Testimony of John Thorne
Before the Antitrust Modernization Commission

Regulated Industries

December 5, 2005

Thank you for inviting me to testify. I am a senior vice president and deputy general counsel of Verizon Communications Inc., where I represented the petitioners in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004) and *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128 (1998) – two decisions involving a regulated industry in which a unanimous Supreme Court dismissed antitrust claims at the pleadings stage. I also am an adjunct faculty member at Columbia Law School where I teach a class on telecommunications law.

I have spent twenty-plus years studying the intersection of antitrust and regulation in telecommunications. Fourteen of those years I spent working on the aftermath of a single antitrust case in a heavily-regulated industry: the AT&T breakup consent decree. I had not expected to spend so much time on one matter. Judge Greene didn't either. When Judge Greene approved the breakup decree in 1982, he wrote that he would not want to administer a broad regulatory injunction even if he employed special masters to help him. To administer such a decree would "require[] … a re-creation of the FCC's Common Carrier Bureau in the guise of an arm of the Judiciary" which the judge understood would be an "undesirable" development "for many different reasons."[1]

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[1] *United States v. AT&T*, 552 F. Supp. 131, 168 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983). Judge Greene explained: "[T]here is no reason to believe that, in the end, a judicially-created bureaucracy would be any more capable than the FCC itself of performing the unending task of vigilance and oversight that would be required to ensure that an integrated Bell System did not engage in anticompetitive conduct. * * * [S]uch a remedy could contravene the separation of powers doctrine because it would involve the creation of a substantial quasi-legislative, quasi-executive bureaucracy within the Judicial Branch of the government. Practically, the remedy could be impossible to administer because of the need for substantial budgetary authority and a large administrative apparatus." *Id.* at 168 & n. 158. Justice Rehnquist, writing for a three-Justice dissent to the summary affirmance of the breakup decree, expressed concerns with Judge Greene's overriding state regulation of telephone service and the intractability of the enterprise Judge Greene was embarking on: "I am troubled by the notion that a district court, by entering what is in essence a private agreement between parties to a lawsuit, invokes the Supremacy Clause powers of the Federal Government to pre-empt state regulatory laws. * * * It is not clear to me that this [public-interest] standard, or any other standard the District Court could have devised, admits of resolution by a court exercising the judicial power established by Art. III of the Constitution. * * * Questions of policy are not submitted to judicial determination …." 460 U.S. at 1002-04 (citations and inner quotes omitted).

Despite Judge Greene's best intentions and his substantial administrative skill, what followed may have been the most ambitious piece of industrial reform ever managed by a single person. Ripping apart the world's largest corporation was easy compared to managing the pieces afterwards. Post-divestiture, the Justice Department issued thousands of advisory letters. Judge Greene's court received more than 6,000 briefs. Thirteen groups of consolidated appeals were carried to the D.C. Circuit. The Supreme Court received a half-dozen divestiture-related petitions for review. The decree developed its own lore, its own common law, its own unique traditions, precedents, procedures, formalities, and technical vocabulary.

The regulatory line-drawing just never ended. May a Bell company repair its local network when there is a network outage?[2] May a Bell company compete for local services outside its initially-assigned footprint against another Bell company?[3] Getting answers to simple questions often took months or even years. In March 1988, for example, the Department of Justice recommended that South Central Bell be allowed to provide private-line service between Northwest Alabama Junior College and its off-campus extension in Tuscumbia, Alabama. Nine months passed before the court authorized the service. It took five years and two months for Bell Atlantic to win an unopposed motion to not have to disconnect cell phone calls in progress on the Amtrak train between Washington, D.C. and Philadelphia. Permissions were granted one local phone company at a time, and sometimes household by household. "Pacific Bell is permitted to provide

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[2] Judge Greene initially threatened that repair might be forbidden (by the decree prohibition on Bell company manufacturing) and that the Bell companies would be "subject to enforcement proceedings." He advised the Bells to seek guidance from the Department of Justice. They immediately did so. The Department, however, declined to provide guidance because it "has neither the obligation nor the resources" to do so. Subsequently, the Department opined that the Bells may engage in some repair functions, but it asked Judge Greene to confirm its interpretation because "the decree's 'manufacturing' prohibition is ambiguous with respect to 'repairs.'" Judge Greene did not immediately respond and the particular repair question became moot. The affected Bell company and the Department urged the court to rule anyway to clarify the issue for the future. Judge Greene refused on the ground that there was no longer any "live controversy." Three years later, during an emergency hearing following a massive network outage affecting millions of local customers, Judge Greene finally ruled that the Bell companies may engage in repairs.

[3] The Department flip-flopped on the question, Judge Greene ruled that the Bell companies were restricted to their territories based on a "policy" of the decree that the Bell companies should "work cooperatively" and not compete, but the D.C. Circuit reversed, permitting the Bells to compete outside their territories against one another. *United States v. Western Elec. Co.*, 627 F. Supp. 1090, 1108 (D.D.C.), *rev'd*, 797 F.2d 1082 (D.C. Cir. 1986).

telephone service to Mrs. Mary Campbell, who lives in the Plymouth exchange in the Stockton, California LATA, via the Placerville central office in the Sacramento, California LATA." "Wisconsin Bell may provide interLATA cross-boundary foreign exchange service to Ms. Vicki Millard and Mr. Ricky Schultz, as directed by the Wisconsin Public Service Commission." These were actual district court orders.

