Five Arguments Laid to Rest After Actavis

Michael Carrier offers an in-depth analysis of the recent Supreme Court reverse-payment decision in Actavis, focusing on the Court’s rejection of several arguments used by the settling parties and adopted by the appellate courts in the pre-Actavis world. Carrier argues that by rejecting these arguments, the Court has ensured a robust role for antitrust in evaluating these agreements.

Illuminating the Story of China’s Anti-monopoly Law

FTC Commissioner Maureen Ohlhausen provides an account of the China Competition Policy Forum—Competition Policy in Transition—held this summer in Beijing. Commissioner Ohlhausen reviews the highlights of the Forum and offers a behind-the-scenes view of antitrust enforcement in China.

A Five Year Review of Merger Enforcement in China

Editor Fei Deng and Cunzhen Huang summarize recently released information from MOFCOM to shed light on merger enforcement in China. The authors conclude that merger enforcement in China resembles enforcement in the United States and the European Union in many respects but that important differences can lead to divergent results.

The Elements of a Policy Statement on Section 5

Neil Averitt reviews the current debate on the scope of Section 5 of the FTC Act and asserts that none of the current proposals emanating from the FTC to clarify the purposes and scope of Section 5 is satisfactory. He proposes a broader but bounded approach that could serve as a basis for a policy statement by the agency.

Paper Trail: Working Papers and Recent Scholarship

Editor Allan Shampine reviews a paper by Fiona Scott Morton and Carl Shapiro on the role of patent assertion entities (PAEs) and their effect on competition. Shampine contends that while the competitive concerns of PAEs are persuasively delineated in the paper, it remains unclear how those concerns should best be addressed.
Five Arguments Laid to Rest After Actavis

Michael A. Carrier

The Supreme Court’s decision in FTC v. Actavis has received widespread attention for its antitrust analysis of settlements by which brand-name drug companies pay generics to delay entering the market. Much of the attention has focused on the continued enforcement of these agreements (known as “pay-for-delay” or “reverse payment”) and the logistics of applying the Court’s rule-of-reason analysis. While the attention has been riveted on how judicial analysis of reverse-payment settlements will proceed going forward, less attention has been paid to the watershed nature of the decision in rejecting pro-settlement arguments offered by the settling parties and adopted by the federal appellate courts.

On the broadest level, the consequences of the decision are historic. For if Chief Justice Roberts had convinced two of his colleagues to join his dissent, judicial scrutiny of these agreements would have ended. In a nutshell, it would have been “game over.” Analysis would have occurred under the nominal “scope-of-the-patent” test, which, in neglecting antitrust law and the Hatch-Waxman Act and assuming the central issues of patent validity and infringement, would have led to the blessing of nearly all agreements.

That did not happen. And while it remains to be seen how lower courts will flesh out the decision, it is not too early to reflect on the breadth and intensity of several arguments that no longer will be successfully invoked to uphold these settlements. This is important because of the intractability of the debates that have raged between the drug companies and the majority of federal appellate courts on one side and the Federal Trade Commission and private plaintiffs on the other.

This article catalogs the arguments that the settling parties have offered, and the majority of appellate courts have adopted, in upholding the agreements. It highlights their prevalence before Actavis and their rejection in the opinion. The arguments concern: (1) the scope of the patent, (2) the importance of settlements, (3) the consequence of large payments, (4) the likelihood of settlement without payment, and (5) the presence of multiple generic challengers. The Actavis opinion was crucial in eliminating (or at a minimum dramatically reducing) the effect of these arguments.

---

3 The Sixth Circuit did not adopt the arguments but instead treated the agreements as per se illegal. See In re Cardizem CD Antitrust Litig., 332 F.3d 896 (6th Cir. 2003).
Scope of the Patent

The “scope-of-the-patent” test is the most notable casualty of Actavis. No framework has wrought as much havoc in the area in the past decade. To be sure, any test focused on a patent’s scope does not need to be deferential to the point of near-per-se legality. For example, the version employed by the Eleventh Circuit in Valley Drug Co. v. Geneva Pharmaceuticals, Inc. was more nuanced, with the court’s antitrust assessment comparing the parties’ settlement to “the likelihood” that the brand firm would “obtain[] [the] protections” of “the preliminary injunction and stay mechanisms.”

But later courts abandoned any such nuance, applying a version that assumed the patent was valid and infringed and upholding the agreement as long as it did not extend beyond the patent’s expiration date. In In re Tamoxifen Citrate Antitrust Litigation, the Second Circuit found that the brand was “entitled to protect its . . . patent monopoly through settlement,” that the “question for th[e] [c]ourt” was “whether the settlement extended the patent’s scope,” and that the settlement did not “unlawfully extend the reach” of the patent. In In re Ciprofloxacin Hydrochloride Antitrust Litigation, the Federal Circuit found that “[t]he essence of the inquiry is whether the agreements restrict competition beyond the exclusionary zone of the patent.” The court held that excluding generics “from profiting from the patented invention” was “well within [the brand’s] rights as the patentee.”

And in the Eleventh Circuit’s decision in Actavis, the court explained that “absent sham litigation or fraud in obtaining the patent, a reverse payment settlement is immune from antitrust attack so long as its anticompetitive effects fall within the scope of the exclusionary potential of the patent.” Addressing ambiguity from earlier decisions like Valley Drug, the court explained that “the phrase ‘strength of the patent’ refers to the potential exclusionary scope of the patent—that is, the exclusionary rights appearing on the patent’s face and not the underlying merits of the infringement claim.”

The settling parties and their supporters have articulated similar approaches. In their briefs in the Actavis case (to pick just one of many potential settings), they argued that “the proper analysis should start from the perspective of patent law and . . . take care to preserve the full scope of rights granted with the patent”; that the test to determine antitrust liability “begins by inquiring whether the restraint or conduct exceeds the scope-of-the-patent”; that court decisions “focus on whether patent-related restraints exceed the substantive or temporal scope of the patent”;

---

4 344 F.3d 1294 (11th Cir. 2003).
5 Id. at 1312.
6 466 F.3d 187, 209 n.22, 213 (2d Cir. 2006).
7 544 F.3d 1323, 1336 (Fed. Cir. 2008).
8 Id. at 1333.
9 FTC v. Watson Pharm., Inc., 677 F.3d 1298, 1312 (11th Cir. 2012).
10 Id. at 1311 n.8.
12 Brief for Respondents Par/Paddock at 38, FTC v. Actavis, 133 S. Ct. 2223 (No. 12-416).
13 Brief for Respondent Solvay Pharmas., Inc. at 14, FTC v. Actavis, Inc., 133 S. Ct. 2223 (No. 12-416) [hereinafter Solvay Brief].
and that “the bounds of the patent monopoly” constitute “the line of demarcation between conduct that is lawful and conduct that may be suspect.”

For all these reasons, the Court’s decision in Actavis was momentous. The Supreme Court made clear that this deferential scope test is not appropriate in determining the antitrust legality of reverse-payment settlements. Just because a payment might be within the scope of a valid and infringed patent does not mean that “that fact, or characterization, can immunize the agreement from antitrust attack.”

The Court correctly explained that the patent “may or may not be valid, and may or may not be infringed.” It understood that the owner of “an invalidated patent” and “even a valid patent” employed against “products . . . that do not actually infringe” cannot refuse to license it or “charge a higher-than-competitive price.” And it recognized that settlements end the “paragraph IV litigation” that “put the patent’s validity at issue.”

Given these observations, the Court found it “incongruous” to “determine antitrust legality by measuring the settlement’s anticompetitive effects solely against patent law policy, rather than by measuring them against procompetitive antitrust policies as well.” Both patent and antitrust policies are “relevant in determining the ‘scope of the patent monopoly’—and consequently antitrust law immunity—that is conferred by a patent.” In short, the Court made it crystal clear that settling parties are no longer able to effectively immunize their settlements by claiming that brand payments to generics lie within the “scope of the patent.”

Importance of Settlements

The second casualty of Actavis is the near-dispositive weight of the policy favoring settlement. In Schering-Plough Corp. v. FTC, the Eleventh Circuit explained that settlements “provide a number of private and social benefits as opposed to the inveterate and costly effects of litigation.” Patent litigation “breeds a litany of direct and indirect costs, ranging from attorney and expert fees to the expenses associated with discovery compliance.” And the “caustic environment of patent litigation” could “decrease product innovation by amplifying the period of uncertainty” that affects research, development, and marketing.

---

15 Actavis, 133 S. Ct. at 2230.
16 Id. at 2231.
17 Id. (emphasis omitted); see also In re K-Dur Antitrust Litig., 686 F.3d 197, 214 (3d Cir. 2012) (test “assumes away the question being litigated in the underlying patent suit, enforcing a presumption that the patent holder would have prevailed”); Michael A. Carrier, Why the “Scope of the Patent” Test Cannot Solve the Drug Patent Settlement Problem, 16 Stan. Tech. L. Rev. 1, 5–7 (2012) (pointing to problems with scope test, including assumption of validity and neglect of infringement issues).
18 Actavis, 133 S. Ct. at 2231. See also K-Dur, 686 F.3d at 214 (“As a practical matter, the scope of the patent test does not subject reverse payment agreements to any antitrust scrutiny,” as “no court applying the scope of the patent test has ever permitted a reverse payment antitrust case to go to trial.”).
19 Actavis, 133 S. Ct. at 2231.
20 Id.
21 402 F.3d 1056, 1075 (11th Cir. 2005).
22 Id.
23 Id.
Viewing patent litigation as lengthy, complex, and costly, courts have regarded settlements as particularly beneficial.24 The Tamoxifen court explained that “courts are bound to encourage . . . settlement[s]” and that “[s]o long as the law encourages settlement, weak patent cases will likely be settled even though such settlements will inevitably protect patent monopolies that are, perhaps, undeserved.”25 The court in Schering found that “[t]he general policy of the law is to favor the settlement of litigation,” and that “the policy extends to the settlement of patent infringement suits.”26 And the court in Cipro pointed to the “long-standing policy in the law in favor of settlements” that “extends to patent infringement litigation.”27

Similarly, in the Actavis briefs, the settling parties and their supporters emphasized that “public policy wisely encourages settlements”28; that “settlements enable the patent holders to manage litigation risk,” which “foster[s] innovation”29; that the FTC's proposed rule of presumptive illegality “would thwart the established judicial policy favoring settlement”30; and that “the law strongly favors resolution of litigation through compromise” because of “the considerable savings gained by settlement.”31

The Court in Actavis recognized “the value of settlements and the patent litigation problem.”32 But it “nonetheless conclude[d] that this patent-related factor should not determine the result,”33 Instead, “five sets of considerations” led the Court to “conclude that the FTC should have been given the opportunity to prove its antitrust claim.”34 In the Court’s own words, those five considerations emphasized that:

- “The specific restraint at issue has the ‘potential for genuine adverse effects on competition.’”
- “These anticompetitive consequences will at least sometimes prove unjustified.”
- “Where a reverse payment threatens to work unjustified anticompetitive harm, the patentee likely possesses the power to bring that harm about in practice.”
- “An antitrust action is likely to prove more feasible administratively than the Eleventh Circuit believed.”
- “The fact that a large, unjustified reverse payment risks antitrust liability does not prevent litigating parties from settling their lawsuit.”35

In short, these considerations reveal the antitrust concern with reverse-payment settlements. And they recognize the agreements’ unjustified antitrust harm and reflection of market power, courts’ ability to analyze the agreements, and parties’ ability to settle cases without reverse payments.

---

24 Recent figures show that patent litigation under the Hatch-Waxman Act in which there is more than $1 million at risk costs $2.65 to $6 million on average. AM. INTELLECTUAL PROP. LAW ASS’N, REPORT OF THE ECONOMIC SURVEY 2013, at 34.
25 466 F.3d at 202, 211.
26 402 F.3d at 1072.
27 544 F.3d at 1333.
28 Actavis Brief, supra note 14, at 51 (citation omitted).
29 PhRMA Brief, supra note 14, at 5.
30 Actavis Brief, supra note 14, at 46.
31 PhRMA Brief, supra note 14, at 20.
32 133 S. Ct. at 2234.
33 Id.
34 Id.
35 Id. at 2234-37.
As a result, any future exhortation to rely on the policy in favor of settlements cannot be considered without incorporating these competing public policies. Given the importance of these five considerations and their lack of direct connection to the policy supporting settlements, the most natural interpretation is that the pro-settlement policy has been subordinated to the facts and antitrust analysis of specific cases.

**Consequences of Large Payments**

The third set of principles flows from the interpretation of large payments. Previous courts had assumed that such payments were a natural, unobjectionable by-product of the Hatch-Waxman Act. Relatedly, courts ignored such payments when determining the antitrust legality of settlements and concluding that a full assessment of the patent-related conduct was not administrable. Finally, backed into the corner of ignoring the payment and abandoning the attempt to determine the patent merits, courts overemphasized the presumption of legality accorded to patents.

In the first element of this analysis, courts claimed that reverse payments frequently occur and do not warrant concern. The *Schering* court explained that “[r]everse payments are a natural by-product of the Hatch-Waxman process” and that “patents, payments, and settlement are . . . all symbiotic components that must work together . . . for the larger abstract to succeed.”

The *Tamoxifen* court noted that reverse payments were “particularly to be expected in the drug-patent context because the Hatch-Waxman Act created an environment that encourages them.” And the *Cipro* court explained that “sizable” reverse payments are a “not unexpected” occurrence under the Act since “the relative risks of litigation are redistributed.” Similarly, amicus briefs in *Actavis* explained that payment “is not a sign of an anticompetitive scheme” but “a natural by-product of the Hatch-Waxman process”; that such payments “are particularly to be expected . . . because the [] Act created an environment that encourages them”; that the Act “shifts the risk of litigation” to the patent holder; and that “the usual form of consideration from the patentee to the infringer—declining to collect a portion of the damages—does not yet exist.”

Courts’ views of reverse payments as natural, innocuous features of the Hatch-Waxman Act led them to ignore payment as a source of relevant evidence in assessing the patent merits. This played a role in their lamenting their inability to analyze patent issues in antitrust litigation. The *Cipro* court concluded that “analysis of patent validity” is not “appropriate in the absence of fraud or sham litigation.” And the Eleventh Circuit in *Actavis* refused to engage in an “after-the-fact calculation of how ‘likely’ a patent holder was to succeed in a settled lawsuit,” seeking to avoid the “turducken task” of deciding “a patent case within an antitrust case about the settlement of the patent case.”

36 402 F.3d at 1074.
37 466 F.3d at 206.
38 544 F.3d at 1333 n.11.
39 PhRMA Brief, supra note 14, at 17.
40 AIPLA Brief, supra note 11, at 22.
41 Id. at 22–23.
42 PhRMA Brief, supra note 14, at 17.
43 544 F.3d at 1337.
44 677 F.3d at 1313.
Amicus briefs also focused on the inadministrability of patent litigation. They stated that “any consideration of the patent merits will inevitably add still more complexity to the antitrust action” 46; that “forcing relitigation of the patent case in a subsequent antitrust suit not only would be unworkable, but also would create a ‘powerful disincentive to settlement’” 47; and (mirroring the Eleventh Circuit in *Actavis*) that “deciding a patent case within an antitrust case” is an “[u]n[palatable] ‘tur[ducken] task.’” 48

Courts acquitted themselves of the difficulties of analyzing the patent merits by emphasizing patents’ presumption of validity. 49 The *Tamoxifen* court found that “the law allows the settlement even of suits involving weak patents with the presumption that the patent is valid.” 50 The *Schering* court relied on the presumption in concluding that a brand firm would not suffer antitrust liability for exclusionary activity unless generics were able to prove a patent’s invalidity or noninfringement. 51 And the *Cipro* court addressed administrability problems by remarking that “a patent is presumed to be valid.” 52 Relatedly, amicus briefs stated that the presumption “is more than a simple procedural device” 53; that the presumption “does not permit the classification of patents as either weak or strong” 54; and that the FTC’s proposed standard of presumptive illegality would “effectively repeal Congress’s decision to afford patents a statutory presumption of validity.” 55

The Court in *Actavis* offered a markedly different approach to the treatment of large payments. Rather than viewing them as natural and plunging into the inadministrability of the patent merits with only a procedural presumption to grasp onto, the *Actavis* Court injected a healthy dose of common sense into the analysis.

The Court recognized that an “unexplained large reverse payment itself would normally suggest that the patentee has serious doubts about the patent’s survival.” 56 And “that fact, in turn, suggests that the payment’s objective is to maintain supracompetitive prices to be shared among the patentee and the challenger rather than face what might have been a competitive market.” 57 In short, “the size of the unexplained reverse payment can provide a workable surrogate for a patent’s weakness, all without forcing a court to conduct a detailed exploration of the validity of the patent itself.” 58

---

46 Brief for Merck & Co., Inc. as Amicus Curiae Supporting Respondents at 24–25, FTC v. Actavis, Inc., 133 S. Ct. 2223 (No. 12-416) [hereinafter Merck Brief].

47 Solvay Brief, supra note 13, at 39.

48 Merck Brief, supra note 46, at 24.

49 35 U.S.C. § 282 (patents “shall be presumed valid”).

50 466 F.3d at 211.

51 402 F.3d at 1066–67.

52 544 F.3d at 1337.

53 Brief of Amici Curiae Bayer AG and Bayer Corp. in Support of Respondents at 32, FTC v. Actavis, Inc., 133 S. Ct. 2223 (No. 12-416) [hereinafter Bayer Brief].


55 Bayer Brief, supra note 53, at 32.

56 Actavis, 133 S. Ct. at 2236.

57 Id.

58 Id. at 2236–37.
As a result, the Court was able to conclude that “an antitrust action is likely to prove more feasible administratively than the Eleventh Circuit believed.” For while the Eleventh Circuit’s holding “avoid[s] the need to litigate the patent’s validity (and also, any question of infringement) . . . to do so, it throws the baby out with the bath water.” Opening one’s eyes to suspicious payments reveals that “it is normally not necessary to litigate patent validity to answer the antitrust question.”

Voilà! By using the size of the payment as a proxy for the patent’s validity and infringement, the Court addressed administrability concerns. At the same time, it avoided the pitfalls facing earlier courts that had placed their eggs in the presumption-of-validity and natural-status baskets. And it did not need to twist itself into knots like those tied by the Second Circuit in *Tamoxifen*, which admitted that such payments were “suspicious” but magically found that its concerns “abate[d] upon reflection.”

