Testimony of Michael E. DeBow

Before the Antitrust Modernization Commission

October 26, 2005

Does America need state antitrust law in the 21st century? Put differently, do the benefits of retaining state antitrust law outweigh the costs of doing so? My overall conclusion is that they do not. Accordingly, I urge the Commission to consider proposing legislation that would amend the Sherman Act to preempt the states substantively – both in terms of state antitrust statutes and the antitrust aspects of state "little FTC acts." I would also urge the Commission to consider legislation to repeal section 4C of the Clayton Act, which conferred *parens patriae* authority on state attorneys general in 1976,[1] or, in the alternative, to provide for a federal-state clearance process for the bringing of such suits.

I say this for three reasons.

First, state antitrust law is an anachronism. It is a holdover from the late 19th century, when the Supreme Court's reading of the Commerce Clause was much narrower than it is today and, conversely, the definition of "intrastate commerce" subject only to state regulation was much wider than it is today. Given the limited view of Congress's commerce power as of the Sherman Act's adoption in 1890, a dual system was virtually a constitutional necessity. State antitrust law was directed at local violators, while federal

[1] 15 U.S.C. § 15(c).

antitrust law could reach business behavior that restrained interstate trade.[2] However, the Supreme Court's post-1937 expansion of the Congressional commerce power cancelled the need for this division of labor between state and federal antitrust enforcers, and rendered state antitrust statutes almost entirely redundant. As a constitutional matter, this remains the case today. State antitrust statutes are a vestige of an earlier age.

Second, the states' involvement in antitrust threatens the coherence of the national antitrust policy developed over the past twenty-five years by successive Republican and Democratic presidential administrations. Antitrust policy experimentation at the state level – in the form of either the enforcement activities of the state attorneys general or the decisions of state courts applying state antitrust statutes – threatens national antitrust policy. This is the most significant cost of continuing the role of state law and state enforcement.

Third, the states' involvement in antitrust to date has not been particularly significant in overall terms – whether measured by number of cases brought or additional enforcement resources brought to bear. This suggests fairly strongly that the benefit from sparing the states from federal preemption is small.

Given the potentially significant costs, and the rather modest benefits, from state antitrust, preemption seems to me the right result. Failing that, Congress should consider a statutory fix to more closely bind the state attorneys general to national antitrust policy.

Permit me to elaborate a bit on the second and third points.

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[2] The Congress that passed the Sherman Act clearly subscribed to this reading. Cantor v. Detroit Edison Co., 428 U.S. 579, 632-35 (Stewart, J., dissenting); Gregory J. Werden & Thomas A. Balmer, *Conflicts Between State Law and the Sherman Act*, 44 U. Pitt. L. Rev. 1, 49-56 (1982). The U.S. Supreme Court followed the same logic in United States v. E.C. Knight Co., 156 U.S. 1 (1895).

The risk of state policy experimentation in antitrust

The idea of a "laboratory of the states" is often invoked to explain and defend American federalism. One of the most famous statements of this idea is Justice Brandeis's dissent in *New State Ice*, where he argued that "It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country."[3]

No such risk-free experimentation is possible in antitrust law, given that every state's economy is interconnected with the economy of every other state. Antitrust policy, if it is to benefit consumers, should be formulated at the national level.

This is true also because, as is widely agreed, the Sherman Act and much of the Clayton Act are sufficiently vague to put the federal courts in the position of having to define the practical meaning of these statues in a common-law fashion. The trajectory of judicial decision making and federal enforcement over the past thirty years has been towards a focus on consumer welfare as the goal of antitrust, and on horizontal price fixing and large horizontal mergers as the greatest threats to consumer welfare. More exotic theories of antitrust injury – such as the Warren Court's concern over the plight of "small, locally owned businesses" in *Brown Shoe*[4] – have been either overruled or politely ignored. This sharpened focus on horizontal price fixing and horizontal merger activity has remained largely constant through the transitions from the Reagan to Bush I to Clinton to Bush II administrations. It is a focus that is clear and fairly administrable,

[3] New State Ice Co. v. Liebmann, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting).
[4] Brown Shoe Co. v. United States, 370 U.S. 294, 344 (1962). For critical commentary, see Robert H. Bork, The Antitrust Paradox 210-216 (1978).

and consumers are better off with this consensus view of antitrust than we would be with any of the alternatives.[5]

Thus, one threat posed by a continued role for state antitrust statutes and enforcement authority is that they might be used in ways that are inconsistent with the consensus view, in order to benefit local economic interests. Specifically, the states might wish to bring in non-consumer welfare considerations into antitrust law – such as (in-state) job losses due to a proposed merger, or the effect of new product development on (in-state) competitors of a monopolization defendant. I will call this threat "state parochialism" – the temptation that state officials might face to place in-state economic considerations ahead of nationwide consumer welfare as the goal sought by antitrust policy.

