

## Interview with FTC Director of the Bureau of Economics Michael R. Baye

**Editor's Note:** In this interview with The Antitrust Source, Dr. Michael Baye discusses his views on horizontal merger analysis, econometrics, and recent activities in consumer protection. Dr. Baye began his job as the Director of the Bureau of Economics in July 2007. He is at the FTC on leave from Indiana University's Kelly School of Business, where he has been the Bert Elwert Professor of Business since 1997. Dr. Baye's academic research focuses on pricing strategies and their impact on consumer welfare and firm profits and has applied tools from game theory and industrial organization to evaluate network industries, mergers, auctions, and online markets. The interview was conducted on February 5, 2008, by Editor Elizabeth M. Bailey for The Antitrust Source.

**THE ANTITRUST SOURCE:** You joined the Federal Trade Commission in the summer of 2007 as the Director of the Bureau of Economics. How has the transition been from academics to the FTC?



**Michael R. Baye**

**MICHAEL BAYE:** It's been the experience of a lifetime. The number of interesting questions that come across my desk each day is pretty astounding.

One big difference between what I do here and my life as an academic is the scope of the issues that I deal with. As you probably know, most academic research tends to be highly specialized. Many academics spend a lot of time working on very narrow technical questions that we hope might be useful or policy-relevant some day. Academic contributions tend to be fairly incremental, which means that the direct relevance of any one academic contribution to a real-world problem is pretty small relative to the cumulative effect of all the research over, say, fifty years.

But here at the FTC, the story is a whole lot different, and that's part of what makes the job so exciting. Every issue that comes across my desk is policy relevant *today*. It's clear that the decisions ultimately made by the Commission are actually going to affect competition and consumer welfare.

**ANTITRUST SOURCE:** How has your academic research informed your work at the FTC?

**BAYE:** My research in oligopoly and game theory, as well as my knowledge of competitive and online markets, has been very helpful to me in a number of merger cases. For instance, in our review of the Google-DoubleClick merger,<sup>1</sup> we considered a number of horizontal and vertical theories of potential competitive effects. My academic thinking shaped how I approached this and other cases.

**ANTITRUST SOURCE:** Can you provide a little more detail on how your academic thinking came into play in that transaction?

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<sup>1</sup> The FTC's announcement closing their investigation of the Google/DoubleClick transaction is available at <http://www.ftc.gov/opa/2007/12/googledc.shtm>.

**BAYE:** I know from my own academic work in oligopoly, game theory, and online markets that there are a lot of different theories that might be relevant in any given merger case in the Internet arena—each with different implications for competitive effects—but it is critically important to carefully examine the assumptions underlying these competing theories against the underlying facts. Only by carefully examining the facts against alternative theories can one determine whether a given merger is likely to have competitive effects.

In Google/DoubleClick, we did just that. We considered a number of theories of potential competitive harm, including ones advanced by competitors, and tested them against the facts. My knowledge of game theory and online markets helped me test relevant theories against the facts.

**ANTITRUST SOURCE:** Before coming to the FTC, had you been involved in any consulting work?

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**BAYE:** My primary focus has been academic research, but I've done some consulting over the years, including several cases for the Antitrust Division at the U.S. Department of Justice. I've also served as an expert in private litigation. But I am primarily an academic and am not hooked up with a consulting shop.

**ANTITRUST SOURCE:** One thing that our readers may find useful is a summary of your responsibilities as the Director of the Bureau of Economics and how you see your role in that position.

**BAYE:** That's a great question. I suspect different Directors come in with different perceptions about the job. The thing that I find really exciting is that there are so many different facets to the job that it makes each new day different than the previous day.

One of my responsibilities is serving as the chief economist, where I advise Chairman Majoras and other Commissioners on matters and work with my deputies and staff in the Bureau of Economics (BE) to ensure that the Commission has the best possible economic analysis when it makes its decisions. Paul Pautler and Mark Frankena, who are my deputy directors for consumer protection and antitrust, have been a godsend and have enabled me to get out of the blocks running.

I also have managerial responsibilities, and a big priority of mine in this regard has been to foster an environment within BE that encourages and promotes policy-relevant economic research. This is essential to ensure that the Bureau of Economics is in the best position possible to provide relevant economic analysis to the Commission both now and in the future. Pauline Ippolito, who serves as my deputy director for R&D and operations, and Elizabeth Callison, who serves as a senior advisor, have both provided immeasurable support and advice on these and other matters.