The Court’s resolution of these interrelated issues addresses the individual problems with each of the lower courts’ analyses. For example, the presumption of validity is entitled to far less weight than courts have accorded it. As I have more fully elaborated elsewhere: it is only a procedural evidentiary presumption; it should be entitled to little deference where settlements prevent validity from even being challenged; invalidity challenges are important under patent law and the Hatch-Waxman Act; and empirical studies have shown that a large percentage of granted patents are invalid.

Furthermore, the “natural” status of reverse payments in no way immunizes them. In allowing the brand firm to prolong its monopoly and provide the generic with the certainty of receiving profits for not entering the market, settlements serve the interests of both sides. But that does not provide cover for the agreements, which threaten collusion and harm to consumers. In short, the legality of reverse-payment settlements in no way depends on their frequency.

Finally, the Court’s concern with reverse payments recognizes the reality that they allow brands to obtain more exclusion than they could by reaching an “entry date” agreement that allows the parties to divide the patent term based on the strength of the patent. As the Third Circuit explained in *K-Dur*, there is “no need to consider the merits of the underlying patent suit because ‘absent proof of other offsetting consideration, it is logical to conclude that the quid pro quo for the payment was an agreement by the generic to defer entry beyond the date that represents an otherwise reasonable litigation compromise.’”

In short, by highlighting the common-sense concern with large payments, the Court addressed administrability and eradicated the previously dispositive natural-by-product and presumption-of-validity tenets.

---

59 Id. at 2236.
60 Id.
61 Id.
62 466 F.3d at 208.
65 See Carrier, supra note 63, at 66–67.
66 686 F.3d at 218.
Settlements Without Reverse Payments

Moving methodically through the pro-settlement arguments, the Actavis Court next tackled the contention that settlements are not possible without reverse payments. Economists have pointed to factors like informational asymmetries regarding a patent’s value and “cash-starved” generics that need to receive cash quickly to explain why certain settlements would not occur absent a payment from the brand to the generic.

Several courts worried about blocking settlements by punishing reverse payments. In Cipro, the Federal Circuit found “no support for the notion that the Hatch-Waxman Act was intended to thwart settlements.” In Tamoxifen, the Second Circuit considered, but rejected, a rule that would have led to the antitrust laws “outlaw[ing]” all, or nearly all, settlements and requiring patentees to litigate each patent to final judgment.

Similarly, in the Actavis briefs, the parties stated that “sometimes . . . no settlement is possible . . . without some additional consideration” that “[i]f any settlement agreement is . . . to be classified as involving a forbidden ‘reverse payment,’ we shall have no more patent settlements;” that the FTC’s rule of presumptive illegality “would present generic companies with a Hobson’s choice” of being “prepared to litigate its patent case to the bitter end” or “trade[ing] that patent litigation for antitrust litigation (and the specter of treble damages)” and that the consequences would be worrisome if “there is no meaningful settlement option and the only possibility is drawn-out, expensive, uncertain litigation to final judgment.”

In sharp contrast to all these claims, the Court in Actavis made plain that “the fact that a large, unjustified reverse payment risks antitrust liability does not prevent litigating parties from settling their lawsuit.” The parties “may, as in other industries, settle in other ways, for example, by allowing the generic manufacturer to enter the patentee’s market prior to the patent’s expiration, without the patentee paying the challenger to stay out prior to that point.”

The Court was correct that reverse payments are not needed for settlement. From 2000 to 2004, after the FTC announced it would challenge reverse-payment settlements, but before the appellate courts deferred to the agreements, not one of twenty reported agreements involved a brand paying a generic to delay entering the market. In 2005, however, after the appellate courts took

---

69 544 F.3d at 1337.
70 466 F.3d at 212.
71 Brief for the Generic Pharmaceutical Association as Amicus Curiae Supporting Respondents at 19, FTC v. Actavis, Inc., 133 S. Ct. 2223 (No. 12-416) [hereinafter GPhA Brief].
72 PhRMA Brief, supra note 14, at 19.
74 Actavis Brief, supra note 14, at 40.
75 133 S. Ct. at 2237.
76 Id.
a lenient view of these agreements, the reverse-payment floodgates opened, with the number of such settlements increasing from three to forty in just seven years.78

While the settling parties often bemoan the consequences for settlements of a non-deferential antitrust analysis of reverse-payment agreements, the Actavis Court understood, while stopping short of prohibiting reverse payments altogether, that settlements would still be possible without these payments.

**Blood in the Water**

A final argument that courts had adopted in dismissing challenges to reverse-payment settlements was that brands would not find it profitable to pay generics to delay entering the market because any such payment would signal to other generics the high likelihood that the patent was invalid or not infringed, leading to additional challenges. As the Actavis majority posed the question: “Would not a high reverse payment signal to other potential challengers that the patentee lacks confidence in its patent, thereby provoking additional challenges, perhaps too many for the patentee to ‘buy off?’”79

Along these lines, the Tamoxifen court found that settlements could be “virtual invitation[s]” to other generics to challenge patents and that it was “unlikely that the holder of a weak patent could stave off all possible challengers with exclusion payments because the economics simply would not justify it.”80 Similarly, the Eleventh Circuit in Actavis found that the FTC’s “ominous forecast discounts the reality that there usually are many potential challengers to a patent.”81 The court continued:

> If the patent actually is vulnerable, then presumably other generic companies, which are not bound by the first challenger’s reverse payment settlement, will attempt to enter the market and make their own challenges to the patent. Blood in the water can lead to a feeding frenzy. Although a patent holder may be able to escape the jaws of competition by sharing monopoly profits with the first one or two generic challengers, those profits will be eaten away as more and more generic companies enter the waters by filing their own paragraph IV certifications attacking the patent.82

The amicus briefs in Actavis similarly stated that “[e]ven if one generic manufacturer reaches a settlement, . . . there are numerous reasons to expect that other generics will fight on”83; that “blockbuster drugs often face swarms” of generics84; that if a brand “were willing . . . to pay generic challengers ‘more than they could hope to earn if they entered the market,’ . . . it would attract a multitude of generic challengers”85; and that the brand “would . . . invite economic holdup, as

79 133 S. Ct. at 2235.
80 466 F.3d at 212 & n.25.
81 677 F.3d at 1315.
82 Id.
83 GPhA Brief, supra note 71, at 22.
84 Solvay Brief, supra note 13, at 52.
85 Id. at 53.
each generic company demanded payment exceeding its potential profits because the brand[ ] stands to lose so much more."86

In contrast to these assertions, the Court in Actavis explained that "[t]wo special features of Hatch-Waxman" mean that it is "not necessarily so" that the situation resembles blood in the water.87 First is the 180-day exclusivity period reserved for the first generic to challenge a brand firm’s patent and seek to enter before the patent expires, as this period has "proved valuable" and "can be worth several hundred million dollars."88

Unlike first-filing generics, "[s]ubsequent challengers cannot secure that exclusivity period, and thus stand to win significantly less than the first if they bring a successful paragraph IV challenge."89 In other words, "if subsequent litigation results in invalidation of the patent, or a ruling that the patent is not infringed, that litigation victory will free not just the challenger to compete, but all other potential competitors too (once they obtain FDA approval)."90 Because "[t]he potential reward available to a subsequent challenger [is] significantly less, the patentee’s payment to the initial challenger . . . will not necessarily provoke subsequent challenges."91

The second reason why sharks might not circle is the automatic thirty-month stay of FDA approval that a brand firm can obtain automatically by suing a generic.92 This period operates like a preliminary injunction that prevents the FDA from approving other generics.93 As a result, "a reverse payment settlement with the first filer (or, as in [the Actavis] case, all of the initial filers) ‘removes from consideration the most motivated challenger, and the one closest to introducing competition.’"94

Despite these disincentives, the number of paragraph IV challengers has increased in recent years, and multiple generics have filed such certifications on the first allowable day, leading to shared exclusivity.95 But even if there is more than one first-filing generic that the brand must deal with, there are not so many that settlement is not possible. By way of example, in the case involving the sleep-disorder medication Provigil, brand firm Cephalon paid more than $200 million to the four first-filing generic firms (that had filed patent challenges on the same day) to delay entry.96

Brand profits often are so much higher than total profits after generic entry that there is room for a range of settlements with generics.97 The (typically $1 million) cost and experience needed to file generic drug applications ensures that the universe of potential challenging generics is not

---

86 Id.
87 133 S. Ct. at 2235.
88 Id.
89 Id.
90 Id.
91 Id.
92 Id.
94 Actavis, 133 S. Ct. at 2235 (citation omitted).
95 See, e.g., GPhA Brief, supra note 71, at 22; Solvay Brief, supra note 13, at 52.
97 See, e.g., K-Dur, 668 F.3d at 214 (explaining that “as the experience of at least one court in th[e Third] Circuit confirms, the high profit margins of a monopolist drug manufacturer may enable it to pay off a whole series of challengers rather than suffer the possible loss of its patent through litigation”).
limitless and that multiple payments are quite possible.\textsuperscript{98} And at a minimum, the litigated cases tend to present the most concerning sets of facts and a clear ability by brands to make payments. In short, it is unlikely that there are so many generic challengers that the brand would not be able to pay them.

**A Watershed Decision**

*Actavis* is a crucial case lying at the intersection of antitrust and intellectual property law. Not only does it set forth a framework for future antitrust analysis of reverse-payment settlements, but it also dispenses with several arguments that the settling parties had offered and the appellate courts had adopted. The Court tackled head-on arguments regarding the scope of the patent, benefits of settlement, presence of large payments, inability to attain settlements without payment, and reduced likelihood of payoffs because of multiple generics.

These arguments had the potential to immunize reverse-payment settlements from antitrust review. In rejecting the arguments and ensuring a robust role for antitrust in evaluating these agreements, *Actavis* was a watershed decision.

Illuminating the Story of China’s Anti-monopoly Law

Maureen K. Ohlhausen

Setting the Stage

On a warm summer night in Beijing, government officials, lawyers, and scholars from China and around the world recently gathered to celebrate the fifth anniversary of the Chinese Anti-monopoly Law (AML). While enjoying a rooftop view of the Forbidden City, the celebrants were treated to a puppet show featuring colorful paper cutouts illuminated from behind as they danced and fought behind an opaque screen. The puppets acted out famous Chinese legends adapted to depict recent cases by the Chinese anti-monopoly authorities, such as the Moutai white liquor resale price maintenance cases. As charming as this puppet show was to witness, it also served as a metaphor for the proceedings at the forum that preceded the celebration. Some commentators have complained that too often the Chinese anti-monopoly authorities themselves operate behind a screen, providing parties and other observers little insight into their thinking or deliberations. At the conference marking the fifth anniversary of the AML, however, the leaders of the Chinese antitrust authorities and several prominent Chinese scholars provided greater illumination of their thinking than we have previously witnessed.

Illuminating the Actions Behind the Screen

The China Competition Policy Forum—Competition Policy in Transition, held in Beijing on July 31 and August 1, 2013, was hosted by the Expert Advisory Board of the State Council on the Anti-monopoly Commission (Expert Advisory Board). The Expert Advisory Board, which is comprised of 21 experts including jurists, economists, and industrial specialists, plays an important role in the Chinese antitrust system. It consults with the three anti-monopoly agencies and the member agencies of the Anti-monopoly Commission, providing advice on competition policy and legal issues and analysis in specific cases.

The structure of the forum itself, as well as the speeches and interactions among panelists, illuminated three major themes. First, the presentations and discussions by Chinese officials and scholars proved to be a surprisingly open conversation. They did not shy away from controversial areas, such as merger review and remedies and the treatment of intellectual property (IP) rights,  

---


3 The three Chinese anti-monopoly agencies are the Ministry of Commerce (MOFCOM), the National Development and Reform Commission (NDRC), and the State Administration for Industry and Commerce (SAIC).
and they intentionally included divergent views, some of which offered strong criticism of the current Chinese approach. Second, the proceedings indicated a serious interest in promoting competition as a societal value and developing a modern competition regime, expressed not only by the Chinese antitrust officials but also by other Chinese government officials. Third, although there was widespread recognition that China must continue to move away from a planned economy, including by challenging administrative monopolies, there was still some support for the government playing a strong role in the market in certain industries, as well as for the consideration of non-competition factors in antitrust matters. Notably, all participants expressed enthusiasm for competition in general, but what actually constitutes free market competition is still open for debate, with some officials seeming to focus more on static competition factors, such as simply expanding or maintaining the number of competitors in a particular market, rather than considering longer-term effects on innovation and consumer welfare.

Shining a Light

The forum’s showcase panel, which was broadcast by China Central Television (CCTV), featured Shang Ming, Director-General (DG) of the Anti-monopoly Bureau of MOFCOM; Xu Kunlin, DG of the Price Supervision and Inspection and Antitrust Bureau of NDRC; and Ren Airong, DG of the Anti-monopoly and Anti-unfair Competition Enforcement Bureau of SAIC. Joining these antitrust officials were two prominent professors, Dr. Huang Yong, Vice Chair of the Expert Advisory Board, and Chinese economist Professor Wu Jianglian. In a wide-ranging discussion, these officials and professors explored the approaches and thinking of the Chinese antitrust authorities on a variety of topics.

The history of Professor Wu, one of China’s most famous economists, provides a crucial backstory. With a strong market orientation, Professor Wu was a brave voice in the 1970s, advocating for a market economy and economic reform in China in the face of government resistance. After suffering persecution in the Cultural Revolution, he later emerged as a prominent voice in China’s economic reform program. At a presentation at Chatham House in London in late 2012, Professor Wu identified a variety of problems with the current Chinese economic system, including the continuing role of state-owned enterprises, government interference with the economy, and deficiencies in the rule of law, all of which have contributed to an economic system that is semi-controlled and semi-market driven. This system, he stated, has two major problems: (1) an export-driven approach that has generated a shortage of resources, damage to the environment, and an imbalance of investment and consumption; and (2) too much power for administrators, which has led to the spread of corruption and rent-seeking activities. Professor Wu’s prescription for these ills is a reform whereby “the government would gradually reduce its intervention in economic activities” and transform into a more market-oriented economy based on the rule of law.

During the panel in Beijing, Professor Wu strongly advocated his viewpoint in exchanges with the antitrust officials. He observed that although enactment and development of the AML has been generally positive, it alone is not enough, and that China needs to do more to establish a competitive system with the market at its core. He identified administrative monopoly as a continuing

---


5 Id. at 4–5.

6 Id. at 5.
problem, as well as interventions by the government to set prices for items such as staple consumer products. In addition, he noted that the imposition of hurdles to market access is another major economic problem, which the AML on its own cannot address.

In addition to the showcase, other panels offered more revelations by Chinese officials and scholars on some controversial issues, such as the panel on IP rights and antitrust. Again demonstrating a commitment to fostering open debate on these issues, the panel included a diversity of viewpoints, from SAIC officials and Chinese and American scholars to representatives of U.S. enforcement agencies, law firms, and companies that have strong IP interests.7

Yang Jie, Director of the Anti-monopoly and Anti-unfair Competition Enforcement Bureau of SAIC, opened the IP and antitrust panel by describing SAIC’s efforts to find the right balance between IP rights and antitrust. She highlighted SAIC’s issuance of numerous versions of its draft guidelines on IP rights8 and its solicitation of comments from domestic and international observers.9 Director Yang also gave examples of what SAIC considered problematic conduct, such as tying, indiscriminate warning letters, and refusals to license. She stated that the refusal to license prohibition, contained in Article 8 of the guidelines,10 was something like the essential facilities doctrine in U.S. and EU case law.

I was invited to speak on the essential facilities doctrine in the U.S. antitrust system with the goal of clarifying that the U.S. Supreme Court has not recognized such a doctrine. During a previous visit to China, several Chinese commentators suggested to me that the Chinese antitrust regulators should adopt the essential facilities doctrine to reflect what they believe exists in U.S. case law. As part of a presentation that focused primarily on Trinko,11 I discussed the Court’s observations that forced sharing may lessen the incentives for innovation that ultimately improve consumer welfare.

In response, some commentators, including Professor Wang Xianlin of Shanghai Jiao Tong University, suggested that regardless of the status of the essential facilities doctrine in U.S. case law, it would still be a useful approach under the Chinese AML. Judge Zhu Li of the Supreme People’s Court, however, emphasized that although IP rights may restrict competition in the short term, this is in exchange for a higher form of competition in the future through innovation. Judge Zhu further asserted that one must consider the risks and expenses of creating new inventions.

7 The IPR/Antitrust Crossroad Panel was chaired by Ren Airong, Director-General of the Anti-monopoly and Anti-unfair Competition Enforcement Bureau of SAIC, and Daniel Sokol, Visiting Professor, University of Minnesota Law School. The panelists were Yang Jie, Director, Anti-monopoly and Anti-unfair Competition Enforcement Bureau of SAIC; Maureen K. Olthausen, Commissioner, U.S. Federal Trade Commission; Zhu Li, Judge, Supreme People’s Court of the People’s Republic of China; Roy Hoffinger, Vice President, Qualcomm Incorporated; H. Stephen Harris Jr., Partner, Baker & McKenzie; and Wang Xianlin, Professor, Shanghai Jiao Tong University School of Law.


9 SAIC has indeed been responsive to comments on the Draft SAIC IP Guidelines. The latest iteration of the guidelines (now styled as regulations) reflects numerous improvements, although some areas still raise concerns, such as the prohibition on unilateral refusals to license when the IP holder is a “necessary facility for the licensee to compete.” See, e.g., Darren Tucker, Inside the Latest Draft of SAIC’s IP Antitrust Rules, Law 360, Aug. 6, 2013, http://www.law360.com/competition/articles/461987/inside-the-latest-draft-of-saic-s-ip-antitrust-rules (discussing this prohibition and identifying several other provisions as potentially problematic).

10 Draft SAIC IP Guidelines, supra note 8, at 4–5.

11 Verizon Comm’cs, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 411 (2004) (addressing an essential facilities argument and stating that “[w]e have never recognized such a doctrine, and we find no need either to recognize it or repudiate it here”) (internal citations omitted).
when evaluating the prices charged for licensing IP. Other panelists, such as Roy Hoffinger of Qualcomm, who discussed issues surrounding standard-essential patents and fair, reasonable, and non-discriminatory (FRAND) commitments, and H. Stephen Harris, Jr. of Baker and McKenzie, who addressed the relationship between antitrust law and IP law, also highlighted the important role of IP protections in spurring competition.

**Competition Currently Has the Leading Role**

In the opening panel of the conference, numerous high-level Chinese officials emphasized the importance of competition in the Chinese economy.\(^{12}\) One after another, they stressed the vital role of the market in allocating resources and observed that deregulation continues to be an important focus of reform. Wang Chao, Secretary-General of the State Council Anti-monopoly Commission and Vice Minister of Commerce, spoke of the need to break down barriers to competition to improve the Chinese economy. Zhang Qiong, Chairman of the Expert Advisory Board, emphasized that economic development depends on competition and market orientation.

