Antitrust as Regulation

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TABLE OF CONTENTS

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I. INTRODUCTION

A strange feature of the contemporary antitrust system is that one can commit a felony by pursuing a course of conduct that benefits consumers. Under the rule of reason, which is antitrust's principal mode of analysis, proof that challenged conduct is efficient is not dispositive.[1] Instead, if a plaintiff establishes that a less restrictive alternative (LRA) existed for the impugned concerted activity, then the law will condemn the same.[2] Although the LRA rule does not explicitly apply to unilateral behavior, this Article explains that the courts have silently incorporated a comparable principle into their monopolization jurisprudence. Thus, a dominant company can run afoul of antitrust rules for behavior that benefits consumers, but restricts rivals' ability to compete more than an alternative form of behavior that is more conducive to competition.[3]

The rationale underlying this tenet of the law, which the Author refers to as the welfare-maximization principle,[4] is hardly esoteric. Antitrust benefits society by spurring competition and thus promoting efficient market processes that inure to the well-being of consumers.[5] It is only natural to suppose, then, that companies should refrain from competition-

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1. *See, e.g.*, Realcomp II, Ltd. v. FTC, 635 F.3d 815, 825 (6th Cir.), *cert. denied*, 132 S. Ct. 400 (2011); Ark. Carpenters Health & Welfare Fund v. Bayer AG, 604 F.3d 98, 104 (2d Cir. 2010); Cont'l Airlines, Inc. v. United Airlines, Inc., 277 F.3d 499, 509 (4th Cir. 2002); Burlington N. Santa Fe Ry. v. Int'l Bhd. of Teamsters Local 174, 170 F.3d 897, 916 n.22 (9th Cir. 1999) (quoting Bhan v. NME Hosps., Inc., 929 F.2d 1404, 1410 n.4 (9th Cir. 1991)), *withdrawn and superseded on reh'g en banc*, 203 F.3d 703 (9th Cir. 2000); Sullivan v. NFL, 34 F.3d 1091, 1102 (1st Cir. 1994).

2. *See Realcomp II*, 635 F.3d at 825; *Bayer AG*, 604 F.3d at 104; *Cont'l Airlines*, 277 F.3d at 509; *Burlington N. Santa Fe Ry.*, 170 F.3d at 916 n.22; *Sullivan*, 34 F.3d at 1103.

3. *See infra* Part IV. This phenomenon is most prevalent in technology-based markets in which enforcement agencies wish to ensure unfettered access to channels of follow-on innovation. One can justify some such enforcement actions on the ground that equal—or at least viable—access to innovation platforms promises to yield long-run gains in the form of lower prices and flourishing technologies from competing sources. These benefits, one might argue, exceed the gains associated with adhering to a Schumpeterian understanding of innovation, which would embrace dominance and proprietary control over technology. On that view, competition law is justified in condemning a monopolist's unilateral conduct that benefits consumers because other, less restrictive forms of behavior would benefit consumers even more. *See infra* Part III.A.

4. A number of authors have defined antitrust's goal as being to maximize welfare. *See, e.g.*, Alden F. Abbott & Suzanne T. Michel, *The Right Balance of Competition Policy and Intellectual Property Law: A Perspective on Settlements of Pharmaceutical Patent Litigation*, 46 IDEA 1, 3 n.5 (2005); Howard A. Shelanski & J. Gregory Sidak, *Antitrust Divestiture in Network Industries*, 68 U. CHI. L. REV. 1, 38 (2001); Michael Sabin, Note, *Antitrust and Positional Arms Races*, 30 HARV. J.L. & PUB. POL'Y 1023, 1023 (2007). It is not clear that authors using the term intend it to suggest that courts should give the term literal application.

5. *See* Christine A. Varney, *Antitrust Immunities*, 89 OR. L. REV. 775, 777 (2011).

hindering conduct for which equally efficient but less restrictive substitutes exist.[6] So stated, the LRA rule appears to make eminent sense, as does the implicit analogue that underlies antitrust rules governing dominant-firm conduct. On this view, the law is correct to insist that companies conduct their affairs in a way that preserves viable paths of future competition for their rivals.

In fact, this aspect of the law is problematic, raising fundamental questions about the proper function of antitrust enforcement. This Article argues that the judiciary has strayed from the proper course in giving the rule of reason, along with section 2 of the Sherman Act, a more expansive role than is desirable. The premise that market-power-wielding companies should follow the most efficient, rather than simply an efficient, path is flawed. Uncritical obeisance to the goal of unbridled competition can blind courts to the truth that less can be more.[7] As antitrust enforcement grows beyond a prophylactic role in outlawing practices that are antithetical to welfare to encompass a broader mandate—maximizing welfare—it blurs the important distinction between antitrust and regulation.[8] This Article advocates for a more pronounced divide between these discrete approaches to industrial organization.

A threshold issue, however, and one that the academic literature has not explored, concerns the nature of consumer harm and its relationship to the pertinent rule of decision. One tends to think of "injury" for antitrust purposes in absolute terms, such that a practice harms consumers only if it leaves them worse off than they were before the conduct's inception. So, for example, if two competitors meet in clandestine fashion to arrest an ongoing price war between them, the ensuing agreement to stabilize price does violence to consumer interests, thus justifying antitrust condemnation.[9] By contrast, were two rivals to agree to establish a joint

6. For a representative view, see Gabriel Feldman, *The Puzzling Persistence of the Single-Entity Argument for Sports Leagues:* American Needle *and the Supreme Court's Opportunity To Reject a Flawed Defense*, 2009 WIS. L. REV. 835, 912–14.

7. *Accord* Jerry A. Hausman & J. Gregory Sidak, *Google and the Proper Antitrust Scrutiny of Orphan Books*, 5 J. COMPETITION L. & ECON. 411, 419 (2009) ([In antitrust,] "the goal of the best often seems to be an obstacle to obtaining actual improvements in economic welfare. This logical fallacy is so common in policy making that a maxim attributed to Voltaire has become a cliché in Washington to describe it: 'making the perfect the enemy of the good.'").

8. *See* Glenn B. Manishin, *No Need for Antitrust Prosecution of Google*, NAT'L L.J., July 4, 2011, at 51, 51.

9. *See, e.g.*, Christopher R. Leslie, *De Facto Detrebling: The Rush to Settlement in Antitrust Class Action Litigation*, 50 ARIZ. L. REV. 1009, 1035 (2008).

venture to share the cost and risk of developing and commercializing a new technology, the resulting new product would not harm but in fact benefit consumers, who would be better off after the venture than they were before.[10]

This account, however, is normatively incomplete. In fact, any conduct that is not the most consumer-friendly action that the company would have been willing to take in the presence of a law prohibiting its preferred course injures consumers. This insight, which is essential to understanding the problems underlying antitrust's welfare-maximization principle, is not immediately obvious because it relies on the economic concept of opportunity cost. In the joint venture example, the price of the arrangement to consumers is the foregone benefit that the best alternative agreement would have bestowed upon them. If the companies would have been willing to pursue a venture that was equally efficacious in facilitating the development of the relevant technology but less restrictive of competition, consumers would have received not only the benefit of the new product but also the gains of greater competition. As a result, many arrangements that leave consumers better off ex post than they were ex ante are in fact inimical to consumer welfare.

This counterintuitive result reveals that there is technically no such thing as a welfare-enhancing arrangement that is not also welfare maximizing. The fact of consumer benefit is not a range but a precise point. As a result, one cannot accurately say that a contract or dominant-firm practice benefits consumers without saying that the relevant conduct maximizes consumers' well-being. An antitrust regime founded on consumer welfare would technically ask, therefore, whether the challenged restraint or exclusionary practice represents the single most welfare-maximizing form of behavior that the parties would have voluntarily pursued.

A legal standard that required proof of such welfare maximization, however, would not only be unworkable, but also severely destructive of the welfare that the law seeks to promote. Courts are institutionally incompetent arbiters of critical facts that underlie the question whether a particular practice is the best one possible for consumers given the circumstances at hand. To make such a determination, one would have to quantify the unknowable future consequences of a challenged act, discount them to present value, consider in addition the static price and substitution effects of the behavior, and contrast the ensuing welfare figure with those arising in counterfactual scenarios. It is often beyond

10. *See, e.g.*, Steven C. Salop, *Question: What Is the Real and Proper Antitrust Welfare Standard? Answer: The* True *Consumer Welfare Standard*, 22 LOY. CONSUMER L. REV. 336, 352 (2010).

courts' ability to establish whether a particular agreement or unilateral practice simply effects an improvement over the status quo—omitting opportunity cost—let alone attempt to calculate the magnitude of that enhancement and compare the same to but-for states of the world in an effort to identify the optimal form of behavior.[11]

This leads to an important conclusion: A meaningful analytic distinction arises between welfare-enhancing and welfare-maximizing behavior due to error, both on the part of the courts and on the part of commercial actors that seek to predict the outcome of ex post antitrust proceedings. We do not live in a world where courts never err, where the cost of the judicial process is zero, and where ex ante legal certainty prevails. As a result, the welfare-maximization ideal should have little if any place in contemporary antitrust jurisprudence.

By omitting implicit reference to opportunity cost, the Article argues, courts would properly consider whether a particular form of behavior leaves consumers better off than if the relevant company had not acted at all. In this way, courts should ask not about perfect outcomes, but merely desirable ones. Thus, when it asserts that a practice "benefits" consumers, the Article means that consumers are better off with the practice than they would be if the actor had not acted at all. It does not mean that the conduct is the single best form of behavior that could theoretically exist. In other words, the Author's definition of consumer benefit, unless otherwise made clear, omits reference to the opportunity cost of the pertinent conduct.

Why are the LRA rule and its implicit analogue in monopolization proceedings improper? Central to the Author's thesis are the real but oft unappreciated dangers involved in requiring welfare maximization in lieu of welfare enhancement. Foremost amongst these is judicial capacity to err in constructing the requisite counterfactual that reveals whether substitute paths less inimical to competition existed.[12] Easily conceived of and applied in the few cases that are straightforward, formulating the parameters of that hypothetical world will more often be a speculative exercise in which hindsight and political predisposition

11. *See, e.g.*, Jerry A. Hausman & Gregory K. Leonard, *Efficiencies from the Consumer Viewpoint*, 7 GEO. MASON L. REV. 707, 719 (1999) ("[H]ypothetical alternatives are typically speculative and not based on a reliable analysis.").

12. *See, e.g.*, Jim Chen, *Poetic Justice*, 28 CARDOZO L. REV. 581, 594 (2006) ("[A]ll counterfactual speculation . . . belongs in the realm of fantasy.").

reign supreme.[13] What begins with a well-intentioned alteration in the law to induce superior outcomes in obvious situations can grow into something more nefarious.

How might courts err in this manner? There are two broad dangers. First, a court may pronounce a rule of decision that produces the right outcome in the case at hand but nefarious results in other settings.[14] In this respect, the precedential value of an antitrust decision that requires efficiency optimization can transcend the fact-specific environment in which it emerged to inform commercial decisionmaking in a wide variety of distinct settings. The enunciated rule may inadvertently increase the cost of an efficient course of conduct beyond a relevant actor's reservation level. A "correct" decision in one setting can therefore depress incentives to undertake desirable conduct elsewhere. This is most likely to occur when courts assume that the rewards of pursuing an LRA are sufficiently large, in light of the requisite cost and risk, that the pertinent actor would rather follow it than abandon the activity altogether.[15]

The second danger is case specific, such that courts find antitrust violations where the defendant would not have willingly pursued the LRA ex ante. Here, the probability of judicial error increases in proportion to the complexity of the given case, while the magnitude of such error increases with the social value inherent in the challenged behavior and the risk undertaken by the defendant in pursuing the same.[16] Thus, judicial efforts to maximize welfare are especially problematic in high-stakes cases, where the likelihood and cost of error are greatest.

A distinct ground of opposition to the LRA rule is its lack of a conceptual limiting principle. Literally applied, the LRA rule would eliminate the distinction between antitrust and regulation. So enforced, the law would require companies, if they act at all, to follow a single path—the socially optimum one. Any departure from the same would invite antitrust liability. The result would be a catastrophic decline in economic activity in cases where commercial actors could not identify

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13. *See, e.g.*, Christopher R. Leslie, *Rationality Analysis in Antitrust*, 158 U. PA. L. REV. 261, 308–14 (2010) (explaining that cognitive biases may afflict judicial analysis in antitrust cases).

14. One might colloquially think of this as the law of unintended consequences. *See, e.g.*, Margaret Howard, *The Law of Unintended Consequences*, 31 S. ILL. U. L.J. 451, 451 (2007).

15. Yet, because degradation in the magnitude and frequency of welfare-enhancing practices can be gradual and, almost by definition, undetectable ex post, society may remain ignorant of the suppressive effects of the LRA rule on desirable behavior.

16. *See, e.g.*, Geoffrey A. Manne & Joshua D. Wright, *Google and the Limits of Antitrust: The Case Against the Case Against Google*, 34 HARV. J.L. & PUB. POL'Y 171, 185 (2011) ("The stakes are also higher in cases involving innovation than in a regular antitrust case.").

ex ante the best possible course that courts would point to ex post.[17] In such a world, only the most prosaic arrangements between competitors would pass muster. Few if any joint ventures, mergers, and other significant multiparty arrangements would survive scrutiny.[18] The fact that antitrust law does not currently operate in this manner reveals that the courts have declined to bring the LRA test to its logical conclusion, which is not a defense but an indictment of the test itself.

The proper solution is largely to abandon the LRA rule and its analogue in section 2 cases, and thus make the legality condition precisely coterminous with whether the net but-for impact of the impugned behavior is positive. This approach is particularly important in high-risk cases where uncertainty afflicts judicial construction of the pertinent counterfactual. It would be dogmatic to argue, however, that antitrust should *never* inquire whether defendants deliberately eschewed equally effective arrangements that would have been significantly more conducive to competition. The problem lies in anchoring judicial comparison of good-versus-better outcomes to straightforward cases where the proclivity for and costs of error are low. Only in this manner can courts avoid depressing desirable activity through misplaced precedent.

As a positive matter, this Article argues that the courts have failed properly to anchor the LRA inquiry. Instead of demarcating the category of cases in which considerations of the best might feature properly, the law has allowed such considerations to become overriding and systemic. Thus the principle underlying the LRA rule has transcended the Sherman Act section 1 context to inform antitrust jurisprudence generally. This phenomenon has led courts and enforcement agencies to launch a perverse attack on innovation and welfare creation.

Contemporary examples abound. The 2011 judicial rejection of the Google Books Search Amended Settlement is the most dramatic

17. *See, e.g.*, Michael A. Carrier, *The Real Rule of Reason: Bridging the Disconnect*, 1999 BYU L. REV. 1265, 1322 (discussing the Chicago School view that "inquiries as to reasonable necessity and less restrictive alternatives could be resolved only on a case-by-case basis, with little guidance provided to businesses, future potential defendants, and antitrust courts").

18. > [I]f the critics' implicit antitrust standard were the law, then every single joint venture that charged anything for its product would be an antitrust violation because it would benefit consumer welfare even more if the joint venture offered its product for free. And if that were the law, no one would propose joint ventures that benefit consumer welfare at all.

Einer Elhauge, *Why the Google Books Settlement Is Procompetitive*, 2 J. LEGAL ANALYSIS 1, 25 (2010).

illustration,[19] but there are others. Critics have called for antitrust action against Google on a variety of other bases, including exclusive dealing, manipulating search results, and violating privacy.[20] As one commentator representative of that view observes, "The question is why not force Google to act more competitively?"[21] After all, "[w]e don't want to live in a 'winner take[s] all' economy where a strong product allows a company to pull up the ladder behind it and destroy its competitors."[22] A similar view may underlie the respective actions of the Federal Trade Commission (FTC) and European Commission against Intel for the chip manufacturer's use of exclusive-sales rebates.[23] It is equally true of antitrust challenges to Apple's exclusive-dealing practices over its iPhone product's voice and data services.[24]

This construction of antitrust law—that dominant companies must affirmatively support their fringe rivals' ability to compete effectively—adopts a perspective of antitrust that is regulatory in nature. It relies on the premise that practices accompanying a dominant firm's innovation, which unequivocally results in continuous growth in consumer welfare, are objectionable because an LRA would benefit consumers even more. The prudence of this premise depends intimately on the capacity for and cost of judicial error in ascertaining the economic effect of the allegedly exclusionary behavior. The risk and magnitude of error, however, are at their peak in the context of unilateral dominant-firm behavior, which suggests that judicial restraint would be appropriate. Yet, if one adopts the increasingly prevalent view that antitrust must facilitate unfettered access to markets, thus spurring free entry and expansion by incumbent rivals, the Sherman Act goes from being a prophylactic device aimed at protecting consumers against welfare-reducing acts to being a misplaced regulatory tool that potentially sacrifices both consumer welfare and efficiency in a misguided pursuit of more of both.

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19. Authors Guild v. Google Inc., 770 F. Supp. 2d 666, 669–70 (S.D.N.Y. 2011).

20. *See, e.g.*, Larry Dignan, *Google in the Antitrust Crosshairs*, CBS NEWS (June 23, 2011, 12:09 PM), http://www.cbsnews.com/2100-205_162-20073700.html; Juliana Gruenwald, *Critics Cheer Possible Google Antitrust Probe*, NAT'L J. TECH DAILY DOSE (June 23, 2011, 4:47 PM), http://techdailydose.nationaljournal.com/2011/06/critics-cheer-possible-google.php.

