March 17, 2006

Via Express Mail and E-mail

Antitrust Modernization Commission
Attention: Public Comments
1120 G Street, N.W.
Suite 810
Washington, DC 20005

Re: Comments Regarding Exclusionary Conduct Standards

Ladies and Gentlemen:

On behalf of the Section of Antitrust Law of the American Bar Association, I am pleased to submit the enclosed comments to the Antitrust Modernization Commission in response to its request for public comments regarding Exclusionary Conduct Standards.

Please note that these views are being presented only on behalf of the Section of Antitrust Law and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and should not be construed as representing the position of the American Bar Association.

If you have any questions after reviewing this report, we would be happy to provide further comments.

Sincerely,

Donald C. Klawiter
Chair, Section of Antitrust Law
Comments of the Section of Antitrust Law of the American Bar Association in Response to the Antitrust Modernization Commission’s Request for Public Comment Regarding Exclusionary Conduct

The Section of Antitrust Law (“Antitrust Section”) of the American Bar Association (“ABA”) is pleased to submit these comments to the Antitrust Modernization Commission (the "Commission") in response to its request for public comment dated May 19, 2005 regarding specific questions relating to Exclusionary Conduct selected for study by the Commission. The views expressed herein are being presented on behalf of the Antitrust Section. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, accordingly, should not be construed as representing the policy of the American Bar Association.

Summary of Comments

The Antitrust Modernization Commission’s (“AMC”) call for comments on the standards for exclusionary conduct was both general and specific. As a general matter, the AMC asked:

How should the standards for exclusionary or anticompetitive conduct be determined (e.g., through legislation, judicial development, amicus efforts by DOJ and FTC), particularly if you believe the current standards are not appropriate or clear?

More specifically, the AMC called for comments on the current standards regarding (1) refusals to deal; (2) the essential facilities doctrine; and (3) bundling and bundled pricing.

A. GENERAL STANDARDS

In answering the question “how should the standards for exclusionary or anticompetitive conduct be determined,” the Antitrust Section’s outline concludes that statutory change is unnecessary.

On the whole, viewed historically, there is broad agreement on the general legal framework for the three offenses prohibited under Section 2 of the Sherman Act. However, there is a lively and continuing debate about the specific standards for distinguishing exclusionary or predatory conduct from aggressively competitive behavior. The Section concludes, however, that areas of consensus on the application of Section 2 are wider than areas of disagreement.

The Supreme Court’s recent decision in Verizon Commc’ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004) summarizes and restates the proposition that possession of a monopoly is lawful, and only acquiring or perpetuating monopoly power through exclusionary means is unlawful. This concept is taken for granted today, although prior
decisions examined the fundamental question whether liability could be imposed for the exercise of monopoly power alone, or whether monopoly power plus anticompetitive conduct must be demonstrated. See, e.g., Hanover Shoe, Inc. v. United Shoe Machinery Corp., 392 U.S. 481 (1968), United States v. Grinnell Corp., 384 U.S. 563 (1966), and United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945).

Similarly, the courts and enforcement authorities agree that we do not impose on monopolists affirmative duties to share with or to assist competitors except in rare circumstances, such as in Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985), where there was a prior course of dealing and the refusal suppressed competition. Refusals to deal in and of themselves only rarely constitute predatory or exclusionary conduct and are otherwise generally lawful.

It is also well-established that Section 2 may not be used to de-monopolize a monopolized market absent a finding that the monopoly was either acquired or maintained unlawfully. By preventing exclusionary conduct to acquire or maintain a monopoly, we preserve the role of market forces in de-monopolizing markets. Monopolists should be subject to liability under Section 2 only when they engage in predatory or exclusionary conduct.

No studies suggest that public or private enforcement of Section 2 has systematically failed to prevent anticompetitive conduct or deterred beneficial conduct by firms with dominant market positions. A review of enforcement statistics suggests that government Section 2 cases have been extremely rare, and have been filed with decreasing frequency over the years.

Finally, although there has been a lively debate among parties to litigation, academics and other observers and commentators in recent years on the question whether there should be a unitary standard for identifying exclusionary or predatory conduct, a single standard that would be appropriate for all exclusionary conduct has not been identified and is not needed to correct the state of Section 2 jurisprudence and ensure the protection of consumer welfare. Hence, the courts should be permitted to continue to evolve appropriate standards on a case-by-case basis, as particular conduct and facts present themselves for consideration.

B. SPECIFIC AREAS OF AMC INTEREST

The Antitrust Section outline also studied the current state of the law and economics as to the three specific areas identified by the AMC:

(1) Liability for refusals to deal with rivals in the absence of a regulatory regime that specifically governs competitive behavior;

(2) The continued role, if any, of the essential facility doctrine; and

(3) Product bundling and bundled prices.

The outline concludes that in the absence of consensus and in light of the trend in the courts to use these doctrines sparingly, it is unnecessary for the Commission to seek
legislative reform pertaining to either (1) refusals to deal or (2) the essential facility doctrine. Improvements may be sought when necessary through the filing of amicus briefs in specific cases and/or through agency guidelines. With respect to (3) product bundling and bundled pricing, the outline concludes that there is no consensus as to the correct standard at this time because their competitive effects are not clear in all circumstances. Therefore, further refinement of the treatment of bundling and bundled pricing should be left to common law development under the Sherman Act.

