Comments of CompTel/ALTS to the Antitrust Modernization Commission

July 15, 2005

Topic IV – Exclusionary Conduct

The Commenter

CompTel/ALTS was formed in March 2005 by the merger of CompTel/ASCENT and the Association for Local Telecommunications Services (ALTS). With more than 300 members, CompTel/ALTS is the leading industry association representing competitive facilities-based telecommunications service providers, emerging VoIP providers, integrated communications companies, and their supplier partners. CompTel/ALTS members compete directly with incumbent monopolists in providing voice, data and video services in the U.S. and around the world. In order to serve their end users, CompTel/ALTS members also purchase essential inputs from these same incumbent monopolists.

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Comments

1. What are the circumstances in which a firm's refusal to deal with (or discrimination against) rivals in adjacent markets violates Section 2 of the Sherman Act? Does the Supreme Court's decision in Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004), state an appropriate legal standard in this respect?

United States v. Microsoft Corp., 253 F. 3d 34, 59 (D.C. Cir. 2001), adopted by a unanimous vote of the *en banc* D.C. Circuit, correctly sets forth the circumstances in which the refusal to deal with rivals or discrimination against them violates § 2. The *Microsoft* standard looks at whether exclusionary conduct makes business sense *independent* of its exclusionary effects (*i.e.*, enhances the monopolist's return by enabling it to improve the price or quality of its service or the efficiency of its internal operations).

CompTel/ALTS agrees with the following statement of the law, as stated in an *amicus* brief submitted by Judge Bork in *Trinko*:

> In its en banc opinion in Microsoft, the D.C. Circuit articulated a four-part test to determine whether a monopolist's conduct is exclusionary. "First, to be condemned as exclusionary, a monopolist's act must have an 'anticompetitive effect.'" Microsoft, 253 F.3d at 58. Second, "the plaintiff must show that its injury is 'of the type that the statute was intended to forestall,' . . . that the monopolist's conduct harmed competition, not just a competitor." Id. "Third, if a plaintiff successfully establishes a prima facie case under Section 2 by demonstrating anticompetitive effect, then the monopolist may proffer a 'procompetitive justification' for its conduct." Id. (citing Eastman Kodak Co. v. Image Tech. Servs. Inc., 504 US. 451, 483 (1992)) (emphasis added). "Fourth, if the monopolist's procompetitive justification stands unrebutted, then the plaintiff must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit." Id.
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> Business efficiency is an affirmative defense and, in the right circumstances can appropriately lead to a balancing of pro- and anticompetitive effects. Balancing is necessary where both efficiency and anticompetitive effect are present.[1]

It is also important that courts not view separate instances of exclusionary conduct on a compartmentalized basis. As one court recently observed in denying a motion to dismiss a monopolization claim: "In a monopolization case conduct must always be analyzed 'as a whole.' A monopolist bent on preserving its dominant position is likely to engage in repeated

[1] Brief for the Project to Promote Competition and Innovation in the Digital Age as *Amicus Curiae* in *Verizon Comm'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), at 2-3, 4.

and varied exclusionary practices. Each one viewed in isolation might be viewed as *de minimis* or an error in judgment, but the pattern gives increased plausibility to the claim."[2]

Protection of the defendant's monopoly rents is *not* a valid justification of exclusionary conduct. In *Otter Tail Power Co. v. United States*, 410 U.S. 366, 380 (1973), defendant presented a "business justification" for refusing to wheel power or sell it at wholesale, arguing that if it did so, "more and more municipalities" would go into the distribution business, and defendant would lose retail customers and "go downhill." The Court rejected this defense, stating that "[t]he promotion of self-interest alone" does not insulate a defendant's efforts to preserve a monopoly from liability under § 2. Rather, the Sherman Act "assumes that an enterprise will protect itself against loss" of retail customers "by operating with superior services, lower costs, and improved efficiency," not by "substitut[ing] for competition anticompetitive uses of its dominant economic power." *Id.*[3]

The relevant question is thus not *whether* the monopolist will earn more through the exclusionary conduct, since monopoly power generally increases profits. The question is *how* it will earn more: does the conduct enhance the monopolist's returns by enabling it to improve the price or quality of its service, or to improve the efficiency of its internal operations? *Microsoft*,

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[2] *Z-Tel Comm'ns, Inc. v. SBC Comm'ns, Inc.* 331 F.Supp.2d 513, 534 (E.D. Tex. 2004), *quoting* II Areeda and Hovenkamp, Antitrust Law § 310c at p. 147 and *Continental Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 699 (1962).