I am also a spokesman of sorts for the Bureau of Economics, and in that capacity travel domestically and abroad to represent the Bureau at conferences and to present papers and speeches. I also help organize conferences and workshops at the FTC. For instance, I worked with Andrew Heimert from the Bureau of Competition to organize a panel at the FTC's unilateral effects workshop on February 12 on the virtues and limitations of econometric versus other approaches for developing economic evidence. I will also be moderating that panel.

Finally, we are in the early stages of planning an industrial organization conference on competition issues for fall 2008 that I hope will become an annual event. The plan is to bring in academic economists to present and discuss research papers on topics of interest to the Commission and thus to help advance our economic understanding of important issues that are arising in our work.

**ANTITRUST SOURCE:** In the time you have been at the FTC, has anything surprised you or has it been as you expected?

**BAYE:** I've been pleasantly surprised by the level of interaction that I have with staff. I was a little concerned originally about the geography of the Bureau of Economics. At headquarters, we have just a handful of economists—basically just me and my deputies. All of our other managers and Bureau staff are housed at our New Jersey Avenue office. But this concern hasn't proven to be a problem, and I've enjoyed the interaction.

It's also been interesting to see the sorts of checks and balances that exist within the agency. For example, when the Bureau of Economics sends up a recommendation on a matter, it includes a recommendation from the BE staff who worked on the case, as well as my own recommendation. The Bureau of Competition (BC) sends up their own recommendations, which includes a recommendation from BC staff and a recommendation from BC management.

These recommendations ultimately go up to the Commissioners, who also receive input from their own attorney-advisors before they ultimately vote. So, it's been very interesting to see how the organization actually works. A lot of inputs go into decisions at the FTC.

**ANTITRUST SOURCE:** Are there any similarities or differences you see in your style compared to that of previous Directors?

**BAYE:** I'm probably not the best person to answer this question, but I'm willing to give it a shot. I am primarily an academic, which probably makes my style closer to that of past academic Directors dating back to Jeremy Bulow than, for instance, David Scheffman, who came from a strong consulting background. But frankly, the organization is set up to function even without someone like me because of the quality and expertise of the deputies who are in place.

**ANTITRUST SOURCE:** How does the Bureau of Economics interact with the Bureau of Consumer Protection?

**BAYE:** The Bureau works very closely with Lydia Parnes, the Director of the Bureau of Consumer Protection (BCP), and her staff. Lydia's Bureau deals with an inordinate number of cases and we have a relatively small group of economists who work on consumer protection issues. Our staff assists attorneys in BCP by evaluating the economic issues in consumer protection matters.

**ANTITRUST SOURCE:** Are there economists who work within the Bureau of Consumer Protection or are all the economists within the Bureau of Economics?

**BAYE:** No, all consumer protection economists are within the Bureau of Economics. That's a very important feature of the institutional structure here at the FTC, and is one of the many checks and balances that ensures that the Chairman and other Commissioners have the best possible economic analysis available when they make their decisions.

**ANTITRUST SOURCE:** Since you've been at the FTC, has your work focused more on antitrust or more on consumer protection?

**BAYE:** I think it's been fairly balanced. A large amount of my time has been spent on Presidential

and Congressional inquiries into gasoline pricing anomalies. I spent the first month or so when I arrived focusing on the FTC's Report on the Spring/Summer 2006 Nationwide Gasoline Price Increases,<sup>2</sup> and since then on a number of ongoing investigations. Our extensive Google-DoubleClick investigation was time consuming. These sorts of antitrust issues have been interesting, but I anticipated these demands on my time.

I've been pleasantly surprised with the number of interesting issues that have arisen on the consumer protection side. It has been an area that I have really enjoyed and have learned a lot about during my short tenure here.

**ANTITRUST SOURCE:** Can you give us some highlights of the interesting issues on the consumer protection side?

**BAYE:** Sure. One of the more interesting projects from an economic point of view was our FACTA credit scoring study,<sup>3</sup> which was released shortly after my arrival. This study was done at the request of Congress and examined the effects of credit scoring on auto insurance risk ratings and on the prices of insurance for various ethnic and racial groups. We have also been doing important and interesting work on mortgage disclosures, privacy issues, and consumer fraud.