Numerous speakers also focused on the importance of raising Chinese society’s awareness of competition issues. Following the storytelling axiom of “show, don’t tell,” this goal of conveying the importance of competition to the public was most strongly expressed by the fact that Yao Zhenshan, a famous presenter from CCTV, hosted the showcase panel, which was aired in its entirety on Chinese television.

As noted above, the forum did not merely laud the accomplishments of the Chinese antitrust authorities in the five years of the AML’s existence. Many speakers throughout the forum also identified challenges ahead. Zhang Qiong characterized China’s competition regime as still being at an early stage and in need of continued improvement in both the theory and practice of antitrust enforcement. Professor Wang Xiaoye of the Chinese Academy of Social Sciences and Hunan University stated that the three current antitrust enforcement bodies were insufficiently independent because they are at the same administrative level of other ministries. Echoing this point, Professor Huang agreed that China needs a single competition agency at a higher administrative level than the three current agencies.

Officials also demonstrated an encouraging openness to ongoing engagement with more developed competition regimes and international scholars to continue to improve antitrust policy and institutions in China. For example, Sun Hongzhi, Vice Minister of SAIC, encouraged working closely with international organizations, noting that China needed the intellectual support of scholars in China as well as around the world.

**The Plot Gets Complicated**

Returning to the showcase panel, despite Professor Wu’s advocacy for a stronger market-based approach, the antitrust officials were more mixed in their endorsement of free-market competition, with several officials emphasizing the need for maintaining regular market order. Although these discussants did not specify what this might mean in practice,\(^{13}\) in response to an audience ques-
tion, one official stated that a cartel should be allowed in exceptional cases if participants in an industry are losing money. Another official stated that competition is a double-edged sword that, if badly used, will diminish innovation.

One of the most interesting exchanges occurred between DG Shang Ming and Professor Wu regarding the hold separate agreement in the Western Digital merger case. DG Shang defended the decision, stating that it was necessary to maintain five players in the market to protect the welfare of China's consumers. He emphasized that China does not produce hard disks, but it is the biggest consumer of them. Professor Wu criticized this approach as being too focused on the number of players in the market rather than on competition overall. He observed that the market and players may change over time and that they should change based on relative efficiencies. In addition, Professor Wu emphasized that for the hard disk industry one does not need to see more producers of the same technology, but rather that competition should spur innovation in new devices and solutions, which is ultimately better for consumers.

Harkening to China’s past as a centrally planned economy, several panelists highlighted the problem of administrative monopolies. Expert Advisory Board Chairman Zhang Qiong noted the tension between industrial policy and market-based competition growth, stating that he deems the latter necessary to achieve sustainable development. Similarly, SAIC Vice Minister Sun Hongzhi stressed that the AML was meant to focus on administrative monopoly as well as abuse of dominance in the private sector. Professor Wu observed that many legacy problems remain from China’s past and that in many industries there are still hidden interests and protections, which seem contradictory to the goals of the AML. He emphasized that these hurdles to free competition were imposed at the direction of the country’s political leadership, not on the advice of competition scholars.

Some important action is taking place offstage, however. Not discussed during the panel was the fact that, in January of this year, a group of 12 ministries led by the Ministry of Industry and Information Technology and including the three anti-monopoly agencies, issued guidance calling for consolidation in nine industries: automobiles, steel, cement, shipbuilding, electrolytic aluminum, rare earths, electronic information, pharmaceuticals, and agricultural processing. The Guiding Opinions call for the consolidation of participants in each of these industries into a small-

13 Article 4 of the AML provides that the State shall formulate and implement competition rules that improve a unified, open, competitive, and orderly market system. AML, art. 4. In a statement made in connection with its enforcement action imposing fines on six manufacturers of infant formula, NDRC stated that the fines were for restricting competition, resale price maintenance, and for using a variety of methods to disrupt market order. See, e.g., China Says Fined Milk Powder Companies “Disrupted Market Order,” REUTERS, Aug. 7, 2013, http://www.reuters.com/article/2013/08/07/china-milkpowder-ndrc-idUSB9N0FP02K20130807.

14 Press Release, Ministry of Commerce of the People's Republic of China, MOFCOM Held Special Press Conference on “Anti-monopoly Work Progress in 2012” (Jan. 5, 2013), available at http://english.mofcom.gov.cn/article/newsrelease/press/201301/20130108513014.shtml. MOFCOM approved the acquisition of the hard disk drive (HDD) business of Viviti Technologies Ltd., formerly known as Hitachi Global Storage Solutions Ltd., by Western Digital subject to the divestiture of production assets and several behavioral remedies. Id. MOFCOM imposed the following remedies: Western Digital shall divest Hitachi's 3.5-inch HDD production assets to a third party; Hitachi's HDD business shall be operated as an independent competitor with respect to, in particular, R&D, procurement, production and sales, safeguarded by firewalls between their respective teams; and Western Digital and Hitachi shall not force consumers to buy products exclusively from them. Id.

er number of large, globally competitive enterprises.\textsuperscript{16} Although consolidation itself, if driven by market forces, may not necessarily be antithetical to competition values, this effort by government to spur consolidation in key industries for purposes of global competitiveness of Chinese industries certainly raises questions whether the free market or the government will be the primary driver of the Chinese economy, at least in these particular industries.

\textbf{What Will the Sequel Be?}

In a keynote speech at the forum, I congratulated the Chinese anti-monopoly agencies on their strong efforts thus far, such as their increasingly sophisticated economic and legal analysis.\textsuperscript{17} I also identified three areas in which I hope we will celebrate more progress in the future:

\textit{1. Non-Competition Factors.} Article 27 of the AML, which covers merger control, sets out the factors for MOFCOM to consider when deciding whether or not to approve a merger.\textsuperscript{18} Three factors are consistent with modern competition analysis: market concentration, share, and power; effects on entry and technological innovation; and effects on consumers. The last two factors, however, expressly allow for broader considerations: the effect of the proposed deal on the development of the national economy, and any other factors determined by the State Council Antimonopoly Enforcement Authority.\textsuperscript{19} Although it is difficult to draw conclusions about whether and to what extent MOFCOM has relied on non-competition factors in its merger analysis because of the small number of published merger decisions under the AML, some practitioners have expressed concerns that factors such as protectionism and employment effects within China have influenced merger review, with regard to both the length of the review process and outcomes.\textsuperscript{20} Practitioners have also reported, however, that MOFCOM’s analysis has shown an increased focus on traditional competition factors as the agency has gained experience.\textsuperscript{21}

In my keynote address, I encouraged the Chinese competition authorities to show consistent movement away from considering non-competition factors in their decisions, which will help promote predictability, fairness, and transparency in their decision making.\textsuperscript{22}

\textit{2. Transparency.} I applauded the disclosures that MOFCOM and DG Shang made recently with respect to merger filings and reviews, as well as SAIC’s publication of a list of all 12 AML decisions it has reached thus far. Increased transparency with the public and parties under investigation is an important value to pursue for any antitrust agency.

\textit{3. International Engagement.} In July 2011, the FTC and the Antitrust Division signed a Memorandum of Understanding (MOU) with MOFCOM, NDRC, and SAIC that establishes a framework for cooperation between the U.S. and the Chinese agencies through a joint dialogue among the senior competition officials at all five agencies and communication and cooperation between indi-

\textsuperscript{16} Ross & Zhou, supra note 15.


\textsuperscript{18} AML, art. 27. Article 1 of the AML also sets out as a goal of the law “safeguarding the . . . social public interest [and] promoting the healthy development of the socialist market economy.” AML, art. 1.

\textsuperscript{19} AML, art. 27.


\textsuperscript{21} Id.

\textsuperscript{22} Ohlhausen, supra note 17, at 11.
The debate at the forum likely reflects a conversation going on behind the screen in China, with some voices arguing for increased market orientation and others favoring a hybrid system that includes greater government involvement in the market. If so, it is vital to help support those within the Chinese antitrust community who are advocating for a market system and to understand the challenges they face in their efforts.

In my keynote remarks, I commended the Chinese competition agencies for their international engagement thus far. I also urged them to become members of the International Competition Network and contribute their learning to the group in helping us shape best practices, as well as to continue bilateral engagement with other agencies on merger reviews and other investigations. This engagement permits us to move together to become better competition enforcers and to protect the interests of consumers around our increasingly interconnected world.

Much of what took place at the forum makes me hopeful of continued progress by the Chinese competition authorities in several of these areas. The most promising is transparency, given the high level and open debate, the active inclusion of critical viewpoints from within China and abroad, and the willingness to focus on controversial areas. The Expert Advisory Board and especially Professor Huang, who organized the conference, deserve enormous credit for their efforts in this area. The interest in increased international engagement also seems to be trending in a positive direction.

The likelihood of further movement away from considering non-competition factors under the AML presents a more mixed picture. On the positive side, one of the strongest messages of the conference was that Chinese government officials and scholars understand that competition offers the best path forward for their country. One should not overlook how remarkable this is, given the challenges they face in efforts.

23 See Press Release, Fed. Trade Comm’n, Federal Trade Commission and Department of Justice Sign Antitrust Memorandum of Understanding with Chinese Antitrust Agencies (July 27, 2011), available at http://www.ftc.gov/opa/2011/07/chinamou.shtm; see also Memorandum of Understanding on Antitrust and Antimonopoly Cooperation Between the United States Department of Justice and Federal Trade Commission, on the One Hand, and the People’s Republic of China National Development and Reform Commission, Ministry of Commerce, and State Administration for Industry and Commerce, on the Other Hand (July 27, 2011), available at http://www.ftc.gov/os/2011/07/110726mou-english.pdf. The MOU identifies several specific avenues for cooperation, including: (1) exchanges of information and advice about competition law enforcement and policy developments; (2) training programs, workshops, and other means to enhance agency effectiveness; (3) exchanges of comments on proposed laws, regulations, and guidelines; and (4) cooperation on specific cases or investigations, when it is in the investigating agencies’ common interest. Id. at 2.


Chinese government’s suppression of market-oriented viewpoints during the Cultural Revolution and the personal experiences of forum participants, most notably Professor Wu. Despite this emphasis on moving away from a planned economy and toward a market system, the discussions still revealed a continuing impulse to factor in effects on Chinese industry and employment rather than focusing simply on efficiency and consumer welfare, as well as ongoing support for more direct government intervention in the market.

This raises a final question: what can we outside observers do to encourage a satisfactory sequel to the first five years of the AML? I believe that the open debate at the forum likely reflects a conversation going on behind the screen in China, with some voices arguing for increased market orientation and others favoring a hybrid system that includes greater government involvement in the market. If so, it is vital to help support those within the Chinese antitrust community who are advocating for a market system and to understand the challenges they face in their efforts. Thus, the most important thing that we in the audience can do toward ensuring a good sequel for the Chinese antitrust story is to pursue patient cooperation and diligent work on both sides when engaging the Chinese agencies, offering them advice and support, and advocating for a competition-based enforcement approach.
Five years have passed since China’s anti-monopoly law (AML) took effect on August 1, 2008. During these five years, the Anti-Monopoly Bureau within the Ministry of Commerce (MOFCOM), which is responsible for merger reviews in China, has been the most active of the three Chinese antitrust agencies, having reviewed more than 600 transactions by the second quarter of 2013. In this article, we look back at the cases MOFCOM has reviewed to date and the decisions that it has published in cases where the transaction was blocked or approved with conditions.1 We compile and summarize characteristics of MOFCOM’s merger review activities to shed light on the trends in merger enforcement in China.

A General Overview of Mergers Reviewed by MOFCOM

When MOFCOM blocks a transaction or gives conditional clearance, it publishes its decision on its website immediately. Through 2012, MOFCOM also periodically published data on the total number of clearances without conditions and provided the names of the merging firms involved in each such clearance. Beginning at the end of 2012, MOFCOM started publishing these data on a more regular quarterly basis. The data can be used to summarize various trends and characteristics of MOFCOM’s merger review.

During the past five years, the vast majority of the filings that MOFCOM reviewed were cleared unconditionally. Up through the third quarter of 2013, MOFCOM completed the review of 693 filings in total, of which 672 were cleared unconditionally, 20 were cleared with conditions, and one was blocked.2

The number of filings and the number of reviews completed each year have been generally increasing. MOFCOM’s work load has almost tripled since MOFCOM first began reviewing mergers five years ago, while the number of staff members has not increased much at all, staying at around 30, including administrative staff. The accumulation of knowledge, skill, and experience has undoubtedly helped MOFCOM staff in becoming more efficient in reviewing mergers, but may still not be enough to compensate for the short-staffing issue.

While all cases filed during 2008 and 2009 were accepted and reviewed, starting in 2010, there has been a sizable gap between the number of cases filed and the number of cases accepted and between the number of cases accepted and the number of cases reviewed each year (see

---

1 All of MOFCOM’s published decisions (in Chinese) can be accessed from its website, http://fldj.mofcom.gov.cn/.

2 See http://fldj.mofcom.gov.cn/article/zcfb/ (where MOFCOM publishes the unconditional clearance data) and http://fldj.mofcom.gov.cn/article/ztxx/ (where MOFCOM publishes its intervention decisions). There are slight discrepancies between our calculated numbers based on the unconditional clearance data and another MOFCOM source, available at http://www.mofcom.gov.cn/article/ae/ai/201308/20130800226124.shtml (MOFCOM’s news announcement on five year antitrust enforcement achievement up through the second quarter of 2013). This news announcement states that the total number of completed reviews is 643, and the total number of unconditional clearances is 624, through the second quarter of 2013, while our calculation indicates the two numbers to be 637 and 618, respectively.
Chart 1). As for the first gap, possible explanations are: (i) a natural time lag, i.e., cases were filed at the very end of the year and accepted early the next year, or (ii) the deal cratered and the filing was withdrawn after the initial submission but before acceptance. As for the second gap, again, other than a time lag (i.e., cases were accepted and under review toward the end of one calendar year but the review was not finished until the next calendar year), it may reflect filings withdrawn by the merging parties. Unfortunately, information about the number of withdrawals or the reasons for them is unavailable. Anticipated opposition from MOFCOM, which may have been viewed by merging parties as more likely after MOFCOM issued its first prohibition decision in 2009, may have contributed to parties abandoning a transaction.

The data can also be used to get a sense for the range of industries in which MOFCOM has been most active. In Chart 2, we classify the reviewed mergers by industry. Of all mergers with review completed by the first half of 2013, most involved heavy industry, such as manufacturing, oil, gas and energy, automobile, chemical, and steel, which are also deemed by the Chinese government as industries crucial to the growth and development of the Chinese economy.

Another question of interest relates to the nationality of the merging firms in those transactions that MOFCOM has reviewed, particularly in the case of acquisitions. As shown in Chart 3, of all
mergers with review completed by the first half of 2013, about 60% can be categorized as acquisitions (i.e., a transaction in which one company acquires all or part of another company). Among the acquisitions, 55% involve a foreign firm acquiring another foreign firm, followed by 20% where a foreign firm acquired a Chinese firm, 18% where a Chinese firm acquired another Chinese firm, and 7% where a Chinese firm acquired a foreign firm. As for non-acquisition mergers, which are mostly joint ventures (JVs), 50% involve both foreign and Chinese firms, 40% involve only foreign firms, and 10% involve only Chinese firms. These results indicate that MOFCOM is not focused

3 A few non-acquisition mergers involved reorganization of the company’s assets, expansion of the company’s business divisions, or increase in capital share.
only on the M&A activities of foreign firms, and that Chinese firms are not entirely ignoring the filing requirements, as some may have speculated. State-owned enterprises (SOEs) can also be found among the filing parties. For example, Shenhua, one of the parties to the GE/Shenhua JV, on which MOFCOM imposed remedies, is an SOE.

An In-depth Study of Decisions Where MOFCOM Intervened

Next, we analyze cases where MOFCOM has intervened, i.e., either imposed remedies or blocked the merger. As of September 30, 2013, MOFCOM has imposed remedies on 20 mergers and blocked one (Coca-Cola/Huiyuan). Accompanying each intervention is a written decision, published on MOFCOM’s website. Information contained in these decisions enables us to study the key aspects of the corresponding cases. By analyzing these decisions, we hope to provide insight on the nature of MOFCOM’s enforcement practices, the factors that prompt MOFCOM’s intervention, and the ways in which MOFCOM has intervened.

**Length of Decision.** We start by counting the number of words in each decision and looking for patterns in the word counts (see Chart 4). From the 527 words in the Inbev/AB decision in 2008, to the record high 17,434 words in the Glencore/Xstrata decision in 2013, it is apparent that MOFCOM has attempted to make more information available to the public and has tried to improve the
explanation of its analysis over time. However, the description of the substantive analyses in these decisions, especially those regarding the assessment of competitive effects, remains very general. Thus, there is still a lack of transparency regarding what specific analyses were done, how these analyses were performed, and how the conclusions were drawn in each case. For example, in MediaTek/MStar, MOFCOM defined two relevant product markets—LCD TV controller chips and cellphone baseband chips—and went on to conclude that there was no competitive concern in the cellphone baseband chips market without providing any reasoning or basis for this conclusion. Increased transparency concerning the types of analysis performed would be very helpful in providing guidance for parties contemplating future deals.

**Duration of Review.** Accompanying the increased complexity of MOFCOM’s reviews is a longer time to complete the reviews, and therefore a longer wait by the merging parties. In Chart 5, we provide the number of days it took MOFCOM to accept and clear cases in which MOFCOM intervened. In theory, the review could take up to six months—phase I lasts 30 days, phase II lasts 90 days, and phase III lasts another 60 days.

4 However, in reality, the merging parties may be required or encouraged to withdraw their filing and refile if the merging parties and MOFCOM cannot achieve a desirable outcome by the end of phase III. In addition, as shown in Chart 5, it can

---

4 In this article, phase III refers to the extended phase II under the AML.
also take quite a while for MOFCOM to confirm the completeness of the filing and thus formally accept it. The longest review period experienced to date was the MediaTek/MStar transaction, where the merging parties withdrew and refiled at phase III in the first round and went through a second round of review, making the total review time more than one year from the time when the parties initially filed.

The fact that a review process is extended to phase II does not necessarily signal that MOFCOM has identified competitive concerns but may instead result from MOFCOM’s thin staff and heavy workload—as discussed above, there are about 30 people within the whole bureau, including administrative staff. Most of the cases get cleared in phase II or later in China, in contrast to the United States and the European Union, where most cases are cleared in the equivalent of phase I.

