenge to a cross-market acquisition, and the practical challenges to doing so. This article examines the applicability of the emerging economic models and empirical evidence on geographic cross-market mergers in health care for antitrust enforcement purposes, presents the case that antitrust enforcers should consider these theories in evaluating cross-market mergers, and discusses the attendant challenges of doing so. Part I describes geographic cross-market mergers and the forces that led to their rise in health care markets. Part II traces the historical evolution of health care antitrust merger enforcement as it adapted to changes in the economic evidence of health care market dynamics. Part III outlines the theoretical model and empirical economic evidence of how geographic cross-market mergers can lead to anti-competitive price increases. Part IV sets forth the legal foundations for bringing a cross-market merger challenge and then identifies areas where further economic and legal analysis is needed. The article concludes that health policy analysts, antitrust enforcers, and academics should begin to consider the anti-competitive potential of geographic cross-market acquisitions and develop a means to analyze them both legally and economically in a much-needed effort to avoid further market consolidation and price increases in health care.

13. See Vistnes & Sarafidis, *supra* note 10, at 254–55.

14. Dafny, Ho & Lee, *supra* note 9, at 2, 29–30; Matthew S. Lewis & Kevin E. Pflum, *Hospital Systems and Bargaining Power: Evidence from Out-of-Market Acquisitions*, 48 RAND J. ECON. 579, 603–04 (2017).

15. See Edith Ramirez, Chairwoman, Fed. Trade Comm’n, Opening Remarks at the Fed. Trade Comm’n & Dept. of Justice Workshop: Examining Healthcare Competition 6 (Feb. 24, 2015) (transcript available at https://www.ftc.gov/system/files/documents/public_events/618591/transcript-day1.pdf).

I. CROSS-MARKET MERGERS

Cross-market mergers in health care involve the merger of health care entities that do not operate in the same geographic or product markets.¹⁶ This article will use the term “cross-market” to describe health care acquisitions across *geographic* markets, regardless of whether the entities offer the same or different products. For example, the merger of hospitals in different counties or the acquisition by a hospital system of a home-health agency in a different metropolitan area would be such a geographic cross-market merger. Under the broad definition, cross-market mergers also include so-called vertical acquisitions of physicians by hospital systems because the two entities offer different products (physician versus hospital services).¹⁷ However, because the early data on cross-market mergers focused on geographic cross-market mergers, this article will also focus on this subset of cross-market mergers, referring to mergers among hospitals and physicians as “vertical” to reflect the separate literature regarding hospital-physician mergers.¹⁸ Cross-market (and vertical) mergers can be contrasted with horizontal or within-market health care mergers that compete in both the same geographic and product markets, such as the consolidation of two hospitals located in the same metropolitan area into a single hospital system.

Cross-market mergers are increasingly common. From 2000 to 2010, roughly one-third of hospital mergers involved cross-market acquisitions.¹⁹ According to another calculation, between 2000 and 2012, more than half of the 528 general acute care hospital mergers involved hospitals or health systems in different geographic areas.²⁰ Prominent examples of national cross-market health care mergers include the 2014 acquisition of 71-hospital Health Management by 135-hospital Community Health System for \$3.9 billion, as well as the 2013 merger of Dallas-based Baylor Health Care System and Temple-based Scott White Health, creating a 43-hospital combined entity with more than 6000 affiliated physicians.²¹ However, cross-market mergers also can be more regional, such as the growth of Sutter Health in Northern California to dominate the areas spanning from San Francisco to Sacramento or the growth of Partners Healthcare in Eastern Massachusetts beyond Central Boston to include

16. Dafny, Ho & Lee, *supra* note 9, at 2.

17. See Caroline S. Carlin et al., *The Impact of Provider Consolidation on Physician Prices*, HEALTH ECON. 1, 2 (2017).

18. See, e.g., *id.*

19. Matthew S. Lewis & Kevin E. Pflum, *Diagnosing Hospital System Bargaining Power in Managed Care Networks*, 7 AM. ECON. J. 243, 244 (2014).

20. Dafny, Ho & Lee, *supra* note 9, at 1 (defining geographic areas as Core Based Statistical Areas, which are metropolitan statistical areas for larger cities and micropolitan areas for smaller towns).

21. *Id.* at 1 & n.3.

physician groups, clinics, and community hospitals spanning from Cape Cod to New Hampshire.²²

Despite antitrust agencies' focus on horizontal health care mergers,²³ the trend of cross-market mergers is growing in importance. The vast majority of hospital markets in major metropolitan areas are already highly concentrated,²⁴ narrowing the options for further concentration in many of those markets. Similarly, many rural areas struggle to support more than one health system.²⁵ Barriers to entry also make it difficult for new firms to open new hospitals as a means of growth.²⁶ As a result, cross-market mergers are likely to increasingly dominate the growth strategy of health care providers.

Under prevailing antitrust enforcement approaches, cross-market mergers in health care have largely escaped antitrust scrutiny. The DOJ's and FTC's traditional view under the Horizontal Merger Guidelines was that mergers across geographic markets did not affect competition because the merging firms did not directly compete in the same geographic or product markets—they were not substitutes at the point of service for any given patient—rendering them either pro-competitive or competitively neutral.²⁷ Without economic evidence to suggest otherwise, U.S. antitrust enforcers have been reluctant to challenge cross-market mergers.

At the same time, growth of health care systems through acquisition (as opposed to building new facilities) has become an industry imperative for providers, and many of these acquisitions have occurred across geographic markets.²⁸ Left unchecked, cross-market acquisitions will continue to allow

22. See DAVID DRANOVE, NAT'L INST. FOR HEALTH CARE MGMT., FEDERAL ANTITRUST ENFORCEMENT IN HEALTH CARE (Mar. 2014), <https://www.nihcm.org/component/content/article/6-expert-voices/1272-federal-antitrust-enforcement?showall=1>.

23. Vistnes & Sarafidis, *supra* note 10, at 254.

24. *E.g.*, David M. Cutler & Fiona Scott Morton, *Hospitals, Market Share, and Consolidation*, 310 JAMA 1964, 1966 (2013) (noting that nearly half of all U.S. hospital markets are highly concentrated); STEPHEN ZUCKERMAN & JOHN HOLAHAN, URBAN INST. HEALTH POLICY CTR., DESPITE CRITICISM, THE AFFORDABLE CARE ACT DOES MUCH TO CONTAIN HEALTH CARE COSTS 2 (Oct. 2012), <http://www.urban.org/UploadedPDF/412665-Despite-Criticism-The-Affordable-Care-Act-Does-Much-to-Contain-Health-Care-Cost.pdf> (noting that as of the mid-2000s, eighty-eight percent of hospital markets in large metropolitan areas are highly concentrated).

25. See KEVIN J. BENNETT ET AL., S.C. RURAL HEALTH RESEARCH CTR., VULNERABLE RURAL COUNTIES: THE CHANGING RURAL LANDSCAPE, 2000-2010 12 (July 2016), [http://rhr.sph.sc.edu/report/\(13-4\)Vulnerable_Rural_Counties_The_Changing_Rural_Landscape_2000-2010.pdf](http://rhr.sph.sc.edu/report/(13-4)Vulnerable_Rural_Counties_The_Changing_Rural_Landscape_2000-2010.pdf) (reporting that “[m]ore than one-fourth of all remote rural counties did not have a hospital in 2010” and there have been seventy-five additional rural hospital closures since 2010).

26. See ORG. FOR ECON. CO-OPERATION & DEV., COMPETITION AND BARRIERS TO ENTRY 1 (Jan. 2007), <http://www.oecd.org/competition/mergers/37921908.pdf>.