**ANTITRUST SOURCE:** What has been your focus on the antitrust side?

**BAYE:** As I mentioned earlier, our work on oil and gas has been a big focus. So has our work related to the health care sector, including hospitals and pharmaceuticals. I have tried to focus on those areas or aspects of cases where my own expertise has the greatest potential for adding value. We've got a portfolio of things that we're in the midst of right now. Obviously, the Google-DoubleClick investigation was very time consuming. We did a very thorough investigation.

**ANTITRUST SOURCE:** There are a number of publications that come out of the Bureau of Economics. For example, in the last issue of The Antitrust Source there was a review of a paper by Malcolm Coate on barriers to entry that relied on some data internal to the FTC. How does the data used in these types of publications become available to someone outside the FTC who would be interested in learning more? Is the data available on the FTC Web site?

**BAYE:** Now that's a very good question. For published academic studies, the data we rely on is often based on data that was not obtained during the course of an investigation. For example, some of our retrospectives in oil and gas mergers involve data that we purchased from third parties like OPIS, and interested individuals can contact the parties directly with their data requests.

Some of the data in our official FTC reports—our FACTA study for example—and other papers rely on data that we are not in a position to share with others.

My advice to academics or anyone else who might be interested in obtaining data used in one of our studies is to contact David Schmidt in our Office of Applied Research and Outreach. Dave can put the person in contact with the people who know whether or not the particular data is available for their use.

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<sup>2</sup> The report is available at <http://www.ftc.gov/reports/gasprices06/P040101Gas06increase.pdf>.

<sup>3</sup> The report is available at [http://www.ftc.gov/os/2007/07/P044804FACTA\\_Report\\_Credit-Based\\_Insurance\\_Scores.pdf](http://www.ftc.gov/os/2007/07/P044804FACTA_Report_Credit-Based_Insurance_Scores.pdf).

**ANTITRUST SOURCE:** Thinking about some of the working papers put out by FTC economists, are these articles a good reflection of the Bureau of Economics' thinking on mergers and other antitrust issues?

**BAYE:** There are five Commissioners and they're the ones who have the authority to determine official positions of the agency. So, for example, the BE working papers and working papers that staff economists might publish in academic journals or disseminate through other academic venues like the Social Science Research Network and so forth are the views of those individual economists and do not necessarily reflect the views of the FTC or the individual commissioners.

*But not all cases are amenable to economic analysis. I think it's extremely important to make sure that the underlying theory that one is using for a case lines up with the facts.*

**ANTITRUST SOURCE:** I want to switch gears a little bit now and talk about horizontal mergers. In one of your first speeches, you talked about the importance of fact-based merger analysis. For the mergers that you've reviewed thus far, have those transactions confirmed or revised your views about the importance of a fact-based analysis?

**BAYE:** I haven't changed my opinion at all. There are a plethora of economic theories which, in the abstract, might predict that a merger does or does not have anticompetitive effects, but the assumptions underlying many of these theories will be inconsistent with the facts. Facts are an essential input in merger analysis because they permit an economist to identify and refine the relevant theory of the case. The theory and facts, in turn, have implications which sometimes may be examined econometrically, provided appropriate data are available. But not all cases are amenable to econometric analysis. I think it's extremely important to make sure that the underlying theory that one is using for a case lines up with the facts.

And I think this is particularly important in this modern era of industrial organization, where one of the important tools that we use to analyze potential competitive effects is game theory. Anyone who's familiar with game theory will tell you that a lot of different things are possible in a game theoretic model. The important thing is to determine whether any of these things are likely or probable.

The classic example that I use with my Ph.D. students is the different predictions between the Cournot and Bertrand models of oligopoly. The only difference in these models is that, in the Cournot model firms are making quantity decisions and in the Bertrand model firms are making pricing decisions. This minor difference in the behavior of firms can have profound implications for such things as a merger. You need to know facts—in this case whether firms are making price or output decisions—to properly analyze the competitive effects.

That's a very simple example, but it illustrates why I think it's extremely important to test theories that one might use in a case against the relevant facts in that case.