Table 1
Relevant Markets for Cases Where MOFCOM Intervened
August 1, 2008 - September 30, 2013

<table>
<thead>
<tr>
<th>Case</th>
<th>Geographic Markets</th>
<th>Product Markets</th>
</tr>
</thead>
<tbody>
<tr>
<td>InBev/AB</td>
<td>—</td>
<td>Carbonated drink market and juice drink market separately</td>
</tr>
<tr>
<td>Coca-Cola/Huiyuan</td>
<td>China ²</td>
<td>MMA, SpMAs, PMMA particle products, and PMMA panel products separately</td>
</tr>
<tr>
<td>Mitsubishi Rayon/Lucite</td>
<td>China</td>
<td>Two separate auto markets and ten separate auto part markets</td>
</tr>
<tr>
<td>GM/Delphi</td>
<td>China</td>
<td>Human pharmaceuticals, specifically including JIC (wide-spectrum penicillin) and N6A (anti-depression and mood stabilizing drugs); animal health products, specifically including swine mycoplasma pneumonia vaccine, swine pseudonabies vaccine, and combination vaccines for dogs</td>
</tr>
<tr>
<td>Pfizer/Wyeth</td>
<td>China</td>
<td>Button-type rechargeable lithium battery, nickel hydrogen battery for civilian use, and automotive nickel hydrogen battery separately</td>
</tr>
<tr>
<td>Panasonic/Sanyo</td>
<td>Global</td>
<td>Ophthalmological anti-inflammatory/anti-infective combinations and contact lens care products separately</td>
</tr>
<tr>
<td>Novartis/Alcon</td>
<td>Global and China ²</td>
<td>Ophthalmological anti-inflammatory/anti-infective combinations and contact lens care products separately</td>
</tr>
<tr>
<td>Unalaki/Silvinit</td>
<td>China’s Import Market ³</td>
<td>Potash</td>
</tr>
<tr>
<td>Alpha V/ordin</td>
<td>Global ²,4</td>
<td>Electronic yarn clearers for automatic winders</td>
</tr>
<tr>
<td>Ge/Shenhua (JV)</td>
<td>China</td>
<td>Licensing of coal-water slurry gasification technology</td>
</tr>
<tr>
<td>Seagate/Samsung</td>
<td>Global</td>
<td>Hard drive market</td>
</tr>
<tr>
<td>Henkel HK/Tiande (JV)</td>
<td>Global ³</td>
<td>Ethyl cyanoacetate, cyanoacrylate monomer, and cyanoacrylate adhesives separately</td>
</tr>
<tr>
<td>WD/Hitachi (Viviti)</td>
<td>Global</td>
<td>Hard drive market</td>
</tr>
<tr>
<td>Google/Motorola Mobility</td>
<td>Global ³</td>
<td>Mobile smart terminals and operating systems for mobile smart terminals separately</td>
</tr>
<tr>
<td>UTC/Goodrich</td>
<td>Global</td>
<td>Alternate current electrical generation systems and eight other aviation parts markets separately</td>
</tr>
<tr>
<td>Wal-Mart/Yihaojian</td>
<td>China</td>
<td>B2C online retail</td>
</tr>
<tr>
<td>ARM/G&amp;G/Emilho (JV)</td>
<td>—</td>
<td>Security solution “Trusted Execution Environment”</td>
</tr>
<tr>
<td>Gencore/Xstrata</td>
<td>Global and China ³</td>
<td>Copper concentrate, zinc concentrate, and lead concentrate separately</td>
</tr>
<tr>
<td>Marubeni/Gavilon</td>
<td>China’s Import Market ³</td>
<td>Soybean, corn, bean pulp, and dry and coarse distillers grains separately</td>
</tr>
<tr>
<td>Baxter/Gambro</td>
<td>Global ³</td>
<td>CRRT monitors, CRRT dialyzers, CRRT blood tubes, and hemodialyzers separately</td>
</tr>
<tr>
<td>MediaTek/MStar</td>
<td>China ³</td>
<td>The design and sale of LCD TV controller chips and cellphone baseband chips separately</td>
</tr>
</tbody>
</table>

Footnotes:
1 Markets of competitive concern are italicized.
2 The relevant geographic market was not explicitly defined, but it could be inferred from the language used in the decision.
3 Global market competition factors were also considered.
4 Impact on domestic market competition was also evaluated.

MOFCOM appears to be aware of the complaints regarding the lengthy review period, and has published draft rules intended to expedite the review of simple cases.\(^5\) However, it remains to be seen which transactions would qualify as “simple” cases and how long the review of simple cases will take.

---

**Market Definition.** Table 1 summarizes MOFCOM’s determinations regarding the relevant product and geographic market definitions in each of the 21 cases that did not receive unconditional approval. MOFCOM has almost always included a description of the relevant markets in its published decisions, but the definition of the geographic market is not always clear-cut—sometimes both global and domestic markets are evaluated. In Uralkali/Silvinit and Marubeni/Gavilon, MOFCOM focused its competitive analysis on the geographic market of imports into China. These two decisions, however, do not explain why domestic production was excluded from the relevant market.

**Market Share and Market Concentration.** MOFCOM often provides information about the market shares of the merging parties, and sometimes also provides the HHI and the market shares of other competitors. Chart 6 lays out the market shares of each of the individual merging parties (if available), along with their combined market share, where indicated by MOFCOM, for each merger with a horizontal overlap. The combined share of the merging parties covers a wide range. The largest combined share was 100% in the Alpha V/Savio transaction. The smallest combined shares were in the Glencore/Xtrata transaction, at 6.8% to 17.8%, and in the Marubeni/Gavilon transaction, at 16.1% to 18.7%. It should be noted that there are other similarities between these two cases: (1) in both cases, the products of concern were raw goods and materials, and the merging parties import them into China; (2) it is mentioned in both decisions that China relies heavily on imports in the industry of concern; (3) it is also mentioned that the downstream Chinese firms are small and have little bargaining power, and thus would be hurt by the merger. It may be that, in these two cases, an industrial policy goal overshadowed traditional antitrust goals in MOFCOM’s review.6

**Competitive Effects Analyses.** Table 2 summarizes some of the key characteristics of the competitive effects analyses, as reflected in MOFCOM’s published decisions. Among the 21 cases where MOFCOM intervened, 12 cases were horizontal, 5 cases were vertical, 2 were a mixture of horizontal and vertical, and 2 were conglomerate. MOFCOM is especially concerned about foreclosure effects in vertical mergers, and leverage effects in conglomerate mergers. In contrast, in the United States, conglomerate mergers are rarely challenged, and vertical mergers are typically of less concern as well.7 In addition, MOFCOM sometimes indicates that it has competitive concerns regarding the merger, such as a negative effect on innovation, without further explanation other than the fact that the market would be more concentrated. The U.S. and EU antitrust agencies are generally more wary of reaching such conclusions without extensive analysis since even mergers that increase market concentration can in some cases enhance innovation.8

In 14 out of the 21 cases, MOFCOM’s decisions contain assessments of the significance of barriers to entry, ranging from “certain obstacles,” “relatively difficult,” to “very difficult.” Also often

---


7 During fiscal years 1996–2011, the FTC issued 464 second requests, of which 28 were based on a vertical theory and none were based on a conglomerate theory. Fed. Trade Comm’n, Horizontal Merger Investigation Data Fiscal Years 1996–2011, tbl. 1 (Jan. 2013) [hereinafter FTC Data], available at http://www.ftc.gov/os/2013/01/130104horizontalmergerreport.pdf.

included is a short description of factors that contribute to barriers to entry, including time and cost to enter, patents or other IP, technology, skills, and regulatory obstacles. Six cases also note a lack of past entry.

None of the decisions, however, mentions any "hot" documents or customer complaints, which are two types of information that the U.S. antitrust agencies consider important.9

The most significant analytical element that is not discussed in MOFCOM's decisions is consideration of efficiencies. None of its 21 decisions include any mention or description of efficiencies. Thus, MOFCOM has provided no guidance to the public on whether or how it evaluates

---

9 See FTC Data, supra note 7, at 4.
merger-related efficiencies in actual cases. It is believed that MOFCOM has been skeptical about efficiencies arguments. This would perhaps not be surprising because, even in the United States and European Union, efficiencies claims made by the merging parties are not accepted by the agencies without careful scrutiny and assessment that the efficiencies are merger-specific and will be passed on to consumers. The concern in China, however, is that there has been no official acknowledgment from MOFCOM that it has considered the parties’ efficiencies arguments in an actual case, which could be interpreted as a signal that MOFCOM discounts efficiencies arguments in general. If this is the case, it could discourage transactions by merging parties that seek to realize procompetitive effects generated by efficiencies. Without consideration of such efficiencies, it may be hard to overcome a presumption of adverse competitive effects arising from high combined market shares.

In some cases, MOFCOM does not explain how it assesses or weighs the procompetitive justifications it recognizes. In its MediaTek/MStar decision, MOFCOM evaluated and considered several factors that “weaken the anti-competitive effect of the merger to a certain extent,” including the dynamic nature of the products and the industry and the facilitating effect on entry of customers’ dual-sourcing behavior. MOFCOM even acknowledged that “the boundary of TV chips, mobile phone chips and computer chips is becoming more and more blurred. Chip manufacturers that have comprehensive research and development capabilities have the ability to participate in the market competition (of the TV chip market) in the future.” However, MOFCOM remained concerned that the merger would have anticompetitive effects in the TV chip market, and imposed remedies on the parties in relation to that market.

Consideration of Third-Party Information and Use of Outside Experts. It can be observed that MOFCOM often seeks opinions and information from third parties, including other relevant government agencies, trade associations, upstream and/or downstream firms, and competitors (see Table 3). MOFCOM also conducted onsite investigations in a few cases, including Panasonic/Sanyo, and UTC/Goodrich, and MediaTek/MStar. The process of MOFOCOM’s consultation with other stakeholders, however, has been rather opaque—e.g., it is unclear what information and opinions were obtained from other government agencies and how MOFCOM views and utilizes such information and opinions in each case. Our experiences indicate that MOFCOM does not communicate such information to the merging parties either. Although the mere fact that other stakeholders may express to MOFCOM views on issues that are not strictly relevant to the competition analysis does not mean that MOFCOM will necessarily take those views into account, there is a danger that other stakeholders’ views, especially the views of other regulatory government agencies, could instill industrial policy goals into MOFCOM’s review and steer the process away from a purely antitrust exercise.

It is also apparent in MOFCOM’s decisions that the agency has sought opinions from experts in law, economics, the relevant industry, and the relevant technical areas. MOFCOM has hired outside economics experts, including Chinese academics and international economic consulting firms, in at least five cases so far: Coca-Cola/Huiyuan, Seagate/Samsung, WD/Hitachi, MediaTek/
MStar, and UPS/TNT Express.\textsuperscript{13} In addition, MOFCOM itself has an Economics Analysis Division, headed by a Ph.D. economist. However, it is not obvious from the decisions what economic analyses, especially quantitative analyses, were conducted or how involved the outside or internal economists were in each case.

**Remedies.** MOFCOM’s remedies have received perhaps the most intense spotlight. At the same time, MOFCOM appears to have devoted substantial resources toward strengthening its understanding and capabilities in this area. MOFCOM enacted Provisional Rules on Divestitures of Assets or Businesses to Implement Concentrations Between Undertakings (Provisional Divestiture Rules) in 2010.\textsuperscript{14} These rules likely will be replaced by a finalized version of Draft Rules

\begin{table}[h]
\centering
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline
Case & Other Relevant Government Agencies & Trade Association & Downstream Firms & Competitors & Outside Experts & Notes \\
\hline
(\textit{a}) & (\textit{b}) & (\textit{c}) & (\textit{d}) & (\textit{e}) & (\textit{f}) & \\
\hline
InBev/AB & \textbf{Y} & \textbf{Y} & \textbf{Y}\textsuperscript{1} & \textbf{Y} & Legal, Economics, and Agricultural Experts & \\
\hline
Coca-Cola/Huiyuan & \textbf{Y} & \textbf{Y} & \textbf{Y}\textsuperscript{1} & \textbf{Y} & & \\
\hline
Mitsubishi Rayon/Luckte & \textbf{Y} & \textbf{Y} & \textbf{Y}\textsuperscript{1} & \textbf{Y} & & \\
\hline
GM/Delphi & \textbf{Y} & \textbf{Y} & \textbf{Y}\textsuperscript{1} & \textbf{Y} & & \\
\hline
Pfizer/Wyeth & \textbf{Y} & \textbf{Y} & \textbf{Y}\textsuperscript{1} & \textbf{Y} & & \\
\hline
Panasonic/Sanyo & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
Novartis/Alcon & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
Uralkali/Silvinit & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Industrial Expert & \\
\hline
Alpha V/Savoa & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
GE/Shenhuia (JV) & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Industrial Expert & \\
\hline
Seagate/Samsung & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Industrial Expert & \\
\hline
Henkel HK/Tiande (JV) & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Industrial Expert & \\
\hline
WD/Huachi (Viviti) & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
Google/Motorola Mobility & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Technical Expert & \\
\hline
UTC/Goodrich & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
Wal-Mart/Yhaodian & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
ARM/G&D/Gerhawo (JV) & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
Glencore/Xstrata & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Industrial Expert & \\
\hline
Marubeni/Gavilon & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
Baxter/Cambro & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & & \\
\hline
MediaTek/MStar & \textbf{Y} & \textbf{Y} & \textbf{Y} & \textbf{Y} & Economics Expert & \\
\hline
\end{tabular}
\caption{Third-Party Information and Opinions Sought Out by MOFCOM for Cases Where MOFCOM Intervened}
\end{table}

Footnotes: \textsuperscript{1} Upstream firms were also inquired by MOFCOM. \textsuperscript{2} “Relevant enterprises” were contacted by MOFCOM according to the decisions. These could be downstream firms, upstream firms, or competitors. Source: http://fldj.mofcom.gov.cn/article/ztxx.

\textsuperscript{13} Information regarding the first four cases is based on MOFCOM’s published decisions. Information regarding UPS/TNT Express is based on the authors’ own experience.

\textsuperscript{14} See http://fldj.mofcom.gov.cn/article/c/201007/20100707012000.shtml.
Regarding Imposition of Restrictive Conditions on Concentrations of Undertakings (Draft Conditions Rules) later this year.15

In its recent decisions granting approval with conditions, MOFCOM has started to attach a separate document describing the parties’ obligations under the imposed remedy. MOFCOM has

<table>
<thead>
<tr>
<th>Table 4</th>
<th>Timing of Remedy Proposal and Behavioral Remedy Obligations for Conditional Approval Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>August 1, 2008 - September 30, 2013</td>
<td></td>
</tr>
<tr>
<td>Case</td>
<td>Competitive Relationship</td>
</tr>
<tr>
<td>InBev/AB</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Mitsubishi Rayon/Lacite</td>
<td>Horizontal and Vertical</td>
</tr>
<tr>
<td>GM/Delphi</td>
<td>Vertical</td>
</tr>
<tr>
<td>Pfizer/Wyeth</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Panasonic/Sanyo</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Novartis/Accentia</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Uralalk/Silvinit</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Alpha V/Savio</td>
<td>Horizontal</td>
</tr>
<tr>
<td>GE/Shenhua (JV)</td>
<td>Vertical</td>
</tr>
<tr>
<td>Seagate/Samsung</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Henkel HK/Tiande (JV)</td>
<td>Vertical</td>
</tr>
<tr>
<td>WD/Hitachi (Viviti)</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Google/Motorola Mobility</td>
<td>Vertical</td>
</tr>
<tr>
<td>UTC/Goodrich</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Wal-Mart/Yhaosian</td>
<td>Conglomerate</td>
</tr>
<tr>
<td>ARM/GKD/Gemalto (JV)</td>
<td>Vertical</td>
</tr>
<tr>
<td>Glencore/Xotrata</td>
<td>Horizontal and Vertical</td>
</tr>
<tr>
<td>Marubeni/Gavilon</td>
<td>Horizontal</td>
</tr>
<tr>
<td>Baxter/Gambro</td>
<td>Horizontal</td>
</tr>
<tr>
<td>MediaTek/MStar</td>
<td>Horizontal</td>
</tr>
</tbody>
</table>

Notes: 1 Excludes application for modification/waiver due to significant changes of circumstances. 2 Divestiture trustees and a hold-separate manager were required. Source: [http://fldj.mofcom.gov.cn/article/ztxx](http://fldj.mofcom.gov.cn/article/ztxx).
included some unique characteristics and unconventional aspects in its remedies. We will highlight these in our discussion below.

**Types of Remedies.** In Table 4, we categorize the remedies imposed on each of the 20 conditional approvals. Structural remedies often involve divesting part of the assets or business of the parties, after which further supervision generally is not required. Behavioral remedies involve some form of ongoing commitments by the parties, such as granting access to infrastructure, licensing key technology, or termination of exclusive agreements, which often require further supervision by the antitrust agency.

MOFCOM appears to have applied behavioral remedies much more often than structural remedies: 12 conditional approvals have pure behavioral remedies, 3 have purely structural remedies, and 5 have a combination of both structural and behavioral remedies.16

In the United States and the European Union, behavioral remedies are disfavored in horizontal mergers and are generally applied only to vertical mergers or are used as temporary measures to support a structural remedy. In contrast, MOFCOM has frequently used behavioral remedies in transactions where MOFCOM identified only horizontal concerns, including Inbev/AB, Panasonic/Sanyo, Novartis/Alcon, Uralkali/Silvinit, Seagate/Samsung, WD/Hitachi (Viviti), Marubeni/Gavilon, Baxter/Gambro, and MediaTek/MStar. In addition, MOFCOM has used behavioral remedies in another two cases, Mitsubishi/Lucite and Glencore/Xstrata, where although both horizontal and vertical concerns were expressed, the remedies were targeted only at the horizontal concerns. In each of these two cases, the vertical concern seems to arise from the fact that one of the parties also participated in the downstream business, so that the merged entity with increased concentration in the upstream business might discriminate in favor of its own downstream business. However, in each case, MOFCOM’s principal concern appears to be horizontal, and the imposed behavioral remedies do not seem to have pertained to the vertical concern, which was alleged but not clearly elaborated in the published decisions.

The fact that more than half of its conditional decisions involved behavioral remedies and 65% of these behavioral remedies were imposed in cases where MOFCOM only (or primarily) expressed horizontal concerns suggests that behavioral remedies are MOFCOM’s de facto preferred type of remedy. A possible reason for MOFCOM’s preference for behavioral remedies might be that a behavioral remedy can be tailored to address specific concerns brought up by different stakeholders, such as downstream firms and other government agencies. For example, MOFCOM expressed concerns in Uralkali/Silvinit about post-transaction market shares of the margining parties (i.e., more than 33.3% globally and more than 50% in import of potash) and did not identify any vertical concerns, but a behavioral remedy was imposed to ensure a steady, reliable, and sufficient supply of potash to Chinese customers.