27. See, *e.g.*, Argue & Stein, *supra* note 11, at 25–26.

28. See *supra* notes 18–19 and accompanying text.

health care systems to grow and charge excessive prices while evading antitrust scrutiny.²⁹

II. THE EVIDENCE-BASED EVOLUTION OF MERGER ENFORCEMENT PHILOSOPHY

Economics and antitrust law are inextricably linked. As the U.S. Supreme Court noted in *Kimble v. Marvel Entertainment, LLC*, as knowledge and understanding of economics evolves, so should antitrust law and its enforcement.³⁰ This mutual evolution of economics and antitrust law has occurred numerous times as new developments have modified traditional understanding of the economic impact of certain types of mergers and acquisitions.³¹ When economists evaluate a particular industry, they develop theoretical models that attempt to capture key features of its competitive market.³² They then use empirical data to test their theoretical models.³³ If the empirical data validates the model, economists can then use both the theory and the analytical model to make predictions about the potential impact of a particular market event, like a merger or acquisition.³⁴ In recent years, advances in economic modeling of health care markets have resulted in significant advances in the agencies' ability to predict the impact of mergers and acquisitions, resulting in a string of successful antitrust challenges to horizontal health care mergers.³⁵ Now, economic evidence has begun to demonstrate the anti-competitive potential of cross-market mergers in health care, and the time has come again to consider adapting current understanding and interpretation of antitrust law.³⁶ This part describes how developments in economic evidence have historically altered antitrust analysis of horizontal and vertical mergers in health care.

Three federal laws protect competition in American markets: the Sherman Act,³⁷ the Clayton Act,³⁸ and the Federal Trade Commission Act.³⁹ Antitrust

29. See Robert A. Berenson et al., *Unchecked Provider Clout in California Foreshadows Challenges to Health Reform*, 29 HEALTH AFF. 699, 702 (2010); see also Berenson et al., *supra* note 3, at 976.

30. *Kimble v. Marvel Entm't LLC*, 135 S. Ct. 2401, 2412–13 (2015) (The U.S. Supreme Court stated that it has “felt relatively free to revise [its] legal analysis as economic understanding evolves and . . . to reverse antitrust precedents that misperceived a practice’s competitive consequences.”).

31. See discussion *infra* Sections II.A, II.C.

32. Cory S. Capps, *From Rockford to Joplin and Back Again: The Impact of Economics on Hospital Merger Enforcement*, 59 ANTITRUST BULL. 443, 447 (2014).

33. *Id.*

34. *Id.*

35. *Id.* at 444–46.

36. See e.g., Dafny, Ho & Lee, *supra* note 9, at 2; Lewis & Pflum, *supra* note 14, at 2–3.

37. 15 U.S.C. §§ 1–11 (2012).

38. 15 U.S.C. §§ 12–27 (2012); 29 U.S.C. §§ 52–53 (2012).

39. 15 U.S.C. §§ 41–45 (2012).

enforcers typically rely upon Section 7 of the Clayton Act to challenge mergers and acquisitions.⁴⁰ Section 7 of the Clayton Act prohibits acquisitions where the effect “may be substantially to lessen competition, or to tend to create a monopoly.”⁴¹ In 1950, Congress amended Section 7 to broaden its applicability from activities that lessen existing competition between the merging parties to those that lessen competition in any line of commerce.⁴² As a result, antitrust enforcers can enjoin any merger with “probable anticompetitive effect[s].”⁴³ However, antitrust enforcers’ views of which mergers have sufficient potential for anti-competitive effects to warrant a challenge have evolved over time in tandem with developments in economic evidence.

A. *Horizontal Merger Enforcement*

Antitrust enforcement tools for analyzing the potential impact of horizontal mergers are the most well developed because the economic models and evidence for the effects of horizontal mergers are similarly well developed. Horizontal mergers enhance market power by eliminating competition between the parties (“unilateral effects”), or combining assets and market share of former competitors and facilitating collusion (“coordinated effects”).⁴⁴ As noted above, antitrust review of horizontal mergers proceeds under Section 7 of the Clayton

40. David Narrow, *Antitrust Overview*, in CHRISTINE L. WHITE ET AL., *ANTITRUST AND HEALTHCARE: A COMPREHENSIVE GUIDE*, § 2-1(a)(2) (2013).

41. 15 U.S.C. § 18 (2012).

42. Clayton Act, ch. 1184, § 7, 64 Stat. 1125, 1125–26 (1950) (current version at 15 U.S.C. § 18 (2012)).

43. *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962); *accord* *Fed. Trade Comm’n v. Proctor & Gamble Co.*, 386 U.S. 568, 577 (1967) (“All mergers are within the reach of § 7, and all must be tested by the same standard, whether they are classified as horizontal, vertical, conglomerate or other. As noted by the Commission, this merger is neither horizontal, vertical, nor conglomerate. Since the products of the acquired company are complementary to those of the acquiring company and may be produced with similar facilities, marketed through the same channels and in the same manner, and advertised by the same media, the Commission aptly called this acquisition a ‘product-extension merger.’”); *United States v. Falstaff Brewing Corp.*, 410 U.S. 526, 531 (1973) (citing *Fed. Trade Comm’n v. Proctor & Gamble Co.*, 386 U.S. 568, 578–80 (1967) for the proposition that Section 7 “also bars certain acquisitions of a market competitor by a noncompetitor, such as a merger by an entrant who threatens to dominate the market or otherwise upset market conditions to the detriment of competition.”); *id.* at 556–58 (Marshall, J., concurring) (citing *Fed. Trade Comm’n v. Proctor & Gamble Co.*, 386 U.S. 568, 577 (1967) and the 1950 amendment for the proposition that Section 7 could apply beyond the elimination of actual present competition). European antitrust law takes a similar position; an acquisition can be prohibited when it “creates or strengthens a dominant position as a result of which effective competition in the common market or in a substantial part of it would be significantly impeded.” Council Regulation (EC) No. 139/2004 of 20 January 2004 on the Control of Concentrations Between Undertakings, 2004 O.J. (L 24) 1, 3 (discussing Regulation (EEC) No. 4064/89 of December 21, 1989).

44. U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, *HORIZONTAL MERGER GUIDELINES 2* (Aug. 19, 2010), https://www.ftc.gov/sites/default/files/attachments/merger-review/100819_hmg.pdf.

Act.⁴⁵ Traditional horizontal merger analysis requires the enforcer to: (1) define the market, including the product and geographic market parameters and the barriers to entry,⁴⁶ (2) determine the market share based on revenues,⁴⁷ (3) determine the existing market concentration and the change in market concentration resulting from the merger via the Herfindahl-Hirschman Index (HHI),⁴⁸ (4) determine whether the merger will significantly increase concentration in the relevant market, giving rise to a presumption of anti-competitive effects,⁴⁹ and (5) consider the balance of pro- and anti-competitive effects of the merger,⁵⁰ including the potential for merger-specific efficiency gains,⁵¹ unilateral effects,⁵² coordinated effects,⁵³ and customer or supplier reactions.⁵⁴ Despite little doubt that horizontal mergers between direct competitors can harm competition, application of this traditional economic and antitrust analysis resulted in a wave of antitrust enforcement losses in hospital merger challenges followed by more than a decade-long hiatus in health care merger enforcement.⁵⁵

The wave of failed challenges by federal and state antitrust authorities to horizontal provider acquisitions led to the birth of new economic studies and analyses demonstrating how such horizontal provider mergers could lead to price increases, with no corresponding efficiencies, under a two-stage model of health care markets.⁵⁶ The two-stage model divides the competitive dynamic in health care markets into two stages: the first stage in which payors bargain with providers over inclusion in a payor's network on both price and non-price considerations, and the second stage in which patients pick providers primarily based on non-price considerations.⁵⁷ Because of the ubiquity of employer-based health coverage and managed care, large employers often sponsor their own

45. 15 U.S.C. § 18 (2012).

46. U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, *supra* note 44, at 7–8, 13.

47. *Id.* at 17.

48. *Id.* at 18–19.

49. *Id.* at 3.

50. *Id.* at 29–31.

