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RICHARD STEUER: We have with us this morning FTC Chairman Jon Leibowitz; Justice Department Antitrust Division Acting Assistant Attorney General, Sharis Pozen; the European Commission’s Competition Commissioner and Commission Vice President Joaquín Almunia; India’s Competition Commission Chairman, Ashok Chawla; and the Chair of the Multistate Antitrust Task Force of the National Association of Attorneys General and Chief of the Antitrust Section of the Office of the Attorney General of the Commonwealth of Pennsylvania, James Donahue.

Joining me this morning to ask questions are the brilliant, and presumably exhausted, Co-Chairs of our Spring Meeting, to whom we owe a tremendous round of thanks, Deb Garza and John Villafranco.

Let me begin by asking Chairman Leibowitz to say a few words.

JON LEIBOWITZ: Thank you so much, Dick. It is always a pleasure to be here, especially this year

1 Editor's Note: This Roundtable has been edited for publication.
with Sharis Pozen, who has done such a terrific job as Acting Assistant Attorney General for Antitrust; Jim, with whom we work productively all the time on hospital investigations and other health care matters; Chairman Chawla, who is growing the Indian competition agency into a real powerhouse; and of course my friend, the extraordinary Joaquín Almunia.

The lead this year from the FTC is that just last night, Maureen Ohlhausen was confirmed and we now have a full complement of Commissioners. We are all very excited about that. I can see Julie Brill, my colleague, in the front, nodding in agreement and happiness. We’re a three-woman Commission now. And we continue to be bipartisan and consensus-driven, most of the time.

Most of the people in this audience know what we have been doing over the last year or two, so I will try to keep it brief.

Health care is a major area for us. As everyone here knows, health care spending is about 18 percent of the GDP in the United States; and in European countries, where the level of care is roughly comparable, it is less than half of that, at about 8 percent of the GDP. Our spending is not sustainable. In fact, if you read the transcripts or listened to the Affordable Care Act oral arguments in the Supreme Court this week, it seemed to be one of the few things on which the Justices actually agreed.

In the last year, we have continued to pursue challenges to anticompetitive mergers and conduct in the health care industry. We have continued to work on restricting pay-for-delay pharmaceutical agreements. We appreciate the excellent work that DG-COMP has done on a parallel track there.

We currently have three hospital cases in litigation:

- There is a four-to-three merger in Toledo, Ohio. We just released that decision, which affirmed liability and divestiture of a hospital.\(^2\) The eminent and distinguished Julie Brill wrote the opinion of the Commission. We have another case in which we are waiting for a preliminary injunction decision.\(^3\) It is a three-to-two merger in Rockford, Illinois.

- And then, perhaps the most interesting case is Phoebe Putney. That is a merger to monopoly, a two-to-one merger, in Albany, Georgia, one of the poorest counties in America. The nonprofit agreed to buy the for-profit hospital and then attempted to avoid antitrust scrutiny by asserting the entire transaction was exempted by the state action doctrine. We lost in the Eleventh Circuit in a three-judge panel.\(^4\) The Solicitor General agreed with us that this case was so important that he has filed a certiorari petition with the Supreme Court.

Also on the health care front, we continue to work to restrict pay-for-delay agreements, settlements in which the branded drug companies—metaphorically at least—put a big bag of cash on the table, and the generics take it because they can earn more by sitting it out and not competing than they would by entering the marketplace. As a result, generic drugs, which are about 15 percent of the price of brand drugs, are not available to consumers. Our Bureau of Economics, led by Joe Farrell, estimates that these deals cost consumers $3.5 billion each and every year.

The Congressional Budget Office has estimated that if legislation passes restricting these

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\(^3\) Editor's Note: Subsequent to this Roundtable discussion, the U.S. District Court for the Northern District of Illinois granted a preliminary injunction enjoining the consummation of the proposed affiliation between the hospitals. See FTC v. OSF Healthcare Sys., No. 11 C 50344, 2012 U.S. Dist. LEXIS 48069 (N.D. Ill. Apr. 5, 2012).

deals, it would save the federal government $5 billion over ten years, which even in today’s world of budget deficits is still meaningful.

We have two pay-for-delay cases on appeal now. One is our appeal in the Eleventh Circuit in the AndroGel case. In the Third Circuit, we filed as an amicus in K-Dur. That decision should be coming soon. We are confident that this issue is going to be resolved in favor of consumers, either by Congress or by the courts.

On the technology front, we have a number of open investigations about which I can say very little publicly.

On the policy front, our efforts continue with projects like our work with the Department of Justice to set guidelines for accountable care organizations. Hopefully, we will have an Affordable Care Act that includes accountable care organizations; we will know that in the next couple of months.

On the consumer protection side, we continue to emphasize two areas.

One is consumer privacy. We have brought lots of privacy cases, as I am sure you know. We also released a report at the beginning of this week that called for more privacy by design, transparency, simplified choice, and a do-not-track option—not run by the government but run by companies voluntarily, that would allow consumers to opt out of having their data collected by third-party sites.

We also continue to do a lot of last-dollar fraud work.

Let me take this opportunity to make a small pitch for the FTC’s 2012 Annual Highlights. It is a new, leaner, more eco-friendly version of the annual report that you are all used to getting at the Spring Meeting. This will give you some highlights and you can link to a longer and a more detailed report about all of our activities on our Website.

MR. STEUER: Thank you.

Assistant Attorney General Pozen.

SHARIS POZEN: Thank you also, Dick. It’s a pleasure to be here, and a pleasure to be here among people that we know so well, not only in the audience but on the stage. It’s a privilege.

Someone said yesterday, “Oh, you’ve had a good year in the Antitrust Division.” I said, “No, we haven’t had a good year in the Antitrust Division. We’ve had an amazing year in the Antitrust Division.” I am happy to talk to you about that today.

There are three things I want to focus on: first, our litigation record; second, our prioritization; and then, finally, who we think are listening and watching and how we’re interacting with them.

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5 Editor’s Note: Subsequent to this Roundtable discussion, the Eleventh Circuit Court of Appeals upheld the district court’s dismissal of the FTC’s complaint under Federal Rule of Civil Procedure 12(b)(6). See FTC v. Watson Pharms., Inc., No. 10-12729, 2012 U.S. App. LEXIS 8377 (11th Cir. Apr. 25, 2012).


I’ll start with our litigation record. If anyone still has a question as to whether or not the Antitrust Division will litigate and win, that question has been answered in the affirmative. Both our criminal program and our civil program have had tremendous victories this year.

The AUO case10 is the most recent, led by our San Francisco Field Office. This is a criminal trial against AUO, which manufactures liquid crystal display screens that are used in televisions, computers, etc. We were put to a test here, and we knew it was a test. This was a significant trial in our criminal program challenging not only whether or not these companies had participated in a cartel, but whether or not we could prove before a jury beyond a reasonable doubt that in fact that cartel resulted in an overcharge.

We had guilty verdicts not only against AUO but its U.S. subsidiary and two key executives. The jury found beyond a reasonable doubt that there was in fact an overcharge of $500 million. That’s doubled to $1 billion. So I would assume that this case is resonating across boardrooms today.

Last night Senator Franken covered AT&T11. It was amazing to have a U.S. Senator stand up and say many of the things that we have said publicly about that acquisition and the benefit to consumers of attempting to block it and then it ultimately being abandoned. That was a tremendous victory for the Division.

And then, of course, H&R Block.12 One former assistant attorney general said to me, “It reads like an antitrust treatise.” It does. It’s eighty pages. I think for us and for the Federal Trade Commission what is particularly important is the use of our 2010 Horizontal Merger Guidelines13 throughout that opinion.

How did we achieve these litigation victories? It was a team effort, there is no doubt about it, and it is across the Division.

Our career staff are some of the best litigators you are going to go against. Using AT&T as an example, we faced at last count nine law firms. We were led by Joe Wayland, our Deputy Assistant Attorney General for Litigation, who is an experienced trial lawyer, who’s a member of the American College of Trial Lawyers. He brought in some help as well. He brought in Glenn Pomerantz and Dave Dinielli from Munger Tolles. That team, working with our career staff, went toe-to-toe with at least nine law firms.

We’ve also institutionalized our litigation function by hiring a director for litigation. We have a thirty-year veteran, Mark Ryan, who joined us from Mayer Brown, who has a lot of trial experience and will be a resource going forward for our litigation efforts.

Second, on prioritization, it was interesting when Jon and I met with Chairman Chawla and talked about how agencies set priorities. I can tell you our priorities in the Antitrust Division were set four years ago by the President of the United States. Barack Obama announced that if he was elected there was going to be a reinvigoration of antitrust enforcement. That is the promise he made, and that’s the promise that we believe we have kept.

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In looking at how you do that, I was thinking when talking to the Chairman that one of the first things we did out of the box three-and-a-half years ago was recognize that we were in the Antitrust Division with the backdrop of one of the most significant financial crises this country has ever faced. We decided early on that we were going to put down a marker, and that marker was going to be a hard marker, that antitrust enforcement was going to be reinvigorated and tougher than ever because it is even more important in distressed economic times to have strong antitrust enforcement to ensure that markets remain competitive. We made a mistake, I would say, after the Great Depression, when there was the thought you actually ease up on antitrust enforcement, and we have learned from that mistake.

So that was our first marker. It was a hard marker put down by Assistant Attorney General Varney and Deputy Assistant Attorney General Carl Shapiro in many speeches and public statements.

Second of all, we focused on those industries that I like to call our “pocketbook” industries. I would highlight four of those: the financial services industry, the telecommunications and technology industry, health care, and agriculture. We looked at these industries holistically. We talked to experts in them, thought about them, thought about what the competitive issues were. Our main focus was on consumers. These are the things that affect the American consumers’ budgets most significantly.

In financial services we found criminal conduct and we prosecuted in our Muni Bonds case.\(^\text{14}\) Muni bonds affect cities and counties around the United States. They are used to build public facilities. We found that there was bid rigging and cartel activity in that industry. We ended up entering into global settlements with many institutions as well as prosecuting individuals.

Also, as I said, in technology—I don’t need to talk about AT&T. There is also Google/ITA.\(^\text{15}\)

In health care we worked on concentration in health insurance markets as well as illegal agreements that we think health insurers and others had been instituting in the form of MFNs and exclusive arrangements.

And finally, in agriculture, we heard from the industry through our workshops, and that has infused our enforcement efforts.\(^\text{16}\) We’ve brought cases in fluid milk, now a criminal action; in tomatoes; also in poultry.

So finally, as I said, who’s listening and who’s watching? We knew business was listening and watching, and we wanted to ensure that there was clarity and transparency in what we were doing. So our competitive impact statements were detailed, we issued closing statements, we gave speeches, so that folks knew where we were drawing the line.

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\(^{14}\) See Antitrust Div., U.S. Dep’t of Justice, Division Update Spring 2012, Criminal Program, Municipal Bonds, http://www.justice.gov/atr/public/division-update/2012/criminal-program.html (describing an “on-going investigation into bid-rigging in the municipal bonds derivatives market” that “has so far resulted in 13 guilty pleas and pending charges against six individuals,” as well as “resolutions with large financial institutions. . . which have agreed to pay a total of $745 million in restitution, penalties and disgorgement”; with links to six settlement agreements and numerous press releases spanning period from October 2009 to January 2012).

The Antitrust Division’s ongoing criminal investigations are paralleled by the civil class action pending under the caption In re Municipal Derivatives Antitrust Litigation, MDL No. 1950 (S.D.N.Y. pretrial proceedings consolidated June 18, 2008).


\(^{16}\) See Sharis A. Pozen, Agriculture and Antitrust: Dispatches and Learning from the Workshops on Competition in Agriculture, ANTITRUST, Spring 2012, at 8.
And then, finally, our international colleagues. We wanted to work cooperatively with our international colleagues and develop new relationships with emerging economies.

I’d like to say on a personal note, as I step down at the end of April, I am so grateful for all the support that I have felt from this community. It has been remarkable. I’d also like to thank the career staff at the Division. I could not work with better colleagues. It has been an honor to serve side-by-side with you. Our front office over the three-and-a-half years and the experts that we brought in were a pleasure to work with.

And finally, I have to thank the former Assistant Attorney General Christine Varney. I wouldn’t be here but for her, coming in as her chief of staff and then being made the Acting by Attorney General Holder.

Thank you all very much. It has been an awesome year.

MR. STEUER: Thank you.

Vice President Almunia.

JOAQUÍN ALMUNIA: Good morning. Thank you very much for inviting me again for the second year in a row. I am very happy to be here in the States with colleagues and friends and honored to be in front of all these very important constituents for all competition enforcers and of course for the European Commission too.

What did we do this year or why did we do it? We focused on three priorities since last year’s discussion here, more or less the same as the year before:

- First of all, the crisis. In Europe, the crisis is probably more pressing than here. We are still dealing with some of the toughest consequences of the financial crisis that started in 2008.

- Second, the very fast technological change, new activities. This is a big challenge for competition enforcers to deal with new activities, with new ways to consider the evolution of the markets, with new behavior that can be considered as breaching the competition rules.

- Third, we continued to work on cooperation. We increasingly need to work together with our colleagues here in the United States and in many other countries and jurisdictions because our cases are becoming global. We need to strengthen our coordination with other enforcers, and we need to improve the way we can work together, even starting from different systems and different legal traditions.

So, allow me to go into some detail on these three priorities. First, the crisis. On top of the traditional competition enforcement that is common to all of our colleagues in other parts of the world, the European Commission also deals with State aid control. Given that a lot of public money is being channeled through the financial sector, in Europe we have a very high responsibility to put order in the use of public money to support the financial system. This requires a lot of efforts from our side.

We are quite happy with how we are able to use our State aid control instruments to restructure financial institutions, to put them on a viable ground for the future, to better organize the burden sharing of the resources and the efforts required to restructure financial institutions. We also work to avoid—and this is extremely important for us—internal barriers and distortions of competition within our internal market. These could arise through the wrong and uncontrolled use of public money. I think we have managed to do a lot of good work this year and succeeded in preserving the integrity of our internal market.

At the end of last year, I had hoped to eliminate the special State aid crisis regime to deal with all these consequences of the financial crisis. But, because of the sovereign debt crisis, we were
obliged to prolong this exceptional regime, at least during this year, and we therefore continue to use this framework.

We have also had some cases with special difficulties in the countries where there are financial programs to deal with the sovereign debt crisis—in Greece, Portugal, Ireland—and we are still facing some difficulties in some other cases. But all in all, I think we can be satisfied with the way we are using State aid instruments.

On the traditional enforcement of competition rules, cartels continue to be priority number one. We adopted four decisions in 2011. Last Wednesday we adopted decisions in two important cartel cases, freight forwarding and mountings for windows. In the freight forwarding case, we have had very good cooperation with our colleagues here in the U.S. and in other cases, with other competition authorities.

Cartels will continue to be priority number one. We expect to issue more cartel decisions this year than in 2011. There are quite a few cases in the pipeline.

We are also using the new settlement instrument more and more. Three out of the four decisions of last year were settlements. I consider this a very useful instrument if we can settle the case. We are not obliged, of course, to settle, and not all cases are suitable for settlements. However, if we can settle under good conditions and put an end to the infringement, we prefer to accelerate the decision-making through a settlement procedure. I think that is good for everybody: we free our resources and companies can restore their reputation. We will continue to use the instrument whenever suitable in the future.

Merger activity has started to grow again in 2011 in Europe and also in the United States and in other areas. We had one particular case that created a lot of difficulties for us and was the only negative decision we took in over a year, the Deutsche Börse/NYSE Euronext case. We had a lot of discussions prior to taking the decision. We asked the parties involved in the merger for divestiture of their European-based derivatives exchange, but this was not possible. For the parties it was a deal breaker. Unfortunately, we had to give a negative decision in this case. If allowed, the merger would have led to a near-monopoly in European financial derivatives worldwide.

During my mandate, during these two years, the only negative decision apart from the Deutsche Börse/NYSE Euronext, involved the proposed merger between two Greek airlines that would have also created a quasi-monopoly on the Greek air transport market.

Even though Deutsche Börse has announced it will appeal, I must point out that a negative decision prohibiting a merger is not the rule for us, it is the exception. To the extent possible, what I will continue to do is to try to find with the parties involved remedies to overcome the difficulties encountered allowing us to clear most mergers. For instance, in recent months, we have cleared some important mergers: Google/Motorola, also in cooperation with our U.S. friends; Microsoft/Skype, another very good example of cooperation with our U.S. colleagues.

In antitrust, we adopted some important decisions and we opened formal proceedings in several cases. A trend that I see is that new technologies, new activities, are becoming a real issue in our antitrust enforcement, especially for abuse of dominant position or unilateral conduct. For example, we are now dealing with cases regarding the so-called patent wars. This is a very important issue, and we are paying a lot of attention to this.

We established with our Horizontal Guidelines more than one year ago the rules of the game, the FRAND terms to license standard essential patents (SEP). This is one of our most important priorities as a new activity. We are not yet at the end of investigations involving this issue, and we also have other ongoing cases including Google.

The last thing that I wanted to mention is how we deal with our colleagues in other countries, with other competition authorities. The global nature of our cases requires more and more cooperation. I am very happy with the kind of cooperation we have reached with Sharis and Jon here in the United States. I am also very happy with the kind of cooperation we have managed to develop with some of our Asian colleagues, like Japan and Korea. We are trying to do the same with our colleagues in the most important emerging countries—China, India, Brazil, and others. I think this is the next challenge for all the competition enforcers around the world. We need to build a stronger community of competition enforcers. We don’t want to be used by different players in different cases because we are not able to coordinate ourselves.

Thank you very much.

MR. STEUER: Thank you.

Turning to India, Chairman Chawla.

ASHOK CHAWLA: Thank you, Richard.

Ladies and gentlemen, it is indeed a daunting task to be here in the midst of such veteran, well-established agencies with wisdom from years of experience. We are actually a baby in this business of competition law. Let me spend the time allotted to me to cover briefly where we come from and where we stand, what are the challenges that we face in India.

As most of you would know, the early years of our economic development were controlled substantially by the state. The philosophy until 1990–1991, was that the states should control the commanding heights of the economy. A lot of that started changing about twenty years ago, in 1991. Physical controls gave way to financial controls. Trade policy was reasonably liberalized, the tax regime was rationalized, customs duties started going down in keeping with the levels in the South East Asian region. The process of regulatory reform also started at that time.

So twenty years have seen a fair amount of change in the Indian economy, with less government, more business, with a system which is less inward-looking than what it used to be.

The precursor of the present competition law was the Monopolies and Restrictive Trade Practices Act, which some of you may have heard of. This was passed way back in 1969, where the focus was more on size and structure. It was intended to control the proliferation of monopolies. But that piece of legislation was clearly out of sync with what was happening in the relatively new India post-liberalization. Therefore, the Competition Act of 2002 was enacted. It faced certain legal difficulties and challenges until amended in 2007.

The advantage that we had as latecomers was that there was the wisdom of the entire world to pick from and put it in the legislation. The Act is, I would say, basically very robust—in fact quite ambitious—built on the best legal practices and systems from around the world. The Act focuses on behavior, not merely on size and structure. It focuses on not just dominance but abuse of dominance, which is what the best practice is.

As part of the Act, the Competition Commission of India was set up. It has powers which are both inquisitorial and of enforcement. The inquiry and the investigation are done by an office that reports to the Commission but is reasonably independent. The Commission adjudicates in matters that come before it.
Appeals lie first to the Competition Appellate Tribunal, which is a full-fledged judicial body, and thereafter the Supreme Court of India.

The Act covers the three main pillars in relation to competition law and the competition culture. There is the unilateral action part, the abuse of dominance; there are provisions relating to cartels; and there is prior mandatory approval for mergers and acquisitions above a threshold, which in the first instance has very consciously and very carefully been kept at a level that is reasonably high so that the normal process of consolidation of business and industry, which is very crucial for future growth and which is the way business grows is not stifled.

The Commission can act on information which comes from informants. This is interesting. They are informants, not complainants, because the person who gives information need not have any specific nexus with the matter which he is raising before the Commission. He gives us information. If we feel there is something in it that needs to be looked into, the matter proceeds. Otherwise it stands closed.

We also have powers to suo moto look at matters which are anticompetitive.

There are provisions for penalties in the case of antitrust behavior which go up to 10 percent of the average turnover of the last three years.

In the case of cartel activity, penalties have been kept higher. It is 10 percent of the profits for each year that the activity continues. But we do not have criminal jurisdiction, as in some of the other countries.

The tools that we have at our disposal to implement the Act are:

- Evidence on paper,
- Oral evidence, which the investigator takes;
- Experts; and
- A leniency provision for cartels, which will presumably become a more serious proposition once a few cartel cases are decided.

What we do not have is search-and-seizure power or the power of dawn raids, which is something that we have suggested to the government. It is possible that an amendment to the Act will be contemplated. But as of now this power is not available.

We have mergers and regulations time limits, which are under the Act 210 days. We have in the regulations kept them at 180 days.

In respect of cases which prima facie do not seem to have any major adverse impact on competition, we have imposed a self-regulating discipline that we will decide those cases in thirty days. All the cases that have come to us in the last eight or nine months since those provisions were enforced have been disposed of within those thirty days because they were relatively simple, straightforward cases.

What are the focus areas? What is it that we will concentrate on as we go ahead?

One, we need to build capacity in the organization both from internal and domestic sources but also by collaborating with some of the more mature jurisdictions, which we are in the process of doing.

Number two, communication—that is the second C—which includes advocacy, advocacy not just with businesses, advocacy not just with other stakeholders, but equally importantly with government, which still operates a number of regulated areas and which has the baggage of policies which may not entirely stand the test of competitive neutrality.

Lastly, the third C is we need to be credible in the manner in which we build our organization as we go ahead.
MR. STEUER: Thank you.

Chair Donahue?

JAMES DONAHUE: Thank you, Richard, and thank you for inviting me here today to speak on behalf of the state attorneys general.

This week the Supreme Court heard arguments on challenges by twenty-six attorneys general to the new health care reform law. Those arguments focused on, among other things, the mandate that people buy insurance and whether that is legal or not. I am not going to talk about that.

There is another part of the law that we get a lot of inquiries about on the antitrust side, and that is the accountable care organizations (ACOs). That provision of the law has had two impacts on state attorneys general offices. One is we have seen an awful lot more mergers. In the past year, Massachusetts has looked at six hospital mergers; Pennsylvania has also looked at six; Connecticut has looked at three. These are states, Massachusetts and Connecticut, where there rarely have been hospital transactions before. I can go through a list: Tennessee, California, Illinois, Ohio—all have seen hospital mergers is the past year, many of them justified on the basis that they need to merge in order to become an ACO.

But it’s not only hospital mergers. We see mergers between hospitals and physician practices, mergers between physician practices within the same specialty; multi-specialty physician practice mergers; and ancillary service mergers, like dialysis centers.

So there is a whole lot of merger activity that is being produced out of this desire to establish ACOs.