21. Nathan Newman, *The Case for Antitrust Action Against Google*, HUFFINGTON POST (Mar. 14, 2011, 7:09 PM), http://www.huffingtonpost.com/nathan-newman/the-case-for-antitrust-ac_b_835675.html.

22. *Id.*

23. *See* Commission Decision of 13 May 2009 Relating to a Proceeding Under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990—Intel) 269, *available at* http://ec.europa.eu/competition/antitrust/cases/dec_docs/37990/37990_3581_11.pdf.

24. *See In re* Apple & ATTM Antitrust Litig., No. C 07-05152 JW, 2010 WL 3521965, at *1 (N.D. Cal. July 8, 2010).

This Article explores the emergence of the LRA test, as well as its dangers, and explains how an equivalent norm underlies recent monopolization cases. The Author concludes that the law should not require business practices to maximize social welfare to pass muster under the antitrust laws. As tools of public policy directed at unilateral market behavior, antitrust and regulation have long played distinct, though complementary, roles. Natural-monopoly regulation has as its immodest goal the maximization of consumer welfare by simultaneously imposing universal service obligations and spurring the efficiencies associated with competition through the imposition of various behavioral constraints. That such regulation has widely been seen as ineffectual should in itself suggest that antitrust needs a distinct focus. Enforcement actions directed at welfare-enhancing practices improperly conflate antitrust and regulation. The consumer is likely to be the ultimate victim.

II. COMPETITION AND THE ROLE OF ANTITRUST

A. What Does Antitrust Require?

This Article argues that antitrust jurisprudence has adopted a broader-than-desirable mandate. To develop this thesis, however, it is first necessary to define the purpose of antitrust enforcement. This is because it would be impossible to articulate a defensible prescription without identifying a metric by which to inform normative conclusions.

In its purest sense, antitrust exists to keep the economy free of artificial restraints that would frustrate competition.[25] The process of competition, in turn, promises to yield a variety of overriding social benefits.[26] Market pressures lead rival manufacturers, distributors, retailers, and technological innovators to focus their efforts on increasing quality and decreasing price to attract sales from their rivals.[27] This economic process is not a zero-sum game in which price-cutting companies simply cede more wealth to consumers.[28] Instead, the effect of competition in

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25. *See, e.g.*, Neil W. Averitt & Robert H. Lande, *Using the "Consumer Choice" Approach to Antitrust Law*, 74 ANTITRUST L.J. 175, 181 (2007).

26. *See, e.g.*, Lawrence L.C. Lee, *Taiwan's Antitrust Statutes: Proposals for a Regulatory Regime and Comparison of U.S. and Taiwanese Antitrust Law*, 6 IND. INT'L & COMP. L. REV. 583, 586 (1996).

27. *See id.*

28. *See* Winton E. Williams, *Resolving the Creditor's Dilemma: An Elementary Game-Theoretic Analysis of the Causes and Cures of Counterproductive Practices in the Collection of Consumer Debt*, 48 FLA. L. REV. 607, 632 (1996) ("In the zero-sum game,

driving price toward marginal cost enhances both allocative and productive efficiency, thus increasing the amount of consumption and hence wealth in society.[29] Economies subject to high levels of competition are characterized by relatively high levels of output, innovation, and employment, as well as reduced inflation.[30]

Although society historically viewed competition as promoting ideals of distributive justice, this view has given way to a goal founded on economic efficiency.[31] Thus, although some peripheral uncertainty remains,[32] most agree that since the 1970s, antitrust law has served to protect "consumer welfare," which the law defines by reference to price theory as the difference between the aggregation of consumers' individual reservation prices and the prices that they ultimately pay.[33] A common refrain is that competition law protects consumers rather than competitors.[34]

It is widely recognized, however, that economists' model of perfect competition seldom encapsulates real-world markets, which are subject to a variety of structural and artificial impediments to competition.[35]

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the winnings of one player are the losses of another, so that the algebraic sum of the payoffs to each player always equals zero.").

29. *See* John Han, Comment, *Antitrust and Sharing Information About Product Quality*, 73 U. CHI. L. REV. 995, 997–98 (2006).

30. *See, e.g.*, Bruno Amable & Donatella Gatti, *Product Market Competition, Job Security, and Aggregate Employment*, 56 OXFORD ECON. PAPERS 667, 667–68 (2004) (U.K.); Marcin Przybyla & Moreno Roma, *Does Product Market Competition Reduce Inflation? Evidence from EU Countries and Sectors* 4–6 (Eur. Cent. Bank Working Paper Series, Working Paper No. 453, 2005), *available at* http://www.ecb.int/pub/pdf/scpwps/ecbwp453.pdf.

31. *See, e.g.*, Herbert Hovenkamp, *Distributive Justice and the Antitrust Laws*, 51 GEO. WASH. L. REV. 1 *passim* (1982).

32. *See* Richard D. Cudahy & Alan Devlin, *Anticompetitive Effect*, 95 MINN. L. REV. 59 (2010).

33. *See* George L. Priest, *The Abiding Influence of the Antitrust Paradox*, 31 HARV. J.L. & PUB. POL'Y 455, 456 (2008).

34. *See, e.g.*, Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 110 (1986) ("[T]he antitrust laws . . . were enacted for the protection of competition, not competitors." (emphasis omitted) (quoting Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 488 (1977)) (internal quotation marks omitted)). Many commentators, including this Author, however, consider that this fundamental principle of antitrust is also the one that competition enforcement agencies and courts are most prone to violate. Furthermore, some scholars have argued that antitrust should abandon the distinction between protecting competition—in other words, consumers—and competitors in new-economy markets. *See, e.g.*, Marina Lao, *Reclaiming a Role for Intent Evidence in Monopolization Analysis*, 54 AM. U. L. REV. 151, 195 (2004).

35. *See, e.g.*, Ignacio De León, *Latin American Competition Policy: From Nirvana Antitrust Policy to Reality-Based Institutional Competition Building*, 83 CHI.-KENT L. REV. 39, 62 (2008). *But cf.* RICHARD A. POSNER & FRANK H. EASTERBROOK, ANTITRUST: CASES, ECONOMIC NOTES, AND OTHER MATERIALS 165 (2d ed. 1981) ("The economic model of perfect competition was never intended as a policy prescription, and it is a basic, though extremely common, error to suppose that markets do not work efficiently if they depart from the model.").

Constraints of the former type include natural-monopoly conditions associated with high ratios of fixed to marginal costs, which often accompany strong network effects.[36] Policymakers either nationalize such industries—as was prevalent in Europe from the 1950s through the 1970s[37]—or, in the case of the United States, grant a private company a certificate of public convenience and necessity, forbid entry or exit, impose quality- and scale-of-service requirements, and regulate pricing.[38] Antitrust has a limited purview in so-called regulated industries because it can do nothing to alter their structural characteristics.

Industries that can efficiently sustain high levels of competition, however, may nevertheless be corrupted by the actions of those entities that operate within them. Private agreements to eliminate price and quality competition, whether through cartel activity or merger to monopoly, can undo the benefits of competition, and thus impose costs on society that go beyond wealth transfers from consumers to sellers.[39] Antitrust operates as a safeguard against such artificial—as distinct from structural—hindrances to competition. It does so by policing concerted and unilateral actions by market actors, both producers and consumers, ensuring that they do not corrupt free-market processes.[40]

A tentative conclusion, therefore, is that the law enforces antitrust rules to promote consumer welfare, economically defined. Two qualifications, however, are necessary. First, allocative efficiency may trump consumer surplus.[41] A tension between these two measures of welfare arises when a restraint simultaneously enhances output and transfers wealth from consumers to the seller side of the market.[42] As economists' primary objection to monopoly is the deadweight loss associated with pricing

36. *See* United Distribution Cos. v. FERC, 88 F.3d 1105, 1122 n.4 (D.C. Cir. 1996).

37. *See, e.g.*, Bob Bell, *Broadband Deregulation—Similar Legislation, Different Results: A Comparative Look at the United States and the European Union*, 10 TUL. J. TECH. & INTELL. PROP. 77, 80 (2007).

38. *See* Alexander C. Larson, *Reforming Telecommunications Policy in Response to Entry into Local Exchange Markets*, 18 HASTINGS COMM. & ENT. L.J. 1, 14 (1995).

39. *See* Thomas A. Piraino, Jr., *The Antitrust Implications of "Going Private" and Other Changes of Corporate Control*, 49 B.C. L. REV. 971, 976 (2008).

40. *See* Shubha Ghosh, *The Fable of the Commons: Exclusivity and the Construction of Intellectual Property Markets*, 40 U.C. DAVIS L. REV. 855, 887 (2007).

41. The Author uses "consumer welfare" and "consumer surplus" interchangeably.

42. The best example involves first-degree price discrimination, which results in allocative efficiency and zero consumer welfare. *See, e.g.*, Douglas M. Kochelek, *Data Mining and Antitrust*, 22 HARV. J.L. & TECH. 515, 527 (2009).

above marginal cost, conduct that increases output may be efficient and therefore desirable, even if it diminishes consumer surplus.

Second, a narrow definition of consumer welfare may be misleading in some circumstances. "Static efficiency" encapsulates the desirable conditions associated with perfect competition, describing the absence of deadweight loss where price equals marginal cost.[43] Static efficiency, which is tied to the concept of consumer surplus, is the relevant lodestar for antitrust analysis, however, only when technological progress is absent.[44] Yet, dynamic efficiency is a key determinant of social welfare.[45] Studies have linked technological innovation to three-quarters of the U.S. economy's post-World War II growth.[46] As scientific progress and commercialization of new technologies bring about dramatic increases in consumer welfare, most consider dynamic efficiency—the realization of optimal rates of innovation—to be more important than static efficiency.[47]

In this respect, the relationship between competition and innovation is complex.[48] Although the weight of the evidence suggests that there is usually a positive correlation between the two phenomena,[49] in some important circumstances—or, perhaps more accurately, within certain parameters—they may be negatively correlated.[50] Optimal innovation policy requires careful calibration of various determinants of research

43. *See* Thomas O. Barnett, *Maximizing Welfare Through Technological Innovation*, 15 GEO. MASON L. REV. 1191, 1194 (2008); *see also* Kevin C. Kennedy, *Foreign Direct Investment and Competition Policy at the World Trade Organization*, 33 GEO. WASH. INT'L L. REV. 585, 589 (2001) (describing static efficiency as the optimum utilization of resources).

44. *See* Konstantinos K. Stylianou, *An Innovation-Centric Approach of Telecommunications Infrastructure Regulation*, 16 VA. J.L. & TECH. 221, 240–41 (2011), http://www.vjolt.net/vol16/issue2/v16i2_221-Stylianou.pdf.

45. *See* Keith Bradley, *The Design of Agency Interactions*, 111 COLUM. L. REV. 745, 775 (2011) ("A proper policy should balance both static efficiency . . . and dynamic efficiency.").

46. *See* ARTI RAI ET AL., U.S. DEP'T OF COMMERCE, PATENT REFORM: UNLEASHING INNOVATION, PROMOTING ECONOMIC GROWTH & PRODUCING HIGH-PAYING JOBS 1–2 (2010), *available at* http://www.commerce.gov/sites/default/files/documents/migrated/Patent Reform-paper.pdf.

47. *See* Barnett, *supra* note 43 *passim*.

48. *See* Gregory J. Werden, *Should the Agencies Issue New Merger Guidelines?: Learning from Experience*, 16 GEO. MASON L. REV. 839, 847 n.59 (2009).

49. *See, e.g.*, Jonathan B. Baker, *Beyond Schumpeter vs. Arrow: How Antitrust Fosters Innovation*, 74 ANTITRUST L.J. 575, 583–86 (2007); Christopher R. Leslie, *Antitrust and Patent Law as Component Parts of Innovation Policy*, 34 J. CORP. L. 1259, 1265 (2009); *see also* Michael L. Katz & Howard A. Shelanski, *Mergers and Innovation*, 74 ANTITRUST L.J. 1, 17–19 (2007) (discussing competition's positive effect on innovation).

50. *See, e.g.*, Kevin Arquit, Keynote Address at the 2009 Cornell International Law Journal Symposium (Feb. 27, 2009), *in* 43 CORNELL INT'L L.J. 1, 17 (2010) ("The Chicago School instructs that monopoly profits actually spur innovation, a conclusion that the Supreme Court echoed as recently as two days ago." (citing Pac. Bell Tel. Co. v. Linkline Commc'ns, Inc., 555 U.S. 438, 454–55 (2009))).

and development (R&D) and commercialization. In some situations, cabined monopoly—such as intellectual property (IP) rights—can efficiently spur competition to acquire the same.[51] This may ultimately be beneficial to society, but any kind of exclusivity, including that created by the IP system, comes at the expense of static efficiency and hence a cabined measure of consumer welfare.[52] In this way, tensions may emerge between the promotion of static and dynamic efficiency, creating difficult issues for antitrust enforcement.[53]

It thus follows that, although consumer welfare is a rather nuanced concept, a consensus has emerged that this is the relevant metric underlying antitrust enforcement.

B. Guardian or Aggressor?: Antitrust's Mandate in Practice

A crucial ensuing question concerns the manner in which competition law purports to achieve its goal of protecting consumers. To understand antitrust, one must appreciate that it furthers consumer welfare only in a passive way. It does not operate as a regulatory system that dictates maximum prices, terms of service to clients, or obligatory actions on the part of even dominant firms.[54] Instead, the definitive characteristic of the Sherman Act is passivity.[55] The law does not instruct companies to act in a particular way ex ante; it merely imposes narrow limits—often defined ex post—on commercial actors' right to conduct their affairs in a manner that proves injurious to consumers.[56]

51. *See* Kenneth W. Dam, *The Economic Underpinnings of Patent Law*, 23 J. LEGAL STUD. 247, 250–51 (1994).

52. *See* Norman Siebrasse, *The Structure of the Law of Patentable Subject Mater*, 23 INTELL. PROP. J. 169, 178 (2011).

53. *See infra* Part III.B.

54. *See Linkline*, 555 U.S. at 452 (quoting Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004)).

55. *Cf.* Nathan B. Grzegorek, Comment, *The Price of Admission: How Inconsistent Enforcement of Antitrust Laws in America's Live Entertainment Sector Hurts the Average Consumer*, 44 J. MARSHALL L. REV. 261, 269 (2010) ("The passive nature of antitrust enforcement in recent history can attributed to the . . . 'Chicago School.'" (citing Mike J. Mandel & Mike France, *The Great Antitrust Debate: Focus on Innovation? Or Stick to Pricing Issues? The Outcome Is Critical*, BUS. WEEK, June 26, 2000, *available at* http://www.businessweek.com/2000/00_26/b3687080.htm)).

56. *See* USM Corp. v. SPS Techs., Inc., 694 F.2d 505, 513 (7th Cir. 1982) ("There is a difference between positive and negative duties, and the antitrust laws . . . have generally been understood to impose only the latter.").

So, for instance, the law prohibits horizontal competitors from entering into naked agreements not to compete on price or in particular geographic regions.[57] Similarly, two or more such companies cannot merge with one another either to form a monopoly or to effect an increase in concentration sufficient to facilitate tacit collusion.[58] Rivals may not share sensitive pricing and sales volume information, which would facilitate parallel pricing behavior.[59] Monopolists cannot engage in practices that are capable of excluding equally or more efficient rivals;[60] no company can agree with another to boycott a rival.[61]

If antitrust imposes a variety of limits on commercial behavior, the law is at least as notable for what it does not require. Antitrust does not condemn an absence of competition in a market, and thus does not require rivals to engage in price-cutting or other socially desirable behavior.[62] Competitors can lawfully engage in cartel-like behavior as long as they do so in parallel fashion, independent of any direct communication or facilitative practices.[63] The law does not condemn a monopolist for charging monopoly prices,[64] nor does it speak to the propriety of terms that a dominant company imposes on its customers or of the quality of service that the monopolist ultimately provides, which are goals that regulation better serves.[65] Thus, although antitrust promotes the interests of consumers, it does so only in a reactionary and limited manner. The law does not compel particular behavior but instead allows companies to operate freely within a large spectrum of commercial

57. *See* United States v. Trenton Potteries Co., 273 U.S. 392, 395–98 (1927); *see also* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES 24 (2010), *available at* http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf.

58. *See* HORIZONTAL MERGER GUIDELINES, *supra* note 57, at 20–27.

59. *See* United States v. Container Corp. of Am., 393 U.S. 333, 334–35, 337 (1969).

60. *See generally* Alan J. Meese, *Monopolization, Exclusion, and the Theory of the Firm*, 89 MINN. L. REV. 743 (2005) (discussing the law governing exclusionary practices by dominant firms).

61. *See* Klor's, Inc. v. Broadway-Hale Stores, Inc., 359 U.S. 207, 212–13 (1959).

62. See Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004) ("The mere possession of monopoly power, and the concomitant charging of monopoly pricing, is not only not unlawful; it is an important element of the free-market system.").

63. *See* Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 227 (1993).

64. *Id.* EU competition law is distinct from U.S. antitrust law in this respect, as Article 102 of the Treaty on the Functioning of the European Union purports to forbid the imposition by a dominant undertaking of unfair purchase or selling prices. Consolidated Version of the Treaty on the Functioning of the European Union art. 102, May 9, 2008, 2008 O.J. (C 115) 47, 89. Neither the European Commission nor the courts, however, have ever applied this provision.