51. Merger-specific efficiency gains include cost savings, quality improvements, and other pro-competitive effects. U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, *supra* note 44, at 29–30.

52. Unilateral effects examine whether the merged firm would have the ability to increase prices or reduce output on its own. *Id.* at 20.

53. Coordinated effects examine whether the merger would facilitate future collusion among market participants. *Id.* at 25.

54. *Id.* at 14; LAWRENCE A. SULLIVAN ET AL., *THE LAW OF ANTITRUST, AN INTEGRATED HANDBOOK* 509 (3d ed. 2016).

55. Capps, *supra* note 32, at 444.

56. See, e.g., *id.* at 444–48, 460; see also, e.g., Steven Tenn, *The Price Effects of Hospital Mergers: A Case Study of the Sutter-Summit Transaction*, 18 INT'L J. ECON. BUS. 65, 71–72, 79 (2011).

57. See, e.g., Gregory Vistnes, *Hospitals, Mergers, and Two-Stage Competition*, 67 ANTITRUST L.J. 671, 673 (2000).

health plans by creating or contracting with a network of providers to offer health care services to employees.⁵⁸

The first stage does not ignore the preferences of the individual consumer. Employers need their health plans to have provider networks robust enough for their employees to have options for obtaining services from providers close to where they live.⁵⁹ By shifting the focus of competitive impact from consumers to health plans, the two-stage model illustrates how acquisitions enable health care providers to gain leverage in their negotiations with insurers by negotiating on an all-or-nothing basis, such that if the insurer does not accept the terms set by the provider system, the system will prevent any of its providers from participating in the insurer's network. All-or-nothing negotiations threaten to create holes in the insurer's provider network, and a new acquisition threatens the creation of an even larger hole thereby increasing the hospital system's negotiating position and market power. Further, the acquisition leaves fewer options for insurers to turn to if the acquiring entity raises its prices post-acquisition.⁶⁰

A number of economic studies have demonstrated a clear relationship between horizontal hospital consolidation and increased prices. In a 2012 review of the literature, Martin Gaynor and Robert Town concluded that "increases in hospital market concentration lead to increases in the price of hospital care."⁶¹ Studies found that hospital mergers in concentrated markets experienced significant price increases in excess of twenty percent compared to non-merging control hospitals.⁶² Additional studies from this time period further suggested that hospital concentration can lead to reductions in quality.⁶³ Gaynor and

58. See Paul Fronstin, *Self-Insured Health Plans: Recent Trends by Firm Size*, EMP. BENEFIT RES. INST. NOTES (Emp. Benefit Research Inst., Washington, D.C.), July 2016, at 2.

59. See, e.g., Fed. Trade Comm'n v. Penn State Hershey Med. Ctr., 838 F.3d 327, 341–42 (3d Cir. 2016); see also United States v. Anthem, Inc., 236 F. Supp. 3d 171, 196, 204, 223 (D.D.C. 2017), *aff'd*, 855 F.3d 345 (D.C. Cir. 2017).

60. See, e.g., Cory Capps et al., *Competition and Market Power in Option Demand Markets*, 34 RAND J. ECON. 737, 757, 760 (2003).

61. MARTIN GAYNOR & ROBERT TOWN, ROBERT WOOD JOHNSON FOUND., THE IMPACT OF HOSPITAL CONSOLIDATION—UPDATE 1 (June 2012), https://www.rwjf.org/content/dam/farm/reports/issue_briefs/2012/rwjf73261.

62. *Id.* at 2 (reporting that "[m]erging hospitals had 40% higher prices than non-merging hospitals") (citing Leemore Dafny, *Estimation and Identification of Merger Effects: An Application to Hospital Mergers*, 52 J.L. & ECON. 523, 544 (2009)); see also Deborah Haas-Wilson & Christopher Garmon, *Hospital Mergers and Competitive Effects: Two Retrospective Analyses*, 18 INT'L J. ECON. BUS. 17, 27–30 (2011); Tenn, *supra* note 56, at 76 (finding that following the merger of Summit and Sutter in California, Summit raised its prices 28.4% to 44.2% compared to the control).

63. WILLIAM B. VOGT & ROBERT TOWN, ROBERT WOOD JOHNSON FOUND., HOW HAS HOSPITAL CONSOLIDATION AFFECTED THE PRICE AND QUALITY OF HOSPITAL CARE? 9 (Feb. 2006), https://www.rwjf.org/content/dam/farm/reports/issue_briefs/2006/rwjf12056/subassets/rwjf12056_1; GAYNOR & TOWN, *supra* note 61, at 4–5.

Town's synthesis of the literature in 2012 confirmed earlier studies from the 1990s and early 2000s providing evidence that hospital consolidation significantly raised prices.⁶⁴

From this body of research, economists developed a new set of analytical tools for assessing competition in health care markets.⁶⁵ Based on the two-stage model of health care markets, economists developed a means to model and empirically measure the leverage gained by providers over insurers following horizontal provider acquisitions.⁶⁶ These analytical tools—willingness-to-pay (WTP) analysis, hospital merger simulation, and diversion analysis—provided a clearer understanding of how health care entities bargain, negotiate, and compete.⁶⁷ The shift in focus from the consumer to the impact of the merger on the health plan's ability to negotiate with entities for inclusion in its network greatly contributed to the agencies' ability to more effectively enforce antitrust laws in those markets.⁶⁸ The use of these models to analyze provider mergers between direct competitors supported a series of decisions barring horizontal provider mergers from federal appellate courts in the Third,⁶⁹ Sixth,⁷⁰ Seventh,⁷¹ and Ninth Circuits.⁷²

B. Vertical Merger Enforcement

Vertical merger analysis has also gained much from the shift in viewpoint from analyzing the impact of the merger on the health care consumer to the impact on the ability of a payor to negotiate with the merged entity for network inclusion. Unlike horizontal mergers, vertical mergers occur between entities that do not directly compete with one another.⁷³ Instead, they provide different

64. GAYNOR & TOWN, *supra* note 61, at 1–2.

65. Capps, *supra* note 32, at 446.

66. *See, e.g.*, Capps et al., *supra* note 60, at 760.

67. *See, e.g.*, Capps, *supra* note 32, at 446.

68. *See id.* at 446–47.

69. Fed. Trade Comm'n v. Penn State Hershey Med. Ctr., 838 F.3d 327, 339–43, 340 n.3, 353 (3d Cir. 2016); Brief of Amicus Curiae Economics Professors in Support of Plaintiffs/Appellants at 9–10, Fed. Trade Comm'n v. Penn State Hershey Med. Ctr., 838 F.3d 327 (3d Cir. 2016) (No. 16-2365), 2016 WL 3251948, at *3.

70. ProMedica Health Sys., Inc. v. Fed. Trade Comm'n, 749 F.3d 559, 571–72 (6th Cir. 2014) (relying on insurer testimony as to the two-stage market).

71. Fed. Trade Comm'n v. Advocate Health Care Network, 841 F.3d 460, 465–66, 468, 470, 476 (7th Cir. 2016); Brief of Amicus Curiae Submitted by Thirty-Three Economists in Support of the FTC and State of Illinois at 8, Fed. Trade Comm'n v. Advocate Health Care Network, 841 F.3d 460 (7th Cir. 2016) (No. 16-2492), 2016 WL 3996861, at *6–9, *11–12, *16–17.

72. Saint Alphonsus Med. Ctr.-Nampa Inc. v. St. Luke's Health Sys., Ltd., 778 F.3d 775, 784 & n.10, 785, 793 (9th Cir. 2015); Brief of Amicus Curiae Economics Professors in Support of Plaintiffs/Appellees at 6, Saint Alphonsus Med. Ctr.-Nampa Inc. v. St. Luke's Health Sys., Ltd., 778 F.3d 775 (9th Cir. 2015) (No. 14-35173), 2014 WL 4312204, at *6.

