

Antitrust Enforcement in the Clinton Administration

David A. Balto

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ANTITRUST ENFORCEMENT IN THE CLINTON ADMINISTRATION

David A. Balto †

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INTRODUCTION

Antitrust laws are crucial for the functioning of a free market economy because they seek to keep markets open and to prevent the aggregation and exercise of market power. Government enforcement of the antitrust laws fosters the ability of firms to battle in the marketplace, ideally making consumers the ultimate beneficiaries of that competition. This view of government enforcement has thrust the enforcement of anti-trust laws into the forefront under President Clinton's administration.

To understand the importance of antitrust in the Clinton Administration, it is necessary to begin with a perspective of the three predecessor administrations. Antitrust is often described in terms of ideological swings. During the Reagan Administration it took a strong swing towards the "right." A major part of that administration's economic program was to reduce government regulation. Antitrust enforcement was perceived as being overly intrusive, out of control, and highly regulatory. In the 1970s, during President Carter's administration, the agencies focused their resources on major corporations such as AT&T, Exxon and IBM, seeking to attack perceived abuses of market power, sometimes using somewhat novel theories of harm. The Reagan Administration considered most of these cases as an economic waste and viewed antitrust enforcement as imposing a tax on the activities of business. The Reagan Administration introduced several initiatives that focused antitrust enforcement away from a perceived preoccupation with the conduct of large businesses towards conduct that was more traditionally viewed as economically anticompetitive, primarily the activities of cartels and other

collusive arrangements.¹ The resources of the antitrust enforcement agencies were substantially reduced during the Reagan Administration.² Some remaining resources were redirected towards local criminal conspiracies (usually involving bid-rigging) and competition-reducing codes of conduct promulgated by associations of small businesses and professions. Most of these cases involved relatively local conspiracies, and the impact on commerce of these enforcement actions was modest at best. The government's ability to litigate cases effectively seemed to be much in doubt. For example, the government's IBM litigation lasted for over a decade without any appearance of resolution.³ In general, the government's civil antitrust enforcement program was all but extinguished, and no monopolization cases were brought during the Reagan Administration.

Similarly, merger enforcement was periodic at best, and the government's efforts at litigating merger cases were generally unsuccessful.⁴ In spite of doubts that it was enshrining lenient enforcement policy, in 1982 the Department of Justice ("DOJ" or "Department") adopted new merger guidelines that made merger analysis far more analytically dependable.⁵ The Reagan Administration sponsored legislation to amend the Clayton Act to create an "efficiencies" defense and require greater consideration of foreign competition.⁶ Most mergers were found safe from any risk of creating competitive harm despite the significant size and market share of a firm created by the merger, often because the agencies were quick to accept arguments about low entry barriers. Vertical merger⁷ or potential competition merger⁸ enforcement was practically nonexistent.

¹ See, e.g., William J. Baer & David A. Balto, *The Politics of Federal Antitrust Enforcement*, 23 HARV. J.L. & PUB. POL'Y 113 (Fall 1999); Robert Pitofsky, *Antitrust Policy in a Clinton Administration*, 62 ANTITRUST L.J. 217 (1993); Nolan E. Clark, *Antitrust Comes Full Circle: The Return to the Cartelization Standard*, 38 VAND. L. REV. 1125 (1985).

² Staffing at the FTC was reduced by 45 %. See FTC Budget Branch, *Full Time Equivalent History*, (visited Apr. 18, 2000) <<http://www.ftc.gov/ftc/finance/apphsii.htm>>.

³ See *In re IBM Corp.*, 475 F.Supp.1372 (S.D.N.Y. 1979), *aff'd* 618 F.2d 923 (2nd Cir. 1980), *mandamus granted*, 687 F.2d 591 (2nd Cir. 1982).

⁴ See John E. Lopatka & James F. Mongoven, *After Preliminary Relief in Merger Cases is Denied, What Then?*, 17 RES. L. & ECON. 149 (1995).

⁵ See DEPARTMENT OF JUSTICE & FEDERAL TRADE COMMISSION, 1982 MERGER GUIDELINES (1982), *reprinted in* 47 Fed. Reg. 28,493 (June 30, 1982) [hereinafter 1982 MERGER GUIDELINES].

⁶ This legislation did not pass.

⁷ A vertical merger is the acquisition of a company that either buys from or sells to the acquiring company. See *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962) (holding that market foreclosure is the "primary vice" of an anticompetitive vertical merger).

⁸ A potential competition merger is defined by what it is not – it is not horizontal and it is not vertical. Mergers of firms in wholly separate industries are rarely challenged; most challenged conglomerate mergers are geographic market extension mergers, see *United States v. Falstaff Brewing Co.*, 405 U.S. 952 (1973), or product market extension mergers, see *United States v. Continental Can Co.*, 387 U.S. 441 (1964).

During the Bush Administration, under the leadership of Janet Steiger at the Federal Trade Commission ("FTC" or "Chairman") and Assistant Attorney General James Rill at the Antitrust Division of the Department of Justice, the pendulum swung back in the other direction, and there was an attempt to bring antitrust enforcement to a more even keel. The Bush Administration made some efforts to expand civil litigation and bring cases under more novel theories of competitive harm.⁹ Merger enforcement increased but the government's success record was still modest at best. Criminal enforcement continued to focus on relatively small bid rigging cases.¹⁰ Perhaps most importantly, the Bush Administration stopped the drain on funding for the antitrust enforcement agencies.

The Clinton Administration's antitrust enforcers faced a threefold challenge. First, the antitrust agencies needed to improve their ability to perform their core mission - enforcement of the antitrust laws. Second, the Administration needed to determine how to contribute to the development of a competition policy in a fast changing economy in which the relevance of antitrust was being called into question. Third, the Administration needed to improve the "antitrust process" to both reduce burdens on business while utilizing the agencies' limited resources effectively.

This article examines why antitrust enforcement has become more prominent, and in what respects current antitrust enforcement is different than that of earlier administrations. Part I of the article explores the current enforcement of the antitrust laws in the areas of criminal enforcement, merger enforcement, enforcement in high-technology markets, distributional restraints and dominant firm conduct. In light of the efficacy of enforcement in those areas, Part II examines how the enforcement agencies under the Clinton Administration have developed a competition policy and made that policy transparent. Part III surveys the process of antitrust enforcement, and how the agencies have improved that process to reduce burdens on business. For each of these issues, the article attempts to describe how the current administration has sought to improve the work of the antitrust agencies to better promote the competitive process and benefit consumers.

⁹ See, e.g., *In re Quality Trailer Products Corp.*, FTC No. C-3403, 57 Fed. Reg. 55,539 (Nov. 25, 1992) (consent order) (regarding invitations to collude).

¹⁰ The typical cases involved bid-rigging on some type of product purchased by government agencies, typically by local or state governments and usually on highway construction. See, e.g., *United States v. Bi-Co Pavers, Inc.*, 741 F.2d 730 (5th Cir. 1984), *United States v. Rubbish Removal, Inc.*, 1985-1 Trade Cas. (CCH) ¶ 66,617 (N.D.N.Y. 1985). While such cases were useful and many were brought, many did not involve consumer products, and this tended to limit the total amount of commerce involved.

I. ENFORCEMENT

During the 1990s, the antitrust agencies have reinvigorated their enforcement programs, and both the number and economic significance of their enforcement actions have grown. Their increased efforts are concentrated in five areas: (1) criminal enforcement, primarily involving international cartels, (2) merger enforcement, (3) enforcement in high technology markets, (4) distributional restraints, and (5) dominant firm conduct.

A. CRIMINAL ENFORCEMENT

The greatest single change in antitrust enforcement policy has probably come in the area of criminal enforcement. The Clinton Administration dramatically refocused this program, switching the attention of the criminal antitrust enforcers from relatively small domestic conspiracies to much larger international cartels. In so doing, the Department of Justice greatly increased the amounts collected in fines, securing over 1.1 billion dollars in fiscal year 1999 (FY 1999).¹¹ At the same time, the DOJ refined a set of procedural tools, making them capable of dealing with sophisticated, cross-border criminal antitrust issues.

1. *Procedural Tools*

The cases against international cartels¹² were successful in part due to the particular litigation teams, but also due to new procedural tools developed to deal effectively with these kinds of long-term, sophisticated, multi-national conspiracies. Some of those procedural innovations are the Corporate Leniency Program,¹³ the enactment of the International Antitrust Enforcement Assistance Act,¹⁴ the entering into numerous Bilateral Cooperation Agreements,¹⁵ and an increased willingness to apply the Sherman Act¹⁶ criminally to overseas conduct that has harmful effects within the United States.

¹¹ 1999 U.S. DEPT. OF JUSTICE, ANTITRUST DIVISION, ANNUAL REPORT 6 (visited Apr. 18, 2000) <<http://www.usdoj.gov/atr/pubdocs.html>>.

¹² See *infra* Part I.A.2.

¹³ The policy is available at (visited Mar. 24, 2000) <<http://www.usdoj.gov/atr/public/guidelines/lencorp.htm>> [hereinafter Corporate Leniency Program]. See also Gary R. Spratling, The Corporate Leniency Policy: Answers to Recurring Questions, Address at the ABA Antitrust Section, 1998 Spring Meeting (Apr. 1, 1998) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/1626.htm>>) (visited Mar. 24, 2000) [hereinafter Spratling, 1998 Corporate Leniency Speech].

¹⁴ 15 U.S.C. §§ 6201-6212 (1999).

¹⁵ The U.S. has entered into newer bilateral cooperation agreements with Germany (1976), Australia (1982), the European Community (1991), Canada (1995), Israel (1999), Japan (1999), and Brazil (1999). These agreements are reprinted at 4 Trade Reg. Rep. (CCH) ¶¶ 13,501-508.

¹⁶ 15 U.S.C. §§ 1-7 (1999).

The Corporate Leniency Program is a way of getting information about activities whose participants are, of course, strongly motivated to keep secret. Under the leniency program, a company and its officers may qualify for protection from criminal prosecution if they voluntarily report their involvement in a crime and satisfy certain other criteria.¹⁷ Under prior administrations, the program was limited to situations where the defendant identified criminal conduct unknown to the Antitrust Division. The Antitrust Division expanded the policy in 1993 to include situations where an investigation had already begun.¹⁸ The results were dramatic. Amnesty applications increased from one a year to over 20 a year.¹⁹

The Corporate Leniency Program is particularly important in an international antitrust context where other enforcement resources are more difficult to utilize, in part because service of process and discovery are much more difficult outside of the country. The key points about the leniency program are that it applies only to the *first* firm to report the violation and cooperate with the investigation, and that disclosure of a previously undiscovered cartel can be used to mitigate the penalties possible in some other matter for which the company is already being investigated.²⁰ These factors tend to create a "prisoner's dilemma," or a race to confess. As observed in an article in *Forbes*, "[i]f someone in your company has been conspiring with competitors to fix prices, here's some sound advice. Get to the Justice Department before your co-conspirators do. Confess and the U.S. Department of Justice will let you off the hook. But Hurry! Only one conspirator per cartel."²¹ Almost all of the Division's major cartel cases, including the vitamin cases, have been advanced by the cooperation of a Corporate Leniency applicant.²²

Another procedural innovation pushed forward by the Clinton Administration is the use of international cooperation agreements, which provide for the sharing of normally nonpublic data.²³ The effectiveness

¹⁷ See Corporate Leniency Program, *supra* note 13.

¹⁸ See *id.*

¹⁹ See Gary R. Spratling, Making Companies an Offer They Shouldn't Refuse: The Antitrust Division's Corporate Leniency Program—an Update, Address at the Bar Association of the District of Columbia's 35th Annual Symposium on Associations and Antitrust (Feb. 16, 1999) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/2247old.htm>>) (visited Mar. 24, 2000) [hereinafter Spratling, 1999 Corporate Leniency Speech].

²⁰ See *id.*

²¹ Janet Novak, *Fix and Tell*, FORBES May 4, 1998 at 46.

²² James M. Griffin, An Inside Look at a Cartel at Work: Common Characteristics of International Cartels, Address before the American Bar Ass'n, Section of Antitrust Law, 48th Annual Spring Meeting, Washington D.C. (Apr. 6, 2000) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/4489.htm>>) (visited Apr. 18, 2000).

²³ For a discussion of the various kinds of international cooperation agreements, see John J. Parisi, Enforcement Cooperation Among Antitrust Authorities, Remarks before the IBC UK Conferences Sixth Annual London Conference on EC Competition Law, London, England

of the agreements in combating cross-border cartels is illustrated by the joint investigation by U.S. and Canadian authorities into a price-fixing conspiracy involving thermofax paper. Although Canadian authorities first uncovered the offense, they sought the cooperation of the Antitrust Division because much of the actual anticompetitive activity occurred in the United States. In 1995, after two years of investigation, the two countries brought criminal charges under their respective laws. They concluded that prices to North American consumers had been increased by approximately 10 percent²⁴ and were mostly imposed on businesses and home fax users. Charges were filed against a Japanese corporation, two American subsidiaries of a Japanese company, and a former president of one of the subsidiaries.²⁵ The defendants pled guilty and agreed to pay criminal fines of more than \$6 million;²⁶ the Canadian antitrust authorities secured fines of nearly \$3.45 million.²⁷

Finally, a third procedural change consists of achieving greater legal clarity on the way authorities will apply American criminal antitrust laws to overseas conduct that has a concrete and harmful effect within the United States. An important clarification in this respect was achieved in the course of the thermofax paper case. A district court had originally dismissed the indictment against one of the defendants, holding that its alleged activities in furtherance of the conspiracy all occurred outside the United States.²⁸ The Division appealed this decision, asserting that the location of the particular activity had no direct bearing on the anticompetitive effects on American consumers and that the Sherman Act should generally extend to whatever criminal activities have a significant impact on the U.S. market.²⁹ The Division was successful in this argument and the First Circuit reversed the district court.³⁰ In so doing, the Circuit Court observed that in today's economy, prohibiting prosecution of extraterritorial actions that have "an intended and substantial effect" in the U.S. would "create perverse incentives for those who would use nefarious means to influence markets in the United States."³¹

(May 19, 1999) (transcript available at <<http://www.ftc.gov/speeches/other/ibc99059911update.htm>>) (visited Apr. 18, 2000).

²⁴ See Department of Justice, Press Release, *Northeast Fax Paper Importer Charged in Justice Department's Ongoing Investigation of International Price Fixing*, May 9, 1995 (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1995/260.at>.

²⁵ See *id.*

²⁶ See *id.*

²⁷ See Canadian Competition Bureau, Press Release, *Mitsubishi Paper Mills Ltd. Pleads Guilty*, Feb. 17, 1997 (visited Apr. 18, 2000) <<http://strategis.ic.gc.ca/SSG/ct01041e.html>>.

²⁸ See *United States v. Nippon Paper Indus. Co.*, 944 F.Supp. 55, 65-66 (D.Mass. 1996).

²⁹ See *United States v. Nippon Paper Indus. Co.*, 109 F.3d 1 (1st Cir. 1997), *cert. denied*, 522 U.S. 1044 (1998).

³⁰ See *id.*

³¹ See *id.* at 4, 8. A trial on the merits resulted in a directed verdict for the defendants, 62 F.Supp.2d 173 (D.Mass. 1999).

2. *International Cartels*

The Clinton Administration also refocused criminal enforcement away from local conspiracies toward international cartels. In the four years from FY 1987-1990, the Antitrust Division did not bring any cases against foreign corporations.³² In FY 1991, only 1 percent of the corporate defendants were foreign-based.³³ By comparison, in FY 1997, 32 percent of the corporate defendants were foreign-based, and in FY 1998, roughly 50 percent were foreign-based.³⁴

The pattern of current investigations suggests that future enforcement actions will continue to have a strong international flavor. In 1999, over 35 sitting grand juries were looking into suspected international cartel activity.³⁵ The companies subject to the Division's investigations are located on five continents and in over 20 different countries.³⁶ Indeed, the illegal activities themselves may have been even more widespread than that, since investigations have uncovered cartel meetings in over 100 cities in 35 countries, including most countries of Europe and the Far East.³⁷

³² See Gary Spratling, *International Cartel Prosecutions: Antitrust Division Policies Relating to Plea Agreements in International Cases*, Remarks Before the National Institute on White Collar Crime, 27 (Mar. 4, 1999) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/2275.htm>>) (visited Mar. 24, 2000) [hereinafter Spratling, *White Collar Crime*].

³³ See *id.*

³⁴ See *id.*

³⁵ See Gary R. Spratling, *International Cartels: The Intersections Between FCPA Violations and Antitrust Violations*, Remarks Before the American Conference Institute's 7th Annual National Conference on Foreign Corrupt Practices Act (Dec. 9, 1999) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/3981.htm>>) (visited Mar. 24, 2000) [hereinafter Spratling, *International Cartels*].

³⁶ See *id.*

³⁷ See *id.* The Antitrust Division estimates that the cartels it has prosecuted since the beginning of FY 1997 have affected over \$10 billion in U.S. commerce and have cost American businesses and consumers many hundreds of millions of dollars annually. See Spratling, *White Collar Crime*, *supra* note 32, at 27. Some of the most significant cartel investigations have involved vital products such as citric acid, lysine, sodium gluconate (an industrial cleaner), and graphite electrodes (used in steel making). See Spratling, *International Cartels*, *supra* note 35. See also *infra* notes 43-48 and accompanying text. As the current Assistant Attorney General Joel Klein has observed, "[i]nternational cartels typically pose an even greater threat to American business and consumers than do domestic conspiracies because they tend to be extremely broad in geographic scope and amount of commerce affected, as well as highly sophisticated, characterized by precise elaborate agreements among the conspirators. . . ." Testimony Before the Antitrust, Business Rights and Competition Subcommittee, Senate Committee on the Judiciary, Mar. 22, 2000 (visited Mar. 24, 2000) <<http://www.usdoj.gov/atr/public/testimony/4381.htm>>.

The Antitrust Division's increased focus on large foreign cartels has led to a striking increase in the amount of criminal fines assessed. Prior to FY 1997, the highest amount of fines obtained in any year was about \$42 million. See Spratling, *White Collar Crime*, *supra* note 32, at 27. In FY 1997 the Division eclipsed that mark by collecting fines of \$205 million—nearly five times more than any previous year in the Division's history. See *id.* Fines in-

The pattern of recent cartel enforcement can be seen in an examination of four recent rounds of cases - those involving lysine, citric acid, sorbates, and vitamins. In those four investigations, the DOJ found over fourteen companies (including Hoffman-LaRoche, twice) and six individuals from four countries guilty.³⁸ The Division collected nearly \$1.2 billion in fines,³⁹ including a fine of \$100 million imposed on Archer-Daniels-Midland Company.⁴⁰ The prosecution of the individual defendants was a most important feature of these cases.⁴¹ The prosecution established the key deterrent concept, perhaps underemphasized in prior administrations, that individuals who commit sophisticated white-collar crimes such as antitrust violations will also face the prospect of serving real jail time.⁴²

A sorbate cartel investigation involved a class of chemical preservatives used in high moisture foods such as cheese and baked goods. As of July 1999, Eastman Chemical Co. of the United States, Hoechst of Germany, and Nippon Gohsei of Japan each pled guilty to fixing sorbate prices and allocating markets for over seventeen years.⁴³ This rebuts the commonly held notion that cartels tend to fall apart relatively quickly, and suggests instead that they can be quite enduring if they are free to organize and police themselves from overseas sanctuaries. This underscores, of course, the importance of enforcement efforts against multinational collusion.

The most recent cartel prosecution is also the one that has resulted in the largest penalties. Collusion in the vitamin industry raised consumer prices for common nutritional supplements such as vitamins A,

creased again in the following year, to over \$265 million. *See id.* And in FY 1999, fines reached \$1.1 billion. *See Spratling, International Cartels, supra* note 35.

Similarly, average corporate fines have increased, from a little under \$320,000 in FY 1991 to about \$ 12 million in FY 1998, an increase of approximately forty fold. *See Spratling, White Collar Crime, supra* note 32, at 27. Top-end fines have similarly increased, from \$2 million, which six years ago was the largest fine ever imposed for a single Sherman Act violation to \$500 million assessed against Hoffman-La Roche in May of 1999. *See Spratling, International Cartels, supra* note 35. Strikingly, of the roughly \$470 million in fines obtained in FY 1997-1998, nearly \$440 million, or more than 90 percent of the total, was in connection with multinational cartel activity. *See Spratling, White Collar Crime, supra* note 32, at 27.

³⁸ *See* 1999 DOJ ANNUAL REPORT, *supra* note 11, at 7.

³⁹ *See id.*

⁴⁰ *See id.*

⁴¹ *See* Department of Justice, Press Release, *Former Top ADM Executives, Japanese Executive, Indicted in Lysine Price Fixing Conspiracy*, Dec. 3, 1996 (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1996/573at.htm>.

⁴² ADM executives are serving between 24 and 30 months of jail time for their involvement in the lysine cartel. *See* United States v. Andreas, No. 96 CR 762, 1999 U.S. Dist. LEXIS 11166, at *46-*50 (N.D. Ill. July 15, 1999).

⁴³ *See* Department of Justice, Press Release, *Japanese Chemical Company Third to be Charged in 17-Year International Price Fixing Conspiracy*, July 14, 1999 (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1999/2560.htm>.

B₂, beta carotene, and vitamin premixes that are used to enrich breakfast cereals and many other processed foods. The Swiss pharmaceutical giant F. Hoffman-La Roche pled guilty and paid a fine of \$ 500 million for leading a worldwide conspiracy to fix prices and to allocate markets.⁴⁴ Attorney General Reno noted that this was not only a record fine in an antitrust case, "but it is the largest fine the Justice Department has ever obtained in any criminal case."⁴⁵ The German firm, BASF, pled guilty and paid a fine of \$ 225 million.⁴⁶ More recently, in September 1999, three Japanese firms pled guilty and paid fines totaling \$137 million.⁴⁷ Equally important, individual foreign executives were also prosecuted, agreeing to pay six-figure fines and to serve substantial U.S. prison terms of three or five months.⁴⁸

B. MERGER ENFORCEMENT

Mergers have dominated civil antitrust enforcement during the past seven years.⁴⁹ Some of the largest mergers in U.S. history are currently being evaluated by federal antitrust enforcers, mergers that impact millions of consumers and the products they purchase on a daily basis. Compared with a decade earlier, the agencies have challenged more mergers in the 1990s than they did in the 1980s. The following two tables shows FTC merger enforcement actions during the periods of FY 1983-88 and FY 1993-98.⁵⁰

⁴⁴ See Department of Justice, Press Release, *F.Hoffman-LaRoche and BASF Agree to Pay Record Criminal Fines for Participating in International Vitamin Cartel*, May 20, 1999 (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1999/2450.htm>.