65. *See* D. Daniel Sokol, *Limiting Anticompetitive Government Interventions That Benefit Special Interests*, 17 GEO. MASON L. REV. 119, 141 n.114 (2009).

conduct that does not bear an unacceptable propensity to interfere with free-market processes.[66]

This discussion, however, leaves an important question unanswered. Specifically, when circumstances call on antitrust to judge the propriety of a particular act, how does consumer well-being align with the legality condition? Of course, an act is surely improper if it injures consumers' long-term welfare, discounted to present value. What if the act, however, modestly benefits them? Does such a showing translate into a conclusive finding of legality? What if a plaintiff can demonstrate that the defendant company had a variety of substitutable paths available to it, all of which had positive effects of varying magnitude on consumer welfare? If the defendant adopted a course that produced the least benefit to consumers, should an antitrust violation follow? Should the Sherman Act require the *most* beneficial path?

In the Author's view, when courts analyze a challenged restraint to determine its status under the Sherman Act, they should not ascertain whether the practice is efficiency maximizing. They should determine only whether the impugned conduct is, in fact, efficient—welfare increasing. The law should recognize exceptions to this rule only if both the risk and cost of error in the case at hand are unusually low. In all other cases, the questions whether an act is efficient and legal should be completely synonymous. Interestingly, this would seem to be precisely what the Supreme Court instructed in its early jurisprudence.[67]

Outside the narrow purview of per se illegal behavior—horizontal price-fixing and market-sharing agreements, as well as certain boycotts—antitrust's principal mode of analysis is the rule of reason.[68] According to the Supreme Court, this form of inquiry asks only whether an objected-to practice suppresses or promotes welfare.[69] It does not make legality contingent on the extent by which the restraint exceeds the threshold of minimal efficiency.[70] As expressed by the Court, "[t]he true test of legality is whether the restraint imposed . . . promotes competition or whether it is such as may suppress or even destroy competition."[71]

66. *See* USM Corp. v. SPS Techs., Inc., 694 F.2d 505, 512–13 (7th Cir. 1982).
67. Bd. of Trade of Chi. v. United States, 246 U.S. 231, 238 (1918).
68. *See* Vincent Chiappetta, *Living with Patents: Insights from Patent Misuse*, 15 MARQ. INTELL. PROP. L. REV. 1, 9–10 (2011).
69. Nat'l Soc'y of Prof'l Eng'rs v. United States, 435 U.S. 679, 688 (1978).
70. *Id.*
71. *Bd. of Trade*, 246 U.S. at 238.

Thus, if an objected-to practice promotes competition, it should pass muster under the Sherman Act regardless of whether a modified form of the conduct would have an even better effect.

Unfortunately, the U.S. Courts of Appeals have not been faithful to the Supreme Court's seminal pronouncement. Each of them has adopted an LRA inquiry in analyzing the legality of an allegedly anticompetitive practice.[72] Furthermore, there is little uniformity among the circuits because they have adopted conflicting interpretations of the LRA rule.[73]

The D.C. Circuit requires that an antitrust defendant prove that its impugned conduct represents the "least restrictive means of achieving the desired goal."[74] This feature of the court's holding is invariant to whether the challenged restraint is conducive of efficiency or otherwise desirable to consumers.[75] The Seventh Circuit has paid homage to the LRA rule in circumstances requiring "a more flexible approach than the traditional rule of reason inquiry," instructing that should a plaintiff meet its burden of persuasion by showing that challenged conduct "restricted competition rather than promoting it, the burden of persuasion would shift to the defendants to show," amongst other things, that the goal of the conduct "could not have been adequately satisfied in a manner less restrictive of competition."[76]

The Second and Fourth Circuits apply essentially the same test, but place the burden on the plaintiff to establish that an LRA existed.[77] Less harshly, the Third and Eleventh Circuits require plaintiffs to prove that the challenged conduct was not "reasonably necessary" to accomplish the desired goal, under which standard one need not make a showing of welfare maximization.[78] The Sixth, Eighth, and Ninth Circuits propound the least draconian interpretation of the LRA rule, obligating plaintiffs to demonstrate that the defendant could have achieved the benefit of the

72. *See* Gabriel A. Feldman, *The Misuse of the Less Restrictive Alternative Inquiry in Rule of Reason Analysis*, 58 AM. U. L. REV. 561, 581–86 (2009).

73. *See generally id.* (providing a detailed discussion of the various approaches to the LRA rule adopted by the U.S. Courts of Appeals).

74. Kreuzer v. Am. Acad. of Periodontology, 735 F.2d 1479, 1496 (D.C. Cir. 1984).

75. *Id.* at 1494–95.

76. *See* Wilk v. Am. Med. Ass'n, 895 F.2d 352, 362–63 (7th Cir. 1990).

77. *See* Ark. Carpenters Health & Welfare Fund v. Bayer AG, 604 F.3d 98, 104 (2d Cir. 2010); Cont'l Airlines, Inc. v. United Airlines, Inc., 277 F.3d 499, 510–11 (4th Cir. 2002).

78. *See* Schering-Plough Corp. v. FTC, 402 F.3d 1056, 1065 (11th Cir. 2005); Am. Motor Inns, Inc. v. Holiday Inns, Inc., 521 F.2d 1230, 1248–49 (3d Cir. 1975) (quoting Walt Disney Prods. v. Am. Broad.–Paramount Theatres, 180 F. Supp. 113, 117 (S.D.N.Y. 1960)).

assailed restraint in a "substantially less restrictive manner."[79] The First and Fifth Circuits also recognize the LRA rule, but have not indicated where the burden of proof lies.[80]

How does the rule operate in practice? It finds literal application only under section 1 of the Sherman Act.[81] Under this provision, courts analyze agreements to determine their impact on competition. Contracts are, of course, indispensable to economic efficiency and ubiquitous for that reason. Few agreements raise competitive concerns. An important exception concerns arrangements between horizontal competitors, though these too can often be efficient.[82] Concerted practices between rivals are rife with competitive dangers—some of them subtle—as competitors have every incentive to collude.[83] Antitrust thus operates as a significant exception to the principle of freedom of contract that otherwise defines a free-market economy.[84] Yet the law's prohibition on concerted behavior between rivals is not absolute. Many cases arise in which restrictions on competition between direct competitors beget larger social gains. A classic example involves a partnership or company.[85] In a world where no interrival agreements are permissible, every industry would be comprised

79. *See* Care Heating & Cooling, Inc. v. Am. Standard, Inc., 427 F.3d 1008, 1012 (6th Cir. 2005) (quoting Nat'l Hockey League Players' Ass'n v. Plymouth Whalers Hockey Club, 325 F.3d 712, 718 (6th Cir. 2003)); Flegel v. Christian Hosp., Ne.-Nw., 4 F.3d 682, 688 (8th Cir. 1993) (quoting Bhan v. NME Hosps., Inc., 929 F.2d 1404, 1413 (9th Cir. 1991)); *Bhan*, 929 F.2d at 1413.

80. *See* Feldman, *supra* note 72, at 585 n.118 (citing Sullivan v. NFL, 34 F.3d 1091, 1103 (1st Cir. 1994); and Copper Liquor, Inc. v. Adolph Coors Co., 506 F.2d 934, 945 n.6 (5th Cir. 1975)).

81. *But cf.* Mark S. Popofsky, *Defining Exclusionary Conduct: Section 2, the Rule of Reason, and the Unifying Principle Underlying Antitrust Rules*, 73 ANTITRUST L.J. 435, 437 (2006) (arguing that "[a]lthough courts usually describe the rule of reason as a particular step-wise test for assessing the legality of concerted action, the rule of reason more generally provides a principle for generating antitrust liability tests in a common-law fashion" and concluding that section 2 jurisprudence incorporates a rule-of-reason test (emphasis omitted)).

82. *See* Fred S. McChesney, *Easterbrook on Errors*, 6 J. COMPETITION L. & ECON. 11, 17–18 (2010).

83. *See* James Langenfeld & Daniel R. Shulman, *The Future of U.S. Federal Antitrust Enforcement: Learning from Past and Current Influences*, 8 SEDONA CONF. J. 1, 8 (2007).

84. *See* Elizabeth I. Winston, *Why Sell What You Can License? Contracting Around Statutory Protection of Intellectual Property*, 14 GEO. MASON L. REV. 93, 132 n.183 (2006).

85. *See generally* R. H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386 (1937).

exclusively of sole traders.[86] Allowing competitors to agree not to compete for the purpose of creating a company, partnership, or other commercial collective allows the ensuing entities to achieve a far greater level of efficiency than individuals could achieve alone. Cognizant of this economic fact, antitrust permits restrictions on competition where necessary to achieve larger gains.

C. *The LRA Rule's Insidious Corruption of Antitrust Jurisprudence*

In light of the preceding discussion, it is clear that the LRA test is an established element of antitrust analysis under the rule of reason. This observation raises at least three questions. First, what are the dangers of the law's requirement that companies shape their agreements in a way to achieve more than a creditable gain in consumer welfare? Second, are these risks localized—are they limited to cases of concerted behavior—or do they threaten broader forms of commercial conduct? Third, have the theoretical dangers of requiring welfare maximization been realized?

As explained above, the LRA inquiry—though well-intentioned—is imprudent. Its error is one of both apprehension and practical consequence. In the former respect, requiring parties to fine-tune their contractual arrangements to maximize welfare is an object of regulation, rather than competition law.[87] Furthermore, it may not be feasible to cabin an LRA-based conception of antitrust to simple cases in which companies can reliably demarcate permissible forms of conduct ex ante. More complex cases invite mistaken determinations about the nature of the but-for world in which courts determine that particular defendants would have entered into superior arrangements.[88]

Importantly, and as Part IV explains, the LRA rule is not unique to cases of concerted behavior. It has transcended the rule of reason—

86. One modern industry that is composed entirely of individuals is the barrister profession in Ireland. For the Author's discussion of this particular feature of the industry, see Alan Devlin, *Questioning the Sole-Trader Rule in the Barrister Profession*, 44 IRISH JURIST 123 (2010) (Ir.).

87. *Cf.* Stacey L. Dogan & Mark A. Lemley, *Antitrust Law and Regulatory Gaming*, 87 TEX. L. REV. 685, 695 n.52 (2009) ("Of course, antitrust and regulation take different approaches to achieving their common goal, but both ultimately aim to maximize efficiency in markets."); Mark D. Whitener, Editor's Note, *Change.gov*, ANTITRUST, Summer 2009, at 4 ("New Deputy AAG for Economics Carl Shapiro recently noted that while some describe antitrust as a form of 'government regulation,' antitrust 'is a fundamentally different exercise' . . . .").

88. *See, e.g.*, Thomas A. Piraino, Jr., *A New Approach to the Antitrust Analysis of Mergers*, 83 B.U. L. REV. 785, 798 (2003) (opining that the requirement that defendants prove that efficiencies are merger specific "allows judges, juries, and antitrust regulators to second-guess defendants' business judgment and substitute speculation on hypothetical 'less restrictive' alternatives").

pursuant to which it explicitly applies—and has percolated throughout antitrust law to corrupt judicial and agency understanding of optimal competition policy more generally.[89] The danger is most pronounced, the Article submits, with respect to innovation-induced dominance. This is the field in which both judicial capacity to err and the social cost of the same are greatest.[90] As a result, it is in this setting that a focus on welfare maximization is most harmful. Part III addresses the relationship between antitrust and innovation, exploring the difficult questions of public policy that underlie the same.[91] This discussion reveals why monopolization cases in innovation markets are uniquely susceptible to erroneous judicial fact-finding. Part IV applies this discussion to recent enforcement actions, explaining that the LRA rule's subtle transmogrification in the field of dominant-firm conduct bears unique dangers that are only now becoming clear.

III. ANTITRUST, INNOVATION, AND WELFARE MAXIMIZATION

This Article explains that antitrust has adopted a well-intentioned but ultimately destructive prescription aimed at engineering welfare-maximizing outcomes. This Part observes that the economic literature addressing the relationship between innovation policy and antitrust oversight of dominant-firm behavior is indeterminate. As a result, courts are uniquely susceptible to err in determining whether an alleged act of predatory exclusion realizes a net gain or loss for consumers. Part III.B explains that moving the goal line beyond a showing of a net increase in

89. This migration is, for reasons explained below, unwelcome, but nonetheless unsurprising, for the nature of antitrust analysis is substantially similar under sections 1 and 2 of the Sherman Act, which address concerted and unilateral behavior, respectively. *See* United States v. Microsoft Corp., 253 F.3d 34, 59 (D.C. Cir. 2001) ("[I]t is clear that the analysis under section 2 is similar to that under section 1 regardless whether the rule of reason label is applied . . . ." (quoting Mid-Texas Commc'ns Sys., Inc. v. AT&T, 615 F.2d 1372, 1389 n.13 (5th Cir. 1980))).

90. *See, e.g.*, David L. Meyer, *Section 2 Standards and Consumer Welfare: Some Lessons from the World of Merger Enforcement*, 2007 COLUM. BUS. L. REV. 371, 409 ("In the Section 2 setting, there is much greater ambiguity: often the short run effects and long run effects will diverge, and even if adverse price or quantity effects are expected, it is much harder to judge whether they were caused by 'bad' behavior or good. Hinging the Section 2 outcome solely on an inquiry about net consumer welfare effects might end up begging a whole series of other, harder questions.").

91. For a representative discussion of some of the policy issues arising at the intersection of innovation policy and antitrust, see J. Gregory Sidak & David J. Teece, *Dynamic Competition in Antitrust Law*, 5 J. COMPETITION L. & ECON. 581 (2009).

welfare narrows the permissible range of desirable behavior, thus gravely compounding the courts' proclivity to commit Type I errors.[92] The cost of false positives, moreover, is especially grave in technology markets, given the inestimable social benefits of innovation.[93]

To be sure, economic theory and empirical investigation have yielded a variety of useful normative conclusions concerning innovation and the market conditions that best foster it. Certain features of an effective innovation platform are clear. These include high levels of education,[94] stable legal systems that enforce contractual and other rights,[95] favorable bankruptcy laws that permit risky but socially desirable entrepreneurial endeavors and enable people with ideas to pursue further projects if their initial ventures fail,[96] employment laws that facilitate the creation and efficient movement of human capital,[97] efficient capital markets that produce venture capital for worthy projects,[98] a proper tax policy,[99] an appropriate level of public-sector spending that does not crowd out private investment,[100] consumer protection laws that ensure the dissemination of accurate information into the marketplace,[101] and immigration laws that allow companies to hire foreigners with specialized training where domestic

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92. For an explanation of Type I and Type II errors, see *infra* note 244 and accompanying text.

93. *See, e.g.*, Gaia Bernstein, *In the Shadow of Innovation*, 31 CARDOZO L. REV. 2257 *passim* (2010).

94. *See, e.g.*, Andrew Jaynes, *Why Intellectual Property Rights Infringement Remains Entrenched in the Philippines*, 21 PACE INT'L L. REV. 55, 107 (2009).

95. *See, e.g.*, Pauline Newman, *The Federal Circuit: Judicial Stability or Judicial Activism?*, 42 AM. U. L. REV. 683, 687 (1993).

96. *See* Daniel H. Cole, *Climate Change, Adaptation, and Development*, 26 UCLA J. ENVTL. L. & POL'Y 1, 8 (2008) (citing DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE, AND ECONOMIC PERFORMANCE 80–82 (1990)).

97. For instance, some have attributed Silicon Valley's considerable success to California's refusal to recognize noncompete agreements. *See, e.g.*, Norman D. Bishara, *Covenants Not To Compete in a Knowledge Economy: Balancing Innovation from Employee Mobility Against Legal Protection from Employee Mobility Against Legal Protection for Human Capital Investment*, 27 BERKELEY J. EMP. & LAB. L. 287, 307–08 (2006). This aspect of California law means that employers in need of highly skilled employees can readily acquire them by offering superior compensation packages. *See id.*

98. *See, e.g.*, Philip J. Weiser, *Innovation, Entrepreneurship, and the Information Age*, 9 J. ON TELECOMM. & HIGH TECH. L. 1, 2–3 (2011).

99. *See, e.g.*, Matthew A. Melone, *The Patenting of Tax Strategies: A Patently Unnecessary Development*, 5 DEPAUL BUS. & COM. L.J. 437, 439 n.5 (2007) (citing I.R.C. §§ 41, 45(c), 174 (2006)).

100. *See, e.g.*, Evan N. Turgeon, *Triple-Dividends: Toward Pigovian Gasoline Taxation*, 30 J. LAND RESOURCES & ENVTL. L. 145, 168 (2010).

101. *See, e.g.*, Mark D. Bauer, *The Licensed Professional Exemption in Consumer Protection: At Odds with Antitrust History and Precedent*, 73 TENN. L. REV. 131, 133 n.15 (2006) (quoting FED. TRADE COMM'N, PERFORMANCE & ACCOUNTABILITY REPORT: FISCAL YEAR 2003, at i (2004), *available at* http://www.ftc.gov/opp/gpra/2003pareport.pdf).

labor supply proves inadequate.[102] Beyond these factors, intellectual property and antitrust laws play a crucial economic role in spurring innovation.[103] Unfortunately, the specific antitrust policies that best promote technological advancement are far from clear.[104]

At its most fundamental, the proper relationship between innovation and antitrust depends on the question whether conditions of monopoly or competition are most likely to spur desirable rates of R&D.[105] After briefly exploring the literature that has addressed this question—and observing that no clear principle of general application has emerged—this Part explores recent calls that antitrust affirmatively require the best. The Author opines that the commentators making such demands do so because they are hostile to concentrated industry structures. Unfortunately, competitive high-technology markets can display just such traits.