**Exclusionary Conduct Standards**

**A. GENERAL OBSERVATIONS**

1. On the whole, viewed historically, there is broad agreement on the general legal framework for the three offenses prohibited under Section 2 of the Sherman Act. However, there is a lively and continuing debate about the specific standards for distinguishing exclusionary or predatory conduct from aggressively competitive behavior.

a. Areas of consensus on the application of Section 2 are wider than areas of disagreement.

b. *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) (“Trinko”) summarizes and restates the proposition that having a monopoly is lawful, and only acquiring or perpetuating monopoly power through exclusionary means is unlawful. This concept is taken for granted today, although prior decisions examined the fundamental question whether liability could be imposed for the exercise of monopoly power alone, or whether monopoly power plus anticompetitive conduct must be demonstrated. *See, e.g.*, *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968), *United States v. Grinnell Corp.*, 384 U.S. 563 (1966), and *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945).

c. Similarly, the courts and enforcement authorities agree that

(i) We do not impose on monopolists affirmative duties to share with or to assist competitors except in rare circumstances, such as in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), where there was a prior course of dealing and the refusal suppressed competition;

(ii) Refusals to deal in and of themselves only rarely constitute predatory or exclusionary conduct and are otherwise generally lawful;
(iii) Section 2 may not be used to de-monopolize a monopolized market absent a finding that the monopoly was either acquired or maintained unlawfully;

(iv) By preventing exclusionary conduct to acquire or maintain a monopoly, we preserve the role of market forces in de-monopolizing markets;

(v) Monopolists should be subject to liability under Section 2 when they engage in predatory or exclusionary conduct.

d. No studies suggest that public or private enforcement of Section 2 has systematically failed to prevent anticompetitive conduct or deterred beneficial conduct by firms with dominant market positions.


e. Despite lively debate among parties to litigation, academics and other observers and commentators, it is difficult to articulate a single standard that would be appropriate for all exclusionary conduct or that is needed to correct the state of Section 2 jurisprudence and ensure the protection of consumer welfare.

B. SUMMARY OF CONCLUSIONS

a. In several relatively limited respects, clarification of the law could be useful, but none of these appear to warrant a broadly-applicable statutory change. Clarification could be accomplished through agency enforcement guidelines and agency amicus efforts to assist judicial development in the following areas:

(i) Liability for refusals to deal with rivals in the absence of a regulatory regime that partially governs competitive behavior;

(ii) Liability for refusals to deal under the “essential facilities” doctrine;
(iii) Product bundling and bundled pricing, which have been the subject of several recent decisions that may lead to under and/or over-deterrence arising from advice of counsel in the face of uncertainty;

(iv) The continuing split of authority among the Federal Circuit and the other Circuit Courts of Appeal regarding the role of Section 2, if any, in policing refusals to license IP. There may also be differences of approach as between the Federal Circuit in the United States and the European Union. Conditional refusals to deal, as in IP licensing, such as “no license if licensee also deals with rival,” may violate Section 2. Should the refusal to license intellectual property rights, without more, ever be found to violate Section 2?

C. OVERVIEW OF ISSUES IN CONTROVERSY

1. Individual case comparisons can give rise to the appearance that standards for bringing Section 2 enforcement cases against allegedly unlawful exclusionary conduct may vary among and between the DOJ, the FTC, and State Attorneys General. See, e.g., enforcement decisions by the DOJ and the FTC and the States in connection with Microsoft. On balance, however, such comparisons may not support any valid generalizations.

   a. Some commentators contend that efficient, pro-competitive business conduct will be encouraged if clear enforcement standards for Section 2 are established. Such commentators criticize the standard for liability offered in the DOJ/FTC amicus brief in Trinko as offering insufficient guidance for business decision-makers.

   b. Under one view, the standards for government enforcement of Section 2 might be confusing if the United States v. Dentsply Int’l, Inc., 399 F.3d 181 (3d Cir. 2005), which the DOJ prosecuted as an exclusive dealing case, were to be interpreted as a “duty to deal” case. For the most part, however, commentators have characterized the Dentsply case as one in which exclusive dealing restrictions were used to prevent erosion of a monopoly position.

2. A survey of scholarly work and recent briefs filed by federal enforcement agencies and private amici reveals a relatively broad range of views on the problem of assessing the competitive effects of exclusionary conduct. See, e.g.:


3. A handful of relatively recent cases have fueled the debate over Section 2 standards.


b. United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001)

c. Le Page’s Inc. v. 3M Co., 324 F.3d 141 (3d Cir. 2003)


e. United States v. AMR Corp., 335 F.3d 1109 (10th Cir. 2003)

f. Confederated Tribes of Siletz Indians v. Weyerhaeuser Co., 411 F.3d 1030 (9th Cir. 2005)

4. The core of the debate centers on the question how to find a standard that strikes an appropriate balance between over-deterrence, which would chill legitimately aggressive competitive conduct, and under-deterrence, which would result in competitive harm that reduces consumer welfare. Courts have articulated the issue variously:

a. “The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of
the free-market system. The Supreme Court has maintained that the opportunity to charge monopoly prices – at least for a short period – is what attracts ‘business acumen’ in the first place; it induces risk taking that produces innovation and economic growth. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct.” *Trinko*, 540 U.S at 879.

b. The purpose of the Act is not to protect business from the working of the market, it is to protect the public from the failure of the market. The law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself. It does so not out of solicitude for private concerns but out of concern for the public interest. *Spectrum Sports*

5. Some disagreement exists among experts as to whether the ability to charge monopoly profits indeed induces risk taking, innovation and economic growth. Nevertheless, Justice Scalia’s observation represents the Supreme Court’s most recent pronouncement on how monopoly power ought to be viewed as a matter of antitrust policy. Thus, when combined with the teaching of *Spectrum Sports*, *Trinko* suggests that Section 2 ought to be construed as imposing liability only as necessary to protect consumer welfare against a failure of the competitive market process when the failure is caused by acquisition or perpetuation of monopoly power by means of exclusionary conduct.