73. WHITE ET AL., *supra* note 40, at § 3-6.

but complementary elements of an economic supply chain.⁷⁴ While hospitals and physician groups are not in a classically vertical relationship, in that hospitals do not purchase services from physicians, physicians supply a crucial component of hospital services, and a clear relationship exists between the two entities.⁷⁵ Hospitals provide facilities free of charge for physicians to treat their patients, and physicians refer their patients to hospitals.⁷⁶

The traditional view among antitrust enforcers is that vertical mergers can promote competition (or at least be competitively neutral) because “arrangements of integrated providers can provide tremendous procompetitive benefits.”⁷⁷ Under optimal conditions, vertical integration should improve product and pricing efficiency by lowering transaction costs, promoting quality enhancement, eliminating overhead and redundancies, and improving coordination.⁷⁸

However, the relationship between the hospital and the physician group also has the potential to increase the market power of the merged entity vis-a-vis the payor trying to build a network for its health plan, which can drive up health care costs.⁷⁹ Vertical mergers can threaten competition if the merger enhances the merged entity’s ability to foreclose competitors, engage in collusion, evade rate regulation, or raise competitors’ costs in upstream or downstream markets.⁸⁰ Health services research in recent years supports this notion by demonstrating that hospital acquisitions of physician groups are associated with price increases for both the hospitals and the physicians, rather than efficiency gains.⁸¹ These

74. *Id.*

75. Thomas L. Greaney & Douglas Ross, *Navigating Through the Fog of Vertical Merger Law: A Guide to Counselling Hospital-Physician Consolidation Under the Clayton Act*, 91 WASH. L. REV. 199, 206–07 (2016).

76. *Id.* at 206.

77. WHITE ET AL., *supra* note 40, at § 3-6 (quoting Christine A. Varney, Comm’r, Fed. Trade Comm’n, Remarks Before the Health Care Antitrust Forum, Chicago, Illinois (May 2, 1995)).

78. See Martin Gaynor, *Is Vertical Integration Anticompetitive? Definitely Maybe (But That’s Not Final)*, 25 J. HEALTH ECON. 175, 177 (2006); see also Roger D. Blair & D. Daniel Sokol, *Quality-Enhancing Merger Efficiencies*, 100 IOWA L. REV. 1969, 1983–84 (2015).

79. See Esther Gal-Or, *The Profitability of Vertical Mergers Between Hospitals and Physician Practices*, 18 J. HEALTH ECON. 623, 629 (1999).

80. SULLIVAN ET AL., *supra* note 54, at 549, 552–53.

81. See, e.g., Laurence C. Baker et al., *Vertical Integration: Hospital Ownership of Physician Practices is Associated with Higher Prices and Spending*, 33 HEALTH AFF. 756, 762 (2014) (finding hospital ownership of physicians is associated with higher hospital prices and spending); James C. Robinson & Kelly Miller, *Total Expenditures per Patient in Hospital-Owned and Physician-Owned Physician Organizations in California*, 312 JAMA 1663, 1668 (2014) (finding hospital-owned physician organizations had ten to twenty percent higher total expenditures per patient than physician-owned organizations); Cory Capps et al., *The Effect of Hospital Acquisitions of Physician Practices on Prices and Spending* 3 (Inst. for Policy Res., Nw. U., Working Paper No. WP-15-02, Feb. 2015) (finding that vertical integration was associated with a 13.7% increase in physician prices); Hannah T. Neprash et al., *Association of Financial Integration Between*

studies provided evidence that the price increases driven by hospital-physician mergers were due to the enhanced market power of the integrated provider entity when negotiating with payors.⁸²

While the agencies are aware that vertical mergers can harm competition, how to evaluate the competitive effect of a vertical health care merger remains largely uncertain, especially in light of the potential for pro-competitive efficiencies and the need to balance those against potential anti-competitive harms.⁸³ As a result, vertical mergers in health care have rarely been challenged directly. In *Saint Alphonsus Medical Center-Nampa Inc. v. St. Luke's Health System, Ltd.*, the Ninth Circuit prohibited the acquisition of Saltzer, the largest and most prestigious group of primary care physicians in Nampa, Idaho, solely on horizontal grounds (the merger of Saltzer with the hospital's existing physician group), rather than addressing the potential harms raised by the vertical aspects of the merger.⁸⁴ While antitrust agencies have not yet brought a pre-merger challenge to a vertical health care merger, they have imposed behavioral conditions on vertical mergers in exchange for allowing such mergers to proceed.⁸⁵ Through these actions, enforcers have acknowledged that vertical mergers in health care between entities that do not compete in the same product market can result in anti-competitive harm as a result of increased negotiating power with payors. This development is significant because it further opens the door to the possibility that cross-market mergers of entities with related products that do not compete in the same product or geographic market could harm competition.

Physicians and Hospitals with Commercial Health Care Prices, 175 JAMA INTERNAL MED. 1932, 1936 (2015) (finding that metropolitan statistical areas with increases in physician-hospital integration experienced median price increases of seventy-five dollars).

82. See Capps et al., *supra* note 81, at 3, 5–7, 36 (finding that physician price increases following acquisition by hospitals were greater as the size of the acquiring hospital's market share increased, perhaps due to increase in willingness to pay for the integrated entity's services); Robinson & Miller, *supra* note 81, at 1668 (noting that the larger the market share of the hospital-owner, the greater the increase in per-patient expenditures due to hospital-physician integration); Neprash et al., *supra* note 81, at 1937 (noting that commercial price differences were greater than price differences for Medicare, suggesting that the price increases were the result of enhanced market power of integrated providers, not just the fact that Medicare policy paid higher prices for outpatient services provided by physicians acquired by hospitals).

83. See Greaney & Ross, *supra* note 75, at 201–02.

84. *Saint Alphonsus Medical Ctr.-Nampa Inc. v. St. Luke's Health Sys., Ltd.*, 778 F.3d 775, 781–82, 792–93 (9th Cir. 2015).

85. See Amended Final Order at 2, *Penn. v. Geisinger Health Sys. Found.*, No 1:13 CV-02647-YK (M.D. Pa. Nov. 1, 2013); Final Order at 6–18, *Penn. v. Urology of Cent. Penn., Inc.*, No. 1:11-cv-01625-JEJ (M.D. Pa. Aug. 31, 2011).

C. Cross-Market Merger Enforcement

Like horizontal and vertical merger enforcement, antitrust enforcement of cross-market mergers should evolve alongside current understanding of the economic and market forces. If economic theory and empirical evidence supported a claim that cross-market health care mergers could harm competition, U.S. antitrust precedents would allow enforcement agencies to challenge a particular cross-market merger that threatened harm to competition. As noted above, Section 7 of the Clayton Act prohibits all mergers or other combinations of entities where the effect “may be substantially to lessen competition, or to tend to create a monopoly.”⁸⁶ Merger analysis turns on whether the consolidation is likely to harm competition by enhancing the opportunity for collusion or enabling the resulting entity to exercise market power through increasing prices, restraining output, or stifling innovation.⁸⁷

One mechanism by which cross-market mergers can harm both consumers and competition is through anti-competitive tying. Tying arrangements occur when the seller of multiple goods and services conditions the sale of one good or service (“the tying product”) on the purchase of another good or service (“the tied product”).⁸⁸ The essence of an antitrust tying claim is that the seller is using its market power in the tying product market to influence sales in the tied product market.⁸⁹ In a cross-market merger, in which a hospital system acquires another hospital in a different geographic market, the potential for tying arises when the newly merged entity then negotiates with insurance companies on an all-or-nothing basis, such that an insurer must include all of the hospital system’s providers in its network or none at all. Large, multi-hospital systems often include hospitals or provider organizations that are “must have” entities, such that an insurer could not build a successful network without them.⁹⁰ Must-have providers generate significant market power for their health systems, which can extend to all other providers within the system via contracting.⁹¹ For instance, large hospital systems that engage in “all-or-nothing” contracting have reportedly added anti-tiering provisions to their contracts with payors to prevent the payor from accepting all system providers at inflated rates and then developing tiered benefit packages that incentivize plan participants to select

86. 15 U.S.C. § 18 (2012).