**Unique Characteristics of Imposed Remedies.** MOFCOM’s conditional decisions so far often lack a detailed discussion of the theory of competitive harm and how the remedies will address such harm. It is therefore difficult to determine whether the imposed remedies were closely tailored to the theory of competitive harm. Nevertheless, several of MOFCOM’s conditional decisions have involved remedies that are not commonly used in other major antitrust jurisdictions.

---

16 Other sources might have categorized the remedy types differently. For example, on August 2, 2013, MOFCOM published a statement regarding its enforcement in the past five years, available at http://www.mofcom.gov.cn/article/ae/ai/201308/2013080226124.shtml. In this statement, MOFCOM stated that structural remedies accounted for 50%, behavioral remedies accounted for 39%, and hybrid remedies accounted for 11% of its first 18 conditional decisions (at that time, Baxter/Gambro and MediaTek/MStar were still under review), without revealing which cases were classified under each type. Based on our categorizations of the first 18 conditional decisions, structural remedies accounted for 17%, behavioral remedies accounted for 61%, and hybrid remedies accounted for 22% of all decisions.
• Refraining from future acquisitions or expansion
In InBev/AB, the merged entity was ordered not to increase its ownership share in two Chinese breweries and not to seek any ownership share in two other Chinese breweries, without further approval by MOFCOM. It is not unheard of in other jurisdictions (e.g., the United States) for the merging parties to be restricted from making future acquisitions in the same industry. However, the fact that MOFCOM did not specify the combined market share of the parties and that it specified four Chinese breweries in which the merging parties are ordered to refrain from investing raise the question of whether this remedy was driven by industrial policy concerns.

In Mitsubishi Rayon/Lucite, in addition to a capacity divestiture, a five-year restriction was imposed both on future acquisitions in the same industry and on establishing new plants. It is quite unusual in the United States and the European Union for merger remedies to impose limitations on capacity growth by the merging parties, because an increase in capacity is viewed as pro-competitive and beneficial to customers. Again, in imposing such terms and conditions, MOFCOM may have been motivated by an industrial policy goal of protecting domestic competitors.

• Maintaining specified trading terms or sales practices
In Glencore/Xstrata, in addition to a divestiture (the sale of Xstrata’s Las Bombas Peru copper mine project) to a MOFCOM-approved buyer, the decision provided for additional conditions that ensured favorable terms for Chinese smelting customers: Glencore must continue for nearly eight years to supply Chinese customers with copper, zinc, and lead concentrates on specified terms under a combination of long term and spot contracts. However, the combined shares in the concentrates markets where MOFCOM required commitments were far below levels that would normally raise issues for U.S. or EU regulators. The parties had a combined market share of 12.1% of copper concentrates sales in China and no overlap in zinc and lead concentrates sales in China. MOFCOM’s decision does not offer a detailed competitive rationale to support the remedies it required.

In Uralkali/Silvinit, which was cleared in 2011, the merged entity was required to maintain a steady, reliable, and sufficient direct supply of various potassium chloride products to China to satisfy a variety of end uses and maintain current sales practices and negotiation procedures with Chinese customers. In the most recent MediaTek/MStar decision, in addition to a Chinese-style hold-separate order (discussed below), the two merging parties were required to maintain pre-transaction practices on supply, after-sale services, and revealing source code, for example.

It is unusual in the United States and the European Union for merger remedies to involve commitments regarding such specific commercial behavior, particularly without a clear analysis of how such commitments address specific antitrust theories of harm.

• Requiring merging companies to remain separate post-transaction
In the two hard disk drive deals (Seagate/Samsung and Western Digital/Hitachi), MOFCOM required that the target should be maintained as an independent competitor after the completion of the transaction. In Marubeni/Gavilon, MOFCOM ordered that Marubeni and Gavilon operate their businesses in soybean sales and imports to China independently for at least two years, despite that fact that the parties’ combined share of soybean imports was less than 18.7%. Unlike the two hard drive deals, this hold-separate order is explicitly limited to the Chinese market only.

The fourth and most recent hold-separate order MOFCOM has imposed on multinationals was MediaTek/MStar. This is in some ways the most stringent hold-separate remedy MOFCOM has issued so far. Although the hold-separate order is limited to the LCD TV chip business, MediaTek’s shareholder rights were reduced to only three: receiving MStar’s dividends, obtaining information
regarding consolidated financial statements of the listed company, and (subject to conditions) appointing directors. In addition, the monitoring trustee’s powers are designed to be very expansive and intrusive, including attending director meetings and reviewing meeting minutes. The most striking requirement in the MediaTek/MStar hold-separate order is that the transaction cannot be closed until its remedy implementation plan is approved by MOFCOM. This requirement is especially worrisome because it may significantly delay the closing of the transaction.

MOFCOM’s long term hold-separate orders prohibit the merging companies from consolidating their operations post-transaction. In the United States and the European Union, such hold separate orders are typically used on a temporary basis and are primarily imposed on companies in the context of a divestiture to minimize the risk of any loss of competitive potential of the to-be-divested business between the date of conditional clearance of the transaction and the date of the completion of the divestiture.\textsuperscript{17} In these situations, the hold-separate orders are limited in scope to the business to be divested to allow the merging parties to realize the procompetitive benefits from the combination in other nondistributed business. The hold-separate orders imposed by MOFCOM can reduce potential cost-savings related to production, procurement, and R&D, create uncertainty for companies involved and for their employees, and generate significant compliance expenses (such as infrastructure cost, monitoring fees, and executive time). Most importantly, antitrust agencies and/or monitoring trustees are not well equipped to intervene in day-to-day business affairs. In our view, intrusive long-term hold-separate orders are likely to violate a guiding principle in both designing and enforcing merger remedies: remedies should minimize interference with ongoing competitive business decisions and preserve merger-related efficiencies to the extent possible.

• Reinforcing MOFCOM’s existing authority over foreign investment policy

The Wal-Mart/Yihaodian decision’s reference to leverage effects suggests that MOFCOM applied a conglomerate theory of antitrust harm, which is not generally used in the United States and is only sparingly applied by the European Commission. The remedies, which were intended to ensure that Wal-Mart/Yihaodian did not extend its market power from the brick-and-mortar supermarket segment to the Value Added Telecommunications Business (VATB) segment, appear to have been imposed to reinforce MOFCOM’s authority over foreign investment policy (i.e., regulating foreign investment in a restricted or prohibited sector such as VATB).

• Other unconventional remedies

In Novartis/Alcon, one of the conditions that MOFCOM imposed was that Novartis stop its sale of anti-inflammatory/anti-infective compounds for the treatment of eyes in China for five years. It is unclear why this remedy was needed when the incremental increase in market share post-transaction was negligible—Novartis had less than a 1% share in China’s market for anti-inflammato-
ry/anti-infective compounds for the treatment of eyes and intended to exit the market.

In Alpha V/Savio, although it was not clear whether Alpha V controlled a Swiss competitor of Savio, Uster Technologies AG, a divestiture of a minority interest (27.9%) owned by Alpha in Uster was required. A less-restrictive remedy (e.g., a firewall) might have been used instead.

MOFCOM was the only antitrust authority around the globe to impose conditions on Google/ Motorola Mobility. Among other conditions, MOFCOM required Google to continue to honor Motor-

\textsuperscript{17} They may also be imposed by the U.S. antitrust authorities in unreportable transactions while they are investigating, and by the European Commission in public tender cases pending antitrust review.
Ola Mobility’s current fair, reasonable, and non-discriminatory (FRAND) obligations on its standard essential patents (SEPs). However, it seems that the concern that was addressed by this remedy is not “merger specific,” and could have been addressed, if needed, under other provisions of the AML by other antitrust authorities in China.

**Duration of the Behavioral Remedy or Time to Apply for Modification/Waiver.** MOFCOM has imposed different durations for behavioral remedies. The longest duration applied to date is eight years in the ARM/G&D/Gemalto JV and around seven-and-a-half years in Glencore/Xstrata (See Table 4). The Draft Conditions Rules provide that MOFCOM’s decision will specify the duration for behavioral remedies, but if the duration is unspecified, then the default duration is ten years.18

In some cases, no fixed duration of behavioral remedy is specified, but the remedy instead provides a time to apply for modification/waiver of the behavioral remedy (see Table 4). All of the hold-separate orders (i.e., Seagate/Samsung, Western Digital/Hitachi, Marubeni/Gavilon, and MediaTek/MStar) are subject to a one-to-three-year duration, after which the merging companies are eligible to apply for MOFCOM’s reconsideration. Such a provision calls into question finality and predictability, which, in our view, are two of the underlying principles for merger remedies. The Draft Conditions Rules make such uncertainty particularly worrisome. Under Article 30 of the Draft Conditions Rules, MOFCOM may impose stricter remedies after the fact “if the market competitive situation has changed to the extent that the restrictive conditions cannot lessen the negative impact.” It would be a very dangerous trend if MOFCOM found it appropriate to employ hold-separate orders, which represent a de facto wait-and-see approach, as a panacea for any transaction on which MOFCOM is reluctant to make a final determination. At a minimum, remedy obligations should not be made more burdensome or restrictive when companies apply for a modification or waiver of the original behavioral remedy, and clear guidance is needed on the procedure and the substantive analysis required when applying for modification of original behavioral remedies (e.g., lifting a hold-separate).

**Monitoring Trustee for a Behavioral Remedy.** MOFCOM has started to use monitoring trustees to supervise the implementation of behavioral remedies, beginning with its decision on Novartis/Alcon. In most behavioral remedy cases, a third-party monitoring trustee was retained by the parties (see Table 4).19 However, in ARM/G&D/Gemalto and Wal-Mart/Yihaodian, MOFCOM reserved the right to supervise the company’s fulfillment of its obligations either by employing a monitoring trustee or by performing the monitoring itself. No monitoring trustee was mentioned in MOFCOM’s decision on GE/Shenhua, a JV transaction.

Monitoring trustees need to have well-defined narrow obligations and the business community would welcome any guidance on (i) avoiding excessive intervention or unreasonable demands by trustees; (ii) ensuring trustees’ independence from potential complainants; and (iii) limiting third-party abuse of the monitoring process. After all, the purpose of merger remedies is to maintain market competition, rather than to provide the government/trustee with an opportunity to regulate day-to-day business of an industry or a single firm.20

---

18 See Draft Conditions Rules at Article 13, supra note 15.
19 A monitoring trustee to supervise implementation of a structural remedy could be the same person or entity as the divestiture trustee.
20 “In determining appropriate conduct remedies, the Division appreciates that displacing the competitive decision-making process widely in an industry, or even for a firm, is undesirable. The Division is not a regulatory agency charged with determining how competition should occur in a particular industry.” U.S. Dep’t of Justice, Antitrust Division Policy Guide to Merger Remedies (June 2011), available at http://www.justice.gov/atr/public/guidelines/272350.pdf.
Suitable Buyers of Divested Business. MOFCOM’s stated requirements regarding suitable buyers of a to-be-divested business, whether under the Provisional Divestiture Rules or under the Draft Conditions Rules, are generally in line with the EU rules and the typical U.S. approach. However, in practice, some have expressed concern that MOFCOM might prefer to approve Chinese buyers on industrial policy grounds not related to competition policy. For example, it is reported that Pfizer/Wyeth and Panasonic/Sanyo were regarded by MOFCOM as two examples of successful implementations of MOFCOM’s divestiture orders, and the buyers of the divested business in both of those transactions were Chinese companies.21

Timing to Propose Remedies. Among the 20 conditional clearance decisions, only InBev/AB and GM/Delphi were cleared in phase I (see Table 4). In the other 18 conditional clearance cases, conditional clearances were issued after cases went to phase II. In some cases, a clearance was obtained early because of an early finalized remedy proposal. Similarly, late finalized remedy proposals have led to late clearances. For example, in Alpha V/Savio, Alpha V proposed remedies in phase I and MOFCOM approved the transaction early in phase II. In Panasonic/Sanyo, the merging parties proposed remedies towards the end of phase II and further discussed and modified the remedy proposal during phase III. MOFCOM cleared the deal conditionally about one week later. However, not every conditional clearance came out shortly after the remedy proposal was finalized. For example, in Baxter/Gambro, the conditional clearance was issued almost two months after the remedy proposal was finalized between the merging parties and MOFCOM. In some cases (e.g., Glencore/Xstrata, Marubeni/Gavilon, and MediaTek/MStar), a long and difficult remedy negotiation between the merging parties and MOFCOM led to a “pull and refile” and another round of extensive negotiation after the proposed transaction was refiled.

MOFCOM does not yet have an effective mechanism for informing the merging parties of its specific concerns that should be addressed by remedies. It is therefore extremely hard for the merging parties to effectively design a remedy proposal. The Draft Merger Remedy Rules state that MOFCOM should identify and explain its competition concerns “at an appropriate point” (Article 7), but it remains to be seen how early and how specifically MOFCOM will be prepared to communicate its concerns to the merging parties.22

Sanctions for Breach. MOFCOM’s current rules provide that, if the parties do not comply with remedy obligations, MOFCOM may establish a time limit for correction and take further action in accordance with the AML if undertakings fail to make these corrections.23 In Mitsubishi Rayon/Lucite, the decision provides that a fine of RMB 250,000 to RMB 500,000 will be imposed if the parties materially violate their remedy obligations during the period from the closing of the proposed transaction to the completion of the required divestiture. No correction period before being fined is explicitly granted in the decision. Clearance decisions in some other cases (e.g., Marubeni/Gavilon, ARM/G&D/Gemalto, Wal-mart/Yihaodian, UTC/Goodrich, Google/Motorola Mobility, Western Digital/Hitachi, Seagate/Samsung, Uralkali/Silvinit and GM/Delphi) provide that MOFCOM may impose sanctions for any violation of remedy obligations.

---

21 It is reported that the Chinese buyer of the divested business in Panasonic/Sanyo happened to be the company that raised concerns with MOFCOM and paid an “exceptionally low” price for the divested business. See Joy C. Shaw, MOFCOM Satisfied with Enforcement of 18 Conditionally Cleared Deals, POLICY AND REGULATORY REPORT (June 4, 2013); see also Julie-Anna Needham & Joy C. Shaw, Glencore Xstrata’s Las Bambas Sale Puts MOFCOM’s Credibility in Spotlight—Analysis, POLICY AND REGULATORY REPORT (Sept. 3, 2013).


The Draft Merger Remedy Rules provide that, for a serious breach of remedy commitments, MOFCOM will be able to enforce sanctions available under Article 48 of the AML, withdraw its review decision, and ask the undertakings concerned to re-notify the transaction. In less serious cases, MOFCOM shall require the parties to rectify their non-compliance within a specified time period. If a divesting party violates ancillary obligations rather than the obligation to complete a divestiture, Article 34 provides that MOFCOM shall order the divesting party to propose new remedies. However, these provisions do not specify a procedure and standards for determining whether the breach is serious and what type of sanction is appropriate. They are also inconsistent with MOFCOM’s current rules on sanctions for breach of remedy obligations, which provide a grace period for correction before any sanctions take effect.

What Have We Observed So Far?

In theory and at a high level, merger enforcement in China follows similar procedures and uses a similar set of methodologies as in the European Union and in the United States. However, there are significant differences in practice. Overall, MOFCOM’s merger enforcement appears to be more restrictive in terms of its lack of consideration of efficiencies, its receptiveness to non-horizontal theories of competitive harm, and its application of behavioral remedies, especially long-term hold-separate remedies. This is especially detrimental to the merging parties as well as to customers and competition generally since the merging parties are unable to realize the efficiencies resulting from the merger. Although in theory the parties could appeal in an administrative tribunal to defend the transaction in China if they do not agree with MOFCOM’s decision, to date no one has appealed.

Some of the early fears about how the AML would be enforced, such as predictions that industrial policy factors could overshadow antitrust considerations, appear to remain a concern, at least in some contexts, while other early fears have not come to pass, such as the prospect of reportable deals involving SOEs or Chinese firms more generally not being notified or reviewed. However, MOFCOM has clearly ramped up at an impressive speed along the learning curve over its first five years. Shorter review duration, more sophistication in analysis, and more transparency can be expected with the enactment of simplified procedural rules, an increased adoption of economic analysis, and more experience.

24 There are still concerns, however, that some reportable transactions involving SOEs were completed without notification to MOFCOM. For example, it is reported that the October 2008 merger between China Unicom and China Netcom, two of the only three telecommunication companies in China (the other one being China Telecom, which is also an SOE) was not notified to MOFCOM. See http://www.eeo.com.cn/eeoljgb/2009/05/04/136558.shtml. According to statistics released by MOFCOM, up to August 1, 2013, MOFCOM has issued warnings or fines related to eight reportable transactions that were not notified to MOFCOM. See http://www.mofcom.gov.cn/article/ae/ai/201308/20130802226124.shtml. However, these eight transactions are unnamed, and therefore it is unclear whether China Unicom/China Netcom is one of them. Moreover, a warning or fine might not be enough to address potential anticompetitive effects from such a 3-to-2 transaction.
The Elements of a Policy Statement on Section 5

Neil W. Averitt

The antitrust side of Section 5 of the Federal Trade Commission Act—which prohibits “unfair methods of competition”—has long resisted attempts to define it more precisely. In 2008, the Commission convened a workshop, with support from Commissioners Jon Leibowitz and J. Thomas Rosch, with the goal of developing more insights, consensus, and structure around the statute. As time went by, however, no report or written guidance emerged from the Commission, and even a minimal consensus appeared beyond reach. Congress began to express alarm about the lack of transparency in agency thinking. On June 19 of this year, Commissioner Joshua Wright unveiled a proposed policy statement in an effort to prompt the start of discussions. A few weeks later on July 25, Commissioner Maureen Olhausen gave a speech outlining her thoughts on the principles that might go into such a statement. FTC Chairwoman Edith Ramirez has not responded formally to these invitations; instead, she has proposed leaving Section 5 guidance to a process of case-by-case development. The issue within the Commission remains as stymied as ever.

Whatever precise form the agency action eventually takes, a relatively short, centrist declaration of policy that will clarify the core features of Section 5 is needed. The declaration should indicate that Section 5 is intended to be broader than the Sherman and Clayton Acts, and that it can be applied more broadly in ways that usefully address some real competitive issues but it has identifiable limits and does not authorize a general interest-balancing power to do good.