6. The facts, reasoning, and specific holding in *Trinko*, which involved a refusal to assist a rival in the context of a regulatory scheme that mandated cooperation, suggest that its specific holding is most clearly applicable to similarly-regulated industries. Nevertheless, the *Trinko* opinion contains language that more broadly characterizes the purposes of the antitrust laws in general, and suggests limitations on the application of Section 2. It is unclear whether and how these observations by the *Trinko* Court ought to influence the analysis of Section 2 cases outside regulated industries.

a. *Aspen Skiing* was reaffirmed, but identified as “at the outer limit” of conduct that violates Section 2.

b. The viability of, or the need for, an essential facilities doctrine was called into question.

c. The viability of “leveraging” apart from proof of either attempt to monopolize or monopolization was disapproved; and

d. The exercise of monopoly power by itself was held to be insufficient to violate the statute.
Beyond its holding – that a refusal to assist a rival by a firm already subject to a regulatory duty to do so, does not itself constitute an independent violation of Section 2 – *Trinko* did not answer the dilemma articulated by the D.C. Circuit in *Microsoft*:

a. “Whether any particular act of a monopolist is exclusionary, rather than merely a form of vigorous competition, can be difficult to discern: the means of illicit exclusion, like the means of legitimate competition, are myriad. The challenge for an antitrust court lies in stating a general rule for distinguishing between exclusionary acts, which reduce social welfare, and competitive acts, which increase it.” United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001).

Antitrust economists and other commentators have presented a range of economic models for analyzing different categories of exclusionary conduct, and there is disagreement as to the balance any of these analyses would strike between over- and under-deterrence. Except in the context of case-specific fact scenarios, it is unclear how such analytical models would assist generally in the development of legal doctrine.

What are the possible standards that could be used to define exclusionary conduct that violates Section 2?

a. Profit sacrifice. The test looks for a departure from profit maximization and has been cited by some courts as critical evidence of exclusionary conduct. Some commentators argue that it should be a necessary condition for a finding of liability associated with all forms of exclusionary conduct. The current test for predatory pricing is an example of profit sacrifice, but is not co-extensive with the profit sacrifice test. For purposes of predatory pricing, a firm must sacrifice all profits, whereas profit sacrifice would also reach conduct that involves some sacrifice but is not necessarily below cost.

(i) Cases: *Aspen*. The conduct was exclusionary because the defendant “was willing to sacrifice short-run benefits and goodwill in exchange for a perceived long-run impact on its smaller rival.” *Aspen*, 472 U.S. at 610-11; see *Trinko*, 540 U.S. at 409 (*Aspen* defendant demonstrated “a willingness to forsake short-term profits to achieve an anticompetitive end”); *Covad Communications Co. v. Bell Atlantic Corp.*, 398 F.3d 666, 676 (D.C. Cir. 2005) (“a ‘predatory’ practice is one in which a firm sacrifices short-term profits in order to drive out of the market or otherwise discipline a competitor”); *MetroNet Services Corp. v. Qwest Corp.*, 383 F.3d 1124, 1134 (9th Cir. 2004).
(ii) Issues. Is sacrifice an appropriate test for any kind of exclusion other than predatory pricing, given its sole focus on the effects of the conduct on the monopolist? Should it be necessary also to consider the effect of the conduct on rivals? On consumers? What justifies foregoing an analysis of effects in predatory pricing cases? Do those same factors necessarily apply to other forms of exclusionary conduct? Are there instances of objectionable exclusion that involve little or no profit sacrifice, or that involve simultaneous or prompt recoupment? Should profit sacrifice be a necessary condition for all forms of exclusion, or just a sufficient one in appropriate cases? What is the justification for requiring that firms sacrifice any legitimate benefit to help rivals or consumers? Trinko indicates that the Supreme Court is skeptical of Aspen, saying that its standard is at or near the outer limits of Section 2.

(iii) Short run profit sacrifice can over-deter as well as under-deter. Short-run profit sacrifice can be an important element in establishing that conduct is exclusionary, but it cannot be sufficient to make conduct exclusionary, because procompetitive conduct, such as R&D or purchasing capital equipment, entails the sacrifice of current profit in the pursuit of greater profit over the longer term. Moreover, some have cautioned that any focus on short-run profit sacrifice should be used cautiously so as to avoid any unintended signal that the antitrust laws will judge monopoly behavior favorably if it involves short-run profit maximization.

b. No economic sense. This test is related to the profit sacrifice test. As advocated by the DOJ, “conduct is not exclusionary or predatory unless it would make no economic sense for the defendant but for the tendency to eliminate or lessen competition.” DOJ has advocated this test in all types of Section 2 cases.

(i) Cases. Microsoft: DOJ argued that a course of conduct that served to protect the defendant’s operating system monopoly was exclusionary because it “would not make economic sense unless it eliminated or softened competition.” American Airlines: DOJ contended that the defendant drove out rivals by adding “money-losing capacity” and that “distinguishing legitimate competition from unlawful predation requires a common-sense business inquiry: whether the conduct would be profitable, apart from any exclusionary effects.” Dentsply: DOJ argued that the defendant’s policies of not using dealers that distributed products of rivals “made no economic sense but for their tendency to harm rivals,” because the policies cost the defendant something, yet produced no possible benefit other than reducing competition. Verizon: DOJ and FTC at first appeared to endorse a “but for” test for all forms of exclusionary conduct in the certiori briefs, but later retreated.
in the merits briefs, suggesting a far more circumscribed role for the test.