⁴⁵ *Id.*

⁴⁶ *See id.*

⁴⁷ See Department of Justice, Press Release, *Three Japanese Companies Agree to Plead Guilty, Pay Criminal Fines, for Participating in International Vitamin Cartel*, Sept. 9, 1999 (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1999/3659.htm>.

⁴⁸ The court, however, retains the ultimate authority to determine the sentence to be imposed under the sentencing guidelines, and to determine whether to accept any proposed plea arrangements. *See generally* U.S. SENTENCING GUIDELINES MANUAL (1995).

⁴⁹ The number of mergers reported to the FTC and the Department of Justice under the Hart-Scott-Rodino (HSR) Act, 15 U.S.C. §§ 1311-1314 (1999), has almost tripled since the beginning of the Clinton Administration: from 1,846 transactions in FY 1993, to an incredible 4,728 transactions in FY 1998. *See* FEDERAL TRADE COMMISSION, ANNUAL REPORT TO CONGRESS (1998) (visited Mar. 24, 2000) <<http://www.ftc.gov/bc/hsr/98annrpt/hsr98annual.htm>>. Fiscal Year 1999 filings closely approximate FY 1998 record pace. *See* Richard G. Parker, Report from the Bureau of Competition, Prepared Remarks before the American Bar Ass'n, Spring Meeting, Washington, D.C, Apr. 7, 2000 (transcript available at <<http://www.ftc.gov/speeches/other/rparkerpringaba00.htm>>) (visited Apr. 18, 2000) [hereinafter Parker, Report]. Equally important is that the value of transactions has increased in more than seven times from about \$200 million in fiscal year 1993 to over \$1.436 billion in fiscal year 1998. *See id.*

⁵⁰ The information for these tables was compiled from the respective years of the Federal Trade Commission's Annual Reports.

FTC MERGER ENFORCEMENT, FY 1983-88

Fiscal Year	Transactions Filed	Enforcement Actions	Ratio (E/T)
1983	1093	4	.0036
1984	1340	9	.0067
1985	1603	13	.0081
1986	1949	7	.0036
1987	2533	12	.0047
1988	2746	23	.0084

FTC MERGER ENFORCEMENT, FY 1993-99

Fiscal Year	Transactions Filed	Enforcement Actions	Ratio (E/T)
1993	1589	21	.0132
1994	1846	28	.0152
1995	2305	43	.0186
1996	2816	27	.0096
1997	3702	27	.0073
1998	4728	33	.0070
1999	4642	30	.0065

The mere number of enforcement actions does not fully depict the differences in enforcement. Many transactions challenged during the 1980s involved relatively small markets, or small transactions. The cases challenged in the last seven years include some of the largest mergers in history, including Staples/Office Depot, Lockheed/Martin Marietta, and SBC/Ameritech.

The general increase in absolute numbers of enforcement actions is attributable in part to the increase in merger activity. But there has also been a general increase in the relative frequency of enforcement actions during the 1990s compared to the 1980s. These distinct changes in merger enforcement since the 1980s can be attributed to the fact that the Merger Guidelines⁵¹ have been applied with greater confidence in their analytical value and consumer benefit. The following discussion focuses on a number of important developments in merger enforcement during the past seven years. The six areas with the most significant changes are (1) the use of unilateral effects analysis, (2) innovation markets, (3) network mergers, (4) vertical mergers, (5) potential competition analysis, and (6) efficiency analysis.

⁵¹ DEPARTMENT OF JUSTICE & FEDERAL TRADE COMMISSION, 1992 HORIZONTAL MERGER GUIDELINES, § 2.21 (1992) reprinted in 4 Trade Reg. Rep. (CCH) ¶13,104 [hereinafter 1992 HORIZONTAL MERGER GUIDELINES].

1. *Unilateral Effects Analysis in Mergers*

Merger enforcement in the past several years has devoted increased attention to the unilateral effects analysis⁵² because of the potential for a firm resulting from the merger to act unilaterally to reduce output and raise price. For example, if firms sell differentiated products or are spatially dispersed, individual sellers compete more directly with some rivals than with others, and a merger of firms selling particularly close substitutes may enable this merged firm to exercise some degree of market power unilaterally. While the concept is not new - it was recognized in the 1982 Merger Guidelines⁵³ - the increased attention to it in recent enforcement actions is significant. This renewed attention can be attributed to two developments. First, the advances in the theoretical literature provide a better understanding of how unilateral effects arise.⁵⁴ In addition, the advances enable the agencies to model unilateral effects more precisely. Second, there is a greater availability of data, such as those derived from point-of-sale scanners, that provide insight into the products that consumers regard as close substitutes, and that exercise a particularly significant constraint on each other's prices.⁵⁵

The concept of unilateral effects is perhaps best illustrated by the FTC's challenge of the proposed merger of Staples, Inc. and Office Depot, two of the three leading office supply superstore chains in the United States.⁵⁶ The two firms together operated about 1,000 superstores and competed head-to-head in numerous metropolitan areas across the country. In 15 major metropolitan areas, including Washington, D.C., Baltimore, San Diego and Tampa-St. Petersburg, Staples and Office Depot were the only superstores, and in 27 other metropolitan areas, the two firms had only one other superstore competitor, Office Max.⁵⁷ The merger also would have eliminated significant future competition be-

⁵² Anticompetitive effects from mergers may occur in two ways. Either the remaining firms in the relevant market are so few that their incentives and their ability to collude are enhanced, or the merged firm will be so dominant that it can unilaterally increase prices or reduce output or innovation. *See id.*

⁵³ *See* 1982 MERGER GUIDELINES, *supra* note 5, at § III.C.1(c) ("Where products in a relevant market are differentiated or sellers are spatially dispersed, individual sellers usually compete more directly with some rivals than with others. . . . If the products or plants of the merging firms are particularly good substitutes for one another, the Department is more likely to challenge the merger"). Similar language is contained in the 1992 HORIZONTAL MERGER GUIDELINES, *supra* note 51.

⁵⁴ *See* Jonathan B. Baker, *Unilateral Competitive Effects Theories in Merger Analysis*, 11 ANTITRUST, Spring 1997, at 21.

⁵⁵ *See id.*

⁵⁶ *See* FTC v. Staples, Inc., 970 F. Supp. 1066 (D.D.C. 1997).

⁵⁷ *See* Robert Pitofsky, An Overview of Antitrust Enforcement, Prepared Statement Before House of Representatives Committee on the Judiciary (Nov. 5, 1997) (visited Mar. 24, 2000) <<http://www.ftc.gov/os/1997/9711/oversigh.htm>> [hereinafter Pitofsky, Antitrust Enforcement].

tween the two firms in areas where one of them was planning to enter the other's territory. However, it was far from obvious at the outset that the merger would pose competitive problems, because the products sold by Staples and Office Depot were available in numerous other stores. The issue was whether those alternative sources would be an effective constraint on post-merger price increases in localities where Staples and Office Depot competed head-to-head.

The evidence revealed that no other stores offered the same combination of price, convenience, and other attributes as these two firms. Moreover, the pricing evidence showed that in localities where Staples and Office Depot competed head-to-head, their prices were significantly lower than in localities where only one of the firms was present.⁵⁸ In markets where Staples and Office Depot did not compete, the other retailers did not supply the level of price competition that existed between two or more superstores.⁵⁹ That evidence demonstrated that those other retailers of office supplies would not prevent Staples from increasing prices in markets where competition from Office Depot was eliminated. The evidence thus showed that Staples and Office Depot were particularly close substitutes in a market with numerous and diverse types of office supply retailers.⁶⁰

The FTC's case argued both a narrow office supplies market, in which the transaction would result in a merger-to-monopoly in many cities, and unilateral effects within a broader market. The district court found a narrow market consisting of office supply superstores, using both the 5-10% test of the 1992 Horizontal Merger Guidelines⁶¹ and the Supreme Court's multi-faceted market definition approach of *Brown Shoe Co. v. United States*⁶² and its progeny. While *Brown Shoe* employed the Court's multi-faceted approach to analyze "submarkets",⁶³ the court in *Staples* used the *Brown Shoe* market definition approach⁶⁴ to assess the nature and extent of the competitive relationship between the

⁵⁸ See *Staples*, 970 F.Supp. at 1075-78.

⁵⁹ See *id.*

⁶⁰ See *id.*

⁶¹ See *id.* at 1076 n.8 (referring to the 1992 HORIZONTAL MERGER GUIDELINES, *supra* note 51).

⁶² 370 U.S. 294, 325 (1962) (stating that, "[t]he outer boundaries of a product market are determined by the reasonable interchangeability of use [by consumers] or their cross-elasticity of demand between the product itself and substitute for it.")

⁶³ See *id.* Economists criticize the submarket approach, noting that any submarket also meets the test as a market and should be recognized as such. Even though *Brown Shoe* used the submarket approach, now out of favor, it remains the seminal case in the relevant market analysis since, after all, a submarket is really a market.

⁶⁴ See *Staples*, 970 F. Supp. at 1074.

merging parties' products and compare that to the competition they face from other firms.⁶⁵

Much of the FTC's merger enforcement during the past several years has applied a unilateral effects theory. While skeptics of the approach may contend that it is simply an attempt to derive narrower markets and higher concentration levels, that is hardly the case. In many respects, in the presence of apparent demand-side alternatives, it can be more difficult to show that two products are particularly close substitutes, than it would be to establish a broader product market. The analysis is intensely fact-based. Despite its complexities, the unilateral effects analysis is an important part of merger analysis, and careful application of the theory can yield significant benefits for consumers. The FTC's enforcement action in *Staples*, for example, saved consumers an estimated \$1.1 billion over five years.⁶⁶

2. Innovation Markets

Antitrust enforcement in recent years also has paid closer attention to mergers that substantially threaten to reduce competition in the area of research and development. Innovation has long been recognized as a major source of welfare gains.⁶⁷ The introduction of "innovation markets"⁶⁸ to merger analysis reflects an increased appreciation that under certain circumstances a substantial reduction in innovation rivalry through a merger can be just as troublesome as the loss of other forms of competition. The renewed focus on innovation and research and development (R&D) competition is probably attributable to several factors. First, the 1995 Intellectual Property Guidelines⁶⁹ drew attention to the concept of innovation markets. Second, there has been a substantial amount of recent merger activity in certain markets where antitrust enforcement may be particularly important in preserving R&D competition, such as pharmaceuticals and defense. Third, there is an increased appreciation of the importance of preserving incentives for strong rivalry in the race to produce new and improved products in many key markets.

⁶⁵ The court issued a preliminary injunction against the merger, *Staples*, 970 F. Supp. at 1093, and the parties then abandoned the transaction.

⁶⁶ See Pitofsky, Antitrust Enforcement, *supra* note 57.

⁶⁷ See Thomas N. Dahdoun & James F. Mongoven, *The Shape of Things to Come: Innovation Market Analysis in Merger Cases*, 64 Antitrust L.J. 405 (1996).

⁶⁸ An innovation market "consists of the research and development directed to particular new or improved processes, and the close substitutes for that research development." U.S. DEPARTMENT OF JUSTICE AND FEDERAL TRADE COMMISSION, 1995 FEDERAL ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY, § 3.2.3 (1995), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,132 (1995) [hereinafter INTELLECTUAL PROPERTY GUIDELINES]. These guidelines are more readily accessible at (visited Mar. 24, 2000) <<http://www.usdoj.gov/atr/public/guidelines/ipguide.htm>>.

⁶⁹ *Id.*

Research, development, and innovation, are critically important to both the domestic and international competitiveness of U.S. firms. Moreover, R&D competition is critically important not only for saving dollars in the purchase of new products, but also for saving lives and ensuring our national security.

The antitrust agencies have intervened in innovation market transactions under very narrow circumstances - namely, where only a few firms possess the specialized assets or characteristics needed to compete successfully in the market, or where a merger is likely to result in a substantial loss of R&D competition. Two cases illustrate the point, *Ciba-Geigy Ltd.*,⁷⁰ and *United States v. Lockheed Martin / Northrop Grumman*.⁷¹

In the 1997 *Ciba-Geigy/Sandoz* case, the FTC challenged a \$63 billion merger of two pharmaceutical giants that threatened to produce a monopoly in key technologies used in the development of gene therapy products, which show substantial promise for the treatment of various cancers and other medical conditions.⁷² The pool of potential competitors was very limited because the merging firms controlled critical patents. The merger therefore would have diminished both the incentives and the ability of other firms to develop competing products.⁷³ Because of the patent portfolios of Ciba-Geigy and Sandoz, competitors would be blocked from commercial development. The case was resolved with a consent order that preserved competition in this important innovation market, in part by requiring the licensing of certain technology and patent rights to a third firm (Rhone-Poulenc Rorer) so that it would be in a position to compete with the merged firm.⁷⁴ According to *Business*

⁷⁰ 123 F.T.C. 842 (Mar. 24, 1997). The first innovation market case was *General Motors*. See *United States v. General Motors Corp.*, No. 93-530 (D. Del filed Nov. 16, 1993) (consent judgment). This 1993 case was the first application of the current innovation market approach by the Department of Justice. The DOJ opposed the merger of the Allison Transmission Division of General Motors and ZF Friedrichshafen, AG, essentially the world's only manufacturers and innovators of medium and heavy automatic transmissions for trucks, buses, and other commercial and military vehicles. The complaint alleged that the GM-ZF combination would diminish competition not only in the production and sale of current products but also in a worldwide innovation market for the technological design, development and production of automatic transmissions for heavy vehicles. Other FTC cases alleging an innovation market include *American Home Products*, 119 F.T.C. 217 (Feb. 14, 1995) (involving merger between two of three developers of rotavirus vaccines); *Sensormatic Electronics Corp.*, 119 F.T.C. 520 (Apr. 18, 1995) (involving research and development of disposable labels for a new type of electronic article surveillance system).

⁷¹ The complaint for this 1998 action is available at (visited Mar. 24, 2000) <<http://www.usdoj.gov/atr/cases/f1600/1609.htm>>. The transaction was subsequently abandoned without public explanation. See Department of Justice, Press Release, (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1998/1830.htm>.

⁷² See 123 F.T.C. 842, at ¶¶ 8-9.

⁷³ See *id.*, at Complaint ¶ 31.

⁷⁴ See *id.*, at Order ¶ IX.

Week, the FTC's enforcement action "shows a new savvy among trust-busters about high-tech competition."⁷⁵

In *Lockheed Martin / Northrop Grumman*, the DOJ challenge to the proposed acquisition of Northrop Grumman by Lockheed Martin was based to a large extent on the loss of innovation competition in a number of defense industry markets where Lockheed and Northrop were two of a very few, and in several cases the only viable market participants.⁷⁶ The DOJ considered the loss of innovation rivalry to be a particularly significant consequence of the transaction, because a major focus of competition in these markets is the development of next-generation and leapfrog technologies.⁷⁷ The transaction was ultimately abandoned by the parties.

3. Network Mergers

Another area of growing analytic increased importance in recent years is the recognition of network effects in certain industries. Such industries are characterized by products where the value of the product to a user increases with the number of users. A common example is the telephone network, which become more useful as the number of network users increases. Like economies of scale, network effects generally benefit consumers. However, the presence of network effects may also mean that entry in a market is difficult, or that exclusionary conduct is more likely to pay off, just as would be the case with more traditional economies of scale. While network effects are not a new theory of competitive harm, in recent years the antitrust agencies have been more attentive to mergers in the network industries that may result in those kinds of adverse effects.

In the 1980s, the antitrust enforcers took a very lax attitude toward network mergers. They thought that entry into network markets would be relatively easy since many networks consisted primarily of computers, and replicating the back office aspects of networks⁷⁸ seemed relatively

⁷⁵ *A Booster Shot for Gene Therapy*, Bus. Wk., Jan. 20, 1997, at 92.

⁷⁶ See *United States v. Lockheed Martin Corp.*, DOJ Complaint, at 2 (visited Mar. 24, 2000) <<http://www.usdoj.gov/atr/cases/f1600/1609.htm>>. The complaint alleged that Lockheed would attain a monopoly position in airborne early warning radar, electro-optical missile warning systems, directed infrared countermeasures systems, the SQQ-89 antisubmarine warfare combat system, and fiber-optic towed decoys. In the markets for high performance fixed-wing military aircraft, on-board radio-frequency countermeasures, stealth technology, and remote mine-hunting systems, the acquisition would have reduced the number of competitors from three to two. See *id.*

⁷⁷ See Constance K. Robinson, *Leap-Frog and Other Forms of Innovation*, Address before the American Bar Association (June 10, 1999) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/2482.htm>>) (visited Mar. 24, 2000).

⁷⁸ Network support functions are usually "scalable," that is the back office functions can support more and more products without much expansion. For instance, the billing and accounting back office of an ATM network can be set up to support a wide range of ATM machines.

simple. For example, the regulators approved mergers of ATM networks because they believed that entry into the back office operations was relatively easy. However, that position was misguided because one key aspect of a network is its relationships with customers and suppliers, an attribute that cannot be easily duplicated.⁷⁹ Nor are computers necessarily a defining characteristic of networks.

The more sensitive view of the potential effects of network mergers is shown by the enforcement actions involving the *Rite Aid/Revco* merger⁸⁰ and the *MCI/Worldcomm* merger.⁸¹ In the *Rite Aid/Revco* action the FTC challenged the proposed merger of the two largest retail pharmacy chains in the United States. The relevant market of concern was the sale of pharmacy services to pharmacy benefit managers ("PBM") - entities that operate pharmacy benefit plans. PBMs buy retail distribution services from pharmacies and sell them to health insurance plans and employer groups. PBMs contract with chains and independent pharmacies to organize a network of participating pharmacies. A PBM needs to have widespread geographic coverage to be credible to their customers - the insurance plans and employer groups. In many markets, it would be feasible to obtain such geographic coverage with either the Rite-Aid or Revco pharmacy chain serving as the "anchor" to the network, possibly in combination with smaller chains or independents, but obtaining wide coverage without either major chain would be either impossible or extremely costly. Before the proposed merger, the pharmacies of Rite-Aid and Revco competed to be the anchor of these PBMs. If one firm priced its services too high, a PBM could use the other chain in combination with other pharmacies. A merger of Rite-Aid and Revco would eliminate that option and allow the merged firm to extract much more favorable terms from the PBMs. In turn, this would have had significant effects on the PBMs' ultimate customers, the employees and other insured who depend upon their health plans for affordable coverage of pharmaceuticals.⁸² The FTC challenged

⁷⁹ A prime example of this kind of error was the merger of the MAC and Cashstream ATM networks, which was approved in 1988, but ultimately led to a Justice Department monopolization suit in 1994. See David A. Balto, *The Murky World of Network Mergers: Searching for the Opportunities for Network Competition*, 42 ANTITRUST BULLETIN 793, 803-08 (1997).

⁸⁰ No. 961 0020 (FTC, 1996). The FTC authorized the filing of a motion for preliminary injunction on Apr. 17, 1996. See FTC, Press Release, *FTC Will Seek to Block Rite Aid/Revco Merger* (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1996/9604/riterevc.htm>>.

⁸¹ *In re MCI Communications Corp.*, FCC No. 98-225 (Sept. 14, 1998) (order) (visited Apr. 27, 2000) <http://www.fcc.gov/Bureaus/Common_Carrier/Orders/1998/fcc98225.txt>. For a complete look at all materials related to the merger, see (visited Apr. 27, 2000) <<http://www.fcc.gov/ccb/Mergers/Worldcom/welcome.html>>.

⁸² See Jonathan Baker, *Unilateral Competitive Effects Theories in Merger Analysis*, Remarks before the American Bar Association, Section of Antitrust Law, Orlando, Florida (Aug.

this merger on the basis of network effects, and the proposed merger was subsequently abandoned.⁸³

The constant intellectual ferment in the computer industry has spawned new industries that have themselves become important centers of commerce in a short time period. The most important of these is the Internet. Already, even in its infancy, it has become established as a potentially huge market, and the efficacy of antitrust oversight at this point may determine the level of competition in this industry for many years to come. The most significant Internet antitrust enforcement action to date was the Justice Department's investigation of the merger between MCI and WorldCom, the two companies that together own over fifty percent of the Internet backbone market.⁸⁴

The Department's case centered around the relevant product market and barriers to entry into the market. The market was defined as limited to Internet backbone services - which is essentially the transmission of traffic between all Internet users - because retail services were not effective substitutes. Internet transmission providers are dependent upon one another for interconnection in order to offer consumers near universal access to Internet service providers and customers. After the proposed acquisition, MCI and WorldCom would have controlled the majority of traffic, and would have had a substantially larger share than the next largest Internet backbone provider. The combined firm would have enjoyed significant network externalities, and would have leverage to dictate the terms, conditions, and pricing of interconnection with other Internet backbone providers. Smaller backbone providers, particularly new entrants, would have been dependent on interconnection with MCI in order to effectively compete. This asymmetric relationship would have left small providers without any leverage and subject to whatever terms and conditions MCI imposed. As a consequence, MCI would have had the incentive, ability, and power to increase the costs to or degrade the quality of interconnection for smaller rivals, and once it did, entry barriers would have been solidified.

6, 1996) (transcript available at <<http://www.ftc.gov/speeches/other/unilat61.htm>>) (visited Apr. 27, 2000).

⁸³ See FTC, Press Release, *FTC Will Seek to Block Rite Aid/Revco Merger* (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1996/9604/riterevc.htm>>; FTC, Press Release, *Rite Aid Abandons Proposed Acquisition of Revco After FTC Sought to Block Transaction* (Apr. 24, 1996) (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1996/9604/ritenogo.htm>>.

⁸⁴ See Constance K. Robinson, *Network Effects in Telecommunications Mergers, MCI WorldCom Merger: Protecting the Future of the Internet*, Remarks before the Practising Law Institute, San Francisco, CA (Aug. 23, 1999) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/3889.htm>>) (visited Apr. 27, 2000).

The settlement⁸⁵ required MCI to sell Internet MCI to Cable & Wireless plc of Great Britain for an estimated \$1.75 billion, making it the largest divestiture of a company in merger history.⁸⁶

4. *Revitalization of Vertical Merger Enforcement*

Scrutiny of vertical mergers⁸⁷ experienced a renewal in the 1990s after a decade in which the government did not bring a single case. According to economic theories, some vertical mergers can be harmful to competition⁸⁸ even though most vertical mergers generally are either procompetitive or at least competitively neutral. However, the revival of vertical merger enforcement is not a return to the often-criticized foreclosure theories that prevailed in the 1960s and early 1970s. The cases in that period tended to focus on loss of business opportunities for non-integrated firms, and the loss of even a relatively small share of the market was considered harmful.⁸⁹ In contrast, current vertical merger enforcement evaluates whether a transaction will enable the merged firm to harm competition, rather than competitors, through various kinds of strategic behavior.⁹⁰

Recent vertical merger enforcement has focused on several theories. One theory is that a merged firm with substantial control over an important input into the upstream or downstream market, will be able to harm competition by substantially impeding its rivals' market access at either the upstream or downstream levels. A related theory is that the merged firm, again, with substantial control over an important input into the upstream or downstream market, will be able to harm competition by raising its upstream or downstream rivals' costs of doing business. Both of these situations involve a vertical merger that threatens to create or

⁸⁵ See *In re MCI Communications Corp.*, FCC No. 98-225, ¶ 227 (Sept. 14, 1998) (order) (visited Apr. 27, 2000) <http://www.fcc.gov/Bureaus/Common_Carrier/Orders/1998/fcc98225.txt>.