87. U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES 2 (Aug. 19, 2010), <https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf>.

88. WHITE ET AL., *supra* note 40, at § 9-2(c).

89. *Id.*

90. See Robert A. Berenson et al., *The Growing Power of Some Providers to Win Steep Payment Increases from Insurers Suggests Policy Remedies May Be Needed*, 31 HEALTH AFF. 973, 973 (2012).

91. See *id.* at 973, 978.

lower priced alternatives.⁹² The possibility of anti-competitive tying exists when a health system spans several geographic and product markets and contracts with insurers or customers that also span those markets.⁹³

While tying claims are most frequently brought under Sherman Act Section 1 which prohibits contracts “in restraint of trade,”⁹⁴ the probable anti-competitive effects resulting from tying can justify a merger challenge under the Clayton Act Section 7.⁹⁵ Section 7 does not require proof of anti-competitive behavior but rather permits courts to predict the likely competitive impact of a proposed merger or acquisition based on past conduct, present facts, and economic modeling. Courts only require evidence of a probable future adverse impact on competition.⁹⁶ Therefore, if economic theory and research support a claim that a cross-market merger posed a substantial threat to competition, the agencies would have the legal basis to bring a pre-merger challenge.

III. THE THEORETICAL AND EMPIRICAL BASES FOR CONSIDERING THE ANTI-COMPETITIVE POTENTIAL OF CROSS-MARKET MERGERS IN HEALTH CARE

Traditionally, antitrust challenges to cross-market mergers were not viable, regardless of whether the case law would permit such a challenge, because of the paucity of economic theory and empirical data to support the notion that cross-market mergers could be anti-competitive. This state of affairs, however, is ripe for review.

Recent breakthroughs in health economics offer both theoretical and empirical descriptions of how cross-market acquisitions in health care can increase prices when a common insurer or common customer purchases products or services supplied by both entities.⁹⁷ First, Vistnes and Sarafidis modeled how a hospital system can, as a theoretical matter, increase prices after acquiring providers in a different geographic market.⁹⁸ In 2016, Dafny, Ho, and Lee expanded upon Vistnes and Sarafidis’ model and findings from Ho and Lee’s earlier research,⁹⁹ demonstrating that the merger of hospitals in different

92. Glenn A. Melnick & Katya Fonkych, *Hospital Prices Increase in California, Especially Among Hospitals in the Largest Multi-Hospital Systems*, 53 INQUIRY 1, 5 (2016).

93. As Part II discusses, anti-competitive tying is not the only mechanism through which a cross-market merger could harm competition, but it currently is the best understood one. See *infra* Part II.

94. 15 U.S.C. § 1 (2012).

95. *Id.* at § 18.

96. *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962); Peter C. Carstensen, *The Philadelphia National Bank Presumption: Merger Analysis in an Unpredictable World*, 80 ANTITRUST L.J. 219, 239–40 (2015).

97. See, e.g., Vistnes & Sarafidis, *supra* note 10, at 260; Dafny, Ho & Lee, *supra* note 9, at 29.

98. Vistnes & Sarafidis, *supra* note 10, at 293.

99. Kate Ho & Robin S. Lee, *Insurer Competition in Healthcare Markets* (Nat’l Bureau of Econ. Res. Working Paper No. 19401, 2013), <http://www.nber.org/papers/w19401.pdf>.

geographic markets could influence insurer reimbursement rates if those insurers had customers (employers) who employed workers in both markets.¹⁰⁰ Dafny, Ho, and Lee theorized that cross-market health care mergers could have anti-competitive effects if the health care system and the acquired provider: (1) bargained with common insurers for network inclusion; and/or (2) had customers in common, i.e., firms with employees in both markets.¹⁰¹ The anti-competitive potential results from the ability of the newly merged entity to sell (or refuse to sell) both the products in ways that increase the utility of (or disutility of not) having both products beyond the sum of their independent utilities.¹⁰² In many respects, this resembles anti-competitive tying. Additional studies by Matthew Lewis and Kevin Pflum, and Glenn Melnick and Katya Fonkych also provide empirical evidence that cross-market mergers can be anti-competitive.¹⁰³

To understand the joint utility loss, imagine that you must choose a health plan for your family, and you care most about a network that covers both your kids' pediatrician and your cardiologist. A plan that includes both is the most desirable, a plan that includes one or the other has slightly less value, but you will not accept a plan that includes neither. A plan that includes both the pediatrician and the cardiologist would provide the most utility, whereas a plan with neither would have even less utility than the sum of the utility lost in plans that lacked either the pediatrician or the cardiologist. Dafny, Ho, and Lee call this the "common customer effect."¹⁰⁴

The common customer effect is experienced by large employers and insurance companies that must negotiate reimbursement rates with merging health care providers. Employers with employees working across numerous geographic markets seek plans with networks that provide the greatest value across all markets. To these employers, the overall provider bundle or network is the product, such that they consider whether one provider bundle is substitutable for another rather than any particular provider in one geographic market.¹⁰⁵ As a result, insurers have incentives to build networks that include key providers for employers even when they are not in the same geographic

100. Dafny, Ho & Lee, *supra* note 9, at 2–3.

101. *Id.* at 5–6.

102. *See id.* at 5.

103. Lewis & Pflum, *supra* note 14, at 603–04; Melnick & Fonkych, *supra* note 92, at 6.

104. Dafny, Ho & Lee, *supra* note 9, at 9–11. Dafny, Ho, and Lee also hypothesized that the same theory would also apply when there are no common customers but instead common insurers—the common insurer effect. *Id.* at 12. In this scenario, cross-market mergers could enable a hospital system to recoup revenues lost due to political or legislative constraints in one market (caps on increases) by acquiring a hospital in a non-constrained market, and then increasing rates in the non-constrained hospital and requiring all insurers to include both hospitals in their networks. *Id.* at 12, 14.

105. *See id.* at 2.

market. Similar to the example above, an acquisition linking two hospitals in distinct geographic markets together for negotiating purposes could make the loss of both hospitals from the network greater than the sum of the losses of each hospital independently in the absence of the acquisition.¹⁰⁶ This effect can manifest through health plan premiums as the health plan must either raise premiums to accommodate the increased provider costs from the merged entity or lower premiums to account for the holes in the network and compromise health plan profits.¹⁰⁷ As a result, for example, a large health care system in Northern California with market power in one or more counties could require insurers, such as Aetna or Blue Shield, to include newly-acquired providers in Central and Southern California in their networks at increased prices. The newly-acquired providers could raise prices by taking advantage of the bargaining leverage of the acquiring health care system, which stems from the threat of more significant network holes if the system leaves a provider network en masse.¹⁰⁸ Importantly, the common customer effect results from a change in the parties' bargaining options, not from increased negotiating skill, which opens the door to antitrust enforcement.¹⁰⁹

Over time, aspects of this theory have been borne out both theoretically and empirically. To test their hypotheses, Dafny, Ho, and Lee examined two distinct samples of acute care hospital mergers over the period of 1996 to 2010 and the price trajectories after those mergers for three groups of hospitals: "(i) hospitals acquiring a new system member in the same state but not the same narrow geographic market ('adjacent treatment hospitals'); (ii) hospitals acquiring a new system member out of state ('non-adjacent treatment hospitals'); and (iii) hospitals that are not members of 'target' (i.e., acquired) or acquiring systems."¹¹⁰ Dafny, Ho, and Lee found that a merger between hospitals in different geographic regions within the same state with common customers or common insurers led to significant price increases of seven to ten percent compared with control hospitals that were not part of a merger.¹¹¹ The authors observed this price effect in "bystander" hospitals, which were part of the

106. *See id.* at 4.