(ii) The test also defines a necessary condition for finding exclusionary conduct: Unless challenged conduct with a demonstrated tendency to eliminate competition would make “no economic sense” but for that tendency, the conduct cannot be characterized as “exclusionary.”

(iii) Issues. Is the “no economic sense” test any better a barometer of exclusionary conduct than the profit sacrifice test? When might the two tests produce different results? As with profit sacrifice, does the no economic sense test suffer from an undue focus on the effects of the questioned conduct on the alleged monopolizer to the exclusion of its effects on rivals and consumers? How would the no economic sense test address conduct that is efficient for the monopolizer, and hence might be undertaken regardless of the tendency to eliminate competition, but that also facilitates the exercise of market power by having a significant exclusionary effect on rivals? If it is an appropriate test for some circumstances, such as a refusal to assist rivals, should it be generalized into a test for other circumstances? This standard preserves freedom of action for defendant firms with monopoly shares, which under the standard have no duty to make the market more beneficial for consumers, much less assist rivals, but instead proscribes only conduct that is anticompetitive and not (otherwise) beneficial to the defendant.

c. **Less efficient rival.** Under this approach, conduct is not exclusionary unless it is likely to exclude an equally or more efficient competitor.

(i) Administratively very difficult.


(iii) Some have advocated that it be incorporated as a factor into other tests, such as profit sacrifice. It is argued that even if there is profit sacrifice, conduct should be actionable only if it excludes an equally or more efficient rival.

(iv) Some have advocated a related test which looks to the impact of the conduct on the efficiency of the monopolist. (Elhauge).

(v) Issues. Focuses on efficiency of target of conduct instead of efficiency of conduct itself. Ignores possibility that welfare consequences of exclusion of a less efficient rival may be
d. Balancing. Under a balancing test, a court would evaluate both the negative effects of the questioned conduct on rivals and consumers and its efficiency benefits for the alleged monopolizer, in order to determine whether on balance the conduct harms consumer welfare more than it benefits the monopolizer. The “Disproportionality” variant of the test would only prohibit conduct when its anticompetitive effects substantially outweigh its benefits. This approach is sometimes analogized to the rule of reason under Section 1 of the Sherman Act.

(i) Case law. In Microsoft, the D.C. Circuit endorsed a four part framework for analyzing allegedly exclusionary conduct. First, the conduct must harm competition, not just a rival of the alleged monopolist. Second, the plaintiff, who bears the burden of proof, must demonstrate that the monopolist’s conduct indeed produced such an anticompetitive effect. At that point, the plaintiff has established a prima facie case, and the burden of production shifts to the monopolist, who may proffer a procompetitive justification. If the monopolist fails to do so, the plaintiff should prevail. But if it is able to do so, i.e., if it produces evidence to support “a nonpretextual claim that its conduct is indeed a form of competition on the merits,” the burden of production shifts back to the plaintiff. At that point, the plaintiff must demonstrate that the anticompetitive effects of the conduct outweigh its procompetitive benefit. The court indicated that if the inquiry reaches this fourth step, it can be characterized as similar to rule-of-reason analysis under Section 1. 253 F.3d 34, 59. Finally, the D.C. Circuit indicated that evidence of intent may also be relevant, but only to the extent it illuminates the likely effect of the monopolist’s conduct.

(1) Some have questioned whether Trinko may have undercut the viability of a balancing test by opining that Section 2 “does not give judges carte blanche to insist that a monopolist alter its way of doing business whenever some other approach might yield greater competition.”

(2) Others have defended the Microsoft framework as a workable and economically defensible approach to Section 2 analysis that takes into account shifting burdens of production and is consistent with the larger body of Section 2 decisions of the Court. It also provides a basis for deciding cases that may involve conduct that produces some efficiency but also has substantial anticompetitive effects.
(ii) Issues. On the one hand, unlike the profit-sacrifice and no economic sense tests, the balancing test more clearly seeks to assess the effect of the questioned conduct on competition. However, it is subject to some of the same uncertainties as the rule of reason. Balancing may be more difficult than it sounds, and hence it may be difficult for a firm to predict its risk in advance of undertaking conduct that, although arguably pro-competitive, has some level of anticompetitive effect. If that is the case, a balancing test may deter competitively beneficial or benign conduct. Also, in the context of refusals to deal, this standard may risk imposing on firms a duty to help competitors even when those competitors fail to take reasonable steps to compete without the assistance of the larger rival.

e. Miscellaneous other issues.

(i) Essential facilities doctrine. The MCI four-part test may be anachronistic in light of later Supreme Court decisions like Aspen and Verizon, which look to both anticompetitive effects and justifications. The Supreme Court certainly seemed skeptical in Verizon that “essential facilities” provides anything useful to the analysis of refusals to deal under Section 2.

(ii) Cheap talk. How to deal with conduct that costs or risks little to the actor but may produce great benefits for it owing to the conduct’s tendency to exclude rivals? There may be conduct that is costless to the defendant and tends to exclude rivals, as in Unocal (In the matter of Union Oil Co. of Calif., FTC Dkt. No. 9305 (still pending before the FTC)) and Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988), but involves no discernable efficiencies. The profit sacrifice and but for standards may not capture this conduct.