[3] *See Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451 (1992) (finding copier manufacturer liable under § 2 for refusing to sell parts to independent service organizations with which it competed in the repair of copiers, despite manufacturer's motive to retain the service component of copier users' business, rather than selling parts at wholesale and risking deterioration of its retail service business).

253 F.3d at 59.[4] If so, the conduct will produce higher profits for the monopolist even apart from its effects in preserving monopoly power, and the monopolist will have preserved its market position through competition on the merits. But if the conduct provides no such net[5] procompetitive benefit, it does not make business sense except by depriving customers of choice.

The sacrifice test, advanced by Verizon and the Department of Justice in *Trinko* and applied by the Courts of Appeals in *Covad Communications Co. v. Bell Atlantic Corp.,* 398 F.3d 666 (D.C.Cir. 2005) and *MetroNet Services Corp. v. Qwest Corp.*, 383 F. 3d 1124 (9th Cir. 2004), is unsatisfactory because it exempts from liability any anticompetitive conduct that does not involve the sacrifice of profits, such as the conduct condemned by the Court in *Otter Tail.* The sacrifice test suggests that a plaintiff must prove that defendant's refusal to deal required a sacrifice of short-tem profits. *MetroNet,* 383 F.3d at 1134; *Covad v. Bell Atlantic*, 398 F.3d at 675.

Among other things, the sacrifice test immunizes the well-recognized propensity of monopolists to destroy competition without ever foregoing a cent of profit, by raising their rivals'

[4] *See Data Gen. Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147, 1883 (1st Cir. 1994) ("a business justification is valid if it relates directly or indirectly to the enhancement of consumer welfare. Thus, pursuit of efficiency and quality control might be legitimate competitive reasons for an otherwise exclusionary refusal to deal, while the desire to maintain a monopoly market share or thwart the entry of competitors would not."); *LePage's Inc. v. 3M*, 324 F.3d 141, 163 (3d Cir. 2003), *cert. denied*, 124 S.Ct. 2932 (2004) ("a defendant's assertion that it acted in furtherance of its economic interests does not constitute the type of business justification that is an acceptable defense to § 2 monopolization.")

[5] The procompetitive benefit to defendant must be a net benefit. It should in no way be a defense for the defendant to point to some small non-exclusionary benefit that results from the refusal to deal, if that benefit is at least offset by the losses that result from the refusal to deal.

costs.[6] Raising rivals' costs has been a primary mechanism by which ILECs have destroyed competition. Where a monopolist controls inputs that are necessary to competition, it can thwart that competition by raising its rivals' costs of obtaining the inputs. The monopolist may raise its rivals' costs directly, as with the type of price squeeze condemned in Judge Learned Hand's classic *Alcoa* opinion, *United States v. Aluminum Co. of America*, 148 F.2d 416, 437-38 (2d Cir. 1945).[7] Notably, the Eleventh Circuit recently held that a competitor's claim of monopolization by price squeezing continues to have validity after *Trinko*. *Covad Comm'ns Co. v. BellSouth Corp.*, 374 F. 3d 1044, 1050-52 (11th Cir. 2004), *cert. denied*, 2005 U.S. LEXIS 2247 (Mar. 7, 2005).

Monopolists may also inflate their competitors' costs indirectly. *See. e.g., Ball Mem'l Hosp., Inc. v. Mutual Hosp. Ins., Inc.,* 784 F.2d 1325, 1339-40 (7th Cir. 1986) ("When a firm finds a way to confront its rivals with higher costs, it may raise its own prices to consumers without drawing increased output from them."); *Forsyth v. Humana, Inc.*, 114 F.3d 1467, 1478 (9th Cir. 1997), aff'd, 525 U.S. 299 (1999) (reversed summary judgment; policy raised factual question of whether conduct raised competitor's costs); *Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal and Prof'l Publications, Inc.*, 63 F.3d 1540, 1553 n.12 (10th Cir. 1995)

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6 *See* Thomas G. Krattenmaker & Steven C. Salop, Anticompetitive Exclusion: Raising Rivals' Cost to Achieve Power Over Price, 96 Yale L.J. 209, 224 (1986) ("Raising rivals' costs can be a particularly effective method of anticompetitive exclusion. This strategy need not entail sacrificing one's own profits in the short run. . . ."); *see also* Herbert Hovenkamp, Post-Chicago Antitrust: A Review and Critique, 2001 Colum. Bus. L. Rev. 257, 318-23 (2001) (discussing economic logic behind raising rivals' cost theory).