One other thing here. We’re almost always doing hospital mergers in urban areas with the Federal Trade Commission because there is a Hart-Scott-Rodino reporting requirement there. All the other mergers, and even hospital mergers in rural areas, we are doing those by ourselves. There is no HSR reporting. So we know about it but maybe the Federal Trade Commission doesn’t. In some of those cases, the Federal Trade Commission comes in and helps us. A lot of these other cases we are doing on our own.

Now, as a little aside, I want to note that neither the health care reform law nor any other law is providing the states with more funding to do all these merger transaction reviews.

The other effect that we see here is that ACOs are raising, not lowering, prices, in part because apparently some of this consolidation is leading to ACOs having market power. We see prices being raised in two ways. One is directly, where the ACO goes and increases the price it is charging to health plans and employers. The other way is they are getting into more restrictive networks and limiting who they are going to deal with.

We had a hospital merger involving Geisinger Health System in a small town in Pennsylvania. We had a concern there that they were going to cut out many of the other Medicare Advantage plans. Because a lot of seniors have chosen Medicare Advantage plans other than the Geisinger Medicare Advantage plan, we thought it was important to protect their ability to go to that hospital and for their Medicare Advantage plan to have access. Otherwise, the local hospital becomes an out-of-network hospital and it becomes very expensive for the seniors to go to that local hospital.18

That is a problem not only in Pennsylvania, but it’s a problem in many areas around the country where there are these ACOs or these vertically integrated organizations that are seen as very efficient. But when it gets down to what they do locally, they may be raising costs to either employers or seniors.

I want to talk about another topic—and Assistant Attorney General Pozen mentioned it—the Muni Bonds case. The Department of Justice has done a fabulous job developing the evidence of liability in that case. It has been a great partnership with them, because we have worked with them to figure out what the wrongful conduct that DOJ uncovered cost our municipalities.

We have settled, with DOJ and a number of other federal agencies, for a total of $350 million in redress. That’s not the entire amount—there are additional fines and other payments. But $350 million of the amount that has been recovered will go back to the municipalities.

We are about to start sending out checks from Bank of America. Those checks are going to 1200 municipalities and nonprofits across the country. Some of those checks are for hundreds of thousands of dollars. I’m sure you can pick up the paper every day, no matter where you are in the country—the city where my office is, Harrisburg, is in the news for not having a lot of money—and you can see that all these entities are distressed. So the ability to give them back money from the effects of price fixing is really terrific.

Lastly, I want to talk about our core business, which is bringing horizontal price-fixing cases.

A week ago, Ohio brought an action against two rock salt producers in the state which had a longstanding agreement to allocate markets. I recommend reading the complaint. It is really detailed and it outlines a conspiracy that has cost the taxpayers of Ohio quite a bit.

We are also looking at this from a preventative standpoint. There is an attorney at DOJ, Fred Parmenter, who noticed that in the road materials area there are a lot of mergers that go through because nobody knows about them. Not every quarry in the United States that may be bought by a big conglomerate or something like that is large enough to trigger an HSR filing. So Fred came to the states, and he has come to the state departments of transportation, and had this great idea to help save taxpayers money and ensure that they have a competitive market when we go out and buy road materials. It has been, I think, pretty successful and it has been a great partnership.

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The last case I want to mention is that Michigan has brought a criminal case against five gasoline stations in Madison Heights, Michigan, and they have obtained criminal fines and guilty pleas of $20,000–$50,000.\footnote{Press Release, Michigan Attorney General Bill Schuette, Schuette Announces Guilty Pleas in Madison Heights Gas Price-Fixing Operation (Dec. 7, 2011), available at http://www.michigan.gov/ag/0,4534,7-164-46849_47203-267032—,00.html.} This is very significant because it’s a criminal case that involves gasoline.

Also, sort of as an aside, I think all of us on the American side up here on the stage get complaints about gasoline prices all the time. Nine times out of ten, we go out and investigate them and we come back and we say, “Well, it’s really because OPEC has done something” or “it’s a change in supply and demand.” It’s really frustrating for us to go back to consumers, who are upset about the fact that the price of gas has gone up. But here was a case where people complained about the price of gas going up and there is actually something that we could do about it. So that’s really terrific.

The wrap-up here is that, from the states’ perspective, we have an excellent partnership with the two federal agencies and we are working very closely with them on lots of cases, and we are out there vigorously enforcing the antitrust laws on our own.

MR. STEUER: Thank you.

We are now going to launch into some questions and some dialogue. To kick it off, John is going to ask Chairman Leibowitz a question about privacy.

JOHN VILLAFRANCO: This has been a big week—actually a big month—for privacy. The White House issued its Policy Framework earlier last month and earlier this week, the FTC issued its own Privacy Report, which apparently is based on unfairness, as opposed to deception.\footnote{THE WHITE HOUSE, CONSUMER DATA PRIVACY IN A NETWORKED WORLD: A FRAMEWORK FOR PROTECTING PRIVACY AND PROMOTING INNOVATION IN THE GLOBAL DIGITAL ECONOMY (2012), available at http://www.whitehouse.gov/sites/default/files/privacy-final.pdf; Federal Trade Comm’n, Protecting Consumer Privacy, supra note 8.} Unfairness, of course, is an act that causes substantial injury not reasonably avoidable without countervailing benefits.

I want to focus on that last prong. There have been commentators who have asked about the effects of privacy regulation on competition, disadvantaged rivals, effect on innovation, and effect on consumers. What are your views on that particular prong and how do the recommendations relate to the effect on competition and consumers?

MR. LEIBOWITZ: Well, I do not think they relate to unfairness at all. In yesterday’s hearing before the Energy and Commerce Committee, we made that point.

Our recommendations are in our Privacy Report, which is very thorough. We had 450 comments on our draft report. Our recommendations are best practices. They are not enforceable. We like companies to rise to the level of best practices. Many are there already. But some believe that meeting the recommendation puts them at a competitive disadvantage. So we want to move forward on privacy in a very self-regulatory way.

Now, our Report has several different tenets. One is privacy by design. When a company is developing the coolest new app, they ought to put privacy protections into it. Some companies do that. We issued a report three weeks ago where we found that mobile apps actually had very low levels of privacy protection. So we are working with industry to move forward with improvements.
The second tenet is choice. Consumers should have more choice about where their information is going. I think most people agree with this concept. Part of the choice architecture is the notion of “do not track,” which would allow consumers to opt out of being tracked by third-party Websites, with a few exceptions for things like bandwidth monitoring and fraud detection.

The third tenet is transparency. We think there ought to be more privacy transparency online, particularly in the mobile space. Let me tell you how bleak privacy notices are online. The Declaration of Independence is about 1300 words. Martin Luther King’s “I Have a Dream” speech is about 1600 words. The average privacy policy online is more than 2100 words. So it is no wonder that people do not read them.

We are very committed to privacy at the Commission. Reasonable people may disagree about exactly how to move forward on it. From our perspective, we aspire to best practices, which some companies are already meeting.

**MS. GARZA:** Assistant Attorney General Pozen, the proposed AT&T/T-Mobile merger was indeed big news this year, so I hope you don’t mind answering a couple questions about that. The first question is, would you discuss the Justice Department litigation strategy you followed there? For some of us, it was one of the most interesting things about the case.

Second, there was a lot of discussion about the merger’s effect on jobs. As I recall, the Justice Department’s press release even referred to job loss. Can you tell us if in fact the Division did consider the impact on jobs and whether you think job impact is a part of antitrust analysis? If so, how you deal with it?

**MS. POZEN:** For us there were really two important things we took away from litigation strategy. One was the team we put together. Second was our work with the Federal Communications Commission.

When I started I talked about our litigation efforts and how things have really moved forward on that with our Deputy Assistant Attorney General for Litigation, with our Director for Litigation, and then bringing in what we call special government employees, Glenn Pomerantz and Dave Dinielli. I was reminded of Teddy Roosevelt, who said that you need to “speak softly and carry a big stick.”

I can tell you in AT&T we had a big stick in terms of our litigation team and the Division-wide effort. I applaud how everyone pulled and worked together and were led by really experienced trial lawyers. That was key.

And then, as I said, our relations with the FCC. The FCC is an expert agency. They know this industry inside and out. They deal with it every day. They have a public interest standard and they consider competition in that. We had developed a strong relationship with them, in particular in our work on Comcast/NBC,23 where again it’s public knowledge that we were sharing documents, sharing databases. That continued on through AT&T.

Their work was particularly important. They looked at jobs as part of their public interest standard, and they unpackaged in their staff report the allegations and assertions about jobs.

It was interesting to live in Washington at the time. I think every morning when you watched the morning news shows, there was a commercial that AT&T ran talking about the job expansion. And it is unusual because, at the same time, when you have parties coming in and talking to you about

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synergies and one of the line items is elimination of redundancies. I think we all know that's job elimination.

But in terms of whether we consider that in our analysis, I actually look at it sort of the other way, that if we continue to promote and ensure competition, the economy expands, innovation occurs, and jobs are created.

So no, it's not part of our regular analysis, but it's something that we are hopeful for if we continue to be the cop on the beat, we continue to maintain competition and markets.

**MR. STEUER:** Vice President Almunia, the European financial issues have dominated the financial news on both sides of the Atlantic. What role do you expect that competition law is going to play in stabilizing the individual economies of Member States?

**MR. ALMUNIA:** I referred briefly in my presentation to the role of our State aid control rules in the financial sector. This is extremely important. Three or four years ago, the financial sector in Europe was affected by the financial crisis, in a similar way to the United States. But there is a second round of problems in Europe because of the links between the sovereign debt crisis and the balance sheets of the financial institutions. We are using our State aid control to allow the treasuries, the public sector, and the budgets in the different Member States in Europe to support the banks when this is needed for financial stability reasons. We do this to avoid the materialization of systemic risk in some countries, but at the same time to preserve the rules and the level playing field in our internal market.

I think we are doing the work that will in the future be carried out by a resolution authority at the European level. The European Commission will put forward legal initiatives for the creation of a resolution authority at the EU level. We are not yet there, but probably in the next few months we will put forward this initiative.

In the meantime, during the process of discussions of this legal initiative by the European Parliament and the Council of Ministers, the ECOFIN Council, we will continue to use State aid control in the same way as we have been doing in the last year.

As I said before, we have now more viable financial institutions that have been restructured. We have been able to avoid the closure of national financial markets. Thanks to the banking sector rules and with the help of the European Central Bank that is providing liquidity, we continue to have an internal market for the financial sector. So far, so good.

In addition, we are modernizing the State aid rules for the good functioning of the economies in Europe. We have right now almost forty different guidelines for the control of State aid in different sectors, for different purposes—environment, research and development, regional aid, small and medium-sized enterprises, risk capital, the maritime sector—and we imperatively need to modernize the way State aid control is managed. We need this reform in order to be able to support the activities that will require public support to overcome the crisis and to foster economic growth, but without giving in to protectionist trends, without establishing new barriers within the internal market and without distorting the level playing field.

This modernization of the State aid regime will be presented in the next couple of months. I will put forward the ideas at the beginning of April to my colleagues in the European Commission, to the ministers, and the European Parliament in the next months.

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I hope that from now until the end of 2013—so before the new budgetary seven-years framework will come into force in Europe—we will have modernized the guidelines for State aid control. I hope that we will have simplified the procedures and established better cooperation with Member States. At the same time, most Member States in Europe are embarked on very ambitious and very demanding fiscal consolidation strategies.

So I want to emphasize the need to use public money better when needed for new activities and at the same time put in more demanding rules to avoid the waste of public money in the fiscal consolidation period that we are living in.

A final point on Europe. When I meet with European companies and European governments, they tell me: “Europe is the only one who is putting State aid under control. What will you do when dealing with public subsidies that are being given in the United States, in Asia, in emerging countries, in all the industrialized countries?”

This is a major issue for the next years. We need to avoid protectionism at all levels, in our market and internationally. We need to cooperate not only on antitrust enforcement, we need also to cooperate—and this is not always the task of other competition authorities, but it is a task for public authorities around the world—to establish clearer rules and a more strict discipline in using subsidies. We have to avoid having protectionist temptations materialize, to avoid further distortions in the way different economies relate with the others. This is necessary because the global economy requires a stronger and clearer framework for the use of public money not only in Europe but also in the other parts of the world.

MR. STEUER: Sometimes, in the short term, and particularly during a crisis, it seems that the priorities behind state aid decisions and competition decisions might be in conflict. Given your responsibility to look at both, how do you strike a balance when they seem to conflict?

MR. ALMUNIA: In relation to the enforcement of the state aid rules, for example, these days we are dealing with a case of a company in France in the transport sector that received in the past a lot of public money. We adopted recently a negative decision, so this public money that was not compatible with the EU State aid rules should be recovered by the French State. This company is facing very serious difficulties and is in a liquidation procedure in France. There is one buyer that wants to buy part of the assets and wants to keep part of the activities of that company. To take into account the social problems around this failed company, to create conditions with our decisions to allow the activities that can be viable in the market to continue, but at the same time to request the company to comply with the State aid rules and with the consequences of a negative decision, is not an easy task, but is a possible task.

Probably at the beginning of next week the Commission, under my proposal, will adopt a decision establishing the right balance between the different interests at stake. We have been able to do so in the past, and the European Court of Justice often supports our decisions and rules against appeals it finds unfounded.

I think that we should be rigorous in enforcing this part of our responsibilities because, if not, the bad money will create the possibilities for bad economic performance, for bad companies, for zombie companies in the market who distort competition. This would prevent new activities to develop and flourish that would allow us to have a more sustainable path of growth.

This is not the first time that we are dealing with these difficult tradeoffs. But on this occasion, given the depth of the crisis, this is a very important task and responsibility.
MR. VILLAFRANCO: Chairman Chawla, the Section and its members are devoting increased attention to India of late. I know many of us are busy with all sorts of matters that have an Indian component to them.

What unique features are there in the Indian economy that require competition rules or procedures that are different from those here in the United States or in the European Union?

MR. CHAWLA: As I mentioned in my opening statement, the law is essentially modeled on the kind of law that prevails in most of the mature jurisdictions. So in terms of legal provisions, there are not many changes or differences.

But I also touched on the kind of economic history that we are carrying on our shoulders. There will be, I guess, some differences in terms of interpretation of law, in terms of the evolving jurisprudence on competition matters as we go ahead, because it cannot be entirely in a vacuum anywhere in the world, and also therefore not in India.

So, basically speaking, the approach will have to be balanced. We will have to strike a balance between the absolutely purist approach and temper that with the development of India so that genuine businesses, genuine parties that wish to invest, companies that wish to merge as part of the consolidation process, are not unduly frightened and it is not seen as something that is anti-growth and anti-development.

Basically, the law will have to be implemented, and the law will prevail, with a certain amount of balance.

MS. GARZA: Chairman Donahue, we understand that local interests have been putting pressure on states to challenge mergers where the federal agencies have decided not to bring an enforcement action. Do you foresee that the states would attempt to challenge a transaction that neither the Federal Trade Commission nor the U.S. Justice Department has decided to challenge?

MR. DONAHUE: The short answer to that question is yes. I think, if you look at our history in Pennsylvania, there have been a number of hospital mergers where the FTC has closed their investigation and we have gone forward, either informing the parties that we are going to sue to block the merger or working out a consent decree.25

I think there are a lot of specific industries where the states have a lot of experience—health care is one, retailing, road materials, prescription drugs—where we have all done litigation. If you take prescription drugs in the TriCor case,26 the states again were prepared to litigate that case by themselves.

I’d be less than honest if I said, “Look, every single case is a case that we’ve got the resources to challenge,” because there are some mergers that involve quite a number of issues, quite a number of different facets, a lot of efficiency claims. And maybe there are some mergers that we don’t have the resources to challenge. The thing is I don’t think anybody can bet that there is a particular transaction that we wouldn’t challenge if we thought there was still a competitive problem.

MS. GARZA: Would that be your answer, including in a situation where a federal agency had entered into a settlement with the parties to a merger?

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MR. DONAHUE: Even if there was a settlement, yes. If we thought that there was an interest there that wasn’t appropriately addressed, we would do that. Not to knock the federal agencies, but there are times when we have a much better insight on local issues than they do. We’ve gotten more information, and we maybe have different information and a different perspective on information.

We were talking among ourselves the other day. North Carolina noted that they were working with the federal agencies on a road material merger, an asphalt merger, and they checked with the Department of Transportation, and I think the DOJ had said, “No, those two asphalt plants are close together.” The North Carolina DOT said, “No, no, no. There’s a mountain between those two plants. When you drive around the mountain, the asphalt cools to the point where it’s no longer usable.” That’s something that we know. That’s something that we can bring and we might act differently than the agencies from here in Washington would.

MR. LEIBOWITZ: Jim is exactly right. Sometimes state AGs have better insight, particularly into local problems or local issues. I would also say—and I think all on this panel agree—that when we work together we are much stronger collectively than we are individually. Our agency and the states have been working cooperatively on a variety of matters.

MS. POZEN: I would echo what you’re saying, Jon. I think—again I’m sorry I’m beating the drum on AT&T—but that was an example. Not only did we work together, but really the states helped us tremendously with the workload there in terms of depositions and discovery, et cetera. It was a wonderful example of cooperation. We instituted new tools there so that we could further cooperate with the states.

Right now we are working with the states on eBooks—I said that at my hearing—and with the EC. Again, together, as we move forward on those kinds of investigations, working in parallel, working together where we can, I agree with you, I think it’s better for us as agencies and law enforcers. I also think it is better for the parties if you know that we’re all on the phone together. It’s more efficient, more effective, for business as well.

MR. STEUER: Thank you.

If we may turn from the lower tech of asphalt to high tech, John has a question for Chairman Leibowitz.

MR. VILLAFRANCO: Technology mergers are making news. Recently, both EC and the U.S. authorities examined acquisitions of patent portfolios that raised concerns about the acquirer using those portfolios for anticompetitive purposes. What tools does the FTC have to address competition issues in the standard-setting area?

MR. LEIBOWITZ: Well, as we know, standards can be procompetitive. They play a big and pro-

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ductive role in interoperability between products and encourage competition on price and innovation. But, as we have seen over the years, the standard-setting process occasionally can be manipulated in anticompetitive ways.

I should note that our Section 5 authority over unfair methods of competition is broader than the antitrust laws and could be a very useful tool in this area.

What we have found in some of our investigations is that a standard-setting organization (SSO) member might deceptively wait until after a standard is agreed, then even wait several more years until a standard has been established, then finally reveal that it has what is known as a “standard essential patent” that covers the standard. And it can use that standard essential patent to try to leverage higher royalties. This was the nature of the Rambus case,28 which was ongoing when Tom Rosch and I came to the Commission. We approached Rambus as a monopolization case.

Another issue we are considering is the problem of SSOs encountering later attempts to say, “Your technology reads on my patent.” They have tried to get members to agree to RAND or FRAND commitments—fair, reasonable, and nondiscriminatory terms—a somewhat amorphous concept to be sure. But what it means is if an SSO participant is competing to have its technology included in the standard, it is promising to license at reasonable terms. Now, if an SSO member again engages in deception, we can go after that entity. And there may also be circumstances that would merit a challenge under Section 5 outside of that. So it may be, for example, that if you have offered a RAND or a FRAND commitment to go into court and seek an injunction, rather than damages, that might itself be a Section 5 violation.

The Commission is looking at this. These are very serious and important issues. You want to make sure that innovation continues. But you also want to make sure that companies cannot engage in licensing that is supposed to be worked out and then hold up that innovation.

MS. POZEN: I’ll add on too because we did issue a closing statement and worked very closely with the EC on Google/Motorola.29 We, coincidentally, had three mergers in front of us—not just Google/Motorola, but also the transfer of Nortel and Novell’s patents, all at the same time. So these were significant patent portfolios being transferred into the hands of significant technology companies—Google, Apple, and Microsoft.

We looked at them very holistically. We convened an internal group on intellectual property to think about what it means when you transfer these patents; in particular, as Jon has articulated, the SEPs, or the standard essential patents, and the likelihood of holdup through injunctions or exclusionary actions with our International Trade Commission (ITC).

At the end of the day, we concluded that it did not violate Section 7 to transfer these. In particular, on those matters, as we noted in our closing statement, three of the companies issued letters to the standard-setting bodies regarding what they would do with the holdup aspect of it, the injunctions and exclusionary practices. Really, just two of them went directly to that issue. Microsoft and Apple articulated in a very clear way—which to some extent gave us some comfort, and we certainly saw that as a positive development.


But you have to remain concerned about this kind of power. You mentioned in your opening, Joaquin, these patent wars that are going on that could possibly inhibit competition if these patents are asserted in a way that results in harm to competition.

**MR. ALMUNIA:** If I may add some words on this, we dealt with this issue when we were discussing the EU Horizontal Guidelines at the end of 2010. We established that the licensing of these patents should be offered on FRAND terms. The question is: how do you define FRAND terms on a case by case basis? It is not always easy.

But after the adoption of the Horizontal Guidelines, we were facing one case, *Apple/Samsung*. We opened proceedings because we think that the use of injunctions from Samsung’s point of view may not have been in accordance with our rules. We are now dealing with this case.

Afterwards, in cooperation with you, we analyzed the *Google/Motorola* case. That was the only one that was notified in the European Union, not the others.

We cleared the *Google/Motorola* case. But I remember I gave a warning, saying, “Well, we didn’t find any merger-specific problems, but there are problems around the use of standard essential patents to possibly abuse market power.”

After this clearance, we received complaints from Apple and Microsoft against Motorola. We are now discussing what to do with these. Probably in the next days you will know what we decide to do.

But the question of patents and the standards—these tensions, this patent war—is not only taking place in this particular sector. The setting of standards can be a powerful instrument to foreclose competitors. We are dealing with one case in the banking sector for e-payments. The European Payment Council, a banking sector organization, was discussing the creation of a framework for e-payments in Europe. We opened proceedings because we thought that there were risks of foreclosing the non-bank competitors in the e-payments. We are dealing with this case.

We also launched a request for information to the big telecom operators in Europe because, for mobile services, payments, and other kinds of services, they were having meetings. We asked them for further information to look into what they are discussing because there is also a risk of establishing some kinds of standards that can foreclose other operators from the possibility of giving these services under normal terms.

So the new technologies are fantastic, but, not only from the privacy point of view but also from the pure antitrust or competition point of view, they give us a lot of work.

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**MS. POZEN:** It’s fair to say what you’re hearing from us is it’s a new frontier that we recognize could have competitive impact. But at the same time I know at DOJ we are particularly mindful that these are property rights, and we are trying to find that right line, that right balance, between when they can be asserted rightfully and when they have gone too far and have been asserted in a way that creates competitive harm.

**MS. GARZA:** Sharis, you have talked about priorities for the new administration. One of the first things that the administration did was to withdraw the *Section 2 Report*, which created expectations that we would then see a Section 2 case. We did see one Section 2 case, *United Regional Health Care System*,34 which involved tiered discounts that amounted to de facto exclusive dealing. Can you explain a little bit about why the DOJ chose to pursue that as a—“pure Section 2 case,” under Section 2 only and not Section 1? And can you tell us whether there are other Section 2 cases in the pipeline?