(iii) Safe harbors for beneficial conduct. Should certain types of potentially exclusionary -- but likely beneficial -- conduct be placed in a prudential safe harbor? For example: (a) Improved product quality, successful R&D, cost-reducing innovations, and the introduction of a new product may be so likely to enhance consumer welfare as to be considered “competition on the merits” and deemed not to violate Section 2, without attempting to identify the exceedingly rare case that would be an exception to this general rule. (b) While perhaps not as clearly established in the case law, the refusal to license intellectual property rights might also be found to violate Section 2 only in exceptional circumstances. At this point, there does not appear to be a clear consensus in favor of establishing safe harbors.
(1) Some argue that firms with significant market shares already enjoy a safe harbor to the extent that they do not hold market shares in excess of levels generally recognized by courts as sufficient to presume monopoly power, i.e., greater than 70 percent. Unilateral conduct by firms with shares smaller than these relatively high thresholds – especially when contrasted with the concept of “dominance,” which prevails in the EU and many other jurisdictions, would generally fall outside the scope of Section 2.

(2) Others contend that the uncertainty of market definition analysis may place firms with much lower market shares at risk of incurring Section 2 liability, thus creating difficulty for antitrust counselors seeking to guide business decisionmakers. Increased reliance on direct evidence of the actual exercise of monopoly power in lieu of market share evidence may also increase uncertainty.

10. What calls for AMC considering the standard?

a. There is no single standard for defining exclusionary conduct beyond Aspen’s definition of “competition on some basis other than efficiency,” which was drawn from the work of Bork and Areeda. A single, clear standard might serve to inform market participants when they would violate Section 2, if it in fact was readily applicable to the wide range of conduct by monopolists that can negatively impact competition. It is not clear, however, whether it is possible to have a single standard that is not facially broad in terms and in need of fact-specific common law rules to make its application clear to different kinds of conduct. This is the situation we have today. What standard could apply to facts as varied as those in Aspen, Kodak, Trinko, Microsoft, U.S. Tobacco, LePage’s, and Dentsply? Is there anything all that inconsistent about the results in these cases that suggests confusion in the application of the general standard?

b. Are the various standards, as applied, leading to undesirable results, such as unnecessary punishment of business, deterrence of procompetitive conduct, failure to protect consumers, or monopolization? (Can we answer this question?)

11. The emergence of differing “dominant firm” standards in other jurisdictions may be having an impact on the business conduct of firms that do business in multiple jurisdictions. Does this suggest a need for change in the standards applicable under Section 2?

a. Some foreign jurisdictions have adopted or are planning to adopt Abuse of Dominance Guidelines.
b. The concept of “dominance” is often triggered at much lower market share thresholds than U.S. monopolization standards.

c. Similarly, the concept of “abuse” may be more inclusive than the “exclusionary/predatory conduct” standard under Section 2. The continuing evolution of varying international standards of conduct may merit further empirical study.

12. The issue posed appears to be whether continued reliance on the evolution of common law is sufficient to strike an appropriate balance over the long term.

a. It does not appear possible to predict that any single standard for Section 2 liability would achieve a better result than the existing common law approach of achieving the dual public purposes articulated by the Supreme Court, i.e., to allow successful competitors to reap the rewards of a legitimate monopoly while ensuring that conduct by a monopolist does not significantly harm the competitive system on which we rely to protect consumer welfare.

b. In light of the difficulty of the questions posed by the choice of an appropriate standard, there appears to be little reason to explore statutory change.

c. In lieu of changing the statute or recommending adoption of a single standard for exclusionary conduct, some have suggested that it might be appropriate to detreble damages for some or all violations of Section 2. The objective would be to reduce the incentives, if any, to bring non-meritorious Section 2 claims. A variation of detrebbling would be to provide flexibility for the court to assess damages up to and including treble damages based on the level of consumer harm associated with specific exclusionary conduct and the extent to which a remedy is needed to deter such conduct in the future. Others observe that detrebbling might significantly reduce the enforcement value of Section 2 and that, since Section 2 cases are rarely brought and even more rarely won by plaintiffs, detrebbling is unnecessary.

D. REFUSALS TO DEAL

1. What are the circumstances in which a firm’s refusal to deal with (or discrimination against) rivals in adjacent markets violates Section 2? What are the circumstances in which a firm’s refusal to deal with (or discriminate against) a customer or supplier violates Section 2? Does the Supreme Court’s decision in Trinko state an appropriate, generally applicable standard?

a. An alternative articulation of the issue would be: “Under what circumstances, if any, should Section 2 impose a duty to deal on a
monopolist or would-be monopolist?” Duties to deal typically arise as remedies for refusals to deal, but may also arise as remedies for other kinds of exclusionary conduct. Hence, monopolist’s dealings with rivals can be approached as: (a) a question of violation (“refusal to deal”); (b) as a remedy to the refusal to deal violation, or (c) as a remedy for other misconduct where necessary to restore competitive conditions disrupted by the monopolist’s challenged conduct. Under U.S. law, sharing is not a remedy without some violation, and refusal to share without more may not be a violation, even in the essential facilities context, under *Aspen* and *Trinko*. There may be some other violation that would call for sharing as a remedy, but it would be the rare case, based on specific facts (e.g., Microsoft Europe).

2. Policy Issue

   a. Finding the right refusal to deal standard is difficult for the same reasons as finding the right definition of exclusionary conduct. An aggressive standard may help to undercut monopolies, but also may undercut incentives to compete, and procompetitive and anticompetitive conduct often looks alike.