7 *See* Steven C. Salop, Economic Concepts and Antitrust Analysis, 56 Antitrust L.J. 57, 58-59 (1987) (evil of price squeeze is not predatory pricing; "rather, it is a claim that firms exclude rivals and gain power over price by raising their rivals' costs").

(raising rival's costs "would qualify as anticompetitive conduct unless [defendants] could demonstrate a legitimate business justification for it").

Part III of *Trinko* (540 U.S. at 407-11), in focusing solely on the voluntary prior dealings aspects of *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), went astray. The existence of voluntary prior dealings, which was present in *Aspen Skiing*, may be one way of showing that a refusal to deal is improperly exclusionary and anti-competitive, but it is not the only way to do so.

2. Should the essential facilities doctrine constitute an independent basis of liability for single-firm conduct under Section 2 of the Sherman Act?

Yes. The essential facilities doctrine has been recognized by all the courts of appeal,[8] and constitutes a sound policy basis for liability. The statement of the doctrine in *MCI Communications Corp. v. American Tel & Tel. Co.*, 708 F.2d 1081, 1132-33 (7th Cir.), *cert. denied*, 464 U.S. 891 (1983), as containing the following four elements, has been widely accepted: "(1) control of the essential facility by a monopolist; (2) a competitor's inability

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[8] *See, e.g., Interface Group, Inc. v. Massachusetts Port Authority,* 816 F.2d 9, 12 (lst Cir. 1987); *Delaware & Hudson Ry. Co. v. Consolidated Rail Corp.,* 902 F.2d 174, 179 (2d Cir. 1990); *Ideal Dairy Farms, Inc. v. John Labatt, Ltd.,* 90 F.3d 737, 748 (3rd Cir. 1996); *Advanced Health Care Servs. v. Radford Community Hosp.,* 910 F.2d 139, 150 (4th Cir. 1990); *Mid-Texas Communications Sys., Inc., v. American Tel. & Tel. Co.,* 615 F. 2d 1372, 1387 n. 12 (5th Cir. 1980); *Directory Sales Mgmt. Corp. v. Ohio Bell Tel. Co.,* 833 F.2d 606, 612 (6th Cir. 1987); *MCI Communications Corp. v. American Tel. Tel. Co.* 708 F.2d 1081, 1132-33 (7th Cir. 1983); *City of Malden v. Union Elec. Co.,* 887 F.2d 157, 160 (8th Cir. 1989); *City of Anaheim v. Southern California Edison Co.,* 955F.2d 1373, 1380 (9th Cir. 1992); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.,* 738 F.2d 1509, 1520 (10th Cir. 1984), *aff'd on other grounds,* 472 U.S. 585 (1985); *Consolidated Gas Co. of Florida, Inc. v. City Gas Co., 880 F. 2d 297 (11th Cir. 1989), reinstated on reh'g*, 912 F. 2d 1262 (11th Cir. 1990) (*en banc*, *per curiam*), *vacated as moot*, 499 U.S. 915 (1991); *Caribbean Broadcasting Sys., Ltd. v. Cable & Wireless PLC,* 148 F. 3d 1080, 1088 (D.C. Cir. 1998); *Intergraph Corp. v. Intel Corp.,* 195 F.3d 1346, 1356-58 (Fed. Cir. 1999). *See also* Robert Pitofsky, Donna Patterson, and Jonathan Hooks, *The Essential Facilities Doctrine Under U.S. Antitrust Law,* 70 Antitrust L.J. 443 (2002).