**MS. POZEN:** To reflect back on when the *Section 2 Report* was withdrawn, what we tried to make clear at that point was it was a tremendous amount of work and effort to put all of the learning about Section 2 in one place. It really was just the conclusions and the discussion about false positives that we disagreed with when we withdrew it. It is still an excellent resource and still used. And, just as you said, our *United Regional* case was our one—we say “pure,” because sometimes in mergers you’ll allege a Section 2 claim, and it had been alleged in the past—but this was our first Section 2 unilateral conduct case since 1999. We thought it was important for a couple of reasons. One, it was in health care. Health care was a priority and will continue to be a priority. We want to ensure that competition flourishes in what has been described as an industry where there can be real competitive problems. Second, as you said, Deb, it was the contracting practices that were the real issue. Here you had a monopoly hospital that was using a pricing scheme to explicitly exclude a competitor.

We worked hard on that consent agreement, because you don’t want to exclude all pricing contracting. Rather, you do want to eliminate those that are exclusionary and leading to barriers to entry or lack of competition.

I mentioned earlier our efforts to be more transparent. I would commend the competitive impact statement on that particular case35 because a lot of care was taken in drafting it to articulate the standard there in terms of the interplay of cost and price and how we would be looking at that going forward.

So we do see it as a significant case. Section 2 cases take a lot of time and effort. I had a question at one point, when we brought the *Blue Cross/Blue Shield of Michigan* MFN case.36 One of the questions was: You didn’t plead that as a Section 2 case. To some degree, that had to do with the market shares across Michigan and the burden under Section 2 that we’re quite mindful of.

So the efforts are under way to ferret out those kinds of monopoly behaviors when they cross the line and they take exclusionary actions, like happened in *United Regional*, and enter into

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predatory acts to maintain monopolies. That is an ongoing effort at the Division and will continue to be.

MR. STEUER: We should talk about cartels. John, I think you have a question for Vice President Almunia.

MR. VILLAFRANCO: Regarding cartels, what do you see as future trends in enforcement? Will leniency continue to be important? The Commission lost several cases last year on the issue of parental liability. Does this suggest a fundamental shift in your view in enforcement against parent companies?

MR. ALMUNIA: Cartels, as I said before, are our priority number one. We are working on a long list of cases right now.

I can signal two areas where we have a lot of work on cartel issues: the financial sector, where other regulators and competition authorities are also dealing with some cases of illegal agreements that we are investigating. And also in the automobile sector, we are dealing with a list of different suspected cartels.

I referred before to how we are using settlements. We are very happy with this new tool. It allows us to decide on cases in a quicker way and with good results, which is different from the experiences we had two or three years ago.

The leniency problems are also very important. It is true that the Court of Justice asked us to legislate, to decide to what extent the information we receive from the leniency applicants should be protected. We are preparing legislation in this regard. We will probably put forward legal initiatives this year to delimit the way we will protect the leniency applicants with the documents they submit to us.

Regarding parental liability, there have also been some recent rulings of the Court of Justice. All in all, I think they support the way we consider the existence of parental liability. In some cases, the Court has asked us to better argue our parental liability claims. In our decisions right now, these kinds of arguments that were requested by the Court of Justice are being included in the original decisions. So, all in all, we consider that our cartel enforcement stands well up to the Court of Justice’s careful scrutiny.

One last issue that I want to mention regarding cartels enforcement is that, as you remember, we adopted the new Fining Guidelines in 2006. We have received three rulings from the Court of Justice supporting the substance of the new guidelines of 2006. These rulings allow us to be on the safe side when discussions about the level of the fines continue.

At the beginning of the implementation of these Guidelines, there were opinions saying, “You are going well above what will be accepted by the Court of Justice.” Now we have possible decisions supporting our enforcement.

MR. STEUER: Chairman Chawla, I wanted to jump in and ask a question of you. I should point out that our Section is going to be having a particular focus in the coming year on India. And so we are especially glad that you could join us today.

I have a question about mergers. In some recent filings in India, it appeared that there were exempt transactions in which premerger notification was filed anyway, and those transactions were approved quite quickly. The examples I have in mind are Alstrom and Siemens reorganizations. Is this what really happened there; and, if it is, what does it mean for other companies that
are considering whether or not they should be filing?

**MR. CHAWLA:** Our regulations provide for certain categories where notifications are not required to be filed. Those two transactions involved only intragroup acquisitions. Intragroup mergers, amalgamations, were not exempt from the notification requirements at that point in time. When these cases came to us, we didn’t really lose time in approving them. In addition, about a month ago we revised our regulations to provide that intragroup mergers and amalgamations no longer need to file.

So the whole idea is that we will continuously, based on our experience, go on fine-tuning the regulations with a view to reducing the compliance burden, particularly in cases where there is really not likely to be any adverse effect on competition. That’s how we handled this particular issue.

**MS. GARZA:** Chairman Donahue, some of the states have continued to pursue per se cases against resale price maintenance after **Leegin Creative Leather Products.** Can you tell me from your perspective what we can expect the states to continue to do?

**MR. DONAHUE:** The states have gone through this before with their indirect purchaser statutes. They went all the way to the Supreme Court in **ARC America,** where the Supreme Court said that the states could have a different antitrust rule in that case, that they could collect damages for indirect purchasers, when the Supreme Court had said in **Illinois Brick,** that you could not collect damages for indirect purchasers under the federal antitrust laws. So the states have done that before.

In the context of the constitutionality of resale price maintenance, whether it’s per se or not, I guess the argument is something along the lines—it’s a Dormant Commerce Clause argument—that because there have been Supreme Court cases which have held that pricing regulations in one state that have an effect on other states are unlawful under the Commerce Clause, that might apply in this situation. Those cases typically involved alcoholic beverages and a law that said: “You must post a price in our state, and you can’t sell to any other distributor in another state at a lower price.” There the Supreme Court said there is an extraterritorial effect, an effect not permitted by the Commerce Clause.

Resale price maintenance is different. First off, there is no price; there is no actual price regulation by the state. Secondly, because resale price maintenance may be per se unlawful in a state, that doesn’t mean that goods are sold at different prices. Prior to the Supreme Court’s decision in **Leegin,** there are plenty of manufacturers that had RPM programs out there that met the criteria in another Supreme Court case, **Colgate,** and lots of goods were sold and are sold at the manufacturer’s suggested retail price.

The key thing here is that you have to take this apart and look at what is resale price maintenance. What are the elements there? You need a good product, the manufacturer has to pick the right price, and it has to pick the right distribution system. If the manufacturer has a poor product or picks the wrong price, then the manufacturer has a problem with its retailers that **Leegin** isn’t

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going to fix. You know, they can have all the *Leegin* policies in the world; those retailers are going
to discount that product because it’s the wrong price.

If the manufacturer chooses the wrong distribution system, then you are using resale price
maintenance to, in effect, establish a cartel among retailers because you have this product dis-
tributed to too many retailers, they are all competing with each other to lower prices, and then you
are using this policy to establish a cartel. I submit that’s unlawful in all fifty states. There’s no con-
stitutional problem.

**MR. STEUER:** I’d like to throw out a couple of questions to all of our panelists and give everybody
a chance to comment on them. One that I think everyone will be interested in is this: Occasionally
counsel are accused of trying to game the system when they’re dealing with enforcement agen-
cies. I’d like to ask each of you what some of the worst abuses are that you have seen and what
really gets under your skin.

Sharis, would you like to begin?

**MS. POZEN:** I’m happy to. I think one of the things I’m sure you’ve heard from your folks as well is
we still have parties today who will tell us one thing about their industry or their markets and tell
the EC something different. I don’t think anyone should take for granted that we aren’t talking to
each other, saying, “Did they say this to you and did they say this to you?” I think that’s trying to
game us. Trying to play us one off each other and not allowing waiver so that we can work togeth-
er, thinking that that’s efficient and effective and doesn’t get under our skin, as you say, is fool-
hardy. We used to always say we had pick-up-the-phone relationships with international authori-
ties. In fact, there is now real-time cooperation.

I think, secondly, I’m a big believer that you come in with the facts that support your case and
you come in and you admit your weaknesses. I think that is a much better way to approach us in
trying to convince us of your point of view.

Those would be my tips.

**MR. STEUER:** Chairman Leibowitz, what annoys you?

**MR. LEIBOWITZ:** I agree with Sharis that the best advocates that come before the agency are ones
that acknowledge that they do not have a monopoly on the truth and that there might be argu-
ments on the other side. I think they come off as more credible and ultimately more persuasive.

But I would say as a whole we have a private bar—on both the competition and the consumer
protection sides—that is incredibly talented and very ethical. I think we are fortunate.

**MR. STEUER:** Vice President Almunia, you’ve seen many lawyers from both Europe and the United
States. What is it that gets under your skin?

**MR. ALMUNIA:** I have no particular complaints. I understand the responsibilities and the job of each
other. I know we are not playing in the same part of the field. But these are the rules of the game.

The important issue is our coordination, our cooperation, our dialogue. As I said before and as
Sharis and Jon have just said, we are cooperating very, very well with other competition agencies.
So I think, just in case, we are protected against some kind of bad games that some would try.

**MR. STEUER:** Chairman Chawla, I don’t know how many bad habits competition attorneys in India
have learned from the rest of the world yet, but are there things that you would warn against counsel who appear before your Commission trying?

**MR. CHAWLA:** Richard, just as we are learning on the job, our counsel are also learning by doing. So I think at this stage they can’t be accused of gaming the system. But having said that, our law doesn’t really provide for or encourage an adversarial kind of situation. But sometimes the counsel who appear before us—now, I don’t know whether they have learned this from you or from elsewhere—they sometimes tend to take very aggressive and strong positions, which are not really going to help the way we carry this forward and the way the jurisprudence evolves. So I guess we all will find a way to handle this as we go along.

**MR. DONAHUE:** This is a little bit inside baseball, but the e-discovery—we will hear things like “Oh no, we’re not creating a database of our documents. We have them all on paper.” “Really, 9 million documents you’ve printed on paper? Oh, come on!”

We’ve kind of had this experience where they’ll say one thing to us and then something completely different to the DOJ or the FTC about what format they are in. We know the stuff has been loaded into an electronic database. There are some compatibility issues we might have to deal with. But that’s one thing that gets under our skin. It really drives up our costs too.

**MR. STEUER:** Now, everybody spoke when we opened about some of the accomplishments that you’ve achieved over the past year. But I’d like to ask each of you if you could speak a bit about your top enforcement priorities for the coming year. If I may begin with Chairman Leibowitz?

**MR. LEIBOWITZ:** I’ll just cover a few.

On both sides of the agency, consumer protection and antitrust, technology issues will be in the vanguard. And we will be working together with our colleagues across the Atlantic on technology issues.

On the consumer protection side, we will focus on last-dollar frauds, foreclosure rescue scams, and credit-reduction scams. We have brought dozens of these cases in the last few years. With our partners, the State Attorneys General, we have been involved in more than 400 cases in that area.

On the competition side, health care will continue to be a critically important driver. One issue that we are beginning to consider involves REMS abuses. REMS is an acronym for risk evaluation and mitigation strategies. These are special protections for drugs that are known to have potentially serious risks. They are dangerous drugs, and you want to have additional safety protections. Additional safety protections make sense. But, under the pretext of concern for patient safety, it seems that some of the branded drug companies may be systematically denying potential generic competitors samples of their drugs by claiming that they cannot provide it to the generic drug manufacturer because the generic does not have adequate protection. This is going to be an issue that we are going to be looking at in the future.

You can read about many of these issues in our “Annual Highlights” brochure, which you can link to, with a picture of the four—now we are five—Commissioners, bipartisan, consensus-driven, and collaborative.41

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MR. STEUER: Assistant Attorney General Pozen?

MS. POZEN: For me it will be a smooth transition to my successor.

MR. LEIBOWITZ: We are all delighted that confirmations are moving forward again.

MS. POZEN: It really is trying to ensure—I tried to do that when I started—and I would say probably more of the same. Our compass is set. It’s vigorous antitrust enforcement. That’s what we’re about.

MR. STEUER: Vice President, Almunia, what do you see for the year ahead?

MR. ALMUNIA: Of course, financial services continue to be a big priority, not only because of the restructuring of the banking system in Europe, but also because we are dealing with cases referring to the good functioning of financial markets and financial services. It is extremely important to avoid creating barriers or market positions that will not allow having more sustainable and efficient financial activities in Europe and throughout the world. We are dealing with some antitrust cases referring to financial markets and services, which will be a clear priority for the next twelve months.

The new technologies: The digital world, of course, is always a priority. We have discussed this morning some of the cases and some of the issues that are at the top of our agenda.

Let me recall that we also have a lot of work in Europe with the pharmaceutical sector. We carried out a pharma sector inquiry a few years ago. Probably in the next twelve months some of the cases that emerged after that sector inquiry will require some decisions on our side. I think this would be a very good step forward, always in this sector in very good cooperation with the FTC.

MR. STEUER: Chairman Chawla, what do you foresee for the year ahead in India?

MR. CHAWLA: The main priority I think we will push this year is cartel investigations, some of which are in the pipeline, because that will surely tell us whether we have cut our teeth or not. There clearly are some prima facie kinds of cases which we are looking at, so we should be able to deliver on that. That will, I guess, enhance our confidence and our skills in what we are doing.

Number two, on the antitrust side, we are getting a lot of stray and random information from all kinds of sources. We are in the process of trying to prioritize what sectors or activities we will examine at this point in time so that we get maximum output from the limited kinds of resources and manpower and time that we are able to devote, so that that makes a good impact on the kind of work and perception about the agency. This of course will necessarily have to be within the framework of the legal processes prescribed.

MR. STEUER: Chair Donahue, what do you foresee in state enforcement for the year ahead?

MR. DONAHUE: A couple of things.

One is we have a lot of things in the pipeline in dealing with horizontal core types of conduct—price fixing, bid rigging, that sort of stuff. Some of our attention gets diverted away from that because of all the mergers that we have been dealing with. So I think we need to be more selective in the merger cases that we pursue and really focus on some of our core things, because we
need to bring these other cases forward.

Obviously, health care is going to continue to be a major focus of our offices, in part because it's inherently local, in part because it is very important to our citizens, and in part because in many parts of our states, health care is the biggest industry, by a long shot.

No matter what happens with the health care reform law, those ideas, like accredited care organizations and can you become more efficient about the way you do things, are still going to be there. There is still going to be a need to go and address the cost issues and the access issues involving health care, regardless of what happens here in Washington with the law. That is going to be a major focus of the Attorneys General.

**MR. STEUER:** This has been a tremendously informative panel. Thank you to all of our panelists.
Interview with Alison Oldale, Deputy Director for Antitrust, Bureau of Economics, Federal Trade Commission

Editor’s Note: In July 2011, Alison Oldale was appointed Deputy Director for Antitrust in the Bureau of Economics at the Federal Trade Commission for a one-year term. In this interview with The Antitrust Source, Dr. Oldale discusses competition enforcement in the United States compared to the United Kingdom, the economic analyses that the FTC undertook in several recent investigations and litigations, and the FTC’s priorities in health care markets.

Prior to this position, Dr. Oldale served as the Chief Economist for the UK’s Competition Commission. In addition, Dr. Oldale worked for over ten years as a consultant on antitrust and regulatory matters in Europe and the United Kingdom. Dr. Oldale holds an undergraduate degree from Cambridge University and a Ph.D. in economics from the London School of Economics.

This interview was conducted on April 24, 2012, by Elizabeth M. Bailey for The Antitrust Source.

ANTITRUST SOURCE: You joined the Federal Trade Commission as the Deputy Director for Antitrust in the Bureau of Economics in July 2011. What are your responsibilities in this role?

ALISON OLDALE: Let me start by talking about the role of the Bureau of Economics. I’ll focus on antitrust enforcement. Our input into cases can take a variety of forms. We work with attorneys to develop the theory and evidence during the investigation. The Bureau of Economics (BE) staff makes a recommendation to the Commission about whether to take enforcement action in a case. If the Commission litigates a case, BE will provide economic input and support. In addition, increasingly often the economic expert during trial will be a BE economist. Economists on the investigation team do not serve as trial experts in the same matters and there are procedures to prevent contamination if another staff economist is serving as a litigation expert.

My role is to oversee all this activity. This means I spend a lot of my time working with the staff economists—which I should say is a real privilege. I am sure this is the best group of antitrust economists anywhere. I may also make my own recommendation to the Commission about what action to take in a case. But in any case investigations also involve a lot of coordination with the Bureau of Competition, and with the Commissioners and their offices, so I spend a lot of time working with them as well, on specific cases and on policy and the Commission’s antitrust work more generally.

As a Deputy Director within BE, I am lucky to be part of a great management team of staff managers, Deputies for Consumer Protection and for Research, and of course the Bureau Director (Joe Farrell, when I started, and Howard Shelanski, who is expected to start in July).

ANTITRUST SOURCE: You mentioned there are several other Deputy Directors. How are responsibilities related to economics divided among the different deputy directors?

OLDALE: In addition to antitrust enforcement, BE is involved in consumer protection enforcement. It also conducts background research to learn more about the markets and issues we deal with.
For example, there is ongoing research in the petroleum and in the hospital industries where the Commission has repeated involvement, as well as research on estimating the cost to consumers of pay-for-delay settlements, an issue the Commission has a continued interest in.

The Bureau Director has three deputies to help manage this broad portfolio. I focus on antitrust enforcement. There is a Deputy Director for Consumer Protection who is responsible for enforcement on the consumer protection side. There is also a Deputy Director for Research who coordinates the Bureau’s research work.

**ANTITRUST SOURCE**: Prior to this position at the FTC, you were the Chief Economist for the UK’s Competition Commission. How are your current responsibilities similar or different to the responsibilities in your previous position?

**OLDALE**: My responsibilities at the Competition Commission (CC) and the FTC are very similar in many ways. In both places I was and am the line manager for the economists engaged in antitrust case work and am responsible for generally making sure the decision makers have access to useful and reliable economic advice.

The institutions are slightly different in the way that decisions are made and, I think that one of the consequences is that economists at the Competition Commission play more of a role in driving the theory of the case and the framework used to evaluate it.

**ANTITRUST SOURCE**: What are some other similarities and differences between the FTC and the Competition Commission?

**OLDALE**: As background for any comparison between the FTC and CC, I should say that the Competition Commission in the UK is the second phase body. It reviews mergers and markets only if they are referred to it by the Office of Fair Trading (OFT). And the Office of Fair Trading will make a reference only after it has conducted its own investigation and has uncovered issues that require an in depth investigation.

So in that sense the CC is very different from the FTC. Unlike the CC, the FTC has the difficult task of setting priorities and deciding what cases warrant a detailed review. But to me the most interesting difference between the two bodies is that the FTC mostly makes decisions about litigation, whereas the Competition Commission decides cases. And the Competition Commission has to publish written decisions setting out its reasons.

Quite a lot of things seem to flow from this difference. One is the role of economists. At the FTC there are a lot more lawyers than economists. Whereas at the Competition Commission it’s the other way around: there are a lot more economists than lawyers. I am sure that difference has a lot to do with the fact that the CC focuses on the substantive questions of whether a merger harms competition, for example. These questions involve understanding markets and the likely effects on competition of, for example a change in ownership. And economists have a great deal to say about these things. Now the FTC is obviously concerned with getting the right answer to these substantive questions as well. But it has other concerns. Much of the FTC’s work involves deciding whether cases should be litigated, and preparing and conducting litigation. Needless to say these are much more the preserve of attorneys.

Another effect of this difference is on the evidence base. At the FTC there is more emphasis on the documents and what people said. The Competition Commission focuses more on facts that can be established using market evidence about what actually happened. I suspect this differ-
ence is related to the mechanics of trying cases, the role of witnesses in putting evidence before a court, and the relative level of comfort with economic evidence of a court judge here, compared with the decision makers at the Competition Commission.

And there is also an effect on the way that teams interact and the way that initial decisions about whether to challenge are made. When it gets to the end of its statutory deadlines, the Competition Commission needs to have a written decision setting out the reasons for whatever decision it has made. This reasoned decision can be very long, and the parties and others need an opportunity to comment on drafts of it. This all means that the staff team at the Competition Commission essentially starts drafting on day 1 of an investigation. And they all work on the same document. Debate and challenge about how the case is developing is continuous and differences in view get resolved very quickly. At the FTC the decisions about whether to bring an enforcement action are much shorter with just a sketch of the reasons. Debate happens throughout an investigation, but it’s fair to say that it is more concentrated at the end of the process. And a variety of views can be represented right up to the end. At the end of the day, everyone who wants it gets to put their point of view to the Commission.

**ANTITRUST SOURCE:** Do the economists at the Competition Commission engage in similar economic analyses as those at the FTC?

**OLDALE:** Yes, in many ways it’s the same economic analysis. The issues that we deal with in competition policy are about how markets work, how firms interact, what the incentives of the firms are, and how incentives are changed by the activities of the firms. The economic analysis of these issues is pretty similar no matter where you are.

But there are some differences. Economists at the Competition Commission tend to play the leading role in framing the theory of the case and it is often the economists rather than lawyers who take the lead in conducting interviews and reviewing documents at the Competition Commission.

Also, I think that the level of technical economic expertise at the FTC is greater than you would find on average at the Competition Commission. And economists at the FTC more routinely use a broader range of more technical economics to analyze cases.

**ANTITRUST SOURCE:** Do you think the proposed changes in the UK that would combine the competition agencies provide any lessons for the U.S.?

**OLDALE:** I doubt it. Although there are two agencies responsible for competition in both the UK and the U.S., the similarity stops there. In the UK, it’s more of a vertical relationship. The Office of Fair Trading conducts preliminary investigations of mergers and markets, and if it finds issues will refer them to the Competition Commission for an in depth review. And the OFT does some things the Competition Commission doesn’t do: it investigates conduct cases, and plays a role in consumer protection. The efficiencies we would hope for from a merger in the UK would be mostly vertical efficiencies: better coordination of related activities.

In the U.S., the split between the DOJ and the FTC seems to be more horizontal—the two do very similar things and both see a case through from start to finish. Any efficiencies from a merger here would probably depend more on whether there were benefits from being bigger.

**ANTITRUST SOURCE:** You are the first person coming internationally to hold this position at the FTC. How have you found this experience?
OLDALE: It's been fabulous. As well as being Chief Economist at the Competition Commission in the UK, I have spent many years in private practice, working mainly in Brussels on cases with DG Comp. So I now have experience of three institutions. It's really interesting to see how different institutions can do essentially the same job in very different ways. I have to say, as well, that I have really enjoyed living in Washington.

And I'd like to think it's a useful experience for the FTC as well. Listening to different perspectives is a vital part of good decision making for any competition agency and is one of the strengths of the FTC. I think my different experiences and perspectives, coming from experience of the CC and DG Comp, have added to the mix in a positive way and I hope this has been an experiment that would be repeated not just by the FTC but by other institutions as well.