The regulation-by-antitrust-court was, as Judge Greene had predicted, "undesirable," leading Congress in 1996 to end Judge Greene's reign and to transfer the remaining issues from the antitrust court to the FCC.[4]

The principal general question for today's panel is how antitrust should apply to already-regulated industries. My general answer is that antitrust courts should approach regulated industries with a realistic (*i.e.*, modest) view of the courts' own institutional abilities; that regulation is often a cause of competition problems, which can be rectified best at the regulatory source rather than clubbing the regulated firm with antitrust judgments; that dominant firms (the ones most likely to be the subjects of regulation) should not be subject to special condemnation when they cut price, invest, or innovate; and that there are several traditional antitrust doctrines designed to avoid conflict with regulation that should continue to be respected. I mentioned the experience under the AT&T breakup decree at the outset because it is the paradigm of what can go wrong when a generalist antitrust court, even a very competent one, attempts to take on the functions of a regulatory agency.

I would like to address today's question more specifically by starting with three general observations about regulation. I will then turn to several specific principles for harmonizing antitrust and regulation.

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[4] The history of the AT&T breakup decree and other antitrust issues in the telecommunications industry is described at length in a series of books I co-authored. *See* Peter W. Huber, Michael K. Kellogg & John Thorne, Federal Telecommunications Law (Aspen Law & Bus. 2d ed. 1999 & Supps. 2004 & 2005) (chapters 4 and 7 of this second edition, plus the 2004 supplement in particular, describe antitrust litigation and mergers in this industry); Michael K. Kellogg, John Thorne & Peter W. Huber, Federal Telecommunications Law (Little Brown & Co. 1992 & Supp. 1995) (chapters 3-8 describe in greater detail the now-superseded AT&T breakup decree and parallel decree governing GTE); John Thorne, Peter W. Huber & Michael K. Kellogg, Federal Broadband Law (Little Brown & Co. 1995) (chapters 8 and 9 describe antitrust issues involving content, conduit, and media power).

Observations about regulation:

1. The goals of regulation and antitrust are often directly adverse.

Economic regulation often is the antithesis of antitrust. Instead of promoting free markets, it prohibits competition. It restricts entry, controls price, skews investment (causing too much or too little), and limits innovation (delaying innovations by subjecting them to regulatory approval, barring marketing of innovations, or forcing innovations to be shared with rivals on regulated terms). There are many, many examples. Here are two:

Telephones. The early history of the telephone industry was characterized by cradle-to-grave regulation. Entry was forbidden. Prices were regulated. Investment initially was encouraged, some observers claim over-encouraged ("gold-plated"), by the prospect of guaranteed recovery of prudently-incurred costs. Investment later was discouraged by requirements that facilities be shared at super-low prices. Innovations were delayed while regulators scrutinized them. A simple innovation like letting phone lines carry data communications required multiple lengthy FCC proceedings before it could be offered.

In the face of uncertainty over how antitrust would apply on top of the regulation, AT&T agreed to a series of antitrust consent decrees that simply added to the agency regulations. When Bell Labs scientists invented transistors, AT&T was forbidden to manufacture radios or computers that used the transistors because those products fell outside the "common carrier communications services" to which a 1956 antitrust consent decree restricted AT&T's business. The 1956 consent decree further required AT&T to license "all existing and future Bell System patents" to all persons at "reasonable royalties," turning AT&T into a sort of common carrier of its intellectual property. The 1974 government antitrust case that led to the 1982 breakup consent decree was at its core attacking a market structure that had been created by regulation. It was a fight between the Justice Department on one side versus the federal and state utility regulators on the other side, with AT&T caught in the middle.

Following the repeal of federal bans on entry and the preemption of state entry barriers, the telephone business is now characterized by a competitive mix of traditional wireline telephone providers, wireless providers, cable telephony, VOIP providers, and new services such as

Verizon's FiOS. These intermodal competitors are capturing an increasing share of the traditional mass market local and long distance telephone business.[5]

Video. The multichannel video market currently is being kept non-competitive by regulation. After suffering some modest competition from satellite services, incumbent cable TV operators assert that all *wire-based* competitors must obtain cable franchises, one by one, from thousands of local municipalities before they may compete.[6] This requirement applies, they say, even to telephone companies that already have local telephone franchises. At the urging of incumbent cable operators, several states have increased the burdens of obtaining franchises with so-called "level playing field" laws.[7] Cable operators are, in my view, testing the outer limits of what they can defend under *Noerr-Pennington* in using regulation as a shield to competition.