practically or reasonably to duplicate the essential facility; (3) the denial of use of the facility to a competitor; and (4) the feasibility of providing the facility." The essential facilities doctrine is an older variant of refusal to deal principles, and is analytically consistent with them. The fourth element of an essential facilities claim, that it would be feasible for the monopolist to provide access, is, as applied by the courts, the equivalent of the legitimate business justification standard applicable in refusal to deal cases. The analysis was succinctly expressed by Judge Greene in the *AT&T* case:

> problems of feasibility and practicability may be taken into account by the Court in determining the sufficiency under the law of the access to essential facilities granted by defendants to non-Bell carriers. To put it another way, parity is not necessarily required. But . . . AT&T and its subsidiaries now discriminate between Long Lines and non-Bell carriers with regard to access to Bell System facilities. . . . this discrimination [is] anticompetitive in its effect. . . . The burden is now upon defendants to show why, despite that anticompetitive impact, such unequal treatment is reasonable.[9]

It should not be an answer to an essential facilities claim that the defendant has made the essential facility available to the plaintiff, if the facility is made available on unreasonable terms. If accepted, this contention would make a nullity of the access requirement. A monopolist could elude the rule simply by making access "available" at a price and under conditions that made access worthless. For example, the owner of a city's only arena suitable for basketball could circumvent a requirement that it rent its facility, when not in use, to a competing team simply by offering to rent the arena, but only at 3:00 a.m. *See Fishman v. Estate of Wirtz*, 807 F.2d 520, 540-41 (7th Cir. 1986). Recognizing that this result would render the access requirement meaningless, the courts that have considered the issue have required that essential facilities be made available on terms that are reasonable. For example, the Second Circuit has written,

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[9] *United States v. American Tel & Tel. Co.*, 524 F. Supp 1336, 1361 (D.D.C. 1981).

"[t]here need not be an outright refusal to deal in order to find . . . denial of an essential facility . . . [i]t is sufficient if the terms of the offer to deal are unreasonable." *Delaware & Hudson Ry. Co. v. Consolidated Rail Corp.,* 912 F.2d 174, 179-80 (2d Cir. 1990). The Seventh Circuit has been equally clear: "[a]greeing to deal on unreasonable terms is merely a type of refusal to deal." *Fishman*, 807 F.2d at 541.[10]

Respectfully submitted,

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[10] *See also Laurel Sand & Gravel, Inc. v. CSX Trans. Inc.*, 924 F.2d 539, 545 (4th Cir. 1991) (applying the "reasonable standard of the access factor"); *Alaska Airlines, Inc. v. United Airlines,* 948 F.2d 536, 542 (9th Cir. 1991) ("the essential facilities doctrine imposes liability when one firm, which controls an essential facility, denies a second firm reasonable access to a product or service that the second firm must obtain in order to compete with the first"); *City of Chanute v. Williams Natural Gas Co.,* 955 F.2d 641, 648 (10th Cir. 1990), *overruled on other grounds*, *Systemcare Inc. v. Wang Labs. Corp.,* 117 F.3d 1137 (10th Cir. 1997) (plaintiff must show that the defendant "did not provide access to its pipeline on reasonable terms, equivalent to a denial of access"); *Nobody in Particular Presents, Inc. v. Clear Channel Communications, Inc.*, 311 F.Supp. 2d 1048 (D. Colo 2004) (court found that defendant's radio stations may have denied plaintiff rock concert promoter access on reasonable, nondiscriminatory terms even though they offered to sell advertising time to plaintiff because there was evidence that defendant had "significantly raised the price of obtaining these services" and had advised its employees to discriminate against outside promoters in providing advertising time); *City of College Station v. City of Bryan,* 932 F. Supp. 877, 888 (S.D. Tex. 1996) ("[t]o satisfy the requirement that Defendants have denied access to its 'essential facility,' . . . it is sufficient if College Station can demonstrate that Defendants do not offer reasonable terms"); *Zschaler v. Claneil Enters., Inc.*, 958 F. Supp. 929, 945 (D. Vt. 1997) (if plaintiffs' allegations are true, "then it may be argued that Plaintiffs have been effectively denied the use of" the facility); *Florida Fuels, Inc. v. Belcher Oil Co.*, 717 F. Supp. 1528, 1532 (S.D. Fla. 1989) ("[u]nder this doctrine, a monopolist . . . must share on fair terms").