Another threat posed by state antitrust is interstate conflict. This risk was dramatically illustrated by the 2002 refusal of Massachusetts and West Virginia to join the settlement of the Microsoft litigation negotiated by the Antitrust Division. Although these states' objections ultimately came to naught,[6] the fact remains that a single state's objection delayed the end of this litigation – which obviously had substantial nationwide implications – for two years. This is very nearly the opposite of the original, late 19th century view of the states' role in antitrust, and raises the prospect of significant negative externalities from the extraterritorial impact of state antitrust enforcement.

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[5] For one statement of the consensus view, see Robert E. Litan & Carl Shapiro, *Antitrust Policy in the Clinton Administration*, in American Economic Policy in the 1990s 435 (Jeffrey A. Frankel & Peter A. Orszag, eds., 2002): "For at least 20 years a broad, bipartisan consensus has prevailed regarding the goal of U.S. antitrust policy: to foster competitive markets and to control monopoly power, not to protect smaller firms from tough competition by larger corporations. The interests of consumers in lower prices and improved products are paramount.")

[6] West Virginia dropped its appeal in June 2003, and Massachusetts lost its appeal in June 2004. Massachusetts v. Microsoft Corp., 373 F.3d 1199 (D.C. Cir. 2004).

While the Microsoft episode is well known, there is another example of this problem now being litigated in Texas that is less well known. The plaintiffs in *Coca-Cola Co. v. Harmar Bottling Co.*[7] are soft drink bottlers in competition with Coca-Cola in northern Texas. They sued Coca-Cola and a number of Coca-Cola bottlers in a Texas state court, arguing that certain of Coca-Cola's marketing practices violated the Texas antitrust statute. I should note that versions of these same practices had been upheld by two federal district courts in other states. Nevertheless, plaintiffs won at trial. The jury awarded plaintiffs damages of $14.6 million, and the trial judge enjoined Coca-Cola from using the challenged marketing practices in a geographic area that includes eleven counties in Texas, three in Oklahoma, and twenty-one in Arkansas, and five parishes in Louisiana. Coca-Cola appealed, but the intermediate appellate court affirmed, with scant discussion of the extraterritorial aspect of the injunctive relief. The case was argued to the Texas Supreme Court in November 2004 and remains pending, according to the website of that court.

An amicus brief filed with the Supreme Court by the State of Alabama describes the interstate disharmony produced by the lower courts' rulings:

> It is the application of the injunction to the operation of retail outlets in Oklahoma, Arkansas, and Louisiana that raise a significant question of interstate comity. The Court of Appeals has divested its sister state courts of their authority to apply those three states' antitrust laws to the marketing arrangements complained of in *Harmar*. The fact that other courts have upheld similar soft drink marketing methods . . . underscores the problems attendant to the extraterritorial application of the decision in this case.[8]

As the Alabama brief notes, there has been little written on the issue of interstate – as opposed to international – comity in antitrust. As Professor Hovenkamp explains, this is

[7] 111 S.W.3d 287 (Tex. App.-Texarkana, 2003), petition for review granted, No. 03-0737 (Tex., 2004).
[8] Letter brief from Attorney General Bill Pryor to Andrew Weber, Clerk, Supreme Court of Texas, dated December 17, 2003 (copy on file with author).

ultimately a question of federal constitutional law.

> To be sure, an application of a state regulatory measure or even an antitrust law can run afoul of the commerce clause if it discriminates against interstate commerce or imposes an undue burden on interstate commerce. Likewise, a state assertion of judicial jurisdiction can be unconstitutional when the action complained of had insufficient foreseeable effects within the state.[9]

It appears that further development of state antitrust law may well require the elaboration of fairly intricate commerce clause case law to handle the externality problem. I submit that this is a trip we should avoid taking, if at all possible.

Having noted the costs of maintaining a role for the states in antitrust policy, I will now turn to the benefit side.

The limited benefit from state antitrust activity

To put it bluntly, the states have not done much to augment federal and private efforts in the field of antitrust enforcement. I base this judgment in part on my review of 120 antitrust actions brought by state attorneys general during the period 1993-2002.[10] I found that "the level of state activity is low, particularly in comparison to federal enforcement efforts. On average, the state brought twelve cases per year (five horizontal, five merger, one vertical, and one monopolization) . . . . By contrast, during fiscal years 1993-2002, the Department of Justice brought an average of forty-seven criminal price-

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[9] 14 H. Hovenkamp, Antitrust Law 300 (1999).