[5] Mem. Opinion & Order, Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control, WC Docket No. 05-75, ¶ 105 (FCC released Nov. 17, 2005). Prices are down in absolute terms and relative to the Consumer Price Index. *Compare* FCC, Statistics of Communications Common Carriers 2004/2005 Edition, Table 5.10 (Nov. 7, 2005) (-2.5 percent annual decrease for all telephone services) *with* Bureau of Labor Statistics, Consumer Price Index Summary News Release (Nov. 16, 2005) (4.3 percent annual increase). There are now more wireless phones than fixed telephone lines. FCC, Statistics of Communications Common Carriers 2004/2005 Edition, Tables 5.1 (178 million combined ILEC and CLEC telephone lines), 5.6 (185 million wireless phones).

[6] Incumbent cable operators control three-fourths of the multichannel video market. *See Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Eleventh Annual Report, 20 FCC Rcd 2755, ¶ 7 (2005). Cable prices increased 40 percent in the last five years – four times faster than the Consumer Price Index. *See Statistical Report on Average Rates for Basic Service, Cable Programming Service, and Equipment*, Report on Cable Industry Prices, 20 FCC Rcd 2718, Attachment 4 (2005). In the few places where incumbent cable operators face competition from a wire-based competitor (not just satellite services), monthly cable rates are 16 percent lower and customers pay 27 percent less per programming channel. *See id.* Attachment 6. Wire-based competitors "induce incumbent cable operators to respond by providing more and better services and by reducing rates and offering special deals." U.S. GAO, Report to the Subcommittee on Antitrust, Competition Policy, and Consumer Rights, Committee on the Judiciary, U.S. Senate, *Telecommunications: Wire-Based Competition Benefited Consumers in Selected Markets* at 12 (Feb. 2004).

[7] *See* Thomas W. Hazlett & George S. Ford, *The Fallacy of Regulatory Symmetry: An Economic Analysis of the "Level Playing Field" in Cable TV Franchising Statutes*, 3 Bus. & Politics 21, 43 (2001) (describing the entry inhibitions of the level-playing-field statutes and cable incumbents' "strategic use of administrative processes to thwart entry" and preserve "a monopolistic equilibrium"). One Wall Street analyst observed that "[c]able providers are aware of the protective effects franchise requirements have and regularly tell their investors how the process will prevent near term competitive entry by the Bells." J. Hodulik, UBS, *Franchise Fight Likely To Delay Video Competition* at 3 (May 2, 2005).

2. Even when regulation and antitrust have the same goals, regulation works by methods that are substantively contrary to antitrust – indeed, regulatory methods tend to preserve monopolies.

Ordinary public utility regulation may bear "a strong resemblance" to competition because it often is designed to produce the same end result that a competitive process would produce.[8] But the compatibility of the desired end results does not mean that antitrust can borrow from regulation in defining duties. Even when the goals of antitrust and regulation are the same, their methods are very different. Antitrust fosters a competitive process. Regulation compels specific results. A few examples illustrate the difference:

Acquiring or continuing a monopoly. Antitrust does not require dismantling of a lawful monopoly.[9] Regulation may require dismantling.

Pricing. Antitrust does not require a monopolist to charge less than a monopoly price.[10] Regulation typically restricts price to some measure of costs.

Dealing. Antitrust generally does not require affirmative dealing with others.[11] Regulation typically does. Common carriers by definition must deal with all customers.

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[8] Alfred E. Kahn, 1 The Economics of Regulation 63 (MIT reprint 1988).

[9] *Trinko*, 540 U.S. at 407 ("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.*"); *United States v. United States Steel Corp.*, 251 U.S. 417, 451 (1920) (Section 2 "does not compel competition"); *Eastman Kodak Co. Image Tech. Servs., Inc.*, 504 U.S. 451, 480 (1992) (power plus *conduct*); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 596 n.19 (1985); *United States v. Microsoft Corp.*, 253 F.3d 34, 51, 58 (D.C. Cir. 2001) (*en banc*) ("merely possessing monopoly power is not itself an antitrust violation"; "having a monopoly does not by itself violate § 2"; "'the successful competitor, having been urged to compete, must not be turned on when he wins,'" quoting *United States v. Aluminum Co. of America*, 148 F.2d 416, 430 (2d Cir. 1945) (L. Hand, J.)).

[10] *Trinko*, 540 U.S. at 407 ("charging of monopoly prices, is not … unlawful").

[11] *Trinko*, 540 U.S. at 408 ("as a general matter, the Sherman Act 'does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal,'" quoting *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919)). Antitrust properly focuses on *negative* duties (to avoid acts that hinder rivals' independent efforts to attract customers) and not *affirmative* ones. *See Illinois ex rel. Burris v. Panhandle Eastern Pipe Line Co.*, 935 F.2d 1469, 1484 (7th Cir. 1991) (negative/affirmative line); *Olympia Equip. Leasing Co. v. Western Union Telegraph Co*., 797 F.2d 370, 375-76 (7th Cir. 1986) ("'There is a difference between positive and negative duties, and the antitrust laws, like other legal doctrines sounding in tort, have

Nondiscrimination. Antitrust generally does not compel equality of treatment (with some exceptions such as the Robinson Patman Act).[12] Regulation typically prohibits unreasonable discrimination between like customers.