⁸⁶ See *id.*

⁸⁷ See *supra* note 7.

⁸⁸ See, e.g., Michael Riordan & Steven Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 ANTITRUST L.J. 513, 515, 527-64 (1995); Thomas Krattenmaker & Steven Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over Price*, 96 YALE L.J. 209, 228 (1986).

⁸⁹ See, e.g., *Brown Shoe Co. v. United States*, 370 U.S. 294, 328-30, 334 (1962).

⁹⁰ See M. Howard Morse, *Vertical Mergers: Recent Learning*, 53 BUS. LAW, 1217; Robert Pitofsky, *Vertical Restraints and Vertical Aspects of Mergers – A U.S. Perspective*, Remarks before the Fordham Corporate Law Institute, 24th Annual Conference on International Antitrust Law and Policy (Oct. 16, 1997) (transcript available at <<http://www.ftc.gov/speeches/pitofsky/fordham7.htm>>) (visited Apr. 27, 2000); Richard G. Parker, *Trends in Merger Enforcement and Litigation*, Remarks before Briefing for Corporate Counsel, Washington, D.C. Sept. 16, 1998) (transcript available at <<http://www.ftc.gov/speeches/other/parker.htm>>) (visited Apr. 27, 2000).

tighten a potential bottleneck somewhere in the chain of production or distribution.

Consider a firm at the upstream level that sells a product to a downstream firm, which in turn adds value through manufacturing or services, and sells its product to the ultimate consumer or user. A bottleneck transaction can have adverse effects at two levels. First, the acquisition can worsen competitive conditions at the downstream level by raising the costs of inputs for competitive rivals or by blocking potential entry - the force that we often rely on to keep markets competitive. Thus, the transaction can create or increase market power in the downstream merger partner through its control of inputs to competitors or potential competitors. Second, a bottleneck acquisition can disadvantage competitors or potential competitors at the upstream level, by impeding their access to customers at the downstream level. Therefore, the vertical merger may enable the parties at either downstream and upstream levels to increase their market power and protect their turf against new competitors. Third, competitive harms can result when a vertically integrated firm acts as both a supplier to, and competitor of, certain firms. The harm emerges when the merged firm, for competitive purposes, misuses commercially sensitive information that it obtains during its course of dealings with customers who are also its competitors at the downstream level.⁹¹ Cases such as *Time Warner Inc.*,⁹² and *Merck & Co, Inc.*,⁹³ illustrate the application of these theories.⁹⁴ As suggested by the length of the discussion, these tend to be complex cases.

a. Time Warner

Time Warner Inc.'s acquisition of Turner Broadcasting System raised concerns regarding bottleneck foreclosure and raising rivals' costs. The transaction involved three major firms in the cable television industry creating the nation's largest media company. Time Warner is a major producer of video programming for cable distribution, including the popular channels, HBO and Cinemax, as well as a major cable systems operator through Time Warner Entertainment, a joint venture with U.S. West.

⁹¹ It is not uncommon in vertically integrated companies for one part of the firm to have a business relationship with a customer (or other entity) that is a competitor of a downstream (or upstream) business within the integrated firm. The nature of that business relationship may require access to some competitively sensitive information that the third party would not want to be released to competitors.

⁹² No. C-3709, 1997 FTC LEXIS 13, at *1 (FTC, Feb. 3, 1997).

⁹³ No. C-3853, 1999 FTC LEXIS 18, at *1 (FTC., Feb. 18, 1999).

⁹⁴ See also *In re Silicon Graphics, Inc.*, 128 F.T.C. 928 (Nov. 14, 1995) (involving access into the highly specialized entertainment industry's graphics software market); *In re PacifiCorp*, No. 971-0091, 1998 F.T.C. 17 (Feb. 18, 1998) (merger between a generator of electricity and a supplier of coal to generating plants would result in increased wholesale and retail electricity costs).

Turner Broadcasting, an owner of CNN, TNT and TBS, is another major producer of video programming. TeleCommunications, Inc. (TCI), the nation's largest cable systems operator, was involved through a substantial stock interest in Turner, which would have been converted to a significant stock interest in Time Warner.⁹⁵ The proposed transaction would have substantially increased the level of vertical integration in the industry. At the programming production level, the transaction would have combined two of the leading producers of video programming sold to multi-channel distributors such as cable systems. Together, Time Warner and Turner accounted for about 40% of all video programming sold to multichannel distributors in the United States.⁹⁶ At the multi-channel distribution level, the transaction would link Time Warner's cable operation, which was already the second largest distributor of cable television in the United States, and TCI, which had a substantial minority interest in Turner that would be converted into an interest in Time Warner after the merger. The acquisition would add to the existing vertical integration by completely integrating Turner's video programming business with Time Warner's cable distribution business, and by creating a link, by ownership and by contract, between Time Warner's programming business and TCI's cable distribution business.⁹⁷

The FTC found that this merger was likely to restrict access to both video programming for firms that distribute multi-channel video programming to households and other subscribers, and to producers of video programming who depend on multi-channel distribution.⁹⁸ Such restrictions could have been imposed not only in absolute terms, but also in terms of the relative cost of access among competing firms.

⁹⁵ TCI operates in about 27% of all cable television households. See FTC Complaint, at ¶ 32, No. C-3709 (Feb. 7, 1997) (visited Apr. 27, 2000) <<http://www.ftc.gov/os/1996/9609/twcmplt.htm>>.

⁹⁶ See *In re* Time Warner, No. C-3709, 1997 FTC LEXIS 13, at *14.

⁹⁷ See *id.* at *17-*19. The latter would happen because TCI and its subsidiary Liberty Media had a 24% interest in Turner Broadcasting that would be converted to a 7.5% fully diluted equity interest in Time Warner, and TCI would have a right of first refusal to acquire the 7.4% interest in Time Warner that Ted Turner would receive as part of the deal. Thus, TCI potentially could own 15% of Time Warner, and more if it chose to make additional purchases of the stock. See *id.* at *10-*11. In addition, as another part of the deal, TCI would enter into a mandatory carriage agreement (the "Programming Service Agreement") with Time Warner, which would require TCI to carry four of Turners top cable channels for 20 years, but at preferential prices. See *id.* at *11-*12.

⁹⁸ Similar concerns, involving different markets, lead to the Commission's earlier challenge of the proposed acquisition of Paramount Communications, a large movie maker, by a group of companies involved in video programming and distribution, including QVC Network, Inc. ("QVC"), Liberty Media Corporation ("LMC") (collectively, the "QVC group"), and Tele-Communications Inc. ("TCI"). See *In re* Tele-Communications, Inc., No.941-0008, 1993 FTC LEXIS 318, at *1 (FTC, Nov. 11, 1993). QVC was ultimately unsuccessful in its bid for Paramount, therefore, the consent agreement was not finalized.

The acquisition would make it more difficult for other producers of video programming to gain access to the distribution market because Time Warner and TCI, through its financial interest in Time Warner, would have a natural inclination to favor their own programming over a competitor's. Since Time Warner and TCI together controlled around 41% of the distribution market, a competing video programmer would find it difficult to achieve profitable distribution.⁹⁹ In addition, it would have been difficult for a competitor to have a financially viable network that could offer meaningful competition to Time Warner and Turner, especially with network programming services that have high sunk costs, such as news channels.¹⁰⁰

Access to video programming was also a concern because Time Warner and TCI could block entry into their distribution markets or raise their rivals' costs through their control of a large portion of video programming. Time Warner and Turner accounted for over 40% of the video programming in the United States, including several popular channels such as CNN, TNT and HBO.¹⁰¹ A potential entrant, such as a telephone or utility company or a company that sees an opportunity to overbuild¹⁰² a Time Warner or TCI market with another cable operation, could have its entry impeded if it cannot gain access to those "must have" channels at non-discriminatory prices. Likewise, an existing competitor such as a direct satellite broadcast service could have its input costs raised above competitive levels. Moreover, even in markets where Time Warner and TCI do not have cable operations, the horizontal combination of the Time Warner and Turner video programming businesses would give Time Warner the power to raise prices unilaterally or condition the sale of marquee channels on the purchase of other channels that the service provider may not want.¹⁰³ The FTC dealt with these concern by imposing a number of conditions on the transaction that were

⁹⁹ See *In re Time Warner*, FTC Complaint, No. C-3709 (Feb. 7, 1997) (visited Apr. 27, 2000) <<http://www.ftc.gov/os/1996/9609/twcmplt.htm>>.

¹⁰⁰ See *In re Time Warner*, No. C-3709, 1997 FTC LEXIS 13, at *15. Development of alternative programming also would be discouraged by TCI's long-term carriage arrangement with Time Warner. See *id.* at *11-*12. That carriage agreement would lessen TCI's incentives to sign up better or less expensive alternatives to the Time Warner programming than those committed under contract. The mandatory carriage commitment also reduced TCI's ability to carry alternative services, because current cable distribution is capacity-constrained to a large extent. TCI might find it difficult to add new channels unless some existing programming is dropped or additional capacity is added through new technology or higher-capacity transmission lines.

¹⁰¹ See *In re Time Warner*, FTC Complaint, at ¶ 31, No. C-3709 (Feb. 7, 1997) (visited Apr. 27, 2000) <<http://www.ftc.gov/os/1996/9609/twcmplt.htm>>.

¹⁰² An overbuild is a situation in which two or more cable companies serve the same geographic market.

¹⁰³ See *In re Time Warner*, No. C-3709, 1997 FTC LEXIS 13, at *44-*45.

designed to control the specific mechanism by which competitive harm could occur.

b. Merck & Co., Inc.

This case involved the acquisition by Merck, a leading pharmaceutical manufacturer, of Medco, the nation's largest pharmacy benefits manager ("PBM").¹⁰⁴ As middlemen between pharmaceutical companies and managed care plans, PBMs provide a variety of services including sophisticated computerized claims processing, drug utilization review, pharmacy network administration, mail-order prescription services and formulary services that include aggressive rebate negotiation with manufacturers.¹⁰⁵ A drug "formulary" is a list of drugs that PBMs give to pharmacies, physicians, and third-party payers to guide them in prescribing and dispensing prescriptions to health plan beneficiaries. According to the complaint outlining the Commission's charges, Medco negotiates with pharmaceutical manufacturers, including Merck, concerning placement of drugs on the Medco formulary. Medco also negotiates rebates, discounts, and prices that Medco's PBMs pay for pharmaceutical products. The FTC's investigation revealed that post-merger, Medco had given favorable treatment to Merck drugs, and in some cases consumers had been denied access to the drugs of competing manufacturers.¹⁰⁶ In addition, the merger made it possible for Medco to disclose to Merck the sensitive pricing information of Merck's competitors, thereby fostering collusion among drug manufacturers.¹⁰⁷

The FTC's complaint charged that the acquisition of Medco by Merck may result in exclusion of other manufacturer's products from Medcos formularies; enhance the chances for collusion and other illegal anticompetitive conduct; eliminate Medco as an independent negotiator of pharmaceutical prices with manufacturers; reduce other manufacturers' incentives to develop innovative pharmaceuticals; and increase the prices and diminish the quality of the pharmaceuticals available to consumers.¹⁰⁸

¹⁰⁴ See *In re Merck & Co.*, No. C-3853, 1999 FTC LEXIS 18, at *1 (FTC., Feb. 18, 1999). For more information on PBMs, see also *supra* notes 82-84 and accompanying text. For an earlier case of the same type involving Eli Lilly's acquisition of the PBM business of McKesson Corporation, see *In re Eli Lilly & Co.*, 130 F.T.C. 243 (1995).

¹⁰⁵ See David A. Balto, *A Whole New World?: Pharmaceutical Reforms to the Managed Care Revolution*, 52 *FOOD & DRUG L.J.* 83 (1997).

¹⁰⁶ See FTC, Press Release, *Merck Settles FTC Charges that its Acquisition of Medco Could Cause Higher Prices and Reduced Quality for Prescription Drugs*, Aug. 27, 1998 (visited Apr. 27, 2000) <<http://www.ftc.gov/opa/1998/9808/merck.htm>>.

¹⁰⁷ See *In re Merck & Co.*, 1999 FTC LEXIS 18, at *5.

¹⁰⁸ See *id.* The consent order against Merck requires Merck-Medco to maintain an "open formulary" - one that includes drugs selected and approved by an independent Pharmacy and Therapeutics ("P&T") Committee. See *id.* at *11-*12. This committee consists of physicians

A noteworthy observation is that many vertical mergers occur in industries in which rapid changes are taking place. Ideally, rapid technological change will prevent a firm from exercising market power because a new competitor with a new technology will soon take its place. Nevertheless, in some situations, a merger can create a roadblock to technological change. A transaction creating a bottleneck may prevent a new technology from reaching the market if a bottleneck cannot be easily expanded or circumvented. For example, the FTC would not be concerned about foreclosure of new entry if an entrant could easily enter at either the upstream and downstream levels.¹⁰⁹ However, entry may not be easy in some markets that have network characteristics, or if there is a large installed base and it would be expensive for customers to switch to a new product.

5. *Potential Competition Mergers*

Antitrust enforcement in the last several years has also rekindled interest in mergers that may eliminate potential competition. For example, potential competition could be eliminated where one of the merger partners, but for the merger, likely would enter the market in competition with the other partner and increase the competitive vigor of the market (actual potential entry), or exercise a procompetitive influence from the fringe even before it enters (perceived potential entry). Like vertical merger theories, potential competition theories fell into disuse during much of the 1980s. A major setback was the FTC's 1984 decision in *B.A.T. Industries, Ltd.*,¹¹⁰ a case involving the actual potential entry theory. In *B.A.T.*, the majority of the Commission imposed a high burden of proof to show that, but for the merger, the potential entrant would have entered the market independently. The majority concluded that a reasonable probability of entry was not enough and that "clear proof" that entry would occur was required.¹¹¹ In that case, clear proof meant "concrete plans" such as a capital acquisition plan or a budget drawn up with entry

and pharmacologists who have no financial interest in Merck. *See id.* at *12-*13. The consent order would require that this P&T Committee independently make all decisions concerning the inclusion and exclusion of drugs on the open formulary. *See id.* at *12. The order also ensures that Medco will accept all discounts, rebates or other concessions offered by any other manufacturer of pharmaceutical products in connection with the listing of those products on the open formulary, and to accurately reflect such discounts in ranking the drugs on the formulary. *See id.* at *14. Merck and Medco were also prohibited from sharing proprietary or other non-public information they receive from one another's competitors such as prices with exceptions for attorneys and auditors. *See id.* at *16-*18. In addition, the consent order would require Merck-Medco to make known the availability of the open formulary to anyone who currently has a PBM agreement with Medco, and (for a period of five years) to prospective customers. *See id.* at *17-*19.

¹⁰⁹ *See supra* notes 91-92 and accompanying text.

¹¹⁰ 104 FTC. 852 (1984).

¹¹¹ *See id.* at Commission Opinion, at 926.

in mind.¹¹² The current Chairman of the FTC, Robert Pitofsky, has criticized that standard:

I believe the “clear proof” standard is inappropriate and in fact essentially guts the actual potential competition doctrine. Section 7 only requires that the effect of the transaction “may be” to lessen competition, and that has been interpreted in the majority of litigated cases as requiring only a reasonable probability. At a more practical level, it is precisely in the most anticompetitive of conglomerate acquisitions that it is least likely that the government or a private party would discover documents assessing the prospects for entry other than by merger. I would not impose a “clear proof” standard if a conglomerate merger were to come up today.¹¹³

The antitrust agencies have in fact challenged significant mergers under potential competition theories in recent years, although none of the cases have been litigated. There have been a number of such cases, however only *Zeneca Group PLC*,¹¹⁴ *ABB*,¹¹⁵ and *United States v. SBC Communication's Inc.*¹¹⁶ are highlighted here.¹¹⁷

a. *Zeneca/Astra*.

Zeneca Group's proposed acquisition of Astra AB raised competitive concerns over the loss of potential competition in a market for long-lasting local anesthetics.¹¹⁸ Astra was the leading supplier of long-acting local anesthetics and one of only two companies approved by the FDA for the manufacture and sale of these kinds of drugs in the United States. Although Zeneca was not yet in that market, prior to the acquisition it had entered into an agreement with Chiroscience Group plc to market and assist in the development of levobupivacaine, a new long-acting lo-

¹¹² See *id.* at 927-28.

¹¹³ Robert Pitofsky, Competition Policy In Communications Industries: New Antitrust Approaches, Address before the Glasser LegalWorks Seminar on Competitive Policy in Communications Industries: New Antitrust Approaches, Washington, D.C. (Mar. 10, 1997) (transcript available at <<http://www.ftc.gov/speeches/pitofsky/newcomm.htm>>) (visited Mar. 24, 2000) (citations omitted).

¹¹⁴ No. C-3880, 1999 FTC LEXIS 115, at *1 (FTC., June 7, 1999). For a more complete discussion of potential competition mergers in the pharmaceutical industry, see David A. Balto & James F. Mongoven, *Antitrust Enforcement in Pharmaceutical Industry Mergers*, 54 *FOOD & DRUG L. J.* 255 (1999).

¹¹⁵ No. C-3867, 1999 FTC LEXIS 51, at *1 (FTC., April 22, 1999).

¹¹⁶ No. 99-0715, 1999 U.S. Dist. LEXIS 16789, at *1 (D.D.C. Aug. 2, 1999).

¹¹⁷ See also *In re Boston Scientific Corp.*, 119 FTC 549 (Apr. 28, 1996) (involving potential competition in the intravascular ultrasound (IVUS) imaging catheter market); *FTC v. Staples, Inc.*, 970 F. Supp. 1066 (D.D.C. 1997).

¹¹⁸ See *Zeneca*, No. C-3880, 1999 FTC LEXIS 115, at *5-*6.

cal anesthetic being developed by Chiroscience.¹¹⁹ By virtue of its agreement with Chiroscience, Zeneca was an actual potential competitor.

The U. S. market for these drugs is highly concentrated and barriers to entry are high due to the need to undertake the difficult, expensive and time-consuming process of researching and developing a new product, obtaining FDA approval, and gaining customer acceptance.¹²⁰ The Commission alleged that the acquisition would result in the elimination of a significant source of new competition, and the case was resolved with a consent order.¹²¹

b. ABB-Elsag Bailey Process Automation N.V.

ABB's proposed acquisition of Elsag Bailey Process Automation threatened to lessen competition in the market for process gas chromatographs and potential competition in the market for process mass spectrometers.¹²² ABB and Elsag were the world's two leading suppliers of process gas chromatographs in a highly concentrated market, and ABB would have had almost a 70% market share as a result of the acquisition.¹²³ The FTC's complaint alleged that the acquisition would have enabled ABB to unilaterally exercise market power, which would have resulted in higher prices and decrease of innovation in the market.¹²⁴ ABB also was one of the world's leading suppliers in the highly concentrated market for process mass spectrometers. Elsag Bailey did not yet manufacture process mass spectrometers, but it was involved in the research and development of a process mass spectrometer that it planned to begin manufacturing and selling in 1999. Thus, Elsag Bailey was an actual potential competitor in the market for process mass spectrometers. The FTC's complaint alleged that the acquisition would eliminate this significant source of future product competition and innovation.¹²⁵ The case was settled with a consent order that required ABB to divest the Analytical Division of Elsag Bailey's Applied Automation, Inc. subsidiary, that involved the manufacture and sale of process gas chro-

¹¹⁹ See *id.* at *1.

¹²⁰ See *id.* at *5-*6.

¹²¹ See *id.* at *8.

¹²² See *In re* ABB, No. C-3867, 1999 FTC LEXIS 51, at *5-*6. Process gas chromatographs are analytical instruments used in process manufacturing applications to measure the chemical composition of a gas or a liquid by separating a sample into its individual components through selective chemical interaction or solubility, and measuring the separated components using a detector. See *id.* at *1.

¹²³ See FTC Complaint, at ¶ 13, No. C-3867, (visited Apr. 27, 2000) <<http://www.ftc.gov/os/1999/9904/abbcamp.htm>>.

¹²⁴ See *In re* ABB, No. C-3867, 1999 FTC LEXIS 51, at *5-*6.

¹²⁵ See *id.*

matographs and the research and development of process mass spectrometers.¹²⁶

c. SBC-Ameritech.

SBC's proposed acquisitions of Ameritech Corp. and Comcast Cellular Corp. threatened to eliminate not only head-to-head competition in seventeen local markets for wireless mobile telephone (cellular) services but also potential competition in local exchange and long distance telephone services in the St. Louis area.¹²⁷ SBC was the incumbent provider of local exchange services in the area, and prior to the announcement of the acquisition, Ameritech had planned to enter the area with competing local exchange and long distance telephone services. Ameritech had planned to bundle its new services with its existing cellular mobile telephone service.¹²⁸ Because there was no existing source for such a bundled product in the St. Louis area, Ameritech expected that its plan would enhance its ability to retain cellular customers.¹²⁹ The DOJ alleged that Ameritech had made extensive preparations for entry before it agreed to be acquired by SBC.¹³⁰ Shortly after the announcement of its planned acquisition by SBC, Ameritech decided not to implement its local exchange and long distance entry plans in the St. Louis area.¹³¹ The DOJ alleged that the acquisition would prevent the realization of this new competition.¹³² The case was settled with an agreement that required SBC and Ameritech to divest a cellular phone system in each of the seventeen markets, and specifically the Ameritech cellular systems in the St. Louis area.¹³³ The purpose of this aspect of the consent decree is to ensure "that a purchaser of the divested Ameritech cellular systems in the St. Louis area would have the ability to pursue a local exchange entry strategy in SBC's local service area."¹³⁴

¹²⁶ See *id.* at *16.

¹²⁷ See 64 Fed. Reg. 23,099, 23,099 (April 21, 1999) (proposed final judgment and competitive impact statement).

¹²⁸ See *id.* at 23,107-108.

¹²⁹ See *id.* at 23,108.