3. Impact of *Trinko*

   a. *Trinko* does not state an all-purpose test for what refusals to deal violate Section 2. Specifically, it doesn’t address refusals to deal absent government regulation of competition or refusals to deal with non-rivals, such as customers or suppliers. It is also subject to varying interpretations.

   b. *Trinko* states that the general rule is that a refusal to cooperate with rivals is not exclusionary conduct and without more does not violate Section 2. The Court then examines the circumstances in which exceptions might be found, making clear that these exceptions are rare. The Court acknowledges one exception it had recognized in the past, *Aspen*, where a previous course of dealing existed, indicating that it is at or near the outer limit of Section 2. It also throws into question the future viability of the essential facilities doctrine. The Court indicates that the presence of regulation makes the expansion of antitrust liability (viz., whether an exception should be created) less necessary and less desirable. Finally, the Court makes clear that monopoly leveraging is not a distinct offense and that Section 2 should not be used for de-monopolization. *Trinko* might also be read to say that absent a prior course of dealing, a refusal to deal cannot itself constitute a violation of Section 2.

   c. *Trinko* certainly does not announce a new Section 2 standard, and the Court did not explicitly mention or endorse the Government’s recommended standard. But the Court’s analysis arguably focuses on the
same facts that suggest a violation under the "no economic sense" standard like that the Government proposed. Distinguishing Aspen, the Court focused on certain facts, including whether the defendant forewent short term profits because it would profit in the long term after competition exited. From this and the fact Verizon won, some have argued that the Court implicitly endorsed the "no economic sense" standard:

(i) Test as stated in government brief: "[C]onduct is not exclusionary or predatory unless it would make no economic sense for the defendant but for its tendency to eliminate or lessen competition." See Brief of the United States and the Federal Trade Commission as Amici Curiae Supporting Petitioner, at 15.

(ii) But government brief on the merits was clear that this test would apply only in cases involving an alleged duty to assist a rival. Id. The more general test advocated was the disproportionality test: “[T]he harm to competition must be disproportionate to consumer benefits…and to the economic benefits to the defendant….” Id. at 14.

4. Conclusion

a. In the absence of consensus and in light of the trend in the courts to use the doctrine sparingly, our recommendation is that it is unnecessary for the AMC to take action regarding refusals to deal.

E. ESSENTIAL FACILITIES DOCTRINE

1. Historical Background: The essential facilities doctrine has never been expressly endorsed by the U.S. Supreme Court, but it has been applied variously by lower courts over a long period of time and appears to have had an important influence on regulation of dominant firm conduct in the European Union. Relatively few cases, however, have actually imposed liability under this doctrine.

a. United States v. Terminal Railroad Ass’n, 224 U.S. 383 (1912); Associated Press v. United States, 326 U.S. 1 (1945): Both cases involved concerted action among competitors to deny access to a jointly owned “facility.” Neither case expressly referenced the essential facilities doctrine.

b. Lorain Journal Co. v. United States, 342 U.S. 143 (1951). Court approved an order requiring a newspaper to accept advertisements, thus ending the newspaper’s efforts to discourage businesses from advertising with a local radio station.
c. *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973): Court upheld liability of wholesale power supplier that denied power to power systems that competed with it on the retail level. Case did not expressly reference essential facilities doctrine, but has been cited by lower courts as endorsing this doctrine.

d. The Seventh Circuit fashioned an influential test to be satisfied before a court can determine that a facility or asset is “essential” and, therefore, the monopolist controlling it might be subject to a duty to share. *MCI Communications Corp. v. AT&T*, 708 F.2d 1081, 1132–33 (7th Cir. 1983): AT&T held liable for refusing to interconnect with MCI because such interconnection was essential for MCI to be able to compete in the long distance business.

*MCI Test*: “(1) control of the essential facility by a monopolist; (2) a competitor’s inability practically or reasonably to duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility.” *MCI Communications Corp. v. AT&T*, 708 F.2d 1081, 1132–33 (7th Cir. 1983).

e. Courts have applied the doctrine to require access on reasonable terms to a wide variety of “bottleneck” assets. *See*, e.g., *Fishman v. Estate of Wirtz*, 807 F.2d 520 (7th Cir. 1986); *Hecht v. Pro-Football, Inc.*, 570 F.2d 982 (D.C. Cir. 1977); *CTC Communications Corp., v. Bell Atl. Corp.* 77 F. Supp. 2d 124 (D. Me. 1999); *Intergraph Corp. v. Intel Corp.*, 195 F.3d 1346 (Fed. Cir. 1999); *City of Anaheim v. S. Cal. Edison*, 955 F.2d 1373 (9th Cir. 1992).

f. Other courts have read the *MCI* test narrowly, noting that it defines limited conditions under which facilities should be viewed as “essential” and serve as the basis for a finding of Section 2 liability. Such conditions may include (1) a refusal to grant access to a facility or asset that cannot be duplicated feasibly; (2) evidence that the refusal totally eliminated competition, not merely impaired it; and (3) that the defendant actually possessed the power to exclude competition in a downstream market and did so. *See*, e.g., *Alaska Airlines, Inc. v. United Airlines, Inc.*, 948 F.2d 536 (9th Cir. 1991). *See also Olympia Leasing v. Western Union Telegraph Co.*, 797 F.2d 370 (7th Cir. 1986).

g. *European Commission*: “A company which has a dominant position in the provision of facilities which are essential for the supply of goods or services abuses its dominant position where, without objective justification, it refuses access to those facilities.” Case COMP D3/38.044 — NDC Health/IMS Health. *See* Sebastien J. Evrad, *Essential Facilities*
2. Issues raised by the Essential Facilities Doctrine:

a. A fundamental tension exists between the doctrine’s implications, i.e., that there are circumstances in which a monopolist has a duty to share its facilities or assets with competitors, and the generally-accepted principle of antitrust law that firms have wide discretion not to deal with or to assist competitors. But see United States v. Colgate & Co., 250 U.S. 300, 307 (1919).

b. Trinko cast doubt on the doctrine’s viability by indicating that prior Supreme Court cases “never recognized such a doctrine.” Trinko at 411. The Court nevertheless expressly refused either to “recognize it or repudiate it,” opining instead that essential facilities claims should be denied “where a state or federal agency has effective power to compel sharing and to regulate its scope and terms.” Id.