Mergers. The antitrust agencies evaluate whether a merger will harm competition. If there is no likely harm, the agency doesn't challenge the merger. By contrast, the FCC requires mergers affirmatively to serve the public interest. This leads the FCC to impose conditions well beyond what either DOJ or the FTC thinks is needed to approve a merger.

Ironically, regulation that imposes a "competitive" *result* can have the effect of preventing competition itself. For example, the swiftest and surest way to end a monopoly is to let it charge a high price; high prices attract entry. Conversely, forcing a monopolist to share its productive facilities with rivals results in shared monopoly, while deterring rivals' independent investments in competing facilities. Treating the symptoms of monopoly may keep it intact longer.

3. Regulation more readily admits of fine-tuning.

Regulation operates procedurally very differently than antitrust. Regulation can be experimental, trying one approach, then another, changing course as the results are seen. Regulatory enforcement mechanisms can be calibrated to provide incentives that motivate desired conduct, making adjustments with experience. Enforcement penalties can be closely tied to

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generally been understood to impose only the latter.'"); S. Breyer, Regulation and Its Reform 157 (1982) (antitrust laws "act negatively, through a few highly general provisions *prohibiting* certain forms of private conduct. They do not affirmatively order firms to behave in specified ways; for the most part, they tell private firms what not to do."). The distinction between acts negatively interfering with others, on one hand, and a failure to lend affirmative assistance, on the other, is fundamental elsewhere in the law. *See DeShaney v. Winnebago County Dep't of Social Servs.*, 489 U.S. 189 (1989) (relying on same line to hold that failure to provide assistance is not "deprivation" under Due Process Clause).

[12] Richard A. Posner, Antitrust Law 82-86 (2d ed. 2001) (discussing "acute difficulty of properly interpreting evidence of alleged price discrimination"; "It would be infeasible to draft a decree forbidding systematic price discrimination that did not constrain or inhibit legitimate pricing behavior as well."). The rare cases when antitrust has required nondiscriminatory dealing have involved *concerted* action. *United States v. Terminal Railroad Ass'n*, 224 U.S. 383 (1912), involved a multiparty agreement for operating a terminal railroad facility, in which the members discriminated against nonmembers. *Associated Press v. United States*, 326 U.S. 1, 10-11 (1945), involved a multiparty agreement that openly discriminated in membership between those who would compete against existing members and those who would not.

the substance of the regulatory duties, with care taken that beneficial conduct such as price-cutting, investment, and innovation is not deterred by excessive or imprecisely administered penalties (which would cause the regulated firm to avoid entire areas out of caution). The administrative agency gains experience over time and the same agency will be there to revisit specific requirements that prove ineffective or counterproductive.

Antitrust is substantively less fine-tuned and procedurally less fine-tunable. It forbids "monopolization" and restraints that are "unreasonable." Its enforcement, involving juries, class actions, and treble damages, is a potent but imprecise deterrent, making it important not to point this weapon in the direction of normally pro-competitive behaviors. The administration of antitrust by one-time lay juries means there is usually no opportunity to gain industry-specific expertise or to make adjustments in light of experience. In particular, a common-law antitrust process is not able reliably to make the right judgments about how much sharing and on what terms will do more good than harm.[13]

Consider the regulatory regime at issue in the *Trinko* case. Trinko alleged that Verizon failed to send prompt acknowledgements of rivals' orders for unbundled telephone lines. A precise specification of what Verizon was supposed to do was contained in three documents: (1) an interconnection agreement between Verizon and Trinko's carrier, AT&T; (2) Carrier-to-Carrier Guidelines established jointly by Verizon, its rivals (known in industry jargon as "CLECs"), and the New York Public Service Commission; and (3) a state-commission administered Performance Assurance Plan that defines automatic penalties to be paid to the CLECs for performance deficiencies. For example, performance measure "OR-8" requires Verizon to check each CLEC order to ensure it is "valid and complete" and then to return an acknowledgement to the CLEC within two hours, 95% of the time. The penalty for missing this performance measure was set with regard to the size of the performance shortfall, its effect on the CLEC business, and whether Verizon had missed this measure in the past. The state commission retained discretion to adjust the weights of penalties up or down as experience was gained.

[13] This is not a new idea. The common law reluctance to define and enforce terms on which mandated sharing of monopolist facilities with aspiring competitors is to be afforded, based only on general standards, is over a century old. *Express Cases*, 117 U.S. 1, 28-29 (1886).