¹³⁰ See *id.*

¹³¹ See *id.*

¹³² See *United States v. SCB Communication's Inc.*, No. 99-0715, 1999 U.S. Dist. LEXIS 16789, at *1 (D.D.C. Aug. 2, 1999).

¹³³ See *id.*

¹³⁴ See Department of Justice, Press Release, *Justice Department Requires SBC to Divest Cellular Properties in Deal with Ameritech and Comcast*, Mar. 23, 1999 (visited Mar. 24, 2000) <http://www.usdoj.gov/atr/public/press_releases/1999/2322.htm>. See also *United States v. Signature Flight Support Corp.*, No.1:99CV00537 (D.D.C., filed Mar.1, 1997), 64 Fed. Reg. 14,785 (proposed final judgment and competitive impact statement). In *Signature Flight*, the Department's complaint alleged that Signature Flight's acquisition of AMR Combs Inc. would eliminate head-to-head competition between Signature Flight and AMR Combs in providing flight support services such as fueling, ramp and hangar space rentals at two airports. See *id.* at 14,764-765. The complaint also alleged loss of potential competition from

Potential competition theory is an important part of merger enforcement where, but for the merger, one of the merger partners is likely to enter the market independently, the market is highly concentrated, and barriers to entry are high. Effective enforcement at the merger stage can preserve incentives to innovate, the potential for future entry, and prevent the future exclusionary use of monopoly power.

6. *Analysis of Merger Efficiencies*

Since the mid-1990s, efficiency¹³⁵ analysis has become a full-fledged part of both merger review and litigation. While efficiencies were addressed in the 1984 and 1992 Merger Guidelines,¹³⁶ and some courts had begun to recognize merger efficiencies in the late 1980s and early 1990s,¹³⁷ for many years consideration of merger efficiencies was largely a matter of prosecutorial discretion.¹³⁸ A need to clarify the analysis of merger efficiencies emerged during the FTC's 1995 hearings on competition policy in a global, high-tech marketplace.¹³⁹ Shortly thereafter, a joint FTC-DOJ task force began a vigorous re-examination of the issue. That effort culminated with a revision of the efficiencies section of the 1992 Merger Guidelines in April, 1997.¹⁴⁰

The 1997 Guidelines revisions accomplished several things. First and most significantly, they tied efficiencies directly into competitive effects analysis. The revisions recognized that cost reductions might re-

Signature Flight at a third airport where Signature had agreed to become the operator of a flight support facility upon its completion in the year 2000 in competition with AMR Combs. *See id.*

¹³⁵ Mergers may be efficient for a number of reasons. For instance, they may enable the merged firms take advantage of economies of scale or scope to reduce costs per unit in production, distribution or marketing. Those efficiencies may offset some of the anticompetition potential of a particular merger. Efficiency analysis is designed to weigh those effects.

¹³⁶ DEPARTMENT OF JUSTICE & FEDERAL TRADE COMMISSION, 1984 MERGER GUIDELINES, § 3.5, *reprinted in* 49 Fed. Reg. 26,823 (June 29, 1984) [hereinafter 1984 MERGER GUIDELINES]; 1992 HORIZONTAL MERGER GUIDELINES, *supra* note 51, at § 4.

¹³⁷ *See, e.g.*, *FTC v. University Health, Inc.*, 938 F.2d 1206, 1222 (11th Cir. 1991); *United States v. Country Lake Foods, Inc.*, 754 F. Supp. 669, 680 (D. Minn. 1990); *United States v. Carilion Health Sys.*, 707 F. Supp. 840, 849 (W.D. Va.), *aff'd*, 892 F.2d 1042, 1084-85 (4th Cir. 1989).

¹³⁸ In fact, the Supreme Court stated in *FTC v. Procter & Gamble Co.* that, "[p]ossible economies cannot be used as a defense to illegality." 386 U.S. 568, 580 (1967). However, literal application of that ruling appears to be a relic of the past.

¹³⁹ *See Hearings Before the Federal Trade Commission on Global and Innovation-Based Competition*, (visited Mar. 24, 2000) <<http://www.ftc.gov/opp/global/GC113095.htm>> [hereinafter *FTC Hearings*]; Federal Trade Commission, Staff Report, *Anticipating the 21st Century: Competition Policy in the New High-Tech, Global Marketplace*, Ch.2, (May 1996) (visited Mar. 24, 2000) <http://www.ftc.gov/opp/global/report/gc_v1.pdf> [hereinafter *FTC Staff Report*].

¹⁴⁰ DEPARTMENT OF JUSTICE & FEDERAL TRADE COMMISSION, 1997 HORIZONTAL MERGER GUIDELINES, § 4 (revised), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,104, at 20,573-11 (1997) [hereinafter 1997 HORIZONTAL MERGER GUIDELINES].

duce the likelihood of coordinated interaction or the incentive to raise price unilaterally.¹⁴¹ These are situations in which consumers are likely to receive the benefits of merger efficiencies. The revised Guidelines instruct that a merger will not be challenged if the efficiencies “are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market.”¹⁴² This is not simply a matter of comparing the magnitudes of the anticompetitive effects and the estimated efficiencies. Rather, it is essential to determine how the claimed efficiencies will affect market behavior. Second, the revisions defined more clearly and explicitly which efficiencies “count,” *i.e.* what Section 4 now defines as “cognizable efficiencies.” In particular, efficiencies must not arise from anticompetitive reductions in output, service or other competitively significant categories, such as innovation.¹⁴³ Third, the revisions refined the concept that efficiencies must be attributable to the merger - *i.e.*, merger-specific - and could not be achieved in a less anticompetitive way.¹⁴⁴ Finally, efficiency analysis now expressly incorporates a sliding scale approach. The revisions state that the agencies will require proof of greater efficiencies as the likely anticompetitive effects of the merger increase.¹⁴⁵

These are standards that defense lawyers, enforcement officials, and judges can and do turn to in arguing efficiency questions, and they have made a difference, both in the way efficiencies claims are presented to the antitrust agencies and in the way they are litigated. For example, the FTC has relied on such efficiencies in deciding not to challenge certain transactions, such as hospital mergers. However, efficiencies should almost never justify a merger to monopoly or near monopoly, and that is true both in the exercise of prosecutorial discretion and in litigated cases. The discussion of two recent cases illustrates judicial analysis of merger efficiencies under the revised Merger Guidelines: *F.T.C. v. Staples, Inc.*,¹⁴⁶ and *F.T.C. v. Cardinal Health, Inc.*¹⁴⁷

a. Staples/Office Depot.

In *Staples*,¹⁴⁸ the court considered efficiencies for the first time since the Merger Guidelines were amended in 1997. The court’s discussion of efficiencies began with the cases that expressed skepticism towards cost savings claims and proceeded with a careful analysis based

¹⁴¹ See *id.* at 20,573-11.

¹⁴² See *id.* at 20,573-13.

¹⁴³ See *id.*

¹⁴⁴ See *id.*

¹⁴⁵ See *id.*

¹⁴⁶ 970 F. Supp. 1066 (D.D.C. 1997).

¹⁴⁷ 12 F. Supp.2d 34 (D.D.C. 1998).

¹⁴⁸ For a more detailed discussion of the facts of the case, see Part I.B.1.

on the Merger Guidelines framework. In particular, the court examined whether the cost savings claims of Staples and Office Depot were substantial, unique to the merger, and likely to be shared with the consuming public.¹⁴⁹

The merging parties asserted many efficiency claims, but the most important was that the combined firm would have greater purchasing power and could extract better prices from its various vendors. The court rejected the efficiency argument on two grounds: first, the claims were substantially exaggerated,¹⁵⁰ and second, even if buying power was an "efficiency," the merger was not necessary to increase buying power because both parties to the merger were expanding rapidly.

The court's rejection of these claims based on the lack of merger specific efficiencies, established an important principle for future merger enforcement. Both parties to the merger were expanding rapidly by opening new stores, as many as 100 or 150 new stores per year for each, so that increased buying power from the merger, even assuming it could be used to extract better prices from vendors, would have occurred as a result of internal expansion absent the merger.¹⁵¹ If there was an efficiency in the merger, it involved the fact that the larger enterprise would be created immediately rather than over a period of 3 or 4 years. Those efficiencies would have been temporary and declining in significance. The merger, on the other hand, and its anticompetitive effects, would have been permanent.

In hindsight that assessment seems to be correct. Just three years after the proposed merger both Staples and Office Depot have achieved the size (about 1000 stores) that the single firm would have achieved through the merger.¹⁵² Thus, whatever efficiencies would have been accomplished through greater size are probably being achieved by both firms today without an attendant loss of competition.

b. Cardinal Health, Inc.

This case involved the FTC's challenge of proposed mergers between Cardinal Health and Bergen, and between McKesson and Amerisource¹⁵³- the four largest drug wholesalers in the United States.¹⁵⁴ If both mergers had been allowed to proceed, the leading national drug

¹⁴⁹ See *Staples*, 970 F.Supp. at 1075-76.

¹⁵⁰ See *id.* at 1089-91. For example, the cost savings estimate submitted in Court exceeded by almost 500% the figures presented to the Boards of Directors of the two firms when they approved the transaction. See *id.* at 1089.

¹⁵¹ See *id.*

¹⁵² See Company Profiles, <<http://biz.yahoo.com/p/s/sls.html>> (Staples), <<http://biz.yahoo.com/p/o/odp.html>> (Office Depot).

¹⁵³ See *FTC v. Cardinal Health, Inc.*, 12 F.Supp.2d 34 (D.D.C. 1998).

¹⁵⁴ See *id.* at 37.

wholesalers would have been reduced from four to two, and those two companies would have a combined market share of up to 80% of the pharmaceutical wholesale market.¹⁵⁵ Like Judge Hogan in the *Staples* case, Judge Sporkin acknowledged that the previous decisions of the Supreme Court probably would preclude giving any weight to claimed efficiencies. However, the judge recognized the tendency of lower courts to take efficiencies into account, and the Federal Trade Commission's departure from the old Supreme Court cases in revising the Merger Guidelines.¹⁵⁶ The court elected to follow the approach of the 1997 Guidelines revisions, and its analysis establishes that although the efficiency claims of the merging firms will be carefully considered, such claims also will be weighed in light of the competitive concerns raised by increases in market power.¹⁵⁷

In *Cardinal Health* the defendants claimed several different sources of efficiencies: (1) distributional efficiencies through the closing of overlapping centers, (2) superior purchasing practices, (3) increased buying power, and (4) reduction in overhead and inventory costs.¹⁵⁸ The parties argued that the efficiencies would be substantial, ranging in the three years after the merger from \$220 million to over \$307 million, that at least 50% would be passed along to consumers (in contrast to their historical average of 80%), and that the efficiencies were a major if not principal reason for the mergers.¹⁵⁹

The court's careful analysis found strong evidence that many of these efficiencies could be produced in the absence of the merger. The court noted that "the history of the industry . . . demonstrates the power of competition to lower cost structures and garner efficiencies as well,"¹⁶⁰ and expressed concern that the mergers would remove the pressure to be more efficient and price competitive.

The court also looked closely at the argument that the mergers would remove excess capacity from the market. Although conceding those actions would produce cost savings, Judge Sporkin used the 1997 Horizontal Merger Guidelines framework to assess how the proposed efficiencies would affect competition in the market.¹⁶¹ The court noted that company documents equated excess capacity with pricing pressures and stiff competition, and the documents expressed hope that consolida-

155 See *id.* at 66.

156 See *id.* at 62.

157 See *id.* at 63.

158 See *id.* at 62.

159 See *id.* at 62-63.

160 *Id.* at 63.

161 See *id.* at 62. See also 1997 MERGER GUIDELINES, *supra* note 141, at § 4 ("The Agency will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market").

tion at the top of the industry would bring "a more orderly market" and "rational pricing."¹⁶² The court relied as well on customer testimony that affirmed the competitive role of excess capacity.¹⁶³ Judge Sporkin concluded that the "mergers would likely curb downward pricing pressures and adversely affect competition in the market."¹⁶⁴

The court correctly posed the ultimate question when it stated, "[t]he critical question raised by the efficiencies defense is whether the projected savings from the mergers are enough to overcome the evidence that tends to show that possibly greater benefits can be achieved by the public through existing, continued competition."¹⁶⁵ The court concluded that, "defendants simply have not made their case on this point."¹⁶⁶ Consistent with the revised 1997 Horizontal Merger Guidelines, efficiency claims were carefully analyzed, but the parties faced a substantial burden in attempting to justify mergers that would result in such a large increase in market power.

C. HIGH TECH AND ANTITRUST

One of the most visible parts of recent antitrust activity has been the number, and importance, of cases in high technology industries. The antitrust agencies devote a significant part of their resources to enforcement in high tech industries, and this enforcement effort has increased in recent years.¹⁶⁷ One reason for the increase is the sheer size of this sector, in terms of the number of firms, total employment, and economic value created. But even more important than the size of the sector is its growing importance as a source of innovation and economic growth.¹⁶⁸ Competition in high tech industries must be protected by a strong antitrust effort aimed at preventing the accumulation of market power either through merger or its abuse in non merger contexts, otherwise U.S. economic performance will suffer.

There are several important characteristics of high tech industries that make application of the antitrust laws especially challenging. The first is that the current pace of innovation is unprecedented.¹⁶⁹ The speed with which technology evolves is increasing in many industries. Per-

¹⁶² See *Cardinal Health, Inc.*, 12 F. Supp.2d at 64.

¹⁶³ See *id.* at 65.

¹⁶⁴ *Id.* at 64.

¹⁶⁵ *Id.* at 63.

¹⁶⁶ *Id.* at 63.

¹⁶⁷ 1999 ATT'Y GEN. ANN. ACCT. REP. § 3.31 (visited Mar. 24, 2000) <<http://www.usdoj.gov/ag/annualreports/ar99/index.html>>.

¹⁶⁸ See 1998 PRES. ECON. REP. 209 ("Many of the fastest growing and fastest changing U.S. industries are to be found in such high-technology fields as aerospace, computer hardware and software, and telecommunications").

¹⁶⁹ See FTC, Staff Report, *supra* note 140, at Ch. 6, 14-15.

sonal computers, software and cellular telephones increase in speed and sophistication as fast as prices fall. Innovation in other high technology areas may seem sluggish in comparison to the computer and telecommunication industries, but it actually proceeds quite rapidly. In the pharmaceutical industry, in particular, firms engaged in genetic research are rapidly expanding the boundaries of knowledge across all areas of medicine. In the financial sector, new technology is rearranging entire industries. This technological fever means that innovation may erode market power, at least where it cannot be controlled or managed by the market leader.

Because of this rapid technological change, competition has come to be defined by innovation in many high tech industries, unlike more traditional industries where competition is most often driven by price. In high tech industries, nonprice attributes of products, such as performance characteristics and compatibility with other products,¹⁷⁰ can be more important to customers.¹⁷¹ The Merger Guidelines explicitly recognize the importance of nonprice competition by noting that competition may be harmed in the area of "product quality, service, or innovation."¹⁷² This increased emphasis on nonprice competition in high tech industries can be procompetitive. Because the range of nonprice attributes is infinite, competitors may find nonprice collusion more difficult than collusion over price.¹⁷³

Much of the agencies' high tech enforcement effort has focused on mergers.¹⁷⁴ When cutting-edge technology is owned or licensed to only a few firms, consolidation among those firms could eliminate the only substantial actual or potential competitors. The agencies have been particularly active in the computer and pharmaceutical industries, bringing a number of cases that have preserved competition without hampering innovation opportunities. A few of those cases are described below.

¹⁷⁰ See Joseph Farrell & Garth Saloner, *Installed Base and Compatibility: Innovation, Product Preannouncements, and Predation*, 76 AM. ECON. REV. 940 (1986).

¹⁷¹ See Dennis A. Yao & Susan S. DeSanti, *Innovation Issues Under the 1992 Merger Guidelines*, 61 ANTITRUST L.J. 505, 506-07 (1993) ("Our own experience at the FTC indicates that there are increasing numbers of mergers that raise issues relating to competition over matters such as new product development, new methods of distribution, or other forms of innovation").

¹⁷² 1992 HORIZONTAL MERGER GUIDELINES, *supra* note 51, at § 0.1 n. 6.

¹⁷³ Although nonprice collusion may be difficult, experience shows that it does occur and can have serious anticompetitive consequences. See *United States v. Automobile Mfrs. Ass'n.*, 1969 Trade Case. (CCH) ¶72,907 (C.D. Cal. 1969) (consent decree).

¹⁷⁴ See David A. Balto & James F. Mongoven, *Antitrust Remedies in High Technology Industries*, ANTITRUST REP., Jan. 1999, at 22.

1. *Digital—Intel.*

In the computer industry, innovation in some markets may be limited to only a few firms.¹⁷⁵ Digital and Intel are aggressive rivals both for current and next generation microprocessors.¹⁷⁶ In addition, Digital's Alpha microprocessor is a significant competitor both to Intel's Pentium microprocessor and to Intel's next generation IA-64 microprocessor.¹⁷⁷ In May 1997, both firms sued each other for patent infringement by their respective products.¹⁷⁸ In October 1997, the suits were settled by agreement contemplating broad patent cross-licenses, the sale of Digital's microprocessor production facilities to Intel, and that Intel would produce Digital's Alpha microprocessors although Digital retained the intellectual property rights to Alpha.¹⁷⁹

The FTC alleged that the agreement would reduce competition in three separate markets: 1) the manufacture and sale of high-performance, general purpose microprocessors capable of running Windows NT in native mode; 2) the manufacture and sale of all general purpose microprocessors; and 3) the design and development of future generations of high-performance, general purpose microprocessors.¹⁸⁰ In each of those markets, Digital's Alpha chips happened to be the highest performing and most technologically advanced threat facing Intel's microprocessors.¹⁸¹ The Commission was concerned that Alpha would not remain competitively viable under the original terms of the agreement. Intel could interfere with Digital's supply of Alpha chips and Digital might not have the incentive to continue to actively develop and promote Alpha.¹⁸²

To resolve these concerns, the FTC issued a consent order under which Digital would license the Alpha architecture to Samsung and AMD or other suitable partners so that they would be able to produce and develop Alpha chips.¹⁸³ Digital also agreed to begin the process of certifying IBM as a foundry for Alpha chips to establish a manufacturing alternative to Intel.¹⁸⁴ This relief preserves the Alpha chip as a viable product and a competitor to Intel's microprocessors.

¹⁷⁵ See *In re Digital Equipment Corp.*, No. 3818, 1998 FTC LEXIS 75, at *8 (July 14, 1998).

¹⁷⁶ See *id.* at *7.

¹⁷⁷ See *id.* at *7-*8.

¹⁷⁸ See *id.* at *3.

¹⁷⁹ See *id.*

¹⁸⁰ See *id.* at *6-*7.

¹⁸¹ See *id.* at *8.

¹⁸² See *id.* at *12-*13.

¹⁸³ See *id.* at *29.

¹⁸⁴ See *id.* at *36.

2. Dell Computer

One of the most contentious areas of antitrust enforcement involves standard setting. Proprietary standards, in particular, may pose a number of antitrust risks. The general danger of allowing a private party to own intellectual property rights in an open standard (or to have it set a *de facto* standard based on its intellectual property) is that the private party at some time may choose to close the standard either by licensing it on a discriminatory basis or by setting an unreasonable price for continued access. If a proprietary standard has been widely adopted in a network market, this form of "intellectual property ambush" can impose a significant cost on the users of the standard.

The FTC faced this situation in its enforcement action against Dell Computer.¹⁸⁵ In 1992, the Video Electronics Standards Association (VESA) adopted a computer hardware standard called the VL-Bus standard, which governs the transmission of information between a computer's central processing unit ("CPU") and its peripheral devices.¹⁸⁶ Each of the members voting to adopt the standard, including Dell Computer Corporation, was required by VESA rules to affirm that they did not own any patent rights that covered the VL-Bus standard.¹⁸⁷ Dell's representative did in fact make such a statement. Nonetheless, eight months later, after the VL-Bus standard had been widely adopted, Dell asserted a patent against other VESA members for using the VL-Bus standard.¹⁸⁸ Dell encouraged the group to adopt a standard that involved technology that Dell allegedly knew was proprietary, and in doing so obtained the help of its competitors in establishing a standard, which it would ultimately be able to control.

Had Dell announced up front that the standards they were backing were proprietary, it is unlikely that the affected participants would have chosen those standards. At the very least, those standards would have faced stiffer competition than they did. Instead, Dell obtained a dominant position it could not have attained in open standards competition.

D. DISTRIBUTIONAL RESTRAINTS

Early during the Clinton Administration, Anne Bingaman, then Assistant Attorney General for Antitrust, signaled a new approach to vertical restraints by announcing the rescission of the Department's Vertical

¹⁸⁵ See *In re Dell Computer Corp.*, C-3586, 60 Fed. Reg. 57,870 (Nov. 22, 1995) (consent agreement).

¹⁸⁶ See *id.* at 57,872.

¹⁸⁷ See *id.*

¹⁸⁸ See *id.*

Restraints Guidelines promulgated in 1985.¹⁸⁹ The Assistant Attorney General described them as having been “controversial from the outset,” and having been, “based on a premise that vertical restraints that only affect intrabrand competition generally represent little anticompetitive threat and involve some form of economic integration between different levels of production or distribution that tend to create efficiencies.”¹⁹⁰ While conceding that the Guidelines, provided some useful guidance, she observed that, “they unduly evaluated theory over factual analysis, and in certain respects were at variance with existing case law,” particularly, “to the extent that they treated all agreements between distributors of a single manufacturer as vertical rather than horizontal agreements, and treated vertical price fixing agreements under a rule of reason analysis if they were ancillary to non-price agreements.”¹⁹¹ The Assistant Attorney General declared that the Antitrust Division would “treat vertical price fixing as per se illegal, and non-price fixing restraints as subject to a meaningful rule of reason analysis,”¹⁹² adding however, that she was not “declaring war” on all vertical restraints, but rather was “cognizant of the potential procompetitive effects of some vertical non-price restraints in a variety of circumstances.”¹⁹³ Her purpose was to “look at vertical restraints in a more balanced manner than was reflected in the rescinded Vertical Guidelines.”¹⁹⁴

Even before the rescission of the Vertical Restraint Guidelines, the agencies renewed vertical enforcement, primarily involving resale price maintenance (“RPM”). Beginning during the Bush Administration and vigorously continuing in the Clinton Administration, the FTC has brought a series of RPM cases. Some of these, indeed most, have turned on the identification of a vertical agreement in ambiguous circumstances, while others have turned on determining whether what was agreed upon amounted to price-fixing.