[10] Michael DeBow, State *Antitrust Enforcement: Empirical Evidence and a Modest Reform Proposal*, in Richard A. Epstein & Michael S. Greve, eds., Competition Laws in Conflict: Antitrust Jurisdiction in the Global Economy 267-287 (Amer. Enterprise Institute, 2004). I compiled my list of state cases from the indices of legal trade publications, including Antitrust and Trade Regulation Reporter (BNA) and Trade Cases (CCH), as well as standard antitrust reference books. (Cases brought by multiple states were counted as single suits.) My list can be downloaded as a PDF file, titled somewhat infelicitously "DeBow's Appendix," through the AEI website, at http://www.aei.org/events/eventID.244,filter.all/event_detail.asp

Subsequent conversations with antitrust lawyers from various state attorneys general have confirmed what I strongly suspected from the beginning: my research did not pick up every case filed by the states during this ten-year period. Nonetheless, my research does provide a starting place for further research.

fixing cases and twelve merger cases per year."[11] The states' emphasis on price-fixing cases is consistent with the national consensus on antitrust I mentioned at the outset, and the merger cases brought by states turn out, with two exceptions,[12] not to exhibit state parochialism to any observable degree.

In addition I discovered a high degree of federal-state cooperation in the states' efforts.[13] Seven of the 52 Sherman 1 cases were filed jointly or cooperatively with the federal enforcement agencies, twelve of the 47 merger cases, and five of the 11 vertical cases. (None of the states' 10 Sherman 2 cases appeared to involve federal cooperation.)

My overall conclusion was that state enforcement had not "depart[ed] sharply from federal priorities" during the period I studied. For this reason, I felt safe in saying that – with the exception of the Microsoft litigation -- "state antitrust on the whole has been, for the past decade, a fairly dull business."[14]

Given the limited resources committed by state governments to antitrust enforcement, this is hardly surprising. As noted by Robert Hahn and Anne Layne-Farrar, "State antitrust expenditures pale in comparison to federal expenditures. Among those states reporting a separate line item, antitrust budgets are usually only one to two percent of the overall AG budget."[15] They conclude that "state efforts in national antitrust enforcement at best amount to little more than free riding on federal actions."[16]

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[11] DeBow, supra note 10, at 272.
[12] In my earlier article I noted two exceptions to this rule – Maine v. Connors Brothers Ltd.,2000-2001 Trade Cas. (CCH) ¶72,937 (Me. Sup. Ct., 2000), and Pennsylvania's attack on Russell Stover's acquisition of the Whitman Chocolates assets from Pet, Inc., Antitrust & Trade Reg. Rep. (BNA), no. 1614 (May 13, 1993), at 583. See DeBow, supra note 10, at 276-77.
[13] For an overview of federal-state cooperation, see I ABA Section of Antitrust Law, State Antitrust Practice and Statutes 1-10 – 1-21(3d ed. 2004).
[14] DeBow, supra note 10, at 271.
[15] Robert W. Hahn & Anne Layne-Farrar, *Federalism in Antitrust*, 26 Harv. J.L. & Pub. Pol'y 877, 889 (2003).
[16] Id. at 890.

Although I would defer to the federal enforcement authorities on the issue of the worth of the states' enforcement efforts, they seem to me to be of a very limited order. This fact, combined with the potential threat state antitrust poses to the national consensus on antitrust policy, leads me to conclude that the public would be benefited by the express preemption of state antitrust statutes and state antitrust enforcement.

An alternative reform

In view of the likelihood that legislation taking away the states' thirty-year-old *parens patriae* authority would be politically difficult, I would like to propose an alternative.[17] If the state antitrust statutes were expressly preempted, it might promote consumer welfare to allow state attorneys general to continue to bring *parens* suits under the federal antitrust statutes, so long as there is enough federal oversight to ensure that the states' efforts do not undermine the national consensus on antitrust policy. I propose a revision of Clayton 4C that would create a formal review process wherein a state attorney general who wished to bring a *parens* case would submit the matter for review by the Antitrust Division and the FTC. If the federal agencies approved the filing, the state could move forward, and if not, not. Such a prior approval requirement would bind the state attorneys general to the national antitrust consensus, as interpreted by the presidential administration in office, and would thus greatly reduce the threat that state antitrust enforcement activity poses to that consensus, and to the national economy generally.

[17] In my 2004 article I proposed another alternative, based on a bill then pending in the Alabama legislature that would have redefined that state's antitrust law solely in terms of horizontal price-fixing. See DeBow, supra note 10, at 280-281. On further reflection, I consider reforming Clayton 4C a more promising route to reform.

I realize that there may be some constitutional questions raised by this proposal, but I disavow any claim of expertise in constitutional analysis. I would hope there would be a constitutionally-permissible way to structure federal oversight of the *parens* authority in the general way I've described.