The regulatory enforcement regime in New York, where Trinko's office is located, put at risk a sizeable fraction of Verizon's annual profits. The FCC approved the New York enforcement regime as potent: "We believe it is useful to compare the maximum liability level to Bell Atlantic's net revenues derived from local exchange service – after all, it is primarily its local service profits that Bell Atlantic would have a theoretical incentive to 'protect' by discriminating against competing local carriers. * * * In 1998, Bell Atlantic reported a Net Return of $743 million in New York: $269 million [the amount then at risk under the Performance Assurance Plan] would represent 36% of this amount."[14]

There are profound problems accompanying calibration of any sharing duties. Excessive sharing (a) undermines the incentive of the regulated firm to invest in creating or maintaining or upgrading facilities (the entire risk is borne by the regulated firm, but rewards must be shared); (b) undermines the incentive of rivals to build or buy when renting at low prices from the regulated firm is cheaper and less risky (the regulated firm is stuck with the facility if demand is disappointing); and (c) harms *facilities-building* rivals, whose investments (*e.g.*, more efficient than the regulated firm but perhaps not as efficient as possible) must compete against rivals renting from the regulated firm at super-low prices. One of the strongest amicus briefs in the Supreme Court in *Trinko* came from the equipment manufacturers, who are neutrals in the competitive fight between incumbent telephone companies and the CLECs; they just want the market to grow so they can sell more equipment. The manufacturers argued that excessive sharing requirements were depressing investments by both the incumbents and new rivals.[15]

Principles for reconciling antitrust and regulation:

Considering the above features of regulation – that regulation's goals sometimes are directly anticompetitive; that even when regulation seeks to compel a competitive result its methods may interfere with free markets; and

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[14] Application of Verizon New York, 15 FCCR 3953 (1999), ¶ 436. The available annual penalty under the New York plan subsequently was increased to $293 million although Verizon's profits from the state had declined. At the time of the *Trinko* decision, the total of available annual penalties in Verizon's states (not counting New Jersey) was $1.24 billion. New Jersey had no annual cap on the penalties that could be incurred.

[15] Amicus Brief of Telecommunications Industry Ass'n, 16 & n.6 (U.S. May 23, 2003) (citing Telecom. Industry Ass'n., 2003 Telecommunications Market Review and Forecast at 55, 60 (2003)).

that regulatory agencies unlike antitrust courts have the ability to experiment and fine-tune – I offer the following principles:

1. Regulation that conflicts with free markets requires heightened justification.

This first principle may not fit within the charter of this Commission, in which case it should be referred to the Regulatory Modernization Commission when and if such a commission ever gets constituted. Just as you require a heightened justification for a rule that restrains free speech, you should require a heightened justification for a rule that restrains competition. Free competition, like free speech, is so central to the Nation's economy and life that restraints must be compellingly justified and no broader than necessary to serve the justification.[16]

Courts reviewing regulation already apply this principle. As an illustration in the telephone context, Justice Breyer's concurrence in a decision striking down an early version of the FCC's overbroad sharing rules noted that the FCC had not sufficiently considered the anticompetitive effects of its rules, specifically that sharing requirements deter investment. "[A] sharing requirement may diminish the original owner's incentive to keep up or to improve the property by depriving the owner of the fruits of value-creating investment, research, or labor. * * * Nor can one guarantee that firms will undertake the investment necessary to produce complex technological innovations knowing that any competitive advantage deriving from those innovations will be dissipated by the sharing requirement."[17] Justice Breyer showed little patience with the FCC's claim that sharing rules always promoted competition: "Increased sharing by itself does not automatically mean increased competition. It is in the *un*shared, not in the shared, portions of the enterprise that meaningful competition would likely emerge. Rules that force firms to share every resource or element of a

[16] Similar arguments were made for limiting statutory departures from the common law, from which antitrust itself derives. *E.g.*, 3 Norman J. Singer, Sutherland Statutory Construction 171 (5th ed. 1992) ("Statutes which impose duties or burdens or establish rights or provide benefits which were not recognized by the common law have frequently been held subject to strict, or restrictive, interpretation.").

[17] *AT&T Corp. v. Iowa Utilities Board*, 525 U.S. 366, 428-29 (1999) (Breyer, J.).

business would create, not competition, but pervasive regulation, for the regulators, not the marketplace, would set the relevant terms."[18]

2. Antitrust should not be rewritten or interpreted to encompass specific regulatory requirements.

As discussed above, there are two kinds of reasons that courts cannot soundly borrow violations of regulatory duties to define antitrust violations.[19]

First, the substantive policies are fundamentally different in what they do about the ideal of "competition." For example, in telephones, the 1996 Act seeks to "jumpstart" competition and "uproot" monopolies; antitrust does neither. The choices made under the 1996 Act about terms of sharing (including the all-but-confiscatorily low prices) are *not* the choices antitrust makes. Most notably, antitrust does *not* require below-monopoly pricing for any sharing. The Supreme Court has specifically cautioned against confusing antitrust wrongs with other wrongs, including even the evasion of regulatory controls on exploitation of a monopoly.[20]

Second, enforcement systems differ. Agency decision-makers are able to act flexibly and prospectively and use calibrated penalties (*e.g.*, the 1996 Act regime), whereas juries act retrospectively through severe treble-damages penalties and judges adopt injunctions that typically are difficult to modify. Thus the Supreme Court has recognized that substantive policy

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[18] *Id*. at 429. Similarly, D.C. Circuit Senior Judge Williams wrote that forced sharing can reduce incentives for innovation and investment: "If parties who have not shared the risks are able to come in as equal partners on the successes, and avoid payment for the losers, the incentive to invest plainly declines." *USTA v. FCC*, 290 F.3d 415, 424 (D.C. Cir. 2002), *cert. denied*, 538 U.S. 940 (2003).