In the Bush Administration, the FTC brought two RPM cases. *In re Kreepy Krauly, USA, Inc.*,¹⁹⁵ was one of the rare cases where there was direct evidence of agreement in the form of a written contract fixing re-

¹⁸⁹ See Anne K. Bingaman, Change and Continuity in Antitrust Enforcement, Remarks before the Fordham Corporate Law Institute, Fordham Law School (Oct. 21, 1993) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/93-10-21.txt>>) (visited Mar. 24, 2000) (referring to the DEPARTMENT OF JUSTICE, 1985 VERTICAL RESTRAINT GUIDELINES, 50 Fed. Reg. 6,263 (Feb. 14, 1985) [hereinafter VERTICAL RESTRAINT GUIDELINES]).

¹⁹⁰ Anne K. Bingaman, Change and Continuity in Antitrust Enforcement, Remarks before the Fordham Corporate Law Institute, Fordham Law School (Oct. 21, 1993) (transcript available at <<http://www.usdoj.gov/atr/public/speeches/93-10-21.txt>>) (visited Mar. 24, 2000).

¹⁹¹ *Id.*

¹⁹² *Id.*

¹⁹³ *Id.*

¹⁹⁴ *Id.*

¹⁹⁵ 114 FTC 777 (1991).

sale prices. In that case, the distribution agreements provided that dealers would use their best efforts to adhere to Kreepy Krauly's suggested retail prices.¹⁹⁶ In *In re Nintendo*,¹⁹⁷ another 1991 case, the Commission inferred agreement from a pattern of coercion and threats of termination.¹⁹⁸ The Commission alleged that Nintendo had not simply terminated dealers that did not comply with the suggested prices, as was its right under *United States v. Colgate*,¹⁹⁹ but instead had used threats to cut off or reduce supplies to noncomplying dealers as a way of coercing assent.²⁰⁰ The consent order prohibited the firm from engaging in various conduct that could implement resale price maintenance agreements, including taking punitive actions against discounting dealers, reducing their supplies, or granting them unfavorable credit terms.²⁰¹ As a matter of "fencing-in relief," the Commission order prohibited Nintendo from terminating dealers on the basis of the resale price they charge.²⁰²

The Clinton Administration's antitrust enforcers built on this foundation of resale price management analysis to evaluate somewhat more novel approaches to restrict resale prices. One area of inquiry involves "structured termination" policies, under which, manufacturers suggest resale prices and give warnings or suspend dealers for a given period of time if they do not conform. A second or third violation generally requires termination.²⁰³ One commentator suggests that these policies constitute an agreement because "the dealer's compliance after the first (or second) suspension constitutes communicated acquiescence."²⁰⁴

While the FTC has neither adopted nor rejected this view, its cases against Reebok²⁰⁵ and New Balance,²⁰⁶ illustrated how "structured termination policies" may lead to conversations that go over the line. Reebok and New Balance had structured termination policies that gave a retailer one warning if it failed to adhere to suggested retail prices. A second violation required termination.²⁰⁷ The problem with these policies, as most manufacturers discover, is that the people who are responsible for implementing the policies are sales representatives, not antitrust

¹⁹⁶ See *id.*

¹⁹⁷ 114 FTC 702 (1991).

¹⁹⁸ See *id.*

¹⁹⁹ 250 U.S. 300 (1919) (recognizing a firm's freedom to select those customers with whom it wishes to do business, when the firm acts independently and does not have absence of market power).

²⁰⁰ See *In re Nintendo*, 114 FTC 702 (1991).

²⁰¹ See *id.*

²⁰² See *id.*

²⁰³ See, e.g., *In re Reebok Int'l Ltd.*, 130 FTC. 20 (1995); *In re New Balance Athletic Shoes, Inc.*, 122 FTC 137 (1996).

²⁰⁴ Richard Steuer, *The Distribution Superhighway*, ANTITRUST, at 4,6 (1994).

²⁰⁵ *In re Reebok Int'l Ltd.*, 130 FTC, at 23.

²⁰⁶ *In re New Balance Athletic Shoes, Inc.*, 122 FTC, at 140.

²⁰⁷ See *Reebok*, 130 FTC at 23; *New Balance*, 122 FTC, at 140.

lawyers. Warnings tend to lead to a series of discussions about the propriety of the retail price or about how the distributor or retailer can come into compliance with the policy. Often these conversations lead to a meeting of the minds about how the parties will behave in the future. For example, dealers might get reinstated when they promise to raise their prices to suggested levels. Those actions may well establish an agreement on resale prices, as they did in these two cases.

The FTC did not address directly the legality of the structured termination policies; rather it challenged the agreements that resulted from the dialogue between the manufacturers and their retailers as an outgrowth of the structured termination policies.²⁰⁸ The consent orders did provide as a matter of fencing-in relief, however, that for ten years the manufacturers could not use such a "structured termination" policy.²⁰⁹ Those structured termination provisions had played a significant role in causing the firms to go over the line, and it was important to remove that source of temptation.

In the rare instance, such as the Commission's enforcement action against American Cyanamid,²¹⁰ the question was not whether there is an agreement, but whether the identified agreement fixed the resale price or price levels.

1. *American Cyanamid*

American Cyanamid had established a rebate program in a \$1 billion agricultural chemical market, reflected in written agreements with its dealers, that paid a substantial rebate for each resale of crop protection chemicals at or above floor prices.²¹¹ American Cyanamid had set wholesale prices equal to the stated minimum prices, so the dealers lost money on every sale below the specified price. In 1997, the Commission challenged this rebate scheme as an attempt by a manufacturer to establish resale prices through finely tuned incentives rather than direct agreement.²¹² The question was not whether there was an agreement, but whether the agreement fixed the resale price or price levels.

In the Commission's view, as the complaint alleged, the program amounted to a quid pro quo between American Cyanamid and its dealers, under which American Cyanamid explicitly promised to pay dealers in exchange for adhering to the suggested price, essentially establishing an

²⁰⁸ See *Reebok*, 130 FTC at 20; *New Balance*, 122 FTC at 137.

²⁰⁹ See *Reebok*, 130 FTC at 23; *New Balance*, 122 FTC at 140.

²¹⁰ 123 F.T.C. 1257, 1260 (1997).

²¹¹ See *id.* at 1258.

²¹² See *id.* at 1260. In part, the consent order prohibits American Cyanamid from conditioning the payment of rebates or other incentives on the resale prices its dealers charge for American Cyanamid products. A multi-state task force obtained a settlement valued at \$7.3 million.

agreement on price or price level.²¹³ This issue shows the contrast between the treatment of traditional cooperative advertising programs,²¹⁴ which are analyzed under the rule of reason,²¹⁵ and schemes in which dealers are explicitly paid to adhere to a particular price or price level, which are not legal. Notably, *American Cyanamid* does not take issue with other cases addressing dealer assistance programs, including price restricted cooperative advertising and discount pass-through programs.

2. Major Music Distributors

One important area of resale price maintenance enforcement involves price-restricted cooperative advertising programs. These programs condition the manufacturer's grant of cooperative advertising allowances to dealers on dealers' agreements not to advertise a price below the manufacturer's suggested price or, in some cases, to advertise affirmatively the manufacturer's suggested price. These are often called minimum advertised price or MAP programs. MAP programs play a vital role in competition in many industries where advertising is important, especially consumer electronics. The legal treatment of MAP programs has changed during the past two decades. During the Carter Administration the agencies treated these as *per se* illegal. In the Reagan Administration, that policy was abandoned and they now are analyzed under the rule of reason.²¹⁶ A recent enforcement action demonstrates how the Clinton Administration has taken a reasonable but careful enforcement position toward these programs.

In May of 2000, the Commission brought an enforcement action against each of the five major recorded music distributors for their use of MAP programs in the sale of compact discs.²¹⁷ The Commission alleged that these programs both facilitated horizontal collusion among the distributors, in violation of § 5 of the Federal Trade Commission Act²¹⁸

²¹³ *Id.* at 1267-68.

²¹⁴ In traditional cooperative advertising programs, manufacturers help dealers pay for advertising or promotion, but add the condition that in the advertisements supported by the manufacturer, the dealer cannot include any price advertising unless the prices are at or above suggested levels. These programs are unlikely to raise antitrust concerns as long as dealers are free to price at whatever level they choose when they buy their own advertisements.

²¹⁵ See *supra* notes 190-195 and accompanying text.

²¹⁶ Federal Trade Commission, Statement of Policy Regarding Price Restrictions in Cooperative Advertising Programs-Rescission, 6 Trade Reg. Rep. (CCH) ¶39,057 (May 21, 1987).

²¹⁷ See *In re Time Warner Inc.*; *In re Sony Music Entertainment Inc.*; *In re Capitol Records, Inc.*, d.b.a. "EMUS Music Distribution"; *In re Universal Music & Video Distribution Corp.* and UG. Recordings, Inc.; and *In re BIG Music*, d.b.a. "BIG Entertainment", No. 971-0070, (visited May 30, 2000) <<http://www.ftc.gov/os/2000/05/index.htm>> (accepted for public comment, May 10, 2000).

²¹⁸ 15 U.S.C. § 45 (1996). This section, in pertinent part, makes unlawful "[u]nfair methods of competition in or affecting commerce." Courts interpret §5 to include conduct prohib-

and, when viewed individually, constituted unreasonable vertical restraint of trade under the rule of reason. Each respondent settled the case agreeing to abandon the practices at issue.²¹⁹

The complaints accompanying the proposed orders allege that the five companies collectively dominate this market, and that they each adopted significantly stricter MAP programs between late 1995 and 1996 in reaction to concern about widespread retail discounting in compact discs that was pressuring both retail and distribution margins.²²⁰ Under these new MAP provisions, retailers seeking any cooperative advertising funds were required to honor the distributors' minimum advertised prices in all media advertisements, even in advertisements funded solely by the retailers. These retailers were also required to adhere to the distributors' minimum advertised prices on all in-store signs and displays, regardless of whether the distributor contributed to their cost. These restrictions went beyond those of traditional MAP programs that restricted solely the prices in the advertisements paid for by the manufacturers. Failure to adhere to the respondents' MAP provisions for any particular music title would subject the retailer to a suspension of all cooperative advertising funding from this distributor for an extended period, typically 60 to 90 days. The complaints assert that the severity of these penalties ensured that even the most aggressive retail competitors would stop advertising prices below MAP. The complaints further allege that by defining advertising broadly enough to include all in-store displays and signs, the MAP policies effectively precluded many retailers from communicating prices below MAP to their customers, and in large part deterred such pricing by depriving it of beneficial effect on sales. The impact on consumers of these restrictions was substantial: consumers ultimately paid more than \$400 million in higher prices.²²¹

The Commission's recent RPM enforcement actions might have suggested that it would treat these programs as per se illegal, but instead,

ited by the Clayton Act, 15 U.S.C. §§ 12-27 (1999), Robinson-Patman Act, 15 U.S.C. §§ 13-13c, 21a (1999), and the Sherman Act, 15 U.S.C. §§ 1-2 (1999). *See, e.g.*, *FTC v. Motion Picture Adver. Serv. Co.*, 344 U.S. 392 (1953); *FTC v. Cement Institute*, 333 U.S. 683 (1948); *American News Co. v. FTC*, 300 F.2d 104 (2nd Cir.), *cert. denied*, 371 U.S. 824 (1962). Similarly, § 5 also extends to certain conduct "even though the practice does not infringe either the letter or the spirit of the antitrust laws." *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 239 (1972).

²¹⁹ *See* FTC, Press Release, *Record Companies Settle FTC Charges of Restraining Competition in CD Music Market*, (visited May 30, 2000) <<http://www.ftc.gov/opa/2000/05/cdpres.htm>>.

²²⁰ *See* FTC Complaints, (visited May 30, 2000) <<http://www.ftc.gov/os/2000/05/index.htm>>.

²²¹ *See* FTC, Press Release, *Record Companies Settle FTC Charges of Restraining Competition in CD Music Market*, (visited May 30, 2000) <<http://www.ftc.gov/opa/2000/05/cdpres.htm>>.

it analyzed the programs under the rule of reason.²²² The Commission's Statement observes that, in the past, the Commission "has employed the rule of reason to examine cooperative advertising programs that restrict reimbursement for the advertising of discounts, because such programs may be procompetitive or competitively neutral."²²³ However, the MAP policies it had dealt with in the past did not prohibit retailers from selling at discount prices or advertising discounts or sale prices with their own funds, and the policies in the cases went well beyond these restraints.

The Commission nonetheless concluded that rule of reason treatment is still appropriate, because it could not find here the "agreement on price or price levels" required by *Business Electronics Corp. v. Sharp Electronics Corp.*²²⁴ as a basis for *per se* illegality of vertical agreements. The advertising payments here were, strictly speaking, tied to advertising of one kind or another, not to pricing itself, and there was even evidence that some retailers on rare occasions had sold product at discount without advertising price, other than as a "guaranteed low price."²²⁵ "In our view," the Commission wrote, "*Sharp* requires something more than a showing that an agreement has some influence on price."²²⁶

The Commission concluded, nonetheless, that the distributors' MAP policies were unlawful under the rule of reason:

The five distributors together account for over 85 percent of the market, and each has market power in that no music retailer can realistically choose not to carry the music of any of the five major distributors. The MAP policies were adopted by each of the distributors for the purpose of stabilizing retail prices. The MAP policies achieved their purpose and effectively stabilized retail prices with consequential effects on wholesale prices, ending the price competition that previously existed in the retail marketplace and the resulting pressure on the distributors' margins. Compliance with the MAP policies - which was secured through significant financial incentives - effectively eliminated the retailers' ability to communicate discounts to consumers. Even absent an

²²² See Statement of Chairman Robert Pitofsky and Commissioners Sheila F. Anthony, Mozelle W. Thompson, Orson Swindle, and Thomas B. Leary (May 10, 2000) (transcript available at <<http://www.ftc.gov/os/2000/05/cdstatement.htm>>) (visited May 30, 2000) (hereinafter "Commission Statement")

²²³ See *id.*, citing Statement of Policy Regarding Price Restrictions in Cooperative Advertising Programs - Rescission, 6 Trade Reg. Rep. (CCH) ¶ 39,057.

²²⁴ 485 U.S. 717, 735-36 (1988).

²²⁵ See Commission Statement, *supra* note 223.

²²⁶ *Id.*

actual agreement to refrain from discounting, this inability to effectively communicate discounts to consumers meant that retailers had little incentive to actually sell product at a discount.²²⁷

The Commission added a strong cautionary note, observing that “[i]n the future” it would “view with great skepticism” MAP programs “that effectively eliminate the ability of dealers to sell product at a discount.”²²⁸

3. Toys ‘R’ Us.

In October 1998, the Commission held that Toys ‘R’ Us had violated § 5 of the Federal Trade Commission Act²²⁹ by inducing major toy manufacturers to agree - both with Toys ‘R’ Us and among themselves - to deal with warehouse clubs, like Costco and Sam’s Club, on less favorable terms.²³⁰ By the early 1990s, Toys ‘R’ Us faced a new competitive threat: the warehouse clubs, with their innovative, low cost, no frills approach, had begun selling toys at prices that were lower than Toys ‘R’ Us prices, which affected the Toys ‘R’ Us low-price image and threatened its market position.²³¹ In response, Toys ‘R’ Us orchestrated agreements with and among toy manufacturers to withhold from the clubs toys they were selling to Toys ‘R’ Us.²³² The agreements permitted the manufacturers to package two or more toys into more expensive, less desirable “club specials,” or to sell other differentiated products.

The effect was to make it more difficult for consumers to make price comparisons between the clubs and Toys ‘R’ Us, thus eliminating the pricing pressure that the clubs were putting on Toys ‘R’ Us.²³³ These restrictions were not in the manufacturer’s individual self-interest. According to the FTC, Toys ‘R’ Us had to threaten that it would not carry toy items that the suppliers sold to the clubs, and provide assurances that other manufacturers were going along with the boycott.²³⁴ The FTC noted that these agreements could be *per se* illegal under *Klor’s, Inc. v. Broadway-Hale Stores, Inc.*,²³⁵ which was similar on its facts, but the

²²⁷ *Id.* (internal citations omitted).

²²⁸ *Id.*

²²⁹ 15 U.S.C. § 45 (1996). *See also supra* note 219.

²³⁰ *See In re Toys ‘R’ Us, Inc. No. 9278, 1998 FTC LEXIS 119, at *1* (Oct. 13, 1998). The Decision and Order have been appealed to the United States Court of Appeals for the Seventh Circuit. *See Toys ‘R’ Us, Inc. v. FTC, Dkt. No. 98-4108* (7th Cir. Filed Dec. 7, 1998). Oral argument was heard on May 18, 1999.

²³¹ *See In re Toys ‘R’ Us, 1998 FTC LEXIS 119, at *19.*

²³² *See id.*

²³³ *See id.* at *22-*23.

²³⁴ *See id.* at *36.

²³⁵ 359 U.S. 207, 213 (1959).

Commission chose to apply the more critical analysis under the Supreme Court's more recent decision in *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.*²³⁶ and accordingly determined that the *per se* rule was appropriate for this case.²³⁷

The FTC also held that Toys 'R' Us' conduct in orchestrating the boycott was unlawful even under a rule of reason review.²³⁸ That holding was based on the FTC's findings that Toys 'R' Us' conduct in organizing a group boycott of the warehouse clubs produced demonstrable anticompetitive effects, such as preventing a decrease in the prices that consumers pay for toys, and that the sole business justification proffered, the prevention of free riding, was mere pretext.²³⁹ The Commission also held that, "each agreement in the series of vertical agreements, standing alone, even without the evidence of horizontal agreement among many of the toy manufacturers violates § 1 of the Sherman Act upon a full rule of reason review."²⁴⁰

Several factors distinguish this case from the typically benign non-price vertical restraint. As an initial matter, the FTC found that the Toys 'R' Us conduct was in no way unilateral conduct protected by *United States v. Colgate*.²⁴¹ The record was full of references to requests for commitments between Toys 'R' Us and the manufacturers, and compliance with these requests²⁴² Toys 'R' Us has not challenged this finding on appeal. As it is well-recognized, vertical non-price agreements can increase competition.²⁴³ An important distinguishing factor in the *Toys 'R' Us* case was that the key manufacturers committed to adopt the restraints only when they received assurances that their competitors were adopting substantially similar restrictions.²⁴⁴ No individual toy manufacturer wanted to give up this promising new retail outlet unless its competitors would do the same. This significantly reduced any likelihood that competition would be increased by the restraints. Indeed, the Commission found that Toys 'R' Us' actions both deprived consumers of the low prices that Toys 'R' Us' competitors could provide and insulated Toys 'R' Us from competitive pressures of the club stores.²⁴⁵

Two other factors distinguish this case from the typical vertical restraint case. First, Toys 'R' Us had significant power to influence the

²³⁶ 472 U.S. 284, 298 (1985).

²³⁷ See *In re Toys 'R' Us*, 1998 FTC LEXIS 119, at *105.

²³⁸ See *id.* at *123.

²³⁹ See *id.* at *144-*45.

²⁴⁰ *Id.* at 157.

²⁴¹ 250 U.S. 300, 307 (1919).

²⁴² See *In re Toys 'R' Us*, 1998 FTC LEXIS 119, at *71.

²⁴³ See *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

²⁴⁴ See *In re Toys 'R' Us*, 1998 FTC LEXIS 119, at *71.

²⁴⁵ See *id.* at *157.

manufacturers. The manufacturers testified that it would be very difficult to replace sales to Toys 'R' Us,²⁴⁶ because it accounted for well over 30% of sales in most major metropolitan areas.²⁴⁷ Toys "R" Us was substantially larger than any other retailer. Second, Toys 'R' Us vigorously asserted a free rider defense and the FTC found it wanting.²⁴⁸ Toys 'R' Us argued its actions were justified to combat free riding by the clubs on services provided by Toys 'R' Us. But the FTC found that Toys 'R' Us received cooperative advertising dollars that covered over 99% of the costs of advertising.²⁴⁹ Toys 'R' Us also argued that the clubs free ride on the fact that Toys 'R' Us carries product much earlier in the year. The FTC found, however, that Toys 'R' Us was specifically compensated for early purchases by not having to pay for the product till the end of the year.²⁵⁰ Finally, Toys 'R' Us argued that the manufacturers testified at trial that they adopted the restraints in response to free riding, yet the FTC found that manufacturers feared being placed at a competitive disadvantage unless their competitors adopted the same restraints.²⁵¹ These findings undercut any notion that the manufacturers restrained sales to the clubs for unilateral reasons such as stopping free riding.

4. *State Oil Co. v. Khan.*

The role of the antitrust agencies is not simply to bring enforcement actions - they should also clarify the law to promote more efficient distribution arrangements. In 1997, the Antitrust Division of DOJ and the FTC joined as *amici curiae* in filing a brief in *State Oil Co. v. Khan*,²⁵² asking the Supreme Court to reverse its 1968 opinion in *Albrecht v. Herald Co.*,²⁵³ that held that maximum resale price maintenance was *per se* illegal. The agencies' brief, relying on the Supreme Court's decision in *Atlantic Richfield Co. v. USA Petroleum*,²⁵⁴ observed that the manufacturer's decision to fix a maximum resale price may actually protect consumers against exploitation by the dealer acting as a local monopolist.²⁵⁵ Thus, it was the agencies' view that in the vertical *maximum* price fixing context, the *per se* illegality rule could be anti-consumer and ought to be changed. Moreover, the agencies asserted that the *per se* rule had little

²⁴⁶ *See id.* at *8.

²⁴⁷ *See id.*

²⁴⁸ *See id.* at *130-*147.

²⁴⁹ *See id.* at *137.

²⁵⁰ *See id.* at *138.

²⁵¹ *See id.* at *145-*146.

²⁵² Brief for the United States and the Federal Trade Commission as Amici Curiae Supporting Reversal, *State Oil Co. v. Kahn*, 522 U.S. 3 (1997).

²⁵³ 390 U.S. 145 (1968).

²⁵⁴ 495 U.S. 328 (1990).

²⁵⁵ *See* Brief for the United States and the Federal Trade Commission as Amici Curiae Supporting Reversal, *State Oil Co. v. Kahn*, 522 U.S. 3 (1997).

effect on government enforcement, since the antitrust agencies had not committed any enforcement resources to challenge a vertical maximum resale price maintenance arrangement in recent memory.²⁵⁶ The Supreme Court accepted these arguments and reversed the prior decision in *Albrecht*.²⁵⁷ One interesting aspect of this case was that the state attorneys general took the opposite position, and filed an amicus brief urging that *Albrecht* be retained.²⁵⁸

5. *Distribution on the Internet*

Clearly the fastest growing retail market is commerce on the Internet. Over the past few years the number of retail sites has grown dramatically and many traditional retailers have entered with their own Internet sites. The amount of commerce on the Internet has grown exponentially.²⁵⁹

The role of antitrust in emerging markets such as electronic commerce ("e-commerce") is to make sure that competitors have the opportunity to compete, to offer new products and services, and to reach the consumer in an efficient manner. Unfortunately when new markets arise, participants in the traditional market may act together to inhibit this development. Boycotts arose in the past in response to new forms of distribution. Discount car dealers, mail order firms, and 800-number retailers, have all encountered illegal boycotts brought by associations of more "traditional" retailers. The FTC has brought several cases in the past where firms attempt to prevent new forms of retailing from arising. Now, antitrust enforcers have again stepped in to prevent the boycott and permit new forms of retailing to grow and flourish in the context of e-commerce.