107. Argue & Stein, *supra* note 11, at 28; *see also* Dafny, Ho & Lee, *supra* note 9, at 36. Interestingly, the economists appear to differ on the underlying mechanism resulting in the ability of cross-market mergers to compromise health plan profits. Dafny, Ho, and Lee argue that it results from a "change in parties' outside options (or threat points) when bargaining." *Id.* at 4. Lewis and Pflum contend that the increase in bargaining power results from system membership either via all-or-nothing bargaining or altering the bargaining power of a particular hospital in the system. *See* Lewis & Pflum, *supra* note 14, at 602. Regardless of the mechanism, the ability to create network holes and demand higher reimbursements remains.

108. *See* Dafny, Ho & Lee, *supra* note 9, at 6, 12.

109. *See id.* at 4.

110. *Id.* at 3.

111. *Id.*

merging system, but not the “crown jewel” motivating the acquisitions.¹¹² The closer in geographic proximity the merging parties were to each other, the larger the price effects.¹¹³ The price effects of the cross-market health care mergers provide empirical evidence that the health system’s market power increases when it adds more providers due to the ability to tie (or “pull through”) the system’s acquired providers to its strongest “must-have” providers when bargaining with health plans. Correspondingly, increasing the number of preferred providers in a system increases the number and significance of network holes the merged health system can threaten if the health plan does not accept the health system’s higher prices.

Dafny, Ho, and Lee’s seminal study is not an outlier. An earlier study by Lewis and Pflum estimated that health care systems can raise prices more for an acquired provider in a different geographic market than a comparable hospital does when it acquires a close competitor within the same market.¹¹⁴ In other words, Lewis and Pflum found that cross-market provider acquisitions in some instances could lead to greater price increases and thus be more anti-competitive than even horizontal provider acquisitions involving direct competitors. Lewis and Pflum then released a second study further evaluating the price effects from cross-market acquisitions, which found that “prices at hospitals acquired by out-of-market systems increased by about 17% more than unacquired, stand-alone hospitals.”¹¹⁵

Furthermore, Melnick and Fonkych, in their study of hospital prices in California, found that “the market power effects of large hospital systems do not necessarily require consolidation between local competitors.”¹¹⁶ Their study revealed that many of the hospitals in California’s largest systems do not substantially overlap with other system hospitals in terms of product and geographic markets.¹¹⁷ The authors concluded that “hospitals in large hospital

112. Dafny, Ho & Lee, *supra* note 9, at 17.

113. *Id.* at 3, 25. This study also theorized that due to the double-marginalization problem, the health care system’s acquisition of a provider in a new geographic market might allow it to retain profits that it would otherwise cede to insurers and thereby raise prices. *See id.* at 12–13.

114. Lewis & Pflum, *supra* note 19, at 244, 246; *see id.* at 248–57 (modeling based on the auction model used for horizontal provider mergers to value access to hospitals on an estimate of the cost function for multi-product firms in general and hospitals, and on bargaining models, in turn, based on the assumption that insurers try to get nearly every hospital into their networks); *id.* at 257 (using data from sources such as the American Hospital Association and the California Office of Statewide Health Planning and Development); *id.* at 266 (“Our results also indicate that, in addition to improving their bargaining position by increasing concentration within a local patient market, system hospitals have significantly higher bargaining power and extract roughly 30 percent more of the surplus generated by the hospital-[insurer] relationship than comparable nonsystem hospitals.”).

115. Lewis & Pflum, *supra* note 14, at 579.

116. Melnick & Fonkych, *supra* note 92, at 6.

117. *Id.*

systems, by tying their hospitals together, are able to achieve market power over prices beyond any local market advantages.”¹¹⁸ While these findings advance understanding of the economic underpinnings of the U.S. health care system, whether antitrust enforcers can use these findings to address the anti-competitive effects of cross-market acquisitions by health care systems remains a legal question for enforcers and courts to resolve.

IV. THE POTENTIAL FOR CROSS-MARKET ANTITRUST ENFORCEMENT

Even with new economic evidence suggesting that cross-market mergers have the potential to harm competition in health care markets and a legal foundation for bringing a claim, bringing a successful cross-market merger challenge is easier said than done. Several economic and legal hurdles remain. First, some skepticism in academic and enforcement circles remains about whether cross-market mergers can be anti-competitive.¹¹⁹ Second, an antitrust enforcer seeking to challenge a cross-market merger must convince her colleagues that the proposed merger presents a significantly higher risk to competition than other potential health care merger challenges as to warrant use of scarce agency resources on a case with a less clearly trodden path through litigation. Third, while the Clayton Act provides a legal basis to challenge a cross-market merger,¹²⁰ successfully litigating the suit will require the development of new economic and legal analytic frameworks and tools for analyzing the potential impact of a cross-market merger to the provider system’s ability to negotiate prices with insurers and employers. As economists continue to conduct research on cross-market mergers and develop models to determine their potential impact, the legal academy and antitrust enforcers should similarly evaluate this research to determine whether and how a cross-market merger challenge should be brought. As economists, lawyers, and academics develop the economic and legal tools needed to build a strong cross-market merger challenge and overcome the third hurdle, the first two hurdles should diminish substantially. As the economic analysis increasingly demonstrates the anti-competitive potential of certain cross-market mergers, skepticism will diminish, and the relative importance of bringing a challenge will increase. The rest of this section highlights areas for further consideration, research, and analysis.

118. *Id.* The authors noted that their study did not control for quality, technological, and financial differences between the hospitals in large systems and other hospitals, but their study did include quality differences at the end, which had a minimal effect on price differences. *Id.*

119. *See, e.g.,* Argue & Stein, *supra* note 11, at 25.

120. *See supra* Section I.C.

A. *Reframing Traditional Merger Analysis*

Typically, in hospital mergers, courts examine the impact of the merger in terms of its impact on the relevant product and geographic markets.¹²¹ For instance, the acquisition of an additional hospital by a large, multi-hospital system could be analyzed in terms of its impact on the price for acute care services (the product market) in Marin County, California (the geographic market). However, the analysis should shift when analyzing cross-market mergers, as the merging entities do not compete in the same product and geographic markets. Instead, antitrust enforcers should consider analyzing the merger based on the potential direct effect it might have on the value of the bundle of services offered by the hospital system to insurers for inclusion in their network. For the Common Customer or Common Insurer, what matters is the market leverage gained by the merged health care entity in terms of negotiating reimbursement rates and network inclusion. How much does the addition of the entity being acquired increase the bargaining position of the acquiring system when negotiating with insurers and employers? Just as the value of adding an additional player to a basketball team depends on the player's skills, who else is on the team, and the existing team chemistry, the value of adding a provider to an existing system will depend not only on the value of the entity being acquired itself, but also on the value of the other individual entities in the acquiring system and the overarching value of the entire post-merger entity. To determine the impact on market power and competition, antitrust enforcers should develop a means to determine the value of a particular acquisition to an entire system—to show the relative value of the target entity in the market (its market power) and then how much value it adds to the system given the other entities in the system, and the cumulative loss experienced by an insurer or employer from not having any of those entities in its network.

Developing such a valuation mechanism will be challenging and must factor in an array of conditions. For instance, state network adequacy laws can significantly affect the value of a particular acquisition to a health system and should be factored into any analysis.¹²² Relatedly, the status of an entity as a “must have” provider, one that is essential to a network, can strongly affect the

121. *E.g.*, WHITE ET AL., *supra* note 40, at 67–68.