This article reviews the current debate about a policy statement to define Section 5 and proposes both general principles and specific language that might go into such a statement.

The Current Proposals

Each of the current suggestions for Section 5 guidance has given us important insights on the role of the statute, but none of them has been sufficiently comprehensive or sufficiently attentive to the agency’s overall architecture to provide a fully satisfactory approach to the subject.

Commissioner Wright began the current debate when he proposed his own draft policy statement on Section 5, accompanied by an explanatory speech to the leadership of the New York State Bar Association. He acknowledged that Congress intended Section 5 to reach beyond the Sherman and the Clayton Acts. He also suggested, however, that the imprecise scope of the statute had created significantly harmful uncertainties for business. Commissioner Wright’s pro-

posed policy statement would therefore impose two new limiting standards on a Section 5 action. The challenged conduct must harm competition in a strict economic sense, generally, as demonstrated through “increased prices, reduced output, diminished quality, or weakened incentives to innovate.” The conduct must also involve actions that produce no cognizable efficiencies; if it does, then it can be challenged only under one of the other antitrust statutes.

Although Commissioner Wright’s proposal must be given credit for highlighting the need to better define Section 5, it suffers from four problems: First, it identifies very few “harms to competition” that are not already Sherman Act violations, thus undercutting the purposes of the statute. Even the proposed statement’s example of incipient harm to competition involves a firm that already possesses “market power,” and so is likely to be within the monopolization law. Second, the proposed efficiencies screen would, as a practical matter, preclude virtually all Section 5 actions. Almost any conduct, no matter how harmful, produces some genuine collateral efficiencies and, in the absence of any rule of reason balancing test, that fig leaf will be sufficient to prevent Commission action. Third, the proposed statement does not consider less disruptive ways of dealing with the real problems of business uncertainty. It does not, for example, consider the use of external references such as asking whether the anticompetitive conduct also violates some external standard of business conduct. Fourth, the proposed statement seems too one-sidedly sensitive to the risks of over-inclusive enforcement and fails to balance this risk against those to consumers from under-inclusive enforcement. In his introductory speech, Commissioner Wright referred nine separate times to the need to avoid “deterring consumer welfare-enhancing business practices.”

Commissioner Wright’s fellow Republican Commissioner Ohlhausen picked up his call in a major speech the following month to the U.S. Chamber of Commerce. She also urged the agency to issue “some type of policy statement or other guidance on how and when [it] will pursue standalone Section 5 cases.” In lieu of a draft of such a statement, she instead offered a set of six principles or screens in an appendix to her written remarks. A Section 5 action would be appropriate, she suggested, only when it addresses harm to “competition or the competitive process” rather than to individual competitors; when the competitive harms are “disproportionate” to the benefits realized; when no other agency is in a better position to address the problem; when the Commission has acquired “substantial expertise” before challenging conduct as a new violation; and when a firm can be given sufficient guidance to know before the fact that its conduct might be challenged. Some areas—such as invitations to collude and facilitating practices—are likely to meet all these criteria. But Commissioner Ohlhausen also added a final principle that would direct the agency toward a primary focus on other parts of the FTC Act. She suggested that when the agency seeks to pursue innovative tasks, it could more profitably focus on non-litigation tools such as research, reports, and advocacies that will improve the quality of mainstream antitrust analysis. Section 5, she thought, “should not play a significant part in the FTC’s competition enforcement efforts.”

---

4 Wright, supra note 2, at 7.
5 See Wright, supra note 3.
7 Id. at 1.
8 Id. at 7–8.
9 Id. at 19.
Commissioner Ohlhausen’s speech was also a helpful effort to move the discussion forward, but it too suffers from a number of difficulties: First, her proposed Section 5 standard of “disproportionate” harm—although less restrictive than Wright’s requirement for no efficiencies at all—is still narrower than the neutral rule of reason balancing that is the general coin of the realm for antitrust analysis. Second, her proposal downplays the possible importance of business torts as an area of Section 5 action, acknowledging in principle that they might harm competition even if they do not create individual market power, but then caricaturing the issue as an effort to “require businesses to play nice with each other.”10 Third, the proposed construction of Section 5 does not have a suitable overview of the relationships between antitrust and consumer protection law. Thus it suggests that deception of a standard-setting organization should be pursued under the Sherman Act as monopolization, but does not consider the simpler possibility of pursuing it as deception under the consumer protection side of Section 5. Fourth, the proposal invites new dangers by looking too closely for other agencies or private litigants that may be better placed to handle an issue. An awareness of these alternatives is reasonable and helpful, but if carried too far it can lead to a jurisprudence of self-help that gives preferential treatment to wealthy litigants or to a diffusion of responsibility among agencies that invites a repeat of problems such as the unsupervised mortgage meltdown of 2008.

FTC Chairwoman Edith Ramirez favors a different course entirely. Rather than developing a comprehensive statement on how Section 5 is construed, she prefers to let the law and guidance both develop through case-by-case adjudication. This was made clear in the follow-up to last April’s antitrust oversight hearings. Republican Senator Michael Lee from Utah asked her, “Why are you resistant to provide [Section 5] guidance in a more comprehensive, published form upon which the business community and others can meaningfully rely?”11 She replied by making the case for an alternative approach:

Case-specific guidance, grounded in detailed facts and sound economic theory, is likely the most useful form of guidance for the business community and lawyers advising the business community. Due to the fact-based nature of antitrust cases, as well as our need to retain flexibility to use Section 5 to protect competition and consumers as markets and economic learning evolve, any non-case-specific guidance document would necessarily be far more general, and thus less useful.12

The course proposed by Chairwoman Ramirez presents, however, its own set of problems: First, common law development of Section 5 is not likely to yield effective guidance because the cases are too infrequent for precedents to accumulate rapidly enough. Second, the lack of an articulated overall vision will hurt the agency in the courts of appeals because the courts will not have confidence that the agency is entitled to Chevron deference in its construction of its statute.13 Third, the lack of guidance will inhibit the Commission’s own lawyers and may leave some competitive problems unaddressed even if they might be within the reach of innovative theories. Fourth, the lack of guidance may also leave the agency vulnerable to political scare tactics. Business exec-

---

10 Id. at 18.


12 Id. at 12.

13 See Chevron U.S.A. v. Natural Res. Def. Council, 467 U.S. 837, 843, 865 (1984) (finding that courts should defer to an agency’s own construction of a statute committed to its administration as long as this involves “a permissible construction of the statute” and the agency “considered the matter in a detailed and reasoned fashion”).
utives can plausibly claim to have been confused and inhibited from beneficial actions even if those claims are exaggerated. Ultimately, the case-by-case approach casts needless doubt on the agency’s effectiveness as an ongoing institution. If it cannot derive general principles even after having had 99 years of experience with Section 5, when will it be able to do so?

So, all things considered, it seems that none of the current efforts to clarify the purpose and scope of Section 5 is fully satisfactory and that the Commission should continue to think about other ways of providing guidance.

General Principles for Construing Section 5
Before turning to the specifics, it seems useful to pause and try to identify general principles that might guide a successful statement.

Seven principles seem particularly fundamental:

1. As a starting point, Section 5 was intended by Congress to be significantly broader than the Sherman and Clayton Acts in at least some respects. The wisdom of any particular extension is naturally open to debate. However, the debate should begin by recognizing the task that Congress gave the agency.

2. The agency is charged with identifying and addressing any form of conduct that is unreasonably harmful to competition. The agency’s mission is limited to these competitive harms; the search for “unfair” methods of competition does not authorize inquiry into social or moral values. But within the competition universe, the agency is instructed to address competitive harms regardless of the particular form they take. Cognizable harm may involve an immediate injury to the process of price competition, or injury to nonprice competition in terms of quality or innovation, or reasonably foreseeable injury to future competition.

3. This inquiry will sometimes lead to condemnation under Section 5 of conduct that is essentially similar to a Sherman or Clayton Act violation, but that nonetheless would not be condemned under those statutes. For example, the Commission might find that certain conduct is likely to lead to outright collusion or monopolization in the reasonably predictable future, even if it does not do so immediately. The legislative history on this power is clear and emphatic.

4. The Commission should nonetheless be slow and sparing in this use of Section 5. Aggressive pursuit of such theories will result in situations where the same conduct is judged differently, depending on which antitrust agency handles the matter. That is a part of the congressional plan, of course. But it nonetheless makes for difficulties in business planning and counseling. And it will be appropriate only in a finite number of cases because the Sherman and Clayton Acts have been judicially expanded over the years so as to reach most applications of real concern.

5. A more important role for Section 5 is to reach forms of competitive harm that are different in kind from Sherman and Clayton Act violations rather than different only in degree. These can include situations in which competition, while remaining intense in some respects, has been diverted into channels that are less beneficial to consumers, such as through the use of misrepresentations, abuse of a regulatory process, commercial bribery, or industrial espionage.

6. Attention to such matters will lead the Commission to refer to other bodies of business law, such as state laws on business torts, as long as the conduct also has market-wide competitive effects. This does not need to imply an undesirable duplication of enforcement effort, but can

---

14 While the FTC has achieved a number of useful settlements on issues like invitations to collude, it has not won a litigated court case relying solely on its competition authority under Section 5 since the “tires, batteries, and accessories” cases of the 1960s. See, e.g., FTC v. Texaco Inc., 393 U.S. 223 (1968). It seems unlikely that businesses are deeply inhibited by concerns about the statute.
instead lead to a beneficial integration of business laws that will lead to greater predictability. It can also help to prevent diffusion of responsibility among agencies, inaction, and enforcement gaps.

7. The most important single body of external law is the Commission’s own consumer protection authority under the other half of Section 5. The Federal Trade Commission is a single agency, applying a single statute, and it should take this occasion to lay out an integrated vision of its mission. The two halves of Section 5 can be shown to work together to protect a market economy that is responsive to consumer choice: antitrust protects the array of options in the marketplace, and consumer protection then safeguards the ability to select among those options. Pointing out this overall architecture of the statute will have several benefits for the agency. It will provide a framework for defining the proper scope of each part of the FTC Act, will suggest when particular matters should be assigned to one or the other side of the statute, and will demonstrate a systematic vision that will make the agency’s construction of its statute more persuasive to the courts of appeals.

A Proposed Policy Framework for Defining “Unfair Methods of Competition”

Effective guidance will require turning these general principles into a short written statement for the antitrust bar and for the FTC itself. That guidance will put the agency formally on record as to how it interprets the prohibition against “unfair methods of competition.” The agency’s statement should describe the areas in which Section 5 is applicable, and also the limitations that it believes are contained in the statute. The analytical elements that are identified in the statement will be the product of the Commission’s experience in applying the statute in a wide variety of circumstances. Guidance can also incorporate the agency’s learning from case law and commentary, including contributions made by participants in the Commission’s 2008 workshop on Section 5.

Legislative History and Early Case Law. Congress enacted the FTC Act in 1914 primarily in response to concerns that the Sherman Act would not reach all business practices that were harmful to competition. Section 5 was therefore made broader than other trade statutes. One of the Act’s principal sponsors noted that it was intended to “make some things punishable, to prevent some things, that can not be punished or prevented under the [Sherman] antitrust law.” The legislative history makes clear that Congress wrote the act broadly as a conscious choice because “there were too many unfair practices to define, and after writing 20 of them into the law it would be quite possible to invent others.” To apply this general standard, Congress created a specialized agency with broad discretion and then determined to “leave it to the [C]ommission to determine what practices were unfair.”

15 Section 5 begins with the following language: “Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful. The Commission is hereby empowered and directed to prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce.” 15 U.S.C. § 45(a) (listings of certain exempt industries omitted).

16 See FTC Section 5 Workshop, supra note 1. Any new policy statement should be limited to unfair competition matters. It should not address the issues involved in interpreting “unfair or deceptive acts or practices” under Section 5 or modify any existing policy statement addressing those issues. Nor should any statement affect Commission competition activities taken pursuant to other statutes, such as Section 7 of the Clayton Act, or the Horizontal Merger Guidelines that interpret Section 7.

17 51 CONG. REC. 12,454 (1914) (statement of Sen. Albert B. Cummins).

18 S. REP. No. 63-597, at 13 (1914); see also H.R. REP. No. 63-1142, at 19 (1914).

19 S. REP. No. 63-597, at 13 (1914).
Congress also set some specific limits on the Commission’s discretion, however. An “unfair” method is to be defined by its effects on competition, not through an assessment of its moral or other qualities.\textsuperscript{20} A Commission action must also be in the public interest; the agency is not to take part in private disputes.\textsuperscript{21} And finally, to compensate for the breadth of its discretion, the new Commission was given correspondingly limited remedies, primarily centered on injunctions and orders to guide future conduct.\textsuperscript{22}

The subsequent case law has confirmed both the breadth and the boundaries inherent in this history. In \textit{FTC v. Indiana Federation of Dentists}, the Supreme Court noted that “the unfair methods of competition” language in Section 5 encompasses “not only practices that violate the Sherman Act and the other antitrust laws, but also practices that the Commission determines are against public policy for other reasons.”\textsuperscript{23} At the same time, other courts have emphasized the importance of maintaining conceptual rigor and predictability in the Commission’s analysis. Businesses must not be “left in a state of complete unpredictability.”\textsuperscript{24}

An effective policy statement will need to show how the Commission approaches the task of harmonizing these two goals.

\textbf{Relationship with Other Statutes.} Defining an “unfair method of competition” can be made easier by taking account of the context in which this statutory language appears. The nature of the Commission’s responsibilities under this provision are best understood in light of the other work of protecting the competitive process, conducted by the Commission and by others, under other adjacent statutes.

One such set of relationships is found with the Sherman and Clayton Acts. Section 5 was intended to go beyond those statutes in certain ways, but also to take them as a starting point for analysis. Some applications of Section 5 are therefore defined by their relationship with the substantive concepts of the Sherman Act, as will be discussed below.

Another set of relationships is found with state trade regulation statutes. Congress anticipated that the Commission would make reference to “the decisions of the courts,”\textsuperscript{25} and the Supreme Court has noted that the agency can take account of “the common law and criminal statutes.”\textsuperscript{26} If conduct that implicates state business practice statutes also harms competition within the meaning of the FTC Act, then the reach and boundaries of the state statutes can be relevant sources of insight, as will also be discussed below.

Most fundamentally, the term “unfair methods of competition” is shaped by its setting within the larger context of the FTC Act as a whole. The Act in its entirety works to protect a market economy that is responsive to consumer choice. Such an economy requires two basic conditions: an

\begin{itemize}
  \item \textsuperscript{20} See 51 CONG. REC. 12,220 (statement of Sen. Francis G. Newlands) (the “legal significance is the same as the economic significance”).
  \item \textsuperscript{21} See FTC v. Klesner, 280 U.S. 19 (1929); 51 CONG. REC. 11,104–05 (remarks of Sen. Albert B. Cummins) (the bill is “not simply trying to protect one man against another;” an unfair method must involve “something that has a tendency to affect the people of the country or be injurious to their welfare”).
  \item \textsuperscript{22} See 51 CONG. REC. 11, 111–12 (statement of Sen. Francis G. Newlands) (explaining decision not to include “extreme penalties” in the FTC Act on grounds that rights and duties under that legislation would be continuously evolving).
  \item \textsuperscript{23} FTC v. Ind. Fed’n of Dentists, 476 U.S. 447, 454 (1986) (dictum); see also FTC v. Sperry & Hutchinson, 405 U.S. 233, 239 (1972) (Commission empowered “to define and proscribe an unfair competitive practice, even though the practice does not infringe either the letter or the spirit of the antitrust laws”).
  \item \textsuperscript{24} E.I. du Pont de Nemours & Co. v. FTC (Ethyl), 729 F.2d 128, 139 (2d Cir. 1984).
  \item \textsuperscript{25} 51 CONG. REC. 13048 (statement of Sen. Albert B. Cummins).
  \item \textsuperscript{26} FTC v. R.F. Keppel & Bro., 291 U.S. 304, 313 (1934).
\end{itemize}
array of options in the marketplace for consumers to select among and an ability on the part of consumers to make that choice in a free and informed manner. The Commission’s consumer protection authority protects the ability of buyers to make these purchase decisions and selections. Its unfair competition authority protects the initial array of marketplace options. An unfair method of competition can therefore be thought of as conduct that unreasonably diminishes the array of market options within the meaning of this plan.27

**The Elements of “Unfair Competition.”** More specificity is needed in order to turn this general concept into an operational definition of unfair competition. That specificity can be grounded in a review of the case law and the record of the public workshop that the Commission held to discuss these issues. Synthesizing this material, I would suggest that an unfair method of competition has three formal legal elements: (1) a definable harm to competition; (2) competitive techniques that are wrongful in the sense that they are not competition on the merits; and (3) an overall result that is harmful to consumers in its net effect. There is also a fourth consideration—predictability—which is not a formal part of the legal offense, but should be an important policy goal nonetheless.

**An unfair method of competition requires,** first of all, conduct that in some way concretely harms competition or that poses an unreasonable risk of harming it in the future. Cognizable harms can take any of several forms.

**Violations of the Sherman and Clayton Acts.** Conduct that would violate the letter of the Sherman or the Clayton Acts will automatically involve sufficient competitive harm to satisfy the standards of the more inclusive FTC Act as well. The Commission does not have jurisdiction to enforce the Sherman Act directly, so all FTC challenges to conduct that would violate that statute are necessarily brought under the authority of Section 5.28 The Commission is specifically authorized to enforce the Clayton Act, so most actions involving those theories of liability will be brought directly under that statute. The agency still has the option of proceeding under Section 5 instead, however.29

Example 1: Competing x-ray laboratories agree about the terms on which they will do business with insurance companies. The FTC can pursue this conduct as an unfair method of competition even though others with direct jurisdiction under the Sherman Act might challenge it under that statute instead.

---

27 The Commission has described the interaction among the components of the FTC Act in the following terms:

The various components of the statute form an integrated whole, allowing the Commission to promote the diverse benefits of a free and open economy. Thus the ban on unfair competition prevents exclusionary or anti-competitive behavior and helps preserve a full variety of marketplace options for consumers to choose among; the ban on deception helps ensure that consumers will not make that choice on the basis of misleading information; and the ban on unfair practices ensures that the choice is not distorted by coercion, the withholding of material information, or similar practices. Safeguards at all three levels are needed to ensure that substantial consumer injury is adequately addressed.

Companion Statement on the Commission’s Consumer Unfairness Jurisdiction, 4 Trade Reg. Rep. (CCH) ¶ 13,203 at 20,909-3 (1980). For a concrete application of these distinctions see, e.g., *International Harvester*, 104 F.T.C. 949 (1984). This general plan also contains some particular exceptions and qualifications that may affect, for example, the treatment of privacy issues on the consumer protection side of the statute; those topics are not addressed here.