In 1998, the FTC brought a case to protect the opportunity to sell cars over the Internet.²⁶⁰ A Chrysler dealership in Kellogg, Idaho, used the Internet to attract customers from around the northwest by creating a web site where consumers could shop for cars from the comfort of their home.²⁶¹ The potential importance of Internet marketing in rural Idaho is substantial. Shopping for cars involves significant search costs and

²⁵⁶ *See id.*

²⁵⁷ *State Oil Co.*, 522 U.S. 3 (1997)

²⁵⁸ *See* Brief of Thirty-Three States and the Territory of Guam in Support of Respondents, *State Oil Co. v. Kahn*, 522 U.S. 3 (1997).

²⁵⁹ *See* The Internet Economy Indicators, (visited Apr. 27, 2000) <<http://www.internetindicators.com>>; David A. Balto, Emerging Antitrust Issues in Electronic Commerce, Remarks before the 1999 Antitrust Institute, Columbus, Ohio (Nov. 12, 1999) (transcript available at <<http://www.ftc.gov/speeches/other/e-commerce.htm>>) (visited Apr. 27, 2000).

²⁶⁰ *See In re Fair Allocation System, Inc.*, No. 971-0065, 63 Fed. Reg. 43,182 (Aug. 12, 1998) (proposed consent order).

²⁶¹ *See id.*

long drives to dealerships dispersed in different parts of the state, and a typical consumer might have few choices. By advertising on the Internet, this Kellogg dealer offered consumers in remote parts of the state the opportunity to shop in a far less costly and less time consuming fashion.

Not all the upper northwest car dealers responded favorably to this innovation. A group of 25 dealerships formed an association called Fair Allocation System ("FAS").²⁶² FAS collectively attempted to force Chrysler to change its vehicle allocation system to disadvantage the Internet advertiser.²⁶³ They threatened to refuse to sell Chrysler vehicles and to limit the warranty service they would provide to customers unless Chrysler changed its allocation system to disadvantage dealers that sold large quantities of vehicles outside their local geographic area.²⁶⁴ The FTC obtained a consent decree barring FAS from coordinating or participating in future boycotts.²⁶⁵

This does not mean, of course, that a manufacturer is compelled to deal with any Internet retailer. A manufacturer acting unilaterally has the right to refuse to deal with whomever it chooses. Indeed, a manufacturer may choose not to deal with retailers on the Internet because those retailers may free ride on the efforts of full service retailers. In the FAS case, that justification was absent since Chrysler applauded this dealership and its use of the Internet.²⁶⁶

E. DOMINANT FIRM CONDUCT

From 1980 to 1992, the antitrust agencies brought less than a handful of monopolization cases. In the 1970s, cases such as *In re IBM*²⁶⁷ and *In re Exxon*²⁶⁸ consumed vast prosecutorial resources in pretrial litigation in cases that were ultimately abandoned without any resolution of the substantive issues.²⁶⁹ Some commentators wondered whether the antitrust agencies could effectively enforce the law against abuse of mo-

²⁶² See *id.*

²⁶³ See *id.*

²⁶⁴ See *id.*

²⁶⁵ See *id.*

²⁶⁶ See *id.*

²⁶⁷ 475 F.Supp.1372 (S.D.N.Y. 1979), *aff'd* 618 F.2d 923 (2nd Cir. 1980), *mandamus granted*, 687 F.2d 591 (2nd Cir. 1982).

²⁶⁸ 98 FTC 453 (Sept. 16, 1981) (dismissal order).

²⁶⁹ In 1982, the Justice Department dropped its long-running case against IBM, a case that was filed on the last business day of the Johnson Administration in 1969. See *United States v. International Business Machines Corp.*, No. 69 Civ. 200 (S.D.N.Y. Jan. 17, 1969) (complaint). In 1981, the Commission dismissed its case against Exxon and seven other major oil companies who had been charged with collectively maintaining and reinforcing a noncompetitive market structure in the refining of crude oil into petroleum products. See *Exxon Corp.*, 98 FTC 453 (Sept. 16, 1981) (dismissal order).

nopoly power.²⁷⁰ Additionally, the agencies brought relatively few monopolization cases because the law in this area is difficult. Both the agencies and the courts recognize that the antitrust laws should not be used to dilute the incentive of companies to compete fiercely for market share even as they get close to monopoly levels. On the other hand, it is clear that monopoly can harm consumers and competition by leading to higher prices, reduced output, and reduced innovation. An effective monopoly policy is essential to maintain consumer choice, competitive prices, and a high level of innovation. Balancing these two priorities is not always easy.²⁷¹

Recent agency activity demonstrates that § 2 of the Sherman Act²⁷² can be enforced in a timely and effective manner by marshaling resources on narrowly focused cases where consumer harm is evident and relief can be accomplished without dampening the competitive aggressiveness of firms with large market shares. Two of the highest profile antitrust cases in years, *United States v. Microsoft*²⁷³ and *In re Intel*,²⁷⁴ both deal with dominant firm behavior in fast-growing industries. Maintaining competition in these industries is vital to the spread of technology and innovation across the entire economy.

1. *Intel*

In 1998, the FTC filed a complaint against Intel, alleging that it violated § 5 of the FTC Act²⁷⁵ by abusing monopoly power in the worldwide general purpose microprocessor market.²⁷⁶ Intel has monopoly

²⁷⁰ See William Kovacic, *Failed Expectations?: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration*, 74 IOWA L. REV. 1105, 1106-09 (1989).

²⁷¹ Of course, it is a generalization to imply that large, complex monopolization cases could never be successful. The Justice Department's monopolization case against AT&T, filed in 1976, led to the break-up of the world's largest monopoly firm and a subsequent period of rapid growth and innovation in the telecommunications industry. See *United States v. AT&T*, 552 F.Supp. 131 (D. D.C.1982) (consent decree), *aff'd sub nom.*, *Maryland v. United States*, 460 U.S. 1001 (1983).

²⁷² 15 U.S.C. § 2 (1999).

²⁷³ 87 F.Supp.2d 30 (2000).

²⁷⁴ No. 9288, 1999 FTC LEXIS 38, at *1 (Mar.17, 1999) (consent); 1999 FTC LEXIS 145, at *1 (Aug. 3, 1999) (decision and order).

²⁷⁵ 15 U.S.C. § 45 (1996). The FTC applies Sherman Act standards under § 5 of the FTC Act.

²⁷⁶ See *In re Intel Corp.*, No. 9288, 1999 FTC LEXIS 38, at *3 (Mar. 17, 1999). The microprocessor market has several unique features. Computer design and manufacture requires complex coordination between a number of different disciplines, almost always spread among many different firms. Microprocessors, memory components, core logic chips, graphics controllers, various input and output devices, and software must all work effectively with each other in order for the final product to work. To achieve effective integration, computer manufacturers require product specifications and other technical information about each component, and they require such information in advance of designing the computer in order to test and debug to insure the reliability and performance of each component and the system as a whole. This information is provided by all component makers, including Intel, subject to

power because its market share was approximately 80 percent of dollar sales.²⁷⁷ The microprocessor market has high entry barriers, including large sunk costs of design and manufacture, substantial economies of scale, customers' investments in existing software, the need to attract support from software developers, and reputational barriers.²⁷⁸ The FTC alleged that Intel sought to maintain its dominance by, among other things, denying advance technical information and product samples of microprocessors to Intel customers ("original equipment manufacturers" or "OEMs") and threatening to withhold product from those OEMs in order to coerce those customers into licensing their patented innovations to Intel.²⁷⁹

The FTC's complaint charged that Intel suspended its traditional information sharing with three customers - DEC, Intergraph, and Compaq - in order to force those customers to end disputes with Intel concerning the intellectual property rights and to grant Intel licenses to patented technology (not just microprocessor technology) developed and owned by those customers.²⁸⁰ Digital and Compaq capitulated quickly and entered into cross-license arrangements with Intel. Intergraph was able to resist only because it succeeded in obtaining an injunction against Intel's conduct in a federal court.²⁸¹

Intel's conduct was exclusionary because it reinforced its dominance of the general purpose microprocessor market in at least three ways. First, Intel's alleged conduct would give it access to technology being developed by others in the industry and disadvantage other microprocessor manufacturers that are trying to challenge Intel's dominance. Second, forcing other firms to license away rights to their proprietary technology dulls the incentive to innovate, thus harming competition in several ancillary markets. Third, Intel's forced acquisition of nonprocessor technology from computer OEMs reduces the abil-

formal nondisclosure agreements. This information sharing has substantial commercial value to both sides of the agreement, the component makers and the computer original equipment manufacturers ("OEMs").

The computer industry is characterized by short, dynamic product cycles, which are generally measured in months. Time to market is crucial. Denial of advance product information is virtually tantamount to a denial of actual parts, because an OEM customer lacking such information cannot design new computer systems on a competitive schedule with other OEMs. An OEM who suffers denial of such information over a period of months will lose much of the profits it might otherwise have earned even from a successful new computer model. Continued denial of advance technical information to an OEM by a dominant supplier can make a customer's very existence as an OEM untenable.

²⁷⁷ See *id.*

²⁷⁸ See *id.* at *4-*6.

²⁷⁹ See *id.* at *6.

²⁸⁰ See *id.* *8-*19.

²⁸¹ See *Intergraph Corp. v. Intel Corp.*, 3 F.Supp.2d 1255 (N.D.Ala. 1998), *vacated* 195 F.3d 1346 (Fed. Cir. 1999).

ity of those OEMs to support a non-Intel microprocessor platform by taking away an OEM's proprietary technology that could have been used to market its machines. Thus, for example, Compaq would be much less able to support an AMD or Digital microprocessor system by advertising its own technology because Intel has forced Compaq to license that other technology to Intel. Intel could in turn license Compaq's technology back to other OEMs that support Intel microprocessor platform.

Such conduct harms consumers, not only because competition brings lower prices, but also because competition is a powerful spur to the development of new, better, and more diverse products and technologies. Unjustified conduct by a monopolist that removes the incentive to such competition by depriving innovators of their reward or otherwise tilting the playing field against new entrants or fringe competitors has a direct and substantial impact upon future consumers. In the absence of a legitimate business justification that outweighs these concerns, such conduct constitutes a violation of § 2 of the Sherman Act,²⁸² and therefore, § 5 of the Federal Trade Commission Act.²⁸³

Intel case was settled by a consent order.²⁸⁴ The consent order prohibits Intel from withholding or threatening to withhold certain advance technical information or microprocessors from a customer for reasons relating to an intellectual property dispute with that customer.²⁸⁵ This requirement is limited to the types of information that Intel routinely gives to customers to enable them to use Intel microprocessors, and it does not impose a "compulsory licensing" requirement in the first instance.²⁸⁶ The order allows companies in disputes with Intel to continue to receive relevant information except where the customer elects to seek an injunction against Intel's manufacture, use, sale, offer to sell, or importation of Intel's microprocessors.²⁸⁷ The order is also careful to protect Intel's legitimate intellectual property rights. Intel is not required to continue providing information or products with respect to the microprocessors that the customer is seeking to enjoin.²⁸⁸ In addition, Intel may withhold information for legitimate business reasons, such as a breach of the disclosure agreement.²⁸⁹

The Intel settlement is important to maintaining competition in several areas. The order has the effect of defining an abuse of monopoly

²⁸² 15 U.S.C. § 2 (1999).

²⁸³ 15 U.S.C. § 45 (1996).

²⁸⁴ See *In re Intel Corp.*, 1999 FTC LEXIS 145, at *1 (Aug. 3, 1999) (decision and order).

²⁸⁵ See *id.* at *10-*11.

²⁸⁶ See *id.* *12-*13.

²⁸⁷ See *id.*

²⁸⁸ See *id.*

²⁸⁹ See *id.*

power as the use of that power to extract proprietary, legally-protected intellectual property from potential competitors. Otherwise, a dominant firm in a high tech industry could use its current market power to extend its dominance to complementary products and to next generation products. For instance, as the selling of PCs becomes more commoditized, there is a danger that an Intel could own the only valuable brand in the industry. Thus, Intel might come to dominate an even larger market than microprocessors.

2. *Microsoft*

The Justice Department's complaint against Microsoft, the second example of a dominant firm in desk top computer markets, is still in litigation at the District Court level, at the time of this writing.²⁹⁰ The complaint alleges abuse of monopoly power in the market for desktop IBM-compatible operating systems ("PC systems").²⁹¹ Microsoft makes the Windows operating system, which has a large share of the world market for PC operating systems.²⁹² However, Microsoft's monopoly power over PC operating systems is threatened by Netscape's Internet browser, which can be used to distribute Sun Java, which in turn enables software programs to run on any operating system.²⁹³

Several key features of this market reinforce Microsoft's monopoly power in PC operating systems. First, there is an "applications barrier to entry" into the operating systems market.²⁹⁴ Software products provide the ends that support the means, the operating system. Without the applications software, there would be substantially diminished demand for the operations software. Second, operating systems are subject to substantial network effects. As the number of users of any operating system increases, the consumer demand for the operating system increases too.²⁹⁵ At some point in the past, the demand for PC operating systems tipped in Microsoft's favor, creating substantial barriers to entry into this market, resulting in the acquisition of market power by Microsoft.

The Justice Department's claim is that Microsoft has abused its dominant power in the PC operating systems market in an attempt to gain dominance in the complementary market for Internet browsers, as well to

²⁹⁰ The most recent activity in the case was the release of findings of fact, see *United States v. Microsoft*, 65 F.Supp.2d 1 (1999), and the conclusions of law on April 3, 2000, see 87 F.Supp.2d 30 (2000).

²⁹¹ See *Microsoft*, 65 F.Supp.2d, at 3-6. Twenty states filed a similar complaint that has merged with the United States' case against Microsoft. See *New York v. Microsoft Corp.*, 65 F.Supp.2d 1 (1999).

²⁹² See *Microsoft*, 65 F.Supp.2d at 4, 24.

²⁹³ See *id.* at 21.

²⁹⁴ See *id.* at 10-11.

²⁹⁵ See *id.* at 11 (explaining how these network effects enhance the barriers to entry.).

maintain its dominance in the operating systems market. For example, Microsoft allegedly requires computer manufacturers, in order to receive a license for Microsoft's Windows operating system, to agree not to remove Microsoft's Internet browser from the computers or not to allow a more prominent display of any rival browser.²⁹⁶ Microsoft has also refused to list Internet service providers on its Windows display screen or in its Internet service providers referral system unless the providers withhold information about other browsers and adopt proprietary standards that make Microsoft's browser work better than competitive browsers.²⁹⁷

The court rejected Microsoft's three defense claims: 1) that its activities in bundling its Internet browser with its Windows operating system are efficient and procompetitive; 2) that putting both features in one product improves the functioning of both the operating system and the applications products written for the operating system; and 3) that its contracts with the Internet service providers are nothing more than industry-common cross-promotional agreements.²⁹⁸

One of the most important aspects of both *Intel* and *Microsoft* cases is the speed and efficiency with which they were litigated. Again, the legacy of the antitrust monopolization cases from the 1970s was that several years would transpire before the cases even went to trial. Since many of these cases involved technology markets, the anticompetitive problems were often cured before the case went to trial. The antitrust agencies had taken these lessons seriously and acted accordingly. The *Intel* case was ready to go to trial less than nine months after it was filed. The *Microsoft* trial started within five months after it was filed. Although antitrust trials are costly and time-consuming, the agencies have focused their priorities to move these litigations in a timely and effective manner.

II. THE DEVELOPMENT OF COMPETITION POLICY

The antitrust agencies, of course, can only litigate a small number of the total antitrust cases. Private litigants bring much of the cases. Beyond bringing cases, the antitrust agencies serve an important role in providing guidance about antitrust practices to the private bar and businesses. They provide guidance through a variety of mechanisms including business review letters, staff opinion letters, guidelines on specific subjects, and even amicus briefs.²⁹⁹ Beyond that, the antitrust agencies can play an important role in developing competition policy more gener-

²⁹⁶ See *id.* at 35.

²⁹⁷ See *id.* at 41.

²⁹⁸ See *id.* at 44-50.

²⁹⁹ See *supra* Part I.D.4.

ally through a variety of mechanisms, including advocacy before regulatory agencies, participation in administration task forces, and reports to Congress. During the Clinton Administration, the antitrust agencies have been playing a more prominent role in developing policy and providing guidance.

A. THE FTC GLOBAL COMPETITION HEARINGS.

Soon after Robert Pitofsky became FTC Chairman, he announced that the FTC would conduct a series of hearings on global competition.³⁰⁰ The goal was a broad ranging reassessment of antitrust policy in light of how both globalization and technology developments were transforming the nature of competition.³⁰¹ Those hearings focused on how competition had changed and whether antitrust rules needed to be adjusted accordingly.³⁰² The FTC held 23 days of hearings and heard over 86 witnesses, including government regulators, academics, business persons, and representatives from the private bar. The FTC issued a report in May, 1996, *Anticipating the 21st Century: Competition Policy in the New High Tech Global Marketplace*.³⁰³ The report discussed a variety of issues, including:

The changing nature of competition - the report documented that the increase in the intensity of high tech competition is changing in important respects the way the world does its business.

The Globalization of Competition – the report noted that vastly increased world trade has significant antitrust implications.

Efficiencies - the report focused and accelerated the debate on the treatment of efficiencies in merger enforcement and more generally in antitrust policy.

Other issues - the report touched on a wide range of other antitrust issues including the failing firm defense, definition of relevant geographic market, and a preview of areas that deserve or require future attention, such as the definition of innovation markets at the intersection of antitrust and intellectual property and competitive effects of networks and standards.

³⁰⁰ See FTC, Press Release, *FTC Announces Hearings on Antitrust and Consumer Protections Laws in Global High-Tech Economy* (visited Mar. 24, 2000) < <http://www.ftc.gov/opa/1995/9507/hearing1.htm>>.

³⁰¹ See *id.*

³⁰² See FTC Staff Report, *supra* note 140.

³⁰³ See *id.*

The hearings reflected a general consensus that the traditional core of antitrust - hostility to cartels, need to control abuses of monopoly power, prudent merger enforcement - has served the country well and requires no drastic change.³⁰⁴ Rather, the report focused on aspects of antitrust that may require adjustment in the light of changing competitive conditions.³⁰⁵

B. GUIDELINES.

One of the important functions of the agencies in providing guidance is the issuance of guidelines on various business practices. The Antitrust Division began this process back during the Johnson Administration when the first merger guidelines were issued.³⁰⁶ This process was accelerated during the Reagan Administration where the merger guidelines were revised and additional guidelines were issued on vertical restraints and international operations.³⁰⁷ Although the merger guidelines have received general praise for putting merger analysis on a sound theoretical foundation, the other guidelines were less favorably received. The vertical restraint guidelines were condemned by Congress as being a trial court brief attempting to move the law.³⁰⁸ The international guidelines³⁰⁹ were similarly criticized for being far broader than their supposed focus on international competition and for attempting to rewrite the law in a variety of other areas.³¹⁰

During the Clinton Administration a number of different guidelines have been issued. First, the international guidelines were reissued to focus strictly on international jurisdiction issues.³¹¹ Second, and perhaps the most important, guidelines on intellectual property licensing were issued.³¹² These guidelines were initiated at the Justice Department and

³⁰⁴ See *id.*

³⁰⁵ See *id.*

³⁰⁶ See DEPARTMENT OF JUSTICE 1968 MERGER GUIDELINES, reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,101.

³⁰⁷ See 1982 MERGER GUIDELINES, *supra* note 5; 1984 MERGER GUIDELINES, *supra* note 137; VERTICAL RESTRAINT GUIDELINES, *supra* note 190; DEPARTMENT OF JUSTICE 1988 ANTITRUST GUIDELINES FOR INTERNATIONAL OPERATIONS, reprinted in 4 Trade Reg. Rep. (CCH) ¶13,109, [hereinafter INTERNATIONAL GUIDELINES] .

³⁰⁸ H.R. 2965, 99th Cong., § 605 (1985) ("Whereas such policy guidelines are inconsistent with established antitrust law. . . be it resolved that it is the view of Congress that the antitrust enforcement policy guidelines stated in "Vertical Restraints Guidelines". . . should be recalled by the Attorney General.").

³⁰⁹ See INTERNATIONAL GUIDELINES, *supra* note 308.

³¹⁰ See Donald I. Baker & Bennet Rushkoff, *The 1988 Justice Department Guidelines: Searching for Legal Standards and Reassurance*, 23 CORNELL INT'L L.J. 405 (1990).

³¹¹ See Department of Justice & Federal Trade Commission, Antitrust Enforcement Guidelines for International Operations, reprinted in, 59 Fed. Reg., 52,810 (draft). The official guidelines were adopted in April of 1995, (visited Mar. 24, 2000) <<http://www.usdoj.gov/atr/public/guidelines/internat.htm>>.

³¹² See INTELLECTUAL PROPERTY GUIDELINES, *supra* note 69.

were adopted both by the DOJ and FTC. The guidelines have established a number of important principles that try to clarify the law on the antitrust treatment of intellectual property.

One of the more controversial antitrust issues during the Clinton Administration has been the antitrust treatment of health care arrangements. In response to controversy in this area, the FTC and the DOJ have issued three sets of guidelines on health care arrangements. The guidelines issued in 1993 provided general guidance primarily about cooperative arrangements among health care providers.³¹³ These were expanded in 1994 with further guidelines that addressed the additional issues of hospital joint ventures, providers' collective provision of fee-related information to purchasers of health care services, and multiprovider networks (e.g., combinations of hospitals and physicians).³¹⁴ The controversy on the treatment of antitrust and health care remained unabated, and in 1996 there were several legislative proposals to provide greater antitrust immunity for healthcare providers who wished to negotiate jointly. In response to these proposals the antitrust agencies once again revised their guidelines to make it clear that a wide variety of collective activity would not raise antitrust concerns.³¹⁵

In the merger area, the 1992 Horizontal Merger Guidelines³¹⁶ have generally gone without a great deal of challenge. As described earlier, based on concerns raised in the 1995 global competition hearings, however, the antitrust agencies revised the efficiencies section of the guidelines in May 1997.³¹⁷ The antitrust enforcement agencies were concerned that the earlier treatment of efficiencies was too narrow and unsympathetic to the potential efficiencies that could arise.