[19] Under the 1996 Telecommunications Act, there is also a textual reason for not incorporating regulatory duties into antitrust: The savings clause precludes using the new regulatory duties to "modify" (add to) pre-existing antitrust duties. It declares that Congress was *not* treating the new 1996 Act duties as if they defined a new standard for "restraint of trade" or "monopolizing" conduct under the Sherman Act. *Compare Robertson v. Seattle Audubon Soc'y*, 503 U.S. 429, 439-40 (1992) (law deeming certain conduct to come within prior statute "modified" prior statute).

[20] *NYNEX v. Discon*, 525 U.S. at 136, 137. That violations of other standards overlap *as a matter of fact* with violations of antitrust standards (*see* ABA, Antitrust Law Developments 249 (5th ed. 2002)) does not mean that wrongfulness under the former is the reason, or even a reason, for finding the conduct wrongful under antitrust. An examination of the ABA statement and its footnote support confirms that it is, at best, a description of *de facto* overlap.

choices now go hand in glove with particular enforcement regimes.[21] Respect for differences in implementation and remedial choices is most important when a regulatory regime "comes as close to the line of overregulation as possible–that is, to achieve the benefits of regulation right up to the point where the costs of further benefits exceed the value of those benefits."[22] The remedial choices of specific statutes thus trigger the principle that the "specific governs the general."[23] And antitrust litigation would inevitably operate as an "extraneous pull" on agency processes themselves (*Buckman Co. v. Plaintiffs' Legal Committee*, 531 U.S. 341, 353 (2001)), distorting the choices of participants and decision-makers alike.

Accordingly, because regulatory determinations are deeply experimental and uncertain, and price regulation in particular "inevitably distorts the incentive to reduce costs or engage in further innovation" and tends to chill new entry that higher prices might attract, "[a]ntitrust courts have rightly resisted undertaking the heavy, continuous, and unguided burden of supervising the economic performance of business firms."[24] The exceptions – recall Judge Greene – prove the principle.

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[21] *See* R. Fallon, D. Meltzer & D. Shapiro, *Hart & Wechsler's The Federal Courts and The Federal System* 841-42 (4th ed. 1996). In many contexts since the 1970s, the Court has rejected the notion that it is better, or even permissible, to add remedies to those Congress chose for particular statutory violations, recognizing the importance of congressional *remedial* choices, such as whether agencies (or numerous individual judges or juries) resolve disputes under potentially open-ended standards, and what remedies attach to violations. *See*, *e.g.*, *Alexander v. Sandoval*, 532 U.S. 275, 290 (2001); *Karahalios v. Nat'l Fed. of Federal Employees*, 489 U.S. 527, 533 (1989); *Merrell Dow Pharmaceuticals Inc. v. Thompson*, 478 U.S. 804 (1986); *Massachusetts Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 145, 146-147 (1985); *Middlesex County Sewerage Auth. v. Nat'l Sea Clammers Assn.*, 453 U.S. 1, 19-20 (1981); *Northwest Airlines, Inc. v. Transport Wkrs.*, 451 U.S. 77, 93-94 (1981); *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 19-20 (1979).

[22] Easterbrook, *Statutes' Domains*, 50 U. Chi. L. Rev. 533, 541 (1983).

[23] *Varity Corp. v. Howe*, 516 U.S. 489, 511-12 (1996); *see Patterson v. McLean Credit Union*, 491 U.S. 164, 180-82 (1989) (refusing "'to read an earlier statute broadly where the result is to circumvent the detailed remedial scheme constructed in a later statute'").

[24] 3 P. Areeda & H. Hovenkamp, Antitrust Law ¶ 720b at 256 (2d ed. 2000) (footnote omitted, noting rare exceptions embodied in judicial decrees); *United States v. Trenton Potteries Co.*, 273 U.S. 392, 397-98 (1927) (recognizing problems with antitrust price administration); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 283 (6th Cir. 1898) (Taft, J.) (to examine reasonableness of price is to "set sail on a sea of doubt"); *see Image Technical Servs., Inc. v. Eastman Kodak Co.*, 125 F.3d 1195, 1225 (9th Cir. 1997) (rejecting even a remedial "reasonable price" order, restricting order to "nondiscriminatory pricing"); *City of Milwaukee v. Illinois*, 451 U.S. 304, 325 (1981) ("Not only are the technical problems difficult– doubtless the reason Congress vested authority to administer the Act in administrative agencies possessing the necessary expertise–but the general area is particularly unsuited to the approach inevitable under a regime of federal common law."). Then-Judge Breyer explained in *Town of Concord v. Boston Edison Co.*,

3. Antitrust should respect regulation in the well-worn traditional ways.

Some of the ways that antitrust and regulation intersect have stood the test of time and there is no reason to alter them. Two century-old doctrines, in particular, should be retained: the filed tariff doctrine and the line extension efficiency doctrine for approving common carrier mergers.