122. Network adequacy laws regulate health plans' ability to provide enrollees with timely and reasonably close access to a sufficient number of in-network primary care and specialty physicians, and hospital and other health care services included under the terms of the contract. *See, e.g.*, Ashley Noble, *Insurance Carriers and Access to Health Care Providers: Network Adequacy*, NAT'L CONF. ST. LEGISLATURES (Nov. 13, 2015), <http://www.ncsl.org/research/health/insurance-carriers-and-access-to-healthcare-providers-network-adequacy.aspx> (last visited Nov. 26, 2017). More stringent network adequacy requirements mean that the value of any essential provider or group of physicians will increase if they cannot be excluded from the insurer's network under the state requirements. *See, e.g., id.*

market power of the acquiring merged health system.¹²³ Furthermore, the value analysis should be able to model the value of a particular acquisition in two alternate conditions: (1) in the instance that the merged system engages in all-or-nothing bargaining and (2) in the instance that the merged system allows insurers and employers to contract for services from its subsidiary entities individually. In sum, the value analysis will require economic modeling that accounts for both the complexities in cross-market mergers as well as the legally relevant variables in any particular case.

B. Model Insurer Willingness to Pay in Cross-Market Mergers

Successful merger challenges typically require economic modeling to predict the impact of the merger on the relevant market. Historically, most research examining the impact of provider consolidation on health care prices focused on traditional horizontal mergers.¹²⁴ Initially, these studies examined the relationship between prices and market concentration, usually measured by the HHI.¹²⁵ More recent studies utilized structural models that account for the fact that provider reimbursement rates often result from complex negotiations between providers (hospitals or hospitals systems) and managed care organizations.¹²⁶ These structural models value the market power of a particular

123. Morgan A. Muir et al., *Clarifying Costs: Can Increased Price Transparency Reduce Healthcare Spending?* 4 WM. & MARY POL'Y REV. 319, 329, 353 (2013).

124. E.g., Lewis & Pflum, *supra* note 14, at 579–80; *see also, e.g.*, David Dranove et al., *Price and Concentration in Hospital Markets: The Switch from Patient-Driven to Payer-Driven Competition*, J.L. & ECON. 179, 180–81 (1993); William J. Lynk, *The Creation of Economic Efficiencies in Hospital Mergers*, 14 J. HEALTH ECON. 507, 507–09 (1995); David Dranove & Richard Ludwick, *Competition and Pricing by Nonprofit Hospitals: A Reassessment of Lynk's Analysis*, 18 J. HEALTH ECON. 87, 87–88 (1995); Alison Evans Cuellar & Paul J. Gertler, *How the Expansion of Hospital Systems Has Affected Consumers*, 24 HEALTH AFF. 213, 213–15 (2005); Glenn Melnick & Emmett Keeler, *The Effects of Multi-Hospital Systems on Hospital Prices*, 26 J. HEALTH ECON. 400, 401 (2007).

125. HHI is calculated as the sum of the squared market share of each entity or health system in a given market multiplied by 10,000. *Herfindahl-Hirschman Index*, U.S. DEP'T OF JUSTICE (July 29, 2015), <http://www.justice.gov/atr/herfindahl-hirschman-index> (last visited Oct. 13, 2017). For hospitals, market share is calculated as proportional share of inpatient admissions or patient days possessed by a hospital relative the rest of the market. *See* Lewis & Pflum, *supra* note 14, at 597. Typically, a market is considered “highly concentrated” if the HHI is greater than 2500, which means there are about four equal sized hospital owners in a given market. U.S. DEP'T OF JUSTICE, *supra*. A market is “moderately concentrated” if its HHI is between 1500 and 2500. *Id.*

126. E.g., Lewis & Pflum, *supra* note 14, at 579–80; *see also, e.g.*, John M. Brooks et al., *Hospital-Insurer Bargaining: An Empirical Investigation of Appendectomy Pricing*, 16 J. HEALTH ECON. 417, 418–19 (1997); Robert Town & Gregory Vistnes, *Hospital Competition in HMO Networks*, 20 J. HEALTH ECON. 733, 734 (2001); Capps et al., *supra* note 60, at 737–39; Katherine Ho, *Insurer-Provider Networks in the Medical Care Market*, 99 AM. ECON. REV. 393, 393 (Mar. 2009); Lewis & Pflum, *supra* note 19, at 245; Gautam Gowrisankaran et al., *Mergers when Prices Are Negotiated: Evidence from the Hospital Industry*, 105 AM. ECON. REV. 172, 173 (Jan. 2015).

provider organization based on a managed care enrollee's "willingness to pay," which evaluates how much more the enrollee would be willing to pay to have access to that hospital as opposed to going to the next best alternative for care.¹²⁷ These models have become widely adopted by antitrust authorities in evaluating the impact of potential hospital and health system mergers.¹²⁸

WTP analysis helps elucidate the two mechanisms by which hospital system formation can affect the negotiated price.¹²⁹ First, when hospitals merge into a system, they typically negotiate with insurers and managed care organizations on an all-or-nothing basis, such that the insurer must include all member hospitals into its networks or none at all.¹³⁰ When the merging hospitals are in a single geographic market, all-or-nothing bargaining means that enrollees cannot substitute one hospital for another in the system, thereby limiting their options. This makes the option value of having access to all hospitals in the system greater than the sum of the option values for having access to only one of the system hospitals if the other hospitals remained in the network.¹³¹ Second, membership in a health system can alter the bargaining power of a member hospital.¹³² This increase in bargaining power can result from system membership via improved information on prior contract negotiations and gained knowledge of agreements between the system and the insurer or employer regarding other providers in the system, and increased negotiating skill.¹³³

Both of these mechanisms can also affect price negotiations in cross-market mergers involving health systems. First, cross-market mergers can alter the bargaining position of the acquiring health system when negotiating with a large employer with employees in different markets or their insurer.¹³⁴ While individual enrollees will not view providers in different markets as substitutable, a large employer or an insurance company looking to build an attractive network for a large employer will highly value a health system with providers in all the markets where its employees live.¹³⁵ Second, the same potential benefits from improved information, negotiating skill, capital access, and knowledge of prior

127. See Lewis & Pflum, *supra* note 19, at 244.

128. *E.g.*, Fed. Trade Comm'n v. Advocate Health Care Network, 841 F.3d 460, 476 (7th Cir. 2016); Fed. Trade Comm'n v. Penn State Hershey Med. Ctr., 838 F.3d 327, 342, 353 (3d Cir. 2016); ProMedica Health Sys., Inc. v. Fed. Trade Comm'n, 749 F.3d 559, 567 (6th Cir. 2014); Fed. Trade Comm'n v. OSF Healthcare Sys., 852 F. Supp. 2d 1069, 1086 (N.D. Ill. 2012).

129. Matthew Lewis & Kevin Pflum, *Hospital Systems and Bargaining Power: Evidence from Out-of-Market Acquisitions 7* (Aug. 25, 2014) (working paper), http://www.unc.edu/~mcmanusb/AppliedMicroSeminar/papers/Lewis_Pflum_hosp_bp.pdf.

130. *Id.*

131. *Id.*

132. *Id.* at 8.

133. See *id.*

134. See Vistnes & Sarafides, *supra* note 10, at 275; see also Dafny, Ho & Lee, *supra* note 9, at 2.

135. Lewis & Pflum, *supra* note 129, at 7–8.

and current contract terms can shift the bargaining power, and therefore the negotiated prices for newly-acquired member hospitals even if they are cross-market acquisitions.¹³⁶

Unfortunately, initial models of WTP, based on the impact of system inclusion on an individual consumer, do not capture the potential anti-competitive effects that may arise from cross-market mergers, as a particular consumer may not value the addition of providers in a different geographic area.¹³⁷ Existing studies and recent antitrust analysis “assume[] that bargaining power is fixed and that enrollee willingness to pay is derived only from local hospital and market characteristics.”¹³⁸ Under this assumption, the insurer’s WTP objective function is linear, and only mergers between hospitals that compete within the same geographic and product market can result in a price increase.¹³⁹ However, the research by Dafny, Ho, and Lee, and Lewis and Pflum cast doubt on the assumption that the insurer’s WTP for a particular provider is in fact linear. Instead, their data suggested that the insurer’s WTP objective function would be concave in this scenario, enabling both within-market and cross-market mergers between hospitals sharing a common customer to result in higher WTP by insurers and price increases.¹⁴⁰ The emerging economic evidence thus suggests that WTP analysis could be revised to encompass cross-market health care mergers by shifting from a fixed to a dynamic model of bargaining power that can encompass multiple markets.