**ANTITRUST SOURCE:** In addition to whether firms are setting prices or setting quantities, are there other key facts that you tend to look for when you go in and evaluate a merger?

**BAYE:** Certainly, there is a whole litany of things—in horizontal mergers, the ability of a firm to increase prices postmerger can depend on customer switching costs, transportation costs, commitment, potential entry, and so on. There are also facts that are relevant for coordinated effects—such as repeated interaction, the underlying transparency of prices, the transparency of decisions, and the ability of firms to monitor and react to the behavior of rival firms.

So, most often the factors that economic theory indicates could be important in a particular case are things that one can test with the underlying facts. These facts are obtained through dis-

covery and investigation to help hone in to determine whether there is a reasonable basis for anticipating potential competitive effects.

**ANTITRUST SOURCE:** Have you come across any situations in which the FTC sees one set of facts and the merging parties see a different set of facts? And if so, how do you, as the Director, resolve that apparent conflict?

**BAYE:** Conflicts over some facts are probably inevitable in any discussion. Some of these conflicts arise because of informational asymmetries. For example, we may be privy to information from third parties that we are not at liberty to disclose during the course of an investigation. This may color how we interpret facts relative to the parties.

Obviously, we try to make sure that any differences are not based on misperceptions about the economic landscape.

**ANTITRUST SOURCE:** For those who are practitioners in this area, both lawyers and economists, what advice do you have on how the merging parties can bolster their credibility or the relevance of the facts that they're bringing to bear when they come in to a meeting with FTC economists present?

**BAYE:** It is important to have as open a discussion of the facts as possible, and to confront the underlying problems directly. For example, if the issue is whether a merger is likely to have significant anticompetitive effects, it's important to be up front with the types of data the parties have to answer that question. I think a lot of people's gut reaction is that there is some inherent value to being secretive, and in my opinion that's just a losing strategy all the way around.

Ultimately, it's better to disclose relevant information before one reaches the litigation stage because we are more likely to be able to amicably resolve a potential concern than by trying to save information as some sort of secret bullet you're going to shoot in litigation.

**ANTITRUST SOURCE:** Let's talk about econometric evidence. What do you do in situations when a transaction or the available data in a transaction does not lend itself to an econometric analysis? How do you identify that situation? And what role does the Bureau of Economics play in that situation?

**BAYE:** BE's role is the same regardless of whether data is available for econometric analysis. My view is that econometric analysis is just one potential piece of evidence that you might use in a merger case. In fact, I would argue that in an ideal setting, econometric analysis or econometric evidence is just icing on the cake.

Pound cakes don't have icing, and you don't have to have icing on every cake. But some people mistakenly try to force an econometric analysis out of inappropriate data because they do not recognize that not all cases or questions can be appropriately addressed with econometric techniques.

In any event, econometrics is not a substitute for the facts of the case. Facts are necessary to provide texture and context, thereby turning an otherwise abstract economic theory into a relevant story. How well the facts fit the theory can be used as a qualitative test of the theory's relevance to the merger. If the facts of a case are not consistent with the underlying story, econometrics is likely to be of little value in understanding the potential competitive effects of a merger.

So, while econometrics is not a substitute for theory and facts, theory and facts can often be used together as a sort of "test" of potential competitive effects. A number of additional tools and

types of information, including merger simulations, advertisements, strategic plans, customer reports, testimony and depositions of customers, and a host of other types of quantitative and/or qualitative data can be useful.

These additional tools can be useful regardless of whether it is possible to put that icing on the cake. For instance, in the Staples-Office Depot case some very sophisticated econometrics work was done to identify the competitive effects of a merger between Staples and Office Depot. But ultimately even absent that sophisticated evidence, there was evidence from advertisements that suggested that there were price differentials depending on whether the parties were competing head to head or not. The icing on the cake helped demonstrate that the price differentials in the ads weren't the result of spurious correlations. But at the end of the day, those advertisements might have been useful on their own.

*One thing I'm always looking for in econometric analysis is the robustness of the results. It's not difficult for any first year graduate student to sit in front of a computer and run a gazillion regressions until he or she ultimately finds some relationship in the data.*

**ANTITRUST SOURCE:** Are you able to identify those situations that aren't likely to lend themselves to econometric evidence pretty early on such that you can then scale back the data-intensive questions that typically accompany a second request?