ANTITRUST SOURCE: You mentioned you worked as a consultant prior to joining the Competition Commission. How does your consulting work inform your work in government?

OLDALE: Seeing the world from the perspective of clients and law firms has definitely helped gain a better understanding of some business realities. I've spent a lot of time talking frankly to a lot of people about how their businesses work and what they were trying to achieve by various actions. This is valuable background for an enforcer trying to understand what is going on in settings where frank discussions can be hard and firms are very guarded, and where we are trying to piece things together from the evidence.

ANTITRUST SOURCE: Let's talk about horizontal mergers. The FTC has had a number of high-profile wins recently, including OSF's proposed acquisition of Rockford Health System and the ProMedica/St. Luke's matter. How have the 2010 Horizontal Merger Guidelines informed those investigations?

OLDALE: Let me start by talking about the Horizontal Merger Guidelines in general. It's broadly right to say there has been no radical change in how we analyze cases arising from Guidelines changes. However, I do feel that there has been some shift in emphasis in the analysis we do engendered by the debate leading up to, and following, the Guidelines revisions. This brought some issues and types of evidence into sharper relief, and some of the FTC's recent cases have highlighted this.

We've just completed the investigation of the Express Scripts/Medco merger.¹ For me, this was a really interesting case. It was very high profile. It started after I came here so I saw the whole process from start to finish. The case itself was challenging and interesting. And it highlights areas of analysis that get greater billing in the revised Guidelines. An initial market share analysis indicated high concentration and suggested that this might be a very problematic transaction. But when we looked at the deal in more detail things weren't so clear. We looked at what customers of one of the merging firms did if they became dissatisfied and switched to an alternative supplier, and found that they rarely went to the other merging firm. The parties were not particularly close competitors, and notwithstanding the large market shares, unilateral effects were not likely.

The Graco/ITW matter was also very interesting.² This was a merger of manufacturers of com-

ponents for industrial spray painting. There are lots of small components that go into industrial spray finishing lines and the components are highly differentiated. Market definition here was potentially messy. If you read the complaint you’ll see that the Commission dealt with this by avoiding a detailed identification of the narrowest markets—as the revised Guidelines emphasized we might sometimes do. Instead of using market definition and shares as the starting point for our analysis we focused more directly on effects, which was much more straightforward in this case.

We had data that allowed us to look fairly directly at the switching behavior of customers between the two merging parties, and this showed significant switching within some product categories. You can see this emphasis in the way the complaint is written, with the analysis of effects first and of market definition second.

But there is still work to do. One case where the revisions clearly hadn’t percolated through enough was Lundbeck, a case the FTC notoriously lost. The case was about a merger of suppliers of the only two drugs for a particular serious pediatric condition. A key piece of evidence in the judge’s opinion revolved around asking a small sample of doctors what they would do if the price of one of the drugs rose. The judge noted that only 1 in 8 of the doctors said they would switch to the other drug, which showed the price elasticity was low, and concluded that drugs were not in the same market. But the real point was that no doctors at all said they would switch to surgery or stop treating the condition. In other words the only alternative to paying the higher price that doctors mentioned was switching to the other drug. So while the elasticity was low, the diversion ratio was really high. And the guidelines emphasize that it is diversion ratios that are most relevant for understanding merger effects.

I do also want to talk about the recent success in the Rockford case because, obviously, it’s important. This was a case where the FTC challenged a hospital acquisition in Rockford, Illinois, got a preliminary injunction, and the parties dropped the deal. It was an important win, particularly given the current rush to consolidation in health care—it shows the FTC is watching and will challenge anticompetitive mergers that are likely to lead to high prices to payers. But our success there was not really a reflection of the revised merger guidelines. The economists in BE have deep expertise at analyzing the effects of hospital mergers, and this was a critical factor in winning the case.

**ANTITRUST SOURCE:** Are there unique features of the health care industry that affect the types of economic analyses that the FTC performs compared to other industries?

**OLDALE:** There isn’t anything particularly unique about the analysis that we do in the health care industry. It’s true that we tend to do quite a lot of empirical analysis in hospital mergers, but that is due to a combination of things. First, it can be more important than in some other cases because location really matters for how closely different hospitals compete, and basing the analysis of effects on defining geographic markets can be very unreliable in those circumstances. Second, it’s possible to do a more direct analysis of how closely the merging hospitals compete because good data are available. And third, we know just what to do with the data. We have looked at quite a few hospital mergers now and can build on what we’ve done in previous research and in past investigations.

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3 FTC v. Lundbeck, Inc., 2010-2 Trade Cas. (CCH) ¶ 77,160 (D. Minn. 2010), aff’d, 650 F.3d 1236 (8th Cir. 2011).
4 FTC v. OSF Healthcare Sys., 2012-1 Trade Cas. (CCH) ¶ 77,850 (N.D. Ill. 2012).
That said, there really is nothing unique that we do in analyzing hospital mergers. We do merger simulation in those cases and we do merger simulation in other cases. We calculate a form of diversion ratios in hospital cases and we look at the diversion ratios in other cases. We look at efficiency issues in hospital mergers and we evaluate efficiencies in other cases.

ANTITRUST SOURCE: What are some of the health care-related antitrust issues that are at the top of the FTC’s agenda?

OLDALE: Pay for delay, or reverse payments, in pharmaceuticals remains a very active area of interest at the Federal Trade Commission. I’ve seen quite a few of these cases now and I am amazed at the complex agreements that rivals enter into in relation to the supply of generics. We will carry on scrutinizing these to make sure they don’t frustrate the benefits of generic competition.

We will watch the effects of accountable care organizations with interest.

ANTITRUST SOURCE: How does the FTC think about the potential for accountable care organizations (ACOs) to raise competitive concerns?

OLDALE: The Federal Trade Commission along with the Department of Justice’s Antitrust Division published a policy statement talking about ACOs. And this makes it clear that the introduction of ACOs doesn’t herald a revolution in thinking on the basic principles of antitrust or merger control. We acknowledge the potential for ACOs to generate important efficiencies, but also the potential for agreements between competitors in the same market to harm competition and customers. As ACOs start to operate we will gather evidence so we can see how they are working out in practice.

ANTITRUST SOURCE: A number of the FTC’s horizontal merger challenges recently have been against consummated mergers. The transaction between ProMedica and St. Luke’s is one such example. What types of economic analyses are useful in evaluating a consummated merger?

OLDALE: The big advantage of consummated mergers is that you’ve got a natural experiment and, in some cases, you can actually look to see whether the merger led to a change in prices or resulted in some loss in competition in another dimension. But it’s important to keep in mind that this should not be transformed into requiring evidence of actual effects in order to challenge a consummated merger. We might lack evidence of actual effects, even if they were there, for any number of reasons, including that the data may not be available or the experiment is not sufficiently clean and our empirical techniques are not sufficiently strong to pick up effects. Also, importantly, the parties may be strategically holding the price down. For these reasons it would be wrong to rely only on an empirical analysis of the natural experiment. Rather, we need to bring to bear all the other evidence of the case that we would have collected and all the analysis that we would have done if the merger were being investigated ex ante and hadn’t been consummated. The abil-

ity to do the natural experiment as well is just an additional source of information that might help us refine our decisions.

**ANTITRUST SOURCE:** From an economic perspective, are there particular analyses that you tend to find informative as to likely competitive effects of a potential transaction?

**OLDALE:** This is a tricky question because the truth is that I don’t think that we can afford to be choosy. Evaluating a merger is a very difficult and tricky exercise. We try to use whatever we can to provide information about the likely effects, to forecast the but-for world of the future with the merger and without the merger. Cases differ dramatically in what sort of evidence is available, in the institutional features of the markets involved, and in whether price information is reliable. They differ in what the parties have said in their strategic documents and how persuasive that is. So really there are no rules about what evidence is persuasive and what is not in a particular case.

In some of the cases I talked about earlier we had good evidence about what customers did when they switched suppliers, and that evidence was very helpful in understanding the competitive dynamics of the market. There are other cases where internal documents have been really key. In another recent case an analysis of what happened when there was entry was very important. We take what we can get.

**ANTITRUST SOURCE:** How, if at all, have FTC economists incorporated behavioral economics into their approach to merger matters?

**OLDALE:** Behavioral economists are clearly correct in saying that people and firms are not the perfect decision makers using perfect information that they are portrayed to be in many economic models. But alternative models that incorporate better assumptions about behavior and which give us useful ways to understand the likely effects of mergers, or particular types of conduct, aren’t there yet. And in the meantime our existing models give us workable approximations. So we haven’t done much yet, but we’ll keep watching developments.

For myself, I wonder whether the first place behavioral economic analysis might be brought to bear on antitrust enforcement will be in areas like coordinated effects or exchange of information. These are areas where our existing theories are not very helpful. For example when looking at coordinated effects in merger control the standard approach focuses a lot on incentives to coordinate. But there are lots and lots of markets where firms have an incentive to coordinate but they don’t seem to be doing so. So it seems there is a big piece of the puzzle that we are missing, and perhaps behavioral economics will be able to tell us something about what to look at in order to get a better handle when coordination is likely in practice.

**ANTITRUST SOURCE:** Tell us about the research conducted by the Bureau of Economics.

**OLDALE:** BE economists conduct research in many different areas—as you can see from a quick look at the FTC website where you can find our working papers. But if I were to comment on areas of focus, I’d want to mention retrospectives. We have published some really important studies of the effects of mergers, especially amongst hospitals. Our research here was directly responsible for reinvigorating enforcement.

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6 FTC Bureau of Economics working papers are available at [http://www.ftc.gov/be/econwork.shtm](http://www.ftc.gov/be/econwork.shtm).
Which brings me to health care generally—a real area of focus for our research. We have investigated the effects of pay for delay agreements for example, and I mentioned our analysis of hospital mergers. We continue to develop our research agenda here.

Another area of particular interest is IP. The FTC has published reports on standard setting, and we are always on the lookout for ways to learn more.

Thinking more about antitrust policy, I have been particularly interested in my time at the FTC in exclusive dealing, where the Commission has been quite active in investigating cases recently. Analysis of exclusive dealing is a tough area because the economic analysis is very complicated and doesn’t lend itself to easy generalizations and rules. But we still need to give advice on matters. Economists here in the Bureau have been working hard to improve our understanding of the issues.

I have also been interested in how antitrust agencies should view supply contracts. These seem to be coming up as complicating issues in a number of pharmaceutical cases. How should we view these? As a remedy for competition problems? As a way firms can use to suppress competition?

**Antitrust Source:** Is there a bright line for thinking about when exclusive dealing arrangements are likely to be anticompetitive?

**Oldale:** Very tricky. Not yet, but we are working on it.

**Antitrust Source:** Thank you. We really appreciate your taking the time to talk with us today.
Managing the Risk of Tagbacks to Leniency Applicants in Cartel Investigations

Michael G. Egge and Alexandra L. Shandell

The leniency program of the U.S. Department of Justice's Antitrust Division and those modeled after it by other jurisdictions provide incentives in the form of both carrots and sticks to companies to disclose cartel conduct. The “leniency-plus” program provides incentives and rewards for companies already under investigation for involvement in one cartel to self-report participation in different cartel conduct, i.e., to disclose new cartels to the enforcement agency. Yet where a leniency-plus applicant reports a conspiracy involving new product areas (whether or not closely related to those covered by the original leniency application), the original leniency applicant risks being “tagged back” by the leniency-plus applicant. This risk threatens the balance of interests between the original leniency applicant and the enforcement agency, and has the potential to disrupt an otherwise mutually beneficial relationship, particularly where the leniency-plus applicant reports a conspiracy involving a product or product area closely related to the original leniency application.

Overview of Leniency and Leniency-Plus Programs

United States. In the United States, the Antitrust Division of the Department of Justice offers, under certain conditions, complete amnesty from criminal conviction and fines to the first company to identify itself as having participated in a criminal antitrust conspiracy. To obtain amnesty, a conspirator must be the first to report the conduct and must cooperate in the DOJ's investigation and prosecution of the other members of the conspiracy. The applicant must provide the DOJ with sufficient information about the industry and the conduct to demonstrate (1) that a criminal antitrust violation has occurred, and (2) that the conspiracy is not one for which there has been a previous amnesty applicant. The applicant must also show that it has taken all necessary steps to ensure that it has promptly and completely ceased participation in the cartel.\(^1\)

The DOJ provides the first applicant to come forward with a marker,\(^2\) protecting its status as “first in” and allowing the applicant a period of time in which to “perfect” the marker. To do so, the applicant must further elaborate on the criminal conduct reported to ensure that it meets the requirements of the DOJ's Corporate Leniency Policy and demonstrate to the DOJ its willingness to cooperate. During this period, the applicant has the opportunity to conduct an internal investigation to identify the full extent of its involvement in the conspiracy. The applicant will then prof-

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\(^2\) A marker, memorialized in a letter issued by the DOJ, serves to block later applicants from seeking to obtain leniency for conduct that the initial applicant has already disclosed to the DOJ. The marker holds the first applicant's place while it gathers evidence to support its initial representations to the DOJ regarding the conspiracy.
fer evidence to the DOJ to define the “scope” of this conduct, for which the DOJ will grant the applicant conditional amnesty. The DOJ usually defines the scope of the conduct simply by the products or the industry coordinated by the cartel. A conditional amnesty letter then memorializes the relevant scope of conduct and assures applicants amnesty from prosecution for the extent of the described conduct, assuming the applicant’s full compliance with its cooperation obligations. The successful applicant eliminates its criminal exposure, including corporate criminal fines, entirely. Should the applicant fail to satisfy its cooperation obligations, the conditional amnesty may be revoked. The DOJ states that only one out of over 100 conditional amnesty letters has ever been revoked.³

In 1999, six years after implementing the present iteration of the amnesty program, the DOJ’s Antitrust Division introduced the first leniency-plus program (referred to in the United States as the “amnesty-plus” program).⁴ The leniency-plus concept is fairly straightforward and simple: where a firm that has been identified as a participant in a cartel for which the amnesty position is no longer available (i.e., when someone else has already ratted the firm out), that firm can secure a significant discount from the criminal fine the DOJ recommends to the court for participation in the original cartel if it is the first to provide information to the DOJ on a new cartel outside of the scope of the first-reported conspiracy.⁵ It is called “leniency plus” because the leniency-plus applicant, if successful, gets full immunity from sanction in the second-reported conspiracy as well as a recommendation of a discount on penalties for its participation in the first-reported conspiracy—the “plus.” The discount on the fines arising from the first-reported conspiracy will be greater than if the leniency-plus applicant had only cooperated in the investigation of the first-reported conspiracy.⁶ This discount, as with any general discount for cooperation, is applied as a recommended reduction to the applicable sentencing guidelines for the conduct.

On the flip side, companies under investigation for participation in a cartel that do not disclose their participation in separate cartels can be subject to “penalty plus” once those other cartels are uncovered. Then, where a company fails to disclose additional anticompetitive conduct, depending on the circumstances, the DOJ will recommend a much higher starting point for the sentencing guidelines range than the company would otherwise receive.⁷

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⁴ The U.S. leniency-plus program is called “amnesty plus” in the United States because of the unique features of the U.S. cartel enforcement regime, most importantly, that cartel conduct is enforced criminally. Given that most other cartel enforcement regimes refer to amnesty plus as “leniency plus,” we use “leniency plus” to refer to the U.S. amnesty plus program.

⁵ Hammond & Barnett, supra note 3, at 8–9.

⁶ Id.

Tagbacks in the Leniency Regime. When a company elects to take advantage of the leniency-plus program, it necessarily must identify its co-conspirators in the second cartel for which it seeks leniency. One of the co-conspirators identified in the second cartel could sometimes be the leniency applicant in the first cartel. This situation is a tagback because the identification of cartel participants in the first application—the “tag”—has set off a chain of events, informed by powerful incentives, resulting in the first cooperator being “tagged back” as a co-conspirator in the second cartel. 8

There are several varieties of tagback scenarios, some more serious than others. Tagbacks may be aptly categorized in much the same way as burns to the human skin: in degrees. Likely the most serious tagback scenario—one creating first degree burns—is where the leniency applicant is clearly the first mover in reporting wrongdoing in a given industry anywhere in the world. That applicant delivers to the DOJ a conspiracy as to a particular product in an industry where there are a range of closely related, but distinct, products offered by suppliers. As is often the case in this setting, cartel conduct may not be limited to the one reported product so the investigation of the first cartel leads, whether aided by leniency applications or not, to discovery of multiple cartels covering different product markets.

In short, the first mover produces the proverbial “whale” to a regulator: a conspiracy that allows the regulator to discover and prosecute a series of separate conspiracies involving related cartel conduct across the industry. The first degree burn results from the first mover’s getting tagged back, through leniency plus granted to another cartel participant, early in the game, and perhaps more than once. In this scenario, the first mover does not enjoy to the fullest the advantages of having been first in, even though the first mover is arguably responsible for the discovery of every cartel identified thereafter. Second and third degree burns would be tagbacks materializing among parties removed from the first mover, with differences in degree turning on how far they are removed. First-degree tagbacks raise the most acute potential for leniency policy disruption. 9

Adoption of Similar Leniency Concepts in Other Jurisdictions. After the DOJ implemented its revised amnesty program in 1993, several jurisdictions observed its success and implemented similar leniency programs modeled on the DOJ’s approach. These leniency programs at times vary in their approaches. All, however, follow the philosophy that to bust cartels, agencies need to give participants incentives to come forward by providing a sufficiently transparent and predictable system that includes (1) guaranteed immunity from penalty and (2) severe penalties for non-disclosure or non-cooperation.

8 Notably, the hypothetical example provided by the DOJ in its Leniency Program FAQs does not involve a tagback. In other words, the initial amnesty applicant was not a participant in the second cartel. Hammond & Barnett, supra note 3, at 9. Indeed, it is unclear whether a tagback has occurred in the fashion we describe in the United States. Yet it is undeniable a situation like that could arise, given the balance of interests at play.

9 There are also different types of tagbacks. A cross-jurisdictional tagback would be where the first mover only moves first in one jurisdiction but fails to think about or act quickly enough in other jurisdictions. Once the first mover has triggered an investigation in one jurisdiction, the other cartel participants secure first-in leniency status elsewhere without having to count on leniency-plus opportunities. It is a stretch to ever rate this scenario as a first degree burn, at least from a fairness perspective, given the evolution of global cartel enforcement and defense practices. In short, the tagback in this instance is the first mover’s own fault. Another type, at least in theory, is a temporal tagback, where the first mover only secures the full immunity position for a specific period of time and a co-conspirator tags the first mover back for the same product but a different period of time. Finally, there is the “different customer” tagback where the original leniency position was defined by price fixing or bid rigging as to a particular customer only, and a co-conspirator secures leniency-plus protection for related conduct as to other customers for the same products.
For example, the European Commission of the European Union, which issued its new Leniency Notice in 2002 and revised it in 2006, offers complete immunity from fines for participation in an illegal cartel to the first company to report the conduct and provide evidence of the cartel. As in the United States, the EC issues the first applicant a marker during which that company may conduct an internal investigation and proffer evidence to achieve a grant of immunity. The applicant must fully cooperate and immediately take steps to end its participation in the cartel.

Unlike the United States, however, leniency applicants to the EC who are not first in may still qualify for a guaranteed reduction in fine if they cooperate and provide “added value” to the investigation. The Leniency Notice specifically states that the first to come forward after the immunity winner will be entitled to a 30 to 50 percent discount on its fines; the second, a 20 to 30 percent reduction; and the third, a reduction up to 20 percent. (This is distinguishable from the DOJ’s assertion that second-in cooperators will receive a discount on their criminal penalties. Although the DOJ’s policy is to recommend a reduction in the sentencing guidelines, the second-in company must still plead guilty to the conduct and its penalty will be subject to the sentencing judge’s discretion.)

While the EC’s 2006 Leniency Notice does not expressly contemplate either leniency-plus or penalty-plus programs, it is possible that reporting and thereby qualifying for full immunity regarding a different cartel could help secure the maximum discount available to a second- or third-in leniency applicant in the original reported cartel.

Canada’s immunity and leniency programs operate in much the same way as the U.S. amnesty program. Canada’s Competition Bureau offers immunity from prosecution to the first to disclose anticompetitive conduct. Companies and individuals who are not the first to report can still receive a recommendation of leniency from the CCB—in the form of a discount—if they cooperate in the investigation. The CCB offers “immunity plus,” to later applicants who are eligible for leniency for a particular offense if they disclose evidence of an additional anticompetitive criminal offense. Under the immunity-plus program, the immunity-plus applicant must meet the requirements of the immunity program for the new conduct. The immunity-plus applicant will then be eligible for immunity for the new conduct, plus an additional discount for its cooperation in the original offense—typically an additional 5 to 10 percent.

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12 Id. at 18.
13 Id. at 20.
15 EU courts have established a doctrine of non-discrimination, under which parties in comparable situations must be treated equally within a case. See Case T-311/94, BPB de Endraacht v. Comm’n, 1998 E.C.R. II-01129. This doctrine may limit the availability to the enforcement agency of expressly granting more lenient treatment to a company in one matter for its cooperation in another, so as to avoid linking cases together and potentially violating the non-discrimination principle.
In Canada, a tagback is, at least in theory, considerably more costly than in the United States. To qualify for immunity in Canada, the applicant must disclose “any and all” competition offenses in which it may have been involved.\(^\text{18}\) By definition, a tagback means the first immunity applicant failed to disclose anticompetitive conduct in which it was involved. Thus the first immunity applicant risks not only higher penalties for that second cartel, but also the loss of immunity for the original conduct. For this reason, the CCB asserts it need not implement a “penalty-plus” program like the United States applies.\(^\text{19}\)

Brazil, too, has implemented a leniency program to reward the first participant in a cartel to come forward to the Secretariat of Economic Law of the Ministry of Justice (SDE). Under the leniency program, successful applicants are granted immunity from administrative sanctions and fines as well as criminal prosecution. As in the other jurisdictions described, the SDE requires that the applicant be the first to come forward to disclose information about the anticompetitive conduct and to cease its participation in the cartel.\(^\text{20}\) The SDE also offers leniency-plus benefits to applicants who do not qualify for leniency in the prosecution of the first cartel disclosed. When a leniency-plus applicant comes forward with information about a second cartel that otherwise meets the requirements of the leniency program, the company is entitled to immunity for the second cartel as well as a one-third reduction in its fines for the first cartel.\(^\text{21}\)

Leniency Policy Incentives and Tagback Risk

At the American Bar Association’s Antitrust Law 2012 Spring Meeting, Scott Hammond, Deputy Assistant Attorney General for Criminal Enforcement at the Antitrust Division, acknowledged that tagbacks, although rare, present a real risk for amnesty applicants. Hammond stated that he had observed only one tagback in the last ten years, but was quick to validate that firms have good reason to be concerned and to protect themselves.\(^\text{22}\)

Applicant Incentives. Leniency programs are specifically designed to maximize incentives to self-report and cooperate by pitting co-conspirators against one another in a race for protection against massive fines and, at least in the United States, reduced exposure to what can be enterprise-threatening private damage liability.\(^\text{23}\) They are (or should be) grounded in transparency and predictability, providing the cartel participant certainty that it will receive the carrot of full criminal immunity in exchange for simply cooperating and telling the enforcer what it knows. The alternatives, of course, are harsh fines and ruinous private damage exposure, if caught.