Example 2: Two supermarket chains agree to a merger. In cases where Section 7 of the Clayton Act covers all significant aspects of the transaction, the FTC will normally proceed under that statute rather than acting under Section 5.

**Technical evasions of the antitrust statutes.** The Commission can also use Section 5 to fill technical gaps in the coverage of the Sherman and Clayton Acts. A “technical gap” exists in this sense where the underlying statute does not literally apply to a particular situation, but where the conduct still has all the same substantive characteristics as a statutory violation and where there is no clear indication that Congress intended to provide an exemption in the circumstance involved. A commonly cited example of this situation is the invitation-to-collude case. Section 5 can apply in these situations to fill the gap. The competitive harm that would have justified application of the original statutes, had the gap not existed, should be sufficient to satisfy Section 5 as well.

Example 3: A maker of vehicle axles invites a competitor to agree with it on prices, but the competitor declines. The firm’s conduct would have made it liable for price fixing if its offer had been accepted. The Sherman Act forbids actual collusion and attempted monopolization, but not attempted collusion. The FTC can nonetheless reach the invitation under Section 5, because doing so does not turn previously innocent conduct into a violation.

Example 4: An automobile manufacturer discriminates among the operators of car-rental fleets in the lease rates it charges. The Robinson-Patman Act prohibits discriminations in price. The FTC could not reach this situation on a theory of a technical gap because doing so would alter the nature of the conduct that is prohibited from selling to leasing.

**Incipient violations of the antitrust statutes.** The Commission’s authority under “unfair methods of competition” should also cover conduct that is not presently a violation of one of the other antitrust statutes but that appears likely to result in such a violation in the foreseeable future. This is one of the best documented goals of Section 5. “A major purpose of [the FTC] Act was to enable the Commission to restrain practices as ‘unfair,’ which, although not yet having grown into Sherman Act dimensions, would most likely do so if left unrestrained.”

Under this theory, the Commission’s task is essentially predictive. What conduct is being used, and what effect is it likely to have at different times in the future? In making this prediction the Commission can look at two possible mechanisms by which consequences can grow: increasing consequences of the conduct in the hands of the originating firm and a possible spread of the conduct as other firms in the industry begin to copy it.

---

31 See also Grand Union Co. v. FTC, 300 F.2d 92 (2d Cir. 1962) (inducing the grant of discriminatory promotional allowances, which would have been illegal for the supplier to give); Cf. Quality Trailer Prods., 115 F.T.C. 944 (1992).
32 The change in substance means that the gap is no longer merely “technical,” and that it can therefore no longer be addressed under this particular narrow application of Section 5. See Foremost-McKesson, Inc., 109 F.T.C. 127, 129–30 (1987) (explaining General Motors Corp., 103 F.T.C. 641, 696, 700–01 (1984)). It is still possible that substantively different conditions can be reached through the broader Section 5 purpose of enforcing the underlying policy of the Sherman Act. That will require a more elaborate assessment of whether Congress intended to distinguish between the two situations, as will be discussed below. An extension to leasing situations would not appear to be warranted under either theory, however.
33 Triangle Conduit & Cable Co. v. FTC, 168 F.2d 175 (7th Cir. 1948), aff’d by an equally divided Court sub nom. Clayton Mark & Co. v. FTC, 336 U.S. 596 (1949). See also FTC v. Motion Picture Adver. Serv. Co., 344 U.S. 392, 394–95 (1953) (“It is . . . clear that the Federal Trade Commission Act was designed to supplement and bolster the Sherman Act and the Clayton Act—to stop in their incipiency acts and practices that, when full blown, would violate those Acts.”).
There are also two limitations on this theory. One is the time horizon beyond which predictions can no longer be made with sufficient confidence. A second limitation comes from the nature of the underlying reference statute. If a substantive statute already contains an incipiency element, then the Commission will not usually use Section 5 to introduce a different standard of incipiency that will look still further into the future.

Example 5: After a long and careful study of certain basing-point prices, the Commission concluded that they had harmful effects, one of which was that their unilateral use increased the likelihood of collusion in a market. When the Commission banned their use in the electrical conduit industry, the Seventh Circuit upheld the order on the basis of that incipient effect.34

Example 6: A coffee manufacturer is charged with using predatory pricing in an effort to attain monopoly power. After investigation, the Commission concludes that the firm is not guilty of attempted monopolization. A charge of incipient monopoly under Section 5 will be dismissed as essentially duplicative.35

Violations of the policy of the Sherman or Clayton Acts. Some conduct takes forms that are similar to Sherman and Clayton Act violations, and may operate through similar mechanisms and have similar consequences, but nonetheless does not come within the scope of those prohibitions. These situations are not the same as the technical gaps because here the conduct is substantively different from that prohibited under the letter of the Sherman and Clayton Acts. Section 5 should still reach these situations, however, if doing so will fulfill the policy or purposes of the underlying statute. In one such case, for example, a firm had made a potentially anticompetitive acquisition through a series of transactions structured so that there may have been no horizontal overlap at the time of the final closing. The conduct was nonetheless successfully challenged as a violation of the policy of the Clayton Act merger provisions.36

This use of Section 5 may become increasingly important as a result of changes in the interpretation of the Sherman Act itself. At one time an argument might have been made that the Sherman and Clayton Acts could be flexibly applied so as to fully carry out their own policies, so that there was no need for a supplemental statute such as Section 5. In recent years, however, through decisions in cases such as Twombly, the Supreme Court has begun to apply the Sherman Act more strictly than before.37 There are understandable policy reasons for this narrowing. The combination of private plaintiffs actuated by personal interests and broad legal theories that made it hard to dismiss complaints at an early stage had worrisome implications. It could lead to inhibiting corporate exposure to treble damage risks and undesirable incentives to settle even non-meritorious claims. But the Court’s corrective narrowing means that some Sherman Act purposes may now need to be protected through the uniquely governmental actions under Section 5.

34 Triangle Conduit & Cable Co. v. FTC, 168 F.2d 175 (7th Cir. 1948). This case is offered to illustrate the general jurisdictional principle; the substantive assessment of basing-point prices is a much debated topic on which no position is taken here.

35 In principle one might believe that the “incipiency” application of Section 5 was intended to look further into the future than the “attempt” provisions of the Sherman Act, but this distinction is too subtle for practical counseling. See Gen. Foods Corp., 103 F.T.C. 204, 366 (1984) (distinguishing between these two theories would require “engaging in such fine distinctions as to challenge the legal philosopher, let alone the competitor trying to conform its conduct to the law”).


In considering a case of this type under the proposed framework, a key issue for the FTC will be ascertaining the intended scope of the underlying statute. Does the letter of the statute express just the core prohibitions that Congress intended to impose most clearly, leaving the further development of those principles to a specialized and neutral administrative agency? Or does the letter of the statute (as interpreted by the courts) fully express the entire intent of Congress so that any effort to expand on it would be contrary to the policy of the statute rather than in fulfillment of it? Each of these situations will no doubt occur on occasion. The proper resolution of this issue will therefore call for careful reading of the legislative history and the statutory scheme in the context of the particular litigation.

Example 7: A petroleum company sells gasoline to its tenant service station operators who have made investments to develop goodwill but whose leases can be terminated easily. The company requests that those stations carry particular lines of tires, batteries, and accessories. A tie-in is not expressly demanded. The Commission finds, however, that the operators react as if an explicit tying arrangement was in force. Section 5 can be used to enforce the policy of the Sherman Act.38

Example 8: A savings and loan company participates in a director interlock that would be illegal if it were engaged in by a bank. A Section 5 action would not be proper here because inquiry into the legislative intent would show that Congress deliberately intended to make a distinction between these two kinds of institutions.39

Facilitating practices. One violation of Sherman Act policy has received particular attention from the FTC. These are facilitating practices, or forms of unilateral but parallel conduct that tend to make it easier and more likely for an industry to arrive at a state of profitable oligopoly coordination. This conduct harms competition by materially facilitating interdependent conduct, and it can violate the basic Sherman Act policy against horizontal coordination.

The challenge in such cases is less the legal theory than the factual analysis.40 Many ordinary and beneficial business practices—such as published price lists and standardized product sizes—also tend to make coordination somewhat easier. The enforcement challenge is to identify the conduct in which the anticompetitive effects predominate with the necessary clarity.

Example 9: In the interval before a competitive bidding process begins, a large supplier of goods to a state government informs government employees of its likely bid price. The firm anticipates that state employees will inform its competitors of that price, and this in fact happens.41 The FTC may challenge this conduct under Section 5.

Example 10: The firms selling a gasoline additive independently offer their refiner customers a number of similar pricing terms. These include delivered pricing, long advance notice of price

38 Shell Oil Co. v. FTC, 360 F.2d 470, 487 (5th Cir. 1966); Cf. FTC v. Texaco Inc., 393 U.S. 223, 229 (1968) (system is “inherently coercive”).
40 See Boise Cascade Corp. v. FTC, 637 F.2d 573, 578 (9th Cir. 1980) (“[T]here is not substantial evidence in the record, considered as a whole, to sustain the Commission’s finding that petitioners’ delivered pricing methods stabilized prices in the plywood industry at supra-normal levels”).
41 If the state employees do not pass the information to other competitors, then no Section 5 action should be brought. One might consider attacking the firm’s conduct as an improper attempt at coordination. However, the conduct of independent state agents seems sufficiently unpredictable, especially when compounded by the further unpredictability of the competitors’ responses, to preclude an inference of attempt in the absence of actual effects.
increases, and most favored nation clauses. Such features may sometimes tend to stabilize prices. However, many of these features are offered here at the customers’ request, and service and safety competition is also important, so it is not clear that the practices have substantially harmed the net terms of sale. A Section 5 case would not be appropriate. 42

**Diversion of competition into less desirable channels.** Competition may also be harmed in a cognizable way if the primary terms of rivalry are shifted into some alternative form that is less beneficial or desirable to purchasers. This is unlikely to be a problem if the action is taken by just a single firm. If other firms are forced to adopt similar behavior in self defense, however, then industry-wide competition may be damaged. 43

Thus, if firms begin to compete with one another through bribery of purchasing agents or industrial espionage, for example, and to present fewer new offerings in terms of price and quality, then competition may be harmed in the sense that the menu of options in the marketplace has been diminished. Competition may also be diminished in the sense that allocative efficiency has been harmed by shifting business away from firms offering better products or lower prices and toward those using illicit means of gaining competitive advantage. Both these effects may occur even if the firms are still competing against each other intensely within the altered terms of rivalry.

Example 11: A major manufacturer of municipal power generators bribes a city official to give its next contract to the firm. This payment effectively excludes the firm’s competitors in the short run and places them under great pressure to adopt similar practices in the future. The Commission may challenge this conduct as a violation of Section 5. 44

Example 12: A firm misrepresents the quality of the material used in its clothing. By itself, that is an instance of consumer deception. If enough firms in the industry come under pressure to compete through making similar misrepresentations, however, the conduct could become an unfair method of competition as well. 45

**Cumulative harm to competition.** In recent years the Commission has encountered business strategies that do not rely on a single readily identifiable anticompetitive action, but that instead harm competition through long-term combinations of methods. These strategies may rely on the cumulative effect of many small but persistent repetitions of the same technique or on the cumulative effects of differing but mutually reinforcing techniques.

The introduction of such strategies may be a natural consequence of an increasingly complex economy in which firms relate to each other in multiple ways. It may also reflect a calculated effort by some firms to pursue anticompetitive goals through complex new methods that are more difficult for the enforcement agencies to detect, characterize, and prosecute.

Cumulative harm to competition may use a number of different tools. It may make use of conventional antitrust violations, contract breaches, deception, or exclusionary misuse of the regulatory process. 46

42 *Cf. Ethyl*, 729 F.2d at 140–41.
43 See FTC v. R.F. Keppel & Bro., 291 U.S. 304, 312–13 (1934) (in the dated context of judging use of gambling techniques to sell candy to children “a trader may not, by pursuing a dishonest practice, force his competitors to choose between its adoption or the loss of their trade”).
44 *Cf. Lockheed Corp.*, 92 F.T.C. 968 (1978). The undesirability of such conduct was confirmed by a legislative judgment. *Cf. 15 U.S.C. 78dd-1 et seq. (Foreign Corrupt Practices Act).*
46 A business strategy of cumulative harm is particularly suitable for assessment under Section 5, which allows the Commission to study new industrial trends. And it lends itself to the Commission’s distinctive use of injunctive remedies that do not create an undue risk of private damage actions before the industry has become familiar with the relevant standards. *See FTC v. Gratz, 253 U.S. 421, 435 (1920) (Brandeis, J., dissenting) (in novel cases, the Commission’s remedies ought to be limited to “prophylactic” measures).*
As a limitation on this theory, however, the Commission will not ordinarily take account of conduct violating those other regulatory laws that do not bear substantially on the relationships between actors in the marketplace. Consideration of additional types of laws would create too much risk of taking Section 5 beyond predictable limits or of creating conflict with another, specialized enforcement regime that may have primary responsibility for the topic.

Example 13: A dominant manufacturer of automotive electronics engages in a series of exclusionary practices. These include making misleading statements about the market readiness of its own products, incorporating certain hidden software to degrade the performance of its rivals’ components, and engaging in bundled pricing and tying arrangements. The Commission may challenge the cumulative effects of this conduct as a violation of Section 5.47

Example 14: A mining company decides not to install expensive pollution-control equipment. This conduct may confer a competitive advantage on it in various areas of operation. The Commission will not challenge this evasion of regulatory duties as an unfair method of competition under Section 5, however, because doing so would create too great a risk of confusion or inconsistency with the work of the Environmental Protection Agency.

Other conduct harmful to competition. Finally, the Commission should have the ability to identify and challenge some new form of conduct that becomes harmful to competition.48 These occasions should not be numerous, however. The well-established applications of unfair competition, discussed above, seem sufficient to reach the great majority of situations that need attention, and the agency should not pursue innovation for its own sake.

Element 2: Use of Wrongful Techniques

To make out an unfair method of competition, it is not enough to simply show that the conduct has been harmful to competition. Many legitimate and beneficial business practices may also have that effect. For example, a firm that properly obtains a patent has excluded competition. A firm that achieves a monopoly through luck or superior competence may have done the same. Indeed, any firm that makes a unilateral decision to drop a product line or to close a local outlet has to some degree diminished competition in that particular area, yet that kind of exercise of business discretion has never been considered actionable. There must also be some element in the conduct that makes it wrongful or not properly competition on the merits.

“Competition on the merits” is the end result contemplated by the consumer choice structure of the FTC Act. It is the process whereby sellers make products or services available, and purchasers decide freely, based on accurate information, which they consider to be the best available offer, thereby rewarding the sellers who offer the more appealing products or services.

Conduct may be determined to be wrongful—in the sense of not being this kind of competition on the merits—by reference to a number of different sources of guidance.

The letter of the antitrust statutes. Many unfair competition actions involve legal theories that simply apply the letter of the Sherman and Clayton Acts. The wrongful nature of conduct violating those statutes is well established. The proper application of the statutory principles to a par-

---

47 Cf. Complaint, Intel Corp., FTC Docket No. 9341 (Dec. 16, 2009); see also id., Concurring and Dissenting Statement of Commissioner J. Thomas Rosch. This case was eventually settled by consent (Aug. 4, 2010).

48 See Cement Institute, 333 U.S. at 693 (Section 5 was intended to hit at every anticompetitive trade practice “then existing or thereafter contrived”).
ticular situation can always be disputed, of course. That is an issue involving the litigation of indi-
vidual cases, however, rather than something that casts doubt on the general wrongfulness of
statutory violations in principle.

Extensions of Sherman and Clayton Act principles. Many other Section 5 cases are also ground-
ed, in some less direct way, in the jurisprudence of the Sherman and Clayton Acts. They involve
technical gaps in those statutes, or incipient violations of their terms, or violations of their intend-
ed underlying policies. In each such case the principles being applied from the underlying laws
are still principles of competition, and so a violation of them is likely to involve conduct that is not
competition on the merits.

External standards of business conduct. Wrongfulness may also be suggested by the violation
of other, non-antitrust standards of business conduct. These will include such external refer-
ences as deception and unfairness law from the consumer protection side of the FTC, contract
law, standards of honesty before other administrative agencies, and state business-tort law. The
legislative history of the FTC Act makes clear that Congress expected the Commission to also
refer to these kinds of sources when defining unfair methods of competition.

These external standards were not necessarily written to serve competition goals, and so a vio-
lation of them does not automatically make out a violation of Section 5. The conduct must also con-
tribute to anticompetitive results within the meaning of the FTC Act. When it does so, however, then
the fact that the conduct violates external standards will strongly suggest that it was a wrongful
form of competition.

Other. Finally, some conduct may not fit neatly into any of the previous categories but may be
found to be wrongful by reference to the underlying principle that it does not involve competition
on the merits.

Element 3: Harm to Consumers in Net Effect

The third element in finding an unfair method of competition should be that the conduct is harm-
ful to competition and consumers in its net effects. It is a showing that the conduct is harmful under
a rule of reason balancing test.

The Commission has long recognized that many business techniques produce both costs and
benefits to consumers. A merger may lessen competition but also increase productive efficiency.

49 Here again the Commission should limit itself to considering just those external standards that bear on the proper relationships among mar-
ket participants rather than looking to regulatory laws more generally.

50 Xerox Corp., 86 F.T.C. 364 (1975) (misrepresentation of dates when new products will be introduced); Cf. Complaint, Intel Corp., FTC Docket
No. 9341 (Dec. 16, 2009) (alleged intentional misrepresentation of product performance). As a matter of resource allocation, the
Commission most often uses its consumer protection authority to protect small businesses and individual persons as purchasers. The
Commission’s mission under the FTC Act is to protect the integrity of market processes for all participants, however. Larger corporations
also depend on the integrity of those processes, and Commission action may sometimes be needed to protect even those firms in their role
as purchasers.

over 200,000 service contracts, supporting a finding of consumer unfairness).


54 “[I]t will be the duty of the Commission to consult the decisions of the courts, the learning of the time, the custom of merchants, the habits
of trade, the writings of studious and thoughtful men, all of which go to make up our understanding of the words ‘unfair competition.’”
51 CONG. REC. 13,048 (statement of Sen. Alfred B. Cummins).
A vertical restraint may lessen competition within one distribution channel but enhance competition with other firms that utilize other channels. In enforcing Section 5 under this framework, the Commission should apply the statute in a way that considers all relevant costs and benefits and condemn only those practices that are harmful in their net effects.