a. Filed tariff doctrine. The filed tariff doctrine was recognized by Justice Brandeis's decision in *Keogh v. Chicago & Northwestern Railway*, 260 U.S. 156 (1922). It "forbids a regulated entity to charge rates for its services other than those properly filed with the appropriate federal regulatory authority."[25] The doctrine has two distinct aspects as to services that must be set forth in tariffs. *First*: the filed tariff doctrine "bars all claims – state and federal – that attempt to challenge the terms of a tariff that a federal agency has reviewed and filed."[26] That prohibition prevents *violations* of tariffs. *Second*: the doctrine "ensure[s] that the filed rates are the exclusive source of the terms and conditions by which the common carrier provides to its customers the services covered by the tariff."[27] That

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915 F.2d 17, 25 (1st Cir. 1990), in the related context of price-squeeze law, "why antitrust courts normally avoid direct price administration":

> [H]ow is a judge or jury to determine a "fair price?" Is it the price charged by other suppliers of the primary product? None exist. Is it the price that competition "would have set" were the primary level not monopolized? How can the court determine this price without examining costs and demands, indeed without acting like a rate-setting regulatory agency, the rate-setting proceedings of which often last for several years? Further, how is the court to decide the proper size of the price "gap?" Must it be large enough for all independent competing firms to make a "living profit," no matter how inefficient they may be? If not, how does one identify the "inefficient" firms? And how should the court respond when costs or demands change over time, as they inevitably will?

[25] *Arkansas-Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 (1981).

[26] *Evanns v. AT & T Corp.*, 229 F.3d 837, 839 (9th Cir. 2000).

[27] *Brown v. MCI WorldCom Network Svcs., Inc.*, 277 F.3d 1166, 1170 (9th Cir. 2002) (emphasis omitted) (quoting *Lovejoy v. AT&T Corp.*, 92 Cal.App.4th 85, 100, 111 Cal. Rptr. 2d 711 (Cal. Ct. App. 2001)) (quoting *AT&T v. Central Office Telephone, Inc.*, 524 U.S. 214, 230-31 (1998) (Rehnquist, C.J., concurring)); *see also Brown*, 277 F.3d at 1170 ("[N]o one may bring a judicial proceeding to enforce any rate other than the rate established by the filed tariff.").

prohibition denies legal effect to service arrangements that fall outside a tariff when the service is one that can lawfully be provided *only* by tariff.[28]

The filed tariff doctrine serves two purposes that remain as vital today as when the doctrine arose. First, it protects against judicial interference with agency determinations of the reasonableness of rates and terms of service.[29] Because the tariffs are approved by an administrative agency, which has primary jurisdiction over the tariff, the filed tariff doctrine ensures that courts will abstain from determining whether a rate or other term is "unreasonable" despite the agency's approval of it.[30] The doctrine thus recognizes that "(1) legislatively appointed regulatory bodies have institutional competence to address rate-making issues; (2) courts lack the competence to set . . . rates; and (3) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime."[31]

Second, the doctrine protects customers against discrimination by precluding a utility from providing service to customers on any terms if those terms are not established in a tariff (which is then available generally).[32] Thus, a plaintiff may invoke the filed tariff doctrine to prevent a carrier from discriminating against it by charging rates higher than those in the tariff, or by providing certain customers with rebates or discounts from the published tariff rates.[33] By holding that the published tariff terms and

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[28] *See* 47 U.S.C. §§ 203, 252(h), 252(i) (requirement of tariff filing); *Central Office*, 524 U.S. at 224-25 (explaining that doctrine prohibits claims for privileges that are covered by topics included in tariff).

[29] *See Wegoland Ltd. v. NYNEX Corp.*, 27 F.3d 17 (2d Cir. 1994).

[30] *See Arkansas-Louisiana Gas*, 453 U.S. at 578 ("Not only do the courts lack authority to impose a different rate than the one approved by the Commission, but the Commission itself has no power to alter a rate retroactively.").

[31] *Fax Telecommunicaciones Inc. v. AT&T*, 138 F.3d 479, 489 (2d Cir. 1998) (quoting *Sun City Taxpayers' Ass'n v. Citizens Utils. Co.*, 45 F.3d 58, 62 (2d Cir. 1995)).

[32] *Maislin Indus., U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 128 (1990); *see also Fax Telecommunicaciones Inc.*, 138 F.3d at 489 (filed tariff doctrine seeks to "prevent[] carriers from engaging in price discrimination between ratepayers").

[33] *See Central Office*, 524 U.S. at 222-23 ("Thus, even if a carrier intentionally misrepresents its rate and a customer relies on that misrepresentation, the carrier cannot be held to the promised rate if it conflicts with the published tariff.").

rates shall govern, the doctrine ensures that carriers cannot discriminate against a particular customer.[34]

b. Common carrier line extension efficiency doctrine. Extending a common carrier's network into new territory through a merger where it can serve additional customers advances the classic efficiency based on network effects. Every new subscriber connected to the expanded network increases the value of the service to existing subscribers. Recognizing this efficiency, many laws seek to promote the extension of common carrier networks, from direct financial subsidies[35] to regulatory (non-antitrust) requirements that different carriers interconnect with one another to knit their separate networks into a unified whole.[36]

Antitrust historically has promoted common carrier network extensions that arise from mergers. Paragraph 4 of § 7 of the Clayton Act, 15 U.S.C. § 18, provides a particularly lenient standard for review of such mergers:

> Nor shall anything herein … prevent such common carrier from extending any of its lines through the medium of the acquisition of stock or otherwise of any other common carrier where there is no substantial competition between the company extending its lines and the company whose stock, property, or an interest therein is so acquired.