c. Academic commentators suggest that the doctrine is necessary in limited circumstances to ensure competition in a market where multiple firms could compete but are prevented from doing so because of a refusal of access to an essential asset or facility.

d. Commentators supporting its use note that, because the doctrine is an exception to the general rule that a monopolist may choose with whom to deal, courts have limited the circumstances under which access to a facility or asset will be ordered. In its limited form, the doctrine may provide a valuable tool for protecting competition and prove to be superior to regulation by government agencies, which may not always be agile and can be subject to capture by the regulated. See, e.g.,


e. Scholars have criticized the doctrine on a variety of grounds:
(i) mandatory sharing obligations may deter investment and innovation;

(ii) the doctrine’s unfettered application to intellectual property could penalize successful innovators;

(iii) the doctrine puts courts into the ill-suited role of public utility regulators;

(iv) the doctrine provides unsuccessful competitors with an inappropriate tool for free-riding on the success of rivals; and

(v) the doctrine requires regulated terms of access which are unlikely to result in efficient pricing.

f. Critics suggest that the anticompetitive concerns to which the doctrine is addressed can be effectively handled through application of precedents applicable to refusals to deal without risking its asserted negative consequences. See, e.g.,:


g. Although some advocate repudiation of the doctrine, there appears to be consensus that the conduct to which it has been applied was appropriately the subject of Section 2 liability. There does not appear to be consensus on how the law would treat denial of access and related claims in the absence of an essential facilities doctrine.

3. Essential Facilities Doctrine Reform: There are a range of potential modifications to the essential facilities doctrine—from abolition to clarification, to invigoration.

a. Abolish the doctrine and replace it with principles to be applied in cases where denial of access to facilities or assets creates competitive concerns.
b. Limit the doctrine to cases involving concerted conduct such as in *Terminal Railroad* and *Associated Press*.

c. Confirm the viability of the doctrine, specify limitations on its use to avoid over-deterrence and endorse a particular test—along the lines of the *MCI* test.

   (i) Restrict the use of the doctrine in cases involving mandatory licensing of intellectual property.

4. If the doctrine is maintained, clarify the standards for determining whether a monopolist’s denial of access to an essential facility is lawful. Tests could include:

   a. **Subjective Test:** Is the intent of the monopolist to harm competition/injure a competitor?

      (i) This has been criticized: “The defendant’s intention is seldom illuminating, because every firm that denies its facilities to rivals does so to limit competition with itself and increase its profits.” Areeda, *supra*, at 852.

   b. **Objective Test:** Does the decision to deny access only make economic sense if it has the effect of monopolizing a separate market?

   c. **Alternative:** “The basic principle is that if a reasonable owner of the facility who had no interest in any downstream operation would have a substantial interest, acting rationally, to refuse access, the owner is entitled to do so.” Temple Lang, *The Principle of Essential Facilities in European Community Law—The Position since Bronner*, 1 J. Network Indus. 375, 385 (2000).

5. Loosen the requirements for an essential facilities claim, by, for example:

   a. Permitting claims in cases where government has the ability to order access, but has elected not to exercise this ability (i.e., reverse that aspect of *Trinko*);

   b. Adopting a more pragmatic and flexible definition of “essential”—which would only require a showing that the facility is competitively important.

**Conclusion:** Because the essential facilities doctrine raises some substantial concern of over-deterrence, many commentators have called for its abolition. In the view of these commentators, the doctrine could be abolished without undermining appropriate enforcement of anticompetitive denials of access that harm consumer welfare. However, other commentators are concerned that anticompetitive unilateral denials of access do not appear to be adequately addressed under other refusal to deal precedents, thus they argue
that abolition of the doctrine even in its current limited form would be harmful, albeit in a limited number of cases. Their conclusion is reinforced by the observed tendency for courts to impose limits on the doctrine. Although there is no clear consensus for abolition or retention of the doctrine, courts have progressively narrowed the application of the doctrine to avoid over-deterrence, while still considering its application in very limited circumstances. In the absence of consensus and in light of the trend in the courts to use the doctrine sparingly, our recommendation is that it is unnecessary for the AMC to take action in this area.

F. PRODUCT BUNDLING AND BUNDLED PRICING

1. The AMC has invited comments on the limited controversy spawned by cases like *LePage’s* with respect to the appropriate legal standard for judging product bundling and bundled pricing when practiced by dominant firms. It has not invited a full review of exclusive dealing, tying, or other sorts of distribution strategies that may constitute exclusionary conduct.

   a. Although product bundling may have some relationship to traditional tying doctrine, it has not been subjected to the *per se* rule of *Jefferson Parish*, and neither has bundled pricing.

   b. A thorough review of tying doctrine, therefore, is beyond the scope of this position paper. We note, however, that the Supreme Court’s decision to grant a writ of certiorari in *Independent Ink*, which presents the issue whether market power should be presumed in the tying context when the tying product is patented, may provide an occasion for the Court to express its views about the continued vitality of the *per se* rule against tying generally.