**BAYE:** If one wants to identify competitive effects econometrically, one has to have some price variation to be able to do that. If we learn early on that it is not possible to obtain price data that's going to allow us to identify differences across markets or time, we wouldn't normally require that the data be delivered.

We work closely with our attorneys in BC to minimize the burdens that are associated with second requests. Open and honest communication is essential for this to work.

**ANTITRUST SOURCE:** In situations that do lend themselves to econometric work, what is your view on the Bureau of Economics staff sharing their econometric work with the merging parties?

**BAYE:** Sometimes it is not feasible to share data because of the reliance on data from third parties and other data that might be available. To the extent that we're able to discuss results and specifications without compromising the underlying confidentiality of data, we do.

To the extent possible, we strive to have a useful dialogue and to share as much information as is possible with parties.

**ANTITRUST SOURCE:** In those cases, are you able to share the structure of what the econometric model looks like or the type of data being used even if you can't turn over the exact data that's involved?

**BAYE:** Yes, and it is a two-way street. It is important for both sides to understand the types of controls that are being used in econometric work. It's also important to understand how the data is being manipulated and constructed.

I think we've had good working relationships with parties since the time I've been here on those cases that have involved econometric issues.

**ANTITRUST SOURCE:** Are there certain types of econometric analysis that you find to be particularly credible or particularly helpful in your analysis?

**BAYE:** One thing I'm always looking for in econometric analysis is the robustness of the results. It's

not difficult for any first year graduate student to sit in front of a computer and run a gazillion regressions until he or she ultimately finds some relationship in the data. What's important to me is whether or not those econometric specifications are based on a sound theoretical model that is consistent with the specifications that are being run. That's very important. And equally important is that the econometric results are robust to alternative specifications or controls.

**ANTITRUST SOURCE:** In the Whole Foods-Wild Oats transaction, the FTC recently filed an appellant brief appealing the district court's denial of the FTC's motion for a preliminary injunction. Can you describe generally the role that the Bureau of Economics plays in deciding whether it makes sense to file a motion like that?

**BAYE:** I'll speak generally, since this case is still in appeal.

It is important to realize that, in any merger case, the Bureau of Economics provides input at every stage of the process—from the time when an HSR filing comes in, the second request, decision to ultimately either close the investigation, or when the Commission votes to file a preliminary injunction. At every stage, the Bureau of Economic is involved, as is the Bureau of Competition.

And at each stage of that process we work closely with the Bureau of Competition. We might recommend changes in the Second Request, changes in complaints or appeals or whatever. But ultimately, anything we do—as with the Bureau of Competition—is a recommendation to the Chairman and the Commissioners. I'm the Director of the Bureau of Economics, but I don't have a vote on the Commission. Jeff Schmidt is the Director of Bureau of Competition, but he doesn't have a vote on the Commission. So, our roles are advisory and our goals are to provide the Commissioners with the information they need to make the best possible decisions.

**ANTITRUST SOURCE:** What was the Bureau of Economics' role in the Equitable Resources-Dominion transaction?

**BAYE:** We helped sort out two interesting and important issues, namely the impact of competition in a regulatory environment and potential efficiencies from the merger.

Both Equitable and Dominion are involved in various energy businesses, but a key part of the transaction involved competitive overlaps in the distribution of natural gas to industrial and commercial customers in certain areas of Pennsylvania. Competition in the interstate transmission of natural gas from producing regions to local distribution companies is common, but competition between local distribution companies, such as Equitable and Dominion, which own the pipelines that distribute gas directly to consumers, is extremely rare.

As a footnote, this unique form of competition in the area started about one hundred years ago when a number of natural gas pipeline companies started competing to deliver natural gas from producing regions in the Allegheny Mountains to the steel mills around Pittsburgh. This generated an overlapping distribution network.

In any event, competition between Dominion and Equitable results in substantial discounts from regulated rates for commercial and industrial customers that are served by more than one local distribution company, while "captive" consumers who do not enjoy such competition are charged regulated rates. So, one of our contributions was showing that there were competitive effects even though prices were regulated. And we obviously evaluated efficiency claims made by the parties in the distribution of natural gas.