A. The Schumpeter-Arrow Debate

Perhaps the single most famous debate in antitrust concerns the question whether competitive or concentrated industries are superior incubators of innovation.[106] In the latter direction, Joseph Schumpeter argued that monopoly is the best driver of invention because the large profits associated with above-marginal-cost pricing produce surplus

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102. *See, e.g.*, *Competitiveness and Innovation on the Committee's 50th Anniversary with Bill Gates, Chairman of Microsoft: Hearing Before the H. Comm. on Sci. & Tech.*, 110th Cong. 18–20 (2008) (statement of William H. Gates, Chairman, Microsoft; Co-Chair, Bill and Melinda Gates Foundation); Kim Hart, *Gates Calls on Congress for Science Education, Visas*, WASH. POST, Mar. 13, 2008, at D3.

103. *See, e.g.*, Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 146 (1989); Weiser, *supra* note 98, at 13; *see also* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION 1–3 (2007), *available at* http://www.justice.gov/atr/public/hearings/ip/222655.pdf.

104. The ultimate issue, from an antitrust perspective, is whether competition rules can force innovation-based monopolists to operate in a manner less injurious to rivals and hence more beneficial to consumers. This basic question dovetails with the debate as to whether the LRA inquiry underlying the rule of reason is well-founded.

105. *See, e.g.*, Mark A. Lemley, *A New Balance Between IP and Antitrust*, 13 SW. J.L. & TRADE AMS. 237 *passim* (2007).

106. *Compare, e.g.*, Richard J. Gilbert & Steven C. Sunshine, *Incorporating Dynamic Efficiency Concerns in Merger Analysis: The Use of Innovation Markets*, 63 ANTITRUST L.J. 569, 570 (1994) (discussing the positive effects of competition on innovation), *with* WILLIAM L. BALDWIN & JOHN T. SCOTT, MARKET STRUCTURE AND TECHNOLOGICAL CHANGE (1987) (exploring how dominant firms foster innovation).

funds for research and development.[107] Furthermore, he maintained, dominant companies have incentives to invest private capital because their installed client base and scale efficiencies lessen the chance that fringe rivals can appropriate the value of any successful inventions.[108] According to Schumpeter, highly competitive markets that involve low profit margins are not apt to foster high levels of innovation.[109] Thus, monopoly may provide a "more stable platform" for R&D investment.[110]

Broadly speaking, the Schumpeterian view counsels a laissez-faire approach to antitrust policy with respect to dominant-firm unilateral behavior.[111] If competition rules force monopolists to license their physical and intellectual infrastructure, or otherwise create conditions that are inimical to high concentration and conducive to entry and rival expansion, the result may be lower prices and higher output, but reduced rates of innovation. Assuming that policymakers wish to promote dynamic over static innovation,[112] interventionist antitrust policy aimed at fostering competition in monopolized markets may have undesirable results.

Kenneth Arrow rejected the view that monopoly is most conducive to R&D and argued that competition best spurs innovation.[113] He explained that dominant firms have relatively weak incentives to research groundbreaking technologies because they face a high opportunity cost in doing so.[114] More specifically, because monopolists earn monopoly profits on the basis of then-existing technology, their spending significant amounts of those profits to realize a new marketable technology may simply displace one profit base for another.[115] This phenomenon is known as the "replacement effect," which renders an invention less profitable than it would otherwise be.[116]

By contrast, a company subject to competition has more to gain by achieving a breakthrough discovery because it will experience a significant

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107. *See* JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY 87–106 (1st ed. 1942).

108. *Id.* at 96.

109. *Id.*

110. Richard Gilbert, *Looking for Mr. Schumpeter: Where Are We in the Competition-Innovation Debate?*, *in* 6 INNOVATION POLICY AND THE ECONOMY 159, 160 (Adam B. Jaffe et al., eds., 2006) (citing SCHUMPETER, *supra* note 107).

111. *See, e.g.*, Raymond Shih Ray Ku, *Grokking* Grokster, 2005 WIS. L. REV. 1217, 1278.

112. The economic literature makes increasingly clear that dynamic efficiency is indeed more important. *See, e.g.*, Sidak & Teece, *supra* note 91, at 582–85.

113. Kenneth J. Arrow, *Economic Welfare and the Allocation of Resources for Invention*, *in* THE RATE AND DIRECTION OF INVENTIVE ACTIVITY: ECONOMIC AND SOCIAL FACTORS 609 (1962).

114. *Id.* at 622.

115. *Id.*

116. *See* JEAN TIROLE, THE THEORY OF INDUSTRIAL ORGANIZATION 392 (1988).

increase in demand, thus taking profitable sales opportunities from its rivals.[117] Arrow showed that for a drastic innovation—one for which the monopoly price is lower than the previous technology's marginal cost—the reward from developing a novel process is the same for both a monopolist and a previously competitive firm, but that the monopolist faces a larger replacement effect.[118] Thus, the firm subject to competition faces a stronger incentive to invent.[119]

The Schumpeter-Arrow debate has generated a considerable body of empirical and theoretic work but few determinative answers.[120] Arrow's model concerned innovation in technological methods, which are apt to diminish a company's marginal costs.[121] The model did not address product innovations, which arguably represent a sphere of invention that is more important to the economy. As an improvement product is less likely to render an old product defunct, however, a monopolist's invention of the former may allow it to price discriminate and hence achieve greater profitability. As a result, and although a competitive firm's replacement cost is likely to be less, a monopolist may have a greater incentive to invent a novel product.[122] Even if a product invention is sufficiently revolutionary as to constitute a drastic invention, as per Arrow's definition, a competitive firm will not necessarily have the greater incentive to invent unless the discovery is so significant that the monopolist cannot use it for price discrimination purposes.[123]

An authoritative 2006 synopsis of the economic literature concluded that the evidence "does not support a conclusion that large firms promote innovation because they provide large and stable cash flows, economies of scale (above some threshold), or risk diversification. . . . At the same

117. Arrow, *supra* note 113, at 620.
118. *Id.* at 621.
119. *Id.*
120. *See, e.g.*, Michael A. Carrier, *Two Puzzles Resolved: Of the Schumpeter-Arrow Stalemate and Pharmaceutical Innovation Markets*, 93 IOWA L. REV. 393, 396 (2008) ("One of the most heated discussions in economic circles in recent years has concerned the relationship between market structure and innovation. After a half-century of debate and innumerable studies, the overwhelming consensus is that there is no clear answer to the question. The diametrically opposed positions of Joseph Schumpeter (favoring concentration) and Kenneth Arrow (favoring competition) both garner support in unending bouts of hand-wringing.").
121. *See* Gilbert & Sunshine, *supra* note 106, at 575 n.22.
122. *See* Shane Greenstein & Garey Ramey, *Market Structure, Innovation, and Vertical Product Differentiation*, 16 INT'L J. INDUS. ORG. 285, 294 (1997).
123. *See* Gilbert, *supra* note 110, at 168.

time, neither theory nor empirical evidence supports a strong conclusion that competition is uniformly a stimulus to innovation."[124] It thus follows that economic models do not lend themselves to an unqualified policy prescription.[125]

Complicating matters further is the question of how to best interpret Arrow and Schumpeterian views from an antitrust perspective. In the first place, it may be a mistake to overemphasize the practical importance of the replacement effect. This phenomenon is apt to be serious only where a dominant company actually enjoys a secure position that fringe rivals or other potential competitors do not threaten.[126] In fact, monopoly positions in technology markets are less secure than one might suppose, even in the presence of network effects.[127] Thus, even dominant companies need to continue innovating to maintain their positions. Furthermore, the fact of monopoly is consistent with Arrow's model, which relied on exclusive rights over one's innovation.[128] Enforcing open standards,

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124. *Id.* at 205–06.

125. Nevertheless, there is some support for the hypothesis that dominant companies innovate differently than those in competitive markets, which may have some relevance to antitrust policy. Monopolists, unconstrained by competitors, are more likely to innovate in a steady, incremental manner, while technological companies subject to fierce competition are more apt to realize dramatic technological breakthroughs in a "lumpy" manner. *See* Alexander E. Silverman, *Intellectual Property Law and the Venture Capital Process*, 5 HIGH TECH. L.J. 157, 169 (1990). *But see* Michael J. Meurer, *Inventors, Entrepreneurs, and Intellectual Property Law*, 45 HOUS. L. REV. 1201, 1210–13 (2008) (exploring the economic theory and empirical evidence surrounding invention and innovation by small and large companies, finding them to be inconclusive). In this respect, academics sometimes use AT&T prior to its breakup on antitrust grounds as the quintessential example against which to judge the innovation associated with small companies, such as start-ups in technology markets. *See, e.g.*, Kristine Laudadio Devine, *Preserving Competition in Multi-Sided Innovative Markets: How Do You Solve a Problem Like Google?*, 10 N.C. J.L. & TECH. 59, 104 n.187 (2008) ("Additional competition may not affect the investment in R&D; companies like AT&T were widely known to have deep investments in innovations, even though many of those innovations never made it to consumers."); John E. Lopatka & William H. Page, *Internet Regulation and Consumer Welfare: Innovation, Speculation, and Cable Bundling*, 52 HASTINGS L.J. 891, 917 (2001); Richard A. Posner, *The Decline and Fall of AT&T: A Personal Recollection*, 61 FED. COMM. L.J. 11, 18 (2008) ("AT&T did a lot of innovation, but they wanted every new thing to be introduced gradually, they wanted uniformity not variety, single not multiple products, and they didn't want customers buffeting them with demands."); *see also* Dan L. Burk & Mark A. Lemley, *Policy Levers in Patent Law*, 89 VA. L. REV. 1575, 1619 (2003) (observing scholarly commentary that contrasts the nonproprietary nature of the Internet that allowed innovation to flourish in the 1990s with "AT&T, which had a monopoly in telephony . . . [and] did not engage in similar innovation").

126. *See* Devine, *supra* note 125, at 104.

127. *See* Richard A. Posner, *Antitrust in the New Economy*, 68 ANTITRUST L.J. 925, 930 (2000) ("Because of the extraordinary pace of innovation, . . . the extraordinary amount of capital that is available worldwide for investment in new enterprises, and the rapidity with which new networks . . . can be put into service, the networks that have emerged in the new economy do not seem particularly secure against competition.").

128. Arrow, *supra* note 113, at 619.

thus eschewing legal recognition of proprietary rights in information, would lead to suboptimal innovation on account of insufficient incentives to invent.[129] In this respect, a policy that sought to maximize competition—literally defined—would run directly counter to Arrow's view.[130] It would myopically substitute technological competition in R&D for price-based competition.

The relevant normative prescription is therefore more subtle.[131] One advancing Arrow's view of fostering innovation would respect intellectual property rights even if they produced monopoly conditions in some circumstances, but would presumably adopt a variety of policies aimed at ensuring that the inventor obtaining such dominance would not use its position to quash actual or potential competition. In this respect, an inventor would not have the right to control follow-on paths of technological research, to use its dominant position to fetter rivals' attempts to research and commercialize new generations of products, or otherwise to appropriate value that goes beyond the nature of the claimed invention itself. In contrast, a Schumpeterian approach might be more willing to allow a dominant company to enjoy the fruits of that position because, one subscribing to that view would argue, an absence of immediate competition over future avenues of R&D would not do violence to long-term innovation. Empirical and theoretical investigations of these alternative approaches, however, have failed to yield a robust policy prescription.

As the dynamics of innovation are both complex and context specific, and because general principles are elusive,[132] it is difficult to determine whether a particular form of dominant-firm behavior enhances or depresses consumer welfare. It is for this reason, in addition to the immeasurability of

129. As noted above, the heterogeneity of industrial innovation means that conditions that are favorable to innovation in one setting may not be in others. It is undoubtedly true that nonproprietary standards may spur greater levels of desirable innovation than closed ones in certain circumstances. The classic example involves the early history of the Internet. *See generally* BARBARA VAN SCHEWICK, INTERNET ARCHITECTURE AND INNOVATION (2010) (providing an overview of how open standards led to rapid innovation in the Internet context).

130. *See* Sidak & Teece, *supra* note 91, at 588 ("Arrow sets aside the appropriability problem (that is, how to capture value from innovation) and posits a perfect property right in the information underlying a specific production technique.").

131. *See id. passim*.

132. *See* F.M. Scherer, *Antitrust, Efficiency, and Progress*, 62 N.Y.U. L. REV. 998, 1011 (1987) ("Although there are fairly simple and well-accepted generalizations as to which market structures stimulate the most rapid pace of innovation, the question of what progress rate is socially optimal, and . . . which market structure driving it is best, is extremely complex and poorly settled.").

long-term effects, that judicial decisionmaking in the section 2 context is highly error prone.

B. Controversy and Competition in the New Economy

Critics have recently assailed the idea that antitrust should have a limited purview.[133] Such commentators would presumably take umbrage at this Author's assertion that, other than in straightforward cases concerning concerted behavior, antitrust has no business requiring that companies tailor their conduct to maximize consumer welfare.[134]

Why would observers criticize this position when the economics concerning optimal industry structures for promoting innovation are indeterminate, and when courts have exceedingly limited ability to gauge the welfare effects of a dominant-firm practice? The answer, this Author submits, is because critics rely on political predispositions hostile to concentrated industry structure when analyzing uncertain market phenomena.[135] It is interesting to observe, then, that revolutionary technological breakthroughs are likely to yield dominant positions. Technology markets have displayed a historical tendency to begin with rapid innovation based on open standards, to progress to increased industry concentration and proprietary control, and from there, often to conditions in which a single company achieves a dominant position.[136] There is, however, a tendency for competition-induced displacement of incumbent monopolists to occur.[137] This reality sits uneasily with those who are favorably predisposed to open technologies, interoperability, low market concentration, and high degrees of price competition.[138] Although some such commentators might acknowledge that agreements or dominant-firm practices implicating new technologies inure to the benefit of consumers, they would argue that antitrust intervention focused

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133. *See, e.g.*, Newman, *supra* note 21 (asserting Google's lack of competition could result in decreased pressures to make better products); Editorial, *Did the Microsoft Case Change the World?*, N.Y. TIMES, May 15, 2011, at WK 7 ("The European Commission is deciding whether Google abused its search dominance, and American authorities are considering an investigation. We support these efforts. Innovation needs competition."); Editorial, *Google's Book Deal: A Universal Library Is a Great Idea, but Not if the Price Is a Monopoly*, N.Y. TIMES, Mar. 31, 2011, at A26.

134. *But cf.* Kochelek, *supra* note 42, at 529 (describing the view that antitrust should concern itself with maximizing consumer welfare).

135. For the Author's broader discussion of this phenomenon, see Alan Devlin & Michael Jacobs, *Antitrust Divergence and the Limits of Economics*, 104 NW. U. L. REV. 253 (2010).

136. *See generally* TIM WU, THE MASTER SWITCH: THE RISE AND FALL OF INFORMATION EMPIRES (2010) (describing how innovative technologies that encourage general use generally fall into the hands of concentrated, dominant companies).

137. *See, e.g.*, Posner, *supra* note 127, at 929–30.

138. *See, e.g.*, WU, *supra* note 136, at 5–12.

on facilitating greater levels of competition would advantage consumers even more.

Recent examples of overwhelming commercial success based on innovation abound. Facebook and Google provide good examples, though of course, few technology companies have achieved such dramatic gains as Apple, which over the last two years has overtaken the operating system giant, Microsoft, in terms of stock market value, revenue, and profitability with a series of profound innovations.[139] Perhaps the clearest recent example of innovation-yielding monopoly is the Google Books Search (GBS) project, which the Author explores in the next Part.[140]

In all of these cases, critics have called on antitrust to restore competition and to deny dominant companies control over the markets in which they operate. No one protests more vituperatively than successful innovators' competitors.[141] Apple's rivals condemned the company's

139. *See, e.g.*, Miguel Helft & Ashlee Vance, *Apple Is No. 1 in Tech, Overtaking Microsoft*, N.Y. TIMES, May 27, 2010, at B1. Apple's notable market-changing products include its iTunes program, which solved the vexing dilemma of designing a product that would be commercially viable in light of wholesale piracy in the online distribution of music and video, its wildly popular iPhone and iPad products, and its Mac computers. All of these innovations have bestowed Apple with considerable market power, which has in turn invited a series of antitrust actions. *See* Matt McMurrer, Note, *Exclusive Gadget:* Apple & AT&T Antitrust Litigation *and the iPhone Aftermarkets*, 36 J. CORP. L. 495, 496 (2011); Thomas Catan & Nathan Koppel, *Regulators Eye Apple Anew: Enforcers Interested in Whether Digital-Subscription Rules Stifle Competition*, WALL ST. J., Feb. 18, 2011, at B1; Josh Kosman, *An Antitrust App: Apple May Be in the Eye of Regulatory Storm*, N.Y. POST, May 3, 2010, at 31, *available at* 2010 WLNR 9151101; Jeffrey Shinder & Ankur Kapoor, *Will Apple iCloud Bring an Antitrust Litigation Storm?*, FORBES (June 20, 2011, 5:14 PM), http://blogs.forbes.com/ciocentral/2011/06/10/will-apple-icloud-bring-an-antitrust-litigation-storm/.