Enforcement agencies expect that, rather than face this risk of sanction and continue their conduct, cartel participants will cease their illegal activity and self-report in exchange for a free pass avoiding sanction. The risk of discovery and punishment is enhanced by the possibility that other

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\(^\text{21}\) Id. at 24; see also art. 35-B, ¶ 8, Law No. 8.884, June 11, 1994, as amended by Law No. 10,149, Dec. 21, 2000 (Braz.).


\(^\text{23}\) Leniency applicants in the United States that have fully met cooperation obligations may avoid joint and several liability or treble damages; their civil damage exposure is limited to their share of single damages assuming they cooperate with the civil plaintiffs. See Antitrust Criminal Penalty Enhancement and Reform Act of 2004, Pub. L. No. 108-237, § 213(a)–(b), 118 Stat. 661, 666–67.
co-conspirators may seize the opportunity and take the one and only pass available. This destabilizing effect can be profound as cartel participants struggle to meaningfully risk-adjust for the likelihood that the cartel will be detected and punished. The DOJ’s relatively simple enhancements to the transparency and predictability of its leniency policy in 1993 triggered a staggering increase in applications and, in turn, guilty pleas for cartel conduct. Once accepted into the program, all of the benefits are conditioned on full cooperation. The applicant has every incentive to carry through with cooperation and protect its position.

Leniency plus generates even greater incentives to report new conspiracy conduct. First, once the first mover has struck with an application in a given industry, the odds of the DOJ’s detecting cartel conduct involving other products by any of the co-conspirators increase significantly even without further leniency applications. The DOJ or any other skilled enforcer will have access to documents and people and will do all it can to leverage the application to investigate conduct related to other products whether in the same or separate industries. The heightened risk of detection helps push the co-conspirator to consider leniency plus.

Second, leniency plus offers greater incentives than the leniency program itself because of the incremental discount the successful leniency-plus applicant receives off its fine for the first conspiracy, in addition to the full immunity it gets on the second conspiracy.

Third, there is the prospect of simple, sweet revenge against the first mover. While revenge is a rather base human motivation that is difficult to rationalize commercially or economically, regulators fully understand that humans run businesses. Leniency plus feeds nicely on the desire for revenge.

Fourth, given the above three factors, the race for leniency over whatever cartel conduct exists in the industry that is not already under investigation becomes incrementally more intense than if there had been no leniency applications within the industry. The gloves are officially off.

Finally, the first mover’s application will trigger a highly invasive internal investigation at each co-conspirator. For many firms, it is efficient to simply expand the investigation to the entire company and all product lines.

These enhanced incentives have returned remarkable results. The DOJ asserts that more than half of its cartel investigations arise as leniency-plus disclosures resulting from investigations of separate cartels.

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24 In addition to the incentives for a company to be first in, there are still benefits available to encourage a co-conspirator to cooperate as the second, or later, in line. A later-in-time cooperator may be able to narrow the scope of the conduct for which it is prosecuted, earn a discount in its criminal fines for its conduct, and minimize the number of “carve-outs” for culpable executives from the company’s plea deal, thereby ensuring that as few individuals as possible are subject to prosecution. Hammond, supra note 7, at 3–10.

25 The leniency application is not public, and does not normally become known until either the leniency applicant makes it public or it becomes known later through civil litigation discovery or mere deduction from guilty pleas and other enforcement action. Once an application is made, however, it triggers or advances an investigation, which the DOJ eventually makes overt through the execution of warrants and/or issuance of grand jury subpoenas.

26 For example, it will ask the infamous “omnibus question” of every witness from the applicant, and at every opportunity: whether the witness knows, under penalty of losing amnesty protection or obstruction of justice or both, of any cartel conduct in any industry and at any time. Scott D. Hammond, Cornerstones of an Effective Leniency Program 15–16 (Nov. 22–23, 2004), available at http://www.justice.gov/atr/public/speeches/206611.pdf.

27 As discussed later, co-conspirators in the earlier-reported conspiracy will generally discover that they have been tagged through one of two ways: The DOJ may decide at some point to take the investigation public or the co-conspirator may itself come forward as a leniency applicant and learn that another company has already secured a marker for that conduct.

28 Hammond, supra note 3, at 9–10.

29 Hammond, supra note 26, at 9.
Enforcer Incentives. The enforcement agency's primary interest is to identify cartel conduct and gather sufficient evidence to successfully prosecute as many cartels as efficiently as possible. Investigating and prosecuting conspiracies is extremely difficult work. Leniency programs dramatically reduce that burden by not only identifying the existence of cartel conduct (in short, telling the agency where to look) but also by producing invaluable admissions and eyewitness accounts of conspiracy and other powerful evidence, without requiring the agency to lift a finger. The evidence is so powerful that the DOJ rarely has to try a cartel case. Co-conspirators routinely plead guilty in the wake of a leniency application. Given these benefits and results, enforcers have a powerful incentive to make leniency and leniency-plus as widely available as possible.

Nonetheless, even with a leniency applicant, the DOJ has to follow through on the investigation and prosecution, which is no easy task. The DOJ's track record in trying cartel cases, even with the benefit of leniency applicants and other cooperators, is not perfect. And while the DOJ can leverage the leniency application process into requiring the applicant to conduct a full internal investigation and produce its fruit, it is ultimately the DOJ's job to convert the leniency application into guilty pleas or convictions. The DOJ therefore has great interest in developing a strong relationship with leniency applicants so that the DOJ can best harvest, understand, and assimilate the information it receives from each applicant. It generally does not want to do anything that will alienate applicants or cool the pace and quality of cooperation.

Further, the DOJ has a strong incentive not to disrupt the transparency and predictability of the leniency program. An applicant needs to know that it is going to be treated fairly and that by coming in and cooperating, it will be given every opportunity to remain protected from prosecution. Any perceived unfair treatment by the DOJ will necessarily shake the applicant's trust in the program.

The Destabilizing Impact of Tagbacks. These incentives demonstrate a powerful alignment of interests between leniency applicants and enforcers. Both want the relationship to be mutually beneficial—the applicant wants to preserve its protection and avoid the DOJ's being anything but pleased with its cooperation (since a perceived failure to cooperate puts the applicant's protection in jeopardy). The DOJ, for its part, wants the applicant to provide high quality, reliable information and wants to trust the applicant to thoroughly investigate any and all wrongful conduct. Any

30 See, e.g., United States v. Dutton, No. 3:02-cr-00220-RLV-1 (W.D.N.C. Jan. 12, 2004) (acquittal of NanYa employee Bradley Dutton in a case where the DOJ had the benefit of an amnesty applicant and a second-in-cooperator who pleaded guilty); United States v. Kim, No. 4:06-cr-00692-P-JH-3 (N.D. Cal. Mar. 21, 2008) (acquittal of DRAM employee Gary Swanson under similar circumstances). Following Dutton, the DOJ subsequently shut down its investigation of the other two implicated firms in the four-firm polyester staple market.

Most recently, a federal jury returned split verdicts in AU Optronics, finding AU Optronics, its U.S. subsidiary, and two executives guilty of conspiring to fix prices of liquid-crystal display panels (LCDs), but acquitting two more individuals, and resulting in a mistrial for failing to reach a verdict with respect to one individual. See Press Release, Department of Justice, Taiwan-Based AU Optronics Corporation, Its Houston-Based Subsidiary and Former Top Executives Convicted for Role in LCD Price-Fixing Conspiracy (Mar. 13, 2012), available at http://www.justice.gov/atr/public/press_releases/2012/281032.pdf. Samsung Electronics Co., Ltd., and its subsidiaries obtained leniency for their cooperation with the DOJ in providing information about the LCD cartel. Several other LCD suppliers subsequently pled guilty as well. But AU Optronics went to trial, and, despite the cooperation of Samsung and others, the DOJ failed to obtain a guilty verdict for three of the five individuals indicted. United States v. AU Optronics Corp., No. 3:09-cr-00110-SI (N.D. Cal. Mar. 13, 2012) (Document # 851, Special Verdict Form, and Document #852, Transcript of Proceedings).

31 Indeed, the DOJ asserts that where an internal investigation reveals illegal conduct not covered by the scope of the conditional amnesty letter, the original applicant is, in most cases, provided expanded coverage by an addendum to the letter so long as that entity meets the criteria for amnesty on that conduct and continues to fully cooperate. See Scott D. Hammond, When Calculating the Costs and Benefits of Applying for Amnesty, How Do You Put a Price Tag on an Individual's Freedom?, Remarks at the Fifteenth Annual National Institute on White Collar Crime at 4 (Mar. 8, 2001), available at http://www.justice.gov/atr/public/speeches/7647.pdf.
disruption to this alignment threatens to doom the relationship and, in some circumstances, potentially impair the transparency and predictability of the leniency program altogether.

The greater the threat of a tagback to a leniency applicant, the greater is the likelihood that the balance of interests between the applicant and the agency will be disrupted. Take, for example, a leniency applicant that has received a marker from the DOJ for a range of products and, in the short time allotted to it under the marker, perfects the marker as to some, but not all, of the products in the range covered by the marker. Suppose also that there are other closely related products within the same industry, which are manufactured and sold by the applicant but are not covered by the marker, yet there are no cartel investigations involving this industry anywhere else in the world. Under these circumstances, the DOJ would give the applicant a conditional amnesty letter that covers the products for which the DOJ believes the applicant has perfected its marker.

At this point, tagback risk to the leniency applicant is relatively low because the investigation has yet to become public and no one else knows they have been tagged. Cartel participants learn that they have been tagged either when they come forward to seek amnesty and find out that a co-conspirator has already secured a marker for the conduct or when the DOJ decides to make the investigation public.

The moment the DOJ investigation becomes public, however, tagback risks increase dramatically as targets quickly learn the amnesty position is taken and start to think about leniency-plus opportunities. In this hypothetical, those opportunities are ripest for products not covered by the original marker but they also exist for the remaining products covered under the marker that were not included in the conditional amnesty letter, at least to the extent that the DOJ does not extend the marker letter.

This situation creates a dilemma for the DOJ because it wants to identify cartels not covered by the first mover's conditional amnesty letter. The DOJ may believe that, having already given at least some opportunity to the original applicant to perfect the marker for the other products covered by the marker and to conduct an internal investigation for all other related products, the leniency-plus candidates may be in a position to provide better information on the related product lines. But if the DOJ allows a tagback in this situation, it could leave the initial applicant materially worse off through no fault of its own (apart from simply running out of time to perfect its marker for the other products or secure additional markers). The DOJ arguably would be responsible for creating the tagback risk in the first place by going public in an investigation that would not have happened but for the first-mover's application. An acceptance by the DOJ of a leniency-plus position that allows a tagback under these circumstances, where the DOJ does not first give the first-mover applicant the opportunity to seek protection for the products covered under the leniency-plus application, would be perceived as grossly unfair by the first-mover applicant. The first-mover applicant, feeling double-crossed, would surely fight any indictment on whatever grounds possible (e.g., detrimental reliance). Moreover, that applicant may cease its cooperation. Most importantly, however, the applicant—and all observers—will have lost confidence in the predictability of the system.

The DOJ can mitigate this risk by giving the first-mover applicant ample opportunity to protect itself. This is done by communicating areas of potential concern to the first-mover applicant and giving that applicant a chance to investigate and secure protection, either by marker or conditional

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32 There does remain nonetheless a risk that any cartel associated with the products not covered by the marker provokes an independent leniency application by another firm.
amnesty letter. Broad deference should be the rule for first-mover applicants lest the leniency-plus program ultimately undermine the foundations of the leniency program—transparency and predictability. In short, as a policy matter, the leniency program should have priority over the leniency-plus program. The first-mover applicant can also mitigate tagback risk by doing everything in its power to investigate and secure prompt protection, by marker or otherwise.

The DOJ appears to acknowledge the destabilizing effects tagbacks can have on the success of the amnesty program by giving first-mover applicants wide berth to protect themselves against tagbacks. In his 2012 ABA Antitrust Section Spring Meeting remarks, Hammond explained that to enable applicants to avoid tagbacks and to fully incentivize information sharing, the DOJ does attempt to grant broad amnesty to the initial applicant.33 Hammond acknowledged the temptation presented to the DOJ when other companies or co-conspirators come forward offering additional information that the initial applicant has not provided. He stated that the DOJ makes an effort to avoid this temptation by offering the initial applicant the opportunity to investigate the same information. Hammond confirmed that the DOJ does not want to allow co-conspirators to tag back first-in applicants.

Responsibility for avoiding tagbacks, however, does not rest solely on the DOJ. When the DOJ says it gives ample opportunity for the amnesty applicant to investigate whether it participated in cartel conduct for other products revealed by an amnesty-plus request, it is also conveying that the original amnesty applicant must do its part, investigate, and report to expand the scope of its amnesty protection.

**Mitigating the Risk of Tagbacks**

Given the risk that tagbacks pose to the original leniency applicant, the leniency applicant must take steps to ensure that it does not fall victim to the disclosures of a former co-conspirator.

**Secure as Broad a Marker as Possible from the Outset.** A marker blocks a leniency-plus position, and hence a tagback. The applicant should seek a marker that will cover as much of the company’s product line as possible. Once a company has secured a marker, enforcement agencies are reasonably amenable to extensions so long as the applicant demonstrates it is investigating and being diligent about cooperating and perfecting its marker for all products. A narrowly construed marker leaves room for a co-conspirator to enter into the surrounding space and seek leniency for related conduct through the leniency-plus program.

Thus, in negotiating the marker language with the DOJ, the applicant should seek to use broad and inclusive product definitions that capture any product markets that may have been touched by collusive activity. In defining the product scope, the applicant should consider both the specific products at issue as well as the greater system of which those products and any related components may be a part. The applicant should seek an inclusive marker definition, rather than seek a marker for specific products.

**Understand the Clock.** Leniency applicants have a timing advantage and should use it. As discussed above, tagback risks materialize once a co-conspirator learns of an investigation. That can occur by the co-conspirator’s seeking a marker on its own and learning that one is not available, or once the enforcement agency issues subpoenas, or the investigation is made public. An applicant cannot control when a co-conspirator presents itself for leniency on its own before the investigation becomes public, but it can understand when the agency is likely to go public with its

33 Hammond, supra note 22.
investigation, and develop a plan for investigating related products not covered by the conditional amnesty letter or the marker.

**Be Prepared to Investigate Comprehensively.** A leniency applicant needs to factor into its application decision the total life cycle costs of its application, and that must include expending considerable resources investigating products that are not covered within the scope of its protection.

**Prioritize Internal Investigation Targets Based on Tagback Risk.** A leniency applicant should be able to figure out the sources of any tagback risk. Co-conspirators are known, so a leniency applicant should prioritize its investigation by focusing on business lines that overlap with co-conspirators (and that are not otherwise covered by the applicant’s leniency application) because that is an obvious point of tagback exposure. The leniency applicant should carefully examine all product markets in which it operates and in which each of its co-conspirators operate. Tagback risk exists in any market where there is overlap between the two companies involved in a cartel because this is where the greatest incentive is for co-conspirators to hunt down collusive conduct and report to the agency in an attempt to reap the rewards of the leniency-plus program. The risk is thus greater where the companies at issue are diversified-product companies selling a variety of related and non-related products.

**Build a Trusting Relationship with the Enforcement Agency.** As discussed above, if the applicant proves to the agency that it will cooperate fully in providing all of the information requested of it, the agency is more likely to maintain a constant dialogue and check with the applicant first if another company comes forward with evidence of conduct in related products. Ideally, the applicant wants the enforcer to be mindful of tagback risks and look out for the applicant by asking if it makes a given product and whether anything reported by the applicant is related to the product. This level of discourse should happen where the applicant has proven itself to the enforcement agency as a strong cooperator. In all events, where this inquiry occurs, the applicant should assume there is a potential tagback risk and work with all deliberate speed to head it off.

**Conclusion**

Tagbacks fueled by the leniency-plus incentive structure pose real risk to leniency applicants and enforcement authorities. Applicants must sufficiently protect themselves because incentives exist for both former co-conspirators and enforcement agencies to pursue leniency-plus opportunities. The applicant must factor the necessity of mitigating this risk into its analysis when applying for leniency and determining its course of action. Enforcement agencies, for their part, should be cognizant of the destabilizing effects tagbacks can have on leniency programs and provide first-mover applicants in an industry ample space to protect themselves against tagbacks.●
The Mistrial:

Novell v. Microsoft and Cross-Market Theories of Causation

Paula W. Render and Thomas D. York

There was a lot of speculation in this but-for world, and we had some evidence. But it’s hard to draw inferences to a but-for world with only so much evidence.

—Corbyn Alvey, holdout juror

On December 16, 2011, after nearly seven years of litigation and following a two-month trial, the federal judge in Novell v. Microsoft declared a mistrial after a panel of jurors failed to reach a unanimous verdict. The jurors’ inability to reach agreement is not surprising in light of the complexity of Novell’s cross-market theories of injury and the uncertain standards that apply to evaluating causation.

Plaintiff Novell, Inc. sold office productivity application software during the period relevant to the issues at trial. Microsoft sold Windows, one of the PC operating system on which Novell’s office productivity applications ran, and also sold its own office productivity software. Novell alleged that Microsoft took steps to delay the launch of Windows 95 versions of Novell’s products—but did not claim that Microsoft thereby caused direct injury to competition in the market for business productivity applications. That claim was barred by the statute of limitations. Instead, Novell claimed that the delay of its business productivity applications injured competition in the market for PC operating systems, a cross-market injury. The limitations period for that claim had been tolled by the U.S. Department of Justice’s litigation against Microsoft for monopolization of the PC operating systems market.

The jury apparently struggled with the attenuated chain of causation on which Novell based its cross-market theories. Moreover, the court struggled with ambiguous case law regarding what Novell had to prove regarding the causation of its injuries: Was Novell required to prove that Microsoft’s conduct “contributed significantly” to maintenance of its monopoly in PC operating systems, or that the conduct was “reasonably capable” of doing so? The court ultimately provided dueling jury instructions on the standard of causation, presumably to give the jury two options and pave the way for an appellate court to resolve the ambiguity without the need for another trial. Instead, the jury appears to have simply found the dueling instructions confusing.

During deliberations, the jurors faced three questions relating to causation: Whether Microsoft engaged in anticompetitive conduct, whether that conduct injured Novell, and whether the conduct that allegedly injured Novell also injured the PC operating systems market in which Novell did not participate. The first and second of these questions are questions of fact for a jury to decide, but the third is a thorny question that could prove confusing for the next jury as well. Clearer direction regarding the standard for proof of causation could address that confusion.

Background

Novell’s claims against Microsoft originate from Novell’s brief ownership of WordPerfect, a word processing application, and Quattro Pro, a spreadsheet program, from 1994 to 1996. Novell
acquired WordPerfect and Quattro Pro in June 1994. Novell marketed these programs together as “PerfectOffice.”

In the early 1990s, as Microsoft developed Windows 95, a new operating system building off Microsoft’s previous successes with Windows, Microsoft initiated a marketing program designed to encourage independent software vendors (ISVs) to support the new operating system. Through this program, Microsoft offered the ISVs access to the “beta” version of Windows 95 as well as technical and marketing assistance. In exchange, Microsoft sought commitments that the ISVs would release a Windows 95-compatible product within ninety days of its launch. WordPerfect (and later Novell) participated in Microsoft’s program, intending to release a new version at or shortly after the Windows 95 launch.

As part of its efforts to enroll ISVs in the pre-launch program, Microsoft promoted certain features that would be included in Windows 95, including certain namespace extension application programming interfaces (APIs). These namespace extension APIs allowed developers to integrate namespace objects into the Windows 95 shell namespace and provide rich, custom views of data. Microsoft released the Windows 95 beta in June 1994, providing sufficient documentation on the namespace extension APIs to allow WordPerfect/Novell and other ISVs to begin writing code for their respective applications. However, Microsoft later withdrew support for the namespace extension APIs in October 1994, citing robustness and compatibility concerns. Novell began to re-engineer its program to address Microsoft’s API changes.

Meanwhile, Novell also experienced programming delays and integration difficulties stemming from its 1994 acquisition of WordPerfect. When Microsoft released Windows 95 in August 1995, Novell was not prepared to release a new version of PerfectOffice. Novell later sold both WordPerfect and Quattro Pro to Corel Corporation in March 1996. Corel released PerfectOffice for Windows 95 in May 1996.

Summary of the Proceedings

**Novell’s Claim.** Novell instituted suit against Microsoft on November 12, 2004, seeking damages in excess of $1 billion.¹ Novell claimed, among other things, that Microsoft injured Novell by thwarting the development of Novell’s office productivity applications. Novell asserted that it relied on Microsoft’s publication of the namespace extension APIs in developing Windows 95-compatible versions of WordPerfect and Quattro Pro, and Microsoft’s later withdrawal of support forced Novell to re-engineer the programs to the new specifications. This time-intensive process made it impossible for Novell to release PerfectOffice within sixty days of the launch of Windows 95, the window Novell believed was crucial to capture customers, who generally only purchase one word processing and spreadsheet product per operating system.

Novell asserted that Microsoft’s conduct was anticompetitive, rather than just injurious to Novell alone, because Microsoft intentionally harmed Novell’s office productivity applications as a way to maintain its monopoly power in the PC operating systems market. According to Novell, Microsoft protected its monopoly in PC operating systems by an “applications barrier to entry” stemming from two characteristics of the software market: first, that most consumers prefer operating systems for which there is an abundance of high-quality, practical applications, and second, that most developers prefer to write programs for operating systems that have a substantial consumer base. This “chicken-and-egg” situation ensures that applications will continue to be devel-

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¹ Complaint, Novell, Inc. v. Microsoft Corp., No. 2:04 CV 1045 (D. Utah filed Nov. 12, 2004) [hereinafter Novell Complaint].
oped for the dominant operating system, Windows, which in turn ensures that consumers will continue to prefer Windows over other operating systems. While many firms possess the financial and technological wherewithal to develop competing operating systems, the applications barrier to entry inhibits demand for anything other than niche systems.

Novell contended that its popular WordPerfect and Quattro Pro applications, though not competitors in the operating systems market, could crack the application barriers to entry in two respects. First, under its “franchise” theory, Novell claimed that its office productivity products were so popular that, if available on rival operating systems, would have “provide[d] a path onto the operating-system playing field” by legitimizing the competing operating system, which would thereby increase competition in the PC operating systems market. Novell further alleged that Microsoft intentionally targeted WordPerfect and Quattro Pro so that Microsoft would own the key office productivity franchises, which would increase the barriers to entry into the operating system market.