Based on this work, the FTC filed a complaint and motions for a Preliminary Injunction to block the merger because customers receiving discounts from regulated rates would likely pay higher rates, postmerger.

The district court granted the parties' motion to dismiss the complaint on state action grounds rather than the economic merits. As you know, the FTC appealed this decision, and recently the parties abandoned the transaction while waiting for the court of appeals decision on the state action issue.

**ANTITRUST SOURCE:** To the extent that you know, was the Equitable Resources-Dominion transaction one in which econometric evidence was important to the Bureau of Economics or was this one that fell into the category of primarily relying on non-econometric evidence?

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conduct.*

**BAYE:** We primarily relied on non-econometric evidence. As I mentioned earlier, there are a variety of other forms of economic evidence, including quantitative evidence, and not all cases lend themselves to, or even require, econometric analysis.

**ANTITRUST SOURCE:** Let's shift gears again. What are some of the things that you learned, or are hoping to learn, from the single-firm conduct hearings?

**BAYE:** I was not here when the hearings took place, but I have been involved in the report that we're working on jointly with the Department of Justice and have reviewed the transcripts. So I am fairly familiar with a number of the issues.

To me, the hearings highlighted the many challenges we face in attempting to prevent unilateral anticompetitive abuses of market power without discouraging procompetitive conduct. Section 2 can stifle firms' incentives to engage in procompetitive conduct because they are afraid of being sued for an abuse of market power. For instance, a firm might be afraid to offer consumers discounts on bundles due to concerns that it might be sued for predatory behavior. While "safe harbors" can mitigate uncertainty and alleviate some of these fears, it is a very difficult challenge to come up with economically sound "tests" that thwart anticompetitive behavior without stifling competition.

The big takeaway for me is that there is tremendous scope for scientific research on these issues.

**ANTITRUST SOURCE:** Do you have an estimate of when that report will be made publicly available?

**BAYE:** My record at forecasting how long it takes to get reports out of the Commission is not particularly good. I will say that we're currently working on this with the Department of Justice and I'm hopeful that it will be out in the not too distant future. But I certainly don't want to go on record giving you a date because it will almost certainly be wrong.

**ANTITRUST SOURCE:** I'd like to ask you about the gas price investigations. Since a report came out in August, from the public point of view, it looks like it has been pretty quiet compared to a year or two ago. You mentioned earlier on that there is quite a bit of activity going on. Can you describe the work that is ongoing?

**BAYE:** Sure. This is a very important area for us here at the FTC, and BE staff contribute in a number of ways.

In the case of proposed petroleum mergers, staff conduct thorough analyses of potential competitive effects and efficiencies, evaluate proposed divestitures, and if the case is litigated, provide an array of support services for our attorneys. This support includes assisting our attorneys in deposition preparation, evaluation of expert reports, and the like.

But much of our work in this area does not involve mergers and is ongoing daily. BE staff monitor gasoline prices in about 360 areas across the country using an econometric model that identifies “anomalies” in gasoline prices. When pricing anomalies are detected, BE staff work closely with attorneys in BC to investigate the potential causes for the anomalies.

**ANTITRUST SOURCE:** Do you have a full-time staff of economists working on these investigations?

**BAYE:** We have a group of economists whose main focus is in the petroleum area. They do the monitoring project but also work on other matters, including Congressional requests for investigations of pricing issues in specific markets.

**ANTITRUST SOURCE:** Are there additional gas price reports that we can look forward to in the future?

**BAYE:** Most of the gas price reports that we produced in the past few years have been either requested by the President or by Congress and I can't predict whether or not they're going to ask us to do another report along those lines. With respect to internally generated reports, our Office of Applied Research and Outreach is in the very early stages of an R&D project that I'm hopeful will provide some value to us in our oil and gas areas.

Dave Schmidt, who is the Assistant Director of the Office of Applied Research and Outreach here in the Bureau of Economics, is heading up a new project to determine whether recent advances in the academic literature on dynamic oligopoly might be useful in our analysis of pharmaceutical, retail, and petroleum markets. I want to stress that this research is in the very early R&D stage, but I am hopeful that it might ultimately permit us to further enhance our gasoline price monitoring efforts.