140. As explained below, the Internet search giant risked massive copyright infringement, developed and utilized groundbreaking scanning technology, and spent hundreds of millions of dollars attempting to make digital copies of every book in the world. *See infra* Part IV.A.1. When Google sought to settle an ensuing copyright class action on terms that would grant the company control over in-copyright works whose authors could not be found—orphan works—and rights over other copyright-protected books whose authors did not opt out, a firestorm of protest resulted. *See infra* Part IV.A.2. Much of the condemnation emanated from the perceived fact that Google, but none of its competitors, would have access to the scanned universe of books, thus providing the company with a secure dominant position. *See infra* Part IV.A.2. Other important examples include Google's Internet search algorithm and Intel's sales practices with respect to cutting-edge computer chips. *See infra* text accompanying notes 259–64.

141. *See, e.g.*, Steve Lohr, *Antitrust Cry from Microsoft*, N.Y. TIMES, Mar. 31, 2011, at B1; Gabriele Steinhauser & Michael Liedtke, *Microsoft Skewers Google in EU Antitrust Complaint*, AP WORLDSTREAM, Mar. 31, 2011, *available at* WL 3/31/11 APWORLD 23:40:45.

exclusive contracts and restrictions on application developers, contending that these practices limited their ability to compete.[142] Amazon, Microsoft, and Yahoo all vilified the GBS project in various colorful terms.[143] Such protest invites a more aggressive form of antitrust intervention—one that may seek affirmatively to regulate the manner in which successful inventors commercialize their inventions and chart future paths of innovation. The question whether such antimonopolization lawsuits are desirable from the standpoint of achieving positive increments in consumer welfare is difficult to answer. As the Author explains below, however, aiming for a greater goal—welfare maximization—has potentially dangerous repercussions. Specifically, taking an ideal form of behavior as a requisite of antitrust legality necessarily expands courts' capacity to make Type I errors, with negative consequences for public policy.

IV. AN ANTITRUST OWN GOAL: THE LAW'S INADVERTENT ASSAULT ON CONSUMER WELFARE

This Article explores the nature of the consumer welfare gain necessary to avert a Sherman Act violation. The U.S. Courts of Appeals have given antitrust's primary mode of analysis, the rule of reason, a broader reading than the U.S. Supreme Court, requiring to varying degrees that a challenged restraint accomplish more than a net increment in consumer welfare.[144] As explained above, this aspect of the law bears nefarious potential and rests awkwardly with antitrust's discrete role within industrial organization policy.[145] More worryingly, however, the welfare-maximization principle has transcended the section 1 context in which it arose to silently embrace section 2 jurisprudence.

This progression is particularly dangerous when applied to monopolization cases founded on innovation. Part III addressed the complex and potentially sensitive economic factors that drive technological progress in the new economy. No broad principles of general application have emerged as

142. *See, e.g.*, Nicola F. Sharpe & Olufunmilayo B. Arewa, *Is Apple Playing Fair? Navigating the iPod FairPlay DRM Controversy*, 5 NW. J. TECH. & INTELL. PROP. 332 *passim* (2007), *available at* http://scholarlycommons.law.northwestern.edu/njtip/vol5/iss2/5/.

143. *See* Objection of Amazon.com, Inc., to Proposed Settlement at 19–20, Authors Guild v. Google Inc., 770 F. Supp. 2d 666 (S.D.N.Y. 2011) (No. 05 CV 8136-DC), 2009 WL 4888799; Objections of Microsoft Corp. to Proposed Settlement & Certification of Proposed Settlement Class and Sub-Classes at 1, *Authors Guild*, 770 F. Supp. 2d 666 (No. 05 CV 8136-DC), 2009 WL 2980742; Objection of Yahoo! Inc. to Final Approval of the Proposed Class Action Settlement at 24, *Authors Guild*, 770 F. Supp. 2d 666 (No. 05 CV 8136-DC), 2009 WL 2980749.

144. See, for example, the application of the rule of reason in the cases cited *supra* note 1.

145. *See supra* Part II.B–C.

to the relative merits of closed monopoly and open competition in spurring optimal R&D, yet the proliferation of IP-protected breakthrough innovations has recently produced a series of dominant positions. In all cases, however, a showing that the impugned exclusionary act promotes long-run welfare discounted to present value should be determinative of its legality.

Why not push for more? The answer is because the immeasurable and unobservable counterfactual, which is crucial to LRA analysis, introduces a systemic risk of judicial error that becomes increasingly unacceptable as the stakes and risks of any given case rise. The monopolization context is uniquely problematic in this regard.

To require more from a firm than that its conduct promote welfare is to introduce a perilous degree of risk. A welfare-maximization principle exacerbates the likelihood of error by narrowing the band of legality within the spectrum of behavior that actually promotes welfare. A policy that requires more than a positive increment in aggregate welfare in the section 2 environment would have to assume that economic theory can identify the welfare-maximizing limit on unilateral conduct or, at an absolute minimum, distinguish between trivial and significant contributions to net welfare. Economics can accomplish neither such task in this setting. Economists have difficulty even determining whether a particular act of vertical integration or other potentially exclusionary behavior is beneficial or detrimental to consumers.[146] To suppose that economics could offer more, enabling judges and juries to demarcate the optimal modes of unilateral behavior, is nothing more than a flight of fancy.[147]

More recent events, however, suggest that the LRA principle has infiltrated the domain of unilateral behavior. As the Author now

146. *Compare, e.g.*, Richard A. Posner, *Vertical Restraints and Antitrust Policy*, 72 U. CHI. L. REV. 229 *passim* (2005) (discussing economic virtues and low anticompetitive consequences of most vertical integration), *with* Joseph F. Brodley, *Post-Chicago Economics and Workable Legal Policy*, 63 ANTITRUST L.J. 683, 683 (1994) (advocating antitrust policy that limits vertical integration). *See generally* IIIB PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW 8–30 (3d ed. 2008) (discussing the economics of vertical integration).

147. *See, e.g.*, David J. Gerber, *Convergence in the Treatment of Dominant Firm Conduct: The United States, the European Union, and the Institutional Embeddedness of Economics*, 76 ANTITRUST L.J. 951, 953 (2010) ("[U]nilateral conduct . . . is the area of antitrust law where the role of economics is most contested . . . [and] presents economics with particularly complex and uncertain issues of prognosis and analysis."). On the limits of economic analysis in antitrust assessment of dominant-firm conduct, see Devlin & Jacobs, *supra* note 135.

demonstrates, the past year's events have brought the theoretical dangers of welfare maximization to fruition. We have reached a point at which the courts have affirmatively harmed consumers in the name of antitrust enforcement.

A. The GBS Project and Antitrust's Consumer Welfare Standard

There is no better example of antitrust's scoring an own goal on account of its efforts to maximize welfare than the debacle involving the GBS project. If one credits the view that competition law should permit welfare-enhancing conduct, the case for antitrust condemnation of the GBS settlement agreement, already amended to assuage concerns, was weak. Although monopolization cases typically involve grave uncertainty as to whether the net effect of the challenged practice is positive or negative,[148] there was no debate that the GBS settlement, if authorized by the court, would realize vast gains in consumer welfare.[149] The only conceivable antitrust objection to the proposed settlement was that although it was desirable, it did not represent the most favorable arrangement that the litigating parties could have realized. Judge Chin of the Second Circuit Court of Appeals, sitting by designation on the U.S. District Court for the Southern District of New York, found that competition concerns weighed against his approving the settlement[150]—a result that makes sense only in light of a welfare-maximization lodestar.

Before explaining the nature of the district court's perverse antitrust ruling, it is necessary to explore both the issues implicated by the GBS project and the material provisions of the rejected settlement agreement.

1. The Backdrop

Collecting every significant piece of writing in existence and placing it all under one roof is a dream that has eluded mankind since the destruction of the Great Library of Alexandria two millennia ago.[151] Given the exponential growth in the volume of written works over time,

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148. *See supra* note 147 and accompanying text.

149. *See* Elhauge, *supra* note 18, at 5 ("A holding that . . . [the] settlement violates antitrust law . . . [would] condemn[] us all to zero output of these books and an effective price of infinity for new copies of them. . . . Even if the critics are right that no Google rival could overcome the barriers to entry in a similar way, a market with one competitor is better than a market with none, because it increases market options and output from nothing to something, thus improving consumer welfare."); *see also* Hausman & Sidak, *supra* note 7, at 437–38.

150. Authors Guild v. Google Inc., 770 F. Supp. 2d 666, 682–83, 686 (S.D.N.Y. 2011).

151. *See* Kevin Kelly, *Scan This Book!*, N.Y. TIMES (May 14, 2006), http://www.nytimes.com/2006/05/14/magazine/14publishing.html?pagewanted=all.

aggregating all of the world's books and articles has long been desirable, though infeasible.[152] Even if it had been practically achievable, the scale of the compiled information would frustrate efforts to synthesize and index it in a manner conducive to effective searching.[153] Yet with the advent of the digital age, organizing the world's information became a real and achievable possibility.[154] By scanning works, making their contents available online, and formulating increasingly sophisticated search algorithms, society could at last have all of the world's information at its fingertips.[155] The long-term educational, scientific, cultural, and commercial ramifications would be immeasurable.

Yet, the fact that technological advance makes such a marvelous outcome possible does not make it inevitable. To translate the potential of the Internet and digital technology into reality, one must overcome a variety of intimidating obstacles. First amongst them is the fact of intellectual property. Copyright laws, which have steadily and controversially expanded in recent decades, allow authors and their assigns to lay claim to a vast array of written work.[156] Creating a digital copy of the entirety, or even a subset, of a book necessarily constitutes a copyright violation absent fair use protection.[157] The law on fair use, however, is ill defined on this question, and so one wishing to copy the world's books without committing what could turn out to be the most massive copyright infringement in history must obtain permission.[158] This leads to a second, albeit related, problem of identification and negotiation costs. Simply tracking down and bargaining with each copyright holder is preclusively difficult, time-consuming, and expensive—factors that should but may not spur a court to find that fair use applies.[159] The third problem—a

152. *See, e.g.*, Mary Murrell, *Digital + Library: Mass Book Digitization as Collective Inquiry*, 55 N.Y.L. SCH. L. REV. 221, 226–27 (2010).

153. See *id.* at 226–32.

154. *See, e.g.*, *id.* at 232–36.

155. *See, e.g.*, *id.*

156. *See* 17 U.S.C. §§ 101–106 (2006 & Supp. IV 2011).

157. *See, e.g.*, Elisabeth Hanratty, *Google Library: Beyond Fair Use?*, 2005 DUKE L. & TECH. REV. 10, ¶¶ 4–7, http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=1130&context=dltr.

158. *See, e.g.*, Guy Pessach, *Museums, Digitization and Copyright Law: Taking Stock and Looking Ahead*, 1 J. INT'L MEDIA & ENT. L. 253, 269–70 (2007). *See generally* Mark A. Lemley, *Should a Licensing Market Require Licensing?*, 70 L. & CONTEMP. PROBS. 185, 185–86 (2007) ("Because fair use relies upon a vague, multi-factor test, it is often impossible to know ex ante whether any particular use will qualify as fair.").

159. *See, e.g.*, Thomas F. Cotter, *Fair Use and Copyright Overenforcement*, 93 IOWA L. REV. 1271, 1277 (2008).

serious one—concerns the mechanics of scanning almost 130 million books[160] within a lifetime.

Combined, these impediments would seem likely to dissuade any rational private enterprise from pursuing this goal in its pure form. A more limited undertaking, which might involve scanning only those books that are readily identifiable and lie in the public domain, would presumably be more attractive for sufficiently well-capitalized and driven companies. Yet, the result of even a successful operation to collect, scan, and make searchable out-of-copyright books would be a relatively impoverished collection that lacks much contemporary work.[161] From a public policy standpoint—or at least one founded on utilitarianism—this leaves much to be desired. Furthermore, even such a limited undertaking would involve considerable risks, as recent history reveals. Microsoft tried and failed to create a digital library through the so-called Live Search Books project, which it abandoned in May 2008.[162] It did not try to engage in unauthorized scanning.[163] The Open Content Alliance, which Microsoft contributed to prior to abandoning its own scanning project, continues.[164]

Given the legal and practical difficulties, creating a searchable online database comprising all of the world's writings, including those that are in copyright, seems a task better suited to government resolution, especially in light of the IP issues that seem deserving of legislative action.[165] Yet there is an immediate problem in relying on government to effect such a monumental innovation, for bureaucratic regimes are rarely viewed as incubators of bold, visionary, and entrepreneurial technological progress.[166]

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160. *See* Leonid Taycher, *Books of the World, Stand Up and Be Counted! All 129,864,880 of You*, GOOGLE BOOKS SEARCH (Aug. 5, 2010, 8:26 AM), http://booksearch.blogspot.com/2010/08/books-of-world-stand-up-and-be-counted.html.

161. It is well-established that most books lose their commercial value before the copyright on them expires. *See, e.g.*, Eldred v. Ashcroft, 537 U.S. 186, 268 (2003) (app. to opinion of Breyer, J., dissenting). For a discussion of the respective limits and advantages of the public domain, see Pamela Samuelson, *Mapping the Digital Public Domain: Threats and Opportunities*, 66 L. & CONTEMP. PROBS. 147 (2003).

162. *See* Satya Nadella, *Book Search Winding Down*, BING SEARCH BLOG (May 23, 2008, 2:45 AM), http://www.bing.com/community/blogs/search/archive/2008/05/23/book-search-winding-down.aspx.

163. *See* Steven Hetcher, *The Half-Fairness of Google's Plan To Make the World's Collection of Books Searchable*, 13 MICH. TELECOMM. & TECH. L. REV. 1, 6 (2006).

164. *See About: What Is the Open Content Alliance?*, OPEN CONTENT ALLIANCE, http://www.opencontentalliance.org/about/ (last visited July 28, 2012).

165. *See, e.g.*, Claire Cain Miller, *Book Ruling Cuts Options for Google*, N.Y. TIMES, Mar. 24, 2011, at B1.

166. *See, e.g.*, JOHN D. DONAHUE, THE PRIVATIZATION DECISION: PUBLIC ENDS, PRIVATE MEANS 140–42 (1989); Ronald J. Gilson & Curtis J. Milhaupt, *Sovereign Wealth Funds and Corporate Governance: A Minimalist Response to the New Mercantilism*, 60 STAN. L. REV. 1345, 1369 (2008); Nancy J. Knauer, *Reinventing Government: The Promise of Institutional Choice and Government Created Charitable Organizations*, 41

Enter Google, which has never been a company of small ambitions. In 2002, cofounder Larry Page embarked on a series of trips to learn about modest-scale digitization projects already under way, including at the University of Michigan.[167] There, he heard that the university expected to finish scanning its library's collection of seven million volumes in one thousand years.[168] He told the university's president that Google could do it in six.[169] Partnerships with the universities of Oxford, Harvard, Stanford, and Michigan, as well as the New York Public Library, soon followed.[170]

The company's efforts proved explosively controversial.[171] No one disputed that Google was making complete digital copies of vast numbers of in-copyright books. In an effort to qualify for fair use protection, Google ensured that users of the service could only see "snippets" of IP-protected books.[172] This was not enough to avoid the wrath of the publishing industry, as both the Authors Guild of America (the Authors Guild) and the Association of American Publishers (AAP) brought lawsuits, alleging "massive copyright infringement."[173] Google countered on fair use grounds, arguing that digitizing books and maintaining copies of those books was no different in principle than copying and indexing

N.Y.L. SCH. L. REV. 945, 948–49 (1997); *see also* Christopher A. Padilla, Ass't Sec'y of Commerce for Exp. Admin., Remarks at the American Conference Institute Export Control Conference: The Future of Export Controls (May 15, 2007), *available at* http://www.bis.doc.gov/news/2007/padilla05152007.htm (describing challenges the U.S. government faces in adapting to rapidly evolving technology).

167. *About Google Books: History of Google Books*, GOOGLE, http://www.google.com/googlebooks/history.html (last visited July 28, 2012).

168. *Id.*

169. *Id.*

170. *Id.*

171. *See, e.g.*, Jan Timothy Williams, *The Pre-Amended Google Books Settlement, International Orphan Works, and German Copyright Law: An Analysis*, 19 U. MIAMI BUS. L. REV. 51, 64 (2011). For a representative objection, see Miguel Helft & Motoko Rich, *Lawyer and Author Adds His Objections to Settling the Google Book Lawsuit*, N.Y. TIMES, Aug. 19, 2009, at B2.

172. *See, e.g.*, Pamela Samuelson, *The Google Book Settlement as Copyright Reform*, 2011 WIS. L. REV. 479, 488; Kathleen E. Kubis, Note, *Google Books: Page by Page, Click by Click, Users Are Reading Away Privacy Rights*, 13 VAND. J. ENT. & TECH. L. 217, 223 (2010).

173. *See* Press Release, Authors Guild, Authors Guild Sues Google, Citing "Massive Copyright Infringement" (Sept. 20, 2005), *available at* http://www.authorsguild.org/advocacy/articles/authorsguildsuesgooglecitingmassivecopyrightinfringement.html; Press Release, Ass'n of Am. Publishers, Publishers Sue Google Over Plans To Digitize Copyrighted Books: Google Print Library Violates Publishers' and Authors' Rights (Oct. 19, 2005), *available at* http://www.publishers.org/press/46/.

websites.[174] It also pointed out that it only made out-of-copyright copies available for unabridged viewing online.[175] Google had to vie with the fact, however, that its copying of the works was commercial and likely nontransformative, such that at trial it would likely have had to prove a lack of market harm to rightsholders to prevail on fair use.