In taking such a view here, the Commission would be consistent with the construction that has been given to “unfair acts or practices” on the consumer protection side of Section 5. The Commission has previously issued a policy statement describing the elements of a consumer unfairness violation. There the agency concluded that “the injury must not be outweighed by any offsetting consumer or competitive benefits that the sales practice also produces.” Congress subsequently concurred in that construction. It added a new Section 45(n) to the FTC Act that codifies some aspects of the consumer unfairness statement and specifies in particular that a practice cannot be found to be unfair unless it causes a substantial injury “which is . . . not outweighed by countervailing benefits to consumers or to competition.”

When efficiencies are presented as part of this analysis, the Commission should consider them to be highly relevant. They should therefore be supported by appropriate empirical evidence, when such evidence is available. The Commission should ordinarily require that the firm engaging in the challenged conduct demonstrate something beyond a theoretical possibility that efficiencies will be realized.

The small exceptions to the rule of reason only streamline and clarify the general principle. Some conduct may be condemned on a per se basis, not through the operation of Section 5, but rather through the operation of some other, underlying statute. Thus, if the Commission were to pursue a price-fixing case, applying the letter of the Sherman Act, it could apply the per se condemnation of the Sherman Act. This treatment really only reflects the judgment, based on the long experience of others as well as of the Commission, that such conduct will always or almost always be harmful in its net effects.

**A Fourth Consideration: Predictability**

Predictability is not, strictly speaking, an element in this proposed framework for defining an unfair method of competition. Congress anticipated that the Commission might have to address new forms of conduct and establish new principles of competition. It did not intend the Commission to consider itself constrained by the *de novo* nature of an action. Senator Cummins was opposed to the inclusion of criminal penalties in Section 5 precisely because it might “become[] necessary in order to preserve competition that we shall prohibit acts which have heretofore been regarded as moral, which have heretofore prevailed in every industrial society in the world.”

---

57 See N. Tex. Specialty Physicians, 140 F.T.C. 715, 719 (2005) (case applied an “inherently suspect” standard, but could have used per se theory); see also Grand Union Co. v. FTC, 300 F.2d 92, 99 (2d Cir. 1962) (when using Section 5 to fill a technical gap in the Robinson-Patman Act, the FTC should apply a per se standard if the underlying statutory provision is itself per se).
58 51 Cong. Rec. 11,539 (1914). Even the court of appeals cases that expressed concern about predictability also suggested that if the facts had more clearly shown an actual harm to competition, then the factor of predictability would not necessarily have prevented a challenge. See, e.g., Ethyl, 729 F.2d at 141 (“Perhaps this argument would be acceptable if the market were clearly as described and a causal connection could be shown between the practices and the level of prices.”).
Even if not required in every case, however, predictability is an important goal and one that the Commission should strive to advance in its actions. Fostering predictability contributes to sound governance in several ways. It assists the majority of law-abiding firms in their efforts to comply voluntarily with the law.\(^{59}\) And it recognizes that even injunctive remedies under the FTC Act can impose real costs on the firms involved, either in the form of harm to reputation or in the transactions costs involved in changing to a different mode of doing business.

Predictability should not be a problem in the great majority of Section 5 cases. The legal theories will be based on concepts and extensions drawn from the Sherman and Clayton Acts, as discussed above. Most extensions will be limited. Firms wishing to keep clear of legal issues should usually be able to do so by avoiding the kinds of conduct that might have led to Sherman Act questions.\(^{60}\) Moreover, if some non-antitrust standard, such as a business tort, is involved as well, then the conduct would be known to be wrongful even if the antitrust issue in a particular case might have been hard to anticipate.

There always remains the possibility that changing business conditions will make it advisable to challenge some form of conduct that had previously been considered legitimate and proper. The Commission can draw on several techniques in order to deal fairly with this circumstance. It may rely on the intrinsic characteristics of the challenged conduct to provide notice. If conduct tends to lead to anticompetitive coordination or exclusion and if it was undertaken without the sort of valid business purpose or efficiency benefit that might justify it in a balancing test, then firms and their counsel should generally be aware that the conduct is questionable. Or if these intrinsic characteristics seem unlikely to give fair notice with respect to a particular business practice, then the Commission may delay formal action until it has had a chance to make its views known in some other way. For example, it may give the business community advance notice of its thinking through informal avenues such as speeches, articles, and congressional testimony.

**Conclusion**

To sum up, the “unfair methods of competition” authority under Section 5 serves three broad purposes. First, it authorizes the Commission to enforce the ordinary standards of the Sherman Act. It thereby ensures that the nation’s competition agencies have broadly similar jurisdictions and apply broadly consistent laws.

Second, the unfair competition authority enables the Commission to go beyond the letter of the Sherman and Clayton Acts, and to address different or emerging forms of anticompetitive conduct that those statutes do not reach. The powers uniquely conferred by Section 5 are defined and constrained by the essential elements discussed in this policy framework. A Section 5 violation should involve a harm to competition, business conduct that is wrongfully different from competition on the merits, and a net injury to consumers. Predictability is an important additional consideration.

And third, the competition authority under Section 5 serves a central function in integrating the variety of different laws that govern how firms manage their competitive interactions. Such laws are numerous, including not only the competition statutes, but also laws on deception, consumer unfairness, contracts, and business torts. Section 5 does not impede the operation of those other statutes or needlessly duplicate their coverage. It does, however, help to fill in any gaps between

---

\(^{59}\) This factor was important in several court of appeals opinions in the 1980s. See *Ethyl*, 729 F.2d at 139, Boise Cascade Corp. v. FTC, 637 F.2d 573, 582 (9th Cir. 1980); *Official Airline Guides v. FTC*, 630 F.2d 920, 927 (2d Cir. 1980).

\(^{60}\) For example, it is only a short step from a theory of actual but tacit agreement, proved through the circumstantial evidence of conduct (Sherman Act), to a theory of parallel unilateral facilitating practices that lead to oligopoly outcomes (Section 5).
them and helps the enforcement of each to draw insights from the others. This helps move our trade laws toward a consistent vision.

The Commission's construction of its unfair competition authority should ultimately be guided by the setting of that provision within the larger context of the entire FTC Act. Procedurally, that Act provides for an administrative process that does not include either private actions or monetary damages and so the agency should construe its authority in a way that gives itself appropriate latitude as the subject-matter expert in its field. Substantively, the Act gives the Commission the overall mission of preserving a free and open market economy that provides fair opportunities for businesses and that is responsive to consumer demands. The agency should view its unfair competition authority within that broader framework and construe it so as to protect market options from any unreasonable harm, thus protecting the competitive process as a whole.
Editor’s Note: Antitrust Source Editor Allan Shampine reviews a paper by Fiona Scott Morton and Carl Shapiro on the role of patent assertion entities and their effect on competition. Send suggestions for papers to review, or comments, to page@law.ufl.edu or jwoodbury@crai.com.

Recent Papers


There has been substantial interest recently in the role of patent assertion entities (PAEs) and their effect on competition. PAEs are defined by the FTC as firms with a business model focused primarily on purchasing and asserting (“monetizing”) patents, typically against operating companies with products currently on the market.¹

The Federal Trade Commission, the Department of Justice, and the Council of Economic Advisors have recently examined PAEs through a number of studies, workshops, and an upcoming FTC Section 6(b) investigation,² which gives the agency power to conduct wide-ranging economic studies of business practices.³ While the number and activity levels of PAEs have grown enormously in recent years, there is no agreement as to whether PAEs are, on balance, pro- or anticompetitive. On the one hand, PAEs are sometimes presented as helping inventors who have patented valuable technology but are unable to exploit it themselves or who wish to locate downstream firms that have copied the technology and are not paying royalties. In this narrative, the PAE improves the functioning of the market for ideas, enhances returns to inventors, and promotes innovation by contributing specialized skills for locating infringing firms, negotiating, and litigating. On the other hand, PAEs are sometimes presented as aggregating weak patents that the original patentees were incapable or unwilling to assert and utilizing a variety of tactics to obtain royalties far in excess of any value downstream firms receive from the patent.⁴

In a recent paper, Fiona Scott Morton and Carl Shapiro develop an economic model to analyze the effects of PAEs on innovation and consumers. They describe different types of PAEs and review available evidence to determine which narrative PAEs appear to most closely fit. They find that the empirical evidence strongly indicates that additional patent monetization by PAEs is problematic from a public policy perspective.

It is the purchase and aggregation of patents that is of interest in their analysis. Entities that obtain patents through invention are not covered. Rather, the authors note that PAEs must expect to earn more from purchased patents than the sellers can achieve. A natural question is why that should be so. Such additional revenues may reflect increased market power as a result of the acquisition or aggregation, the exploitation of problems in the patent and legal systems that allow PAEs to obtain excessively high payments, and/or expertise on the part of the PAE in locating and negotiating with infringing firms. Some of these reasons are benign. Others may run afoul of antitrust laws, while still others may be legal but economically inefficient.

The authors describe three types of PAEs. “Pure” PAEs are firms with no other business interests than aggregating and asserting patents. “Hybrid” PAEs are firms that aggregate and assert patents, are not manufacturers themselves, but negotiate contractual relationships with downstream firms. Finally, some downstream firms act as PAEs by purchasing patents relevant to their industry.5

The economics of such acquisitions are relatively straightforward in a couple of instances. The economics of a downstream firm purchasing patents relevant to its industry are essentially those of a firm acquiring an input that its downstream rivals need. The potential anticompetitive effects from such a vertical merger are well understood. Recent examples of such behavior include Google’s acquisition of Motorola and its patent portfolio and the purchase of the Nortel portfolio of patents by a consortium of Apple, RIM, Microsoft, and others. Both of those transactions were permitted by regulators after the parties made commitments limiting the purchasers’ rights, including agreeing not to seek injunctive relief on standard essential patents.6 Similarly, acquisition by a firm of patents that are substitutes for other patents held by the firm is essentially a horizontal merger. That is, two firms holding patents that are substitutes compete to license those patents (i.e., to supply firms with an input of intellectual property)—combining the ownership of those patents can remove that competition in the same manner as any horizontal merger of competitors.7

The economics of pure and hybrid PAEs, however, are more complex and raise a variety of issues that may not be clearly covered by antitrust laws. The authors begin with the premise that reasonable royalties, defined as the royalties that would be negotiated between willing parties prior to infringement (also referred to as ex ante royalties), are part of a well-functioning market for ideas. However, the business model for PAEs assumes that the PAE can extract higher royalties than whatever parties the PAEs are purchasing the patents from. Why then are the PAEs able to do so and is it possible they are extracting amounts greater than reasonable royalties? The authors suggest four sets of tactics that can result in royalties in excess of reasonable royalties.

First, the authors suggest that PAEs may be especially skilled at generating “outsized threats.” In bargaining theory, the negotiated outcome is greatly influenced by each party’s outside option, or “threat point.” If one party can create an “outsized” threat—a threat well in excess of the value

---

5 Id. at 17, 18, 20.
6 Id. at 20–21.
7 Id. at 16–17.
to the user of the patented technology—then it can potentially obtain more than a reasonable royalty. One straightforward way to do so is to place a firm’s whole business at risk. This may be done through injunctions, exclusion orders, strategic timing (such as suing a firm immediately prior to an IPO or other funding event, effectively holding the IPO hostage to resolution of the lawsuit), or suing a firm’s customers.\(^8\) As all of these tactics are available to any patent holder, the potential problem appears to be that patents are being sold to a firm that is better able to exploit inefficiencies in the patent laws. That may not be socially desirable, but it is not clear that antitrust is the best avenue for addressing such a problem. It would be a very peculiar antitrust rule that a patent could only be sold to a firm that was no better a litigator than the seller. Such a rule may also raise Noerr-Pennington-type issues about restricting firms’ access to legal remedies. The authors do not identify any role for antitrust enforcement with respect to such behavior.

Second, the acquisition of patents by PAEs may be used to evade explicit or implicit contracts limiting the revenues that might be obtained from patents. A common example has to do with commitments made to standard-setting organizations (i.e., commitments to license patents on fair, reasonable, and non-discriminatory, or “FRAND,” terms). A firm acquiring such patents may argue that it is not bound by the original patent holder’s commitments. Also, firms that practice together in an industry may have an informal détente, with multiple avenues by which other firms could retaliate against a firm suing them. However, such limitations are likely not present for a PAE that has no business other than asserting patents.\(^9\)

Again, the authors do not discuss the antitrust implications of such behavior, but selling a patent from a firm with constrained pricing to a firm without constrained pricing may well have antitrust implications, depending on the nature of the constraint. For example, if a firm had contractual obligations or, because of its position in the industry was limited in its ability to monetize a patent but sold it to a firm that did not have such obligations, arguably that transaction would be creating market power and might raise antitrust concerns. Federal Trade Commissioners Rosch and Leibowitz made similar arguments with respect to the sale of Ovation Pharmaceuticals’ drug, Indocin, arguing that the selling firms’ ability to exercise market power was limited by marketplace considerations, but the purchasing firm’s ability to do so was not, and that such a sale therefore violated Section 7 of the Clayton Act.\(^10\)

Third, PAEs may obscure their precise holdings and the means by which they obtained them, making it more difficult for firms to determine whether they already hold licenses to some of the patents, or to effectively evaluate PAEs’ claims as to the importance of a portfolio. To an economist, it is very peculiar for an entity to demand royalties for a portfolio without disclosing the contents of that portfolio. As the authors note, the fact that PAEs choose not to reveal the contents of portfolios indicates that such secrecy increases the PAEs’ profits. It is difficult to see how such secrecy could be procompetitive.\(^11\)

Fourth, PAEs may use the threat of excessive damages awards to increase their bargaining leverage. Such awards may partly be a function of patent litigation generally, as the authors sug-

---

\(^8\) Id. at 6–7.

\(^9\) Id. at 7–8.


\(^11\) Scott Morton & Shapiro, supra note 4, at 8.
gest that the *Georgia Pacific*\(^{12}\) structure may be prone to producing excessive rewards. Similarly, the authors suggest that rewards in patent litigation may be biased upwards because of royalty stacking—rewards in an individual case may not consider royalties owed on other patents in the sector. That is, a royalty on a product may be “reasonable” viewed by itself, but be “unreasonable” when viewed in the context of all the other patents involved in making the product. Finally, the authors note that developing a reputation for successfully using these tactics can itself provide increased bargaining leverage.\(^{13}\)

The authors do not make clear why PAEs should be better able to take advantage of such inefficiencies (if they exist—the recent ruling in *Motorola v. Microsoft* explicitly took royalty stacking into account\(^{14}\)). However, the authors do claim that PAEs with sufficiently large portfolios can create a stacking problem by dividing the portfolio up among multiple entities.\(^{15}\)

Again, it is not clear whether this or their concern about PAEs being better able to exploit inefficiencies are problems that can or should be addressed by antitrust. On the one hand, referring to historical restrictions on champerty (the buying in of a third party into a lawsuit in exchange for a share of the proceeds) may offer some guidance here, but on the other hand, *Noerr-Pennington* considerations also come into play.\(^{16}\)

Professors Scott Morton and Shapiro develop a model to help evaluate which narrative concerning PAEs appears to best fit the industry. The model is based around a set of trade-offs. On the one hand, permitting a PAE to extract greater amounts from downstream firms is more likely to promote innovation and benefit consumers if: (1) more of that money flows to the original upstream inventor; (2) increased rewards cause upstream inventors to be more innovative; or (3) there are significant benefits (spillovers) to the downstream firms and consumers flowing from the patents. (Such spillovers only occur if there is a technology transfer from the patent holder to the downstream firm. If the downstream firm independently arrived at the innovation, there are no such benefits.) On the other hand, permitting a PAE to extract greater amounts from downstream firms than the prior patent owner is more likely to be problematic if: (1) the downstream firm reduces its own investments and innovation in response to increased payments to the PAE; (2) consumers receive significant benefits from the downstream firm’s investments and innovation; and (3) only a small share of the revenues flow through to the original patent-holder (i.e., the PAE is a leaky bucket for transferring funds to innovators).\(^{17}\)

The authors claim that very little flows through to original patent holders from PAEs relative to the costs imposed on downstream firms, that upstream inventors are generally no more responsive to changes in funding than downstream firms, and that software patents are typically not copied, so there is no technology transfer and thus no spillover benefits from the patent. In these

---

12 The *Georgia Pacific* decision set forth a number of factors that are frequently referred to when determining patent royalties, including the licensing policy of the patent holder, royalty rates on other patents, and whether the patent holder and the licensee compete with one another. Ga. Pac. Corp. v. U.S. Plywood Corp., 318 F. Supp. 1116 (1970).

13 Scott Morton & Shapiro, supra note 4, at 10.


15 Scott Morton & Shapiro, supra note 4, at 9.


17 Scott Morton & Shapiro, supra note 4, at 11-12.
circumstances, they find that the ability of PAEs to extract more from downstream firms is, on net, harmful to society.18

Although the authors find that enhanced monetization by PAEs is problematic from a social perspective, their discussion of antitrust implications is limited to the observation that efficiencies justifications for PAE transactions are relatively unlikely, that acquisition of substitute patents is effectively a horizontal merger, and that acquisition by a downstream firm (or a PAE associated with that downstream firm) of upstream patents used by rivals can raise vertical concerns, such as raising rivals’ costs. There is an undeveloped implication that a transaction resulting in higher prices to downstream firms—the sale of a patent to a PAE able to obtain higher rates from licensees—may raise antitrust concerns. As noted earlier, there is some precedent for thinking of such actions as possibly violating Section 7 of the Clayton Act, but the authors do not raise this possibility nor do they provide any specific theory or legal framework for applying antitrust to their broader concerns.

Furthermore, while PAEs may (or may not) be particularly skillful at exploiting inefficiencies in the patent and legal systems, the authors’ logic would appear to apply to most firms holding patents. That is, the particular tactics discussed by the authors are available to all firms, although some may be better at exploiting them than others. If a firm acts unilaterally to exploit such tactics, can that raise an antitrust concern, or can concerns only arise when a transfer between firms occurs?

The authors clearly identify a variety of concerns about how the patent system currently functions and persuasively argue that those concerns are of significant and growing magnitude, but it remains unclear how those concerns are best addressed. Further research might investigate the degree to which PAE activity falls into the more traditional horizontal and vertical analyses as opposed to the other inefficiencies identified by the authors, such as particular expertise in making “outsized” threats. Also, it would be useful to investigate further whether antitrust can or should play a role in addressing these other inefficiencies, and how potential patent system reforms might interact with or replace antitrust intervention.

—ALS

---

18 Id. at 13–14.