Besides guidelines, an important function of the antitrust agencies is to provide guidance to specific businesses about contemplated business practices. The FTC and the Antitrust Division have different procedures in place. The Antitrust Division has a business review procedure and the FTC provides what are known as staff opinion letters. These procedures were not used often in the early 1990s mostly because the agencies often did not respond in a timely fashion.³¹⁸

³¹³ See *Enforcement Statements in the Health Care Area*, 4 Trade Reg. Rep. (CCH) ¶ 13,151 (1993).

³¹⁴ See *Statement of Enforcement Policy and Analytical Principles Relating to Health Care and Antitrust*, 4 Trade Reg. Rep. (CCH) ¶ 13,152 (1994).

³¹⁵ *Statements of Antitrust Enforcement Policy in Health Care*, 4 Trade Reg. Rep. (CCH) ¶ 13,153 (1996). For a description of the evolution of these guidelines, see David A. Balto, *Cooperating to Compete: Antitrust Analysis of Health Care Joint Ventures*, 42 St. Louis L.J. 191 (Winter 1998).

³¹⁶ 1992 HORIZONTAL MERGER GUIDELINES, *supra* note 51.

³¹⁷ See 1997 HORIZONTAL MERGER GUIDELINES, *supra* note 141.

³¹⁸ In one case it took the Antitrust Division over four years to issue a business review letter. By that time the business that had requested the letter had gone out of business

With the issuance of the Health Care Guidelines,³¹⁹ both agencies committed to respond to requests for staff opinions and advice within 90-120 days. Based on that commitment, the number of advisory opinions issued by the two agencies increased substantially over the past few years.³²⁰

C. *AMICUS CURIAE* PARTICIPATION

An important aspect of the antitrust agencies is participation as an amicus in private antitrust litigation. Both agencies have intervened in this fashion in order to inform the courts about various issues of antitrust law.³²¹

At the beginning of the Reagan Administration, the DOJ had a particularly aggressive amicus program. Through that program it sought to provide greater clarity to the economic analysis behind various types of anticompetitive conduct. Although much of the program was successful, the Democratic-controlled Congress did not favor it. When in 1984 the DOJ filed an amicus brief before the Supreme Court asking the Court to rescind the *per se* illegality rule against resale price maintenance,³²² Congress passed a rider to the Antitrust Division's appropriations preventing it from arguing the case before the Court.³²³

The amicus program in the Clinton Administration, which tries to clarify the law where appropriate, has taken a fairly balanced approach. Besides the participation in *State Oil v. Kahn*,³²⁴ the agencies have been involved in a number of other matters. Two examples of such involvement are *NYNEX v. Discon, Inc.*³²⁵ in the Supreme Court, and *Surgical Care Center v. Hospital Service District*³²⁶ in the Fifth Circuit.

1. *NYNEX*

In *NYNEX*,³²⁷ Justice Breyer, writing for a unanimous Court, addressed the question of "the applicability of the *per se* group boycott rule where a single buyer favors one seller over another, albeit for an improper reason."³²⁸ The case arose from the aftermath of the break-up of the Bell System in 1984. In order for the local operating companies to

³¹⁹ See *supra* note 315.

³²⁰ See Department of Justice, Antitrust Division, *10-year Workload Statistics Reports, Fiscal Year 1990-1999* (visited May 2, 2000) <<http://www.usdoj.gov/atr/public/4504.htm>>.

³²¹ See *supra* note 256.

³²² See *Monsanto v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984).

³²³ H.R. 2965, 99th Cong., § 605 (1985).

³²⁴ 522 U.S. 3 (1997).

³²⁵ 525 U.S. 128 (1998).

³²⁶ 171 F.3d 231 (5th Cir. 1999) (en banc).

³²⁷ 525 U.S. 128 (1998).

³²⁸ *Id.* at 133.

provide to their customers the mandated access to long-distance companies competing with AT&T, old switching equipment often had to be removed and new equipment installed. Discon sold removal services to a NYNEX subsidiary, but filed suit alleging that NYNEX and its subsidiaries took actions that injured Discon and benefited a removal services competitor, AT&T Technologies. The district court dismissed the complaint, and the Second Circuit affirmed the dismissal with one exception—an allegation that a NYNEX subsidiary switched its purchases from Discon to AT&T Technologies as part of an attempt to hoodwink regulators and overcharge customers.³²⁹ The Second Circuit revived this allegation under a theory that it stated at least a cause of action under § 1's rule of reason,³³⁰ and possibly a *per se* violation, as a group boycott.³³¹ The Supreme Court granted *certiorari* to consider that exception.³³²

The antitrust agencies filed an amicus brief expressing their concern that *per se* rules may be over-extended to situations with ambiguous competitive effects.³³³ The Court concurred with the agencies' position. The Supreme Court clarified that it will not treat a boycott as *per se* illegal unless it involves a horizontal agreement, relying in part on the *Business Electronics v. Sharp Electronics*³³⁴ holding that vertical restraints are not illegal *per se* unless they include some agreement on price or price levels.³³⁵ The court reiterated the distinction between antitrust violations and business torts, even those involving "pure malice."³³⁶

2. *Surgical Care Center*

In *Surgical Care Center v. Hospital Service District*,³³⁷ the question was the scope of the "state action" exemption as applied to the actions of a political subdivision of the state rather than the state acting as sovereign.³³⁸ The FTC's concern with application of the "state action" exemption to political subdivisions of the state has generally come up in the context of FTC's antitrust actions against state regulatory bodies.³³⁹

³²⁹ 93 F.3d 1055, 1063-64 (2nd Cir. 1996).

³³⁰ 15 U.S.C. § 1 (1999).

³³¹ *See id.* at 1061.

³³² 523 U.S. 1019.

³³³ Brief for the United States and the Federal Trade Commission as Amici Curiae in Support of Vacating the Judgment, *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 123 (1998).

³³⁴ 485 U.S. 717, 735-36 (1988).

³³⁵ *See NYNEX*, 525 U.S. at 136.

³³⁶ *Id.* at 137.

³³⁷ 171 F.3d 231 (5th Cir. 1999) (en banc).

³³⁸ *See id.* at 234.

³³⁹ *See, e.g., In re Massachusetts Board of Registration in Optometry*, 110 FTC. 549 (1988); *FTC v. Tigor Title Insurance Co.*, 504 U.S. 621 (1992).

In *Surgical Care Center*, a panel of the Fifth Circuit initially upheld the district court. The Fifth Circuit found that the authorizing state legislation invoked by the hospital district exempting its alleged antitrust violations satisfied the *Town of Hallie v. City of Eau Claire*³⁴⁰ test as to whether the state had shown a “policy to displace competition.”³⁴¹ These earlier decisions had relied on a statute that merely enabled the hospital district to enter into joint ventures and conduct closed meetings—to act in those regards like a private business entity—in order to put it on an equal competitive footing with private businesses. The FTC and the Antitrust Division, as enforcement agencies, had serious concerns with such a stunningly broad reading of the state legislation. The *en banc* court shared these concerns, and reached the conclusion that a statute intended to authorize a government agency to act like a business didn’t contemplate that it would act like a business that was violating the antitrust laws.³⁴²

III. IMPROVEMENTS IN THE PROCESS

Antitrust agencies are administrative bodies, and one of the important aspects of antitrust enforcement is improving the process of those agencies. Antitrust investigations can impose significant burdens on businesses, both in terms of compliance with information requests and in delays in proposed business conduct, such as mergers. Antitrust agencies face ever-increasing challenges and demands on the increasingly limited enforcement resources. For these reasons, the agencies have looked critically at their enforcement process to find more efficient and effective means of utilizing their resources. Three examples are the Hart-Scott-Rodino (“HSR”)³⁴³ merger process, merger divestitures, and the FTC’s administrative adjudication process.

A. MANAGING THE HSR PROCESS.

The premerger notification process established by the Hart-Scott-Rodino Act in 1976 is a cornerstone of modern merger enforcement.³⁴⁴ The Act provides timely notification to the antitrust agencies of proposed mergers and acquisitions,³⁴⁵ so the agencies can review a proposed transaction for possible competitive problems,³⁴⁶ and provides a waiting pe-

³⁴⁰ 471 U.S. 34 (1985).

³⁴¹ *Surgical Care Center*, 153 F.3d 220, 224 (5th Cir. 1998), *rev’d en banc*, 171 F.3d 231 (5th Cir. 1999), *cert. filed*, Aug. 2, 1999.

³⁴² *See Surgical Care Center*, 171 F.3d at 234-35.

³⁴³ Hart-Scott-Rodino Antitrust Improvements Act of 1976, Pub. L. No. 94-435, 90 Stat. 1383 (codified in pertinent part at 15 U.S.C. § 18a (1999)).

³⁴⁴ *See Clayton Act*, § 7(a), 15 U.S.C. § 18a (1999).

³⁴⁵ *See id.* § 18a(a), (b).

³⁴⁶ *See id.*

riod before the transaction can proceed to give the agencies sufficient time to review a transaction and, if necessary, initiate action to resolve competitive problems before they arise.³⁴⁷ The HSR program has been hugely successful in achieving its statutory objectives to give the anti-trust agencies a meaningful opportunity to review and, if necessary, challenge anticompetitive mergers and acquisitions before they occur, and to preserve a meaningful opportunity for effective relief. Pre-HSR history demonstrated that post-consummation merger challenges took an inordinate amount of time to resolve, were costly, and often ended in ineffective relief even if the court ruled for the government at trial - it was too difficult to "unscramble the eggs" and restore effective competition.³⁴⁸ To remain a useful enforcement tool, however, the HSR program must be administered with care.

Undeniably, the HSR process can impose significant burdens on businesses. The premerger rules are complicated, and may require the submission of a considerable amount of information in the second request phase. But the appropriate question is whether the premerger requirements are reasonably necessary in light of the agencies' enforcement responsibilities and the resulting consumer benefit. For the most part, the burdens imposed by HSR are fundamental to the process and are unavoidable if HSR is to achieve its statutory objectives. Nonetheless, government has a self-imposed obligation to minimize those burdens, and to eliminate any unnecessary burdens. Careful management of the HSR process, therefore, is a core function of the antitrust agencies.

During the early days of the Clinton Administration, then-FTC Chairman Janet Steiger and Assistant Attorney General Anne Bingaman announced an ambitious set of policy initiatives aimed at addressing concerns about the HSR process.³⁴⁹ Those reforms included:

- Development of proposals to increase the number of transactions exempt from HSR requirements;
- Adoption of procedures to expedite the clearance process;
- Issuance of a joint FTC/DOJ model second request;³⁵⁰

³⁴⁷ See *id.*

³⁴⁸ For a review of the HSR Act and its successes, see, e.g., William J. Baer, *Reflections on Twenty Years of Merger Enforcement Under the Hart-Scott-Rodino Act*, 65 ANTITRUST L.J. 825 (Spring 1997).

³⁴⁹ See U.S. DEPARTMENT OF JUSTICE AND FEDERAL TRADE COMMISSION, HART-SCOTT-RODINO PREMERGER PROGRAM IMPROVEMENTS (Mar. 23, 1995).

³⁵⁰ The HSR stays a merger for a certain period of time, usually 30 days. If, during that period, the reviewing agency decides that it needs more information in order to determine if the merger is likely to be anticompetitive, it may issue a request for additional information, commonly called a "second request." The second request stays the consummation of the merger for an additional 20 days from the date of substantial compliance with the second request.

Implementation of uniform procedures to review the burden of second requests and to examine disputes as to substantial compliance;
 Adoption of a joint "quick look" policy for reviewing HSR filings.

Below we discuss the agencies' records in building upon those initiatives, along with another core function, maintaining the integrity of the HSR process.

1. *Reducing Burdens Generally*

Two problems have been identified over the years. The first problem is the number of transactions covered by HSR requirements. Critics of the process have urged the expansion of HSR exemptions and raising of HSR reporting thresholds.³⁵¹ The second problem is the time required for the antitrust agencies to complete their review. These issues are discussed below.

a. *Expanded HSR Exemptions and Higher Thresholds*

Exempting transactions from HSR requirements has been a difficult issue because the transactions with real competitive significance need to be reported and examined prior to closing. Although relatively few transactions present serious competitive concerns, it is usually impossible to determine the competitive ramifications of any particular transaction until it is reviewed, because merger analysis is very fact-specific and case-specific. Therefore, it is necessary to review a large number of transactions to find the relative few that are problematic.

The agencies have remained open to promulgating exemptions from HSR requirements, but have proceeded cautiously. Broad exemptions from HSR requirements are not practical, because it is exceptionally difficult to specify what should be exempt. There have been two major expansions of HSR exemptions since the premerger rules were implemented.³⁵² The first was in 1979, three years after the HSR Act became law, and only one year after the implementing rules came into effect.³⁵³ The FTC, with the concurrence of the Department of Justice, revised section 802.20 of the rules to exempt a large number of very small transactions.³⁵⁴ A review of the first year's experience under the premerger

³⁵¹ Responding to such criticism, several bills have been introduced in the current Congress to raise HSR thresholds. For example, Congressman Rogan introduced the "Small Business Merger Fee Reduction Act of 2000." H.R. 4194, 106th Cong. (App. 5, 2000).

³⁵² There have been other amendments, in 1983 and 1987, to clarify and refine the premerger rules.

³⁵³ See 44 Fed. Reg. 66,781 (Nov. 21, 1979) (codified as amended, 16 C.F.R. § 802.20).

³⁵⁴ See *id.* at 66,782.

rules indicated that those transactions were unlikely to raise any antitrust concerns.³⁵⁵ The revised rule decreased the number of required filings by about 20%.³⁵⁶

The second major expansion of HSR exemptions took place during the Clinton Administration. The FTC, with the concurrence of the Department of Justice, formally adopted five amendments to the premerger rules that broadened the classes of transactions exempt from HSR requirements.³⁵⁷ One purpose of the amendments was to clarify the requirements and broaden the class of acquisitions exempt from HSR requirements as transfers of goods or realty in the "ordinary course of business."³⁵⁸ Other rules exempted from HSR requirements the acquisitions of certain categories of real property assets,³⁵⁹ the acquisitions of oil and natural gas reserves valued at \$500 million or less,³⁶⁰ the acquisitions of coal reserves valued at \$200 million or less,³⁶¹ and the acquisitions of securities whose underlying value is represented solely by those kinds of exempt assets.³⁶² Those acquisitions are unlikely to violate the antitrust laws. Another rule exempted acquisitions by certain investors of rental real property. Those transactions likewise are not likely to violate the antitrust laws.

These new exemptions eliminated the filing requirement for up to 10% of the transactions that would have been reportable under the previous rules. This results in substantial saving of time and money for certain businesses. Despite such efforts to reduce the number of filings, there is some criticism that the Act requires the reporting of too many transactions.³⁶³ This is a serious public policy issue, and there are some legitimate arguments on both sides. Any modifications of the thresholds should be drafted carefully to avoid undermining the public interest in effective antitrust enforcement.

b. Expedited Inter-Agency Clearance.

One significant issue the FTC and the Department of Justice have faced over the years is the amount of time it takes for the two agencies to

³⁵⁵ See Malcolm R. Pfunder, *Premeger Notification After One Year: An FTC Staff Perspective*, 48 ANTITRUST L.J. 1487, 1490-91 (1979).

³⁵⁶ See *id.* at 1491 (stating that changes, "would have eliminated about 20 percent of the filings received . . . about the first of April of 1979.").

³⁵⁷ See 61 Fed. Reg. 13,666 (Mar.28, 1996) (codified as amended, 16 CFR §§ 802.1, 802.2, 802.3, 802.4, 802.5, 802.15).

³⁵⁸ *Id.* at 13,668.

³⁵⁹ See *id.* at 13,674-678.

³⁶⁰ See *id.* at 13,678.

³⁶¹ See *id.*

³⁶² See *id.* at 13,679.

³⁶³ See generally Symposium: Twenty Years of Hart-Scott-Rodino Merger Enforcement, 65 ANTITRUST L.J. 813 (1997).

decide jurisdiction over a transaction. That process is called "clearance," and given the short period allowed for HSR investigations, a timely decision as to which agency will investigate is critical. Most transactions are cleared quickly to one agency or the other. However, where both agencies have an interest in investigating a transaction, it may take some time to determine which agency is best suited to the task. At the outset of the Clinton Administration, there was growing concern that the FTC and the DOJ were taking too long to resolve the issue which agency will conduct the investigation. Lack of a timely resolution imposed unnecessary delay on the parties and reduced the time available for staff to conduct the initial review of the transaction.

The agencies acknowledged the problem and implemented new procedures that substantially shortened the average time for resolving clearance in April, 1995.³⁶⁴ The faster clearance has benefited both the agencies and merging parties. The agencies have benefited by having more time for investigation during the initial waiting period, resulting in more focused investigations and better-informed decisions on whether to issue a second request. First, in some cases the agencies can complete their initial review and grant early termination of the HSR waiting period at an earlier date than was previously possible. In fiscal year 1998, for example, 69% of the transactions were granted early termination of the waiting period, and the average time was 15.8 days to early termination.³⁶⁵ Second, earlier clearance allows the agencies to resolve potential competitive concerns without resorting to the second request process nearly as often. As shown below, only one to two percent of the transactions receive requests for additional information; the remainder are cleared to proceed within 30 days.³⁶⁶ Consequently, premerger review is more efficient. The clearance process still encounters occasional delays, but overall the process has been significantly improved.

2. *Reduction of Second Request Burdens*

The burden of responding to requests for additional information is another issue the agencies have addressed. In part, the improvement is the result of the above-described improvements in the clearance process. As a result of having more time for investigation during the initial 30-day waiting period, there is less need to issue requests for additional informa-

³⁶⁴ See Federal Trade Commission, Press Release, *Federal Trade Commission Announces New Joint Hart-Scott-Rodino Merger Review Procedures with the Department of Justice*, Mar. 23, 1995.

³⁶⁵ See 1998 HSR ANN. REP. (visited May 2, 2000) <<http://www.ftc.gov/bc/hsr/98annrpt/hsr98annual.htm>>.

³⁶⁶ The FTC's goal under the Government Performance and Results Act, 31 U.S.C. § 1101 (1999), is to keep the average time from filing to completion of the review for all transactions to less than 20 days.

tion. For example, as shown in the following table, during the fiscal years 1996-98, the FTC issued significantly fewer second requests as a percentage of reportable transactions compared to the previous three-year period.

FTC SECOND REQUESTS
FY 1993-98

Year	Adjusted Transactions*	FTC Second Requests	Second Requests/ Adjusted Transactions
1993	1,745	40	2.2%
1994	2,128	46	2.2%
1995	2,612	58	2.2%
1996	2,864	36	1.3%
1997	3,438	45	1.3%
1998	4,575	46	1.0%

* Adjusted transactions exclude those that are not subject to requests for additional information, including incomplete filings and non-reportable transactions.

In addition to reducing the relative frequency of issuing second requests, the agencies have reduced burdens on parties that receive them. The FTC's Bureau of Competition has made various efforts through the years to keep these burdens to reasonable levels, including using a "quick look" approach, model second requests, and at one time, appointing a second request "czar" to review second requests before they went to the Chairman's Office with a recommendation for issuance. In the mid-1990s, the agencies made further efforts to reduce the second-request burden through the development of an annotated, uniform model second request for both agencies. The goal was to achieve greater consistency between the two agencies, and to decrease burdens on reporting companies.

Since the adoption of the uniform model, there has been an overall reduction in document production burden in second requests. The sometimes-expressed perception that second requests invariably require a massive document production is not correct- some do, but those are the minority. In fiscal year 1998, at the FTC almost 50% of second requests resulted in productions less than 20 boxes for both parties combined, and over 70% had productions smaller than 50 boxes.³⁶⁷

In conjunction with the new model, the FTC has continued to use, whenever possible, a "quick look" policy that encourages document production in stages, focusing initially on issues that may be determinative in concluding that the transaction likely does not raise competitive

³⁶⁷ See Parker, Report, *supra* note 49, at 4.

problems. If the FTC can reach that conclusion based on a quick look, full document production is not necessary. A related benefit of a reduced burden of document production is that parties can respond to second requests more quickly. There has been an overall reduction in the time between issuance of the second request and substantial compliance, although, again, some merging parties still take considerable time to comply.

Perhaps the best measure of whether the HSR process is being managed effectively is comparing the number of second requests to the number of enforcement actions. The FTC secures relief in the vast majority of cases in which it issues a second request. Of course, bringing enforcement actions in 100% of our second requests would not be an appropriate measure of success, since in some cases issues can only be resolved based on information gathered in the second request.

The statistics demonstrate that the agencies are becoming even more diligent and select carefully the cases for second request review. The FTC has become even more proficient at issue identification and information gathering during the initial 30-day period. In addition, in many cases the parties have provided significant assistance by supplying the necessary information to avoid a second request. Thus, second requests are increasingly utilized only in the few cases that are necessary.

3. *HSR Enforcement*

The agencies also have stepped up enforcement against violations of the HSR. This is another element of the program to maintain and improve HSR as an effective enforcement tool. The success of the pre-merger notification program depends critically upon compliance. Since there can be strong incentives to avoid reporting certain transactions, it is important to prevent those incentives from determining the behavior of merging parties. Congress wisely provided for significant civil penalties for non-compliance—now \$11,000 for each day a firm is in violation,³⁶⁸ which can amount to millions in penalties before it is over.

Nonetheless, there have been some problems with various kinds of non-compliance, some inadvertent, some intentional. The FTC has taken vigorous action where it was warranted. In 1996, for example, the FTC collected record civil penalties in excess of \$7.5 million for violations of HSR with respect to three transactions.³⁶⁹ During the three years from FY 96 through FY 98, the FTC obtained consent judgments totaling \$13.9 million, almost 44% of the total collected during the 21 year his-

³⁶⁸ See Debt Collection Improvement Act of 1996, Pub. L. No. 104-134, § 31101(s) (codified as amended at 28 U.S.C. § 2461 nt. (1999)).

³⁶⁹ See FEDERAL TRADE COMMISSION, BUREAU OF COMPETITION, ENFORCEMENT ACTIVITIES, FISCAL YEAR 1996-MAR.31, 2000, 27-29.

tory of the program.³⁷⁰ A few examples will illustrate some of the problems encountered thus far.