In an act of ingenuity befitting its reputation, Google entered into a settlement agreement with the Authors Guild and AAP that put in place a framework that would not only compensate copyright holders through a sophisticated royalty system but would also allow Google to make all copyright-protected works both searchable and purchasable online, including "orphan works"—books by authors who cannot be found.[176] Part of the genius of the agreement is that it would have made those orphan works available for the first time to the consuming public.[177] At present, no company can produce copies of such books without risking subsequent copyright infringement should the rightsholders ever assert their IP. As the next subpart explains, however, the settlement agreement proved to be immensely divisive.

2. The Settlement Agreement and Ensuing Controversy

The original 2008 agreement encompassed all in-copyright works—excluding periodicals, music, personal papers, and public domain and government works—published before January 5, 2009.[178] It required Google to pay the class members $45 million in compensation for its prior unauthorized digitization but authorized the company to continue copying books, sell institutional subscriptions to the searchable electronic GBS database, sell online access to individual works, and employ so-called access uses.[179] The arrangement also required Google to give $34.5 million to establish and maintain a "Registry" that would act on behalf of the rightsholders by locating rightsholders, as well as collecting and distributing royalties to them.[180] Class members would have received sixty-three percent of the revenues earned from the GBS service, but

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174. Answer, Jury Demand, and Affirmative Defenses of Defendant Google Inc., Authors Guild v. Google Inc., 770 F. Supp. 2d 666 (S.D.N.Y. 2011) (No. 05 CV 8136-DC), 2005 WL 3309666.

175. *See, e.g.*, Eric Schmidt, Op-Ed., *Books of Revelation*, WALL ST. J., Oct. 18, 2005, at A18.

176. *See* Amended Settlement Agreement, *Authors Guild*, 770 F. Supp. 2d 666 (No. 05 CV 8136-DC), *available at* http://www.googlebooksettlement.com/agreement.html.

177. *See, e.g.*, Elhauge, *supra* note 18, at 17.

178. *See* Settlement Agreement § 1.16, *Authors Guild*, 770 F. Supp. 2d. 666 (No. 05 CV 8136-DC), *available at* http://static.googleusercontent.com/external_content/untrusted_dlcp/books.google.com/en/us/booksrightsholders/Settlement-Agreement.pdf.

179. *Id.* § 2.1(a)–(b).

180. *Id.* §§ 2.1(c), 6.1–6.7.

could remove their books from the database or request that Google not copy the same.[181]

The settlement agreement drew an important distinction between "commercially available" and unavailable works, as well as between in-print and out-of-print books.[182] A book was commercially available and presumptively in-print if the rightsholder made the book available for sale in the United States and not commercially available otherwise.[183] The distinction concerned the uses in which the agreement authorized Google to engage. The agreement permitted Google to engage only in "display uses" for books that were not commercially available—the company could engage in such uses for an available or in-print work only with the relevant rightsholder's permission.[184] It granted Google permission to engage in display uses for out-of-print works unless the pertinent rightsholders requested otherwise.[185]

The arrangement defined display uses as access and preview uses, as well as snippet displays.[186] In contrast, access uses involve viewing, annotating, printing, and copying and pasting portions of the relevant book.[187] The agreement permitted individual consumers to pay for online access to the works and allowed educational, government, and corporate institutions to purchase time-limited subscriptions to the same.[188] Rightsholders could either set the sale price of their works themselves or avail of a default pricing formula that sought to maximize revenues for sales of the books.[189] The agreement also stated that Google would provide, upon request, a free public access service for a computer terminal at each public library.[190] Preview uses, as a default, allowed consumers to view up to twenty percent of a work before making a purchase decision.[191] In yielding results to a user's search, Google could display approximately four lines of text—a snippet—from a work.[192]

181. *Id.* § 2.1(a).
182. *Id.* §§ 1.28, 3.2(d)(ii).
183. *Id.* § 1.28.
184. *Id.* §§ 1.48, 3.2(e)(i).
185. *Id.* § 3.2(d)(ii).
186. *Id.* § 1.48.
187. *Id.* §§ 1.1, 4.1(d), 4.2(a).
188. *Id.* §§ 1.74, 4.1(e).
189. *Id.* § 4.2(b)(iii), (c)(i).
190. *Id.* § 4.8(a)(i)(1).
191. *Id.* § 4.3(b)(1).
192. *Id.* § 1.147.

The agreement also provided for a "Research Corpus" containing digital copies of all scanned books made available for "non-consumptive research."[193] The parties agreed, however, to limit access to "qualified users,"[194] a definition that Google's competitors do not clearly meet.[195]

Criticism was swift and biting, focusing in particular on the perceived fact that the settlement would bestow on Google a de facto monopoly over orphan works.[196] Chicago antitrust expert Randal Picker provided what was perhaps the leading academic expression of this view.[197] He also opined that the pricing algorithm could amount to an illegal joint-pricing mechanism between horizontal competitors, namely, rightsholders.[198] The director of Harvard University Library decried the settlement on the ground that it "provides no assurance that the prices charged for access will be reasonable . . . especially since the subscription services will have no real competitors."[199] Berkeley scholar Pamela Samuelson condemned the settlement for providing Google exclusive rights over orphan works, surmising that "[i]f asked, the authors of orphan books in major research libraries might well prefer for their books to be available under Creative Commons licenses or put in the public domain so that fellow researchers could have greater access to them."[200] The Internet Archive protested that the settlement provided Google alone immunity from copyright infringement for digitization of in-copyright books, thus preventing any other entity, itself included, from "provid[ing] some of these same services due to the uncertain legal issues surrounding orphan

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193. *Id.* §§ 1.130, 7.2(b)(vi).

194. *Id.* § 7.2(b)(vi).

195. *See, e.g.*, Randal C. Picker, *The Google Book Search Settlement: A New Orphan-Works Monopoly?*, 5 J. COMPETITION L. & ECON. 383, 395 (2009).

196. *See, e.g.*, Robert Darnton, *A Digital Library Better than Google's*, N.Y. TIMES, Mar. 24, 2011, at A31 (quoting Authors Guild v. Google Inc., 770 F. Supp. 2d 666, 682 (S.D.N.Y. 2011)).

197. *See generally* Picker, *supra* note 195 (concluding that the settlement gave Google unique access to orphan works).

198. *Id.* at 390, 398.

199. Laura G. Mirviss, *Harvard-Google Online Book Deal at Risk*, HARV. CRIMSON (Oct. 30, 2008), http://www.thecrimson.com/article/2008/10/30/harvard-google-online-book-deal-at-risk/. Conversely, Michigan's Paul Courant, despite noting that the arrangement transformed Google's original universal digital library into a bookstore, welcomed the settlement on the ground that it facilitated far quicker widespread consumer access to in-copyright books, as negotiating with each copyright holder directly would have taken many years. Paul Courant, *The Google Settlement – From the Universal Library to the Universal Bookstore*, AU COURANT (Oct. 28, 2008), http://paulcourant.net/2008/10/28/the-google-settlement-from-the-universal-library-to-the-universal-bookstore/.

200. *See* Pamela Samuelson, *Legally Speaking: The Dead Souls of the Google Booksearch Settlement*, O'REILLY RADAR (Apr. 17, 2009), http://radar.oreilly.com/2009/04/legally-speaking-the-dead-soul.html.

books."[201] Virginia professor Siva Vaidhyanathan, despite professing sympathy "to the claim that something is better than nothing and sooner is better than later," criticized the settlement in light of "just how great an alternative system could be, if everyone would just mount a long-term, global campaign for it rather than settle for the quick fix."[202]

In November 2009, Google, the Authors Guild, and the AAP entered into an amended settlement, which differed in a number of material ways from the 2008 agreement.[203] First, the revised agreement did not encapsulate foreign works, save those published in the United Kingdom, Australia, and Canada.[204] Second, it granted rightsholders the ability to negotiate different revenue shares and permitted Google to engage in price discounting.[205] Third, it clarified that rightsholders can make their works freely available or license them under Creative Commons or other licensing conditions.[206] Fourth, it jettisoned the most-favored-nation clause that would have required the Book Rights Registry to offer Google terms at least equally favorable as those that it would offer third parties.[207] Perhaps most significantly, the new arrangement did not allow the parties to benefit from orphan work royalties, but instead created a trust that would hold the payments, use part of the money to fund the rightsholder search process, and ultimately distribute the revenue *cy pres* if the rightsholders were never identified.[208] Last, but certainly not least, the revised settlement agreement modified the pricing algorithm that the Book Rights Registry would use in calculating a price for each book to simulate pricing in a competitive market.[209] This was in distinction to

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201. Letter from Hadrian R. Katz, Attorney for the Internet Archive, Arnold & Porter LLP, to Hon. Denny Chin, U.S. Dist. Court for the S. Dist. of N.Y. (Apr. 17, 2009), *available at* http://www.scribd.com/doc/14308286/Internet-Archive-Intervention-Google-Book-Search; *see also* Memorandum of Amicus Curiae the Internet Archive in Opposition to Amended Settlement Agreement, Authors Guild v. Google Inc., 770 F. Supp. 2d 666 (S.D.N.Y. 2011) (No. 05 CV 08136-DC), 2010 WL 451142.

202. Siva Vaidhyanathan, *My Initial Take on the Google-Publishers Settlement*, GOOGLIZATION EVERYTHING (Oct. 28, 2008), http://www.googlizationofeverything.com/2008/10/my_initial_take_on_the_googlep.php.

203. *See* Amended Settlement Agreement, *supra* note 176.

204. *Id.* § 10.2(h).

205. *Id.* § 4.5(a)(iii), (b).

206. *Id.* § 4.2(a)(i).

207. *Id.* § 2.1; *see also* Yuan Ji, Comment, *Why the Google Book Search Settlement Should Be Approved: A Response to Antitrust Concerns and Suggestions for Regulation*, 21 ALB. L.J. SCI. & TECH. 231, 245 (2011).

208. Amended Settlement Agreement, *supra* note 176, § 6.3(a)(ii)(3).

209. *Id.* § 4.2(c)(ii)(2).

the original agreement, which entailed an algorithm that would calculate price to maximize revenue for the rightsholders—a provision that some commentators viewed as potentially enabling price collusion among competing copyright holders.[210]

These significant changes, however, failed to arrest the controversy. To the surprise of the Author, the Justice Department filed an amicus brief, urging the district court not to approve the settlement.[211] The government argued that the revised agreement still bestowed on Google a monopoly over orphan works, and purported to grant rights on the parties beyond those at issue in the underlying lawsuit.[212]

3. The Court's Opinion

In a surprisingly terse opinion, the U.S. District Court for the Southern District of New York rejected the amended settlement agreement, based in large part on its concern that the arrangement granted proprietary rights over orphan works.[213] The court viewed such an outcome with consternation, believing that it would improperly award Google for copying books without permission while denying its competitors rights to the in-copyright books for which the rightsholders could be found.[214] It expressed profound skepticism about the virtue of permitting private parties to effect such an arrangement in lieu of legislative action, opining that "the establishment of a mechanism for exploiting unclaimed books is a matter more suited for Congress than this Court."[215] The fact that the settlement proposed to address a variety of issues not implicated by the issues presented by the lawsuit similarly concerned Judge Chin.[216] He concluded, however, that the parties would assuage his concerns if they revised the agreement such that it would only encapsulate the works of those rightsholders who affirmatively opt in.[217]

Antitrust concerns contributed to the district court's decision not to approve the settlement agreement:

> The United States, Amazon, and Microsoft, among others, raise a number of antitrust concerns presented by the ASA.

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210. *See* Picker, *supra* note 195, at 385.

211. Statement of Interest of the United States of America Regarding Proposed Amended Settlement Agreement, Authors Guild v. Google Inc., 770 F. Supp. 2d 666 (S.D.N.Y. 2011) (No. 05 CV 8136-DC), 2010 WL 979111.

212. *See id.* at 3–4; *see also* Miguel Helft, *Justice Dept. Criticizes Latest Google Book Deal*, N.Y. TIMES, Feb. 5, 2010, at B2.

213. *Authors Guild*, 770 F. Supp. 2d at 682, 686.

214. *Id.* at 678–79.

215. *Id.* at 677.

216. *Id.*

217. *Id.* at 686.

> The ASA would give Google a de facto monopoly over unclaimed works. Only Google has engaged in the copying of books en masse without copyright permission. As the United States observed in its original statement of interest:
>
> > This de facto exclusivity (at least as to orphan works) appears to create a dangerous probability that only Google would have the ability to market to libraries and other institutions a comprehensive digital-book subscription. The seller of an incomplete database—*i.e.*, one that does not include the millions of orphan works—cannot compete effectively with the seller of a comprehensive product.
> >
> > And as counsel for the Internet Archive noted, the ASA would give Google "a right, which no one else in the world would have, . . . to digitize works with impunity, without any risk of statutory liability, for something like 150 years."
>
> The ASA would arguably give Google control over the search market. The ASA would permit third parties to display snippets from books scanned by Google, but only if they "have entered into agreements with Google." Likewise, the ASA would permit third parties to "index and search" scanned books only if they are non-commercial entities or they otherwise have Google's prior written consent. The ASA would broadly bar "direct, for profit, commercial use of information extracted from Books in the Research Corpus" except with the express permission of the Registry *and* Google. Google's ability to deny competitors the ability to search orphan books would further entrench Google's market power in the online search market. . . . (*See* Mem. of Internet Archive in Opp'n to ASA 3–4, ECF No. 811 ("Internet Archive Mem.") ("Google would have the right to make complete copies of orphan works and use them for both display and non-display purposes, with no risk of copyright liability. Competitors that attempted to do the same thing, however, would face exposure to statutory damages.")).[218]

These antitrust concerns upon which the district court relied possess an intuitive quality but are misplaced. One could conclude otherwise only if one adopts the norm criticized throughout this Article that antitrust requires the best.

4. The Perversities of the Welfare-Maximization Principle

Vexing policy questions pervade the GBS arrangement. Is it acceptable that a single dominant company should enjoy exclusive proprietary control over orphan works, the owners of which have not issued licenses to reproduce and distribute the same? Would Google engage in price gouging with respect to institutional subscribers that lack alternatives, or would reputational and other constraints keep the cost of GBS reasonable? If the court approved the settlement, would Google's exclusive ability to

218. *Id.* at 682–83 (citations omitted).

sell access to orphan works endure? Would it be feasible for third parties to follow Google's footsteps and create a rival digital library? Is it appropriate, let alone desirable, that the agreement would leave unanswered the crucially important legal question at issue in the GBS lawsuit—does wholesale digital copying of entire works and making snippets of the same available online without permission from the relevant rightsholders qualify for protection under copyright's fair use doctrine? Would the continuing absence of legal certainty and the potentially catastrophic damages that would accompany a finding of copyright infringement foreclose the emergence of viable substitute services? If competitive entry is feasible, is it even desirable? May it be that the cost of digitization is such that Google's digital library is an "essential resource" that would be inefficient to duplicate, in which case the digital library of works is a natural monopoly deserving of regulation? Could Google even be an inadvertent victim of collective monopoly on the part of rightsholders who, acting collectively, yield power over the GBS service?

These and related questions have been the subject of intense debate within the academic community and beyond. More striking than these questions' complexity, however, is their utter irrelevance from an antitrust standpoint. Understanding why they are, in fact, immaterial is central to appreciating the fact of and reasons for antitrust's discrete function.

No universal digital library predated the GBS project, nor did that project foreclose or otherwise hinder the private or public development of a rival database.[219] Orphan works, by definition, are unavailable to the consuming public absent the arrangement.[220] It follows that, even if critics' worst fears about the settlement were well-founded—such that Google would set monopoly prices and no rival service would likely emerge—the GBS service constitutes a very significant addition to consumer welfare. That alone should be enough to satisfy the antitrust laws.[221]

219. To the contrary, Google's efforts revealed valuable information to third-party observers, thus reducing the cost to competitors of following suit. *See* Hausman & Sidak, *supra* note 7, at 429–32. Criticism that the settlement left the fair use question unaddressed, thus foreclosing viable entry, is an argument as to why Google's risk-filled project did not reveal even more information to competitors than it did.

220. *See* Alessandra Glorioso, Note, *Google Books: An Orphan Works Solution?*, 38 HOFSTRA L. REV. 971, 988 (2010).

221. Academics opposed to the arrangement assume that antitrust requires more than an increase in consumer welfare. *See, e.g.*, Picker, *supra* note 195, at 408; Pamela Samuelson, *Google Books Is Not a Library*, HUFFINGTON POST (Oct. 13, 2009, 12:38 PM), http://www.huffingtonpost.com/pamela-samuelson/google-books-is-not-a-lib_b_317518.html (objecting that "Google will have a de facto monopoly on out-of-print books" and observing that "[l]ibraries everywhere are terrified that Google will engage in price-gouging when setting prices for institutional subscriptions to GBS contents").

Of course, courts could require more, thus presumably rendering consumers even better off. As explained above, however, this is a dangerous policy because courts are vulnerable to misreading the relevant counterfactual.[222] It is all too easy, with the benefit of hindsight, to underestimate the cost and risk that an innovator undertook in pursuing new technologies, and thus mistakenly assume that the inventor would have been willing to undertake an alternative, even more desirable course ex ante. Google tells this story well—economists have estimated that the company spent up to $100 million digitizing books and took an enormous risk in exposing itself to potentially incalculable damages in the event of established copyright infringement.[223] That a private company would undertake such a risk-filled path in pursuit of an innovative, social-welfare-enhancing goal is a wonderful testament to the U.S. capitalist system. A responsible innovation policy would work to foster incentives conducive to such socially valuable risk taking.