2. Bundled pricing of the kind at issue in *LePage’s* is probably a ubiquitous practice. Commentators differ in their views of whether and under what circumstances it may pose significant competitive concerns, but to the extent it does, it is likely to do so only in limited circumstances.

   a. There have been relatively few reported cases of challenges to bundled pricing, and these cases have reached varying conclusions. Those cases include:


   See also *Michelin v. EC Commission*, Case T-203/01, Sept. 30, 2003 (Ct. First Instance) ("Michelin II").
b. Other forms of pricing by dominant firms have also been scrutinized by the courts, such as various kinds of incentive payments, rebates, loyalty and market share discounts. Some other related cases include:


3. DOJ/FTC Amicus in *LePage’s*

a. Third Circuit’s decision is open to criticism on a number of grounds.

b. It has been openly questioned by at least one district court in *J.B.D.L.*, which is currently on appeal.

c. 3M and some commentators argued that it is inappropriate in cases of bundled pricing to rely as the Third Circuit did on *Aspen* and *Kodak*. Instead, it should be analyzed under *Brooke Group* and *Matsushita* as a species of predatory pricing and be unlawful only (1) when below some measure of cost, and (2) in a context where recoupment is likely. Otherwise, it is argued, pro-competitive strategies that result in lower prices will be over-deterred.

d. Commentators also urge action because *LePage’s* has led to significant uncertainty as to the legality of pricing strategies by dominant firms, which increases compliance costs and may inhibit pro-competitive price-lowering strategies.

e. But DOJ argued to the Supreme Court that it would be premature for the Court to take the case. The law and economics of bundled pricing is not yet fully developed and requires further study both by courts and economists. The government argued that bundled rebates are distinguishable from predatory pricing, and hence should not be evaluated, as 3M urged, under the elevated standards of *Brooke Group*, which have been justified by fears of false positives and loss of immediate consumer benefits. Indeed, it argued, although “bundled rebates are widespread and are likely, in many cases, to be pro-competitive. . .the bundling of rebates (as distinct from the price reductions that may result) is not necessarily procompetitive.” The brief continued:

>Unlike a low but above-cost price on a single product, a bundled rebate or discount can – under certain theoretical assumptions – exclude an equally efficient competitor, if
the competitor competes with respect to but one component of the bundle and cannot profitably match the discount aggregated over the other products, even if the post-discount prices for both the bundle as a whole and each of its components are above cost.

f. Although a clear test would be welcome, it is not clear yet what that test should be and what empirical basis exists for endorsing any particular test, including the predatory pricing standard of *Matsushita-Brooke Group*.

4. The legal and economic issues relating to bundled pricing are complex and have led to a somewhat unsettled area of antitrust law.

a. Standards for Price Predation vs. Non-price Exclusionary Conduct (*Matsushita-Brooke Group* vs. *Aspen-Kodak-Verizon*) can lead to very different results when applied to price-related behavior such as bundled rebates.

b. As noted above, 3M and some advocates and commentators have urged the courts to evaluate all pricing strategies by dominant firms under the predatory pricing standards of *Matsushita-Brooke Group*, whereas others have argued that predatory pricing is economically distinct from bundled pricing and other forms of pricing strategies.

c. In *LePage’s*, the Third Circuit rejected reliance on the predatory pricing standard, pointing to such factors as: the effects of 3M’s bundled pricing on LePage’s, which did not produce an equally diverse set of products; entry barriers; the degree to which 3M’s discounts impaired LePage’s ability to maintain minimal scale economies; the likelihood that 3M would recoup its discounts through the later exercise of its monopoly power by raising prices after LePage’s was eliminated; its intent to do just that in adopting the bundled discounts; the degree to which the discounts 3M offered to its customers greatly exceeded any savings it may have realized from bundling; and 3M’s lack of evidence of any other valid business reasons for its conduct.

d. In *Ortho Diagnostic*, the district court proposed the following test for evaluating bundled rebates:

“[A] Section 2 plaintiff in a case like this—a case in which a monopolist (1) faces competition on only part of a complementary group of products, (2) offers the products both as a package and individually, and (3) effectively forces its competitors to absorb the differential between the bundled and unbundled prices of the product in which the
monopolist has market power—must allege and prove either that (a) the monopolist has priced below its average variable cost or (b) the plaintiff is at least as efficient a producer of the competitive product as the defendant, but that the defendant's pricing makes it unprofitable for the plaintiff to continue to produce.”

e. In lieu of a tailored standard, the various incentive, rebate, and discount cases in the courts have undertaken a case-by-case, fact specific, economic analysis of various examples of allegedly exclusionary pricing strategies by dominant firms, looking to their effects and economic justifications.

5. Academic study continues, but critical questions remain unanswered. A great deal of commentary has been generated in response to LePage’s:


h. Nalebuff, Barry, *Bundling as a Barrier to Entry*, 119 Q. J. of Econ. 159 (2004) [Note: Nalebuff has done extensive work in the field and has several other published and unpublished papers evaluating various aspects of bundling).


6. Commentators have yet to reach a consensus, however, in response to the call for further study expressed by the government in its brief in *LePage’s*, as to the economic consequences of bundling.

See Kobayashi, Bruce H., *Bundling: A Survey of the Economic Literature* (2005) (working draft; available from author – collecting and surveying economic literature on bundling and concluding that “a review of the economic literature supports the SG’s position [in *LePage’s*] with respect to delaying the promulgation of antitrust standards for bundling.”)

7. There is little doubt that a great deal of uncertainty has been spawned by *LePage’s*, and there are always costs associated with such uncertainty. It complicates and increases the cost of antitrust counseling, complicates the task of risk assessment by firms evaluating pricing strategies, and may even inhibit some firms that are dominant from undertaking certain kinds of aggressive pricing strategies.

a. Advocating a conduct-specific standard, especially if attempted through legislation, would be contrary to the long-standing common law history of the Sherman Act, including Section 2.

b. Even if the AMC concludes that the statement of a standard to clarify the area would be helpful, it is not at all clear what that standard should be, and there is currently no basis for adopting any particular standard for judging bundled pricing.

c. The AMC should permit the issue to continue to develop in the literature and the Courts.