PERCENT OF SECOND REQUESTS THAT RESULT IN
ENFORCEMENT ACTIONS*

Fiscal Year 95 (34/58)	58.6%
Fiscal Year 96 (23/36)	63.9%
Fiscal Year 97 (24/45)	53.3%
Fiscal Year 98 (31/46)	67.4%
Fiscal Year 99 Year to date (12/14)	85.7%
TOTAL (124/199)	62.3%

In *United States v. Sara Lee Corp.*,³⁷¹ FTC staff found reason to believe the acquiring firm had deliberately understated the value of U.S. assets it was acquiring (Kiwi Brands) in order to avoid reporting a highly problematic transaction. The agency found out about the acquisition after the fact, and investigated both the merger and the failure to comply with HSR. In 1994, Sara Lee agreed to a divestiture order to resolve a probable violation of § 7 of the Clayton Act.³⁷² In February, 1996, Sara Lee agreed to pay a then—record \$3.1 million civil penalty to settle charges that it violated the HSR Act.³⁷³

In *United States v. Automatic Data Processing Inc.*,³⁷⁴ the issue was whether the company had complied with the reporting form.³⁷⁵ Item 4(c) of the reporting form requires merging parties to turn over documents prepared by or for the parties for purposes of analyzing the transaction.³⁷⁶ Thus, 4(c) documents can quickly reinforce or contradict competitive concerns that investigators might have, or alert them to some that might otherwise be missed.³⁷⁷ In 1995, Automatic Data Processing

³⁷⁰ See *id.*

³⁷¹ See *In re Kiwi Brands*, 59 Fed. Reg. 48,894 (Sept. 23, 1994). See also Federal Trade Commission, Press Release, *Sara Lee Agrees to Pay Record Civil Penalty to Settle Charges Over Shoe Care Product Acquisition*, Feb. 6, 1996 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1996/9602/sara.htm>>.

³⁷² See *In re Kiwi Brands*, 59 Fed. Reg. 48,894 (Sept. 23, 1994).

³⁷³ See Federal Trade Commission, Press Release, *supra* note 372.

³⁷⁴ 124 FTC 456 (Oct. 24, 1997). The matter was placed before an administrative law judge in November of 1996, however the action was removed to the FTC on May 22, 1997 on a motion by both parties. See , 62 Fed. Reg. 34,293, 32, 294 (June 25, 1997) (proposed consent agreement).

³⁷⁵ See *Automatic Data Processing Inc.*, FTC Complaint (visited Mar. 24, 2000) <<http://www.ftc.gov/os/1996/9611/d9282cmp.htm>>.

³⁷⁶ See Federal Trade Commission, *Premerger/Hart-Scott-Rodino Form*, (visited Mar. 24, 2000) <<http://www.ftc.gov/bc/hsr/hsrform.htm>>.

³⁷⁷ Congressman Rodino recognized the critical importance of these kinds of documents when he sought passage of the premerger notification act that bears his name, “[T]he government will be requesting the very data that is already available to merging parties, and has

Inc. ("ADP") submitted an HSR filing without any 4(c) documents.³⁷⁸ After the transaction had been closed, the agency received complaints from the public that the acquisition had caused competitive harm. The discovery in the ensuing investigation revealed documents that clearly should have been filed under 4(c). The federal court complaint against ADP alleged that the HSR filing had been materially deficient, and that ADP failed to take the 4(c) requirement seriously.³⁷⁹ ADP agreed to settle those charges for \$2.97 million.³⁸⁰ This represented \$10,000 per day for each day ADP had failed to submit the 4(c) documents (the maximum daily penalty at the time)³⁸¹— up to the time the company submitted the documents and recertified its premerger notification. The investigation also uncovered evidence substantiating the concerns that ADP's acquisition was anticompetitive.³⁸²

Automatic Data Processing Inc., is not an isolated incident.³⁸³ Some HSR filings do not contain the kinds of 4(c) documents that one

already been assembled and analyzed by them. If the parties are prepared to rely on it, all of it should be available to the Government." 122 CONG. REC. H10293 (daily ed. Sept. 16, 1976) (statement of Rep. Rodino).

³⁷⁸ See *Automatic Data Processing Inc.*, FTC Complaint, *supra* note 376 ¶¶ 6, 7.

³⁷⁹ See *id.*

³⁸⁰ See Federal Trade Commission, Press Release, *ADP Settles FTC Charges Over Autoinfo Acquisition*, June 18, 1997 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1997/9706/adpauto3.htm>>.

³⁸¹ See Clayton Act, 15 U.S.C. § 18a(g)(1) (1999).

³⁸² The Commission later issued a decision against ADP under Section 7 of the Clayton Act and Section 5 of the FTC Act, including charges that ADP attempted to monopolize, and did in fact monopolize, a market for automobile salvage yard information systems. See 124 FTC 456 (Oct. 24, 1997).

³⁸³ For example, in 1997, the FTC obtained a consent judgment of over \$5.6 million - the highest civil penalty amount ever obtained under the HSR Act for a single transaction - against Mahle GmbH, a German automotive and diesel engine parts manufacturer with businesses in the United States, and Metal Leve, S.A., a competing Brazilian manufacturer, for their failure to file a premerger notification. See Federal Trade Commission, Press Release, *FTC Obtains \$5.6 Million from German and Brazilian Piston Manufacturers for Failure to File for U.S. Antitrust Review; Civil Penalty is Largest Ever*, June 19, 1997 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1997/9706/mmlcivp4.htm>>. The complaint alleged that both firms knew that their deal posed serious antitrust problems yet they completed the transaction knowing that they were violating the HSR Act. See FTC Complaint, (visited Mar. 24, 2000) <<http://www.ftc.gov/os/1997/9706/mahlecomp.htm>>. According to the complaint, each of the two firms "consulted with U.S. counsel or U.S. investment bankers and were apprized of the requirement under the HSR Act that they each file Notification and Report Forms with U.S. antitrust authorities." *Id.* at ¶ 18. In fact, the complaint alleges that each firm had "considered ignoring the HSR reporting requirements" and treating the HSR reporting obligation "as a trade off between the costs of compliance with the Act and the potential risks of noncompliance with the Act." *Id.* ¶ 20.

More recently, in the spring of 1999, the FTC obtained a \$2.785 million, the maximum available, consent judgment against Blackstone Capital Partners II Merchant Banking Fund LP in connection with its acquisition of Prime Succession, Inc. See Federal Trade Commission, Press Release, *Merchant Banking Firm, Partner Settle FTC Charges from Incomplete Pre-Merger Report*, Mar. 30, 1999 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1999/9903/blackst.htm>>. Moreover, for the first time, the agency required an official of the company to

would ordinarily expect from companies engaged in complex transactions in which the firms may be engaged in the same or related businesses. Sometimes, these documents show up only in response to a second request, and that late arrival is not considered timely compliance. If firms do not file those documents in response to Item 4(c) of the initial notification, and second requests are not issued, and the antitrust agencies may never discover those documents unless third parties come forward complaining about the merger, as was the case in *Automatic Data Processing Inc.* Accordingly, the antitrust enforcement agencies have made it a high priority to ensure that filing persons comply fully with Item 4(c).

The HSR Act was passed because it is difficult or even impossible to obtain effective antitrust relief after parties have merged their operations. In order to preserve the possibility of effective remedies for anticompetitive transactions, the Act establishes strict waiting periods during which the antitrust agencies may conduct their premerger review of all proposed transactions.³⁸⁴ Parties must wait until the period expires or is terminated by the agencies before they may proceed with their transactions.

Finally, while the FTC generally has not sought penalties for first-time negligent violations, a recent case suggests that it will not look the other way when a company clearly should have realized its filing obligation. In 1998, the FTC obtain a consent judgment for a \$500,000 civil penalty against Loewen Group, Inc., for its failure to make an HSR filing in its acquisition of Prime Succession, Inc.³⁸⁵ In this case, Loewen was an experienced acquirer intimately familiar with the HSR process, and it knew that the acquisition it planned - one of the three largest funeral home chains buying the fourth largest, which operated in many of the

pay a civil penalty as well. *See id.* The *Blackstone* case involved a failure to file a 4(c) document. *See* FTC Complaint, No. 1: 99C V00975, 1999 FTC LEXIS 73. Blackstone's request for early termination of the waiting period was granted and only after the merger was consummated did the FTC learn of a competitive problem. The FTC also required the payment of a civil penalty from the Blackstone official who certified the filing as "true, complete and correct" and was one of the authors of the 4(c) document that Blackstone failed to submit. *See id.* ¶¶ 40-47. There were a number of reasons for holding the individual liable. The investigation revealed that this official had primary responsibility for negotiating the underlying deal, knew it might raise antitrust questions, and knew that delaying the deal could jeopardize its closing. Moreover, he was one of the authors of the critical 4(c) document, knew of its importance to Blackstone's decision-making, and had a copy of it in his files. Finally, when questioned on Blackstone's failure to provide the document, he gave inconsistent answers. Therefore, the investigators were convinced that he knew or should have known that the filing was not "true, complete and correct."

³⁸⁴ *See* 15 U.S.C. § 18a(b) (1999).

³⁸⁵ *In re* Loewen Group, 122 F.T.C. 22 (July 29, 1996). *See also* Federal Trade Commission, Press Release, *Loewen Group Agrees to Pay \$500,000 Civil Penalty to Settle Federal Charges of Hart-Scott-Rodino Act Violations*, Mar. 31, 1998 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1998/9803/loewen.htm>>.

same markets - would receive antitrust attention. Further, Loewen's failure to file may have had something to do with the fact that the company faced a deadline to close the deal and the loss of a large down payment if it did not meet that deadline.

B. DIVESTITURE PROCESS

In the past few years the process of divestiture has been an area of considerable attention on the part of the antitrust enforcement agencies because most merger challenges are resolved through an agreement in which the parties consent to divest certain assets. Over the past few years there has been renewed attention to assuring that divestitures adequately restore competition. There was a perception by the private bar and business community that the agencies were primarily focused on bringing cases and paid less attention to whether or not the remedy in a particular case was adequate. The true test of success is not the number of settlements negotiated but whether the divestitures they called for promptly restored competition to effective markets. From the agencies' prospective, divestitures took too long, averaging typically well in excess of a year, and many failed to achieve their remedial purpose.

In 1995, the FTC staff began a study of divestiture orders issued from fiscal years 1990 through 1994. The study was released in August, 1999.³⁸⁶ This was the first systematic analysis of the FTC divestiture orders since the passage of the Hart-Scott-Rodino Premerger Notification Act in the 1970s.³⁸⁷ The staff reviewed 35 consent orders and conducted interviews in a case study format.³⁸⁸ The report discussed factors that made divestitures more or less successful and recommended how to make divestitures more effective.³⁸⁹ The experience reflected in this report provides a clear framework for understanding and changing the FTC's divestiture process.

Perhaps the most important change is the requirement that parties identify buyers in advance of accepting a divestiture settlement.³⁹⁰ The FTC now routinely insists upon finding up-front buyers as a part of every settlement. There are many advantages to identifying prospective buyers up front. In cases where there are concerns about the adequacy of a settlement, doing so allows the FTC to have some assurance that compe-

³⁸⁶ See FEDERAL TRADE COMMISSION, A STUDY OF THE COMMISSION'S DIVESTITURE PROCESS (Aug. 6, 1999) available from (visited Mar. 24, 2000) <<http://www.ftc.gov/os/1999/9908/index.htm#6>> [hereinafter FTC STUDY]. See also Federal Trade Commission, Press Release, *FTC Release Report on Commission's Divestiture Process*, Aug. 6, 1999 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1999/9908/divestreport.htm>>.

³⁸⁷ 15 U.S.C. §§ 1311-1314 (1999).

³⁸⁸ See FTC STUDY, *supra* note 386, at 7.

³⁸⁹ See *id.* at 15-38.

³⁹⁰ See Parker, Report, *supra* note 49, at 11.

tion will in fact be restored. In other words, it allows the FTC to determine whether the package of assets has been "market tested" by identifying a buyer with experience who believes those assets can adequately restore competition. Additionally, identification of up-front buyers allows quicker divestitures. Over the past three years the Commission has used up-front buyers in approximately 60 percent of all cases in which divestitures were required.³⁹¹

In cases where an up-front buyer is not required, the FTC has also significantly shortened the period of divestiture. Prior to 1995, the time period for divestiture was typically twelve months, and with additional time for public comment, that period often would extend for at least fifteen months.³⁹² Although some assets may be very complex and take some time to divest, a 12-month period was too long. Moreover, a long divestiture period allowed respondents to treat their promised divestitures as a low priority. Respondents would routinely file divestiture applications at the eleventh hour and these applications were often deficient. In response to this, the FTC significantly shortened the standard divestiture period. The period is now 4 months in most cases and is rarely more than 6 months.³⁹³ Moreover, the FTC has significantly improved its review of divestiture applications so these applications are reviewed and approved within a much shorter period of time.

The FTC began integrating the results of the Divestiture Study to the divestiture process, as the study was ongoing. In response to some of the concerns raised by the Divestiture Study, several changes were made in the approach to divestitures including shorter divestiture periods, up-front buyers, broader assets packages, and crown jewel provisions.³⁹⁴ Inclusion of such provisions is now the starting point in consent negotiations. As a result of these changes, the average time from the date the divestiture order is provisionally accepted and the date the Commission approves the order of divestitures has dropped from 15 months in FY 1995 to 7 months in FY 1996 to approximately 3 months FY 1997.³⁹⁵ Moreover, each of these changes has improved the ability of the party acquiring the divested assets to adequately compete.

Ultimately, the critical factor in merger cases is identifying the appropriate package of assets to be divested. The antitrust agencies are typically less willing to accept divestitures of assets that are short of

³⁹¹ See *id.*

³⁹² See FTC Study, *supra* note 386, at 39.

³⁹³ See *id.*

³⁹⁴ A "crown jewel" is a set of assets valued by the divesting company higher than the value placed on the assets to be divested. Thus, an order giving the trustee the power to divest the crown jewel assets if the other assets are not successfully divested by a certain time will provide the maximum incentive to complete the required divestiture in a timely fashion.

³⁹⁵ See FTC Study, *supra* note 386.

ongoing business because the FTC found that relief short of complete divestiture was often inadequate.³⁹⁶ For example, a licensing arrangement requiring an ongoing relationship between the divested and divesting parties often did not fully restore competition. Thus, the antitrust agencies' approach is typically to move away from forms of behavioral relief or licensing arrangements.

In addition, the antitrust agencies have been looking for broader assets packages. Economies of scale and scope often require that complementary products be manufactured or sold with the products, thereby raising competitive concerns. Therefore, the divestiture of a group of assets that is broader than a particular business is often necessary to assure the marketability, viability and competitiveness of the divestiture package.

Many recent enforcement actions involve high technology businesses in which the divested assets are rather sophisticated. In addition, in situations involving products such as pharmaceuticals, the party acquiring the divested assets must go through a regulatory approval process for their new product. To protect the divestiture process in these types of the cases the FTC is increasingly using trustees to monitor the divestiture process. During the period of divestiture it is important that someone with knowledge of the industry monitors the divestiture efforts to ensure that the seller is providing the needed assets and support, and the acquirer is diligently pursuing the approval process to quickly restore competition. Use of an interim trustee assures that the assets will remain viable until they are put into full production.

However, the best-drafted orders the FTC can put together will be of little use if cannot assure compliance. Consequently, the antitrust agencies have insisted on very firm compliance enforcement policy. Within the past 2 years the FTC has secured civil penalties of (1) \$3 million from Schnuck's Markets for failure to maintain the value and competitive viability of a group of stores it had agreed to divest;³⁹⁷ (2) \$600,000 from CVS because it, like Schnuck, had failed to maintain adequately some of the assets it had agreed to divest - before transferring the pharmacies at issue to Eckerd, the divestiture purchaser, CVS had removed its automated computer prescription system, creating big problems for Eckerd in accessing customers' prescription records;³⁹⁸ (3) \$900,000 from Rite-Aid to settle charges that it failed to divest three

³⁹⁶ See *id.* at 38.

³⁹⁷ See Federal Trade Commission, Press Release, Mar. 27, 1998 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1998/9803/petapp20.98.htm>>.

³⁹⁸ See Federal Trade Commission, Press Release, *CVS Agrees to Pay \$600,000 Penalty for Violating FTC Asset Maintenance Agreement*, Mar. 27, 1998 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1998/9803/cvs.htm>>.

drug stores in Maine and New Hampshire under a 1994 order;³⁹⁹ and (4) \$2.5 million from Columbia/HCA Healthcare Corporation to settle charges that it failed to divest hospitals in Utah and Florida in a timely manner, failed to hold the Utah hospitals separate until divestiture, and failed to carry out other obligations.⁴⁰⁰

C. ADMINISTRATIVE LITIGATION

The FTC is also an administrative body that adjudicates disputes before its Administrative Law Judges (“ALJ”). Although administrative litigation is an important tool, especially in novel areas that call upon the unique expertise of the Commission, the pace of administrative litigation at the FTC has often been criticized.⁴⁰¹ In the 1980s, cases would take several years in pretrial disputes and the decisions by both the ALJs and the FTC could also take several years.

To rectify the problem Chairman Pitofsky formed a task force, under the leadership of then-General Counsel Stephen Calkins, to suggest reforms of the administrative litigation process. The task force suggested several reforms that were adopted by the Commission in September 1996.⁴⁰² The reforms established shorter deadlines, streamlined pre-trial discovery, and mandated speedier trials.⁴⁰³ In most cases, the reforms required the administrative law judge to issue an initial decision within one year after the FTC filing of an administrative complaint. The preliminary results are promising.

For example in the *Toys ‘R’ Us* case,⁴⁰⁴ sixteen months passed from the issuance of the complaint in May 1996 to the decision of the administrative law judge in September 1997.⁴⁰⁵ This time included a very tough discovery schedule, which produced more than 9500 pages of transcript

³⁹⁹ See Federal Trade Commission, Press Release, *Rite Aid to Pay \$900,000 in Civil Penalties for Failure to Divest Three Drug Stores in Maine and New Hampshire as Required under FTC Agreement*, Feb. 25, 1998 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1998/9802/ritecp.htm>>.

⁴⁰⁰ See Federal Trade Commission, Press Release, *Columbia/HCA to Pay \$2.5 Million Civil Penalty for FTC Order Violation*, July 30, 1998 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1998/9807/columbia.htm>>.

⁴⁰¹ See Lopatka & Mongoven, *supra* note 4, at 174.

⁴⁰² See 61 Fed. Reg. 50,640 (Sept. 26, 1996). Federal Trade Commission, Press Release, *FTC Announces a Set of Procedural Rule Changes Designed to Streamline Administrative Trial Process*, Sept. 18, 1996 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1996/9609/adminlit.htm>>.

⁴⁰³ Federal Trade Commission, Press Release, *FTC Announces a Set of Procedural Rule Changes Designed to Streamline Administrative Trial Process*, Sept. 18, 1996 (visited Mar. 24, 2000) <<http://www.ftc.gov/opa/1996/9609/adminlit.htm>>.

⁴⁰⁴ See *supra* Part I.D.3.

⁴⁰⁵ The case was litigated before the new procedural reforms were implemented, so the 12-month rule did not apply.

and 2600 exhibits, forty-three days of hearings, and numerous motions.⁴⁰⁶ The result was a very thoughtful 126-page opinion.⁴⁰⁷

Although no case has yet been brought to an Initial Decision under the 12-month rule, the procedural reforms have speeded pretrial proceedings and led to more timely resolution of cases. For example, in the first merger case litigated under the 12-month rule, *In re Associated Data Processing*,⁴⁰⁸ the ALJ scheduled the trial to start about six months after the complaint was filed. After about four months of pretrial proceedings, and with trial imminent, the parties sought a settlement and the case was removed from administrative litigation.⁴⁰⁹ The Commission approved the consent order months after filing the complaint. The first antitrust case for which trial has been completed under the rule, *In re Summit Technology, Inc.*,⁴¹⁰ presents a somewhat mixed picture. The complaint was issued on March 24, 1998, charging anticompetitive patent pooling, price fixing, and fraud on the part of VISX in obtaining a key patent. Trial commenced on December 14, 1998, closing arguments were completed on February 24, 1999, and the decision was issued in May 1999. The Administrative Law Judge found that extraordinary circumstances justified a 60-day extension of the rule period.⁴¹¹ Clearly, although there has not been complete success for the new rule, it nonetheless has had an obvious effect in accelerating administrative litigation at the FTC.

In addition, as a consequence of some other reforms, the Commission has been far more diligent in issuing opinions in a timely manner. In two of the three litigated cases decided most recently—*California Dental Association*⁴¹² and *International Association of Conference Interpreters*⁴¹³—the Commission issued its opinion within four months after the cases were argued.

⁴⁰⁶ See *supra* Part I.D.3. The case involved issues of vertical and horizontal collusion, market power, and intriguing issues of legal interpretation.

⁴⁰⁷ See *In re Toys 'R' Us, Inc.* No. 9278, 1998 FTC LEXIS 119, at *1 (Oct. 13, 1998). The Decision and Order have been appealed to the United States Court of Appeals for the Seventh Circuit. *Toys 'R' Us, Inc. v. FTC*, Dkt. No. 98-4107 (7th Cir. filed Dec. 7, 1998). Oral argument was heard on May 18, 1999.

⁴⁰⁸ 124 FTC 456 (Oct. 24, 1997).

⁴⁰⁹ See *supra* note 375.

⁴¹⁰ No. 9826, 1999 FTC LEXIS 23, at *1 (Feb. 23, 1999).

⁴¹¹ In September, 1998, the Commission accepted for public comment a proposed consent order that would settle all of the allegations of the complaint against Summit and part of the allegations against VISX. See 63 Fed. Reg. 46,452 (Sept. 1, 1998). The patent-pooling and price fixing charges against both parties were included in the settlement, but the charge that VISX fraudulently acquired a key patent remained under litigation, although it too was later dismissed. See No. 9286, 1999 FTC LEXIS 113, at *1. The settlement was made final in 1999. See *In re Summit Tech., Inc.*, No. 9286 (Mar. 7, 1999) (consent order) (visited May 2, 2000) <<http://www.ftc.gov/os/1999/9903/d09286visxd%26o.htm>>.

⁴¹² 121 FTC 190 (1996).

⁴¹³ 123 FTC 465 (1997).

IV. CONCLUSION

Antitrust enforcement in the past seven years has been particularly pragmatic, well focused and balanced. But perhaps the most intriguing change is how the core values of antitrust enforcement are recognized by an increasingly bipartisan constituency. The antitrust agencies have charted a prudent middle course, bringing sound, limited enforcement actions, attempting to clarify the law to facilitate the ability of firms to compete, and focusing on real world results rather than ideological battles. Unlike the 1980s, antitrust is rarely the subject for political battle before Congress. Perhaps the greatest achievement of the leadership of the enforcement agencies, not yet fully achieved, will be the development of a bipartisan consensus of the value of antitrust enforcement to the competitive process and the American economy. As the U.S. economy faces the challenges of the 21st century world economy, antitrust will play a critical role in assuring consumers receive the benefits of a competitive marketplace.