What folly it is, then, to second-guess such an innovator after the fact and assume that the company would have been willing to undertake its trailblazing course of digitization had it known that the courts would not have allowed it to enter into a settlement agreement that encompassed orphan works. The U.S. District Court for the Southern District of New York, however, adopted precisely the wrong perspective—it supposed that legislative action was the only appropriate avenue by which to make orphan works commercially available.[224] To say that Congress has been a lumbering mule when it comes to envisioning, let alone realizing, the full potential of digitization and universal libraries would be kind.[225] To envision a superior world in which the legislative branch acted with the foresight and ingenuity of private enterprise in a fast-growing innovation market is one thing. To appeal to such a hypothetical world as

222. *See supra* notes 14–16 and accompanying text.

223. *See* Hausman & Sidak, *supra* note 7, at 412 (citing David Chen, *Google's Book Search Library Project Faces Legal Challenges*, ILL. BUS. L.J. (Nov. 21, 2007), http://www.law.illinois.edu/bljournal/post/2007/11/21/Googles-Book-Search-Library-Project-Faces-Copyright-Challenges.aspx).

224. Authors Guild v. Google Inc., 770 F. Supp. 2d 666, 677 (S.D.N.Y. 2011).

225. Congress has started a digitization project, but it does not approach the scale—and hence the value—of the GBS project. *See, e.g.*, Katie Hafner, *Google Gift to Digital Library*, N.Y. TIMES, Nov. 22, 2005, at C6, *available at* 2005 WLNR 18838068 ("Long on ambition, but short on the necessary funds, the Library of Congress has increasingly turned to the private sector for underwriting its digitization projects.").

justification for fettering a real-life, second-best alternative, however, as the district court did, is public policy of the most shortsighted kind.

The most striking perversity of the GBS case, however, lay in the district court's insistence on a course that *negatively* impacts consumer welfare. Judge Chin made it clear that he would approve a further amendment to the settlement agreement to include as class members only those rightsholders who affirmatively opt in.[226] That ruling will without a doubt significantly reduce the number of books included within the GBS and will by definition exclude every orphan work. This largely defeats the purpose of the GBS project and comes at the direct expense of consumers. Rarely does one witness a court employing a rule of law dedicated to advancing the interests of consumers to effect a significant hurt upon them. The ruling presumably reflects a rights-based conception of copyright that operates, in this instance, in opposition to utilitarian concerns.

To clarify, utilitarian considerations do not warrant stripping copyright holders of their exclusive rights even if they stubbornly refuse to commercialize or license their IP in a manner that would benefit the larger world. Few doubt that copyright law, unlike antitrust, displays prominent features of a rights-based system.[227] In this respect, the fact that the GBS service would enhance social welfare by scanning and making available copyrighted works against the wishes of rightsholders would not justify the copyright violation. This does not mean, however, that courts should be blind to consequential public policy concerns in determining the fact of consent. It is dogmatic to suppose that a copyright holder can only give consent by affirmatively expressing the same, such that passive acquiescence does not qualify. In the Author's view, the fact of agreement occupies a spectrum within which there exists a range of legitimate consent. Courts should appeal to public policy in defining that range.

226. *Authors Guild*, 770 F. Supp. 2d at 686.

227. Of course, the U.S. Constitution provides a utilitarian justification for the IP laws, and, despite signing the Berne Convention, the United States has controversially declined to recognize a moral rights justification for its copyright system. *See* Brandi L. Holland, Note, *Moral Rights Protection in the United States and the Effect of the Family Entertainment and Copyright Act of 2005 on U.S. International Obligations*, 39 VAND. J. TRANSNAT'L L. 217, 228–31 (2006). Furthermore, one can argue with some force that the rights-based approach observed in U.S. copyright law has a utilitarian foundation such that, even if violation of those rights in certain instances would enhance net utility, in the long run such violations would inure to the detriment of all. Nevertheless, copyright displays a number of features that are irreconcilable with utilitarian considerations. For instance, the law grants authors protection even in circumstances where IP law is not the but-for cause of the writings, such as is the case with respect to dissertations and theses written in university. Ryan M. Seidemann, *Authorship and Control: Ethical and Legal Issues of Student Research in Archaeology*, 14 ALB. L.J. SCI. & TECH. 451, 471 (2004).

The law and economics literature has addressed the circumstances in which acquiescence should translate into legally cognizable consent.[228] Applied to the GBS settlement, requiring class members to opt out should not have been problematic because that feature of the agreement respects the right of copyright holders to refuse permission, but also takes the appropriate default position that authors would want to make their works available for the world to read and purchase. Public policy ought not to be indifferent between default positions, for they matter enormously as a consequential matter. The opt-out nature of the rejected GBS settlement promised to bring millions of more books to the consuming public than would a settlement founded on opt-in. Judge Chin's invitation to amend the agreement to include only those authors who affirmatively grant permission misses these points entirely, and perversely denies consumers access to orphan works that they could otherwise have enjoyed.

B. Expanding the Scope of Section 2 Enforcement

The GBS settlement is the ultimate example of how using competition law to require optimal outcomes can ironically reduce consumer welfare. The case is particularly illuminative because it lacks a feature that most antitrust cases display prominently—uncertainty as to whether enforcement proceedings against a challenged course of conduct will ultimately inure to the public benefit. It was an undeniable fact that the GBS arrangement would have enhanced consumer welfare, yet the district court declined to approve it. In this respect, the case implicitly—though far from subtly—embraced the principle enshrined in the LRA rule that "mere" welfare enhancement does not render an act conclusively legal under the antitrust laws.

The GBS case differs from most in which the courts have explicitly applied the LRA rule, however, because it does not involve a horizontal agreement as to Google.[229] Instead, the case is better understood as a vertical arrangement that bestows Google with a dominant position in the distribution of a comprehensive digital library that includes orphan works, which are not available in physical or digital form anywhere

228. *See* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW § 4.3 (8th ed. 2011).
229. There is a horizontal element to the arrangement, however, between rightsholders who engage in horizontal competition with one another.

else.[230] Thus, the vertical arrangement promised to create a new, albeit monopolized, market. Although section 1 of the Sherman Act applies to vertical agreements, one can more meaningfully analyze the GBS arrangement through the lens of section 2,[231] which governs actual and attempted monopolization, as well as conspiracies directed toward the same—for our purposes, Google's supposed monopolization of orphan works.[232] For the reasons explained above, the judiciary's decision not to approve the settlement agreement effected a significant harm to welfare.[233] That the parties did not mold the arrangement in such a way as to achieve the maximum feasible benefit for consumers is no ground for antitrust concern absent a compelling reason to think that a less lucrative agreement would have provided sufficient impetus to the innovator, Google, to pursue the course that it did. This is the best contemporary example of why construing antitrust through a regulatory lens can lead to perverse outcomes.

The harm occasioned by antitrust's implicit requirement of welfare maximization in the field of unilateral conduct, however, is not limited to the case of Google Books, which was in some respects sui generis. This Author argues that quiet adoption of the LRA principle under section 2 of the Sherman Act, particularly when applied to innovation-based markets, bears unique dangers and thus should be opposed.[234] These dangers emanate from the grave uncertainty that is a hallmark of

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230. *Cf.* Eric M. Fraser, *Antitrust and the Google Books Settlement: The Problem of Simultaneity*, STAN. TECH. L. REV. 10–11 (Sept. 24, 2010), http://stlr.stanford.edu/2010/09/antitrust-and-the-google-books-settlement/ (describing the settlement agreement as having a similar effect as a horizontal agreement between competitors).

231. *See, e.g.*, Perington Wholesale, Inc. v. Burger King Corp., 631 F.2d 1369, 1377 (10th Cir. 1979) ("Traders oriented vertically to each other can be found in violation of section 2 by conspiring to monopolize one horizontal market intersecting the vertical arrangement.").

232. Notably, the procedural posture of the GBS settlement required the court to consider whether the proposed agreement satisfied Federal Rule of Civil Procedure 23(e), which requires courts to determine whether settlements are "fair, reasonable, and adequate" to the class members—in the GBS case, rightsholders. FED. R. CIV. P. 23(e). It is not clear that antitrust rules should apply to this calculus. C. Scott Hemphill, Comment, *Collusive and Exclusive Settlements of Intellectual Property Litigation*, 2010 COLUM. BUS. L. REV. 685, 701–02. Nevertheless, because the district court saw fit to consider the public interest effects of the settlement from an antitrust perspective, it is appropriate to use the GBS case as an important illustration of how the norms underlying the LRA rule have transcended rule of reason cases to encapsulate monopolization cases.

233. *See supra* Part IV.A.4.

234. *See also* Manne & Wright, *supra* note 16, at 185 ("[I]nnovation is closely related to antitrust error. . . . This bias is likely to do even more damage when economists have less systematic theoretical and empirical knowledge about the relationship between competition and innovation on policy-relevant margins than they do about other traditional forms of competition.").

monopolization actions. Pertinent counterfactuals are rarely as elusive as they are in those settings.

Explaining the propensity for error requires a brief return to Part III of the Article. Although concentrated markets can yield less-than-desirable levels of price competition and innovation, depending on the circumstances, they can also act as incubators of innovation.[235] Unfortunately, the economics literature has yet to produce a reliable prescription capable of broad application regarding the relative virtues of competition and dominance in yielding greater rates of invention.[236] Nevertheless, both theory and evidence suggest that competition in some form is a prerequisite of consistently high rates of innovation, especially of groundbreaking technologies that tend to disrupt the status quo.[237] This competition, however, need not take the form of price wars amongst numerous rivals. That is, competition is not synonymous with an unconcentrated market structure comprised of a significant number of companies. Instead, IP and other legally recognized appropriation mechanisms can deflect competition from active sales in the marketplace to technology races in the laboratory, and may in fact feed greater levels of dynamic efficiency, albeit at cost to static efficiency.[238] The fact that an industry may be highly concentrated, therefore, does not necessarily mean that competition is absent. From an enforcement perspective, however, the fact that monopoly market share and competition are consistent complicates the question whether circumstances warrant antitrust intervention.

As long as third-party researchers maintain active levels of R&D, and as long as they possess means to commercialize new technologies either themselves or through licensees, their presence will spur ongoing innovation by incumbent monopolists. Incumbents that fail to stay ahead of the pack will find their seemingly secure monopolies quickly eroded, an observation for which the history of new economy industries founded on innovation provides much evidence.[239] Google and Apple's continuing evisceration of Microsoft's previously unassailable market positions are good contemporary examples.[240]

235. *See supra* Part III.A.
236. *See supra* Part III.A.
237. *See supra* Part III.A.
238. *See supra* Part III.A.
239. *See* Posner, *supra* note 127, at 930.
240. *See* Robert Cyran & Martin Hutchinson, *At Microsoft, Bing Too Costly To Keep*, N.Y. TIMES, July 25, 2011, at B2; Editorial, *Remember Microsoft?*, N.Y. TIMES, June 11, 2011, at A20; Elizabeth Flock & Hayley Tsukayama, *Apple Announces Free*

This suggests that antitrust policy in technology markets should concern itself less with policing high levels of industry concentration and more with incumbents' exclusionary practices that fetter rivals' ability to introduce potentially superior technologies.[241] Unfortunately, the economics of exclusion are hotly debated, and little consensus has emerged as to the likely efficacy of dominant-firm practices in foreclosing the emergence of rival-marketed technologies.[242] As a result, context-specific analysis is necessary to determine the need for antitrust actions to protect competition in innovation in any particular case.

Such is the unfortunate reality of antitrust oversight of monopolistic practices in innovation markets. As a result, enforcement actions against dominant-firm conduct in high-technology markets display unique difficulties. Enforcers must grapple with the preceding characteristics of innovation markets and attempt the laborious and imprecise process of determining whether a challenged practice is injurious to consumers.[243] Such determinations take place without the benefit of empirical evidence favoring intervention or noninvolvement, and necessarily involve tradeoffs with immeasurable long-run effects.

In determining whether a practice is harmful by virtue of its being likely to perpetuate monopoly conditions or frustrate the emergence of competing technologies, principles of decision theory come to the fore. Economists generally believe that Type I errors—incorrectly finding that dominant-firm conduct is monopolist—are more serious than Type II

iCloud Service, WASH. POST, June 7, 2011, at A10, *available at* 2011 WLNR 11320863; Martin Peers, *A Window into Microsoft's Profit Outlook*, WALL ST. J., Mar. 20, 2010, at B16; Seth Schiesel, *Game Changer: Downtime Becomes a Pastime*, N.Y. TIMES, June 9, 2011, at F1.

241. *Accord* ANTITRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATIONS 34 (2007), *available at* http://permanent.access.gpo.gov/lps81352/amc_final_report.pdf ("Economic research found procompetitive reasons to explain highly concentrated markets—that is, that the most efficient firms were winning the competitive struggle and thereby achieving high market shares.").

242. *See, e.g.*, Louis Kaplow, *Why (Ever) Define Markets?*, 124 HARV. L. REV. 437, 498 n.117 (2010).

243. To take but one topical example, consider the debate over network neutrality. Proponents of such a doctrine fear that broadband Internet service providers have incentives to give preferential treatment to certain forms of content and may even block applications or conduct from companies with which they compete in an upstream or downstream market. *See, e.g.*, Tim Wu & Christopher Woo, *Keeping the Internet Neutral?*, 59 FED. COMM. L.J. 575, 581–82 (2007). Opponents of net neutrality rely on competition and the economic incentives possessed by network operators to maximize the value of the network to consumers as adequate protections against abuses and also point out that certain forms of discrimination are in fact efficient. *See, e.g.*, *id.* at 575–76. Much of the debate centers on currently improvable assumptions concerning both the curative powers of competition in network industries and the tendency of concentrated versus unconcentrated markets to yield optimal amounts of innovation. *See id. passim*.

errors—incorrectly approving collusive practices—because the market will eventually correct the latter, but may be unable to remedy the former.[244] This suggests that enforcers should err on the side of nonenforcement in situations of uncertainty. But what should be the extent of that bias? Even if one decides that a dominant-firm practice is sufficiently problematic that policy requires its arrest, one must weigh both the cost of enforcement and the practical remedial limitations accompanying even a successful suit. Monopolization actions are typically protracted such that, in quickly evolving technology markets, what may have once been a problematic exclusionary practice may be an anachronism of history by the time a court considers remedies.[245] Even if anticompetitive conditions endure, antitrust remedies directed at spurring competition in monopolized industries are famously ineffectual.[246] As a result, sound policy requires establishing not only that a particular practice is exclusionary, but also that the net effect of costly antitrust proceedings is likely to be positive.[247]

This brings us to the issue of welfare maximization. When it is difficult to determine the merits of an impugned practice by a dominant firm, one might view the question whether antitrust requires the most, or simply more, as inconsequential. In other words, the indeterminate long-term impact of unilateral dominant-firm behavior is presumably a neutral fact, making a strong case for neither aggressive enforcement nor liberal laissez-faire policy. This view would be incorrect, however, for two reasons. First, errors in different directions carry distinct costs that may

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244. For the classic discussion of this position, see Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1 (1984); *see also* Richard A. Epstein, Bell Atlantic v. Twombly*: How Motions To Dismiss Become (Disguised) Summary Judgments*, 25 WASH. U. J.L. & POL'Y 61, 68 (2007) (assigning more weight to Type I errors). For an opposing view, see William Kolasky, *The Justice Department's Section 2 Report: A Mixed Review*, ANTITRUST SOURCE, Oct. 2008, at 1, 4, *available at* http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Oct08_FullSource10_27f.authcheckdam.pdf.

245. *See, e.g.*, Lee Goldman, *Oligopoly Policy and the* Ethyl Corp. *Case*, 65 OR. L. REV. 73, 93–94 (1986).

246. *See, e.g.*, Jonathan B. Baker, *Preserving a Political Bargain: The Political Economy of the Non-Interventionist Challenge to Monopolization Enforcement*, 76 ANTITRUST L.J. 605, 616–17 (2010) (summarizing the Chicago School view as to why monopolization enforcement is likely to be ineffective and counterproductive); Einer Elhauge, *Disgorgement as an Antitrust Remedy*, 76 ANTITRUST L.J. 79, 87 (2009); John E. Lopatka, *Assessing* Microsoft *from a Distance*, 75 ANTITRUST L.J. 811, 813–14 (2009).

247. *See, e.g.*, John E. Lopatka & William H. Page, *Economic Authority and the Limits of Expertise in Antitrust Cases*, 90 CORNELL L. REV. 617, 639 (2005) ("[A]ntitrust commentators have been skeptical that the 'big case' is worth its institutional costs.")

justify a systemic preference in favor of either Type I or Type II errors.[248] Second, and of principal relevance to this Article, the view that the uncertain economic effect of monopolistic conduct supports neither under- nor over-enforcement assumes that consumer harm does not encapsulate opportunity cost.

In fact, demanding that unilateral conduct do more than bring about a positive increment in consumer welfare shifts the legality condition in a troubling way. Specifically, requiring the best possible, or even a better-than-positive, outcome for consumers in cases of uncertainty narrows the zone of permissible unilateral behavior to a small subset of what is in fact socially desirable conduct. This effect enhances the probability of judicial Type I errors. The danger is that enforcement agencies may seek to engineer superior market outcomes by using the antitrust laws as a form of industry regulation—a goal that may compound false positives to the long-term detriment of consumers.