Health economists working in this area should begin testing and validating the WTP models proposed by Dafny, Ho, and Lee, and determining whether the model applies to geographic cross-market hospital mergers, as well as health system acquisitions of physician groups. They should also try to incorporate legally relevant variables such as network adequacy laws and state insurance requirements. Further refining the economic models also offers the opportunity to develop potential limiting principles that will help identify anti-competitive cross-market mergers.

C. *Develop Limiting Principles*

Key limiting principles would delineate when cross-market acquisitions by provider systems should be proscribed under the antitrust laws as having likely anti-competitive effects. To trigger legal intervention and potential antitrust remedies, price increases must be due to abuses of market power, rather than quality improvements, better negotiating skills of the merged entity, greater

136. *See id.* at 8.

137. *See id.* at 2.

138. *Id.* at 8.

139. Dafny, Ho & Lee, *supra* note 9, at 8.

140. *Id.* at 5.

ability to bear risk, or other legitimate drivers of price.¹⁴¹ Health economists, legal academics, and antitrust enforcers should identify and test limiting principles to isolate acquisitions that are likely to have anti-competitive effects from those that are likely to have pro-competitive or neutral effects. Such limiting principles would provide important guidance to both antitrust enforcers and the health care community, and help avoid unnecessary costs and ineffectual results.¹⁴²

Several potential limiting principles have already arisen in economic research and case law. First, Dafny, Ho, and Lee's research suggests that there must be a common customer with employees or insureds that span the markets served by the merging entities.¹⁴³ Second, existing case law and economic research also recommend considering whether the acquiring entity had market power in one or more markets prior to the acquisition.¹⁴⁴ Researchers and

141. See SULLIVAN ET AL., *supra* note 54, at 30–31.

142. See Eric A. Posner, Fiona Scott Morton & E. Glen Weyl, *A Proposal to Limit the Anti-Competitive Power of Institutional Investors*, ANTITRUST L.J. (forthcoming) (manuscript at 9–10, 46–47) (advocating that hedge fund investment in oligopolistic industries be barred under Section 7 only if certain limiting principles are not present and noting that such principles are needed to avoid vast costs and uncertainty or ineffectual outcomes).

143. Dafny, Ho & Lee, *supra* note 9, at 5–6; see also Vistnes & Sarafidis, *supra* note 10, at 274–75, 282 (discussing bargaining in a post cross-market acquisition situation where common employers are involved that must offer plans covering all their employees at the same price, no matter where those employees live in a state).

144. See *United States v. Falstaff Brewing Corp.*, 410 U.S. 526, 558–59 (1973) (Marshall, J., concurring); U.S. DEP'T OF JUSTICE, ANTITRUST DIVISION SUBMISSION FOR OECD ROUNDTABLE ON PORTFOLIO EFFECTS IN CONGLOMERATE MERGERS 20 (2001), <https://www.justice.gov/sites/default/files/atr/legacy/2015/01/26/9550.pdf> (noting that any theory of competitive harm from tying in the General Electric-Honeywell merger depended on General Electric having market power in the market for large aircraft engines); Dafny, Ho & Lee, *supra* note 9, at 29 (“Prior researchers have shown that mergers of nearby, similar rivals can lead to increases in market power and higher prices. The existence of a common customer effect implies that market power may arise from combinations over even broader geographic areas and across product markets. This finding does not imply more expansive boundaries for mechanical calculations of market shares and ‘ΔHHI’ used to evaluate whether mergers are likely to be anticompetitive; rather, we believe it favors an emphasis on the ‘direct effects’ likely to arise from a merger, a concept promulgated in the 2010 Horizontal Merger Guidelines.”); Lewis & Pflum, *supra* note 129, at 3 (“Together the findings reveal that systems can have a significant impact on the market power of hospitals in ways that have not been studied or taken into consideration in recent antitrust analysis.”); *id.* at 37–38 (“Taken together, these findings indicate that there are important cross-market dependencies present in the market allowing hospitals to gain market power vis-à-vis MCOs in the price negotiation game by joining an out-of-market system.”); see also Einer Elhauge, *Rehabilitating Jefferson Parish: Why Ties Without a Substantial Foreclosure Share Should Not Be Per Se Legal*, 80 ANTITRUST L.J. 463, 505–06 (2016) (tying firm with market power in the tying market adversely impacts consumer welfare even if that tying conduct only impacts a non-trivial amount of sales in the tied product market); Christopher R. Leslie, *Tying Conspiracies*, 48 WM. & MARY L. REV. 2247, 2262 (2007) (explaining how tying conspiracies can allow firms with individually small market shares to exercise market power in the aggregate).

antitrust enforcers should consider whether designating a threshold of market power, such as thirty percent, would prove valuable to identifying cross-market acquisitions that substantially threaten competition, and are worthwhile to challenge. Dafny, Ho, and Lee do not suggest that a market share threshold is required for anti-competitive effects to be likely. However, antitrust enforcers may want to designate a market share threshold for practical purposes to help them identify the mergers that pose the most risk to competition. Third, due to state insurance laws that govern network adequacy, institute coverage mandates, and regulate insurance more generally, examining cross-market acquisitions of providers within the same state as the health care system may be a good starting point for analysis.¹⁴⁵ This is not to say that only same-state, cross-market mergers can be anti-competitive, but initially this restriction may help simplify the analysis. Interestingly, Dafny, Ho, and Lee found that the closer the hospitals were “in terms of drive time,” the more likely employers are to have employees living in both locations or commuting between them.¹⁴⁶ Disentangling the effects of driving distance from the effects of same-state acquisitions will prove very important in terms of limiting principles, as large employers often employ workers across state lines at distances that may be much smaller than the distance between merging entities in the same state. Antitrust enforcers, legal academics, and health economists should begin evaluating potential limiting principles to help develop the required legal framework for bringing a cross-market challenge.

CONCLUSION

As understanding of the forces that shape health care markets evolve, so should the ability to protect those markets from anti-competitive behaviors. Now that economic research has provided empirical and theoretical support for the claim that cross-market mergers have the potential to lead to increased market power and increased prices, the time has come for the antitrust community to begin to evaluate this claim. Health care consolidation is a leading driver of health care costs in the United States.¹⁴⁷ To develop effective health care reform, policymakers must have an understanding of all the ways that consolidation can influence market power and increase costs. Health economists, legal academics, and antitrust enforcers should begin examining this research to determine whether, under what circumstances, and how challenges to cross-market

145. See Vistnes & Sarafidis, *supra* note 10, at 292–93 (expressing doubt that the implications of the author’s modeling could apply to *interstate* cross-market acquisitions); *cf.* Fed. Trade Comm’n v. Sysco Corp., 113 F. Supp. 3d 1, 49 (D.D.C. 2015) (finding both a nationwide market for food broadline distribution based on the shared characteristics of a core group of customers as well as *intrastate* local markets for food broadline distribution for other customers based on driving time).

146. Dafny, Ho & Lee, *supra* note 9, at 26.

147. See, e.g., GAYNOR & TOWN, *supra* note 61, at 1.

mergers should be brought to promote and protect competition in health care. This article outlines the hurdles to bringing such a challenge and identifies potential limiting factors for consideration. Developing the legal and economic frameworks needed to bring an antitrust enforcement suit will take time and cooperation, and the antitrust community should begin addressing these concerns now, before the consolidation further harms U.S. health care markets and increases costs.