Second, under its “middleware” theory, Novell argued that its PerfectOffice applications (along with certain related applications) lessened the applications barrier to entry because they functioned as “middleware.” Middleware relies on interfaces provided by the underlying operating system while simultaneously exposing its own APIs and related functionality to software developers. Developers can then write their own applications using the middleware’s APIs, and not those of the underlying operating system. Middleware thus allows application developers to write one version of an application for use on multiple operating systems, by writing to middleware instead of to the actual APIs of each operating system. It also reduces the need for end-users to upgrade their operating system in order to obtain new application features. By attacking the middleware, Novell claimed that Microsoft “widen[ed] the moat” of the applications barrier to entry and thereby unlawfully maintained its monopoly in the PC operating systems market.

Relevant Markets. Novell’s cross-market theory of harm implicates multiple product markets: the word processing and spreadsheet application markets, as well as the PC operating systems market.

The word processing market consists of software used to create, edit, print, and store text-based documents. In its complaint and subsequent briefs, Novell claimed that WordPerfect was a significant player in the late 1980s, peaking at about 47 percent market share across all operating systems in 1990. However, its share declined precipitously in the early 1990s, and by 1996 it held less than 10 percent market share. The share of Microsoft Word, initially a small player, exploded from 20 to 90 percent share during the same time.

The spreadsheet application market was similarly characterized by numerous players during the relevant time, including Quattro Pro and Microsoft Excel. Quattro Pro was a small player, possessing only a “very, very small fraction” of the Windows-compatible spreadsheet market.

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3 Novell, Inc., 505 F.3d 302 at 308.
5 Complaint, supra note 1, ¶ 62 (internal quotations omitted). See also Novell’s Opp. to Ren. JMOL, supra note 2, at 70.
Both the word processing and spreadsheet application markets feature a common unique characteristic in that consumers typically purchase only one product per operating system. Thus, to be successful, developers must have a new version of their software ready at the time a new operating system is released or else they will be effectively foreclosed from a large percentage of the market.

The Intel-compatible PC operating systems market consists of software that controls a PC's resources and manages the execution of software applications. During the relevant time, Microsoft was a market leader (if not a monopolist) in the PC operating systems market, first with its Windows 3.0 operating system and later with Windows 95.7

Relationship to U.S. v. Microsoft. Novell's claim echoes those made by the Department of Justice in its investigation and subsequent 1998 civil suit against Microsoft in United States v. Microsoft Corp.8 In that action, the DOJ alleged, among other things, that Microsoft maintained its monopoly in the PC operating systems market by targeting “middleware” products, such as Sun's Java programming environment and the Netscape Navigator Web browser. Java and Netscape Navigator are not operating systems and did not compete directly with Microsoft's Windows. However, the DOJ claimed, and the courts agreed, that the middleware applications “ha[d] the capability to serve as platforms for software applications themselves” for which developers could write applications rather than rewriting them for each operating system.9 Despite the fact that the primary threats operated outside of the PC operating systems market, the courts found that Microsoft unlawfully monopolized that market by harming middleware products.

Like the cross-market theory espoused in U.S. v. Microsoft, Novell asserted that it suffered antitrust harm from Microsoft injuring competition in the PC operating systems market, a market in which Novell did not participate. Given the similarity of many of the facts and issues, Novell argued in its complaint that many of the findings of fact and conclusions of the District Court for the District of Columbia were binding on Microsoft under principles of collateral estoppel, including the court's findings on the “applications barrier to entry” and the existence and significance of middleware.

The Cross-Market Causation Issues

Over the course of the proceedings, the court condensed Novell's claim to three elements: (1) whether Microsoft's withdrawal of the namespace APIs was anticompetitive; (2) whether Microsoft's conduct caused injury to Novell by delaying the introduction of Novell's applications for Windows 95; and (3) whether the Microsoft conduct which caused injury to Novell also caused anticompetitive harm to the PC operating systems market.10 The third element—the crux of Novell's cross-market causation claim—was, and remains, hotly contested.

One of the key points of contention has been the extent to which Novell was required to show that Microsoft's withdrawal of the namespace extension APIs impacted the relevant market—i.e., the PC operating systems market. Microsoft argued that Novell was required to show that Microsoft's conduct contributed significantly to the maintenance of Microsoft's monopoly in the PC

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7 The District Court for the District of Columbia made findings of fact in the government's case against Microsoft that Microsoft possessed a monopoly in the PC operating systems market. See U.S. v. Microsoft, 84 F. Supp. 2d at 14–28.
9 Novell, Inc., 505 F.3d at 309 n.14 (citing U.S. v. Microsoft, 253 F.3d at 53).
operating systems market. Novell argued that it need only show Microsoft’s conduct was reasonably capable of contributing to Microsoft's continued monopoly power. Another key dispute concerned the sufficiency of Novell’s proof that Microsoft’s conduct caused Novell’s claimed injuries.

**How the Courts Addressed Causation.**

**Microsoft’s Motion to Dismiss.** Microsoft moved to dismiss Novell’s complaint in January 2005, claiming that Novell lacked antitrust standing for harm caused to the PC operating systems market. Microsoft challenged Novell’s cross-market theories of injury, arguing that Novell was neither a consumer nor a competitor in the relevant market for PC operating systems and that its injuries were too remote to the alleged antitrust violation to confer standing. The district court rejected this argument, however, holding that there was no bright-line rule providing standing only to consumers or competitors. Additionally, the court foreshadowed the dispute over the standard of proof by noting that Novell alleged specific facts that, if proven, could show that Microsoft had engaged in a strategy of maintaining its operating system monopoly through ownership of key application franchises, such as Microsoft Word and Excel. The court also held that Novell stated facts sufficient to show that Microsoft intended to harm WordPerfect and Quattro Pro by withholding key Windows integration functionality from Novell. These specific allegations, demonstrating intent to harm Novell and a causal link to the relevant market, were sufficient to plead the basis for antitrust standing. The Fourth Circuit affirmed.

**Summary Judgment.** On cross-motions for summary judgment, the district court reduced Novell’s “unique” monopolization claim to three elements: (1) whether Microsoft’s withdrawal of the namespace APIs was anticompetitive; (2) whether Microsoft’s conduct caused injury to Novell’s applications; and (3) whether the Microsoft conduct which caused injury to Novell also caused anticompetitive harm to the PC operating systems market.

With regard to the first question, Judge Motz found that Novell raised questions of material fact regarding whether Microsoft engaged in anticompetitive conduct. The judge did not address the second question, whether Microsoft’s conduct had caused Novell’s claimed injuries.

Judge Motz’s discussion of the third question would eventually give rise to the dispute between the parties (as discussed below) as to whether Novell was required to prove that the challenged conduct contributed significantly, or the lesser showing that the conduct was reasonably capable of contributing significantly to harm to competition through Microsoft’s continued monopoly. In finding that Novell established a triable issue of fact regarding whether Microsoft’s anticompetitive conduct caused anticompetitive harm in the PC operating systems market, Judge Motz addressed the standard by which Novell had to prove that causation. He explained that Novell was required “to show that the conduct at issue ‘contributed significantly’ to a [Microsoft’s] con-

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12 Novell’s Opp. to R en. J M O L, supra note 2, at 75. As noted, the thorny causation issue would not have arisen if Novell’s action against Microsoft had been for unlawful monopolization of the office productivity application markets. These claims, however, were time-barred by the time Novell filed its complaint. See Novell, Inc., 505 F.3d at 320–23.
15 Novell, Inc., 505 F.3d at 315–16.
continued monopoly power.” As authority for this standard, he cited and quoted three cases. One of these cases "suggest[ed]" that the plaintiff must prove a “measurable impact” on competition. Microsoft would later urge that this holding by Judge Motz established that Novell was required to prove that Microsoft’s conduct “contributed significantly” to injury to the PC operating systems market.

The other two cases on which Judge Motz relied both provide that a plaintiff need only prove that the alleged anticompetitive conduct is reasonably capable of contributing to creating or maintaining monopoly power. In addition, Judge Motz explained that the “plaintiffs need not ‘present direct proof that a defendant’s continued monopoly power is precisely attributable to its anticompetitive conduct.’” He noted that “Novell has no obligation to create some ‘hypothetical market place,’ in which none of the other ISVs or applications had been weakened by anticompetitive conduct, and then prove that the conduct at issue would still have significantly contributed to anticompetitive harm in that hypothetical market.” Novell would take the position later, in the battle over jury instructions and in Microsoft’s post-trial motion, that this discussion established that Novell was required only to show that Microsoft’s conduct was reasonably capable of contributing significantly to its monopolization of the PC operating systems market.

**TRIAL PROCEEDINGS.** At trial, Novell limited its allegations to the three questions identified by Judge Motz in his summary judgment opinion: (1) whether Microsoft’s withdrawal of support for the namespace extension APIs was anticompetitive, (2) whether it delayed Novell’s release of WordPerfect and Quattro Pro for Windows 95, and (3) whether such delay harmed competition in the PC operating systems market. The first two questions were simply questions of fact for which the jury had to consider the quantum of evidence presented by each party. The third question, however, gave rise to the cross-market problem as well as the dueling jury instructions on the standard by which to judge causation.

**The Cross-Market Problem: Did Novell Prove Injury to a Market in Which It Was Not a Participant?** Microsoft advanced three primary arguments. First, Microsoft argued that Novell’s products were not “middleware” as claimed, and in any event would have had no impact on the applications barrier to entry. The district court in *U.S. v. Microsoft* defined “middleware” only as those products that run on multiple operating systems and that expose a sufficient number of APIs to allow ISVs to design general purpose productivity applications that call upon the APIs exposed by the software, rather than on the APIs exposed by the underlying operating system. Microsoft argued principally that Novell’s products failed to fall within the scope of this definition. As such, WordPerfect and Quattro Pro had “no potential to displace Windows as a platform for developing”

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17 Id. at 747–48 (quoting *U.S. v. Microsoft*, 253 F.3d at 80, and citing *Data Gen. Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147, 1182 (1st Cir. 1994) and *Morgan v. Ponder*, 892 F.2d 1355, 1361–63 (8th Cir. 1989)).
18 Id. at 748 (quoting *Morgan*, 892 F.2d at 1361–63).
19 Id. at 748 (citing *U.S. v. Microsoft*, 253 F.3d at 80 (plaintiff needs to show that the conduct at issue is “reasonably capable of contributing to a defendant’s continued monopoly power”) and *Data General Corp.*, 36 F.3d at 1182 (explaining that exclusionary conduct is conduct “that reasonably appears capable of making a significant contribution to creating or maintaining monopoly power.” (internal citations omitted))).
20 Id. (quoting *U.S. v. Microsoft*, 253 F.3d at 79).
21 Id. at 749.
general purpose productivity applications and Microsoft’s withdrawal of the namespace extension APIs could not have harmed the PC operating systems market. Novell countered by arguing that its products would have become middleware but for Microsoft’s conduct, and that it only had to show that its products could have weakened the applications barrier to entry, not destroyed it by displacing Windows.

Second, Microsoft attacked Novell’s franchise applications theory on the ground that Novell’s applications were not sufficiently popular to sway users one way or another when purchasing an operating system. Microsoft further pointed to the U.S. v. Microsoft findings of fact, which explained that the applications barrier to entry arises from a positive feedback loop consisting of tens of thousands of applications. Under this definition, Microsoft argued that WordPerfect and Quattro Pro standing alone could not have significantly affected competition in the PC operating systems market. In response, Novell pointed out that, during the relevant time, consumers spent the majority of their time on PCs using word processing and spreadsheet applications, and cited internal Microsoft documents to demonstrate the importance of the WordPerfect and Quattro Pro franchises.

Finally, Microsoft argued that Novell’s utilization of the namespace extension APIs would have enhanced the attractiveness of Windows, which would have increased overall sales and market share. Thus, withdrawing support for the functionality could not have caused anticompetitive harm to the PC operating systems market, nor could it have contributed to Microsoft’s monopoly in that market. Novell rebutted this argument by pointing out that Microsoft’s conduct made no commercial sense, and as such was consistent with a monopolist’s sacrifice of short-term profits in exchange for a long-term competitive advantage.

Jury Instructions. The dispute about the correct standard under which Novell had to prove harm to competition in the PC operating systems market (“contributed significantly” or “was reasonably capable of contributing significantly”) appears to have crystallized during the protracted battle over jury instructions. Judge Motz gave the jury a verdict form with seven questions it was to answer in deciding the case, two of which (Questions 4 and 5) reflected the dueling standards. The jury was first asked to answer whether (1) Microsoft’s decision to withdraw support for the namespace extension APIs caused Novell’s productivity applications to be late to market; (2) but for Microsoft’s decision, Novell would have released its productivity applications at or shortly after the release of Windows 95; and (3) Microsoft’s decision amounted to anticompetitive conduct.

If the jury answered Questions 1–3 in the affirmative, then Judge Motz directed it to answer Questions 4 and 5. Judge Motz prefaced those two questions by saying, “You are being asked to answer questions 4 and 5 because of uncertainties I believe exist in antitrust law, and your answers to them may clarify the record and prevent a retrial of this case. These questions are important because they are related to an element of Novell’s claim that Novell must prove.” The questions were:

4. Has Novell proven by a preponderance of the evidence that the delay caused to Novell by Microsoft’s decision to withdraw support for the namespace APIs caused harm to competition in the market for PC operating systems and contributed significantly to the maintenance of Microsoft’s monopoly in that market?

5. Has Novell proven by a preponderance of the evidence that Microsoft’s withdrawal of support for the namespace extension APIs was reasonably capable of contributing

23 Id. at 41 (citing U.S. v. Microsoft, 84 F. Supp. at 14–15).
significantly to the maintenance of Microsoft’s monopoly in the market for PC operating systems?" \(^{24}\)

Question 4 thus represented Microsoft’s view that Novell had to show Microsoft’s conduct appreciably affected the PC operating systems market by increasing the applications barrier to entry. The alternative formulation in Question 5 demonstrates Novell’s view that Novell need not prove harm, but instead merely show that Microsoft’s conduct could have increased the applications barrier to entry.

The jury apparently struggled with these questions. A local newspaper reported on December 15, 2011, that the jury sent the judge a note asking him to explain the difference between Questions 4 and 5. \(^{25}\)

\textbf{Mistrial and the Jurors’ Views.} After three days of deliberation, the district court declared a mistrial because the jurors could not reach a unanimous verdict. One juror, twenty-one-year old security guard Corbyn Alvey, held out for a defense verdict despite the agreement of the other eleven jurors on a verdict for Novell. But in discussions with the media following the mistrial, it emerged that even the eleven jurors who wanted to reach a verdict for Novell had differing views of Novell’s case.

As noted above, the three questions on which Novell focused at trial were (1) whether Microsoft’s withdrawal of support for the namespace extension APIs was anticompetitive, (2) whether it delayed Novell’s release of WordPerfect and Quattro Pro for Windows 95, and (3) whether such delay harmed competition in the PC operating systems market. All twelve jurors agreed that Microsoft failed to overcome Novell’s showing that Microsoft had engaged in anticompetitive conduct, and that Novell had prevailed as to the first question. Alvey, the holdout juror, discussed his views in an interview with KSL.com, a local news provider. \(^{26}\) He explained, “It’s been 17 years, [Bill Gates] could have forgotten. But it just seems to me that he—his testimony wasn’t matching up with the e-mails he had written in ’93, ’94, and ’95.”

With respect to the second question, the jury was more divided. Alvey did not believe that Novell had proven that Microsoft’s anticompetitive conduct caused Novell’s injuries. In the video news report, Alvey was asked, “You think [Microsoft] used anticompetitive behavior, but that it didn’t have the impact that Novell claimed?” He responded emphatically, “Yes. Yes. And yes.” Alvey also told a reporter that he believed a Microsoft expert’s testimony that WordPerfect already was in a steep decline by the time Novell bought it in 1994, shortly before Gates’ fateful decision. \(^{27}\) Alvey was not alone among the jurors in this view. Other jurors shared the view that Novell was at least partially responsible for its own problems. Jury foreman Carl Banks explained to a reporter that some jurors believed Novell’s CEO “didn’t put as much emphasis on that WordPerfect stuff as everybody else felt it needed, and [Novell] kind of self-destructed because of some choices the upper echelon made.” Banks also told the reporter, “There were three or four people who said [Novell] hurt [itself] and couldn’t be awarded and there were other people who felt they should be awarded the maximum.”

\(^{24}\) Jury Instructions at 11, \textit{Novell, Inc.}, No. 2:04 CV 1045 (emphasis added).


With respect to the third question, holdout Alvey was unwilling to find for Novell. According to *The Salt Lake Tribune*, Alvey said that “he just couldn’t agree with the question on the verdict form about Novell’s assertion that a successful WordPerfect/Quattro Pro suite would have raised the ‘prospect’ that consumers might have an ‘attractive alternative to Windows.’”28 In other words, the holdout juror was unconvinced of Novell’s theories that delay of its office productivity products caused injury to the PC operating systems market. Because Alvey held out for no liability at all, the other jurors did not have to resolve their conflicting views about the extent to which Microsoft was responsible for Novell’s claimed injuries.

**Post-Trial.** Following the hung jury, Microsoft renewed its motion for judgment as a matter of law. Microsoft’s brief and reply emphasized that Novell failed to provide sufficient evidence that Microsoft’s withdrawal of support for the namespace extension APIs actually harmed competition in the PC operating systems market.29 Microsoft further argued that no reasonable juror could find that Microsoft was responsible for the delays in Novell’s introduction of its PerfectOffice suite, as the evidence at trial demonstrated that the delays resulted from internal issues at Novell.

Novell, on the other hand, argued in its opposition brief that it need only prove that Microsoft’s conduct “appeared to be reasonably capable of contributing significantly to maintaining monopoly power.”30 Novell cited *U.S. v. Microsoft* for the proposition that “neither plaintiffs nor the court can confidently reconstruct a product’s hypothetical technological development in a world absent the defendant’s exclusionary conduct” and requiring such proof would only encourage monopolists to take “more and earlier anticompetitive action.”31 Thus, Novell asserted that it only must show that its applications “could have” diminished or weakened the applications barrier to entry, thereby affecting the PC operating systems market, to recover damages.

Novell’s attorneys also indicated that they would seek a new trial.

**The Standard of Proof for Cross-Market Causation**

In its post-trial motion, Microsoft continued to urge the court to require Novell to show that Microsoft’s withdrawal of support for the namespace extension APIs “contributed significantly” to its monopoly in PC operating systems. Novell, on the other hand, argued that the applicable standard is that which prevailed in *U.S. v. Microsoft*, that the alleged anticompetitive conduct is *reasonably capable* of contributing to creating or maintaining monopoly power. But case law and the relevant authorities suggest that the appropriate standard lies somewhere in between.

**The Standard of Proof of Causation by a Private Plaintiff.** Microsoft’s test, that its conduct “contributed significantly” to its monopoly, would require Novell to prove the impossible. As the Areeda and Hovenkamp treatise—cited by both Novell and Microsoft in their briefs—explains, many exclusionary practices “are one-of-a-kind situations in which it is impossible to prove that an outcome would have been different absent the violation. . . .”32 To require a plaintiff to prove that the defendant’s conduct did in fact contribute to harm to competition is simply not possible once the conduct has occurred.

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28 Id.
30 Novell’s Opp. to Ren. JMOL, supra note 2, at 3 (citing Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal & Prof’l Publ’ns, Inc., 63 F.3d 1540, 1550 (10th Cir. 1995)).
31 Id. (quoting *U.S. v. Microsoft*, 253 F.3d at 79).
But Novell’s test, whether defendant’s conduct is “reasonably capable” of creating monopoly power, overlooks the distinction between private and government plaintiffs. Unlike the government, private plaintiffs seek recovery of damages, and damages are not available unless a plaintiff proves actual injury to business or property. Thus, as Areeda and Hovenkamp observe, “[I]t is well established that the . . . plaintiff must demonstrate not only that the defendant has violated the antitrust laws, but also that the plaintiff’s business or property in fact suffered compensable injury as the result of that violation.”33 While the government must simply show that anticompetitive consequences are a likely outcome of the challenged conduct, a private plaintiff must show “somewhat more . . . [I]f it shows a violation and harm of a type that is highly likely to be the result of such a violation, then the ordinary tort rule would shift the burden of proof to the defendant to show that the harm had a different source.”34

Thus, the applicable standard for Novell to prove that its injury resulted from the violation should be neither the standard from the government’s case against Microsoft nor the strict proof demanded by Microsoft. Applying the formulation offered by Areeda and Hovenkamp, if Microsoft is found to have committed an antitrust violation (harm to the PC operating systems market through unlawful maintenance of monopoly), Novell would then be required to show that its alleged injury is “highly likely” to have been the result of that violation. Thus, appropriate jury instructions on the issue of whether Novell’s injury was caused by the violation could be:

1. Has Novell proven by a preponderance of the evidence that Microsoft’s withdrawal of support for the namespace extension APIs caused the delay in Novell’s introduction of its Windows 95 office productivity software products?

2. (If yes:) Has Novell proven by a preponderance of the evidence that the delay in Novell’s introduction of its Windows 95 office productivity software products was highly likely to have contributed to Microsoft’s maintenance of monopoly power in the PC operating systems market?

Under the preponderance standard, of course, Microsoft would then be entitled to present evidence showing that the claimed harms resulted from other causes.35

**The Cross-Market Nature of Novell’s Theories Made the Standard of Proof Unusually Problematic.** Courts, of course, routinely instruct juries about the standard by which a plaintiff must prove antitrust injury in monopolization cases. It is the cross-market nature of Novell’s theories that appears to have made the standard problematic in this case.

For example, in *Masimo Corp. v. Tyco Health Care Group*,36 plaintiff Masimo alleged that Tyco unlawfully abused its monopoly power in the market for pulse oximetry products to exclude competition, by offering loyalty discounts, bundled rebates, and other conduct. Both Tyco and Masimo were participants in the pulse oximetry product market. The jury reached a verdict for Masimo on its Section 2 claim (although it awarded no damages on that claim, having already awarded damages for the same conduct on other claims).

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33 Id. ¶ 657a.
34 Id. ¶ 657a2 (emphasis added).
35 See id. (noting that “if [the plaintiff] shows a violation and harm of a type that is highly likely to be the result of such a violation, then the ordinary tort rule would shift the burden of proof to the defendant to show that the harm had a different source”).
After instructing the jury with respect to proof of the violation, the court explained that to establish antitrust injury, “Masimo must have offered evidence that establishes as a matter of fact and with a fair degree of certainty that Tyco’s alleged illegal conduct was a material cause of Masimo’s injury. . . . It is enough if [Plaintiff] has proved that the alleged antitrust violation was a material cause of its injury. Injury may be established by inference of circumstantial evidence.” This instruction could be read to support either Microsoft’s or Novell’s proposed standard. It requires demonstrating that the defendant’s violation was a “material cause” of the plaintiff’s injury, thus supporting Microsoft. But it also requires only a “fair degree of certainty,” thus supporting Novell.