**ANTITRUST SOURCE:** Let's talk about consumer protection for a moment. What are some of the recent issues that the Bureau of Economics has been actively involved?

**BAYE:** Economists in our consumer protection shop have considerable expertise in understanding the effects of disclosures in general, and mortgage disclosures in particular. We've got a great team in Jim Lacko and Jan Pappalardo. They recently released a study showing that a lot of consumers don't really understand what they're signing when they sign the mortgage papers.

**ANTITRUST SOURCE:** Is this related to subprime lending issues?

**BAYE:** Subprime lending is an important issue that has ramifications for the safety and soundness of our banking system—an issue that obviously falls under the Fed's oversight. But there is one particular facet of subprime lending where I believe the FTC can play a potentially important role. Jim and Jan found that both prime and subprime borrowers failed to understand key loan terms in current disclosures, and that improved disclosures benefited both types of borrowers. Further, they found that improved disclosures provided the greatest benefit for more complex loans, where both prime and subprime borrowers had the most difficulty understanding loan terms.

So, to the extent that loans in the subprime market tend to have more complex features than loans in the prime market, or if subprime borrowers are in a weaker position to “adjust” to changes in payments they did not anticipate due to their failure to understand the terms of their mortgages, one part of the solution to subprime issues could be improved mortgage disclosures.

Economists in the Bureau of Economics are currently working with others at the FTC to look for ways to improve current mortgage disclosures. We are also in conversations with the Federal Reserve and with HUD on these issues.

**ANTITRUST SOURCE:** Are there other issues you’ve been out in front with on consumer protection?

**BAYE:** In addition to our FACTA scoring studies and mortgage disclosures, we are also involved in work on carbon offsets. As you know, we had a workshop awhile back on that and I think there are some potentially interesting roles for economists there.

**ANTITRUST SOURCE:** What type of role do you see for economists in looking at carbon offsets?

**BAYE:** There’s evidence that some consumers make choices based on their perceptions of a company’s environmental record on carbon offsets. I believe a useful first step is for economists to help us gain a better understanding of what consumers take away from the various claims being made—that is, measuring consumer perceptions about carbon offset claims.

Economists in the Bureau of Economics have a lot of experience in evaluating consumer perceptions in areas that include mortgages, health claims, and advertising. Building on what we have learned in these areas, and our expertise in the scientific method and statistical analysis, another potential role of BE economists is to evaluate the scientific evidence that underlies the substantiation of carbon offset claims.

I think it’s a really fascinating area and that there is a lot of important economic work to be done in this area.

**ANTITRUST SOURCE:** You mentioned earlier that you have done some traveling, including international travel. How much interaction do you have with your European counterparts?

**BAYE:** I’m really fortunate that the FTC has an Office for International Affairs that’s headed up by Randy Tritell. Randy’s office has done a great job helping me forge working relationships with our non-U.S. counterparts. For instance, in October I participated in the U.S.-European Commission Competition Consultations, and also met privately with Damien Neven—the EU’s Chief Competition economist—to discuss a variety of matters. Good relations with all of our international counterparts are important in helping us fulfill our missions.

**ANTITRUST SOURCE:** Do you find that the economic frameworks used in the EU or the other areas where you interact similar to the frameworks that you and your staff in the Bureau of Economics use to evaluate antitrust issues?

**BAYE:** So far I have. One thing nice about dealing with economists is that we have a common language. We read the same textbooks, we publish in the same journals, and we read the same journal articles.

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I think it's a bit different for lawyers because legal frameworks differ across countries. I think a lot of the differences that we have with Europeans, for instance, don't so much stem from differences in the economics, but from differences in the legal frameworks and standards of proof.

**ANTITRUST SOURCE:** When you're interacting in this international context, how closely do you coordinate with the Department of Justice or with other federal agencies or state agencies?

**BAYE:** Very closely. For instance, Dennis Carlton also participated in our EU Consultations. Prior to his departure last week, Dennis served as my counterpart at the Department of Justice, where he was the Deputy Assistant Attorney General for Economic Analysis in the Antitrust Division.

**ANTITRUST SOURCE:** We really appreciate your taking the time today to talk with us. Thank you very much.

**BAYE:** Thanks so much for giving me this opportunity. It's been a pleasure chatting with you. ●