The nature of this risk requires some elaboration because it is not immediately obvious. As noted in the introduction, there are competing definitions of consumer harm, and the differences matter enormously. In a world of perfect legal and factual certainty—both ex ante and ex post—consumer harm is synonymous with any departure from the welfare-maximizing path. It is the actors' limited ability to determine the factual and legal consequences of their behavior, and the courts' restricted capacity to construct the necessary counterfactual, that creates a spectrum, rather than a point, of consumer benefit. As we obviously live in a world where legal certainty does not prevail and where courts routinely err, the law should define consumer injury without reference to opportunity cost.[249] If a challenged restraint brings about or otherwise facilitates an increase in purchasers' well-being, as compared to a world in which the defendant did not act at all, the relevant behavior benefits consumers and should therefore be lawful. The only exception should be where enforcement agencies and courts can reliably construct the relevant counterfactual and accurately conclude whether the defendant would have followed a better course were the law to forbid the company's preferred, though less consumer-friendly, course.

Not all counterfactuals are hopelessly indeterminate. Indeed, the Author's view that the law should ignore opportunity cost in defining consumer injury reflects the premise that courts can demarcate the but-for world in which the defendant eschewed any form of substitute

248. See Alan Devlin & Michael Jacobs, *Antitrust Error*, 52 WM. & MARY L. REV. 75 (2010) for the Author's extended discussion of error analysis in antitrust jurisprudence.

249. To be specific, this is the opportunity cost associated with substitute behavior that displays LRA characteristics.

behavior and simply declined to act at all. That particular counterfactual is easier to construct, however, than the multitudinous ones in which a company may or may not have undertaken specific forms of conduct that are more conducive of consumer benefit than the practice at hand.[250] It is only where a court can determine the nature of the relevant counterfactual with complete confidence that one can reliably argue that consumers can be injured by a beneficial, though not ideal, arrangement. As courts can rarely, if ever, make such a factual finding with the requisite confidence, and because no effective limiting principle exists, the LRA rule is misplaced.

To appreciate the danger of applying welfare-maximization principles to dominant-firm conduct, consider the following example. Suppose that an innovative company achieves a dominant position on the basis of its technologically superior product. In order to maintain its monopoly, the company devotes considerable resources to R&D, thus continuously improving its flagship good, though it also engages in an ancillary practice that is simultaneously attractive to its customers and disadvantageous to its fringe rivals. This practice is volume discounting, which allows the monopolist to achieve scale efficiencies, though the conduct generates potentially offsetting exclusionary effects.[251] Does consumer harm exist?

To answer this question, one must determine the but-for world in which the dominant company declined to undertake the impugned practice—volume discounting—at all. If consumers would be better off without the discounting—that is, with flat-rate pricing—then that conduct injures them under any definition of "injury," and an antitrust violation should follow. If discounting with scale yields net gains for purchasers vis-à-vis fixed pricing, however, then consumers are "better off" in the

250. As explained above, this is not to say that a court can never appropriately impose antitrust liability for declining to pursue an obviously less restrictive but equally effective agreement. The LRA rule may be appropriate where the court, ex post, can be confident that its finding of a Sherman Act violation would not have induced the defendants to decline to act at all ex ante. It is critical, however, that the courts cabin such findings to the narrow circumstances in which such confidence is justified. The Author is of the view, however, that monopolization cases are categorically inappropriate subjects for welfare-maximization principles.

251. It should be borne in mind that a competitor's "efficiency" does not necessarily refer to the marginal cost at which that rival operates because that metric is typically contingent on scale, and hence, contingent.

sense used by this Article. In the Author's view, this should in itself demonstrate the absence of a Sherman Act violation.

What if the law, however, interjected with an additional question: would a different form of volume discounting yield even greater gains for consumers and still provide comparable efficiency gains to the dominant firm? For instance, a court could find that less severe discounting would allow the monopolist to achieve similar scale efficiencies, but would have less detrimental an effect on rivals' ability to expand output from fringe positions in the market. To be sure, less pronounced discounts harm the firm's consumers, but they would also increase the propensity for long-term competition. If the benefits of that long-term competition outweighed the higher average selling prices in the short run, antitrust condemnation of the volume discounting would follow.

In a perfect world—one characterized by zero judicial error and legal certainty—policy considerations would justify courts' making the legality of a dominant-firm practice contingent on its being the most consumer-friendly version possible. In reality, however, such an approach would introduce another confoundingly difficult question into the antitrust calculus. Every time a court made a Type I error in determining whether the welfare-enhancing practice before it was the best possible such practice—and one would expect that the judiciary would make such errors regularly—the law would condemn a unilateral practice that benefits consumers. Such perversities would be justified only if the effect of a rule requiring the best possible variant of an efficient practice would be to induce monopolists to undertake consistently superior courses of action. Given companies' limited means to foresee the outcomes of judicial analysis under section 2, in addition to the judiciary's incapacity to engage reliably in the fact-finding necessary for accurate monopolization analysis, such an effect seems most unlikely.

This risk is by no means limited to the example of loyalty discounting. The law could always second-guess the consumer-benefitting acts of exclusive contracting, product tying, low or "predatory" pricing, loyalty rebates, and vertical integration, and suppose that material modifications of the behavior would give consumers an even better deal.

This is no academic threat, but goes to the very heart of the antitrust enterprise. If the LRA rule informs the jurisprudential meaning of consumer harm, it is unlikely that those responsible for enforcing the law will embrace the welfare-maximization principle only in a narrow subset of circumstances. Instead, that principle is apt to inform one's understanding of antitrust law, as well as the nature of commercial practices that that body of law seeks to arrest. The highly publicized Google Books Search settlement agreement reveals that the LRA mindset resonates not only with Judge Chin, who rejected the agreement, but with the scores of commentators who decried the monopoly-producing nature of the arrangement. Has the goal of welfare maximization corrupted monopolization proceedings under section 2? The answer is not obvious, for enforcement agencies have little incentive to announce that their principal objection to a dominant firm's practice is that it is does not benefit consumers quite as much as they would like.

In one respect, it is clear that the welfare-maximization principle does not find unqualified application in the realm of unilateral behavior. It has long been settled that even dominant firms enjoy considerable freedom in tailoring their behavior, and it is unlikely that the law will widely seek to micromanage unilateral conduct to achieve optimal adjustments to welfare-enhancing conduct.[252] Yet, a form of analysis under section 2 known as "the unnecessarily restrictive conduct test" suggests that a variant of the LRA rule is indeed present.[253]

In the Author's view, there is a significant risk that is both subtle and insidious. Specifically, the welfare-maximization principle is most likely to inform agency and judicial determinations silently at the margin. In concentrated technology markets, agencies may observe high levels of R&D that translate into ongoing positive increments in consumer welfare but also see propriety control that provides the dominant incumbent systemic advantages for conducting follow-on innovation. Public choice theory predicts, accurately as it turns out, that out-competed companies will often seek recourse through the judicial process generally, and antitrust laws in particular.[254] Bombarded by competitor complaints and buoyed by the successful company's dominant market share, enforcement agencies may decide that even though the status quo is consumer-friendly and highly innovative, intervention may facilitate even better outcomes. Recent enforcement actions against Intel, Apple, and Google suggest that this may indeed have occurred.

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252. *See, e.g.*, Goldwasser v. Ameritech Corp., 222 F.3d 390, 397–98 (7th Cir. 2000) ("Part of competing like everyone else is the ability to make decisions about with whom and on what terms one will deal. . . . In general, then, even a firm with significant market power has no duty to deal with certain suppliers or distributors . . . .").

253. *See* Steven C. Salop & R. Craig Romaine, *Preserving Monopoly: Economic Analysis, Legal Standards, and Microsoft*, 7 GEO. MASON L. REV. 617, 659 (1999).

254. *See, e.g.*, D. Daniel Sokol, *Antitrust, Institutions, and Merger Control*, 17 GEO. MASON L. REV. 1055, 1073–74 (2010). *But cf.* Shubha Ghosh & Darren Bush, *Predatory Conduct and Predatory Legislation: Exclusionary Tactics in Airline Markets*, 45 HOUS. L. REV. 343, 367 (2008) (concluding that public choice theory has not lead to excessive litigation).

Spatial constraints foreclose detailed discussion of these recent monopolization actions, but a brief discussion makes the danger clear. Apple launched the first version of its wildly successful iPhone on June 29, 2007, with AT&T providing exclusive coverage.[255] This innovation invited a wave of lawsuits alleging that the exclusionary contracts violated the antitrust laws.[256] Academics hostile to closed over open systems object to such exclusivity on the ground that consumers would be better off if they enjoyed choice as to their preferred wireless provider.[257] What these views and the accompanying lawsuits fail to consider is why the appropriate point of reference is the best possible outcome for consumers as opposed to the state of the world in which no iPhone innovation occurred at all. As explained above, systemic judicial error and ex ante legal uncertainty make the former reference point a generally undesirable one. As there is no dispute that consumers are better off with inventions like the iPhone with incidental contractual restraints than they are with no such invention, this is all that antitrust should require in the section 2 setting. The fact that the lawsuits prove enduring is of great concern, and suggests that a silent LRA principle underlies section 2 analysis.

The controversy concerning Apple's iPhone was by no means unique—the earlier introduction of the iPod, and more recent launch of the iPad, invited great controversy because of the lack of interoperability.[258] Once more, competition concerns arose because consumers, although displaying an overwhelming demand for the new product, would have preferred if it operated as part of an open system.

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255. *See* Brian X. Chen, *June 29, 2007: iPhone, You Phone, We All Wanna iPhone*, WIRED (June 29, 2007, 12:00 AM), http://www.wired.com/thisdayintech/2009/06/dayintech_0629/.

256. *See, e.g.*, *In re* Apple & AT & TM Antitrust Litig., 596 F. Supp. 2d 1288, 1306 (N.D. Cal. 2008); *see also* Matt McMurrer, Note, *Exclusive Gadget:* Apple & AT&T Antitrust Litigation *and the iPhone Aftermarkets*, 36 J. CORP. L. 495 (2011) (providing an overview of the antitrust litigation related to the iPhone's exclusionary contracts).

257. *See, e.g.*, Tim Wu, *Wireless* Carterfone, INT'L J. COMM. 389, 398–99 (2007), http://ijoc.org/ojs/index.php/ijoc/article/view/152/96 (critiquing the retail barriers omnipresent in the mobile phone industry).

258. *See, e.g.*, Miguel Helft, *IPad Service Draws Scrutiny*, N.Y. TIMES, Feb. 18, 2011, at B4; *see also* Niva Elkin-Koren, *Making Room for Consumers Under the DMCA*, 22 BERKELEY TECH. L.J. 1119, 1126–27 (2007) (discussing competition concerns related to the iPod's interoperability constraints); Jane Winn & Nicolas Jondet, *A New Deal for End Users? Lessons from a French Innovation in the Regulation of Interoperability*, 51 WM. & MARY L. REV. 547, 555–56 (2009) (linking France's desire to regulate interoperability to Apple's iPod and iTunes business strategy).

More recently, in late June 2011, the FTC announced a formal antitrust investigation of Google's Internet-search algorithm.[259] The economics at play in this industry are fascinating but complex, and thus require more detailed treatment than is possible within the confines of this Article.[260] It bears noting that Google's dominant position, founded on a history of sustained qualitative superiority over its rivals, continues to produce consumer-welfare-enhancing innovation. A concern with Google's vertical integration underlies the investigation,[261] which suggests that the FTC is worried that further entrenchment by Google may not be as conducive of competition, and hence not as productive to consumer welfare, as is possible. It is possible that alleged bias in Google's search results could harm long-term consumer welfare discounted to present value, but it seems to the Author that, given the extraordinary rate of innovation in the markets involved, the likelihood that Google's practices are injurious to welfare is slight. If this is indeed the case, the FTC's view is, in effect, regulatory. The FTC may be taking aim at Google's primary service, which has been overwhelmingly successful in the United States based on its superiority, and concluding that it could be better. A desire to maximize consumers' well-being, rather than accept current and ongoing consumer benefits, is misplaced in this section 2 setting for all the reasons explored above.[262]

Finally, the recent FTC action against Intel for the chipmaker's loyalty discount policies is also worrisome in this regard.[263] Economic analysis suggests that the attacked pricing caused no consumer harm, at least in the short run, which suggests that the agency's primary goal in bringing the suit was to engineer market conditions more conducive to long-run

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259. *See* Jessica Guynn & Jim Puzzanghera, *FTC Launches Investigation of Google*, L.A. TIMES (June 25, 2011), http://articles.latimes.com/2011/jun/25/business/la-fi-google-ftc-20110625.

260. For an interesting representative discussion, see Josh Wright, *Search Bias and Antitrust*, TRUTH ON MARKET (Mar. 24, 2011), http://truthonthemarket.com/2011/03/24/search-bias-and-antitrust/.

261. Guynn & Puzzanghera, *supra* note 259.

262. *See supra* Part IV.B. It also bears noting that the other merits of the case are questionable. The switching barriers that lock consumers into Google's search engine are unusually low, and an appropriate remedy is most unclear—the idea that the government would have to approve continuous changes in the company's algorithm is disturbing, given the history of regulators' stymieing rapid innovation when placed in a position of approving technological alterations in far less innovative and more slow-moving industries.

263. *See, e.g.*, Herbert Hovenkamp, *The Federal Trade Commission and the Sherman Act*, 62 FLA. L. REV. 871, 888 (2010).

entry.[264] As explained above, however, asking whether a company could substitute a consumer-friendly pricing practice for one that is more facilitative of rival expansion introduces an additional factual element into the antitrust analysis—one that courts are far from well-placed to address. Indeed, by requiring more than a showing that the challenged practice benefits consumers, the law enhances the risk of Type I errors at great potential risk to the very goal that the law purports to champion.

V. CONCLUSION

Antitrust is suffering an identity crisis. Properly understood as a prophylactic device aimed at arresting practices that are harmful to consumer welfare, the courts have steadily transformed this area of law into something different. Undoubtedly with noble intentions, the judiciary has rewritten the rule of reason to require the best outcome available, rather than a mere improvement. Given the ex post posture in which courts operate—characterized by hindsight bias and a concomitant temptation to conflate possible outcomes with necessarily attainable ones—it is perhaps unsurprising that judges would seek to engineer superior market outcomes when they can identify less restrictive alternatives to impugned conduct. The danger, however, is at once subtle, systemic, and serious.

This phenomenon is perhaps a manifestation of the reversed aphorism that easy cases make bad law. Confronted with actions in which defendants had adopted a practice that was simultaneously efficient and injurious of rivals' ability to compete on equal footing, courts may understandably insist that the defendant companies eschew one practice in favor of another that is equally efficient but more facilitative of competition. Especially in cases involving entrenched dominance or the emergence of new markets—through a joint venture, for example—requiring competitors not to pull the ladder up behind them when less detrimental alternatives exist arguably promotes Kenneth Arrow's view of competition by helping to ensure equality of opportunity.

Yet, two serious problems emerge. First, the LRA test lacks a theoretical limiting principle. Literally applied, it would preclude all manner of ubiquitous—and desirable—business arrangements, including joint ventures and mergers. The fact that the courts have not applied the test in this

264. *See, e.g.*, Joshua D. Wright, *An Antitrust Analysis of the Federal Trade Commission's Complaint Against Intel* (ICLE Antitrust & Competition Policy White Paper Series, George Mason Law & Econ. Research Paper No. 10-27, 2010), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1624943; Keith N. Hylton et al., *Commentary: U.S. Antitrust Enforcement Becomes More European*, FORBES (May 18, 2009, 9:30 AM), http://www.forbes.com/2009/05/18/intel-amd-antitrust-ftc-opinions-contributors-christine-varney.html.

manner is not a convincing defense of the rule, but instead demonstrates its incoherence.

Second, and more seriously, by injecting a high-level view that antitrust focuses on maximizing, rather than simply improving, welfare, the law invites findings of antitrust violations in high-stakes cases where courts cannot reliably identify the relevant counterfactual. The problem here is partially one of precedential cabining. By applying the LRA test in obvious cases—those where the defendants could easily have followed an equally effective course without impeding competition as much or at all—the courts open more complex cases to similar treatment. Crucially, however, both the judicial capacity to err and the magnitude of the social cost involved in courts' mistakes rise sharply as the difficulty and the stakes of any given case increase.

The Author argues that the courts' construction of the Sherman Act requiring more than a progression in welfare improperly conflates antitrust with regulation. Unfortunately, courts have not limited this misguided principle to proceedings involving concerted behavior. Instead of focusing the LRA inquiry on contractual restraints on competition alone, the judiciary and enforcement agencies have adopted the principle of welfare maximization in monopolization cases. This phenomenon is seriously problematic, especially in cases where defendant companies achieved their monopoly status on account of significant and ongoing innovation. Here, both the proclivity for and cost of false positives are at their peak, rendering the law's requirement of the best to be especially perverse.

This improper adoption of the welfare-maximization principle reached its logical conclusion in the Google Books Search case. Unfortunately, the harm is unlikely to stop there. A variety of recent actions portend a troubling rise in authorities' attempts to employ antitrust as an affirmative tool of public policy, instead of using it as a barrier against social-welfare-reducing activities. By seeking to facilitate more open competition in the future by restricting practices that are undeniably efficient today, antitrust enforcers may paradoxically provide consumers with less.

The Author urges the judiciary to reorient antitrust jurisprudence toward its traditional and proper mandate, which is to prohibit practices that are apt to harm consumers, and to do so only when such harm is not incidental to the company's legitimate exercise of market power. The courts and enforcement agencies would do well to recall one of the key principles underlying the field of antitrust law: it is not regulation.