Because Masimo and Tyco were participants in the same market, there was no cross-market causation problem to test the standard. Applying the dueling standards sought by Microsoft and Novell to these facts makes little difference to the analysis. Did Tyco’s discounts and rebates “contribute significantly” to Masimo’s loss of business? Or was Tyco’s conduct “reasonably likely to have significantly contributed” to that loss? Nor does the Areeda and Hovenkamp formulation, whether the plaintiff’s harm was “highly likely” to result from the violation, make any significant difference. Given that the question was simply whether Tyco’s conduct caused customers to buy from it rather than from Masimo, the degree of certainty in the causal link would not be likely to become a sticking point in the litigation.

In the Novell-Microsoft case, however, the cross-market nature of Novell’s theories of injury made the degree of certainty in the standard of proof more significant. Unlike Masimo, it was not enough for Novell to simply prove that the antitrust violation was the cause of its injury. Novell faced the additional challenge of linking that conduct to Microsoft’s monopoly power in PC operating systems. And because cross-market theories of harm allege “one-of-a-kind situations” that can be “impossible to prove,” Novell was forced to ask the jury to make additional inferences to connect harm across two separate product markets. Thus, the standard for causation becomes critical for Novell, where it was much less so in Masimo.

There is no way to know whether Alvey, the holdout juror, would have reached a different conclusion if he had been given the jury instruction proposed above. As noted above, he “just couldn’t agree . . . that a successful WordPerfect/Quattro Pro suite would have raised the ‘prospect’ that consumers might have an ‘attractive alternative to Windows.’” Thus, he may not have believed Novell met even its proposed lower standard. But other jurors, believing that Novell may have caused some but not all of its own injuries, might have reached a different conclusion—and so might the next jury.

**Conclusion**

The fractured jury in the Novell v. Microsoft mistrial demonstrates the inherent difficulties in proving an unlawful monopolization claim using a cross-market theory of harm. A but-for counterfactual world is difficult to prove in ordinary circumstances. But when the but-for world involves harm in one market resulting from conduct in a different market, the theory of causation can become even more difficult to demonstrate.

The holdout juror may have said it best: “The problem was there was so much differing in the understanding of the evidence and what could have happened in the but-for world and what happened in the real world.”

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Analyst Calls and Price Signaling Under EU Law

Howard Rosenblatt and Tomas Nilsson

Information exchanges have become a hot topic in the European Union. The European Commission's recently updated Guidelines on horizontal arrangements give the subject prime space, and information exchanges increasingly are the basis of investigations and enforcement efforts. No one therefore should be surprised if U.S. companies with European operations find their U.S. investor analyst calls scrutinized by the Commission. The U.S. Federal Trade Commission has already brought two high-profile enforcement actions finding that senior executives used these calls to signal competitors in an effort to coordinate price and allocate customers.

Yet the theory for an infringement in Europe would need to be different than in the United States. Despite a decade of steady convergence between the two jurisdictions, the basis for the FTC's enforcement actions in the United States—unilateral invitations to collude—does not exist in Europe. There is no counterpart to Section 5 of the FTC Act in Europe. Unilateral conduct can infringe EU competition law only when it constitutes an abuse of an existing dominant position.

However, the European Commission has other enforcement tools at its disposal. In addition to anticompetitive agreements, the governing law separately prohibits so-called concerted practices, an often ambiguous concept but one the Commission describes as requiring something less than an express agreement. And the Commission's recent Guidelines show a willingness to stretch the concept still further to reach suspicious conduct.

No company wants to be a test case, particularly for entirely preventable conduct of its senior executives. Understanding the European Commission's current approach to information disclosures can help companies reduce unnecessary risk as they balance the interests of investors with the demands of EU competition law.

Information Exchange and Analyst Calls—The U.S. Experience

In the United States, information exchanges typically are analyzed as “agreements” under Section 1 of the Sherman Act because the parties at least implicitly agreed to exchange the information. Often, the exchanges also further an underlying cartel, as was the case most recently in the FTC's complaint this year against three suppliers of iron pipe fittings.\(^1\) However, purely one-way disclosures, without any evidence of reciprocity, can constitute an invitation to collude under Section 5 of the FTC Act, for which there is no analog in Europe.\(^2\)

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\(^2\) See, for example, the Stone Container case, where the FTC challenged a unilateral initiative to increase linerboard prices through a scheme that included public statements and press releases allegedly addressed to competitors. The FTC's action was resolved through a consent decree. See Stone Container Corp., FTC File No. 9510006 (1998), available at [http://www.ftc.gov/os/caselist/1010080/120104sigmacmpt.pdf](http://www.ftc.gov/os/caselist/1010080/120104sigmacmpt.pdf).
Information disclosures made during analyst calls have been the subject of two recent enforcement actions in the United States. Though conceding that companies have an obligation to disclose a range of information to the investing public, the FTC has found that certain disclosures were nothing more than efforts to engage in price fixing and market allocations with competitors and were thus a unilateral invitation to collude under Section 5 of the FTC Act. The statements were a violation regardless of whether anyone was listening, let alone did anything in response.

**The Valassis Case.** The FTC's first case involved Valassis, which had a single competitor for newspaper advertising inserts. Valassis's analyst call took place in the context of an ongoing pricing war between the companies, which Valassis had unsuccessfully tried to end by increasing its prices. It rolled the prices back when its competitor, News America, did not follow. The FTC alleged that Valassis "developed a new strategy," namely, to communicate with its competitor via its quarterly earnings call, which Valassis knew News America would be monitoring.

Valassis's President and CEO allegedly used the call to give highly detailed instructions on how News America could end the price war. In particular, Valassis said that: it would abandon its 50 percent market share goal; it would defend its existing customers; it would submit bids for News America customers with expiring contracts at substantially higher prices; it was content to maintain its existing share for each customer who split its business between the two competitors; and if News America continued to compete for Valassis customers, the price war would resume. The executive's remarks included references to specific market share targets, dates, and prices.

The FTC concluded these statements were made with an intent to facilitate collusion, lacked any legitimate business purpose, and thus violated Section 5 of the FTC Act. The FTC's action was resolved through a negotiated consent decree.

**The U-Haul Case.** Unlike the Valassis case, the FTC's case against U-Haul concerned answers to analysts' questions. The FTC alleged that U-Haul had developed a strategy for increasing industry prices of one-way rentals by raising its own price and contacting regional managers of its main rival, Budget, to encourage them to do the same.

U-Haul's CEO allegedly used the company's quarterly earnings calls to further this plan, knowing Budget would be monitoring them. He opened the call by describing U-Haul's effort to "show price leadership." When asked for additional information about industry pricing, the CEO allegedly responded that: Budget should follow U-Haul's price leadership; Budget's refusal to match U-Haul's higher rates hurt the industry; U-Haul would wait a little longer for Budget to respond appropriately; and Budget could keep its prices slightly below U-Haul's so long as the differential was not significant.

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4 Id. ¶¶ 11–12.
5 Id. ¶ 13.
6 For example, the FTC alleged the executive stated that "Our net price after ancillary price discounts, rebates, et cetera, will not go below $6 [per thousand] for a full page and $3.90 [per thousand] for a half page." Id. ¶ 13(c).
8 For example, the FTC quoted the CEO as instructing in a memorandum to his own regional managers: “Budget continues in some markets to undercut us on One-Way rates. Either get below them or go up to a fair rate. Whatever you do, LET BUDGET KNOW.” Id. ¶ 13.
9 Id. ¶ 24.
10 Id.
As in the *Valassis* case, the FTC found that U-Haul lacked a legitimate justification for these statements and that its intent instead was to facilitate collusion with Budget. And as with the *Valassis* case, the FTC resolved its concerns without litigation through a consent decree.

These cases raise some key points. First, although the cases make clear that earnings calls should be handled with antitrust issues in mind, nothing in them should preclude a company from providing information that is genuinely important to investors. The FTC acknowledged in *Valassis* that corporations “have many obvious and important reasons for discussing business strategies and financial results with shareholders, securities analysts, and others.”\(^{11}\) The FTC therefore “is extremely sensitive to the fact that antitrust intervention involving a corporation’s public communications must take care not to unduly chill legitimate speech.”\(^{12}\) The FTC’s orders expressly excluded from their prohibition information required to be disclosed by the securities laws. In both cases, however, the FTC concluded that the sole purpose and effect of the statements were to induce competitors to engage in collusion.

On the other hand, the FTC avoided any line-drawing to identify analyst call statements it will find suspicious. Although the facts in both *U-Haul* and *Valassis* appear relatively straightforward and egregious, the FTC warned in *U-Haul* that “it is possible less egregious conduct may result in Section 5 liability.”\(^{13}\) The FTC also said it has no obligation to “find repeated misconduct attributable to senior executives . . . or establish substantial competitive harm, or even find that the terms of the desired agreement have been communicated with precision.”\(^{14}\)

Finally, companies making these sorts of public statements may run the additional risk that their competitor will respond in kind, creating suspicions that both are engaged in a cartel, albeit a highly public one. The Justice Department in 1992 famously accused eight major airlines of using their joint computerized reservation system to exchange and ultimately agree on future pricing, all in the open.\(^{15}\) Exchanging sensitive information also can provide the needed “plus factor” that allows courts or juries to infer that parallel moves are the result of an agreement.

### Information Exchanges in the European Union

Information exchanges and disclosures in Europe can be assessed as “concerted practices,” a concept more loosely defined than agreements. Although concerted practices unquestionably require more than purely unilateral conduct, the European Commission has stated a willingness to stretch the concept beyond even the most informal agreements.\(^{16}\) As the 2011 EC Horizontal Guidelines recently reaffirmed: “[T]he concept of a concerted practice refers to a form of coordination between undertakings by which, without it having reached the stage where an agreement properly so-called has been concluded, practical cooperation between them is knowingly substituted for the risks of competition.”\(^{17}\)

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\(^{12}\) Id.


\(^{14}\) Id.

\(^{15}\) United States v. Airline Tariff Publ’g Co., 1994-2 Trade Cas. (CCH) ¶ 70,687 (D.D.C. 1994).

\(^{16}\) This can be significant in some cases, given that the Commission and the EU courts already define agreements broadly to include all situations where the parties share a common will and manifest it. See Case T-41/96—Bayer v. Comm’n, 2000 E.C.R. II-3383, ¶ 173.

Although this definition, if taken literally, would be broad enough to cover even the sort of conscious parallelism that is common and lawful in oligopolistic markets, the Horizontal Guidelines acknowledge that companies have “the right to adapt themselves intelligently to the existing or anticipated conduct of their competitors.”18 Unlawful concerted practices instead are limited to instances where there is some direct or indirect communication between competitors with the potential to harm competition. The doctrine “preclude[s] any direct or indirect contact between competitors, the object or effect of which is to create conditions of competition which do not correspond to the normal competitive conditions of the market in question. . . .”19 Properly understood, concerted practices therefore require some sort of communication that leads to a common understanding among the players even if the specific goal of, for example, price fixing remains unspoken.

The Guidelines underscore the authority’s keen focus in this area by devoting many pages to information exchanges. While observing that information exchanges are often pro-competitive, the Guidelines say the practice can facilitate coordination by “artificially increasing transparency in the market,” at least if the information is strategic enough and the market is otherwise conducive to coordination.20

But the headline-grabbing feature of the Guidelines’ discussion on information exchanges is the creation of a new restriction by object. While the lawfulness of most agreements turns on their likely competitive effects in the circumstances of each case, agreements whose “object” is to restrict competition are presumed anticompetitive without the need to prove their actual likely effect. In this sense, restrictions by object are similar to per se violations in the United States. Unlike in the United States, however, restrictions by object can be defended by showing sufficient efficiencies that meet the stringent requirements of Article 101(3), although the showing is particularly difficult and rarely successful.

At a time when advancements in economic analysis typically favor more nuanced competitive assessments over bright line tests, the Guidelines contend that one kind of information exchange is “by its very nature” likely to restrict competition: “Information exchanges between competitors of individualized data regarding intended future prices or quantities should therefore be considered a restriction of competition by object.”21

Ultimately, the EU courts will decide whether an agreement is a restriction by object. But the stated approach of one of the world’s most active antitrust enforcers is highly instructive. For many companies, this new standard will not make much difference, as they already have been counseled to avoid sharing this sort of highly sensitive information. But the change, if confirmed by the courts, can free the Commission from the burden of proving likely anticompetitive effects and thus give it a potentially powerful enforcement tool.

**Analyst Calls In the EU**

With their intensified focus on information exchanges, we can expect the European Commission to be highly motivated to find a theory of enforcement against the sort of conduct described in

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18 Id. ¶ 61.
19 Id.
20 Id. ¶ 65.
21 Id. ¶ 74. The Commission does not cite any judicial support for this proposition but Case C-8/08—T-Mobile, 2009 E.C.R. I-4529, touches upon the topic.
U-Haul and Valassis. But the key court case involving public disclosures, the *Wood Pulp* case, is over two decades old and more of a hindrance than a help for the Commission. The Commission's recent Guidelines, in contrast, suggest a willingness to expand liability for public statements with the use of presumptions that, at the very least, could subject companies to burdensome and risky investigations.

**The Wood Pulp Case.** In the *Wood Pulp* case, the European Commission charged forty producers of bleached sulfate wood pulp used in paper manufacturing and three of their trade associations with colluding on prices. While there was no evidence of expressed agreements, the Commission's case rested on a concerted practice to fix prices, based on two key factors. First, the Commission found direct and indirect exchanges of information between the competitors that made the market artificially transparent. The exchanges were:

- A system of quarterly public price announcements to the trade press or sales agents where “the producer could expect that the prices he announced would immediately reach his competitors, just as he himself would expect to be given details in the way of his competitor's prices.” The fact that prices were published well in advance gave other producers sufficient lead time to announce their own corresponding new prices and apply them from the start of the quarter.
- Prices exchanged at meetings and through fax messages between some of the producers.
- Prices exchanged between U.S. producers within two trade associations, which the Commission also considered an independent infringement.

Second, the Commission found that these exchanges had an anticompetitive effect by resulting in parallel pricing. This parallelism could not be explained by the market's structure since it was not particularly concentrated, nor was there a market leader setting the price for others to follow.

But the Commission was reversed on appeal. The European Court of Justice held that the public announcements of future pricing, standing alone, did not infringe the competition rules because the players could not be “sure” that others would follow. While the same might be true of even the most organized cartels, the allegations in this instance were “market behaviour which does not lessen each undertaking’s uncertainty as to the future attitude of its competitors.” The Commission had failed to present enough evidence to rule out other plausible explanations for the parallel pricing. Instead, the price announcements could have had the legitimate purpose of giving customers relevant information for upcoming dealings in the wood pulp market.

Nor did the parallel timing of the announcements help the Commission’s case. The announcements could just as easily have resulted from natural transparency in the market, one characterized by free-flowing information, as buyers informed each other of prices and some agents acted for several producers. Finally, the Court found the market to be more oligopolistic than the Commission believed, providing a further explanation for the parallel prices and trends.

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23 Id. ¶ 108.
24 Id. ¶ 110.
25 Id. ¶ 109.
26 Id. ¶¶ 82, 87–89.
28 Id. ¶ 64.
29 Id. ¶¶ 126–127.
The EU Guidelines. The Wood Pulp case did not deter the Commission from staking out an aggressive stance in its recent Guidelines. The Commission first noted that “unilateral announcements” that are “genuinely public” generally do not constitute an unlawful concerted practice. However, the Guidelines say the Commission is willing to find a concerted practice when the announcement is followed by similar announcements by competitors that suggest an effort to coordinate:

[F]or example in a situation where such an announcement was followed by public announcements by other competitors, not least because strategic responses of competitors to each other’s public announcements (which, to take one instance, might involve readjustments of their own earlier announcements to announcements made by competitors) could prove to be a strategy for reaching a common understanding about the terms of coordination.30

This is not terribly surprising, but reaffirms that an ill-advised public statement by one competitor, as a practical matter, can limit otherwise unilateral decision-making of its rivals lest they be accused of engaging in a highly public cartel or land the unwitting competitor in a concerted practices investigation even though its initial intentions may have been entirely innocent. The Commission needs to find “a strategy for reaching a common understanding,” but it can be quick to do so when the public statements involve particularly sensitive information in the absence of a legitimate justification.

In other instances, the Guidelines condemn seemingly unilateral communications and shift the burden on the parties to prove their lawfulness. Passive listeners are deemed to have an obligation to reject the information somehow or else risk being charged with a concerted practice. The Guidelines say that “a situation where only one undertaking discloses strategic information to its competitor(s) who accept(s) it can also constitute a concerted practice.”31 According to the Commission, “It is then irrelevant whether only one undertaking unilaterally informs its competitors of its intended market behavior, or whether all participating undertakings inform each other of the respective deliberations and intentions.”32 The Commission goes on to say that a purely passive listener can be fined under Article 101:

[M]ere attendance at a meeting where a company discloses its pricing plans to its competitors is likely to be caught by Article 101, even in the absence of an explicit agreement to raise prices. When a company receives strategic data from a competitor (be it in a meeting, by mail or electronically), it will be presumed to have accepted the information and adapted its market conduct accordingly unless it responds with a clear statement that it does not wish to receive such data.33

This language is broad and troublesome if applied to public statements. But in reality, it apparently is meant for private communications among competitors, where the particular facts might suggest a greater justification to infer that a listener’s silence constituted consent.34 In any event, the Guidelines show the Commission’s willingness to shift the burden of proof when it comes to disclosures of competitively sensitive information, something to be kept firmly in mind in the context of investor analyst calls.

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30 Horizontal Guidelines, supra note 17, ¶ 63.
31 Id. ¶ 62.
32 Id.
33 Id.
Managing the Risks

Although unilateral invitations to collude are not an infringement in Europe, the type of conduct found unlawful in the United States under that theory can certainly motivate the Commission and inspire a burdensome investigation. The Commission’s position on presumptions and burdens of proof, combined with its stated view of concerted practices, should make companies alert to the legal consequences in Europe as well as the United States so that the risks can be managed.

European authorities can be suspicious of public disclosures of sensitive information and, although they do not have Section 5 of the FTC Act at their disposal, the authorities can try hard to find the additional elements of proof needed for a concerted practice. And in the Commission’s view, the proof can come from events entirely outside the speaker’s control, such as the public or private responses from the speaker’s competitors. At the very least, these circumstances can shift the burden of proof to the parties to prove a negative—that no common understanding existed.

The Commission does recognize that public statements may require more evidence than private ones before being found unlawful. Private conversations between competitors can be viewed as inherently suspicious by the enforcers, in any country, and the enforcers can infer an infringement based on a limited amount of additional circumstantial evidence. But there is nothing inherently suspicious about analyst calls unless and until the topics move beyond what investors typically need to know and move closer to what cartelists need to know. The still controlling Wood Pulp case saddles the Commission with the burden of proving that the intended audience was indeed competitors and that the disclosures lack a legitimate business justification. This is true even in the face of parallel pricing behavior. And unlike in the United States, the Commission would have to show at least some sort of response from rivals, enough to make the practice “concerted,” although the contours of this element will continue to be litigated.

Yet this uncertainty in Europe should not cause undue alarm. As in the United States, the risks can be managed with careful preparation of the executives conducting analyst calls. Nor should a company be precluded from providing information genuinely important to investors. Some basic precautions should reduce the risk in Europe as in the United States. First, speakers should use caution when discussing the company’s pricing or output strategy. If these topics must be discussed, comments should be strictly limited to what investors need to know. Second, statements about the activities of competitors, or industry prices, also should be made with caution to avoid an appearance that the intended audience is competitors rather than investors. Finally, speakers should be aware that the authorities in the United States and European Union may monitor earnings calls and scrutinize transcripts.

In other words, the absence of precedent in the EU relating to analyst calls may not stop the authorities from investigating them. But neither should it inhibit companies from managing that risk with some basic measures informed by the Commission’s general approach to public statements and concerted practices.●
Paper Trail: Working Papers and Recent Scholarship

Editors’ Note: In this edition our editors review two papers: a forthcoming article by Robert Klonoff, in which he surveys and critiques recent decisions that demonstrate what he identifies as disturbing trends in the federal case law of class actions; and a paper by DOJ economists Yan Li and Russell Pittman on the proposed AT&T/T-Mobile merger, in which they conclude that there is no evidence of any substantial scale efficiencies that would have been generated by the merger. Send suggestions for papers to review to: page@law.ufl.edu or jwoodbury@crai.com.

—WILLIAM H. PAGE AND JOHN R. WOODBURY

Recent Papers


In this paper, Robert Klonoff, Dean of the Lewis & Clark Law School and a leading class action scholar, identifies several “disturbing trends”1 in the federal case law of class actions since the adoption of Federal Rule of Civil Procedure 23(f)2 in 1998 and the enactment of the Class Action Fairness Act in 2005.3 His primary targets are the Supreme Court’s decisions in Wal-Mart Stores, Inc. v. Dukes,4 AT&T Mobility LLC v. Concepcion,5 and (going back further) Amchem Products, Inc. v. Windsor,6 but he also criticizes numerous recent appellate and district court decisions. He acknowledges that opposing, class-friendly decisions have also been issued at all levels. Nevertheless, Klonoff argues that the wide range of decisions “that cut back on the ability to pursue classwide relief represents a troublesome trend that undermines the compensation, deterrence, and efficiency functions of the class action device.”7 Although some of the decisions he discusses do not primarily affect antitrust class actions, antitrust practitioners will likely find Klonoff’s survey interesting.

Klonoff notes that, for much of the history of class actions, a familiar narrative has portrayed them as abusive because they enrich class counsel without providing significant redress to class members. At the heart of this narrative is the idea that a court’s decision certifying a class imposes an overwhelming pressure on the defendant to settle rather than risk a full trial and a potentially “bankrupting” judgment. This coercive characteristic of certification was especially troubling as

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2 Fed. R. Civ. P. 23(f) now provides in relevant part: “A court of appeals may permit an appeal from an order granting or denying class-action certification under this rule if a petition for permission to appeal is filed with the circuit clerk within 14 days after the order is entered.”
5 131 S. Ct. 1740 (2011).
7 Klonoff, supra note 1, at 5.
long as the certification decision was not immediately appealable. Even if a defendant thought the decision was wrong, it could not seek review without risking a trial and crushing jury verdict. Jurisdictional constraints also magnified the concerns because a small number of pro-plaintiff state courts routinely certified classes and approved settlements in cases against nonresident defendants.

Judge Posner changed the landscape, Klonoff argues, by his 1995 opinion in Rhone-Poulenc,8 which used mandamus to review a class certification decision, identifying the decision’s coercive effect as a justification for issuing an extraordinary writ. This and other limiting decisions by federal courts set the stage for adoption of Rule 26(f) and later for the enactment of CAFA, which drastically reduced the usual standards for diversity jurisdiction,9 thus giving federal district courts subject matter jurisdiction over most state-law class actions, either by original filing or by removal. Once in federal court, the state-law cases with common issues can be transferred to a single district for pretrial, including a decision on class certification, which is then potentially appealable under Rule 26(f).

