Reply to Coleman and Simons

Warren S. Grimes

Mary Coleman and Joseph Simons have written a spirited response to John Kwoka's and my article on the FTC's decision to close its investigation of the cruise mergers.[1] This exchange could not have occurred without the published opinions of the three member Commission majority and the two dissenting commissioners. In our article, we lauded the FTC's efforts to provide transparency to a decision to close an investigation. Full transparency to any agency decision is unattainable and probably undesirable.[2] It may well be, however, that the debate reflected in this exchange might have been narrowed and refined with fuller disclosure.

I address here, as Coleman and Simons do in their response, the role of the Merger Guidelines' presumption of anticompetitive effects that attaches when a merger would substantially increase concentration in an already concentrated industry. We indicated, and Coleman and Simons agree, that the presumption is rebuttable. Our difference of view appears to center on how the presumption operates or, indeed, whether it operates at all.[3]

Our view is that the presumption operates only when the staff or opponents of a merger offer a credible theory of anticompetitive effects that is consistent with available evidence. This approach reflects the practice at the antitrust agencies well before the Muris Commission. We also believe, however, that once a credible theory has been presented, the burden should be on the proponents of the merger to explain why anticompetitive effects are unlikely. As the premerger HHI level and postmerger increase in HHI become larger, the burden on proponents of the merger should be heavier.

The Commission majority, after conceding that the presumption was "interest-provoking," appeared to ignore it, placing the burden of persuasion on merger opponents to provide evidence of likely anticompetitive effects. In their response, Coleman and Simons assert that the merging parties met their burden of rebutting the presumption by providing "extensive data and other information." Of course, effective rebuttal is measured by relevant and persuasive evidence, not by its sheer volume. In the face of genuine concern about specific anticompetitive effects, Coleman and Simons track the Commission majority in responding with sweeping pronouncements about indus-

■

***Warren Grimes** is Professor, Southwestern University School of Law.*

[1] Warren Grimes & John Kwoka, *A Study in Merger Enforcement Transparency: The FTC's Ocean Cruise Decision and the Presumption Governing High Concentration Mergers*, ANTITRUST SOURCE, May 2003, *available at* http://www.abanet.org/antitrust/source/may03/metstudy.pdf.

[2] For more expansive treatment of the transparency issue as it applies to merger enforcement, see Warren S. Grimes, *Transparency in Federal Antitrust Enforcement*, 51 BUFFALO L. REV. 937 (2003), and the responsive comments from Robert Pitosfsky, Peter C. Carstensen, and John M. Nannes.

[3] Coleman and Simons suggest that our article grew out of a desire to reargue positions that the American Antitrust Institute took in opposing the cruise mergers (both of us were members of a Committee that developed the AAI's position). Our earlier involvement in the case was fully disclosed and should be no more disqualifying than Coleman's and Simons' understandable interest in defending positions that they may have advocated before the divided Commission. Neither we, nor they, had any financial interest in the outcome of the case.

try conditions and arguments that there was insufficient evidence or analysis in support of the concerns. This approach appears to give little, if any, weight to the presumption.

In justifying the closure of the investigation, Coleman and Simons find comfort in the Pitofsky Commission's closure without challenge of at least seven merger investigations despite asserted comparable or higher concentration and concentration increase levels. With the virtual complete lack of transparency that accompanied such closures in the past, little can be said about their relevance as precedents. As the Commission majority itself said in its Cruise Merger statement, merger enforcement is case specific.

Should the burden be on opponents of a high concentration merger to demonstrate with specific evidence that the merger is likely to produce anticompetitive effects? We find this view troubling because it ignores venerable economic learning and theory that underlies *Philadelphia National Bank*[4] and four iterations of horizontal merger guidelines. Even when the risk of anticompetitive effects is at its highest, the burden would be placed on the Commission and its staff, or on outside opponents of the merger, to produce information (which only the merging parties may possess) to demonstrate in conclusive fashion that anticompetitive effects are likely.

Given our view of how the presumption should operate, our point is not that the Commission majority's decision was incorrect. Rather, it is our view that credible theories of anticompetitive conduct were not adequately addressed or refuted in the Commission majority's statement. We could not know then, and do not know now, the full extent of the evidence available to the Commission and its staff. Of course, the Commission itself may have failed to gather critical evidence if, in conducting the investigation, it gave insufficient weight to a credible theory of anticompetitive effects. The burden, however, should be on the parties to the merger who are most likely able to provide dispositive evidence in the face of structural circumstances that suggest a high risk of anticompetitive effects.

Both the Commission majority, and Coleman and Simons in their response, give weight to aggregate analysis of overall conditions in the cruise line industry.[5] For example, they stress the "high demand elasticities" that exist in cruise lines, a condition that might appear to lessen the risk of anticompetitive effects. But this aggregate analysis says nothing about whether conditions of high demand exist in this industry. That such high demand conditions do exist is a given because, as described below, the yield management systems that cruise lines employ are specifically designed to take advantage of high demand conditions. Shouldn't the Commission have examined sample niche markets or areas of overlap to determine whether anticompetitive effects were possible? Had they ruled out such effects in areas in which the potential for rent seeking was highest, they could have comfortably and convincingly closed this investigation.

In rejecting both unilateral effects theories and coordinated effects theories, we criticized what appeared to be the Commission's decision to highlight overlap (in rejecting unilateral effects theories) but then highlight the lack of overlap (in rejecting coordinated effects theories). Hence, our view that the Commission was engaging in Goldilocks economics: seeking elusive middle ground

---

[4] United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963).

[5] This criticism is not based on the lack of detailed data provided to the Commission (see Coleman & Simons, n.5), but on the way in which the Commission majority and Coleman and Simons employ this data to draw sweeping conclusions about industry conditions (high demand elasticity, low critical loss, and complexity in pricing) as a basis for dismissing any and all potential anticompetitive effects. Some of these industry conditions, such as pricing complexity, are inapplicable or less applicable to certain anticompetitive effects (e.g., coordination in the pricing of on-board amenities). Why didn't the Commission majority use the wealth of individual data to address these special areas of concern?

("not too hot, hot too cold, just the right temperature") in its treatment of these issues. We stand by this criticism. For example, Coleman and Simon stress "the complexity revealed by actual transaction prices" and the lack of cruise line offerings that are "uniquely close substitutes." These conclusions—apparently based on aggregate data analysis—might make coordinated effects less likely but would appear to make unilateral effects more likely.

With respect to coordinated effects, Simons and Coleman say that we offer "little by way of countervailing analysis" beyond our reliance on the presumption that large mergers in concentrated industries are suspect. Our view is that the presumption should be particularly forceful in the area of coordinated effects. Merger policy is prophylactic, and offers federal agencies a "last chance" to thwart an industry structure that would be conducive to oligopolistic rent seeking. Tacit parallel conduct among oligopolists is just as harmful to consumers and competition as cartel conduct, probably cannot be reached by the Sherman Act, and should be addressed in a careful prophylactic merger review.[6]

With respect to computerized yield management programs, we challenged the Commission majority's supposition that the complexity in pricing reflected by these programs meant that coordination was less likely. Coleman and Simons claim that these programs led to "substantial nonsystematic, unpredictable, and largely unobservable variation in prices, precluding effective price coordination." The conclusion, again apparently based on aggregate analysis, seems transparently overdrawn. The computer programs that are used to adjust prices have the same purpose for all firms in this industry. For example, yield management programs would vary price based on how full the ship is and how near the date of sailing is. In conditions of high demand, the response of the yield management program is anything but nonsystematic and unpredictable: prices will go up, and rival firms might well seek to set comparable prices for particular trips that closely parallel one another. That parallel sailings may be rare is a valid point, but cruise lines will also know that high demand exists at certain seasonal points and that many customers will look at alternative destinations, giving the firms an opportunity to set prices in tacit coordination during such high demand periods. The use of sophisticated yield management programs should make such targeted tacit coordination easier, not more difficult.[7]

Coleman and Simons chide us for describing yield management as a "sophisticated tool of price discrimination" that may allow the setting of prices above competitive levels. That there is sophisticated price discrimination in the sale of cruises, hotel rooms, and air travel is beyond dispute. But Coleman and Simons apparently believe that the ubiquity of these practices demonstrates that they are consistent with competition.[8] The issue faced by the Commission, however, is not the lawfulness of price discrimination in general or in its particular application in cruise lines, but whether to proscribe a merger that, by increasing the likelihood of coordinated practices, might enhance the discrimination and produce higher prices for cruise passengers.

---

[6] Coleman and Simons offer no response to our point that coordination of the availability of amenities becomes more likely in a more concentrated industry. With fewer rivals, it becomes easier for firms to tacitly follow a practice of refusing to pay refunds or forcing passengers to pay extra for on-board amenities. The issue is consequential—we cited an industry expert who indicated that on-board charges generate up to one-fifth of the cruise lines' total revenues.

[7] Yield management programs have not been a bar to tacit parallel pricing among airlines, and appear to facilitate such conduct.

[8] We join Coleman and Simons in commending the Symposium on Competitive Price Discrimination, 70 ANTITRUST L.J. 593 (2003). The Symposium presents a variety of views on price discrimination, but surprisingly, none of the participants even mentioned the wealth transfer loss to consumers caused by price discrimination. This omission is substantial since the avoidance of wealth transfer loss is embraced by many scholars as a central goal of antitrust law. For that perspective, see LAWRENCE A. SULLIVAN & WARREN S. GRIMES, THE LAW OF ANTITRUST: AN INTEGRATED HANDBOOK § 2.5 (2000).

Finally, Coleman and Simons challenge our concern that the cruise mergers might enhance opportunities for anticompetitive strategic conduct. Here again, our point is not to finally decide whether the likelihood of strategic conduct was or was not enhanced by the merger, but merely to observe that serious concerns along this line, raised in the dissenting opinion, were not addressed by the Commission majority. That powerful market players may engage in strategic conduct to raise rivals' costs is hardly a novel theory. As we pointed out, it is well grounded in the literature and recognized in the jurisprudence of the Commission (in cases such as *Time Warner*).

Coleman and Simons response is to suggest that conduct, such as making favorable or exclusive agreements with travel agents or influencing regulators to limit rival's access to land facilities, is unlikely to be anticompetitive and may well be procompetitive. Readers should judge for themselves whether this conclusory statement is persuasive in light of the substantial theoretical literature and case law addressing conduct to raise rivals' costs. Coleman and Simons also argue, however, that "there was no credible evidence that either merger enhanced the risk of any sort of 'strategic conduct.'" This statement highlights the striking difference between our application of, and their apparent disregard for, the presumption against large mergers in highly concentrated industries. We believe that, once a credible theory of anticompetitive effects has been advanced, the presumption operates to place the burden of proof on proponents of the merger. Coleman and Simons apparently embrace a view that the presumption has no effect: the burden remains on opponents of the merger to come up with evidence that the merger will have anticompetitive effects. The disregard of the presumption is apparently of less concern because, the response suggests, should anticompetitive effects occur, they "could be challenged later separate and apart from the merger." This last point suggests a de-emphasis on the prophylactic role of merger enforcement and a confidence in the ability of antitrust enforcers to ferret out and prosecute post merger abuses. If this confidence is well-placed, perhaps we no longer need a merger enforcement policy. ●