Reviewing the experience of several years of practice under these reforms, Klonoff argues that district court and appellate decisions have erred in a variety of ways. Most of the mistakes involve unduly strict standards for class certification, as might be expected given the assumption that certification is the decisive moment in class litigation. As important as any, however, are recent decisions on the effect of contractual arbitration clauses, particularly those that include class waivers.

Appeals Under Rule 23(f) Have Dramatically Favored Defendants

Although applicable to both grants and denials of certification, defendants bring most appeals and these have succeeded at a much higher rate. Klonoff reports that defendants have taken 70 percent of the appeals under Rule 23(f), and have obtained reversals of 71 percent of those decisions. CAFA had magnified these effects by allowing a host of state-law class actions to reach federal district court and then be subject to interlocutory appeals at the certification stage. Klonoff argues that courts too freely grant review to defendants simply on the ground that certification imposes pressure to settle. Many procedural decisions increase pressure to settle. Rather, he contends that, to justify immediate appeal, a certification decision should involve an unsettled question of law.

Judges Are Inappropriately Resolving Factual Merits Issues at the Certification Stage

In General Telephone Co. v. Falcon,10 the Supreme Court required courts to conduct a “rigorous analysis of the requirements for certification,” even if that meant “prob[ing] behind the pleadings.”11 Judge Easterbrook, in Szabo v. Bridgeport Machines, Inc.,12 went further to require courts actually to resolve merits issues if they intersected with the requirements for certification. Other cir-

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8 In re Rhone-Poulenc Rorer Inc., 51 F.3d 1293 (7th Cir. 1995).
9 If there are 100 or more members in the aggregate in all proposed plaintiff classes, then the statute uses a standard of minimal rather than complete diversity and establishes aggregate amount in controversy requirement of over $5 million rather than an individual requirement of over $75,000. 28 U.S.C. § 1332(d).
10 457 U.S. 147 (1982).
11 Id. at 160–61.
12 249 F.3d 672 (7th Cir. 2001).
cuits have followed suit. In *In re Hydrogen Peroxide Antitrust Litigation*, for example, the Third Circuit required a district court, before certifying a class, to resolve a conflict between qualified experts on whether impact of a conspiracy on direct purchasers could be established by class-wide proof. It was not enough for the plaintiff to make a “threshold showing” that classwide proof would be forthcoming.

Klonoff objects that this requirement delays the certification decision until discovery is complete, long after the “early practicable time” Rule 23(c)(1)(A) demands. More important, he argues, the decision violates the right to a jury trial by requiring the court to resolve key factual issues on the merits. He endorses the majority opinion in *Behrend v. Comcast Corp.*, a 2011 Third Circuit antitrust decision that interpreted *Hydrogen Peroxide* to require only that the plaintiff offer evidence “that the element of antitrust impact could be proven at trial through evidence that was common to the class, and that a common methodology was available to measure and quantify damages on a classwide basis.” At the same time, Klonoff believes the district court must conduct a full Daubert review of experts’ qualifications at the certification stage to determine if the plaintiff will be able prove impact by admissible evidence.

**Courts Have Too Readily Denied Certification Through Excessive Rigidity**

Some courts have denied certification on the grounds that the class is inadequately defined—usually because it would require an individualized inquiry to determine if someone was even a member of the class. Klonoff suggests that, rather than deny certification in those situations, courts should try to redefine the class more narrowly and clearly. Other courts, he argues, have wrongly insisted on specific proof that the defined class satisfies the numerosity requirement, rather than using reasonable inferences or common sense to make their findings.

Klonoff is particularly critical of the Supreme Court’s treatment of the commonality requirement in *Wal-Mart v. Dukes*. *Dukes* was a 23(b)(2) class action, i.e., one asserted to arise from acts or refusals to act “on grounds generally applicable to the class so that final injunctive relief or corresponding declaratory relief is appropriate respecting the class as a whole”; it was therefore not subject to 23(b)(3)’s requirement that common issues “predominate” over individualized issues. Yet the majority opinion required the plaintiff to assert a common issue that was central to its claim. In doing so, Justice Scalia uncharacteristically relied on standards proposed in a law review article that, Klonoff and the dissenting justices argued, analyzed the meaning of the predominance requirement, not commonality.

Klonoff also criticizes courts that deny certification on the grounds that the class representatives or counsel do not adequately represent the class because they have not asserted all of the potential claims for relief. Courts assume that res judicata might bar the omitted issues. Klonoff

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13 *E.g.*, *In re Initial Public Offerings Secs. Litig.*, 471 F.3d 24, 27 (2d Cir. 2006).
14 552 F.3d 305 (3d Cir. 2008).
15 *Id.* at 307.
17 Klonoff, *supra* note 1, at 21.
argues that res judicata should not preclude issues that are omitted because they are not appropriate for class treatment. In any event, he contends that courts should limit the scope of the judgment to preserve the omitted claims.\(^\text{21}\)

**The Supreme Court in *Dukes* Incorrectly Denied Certification of a 23(B)(2) Class Action that Included Back Pay Claims**

Before *Dukes*, according to Klonoff, courts had established various standards for inclusion of claims for monetary relief in injunction class actions under 23(b)(2), but all had allowed inclusion of back pay claims in employment discrimination cases as an aspect of the injunctive relief. In *Dukes*, the Supreme Court unanimously concluded that the back pay claims at issue sought individualized damages and thus had to meet the more exacting standards of 23(b)(3).

**Courts Wrongly Interpret the Predominance Requirement to Exclude Certain Cases Categorically**

Some courts have denied certification of 23(b)(3) classes alleging fraud simply because they involve individualized issues of reliance. Other courts have denied certification of nationwide classes simply because they involved the application (or potential application) of multiple states’ laws. Klonoff cautions that the predominance inquiry requires weighing the common issues against individualized issues. In some cases, issues of reliance might be similar for all class members; even if they are not, the existence of a common fraudulent scheme might be so central to the case that it predominates over individual representations. Similarly, he argues, state laws can be essentially the same in their requirements, or can at least be grouped in categories for class treatment.

**Courts Have Refused to Certify Settlement Classes on Grounds that Should Apply Only to Trial Classes**

In some instances parties agree to settlement terms for the class certification decision. In those cases, the court must not only determine the fairness of the settlement, it must also certify the class. The Supreme Court’s decision in *Amchem* held that settlement classes must meet the standards of certification, except those relating to manageability of a trial. For damage class actions, the most important requirement is predominance. Many cases have denied certification of settlement classes on the grounds that individualized issues predominated, even though those issues would never have to be tried.

Klonoff briefly discusses the Third Circuit’s remarkable recent en banc decision in *Sullivan v. DB Investments*,\(^\text{22}\) which certified a nationwide settlement class of indirect purchasers of DeBeers diamonds, even though many states do not authorize indirect purchaser standing under any theory.\(^\text{23}\) He endorses the *Sullivan* majority’s application of *Amchem*, which excluded variations in state law from the analysis of predominance in settlement classes because those differences related primarily to trial manageability. Nevertheless, he argues that *Amchem* should be displaced by clearer guidance for settlement classes. He describes various efforts to amend Rule 23(b) to

\(^{21}\) Such an approach may, however, impede settlements because defendants often demand broad preclusion as a condition of establishing a common fund.


\(^{23}\) *Id.* at 302.
authorize settlement classes on different grounds than trial classes, including an American Law Institute recommendation (that he helped draft)\textsuperscript{24} that would allow a court to:

approve the settlement if it finds adequate representation; determines that the relief afforded by the settlement is fair (and that the class members are treated equitably); finds that the settlement was negotiated at arm’s length; determines that numerosity is satisfied; and finds the class definition “sufficient to ascertain who is and who is not included in the class.”\textsuperscript{25}

Strict application of certification standards to settlement classes, he argues, discourages settlements that would be substantially better than the alternatives for class members.

**Courts Have Denied Certification of Issues Classes on Improper Grounds**

Despite Rule 23(c)(4)’s authorization of class actions “with respect to particular issues,” some courts refuse to certify issues classes unless the action as a whole meets certification standards.\textsuperscript{26} Klunoff favors the approach of other circuits that authorize issues classes when it would “materially advance” the resolution of the dispute. He notes, for example, an opinion by Judge Posner certifying issues classes as to liability questions in a post-\textit{Dukes} employment discrimination case, leaving the damages issues for individualized proceedings.\textsuperscript{27} Concerns some courts have raised about the effect of this bifurcation of issues on the right to a jury trial, he suggests, are misplaced.

**Courts Have Enforced Arbitration Clauses to Foreclose Class Actions**

In addition to his concerns about heightened standards of class certification, Klunoff expresses concern that the Supreme Court’s recent interpretations of the Federal Arbitration Act\textsuperscript{28} foreclose class relief and may entirely foreclose rights that plaintiffs can practically enforce only by class actions—so-called negative value suits. In \textit{Stolt-Nielsen},\textsuperscript{29} the Court held that when parties had agreed to a contractual arbitration clause that did not mention class treatment of claims, the FAA foreclosed classwide arbitration of an antitrust claim. Last year, in \textit{Concepcion},\textsuperscript{30} the court held that an arbitration clause with a class action waiver foreclosed classwide arbitration of small state-law claims for wrongful charges in phone bills, and that the FAA preempted a state doctrine that condemned the clauses as unconscionable. Klunoff cites some scholars who argue that \textit{Concepcion} will foreclose consumer and employment class actions entirely.

For federal statutory claims, including antitrust claims, the issues and the outlook are somewhat different. Klunoff notes that in \textit{American Express III},\textsuperscript{31} the Second Circuit recently held an arbitration clause unenforceable on the grounds that it effectively foreclosed antitrust claims that plaintiffs could, as a practical matter, vindicate by a class action. (As I write this note, the Second

\textsuperscript{24} \textit{Principles of the Law of Aggregate Litigation} §§ 3.05, 3.06 (Am. Law Inst. 2010).

\textsuperscript{25} Klunoff, supra note 1, at 55 (quoting \textit{Principles of the Law of Aggregate Litigation}, supra note 24, § 3.06(b)).

\textsuperscript{26} \textit{E.g.}, Castano v. American Tobacco Co., 84 F.3d 734 (5th Cir. 1996).

\textsuperscript{27} McReynolds v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 672 F.3d 482 (7th Cir. 2012).

\textsuperscript{28} 9 U.S.C. § 2 (agreements to arbitrate “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract”).


\textsuperscript{30} \textit{AT&T Mobility LLC v. Concepcion}, 131 S. Ct. 1740, 1744–45 (2011).

\textsuperscript{31} \textit{In re Am. Express Merchants’ Litig.}, 667 F.3d 204 (2d Cir. 2012).
Circuit has just denied the request of “an active judge” for a rehearing en banc of *American Express III.*[^32] It did so over a strongly worded dissent by Chief Judge Jacobs, joined by two others, arguing that the panel decision was inconsistent with *Concepcion* and with the FAA and was “already working mischief in the district courts.”[^33]

In a final Part of his paper, Klonoff sets boundaries on his argument and makes some general suggestions for reform. He acknowledges that some of the Supreme Court’s recent decisions have favored class actions,[^34] although he believes they are of less practical importance than *Dukes, Concepcion,* and *Amchem.* He also emphasizes that there are divisions among and within circuits, leading to a complex pattern of forum shopping after CAFA: plaintiffs tend to file originally in federal court in class-friendly circuits and districts, while defendants tend to remove to federal court in less class-friendly circuits and districts.

Finally, and importantly for readers of *The Antitrust Source,* he notes that some kinds of class actions continue to be certified regularly. Among these are securities fraud, wage and hour, ERISA, and “to a lesser extent,” antitrust cases.[^35] Klonoff’s brief reference to antitrust class actions is consistent with my own recent study, which finds that federal courts routinely certify direct purchaser classes and that the pattern for indirect purchaser classes mirrors the split in state court decisions before CAFA.[^36]

Despite these qualifications, Klonoff asserts that law reform is necessary to correct some of the restrictive decisions he considers in the paper. In some instances, such as numerosity and class definition, district courts have discretion to adopt a less restrictive approach. On the other hand, Klonoff recommends adopting some (unspecified) amendments to Rule 23 to clarify the evidentiary requirements for class certification, the standards for commonality, and the standards governing certification of settlement classes. He also proposes legislation to overrule *Concepcion.*

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**William H. Page**

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In the recent agency review of the proposed AT&T/T-Mobile merger, a key point of contention between the agencies—the Federal Communications Commission and the Department of Justice—and the merging parties was the scope of the expected, cognizable efficiencies.[^37] AT&T

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[^33]: Id. at *5 (Jacobs, C.J., dissenting).

[^34]: See, e.g., Erica P. John Fund, Inc. v. Halliburton Co., 131 S. Ct. 2179 (2011) (plaintiff need not prove causation of loss for class certification); Smith v. Bayer Corp., 131 S. Ct. 2368 (2011) (federal district court that had denied certification could not enjoin a state court from certifying a similar class); Shady Grove Orthopedic Assocs. v. Allstate Ins. Co., 130 S. Ct. 1431 (2010) (plurality opinion) (federal district court could certify a class action under Rule 23 even if a state statute prohibited class actions for the same claim).

[^35]: Klonoff, supra note 1, at 71.


argued that the efficiencies that would result from the merger would be so substantial that they
would more than offset any tendency for prices to increase as a result of the merger. In this paper,
Yan Li and Russell Pittman—economists at the Antitrust Division of the DOJ—summarize the
basis for the agencies’ views that the evidence for the efficiencies presented by the merging par-
ties was weak, at best. The authors then offer an alternative method for identifying the extent to
which there may be unrealized cost savings that could have been expected from the merger. They
conclude that there is no evidence of any substantial scale efficiencies that would have been gen-
erated by the merger.

Summary of AT&T’s Efficiency Claims and Agency Responses
By way of background, in the course of the FCC’s review of the proposed merger, AT&T submit-
ted to the FCC and DOJ iterations of a detailed engineering model that provided estimates of the
efficiencies that could be expected from the merger. AT&T’s economists then employed these esti-
mates in a simulation model that was used to estimate the likely price changes from the merger
in fifteen local markets. AT&T’s economists concluded that the most likely effects of the merger on
(quality-adjusted) prices in these markets were either very small increases or actual declines.

The authors of this paper first provide an estimate of the magnitude of the efficiencies claimed
by AT&T. Because the cost-savings estimates are not in the public record, the authors provide an
interesting way of inferring the claimed efficiencies from publicly available information. They infer
that the estimated efficiencies proffered by AT&T must have been in the range of 13.6% to 25.8%,
which would be substantial indeed.

While the DOJ’s complaint simply notes that the efficiency claims were not credible, the FCC
Staff identified a number of specific reasons for skepticism. The Li and Pittman paper notes that
the Staff’s strongest criticism focused on the algorithm used to compare the number of cell sites
needed by the merged firm and those needed by the standalone AT&T and T-Mobile. In particu-
lar, the FCC Staff found that the algorithm “appears to cause the model to greatly overestimate
incremental costs, and the overestimate is much greater for the standalone firms than the merged
firm.”

An Alternative Approach to Gauging the Significance of the
Proposed Merger’s Efficiencies
Of course, the fact that AT&T did not convince the agencies that there were substantial cogniz-
able efficiencies that could be expected from the merger does not mean that there were none. To
determine if in fact such efficiencies were likely to exist, the authors estimate a “translog” pro-
duction function for the provision of wireless services. The translog production function is one that
has been widely used in economics, a key advantage among others being that (roughly speaking) it imposes fewer restrictions than other models on the input combinations that can be used to
produce any given level of output. In addition, the formulation used in the paper allows for the


39 Id. ¶ 147. The FCC noted numerous other reasons to question AT&T’s engineering and simulation models. For example, using the cost-
savings estimates from the engineering model to predict the going-forward costs of the standalone AT&T in the simulation model gener-
ated unreasonable predictions of AT&T’s standalone subscriber counts and market shares. In addition, while AT&T announced its intention
to withdraw the T-Mobile brand, the simulations assumed its continued existence. For a summary of these and other FCC objections, see
Besen, supra note 37, at 31–33.
The authors use two different measures of efficiency. One is the standard estimate of returns to scale (RTS). For example, the authors ask whether a doubling of all inputs leads to a doubling of output (constant RTS), more than a doubling of output (increasing RTS), or less than a doubling of output (decreasing RTS). If there are increasing returns to scale, then the merged firm would realize cost savings that (at their current output levels) neither stand-alone firm could attain.

The second measure is a scale efficiency (SE) metric, effectively measuring the extent to which the actual productivity of inputs used by a firm falls short of the maximum attainable. The maximum value the SE can attain is one, indicating that the firm is operating at its most productive scale size. To the extent that SE is less than one, the firm is not operating at its most productive scale and efficiencies could be realized by growing larger.\(^{40}\)

The paper notes that there are two kinds of production/cost economies that are relevant. One is economies of density—for any given size of the network, the merger will lead to more efficient utilization of spectrum and cell towers in particular, which would be specific to particular geographic areas. The other is firm-wide economies that are independent of density in local areas—the authors cite those savings as ones that might be associated with marketing, customer service, procurement, and “overall company administration.”\(^{41}\) Since the data used by the paper is firm-wide (described below), the authors acknowledge that they cannot estimate the unrealized efficiencies (if any) at the level of the local market.

The data used to estimate the wireless services production function are sourced from the annual reports of twenty-two wireless service providers in the United States and six other countries (Canada, the United Kingdom, France, Germany, China, and Korea), spanning the period 1998–2007 (although data for all years are not available for all carriers). The measure of output is the total revenue of the carrier divided by the national average mobile price. The three inputs used are labor (the number of employees working in the mobile service segment), materials (measured as material costs divided by a materials price index), and capital (measured as total depreciation and amortization costs divided by the capital cost, which is the weighted average cost of borrowing reported in the annual reports).

Using these data, the paper estimates the production function for all years and firms. Firm-specific fixed effects are used to capture unmeasured factors associated with each carrier while a common time trend is used to capture overall changes in technology.\(^ {42}\) Using the estimated parameters of the production function, the authors then generate estimates of the RTS and SE scores for all of the carriers in the sample using the most recent data (2007) in the sample. For RTS, there is a possibility that the firm is not on the production “frontier,” i.e., that it is not producing output efficiently.

40 Note that even if there are increasing RTS, or if the SE is less than one, that does not mean that the efficiencies would be cognizable. There may be other ways of attaining the necessary scale short of merger. The only efficiencies that would “count” are those over and above those that could be reasonably attained without the merger.

41 I note in passing that I interpreted AT&T’s claimed efficiencies at the local level to include both density and “scale” economies—within any given local area, the costs of expanding service would be lower than that for the (sum of the costs) of the standalone firms.

42 I should note that the authors are very careful to test (1) the validity of the translog production function against another production function that has been used extensively in the literature (the Cobb-Douglas production function) but which employs more restrictive assumptions on the use of input combinations; (2) the assumption that technology has changed over time; and (3) the validity of the assumed distribution for the inefficiency component of the error term in the estimation. These tests suggest that “the preferred empirical frontier model for our study is a translog stochastic production function with the inclusion of time effects, and normal truncated-normal distribution in the inefficiency errors.” (p. 11).
the paper observes that “on average, almost all observed firms operate in either constant . . . or mildly increasing returns to scale.” (p. 14). In particular, the RTS estimates suggest that both AT&T and T-Mobile are in the range of constant returns to scale. If so, then the merger would not be expected to generate any significant scale-related efficiencies. Similarly (and recalling that the maximum value of SE is one), the SE scores for all carriers generally and for AT&T and T-Mobile in particular are not statistically different from one, suggesting that both firms are already operating at their most productive scale and one would not expect any efficiency gains from the merger.

**Final Observations**

Although the approach taken by the authors is interesting and even promising, it suffers from sufficient data deficiencies such that it would probably not have been particularly probative in the evaluation of the AT&T/T-Mobile merger. For example, note 27 of the paper reports that the data to estimate the production function frontier for AT&T were unavailable because the information in AT&T’s annual reports was apparently not sufficient to disaggregate the labor, material, and capital inputs. (The authors do provide estimates of the RTS and SE “scores” for AT&T, but it is not obvious how those estimates were generated.) The inability to estimate the production function frontier for AT&T in a manner comparable to that of other wireless providers would seem to render the conclusions of the paper too tentative for evaluating the effects of the proposed AT&T/T-Mobile merger.

In addition, there are numerous unanswered questions that would need to be addressed for this analysis to be probative rather than merely suggestive. As one example, output—total revenues divided by price—is not interpreted as anything concrete. To be sure, total revenue equals price times quantity, but how is the quantity here defined? Is there any reason to believe that this inferred quantity is highly correlated with, say, megabytes of data (and voice minutes converted to megabytes), which would be a reasonable output measure? Alternatively, the wireless providers can be viewed as producing multiple outputs, depending upon the characteristics of the various plans and handset devices (e.g., 3G vs. 4G devices, limitations on data usage) and of the quality of service offered by the various carriers (e.g., percentage of dropped calls, geographic coverage). A multi-output approach might yield results that are quite different than those obtained by the authors when assuming a single homogeneous output.\(^4\)

The paper also fails to discuss how the different regulatory regimes in each of the seven countries might affect the results. This might be partially solved with country-specific fixed effects (which are curiously not included in the estimation), but even that may not be sufficient where regulatory regimes are changing.

Most importantly, the data available can only be used by the authors to address scale and efficiency effects at a national level and so cannot account for the very efficiencies that AT&T and its economists identified as substantial: significantly lower costs in local geographies as a result of what the paper earlier described as economies of density. Thus, the paper could be viewed as addressing a component of the claimed efficiencies (and the paper may be more persuasive on that score) but not what may be the most critical efficiencies component of the AT&T argument.

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\(^4\) If one considered the output calculation as including significant measurement error (as opposed to misspecification of the model), then any correlation between the errors in measuring outputs and the inputs (for example) could lead to parameter estimates biased towards zero. If AT&T were in a range of increasing RTS, that estimate might be sufficiently biased that it would generate an estimate suggesting constant RTS. Having said that, as I note below, data availability likely was insufficient to adopt a more refined output measure. My suggestion here is only that discussing the implications of these alternatives for the paper’s more limited analysis would have been helpful.
It may well be that with access to confidential data provided by the parties in the AT&T/T-Mobile proceeding, the paper could have overcome some of the clear data limitations confronted by the authors. It is certainly true that perfecting an analysis such as the one in this paper will provide an alternative way of addressing efficiency claims in future proposed wireless mergers and, more generally, efforts like this are certainly worth pursuing. While in graduate school, I once asked a question about how one could rely on any study with only a relative handful of data points. My professor responded tongue-in-cheek, “If that’s all the data God gives you, who are we to argue with God?” Perhaps, but even so, the data in this paper, while plentiful, nonetheless did not match the sophistication of the empirical exercise and it would be helpful if the authors could indicate the extent to which that limits the confidence one can have in their results.

—JOHN R. WOODBURY