The Seventh Circuit held that this common carrier merger provision requires a comparison of the competition-reducing overlaps against the rest of the transaction, disregarding insubstantial overlaps between the carriers:

> The proviso was intended to prevent full scale application of § 7 to such mergers. Congress must have contemplated a public benefit from line extensions, through gains in efficiency or the like, sufficient to outweigh the destruction of minor instances of competition between the carriers.

[34] *See Fax Telecommunicaciones Inc.*, 138 F.3d at 489.

[35] *E.g.*, 47 U.S.C. § 254 (prescribing a mechanism for funding universal service).

[36] *E.g.*, 47 U.S.C. § 251(a)(1) (carriers' duty of interconnection).

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> To give effect to this exemption, § 7 as a whole must be applied to carriers in this way: a first carrier serving geographic markets so much distinct from those served by a second carrier that it can be said there is no substantial competition between them can acquire the second carrier even though the resulting common control can substantially lessen competition in some specific markets where both are doing business. Such an acquisition, of course, would violate paragraph one of § 7 but for the protection of the common carrier exemption.[37]

The Seventh Circuit subsequently held that the common carrier line extension efficiency doctrine applies to telecom mergers. After the Department of Justice cleared the Bell Atlantic/NYNEX and SBC/Ameritech mergers, Judge Easterbrook affirmed dismissal of a private challenge to the SBC/Ameritech merger based on paragraph 4.[38] The original text of this paragraph in the House version of the Clayton Act was limited to railroads. Rep. Vaughan wanted to expand the provision to local telephone companies and proposed an amendment to the House bill to permit the "selling [of] local exchanges to competitors for local business."[39] Rep. Vaughan's amendment was not adopted, but when the Clayton Act went to the Senate the following month, the Senate Committee expanded the

[37] *Navajo Terminals, Inc. v. United States*, 620 F.2d 594, 601 (7th Cir. 1980) (upholding a finding of substantial lessening of competition in four city-pair geographic markets but permitting the merger to go forward because "it is equally clear that each [carrier] serves a large territory not served by the other").

[38] *South Austin Coalition Community Council v. SBC Communications Inc.*, 274 F.3d 1168, 1172 (7th Cir. 2001).

[39] House Debate, 63d Cong., 2d Sess., 51 Cong. Rec. 9538, 9597-9598 (June 1, 1914), reprinted in Kintner, 2 The Legislative History of the Federal Antitrust Laws and Related Statutes, Part 1, at 1633 (explaining: "I happen to live in a town where we have two systems, one exchange is located in Texas and the other in Arkansas, and I wish to make it certain that my people will not always be compelled to patronize and maintain two telephone systems.").

railroad provision to include telephone companies.[40] Experience continues to show that common carrier mergers produce substantial efficiencies.[41]

4. Presence of regulation counsels against novel expansions of antitrust.

The Court's opinion in *Trinko* explains that when there is no previously recognized antitrust duty, the presence of regulation is an important factor in concluding not to create a duty.[42] I won't repeat the Court's explanation but want to emphasize that the Court did not need to call for a trial to determine whether regulation is sufficiently effective to preclude a novel expansion of antitrust. The Supreme Court was able to determine that regulation under the 1996 Act is "an effective steward of the antitrust function" based on the face of the statute. Similarly, in *Town of Concord*, the First Circuit reversed a verdict and rejected a Section 2 claim of price squeeze, as a matter of law, because both the wholesale and retail levels of the product (electric power) were price regulated. Regulation, the court explained, "dramatically alters the calculus of antitrust harms and benefits" and "significantly diminishes the likelihood of major antitrust harm"; it also creates special potential for institutional interference, so that "the relevant antitrust considerations differ significantly, in degree and in kind."[43] That use of regulation in shaping antitrust standards required no trial of regulatory effectiveness; the First Circuit relied entirely on publicly available legal and economic materials.[44]

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[40] Sen. Rep. No. 698, 63d Cong., 2d Sess., at 48 (July 22, 1914), reprinted in Kintner, 2 The Legislative History of the Federal Antitrust Laws and Related Statutes, Part 1, at 1748. "The House provision ... is amended so as to apply to any common carrier, thus including telephone and pipe lines, the committee believing that all common carriers should be given the same rights in this respect and that the extension of the rights to telephone and pipe lines would inure to the benefit of the public." *Id*.

[41] *E.g*., DOJ Press Release, Justice Department Requires Divestitures in Verizon's Acquisition of MCI and SBC's Acquisition of AT&T (Oct. 27, 2005) (noting "exceptionally large merger-specific efficiencies"), available at http://www.usdoj.gov/atr/public/press_releases/2005/212407.htm.

[42] *Trinko*, 540 U.S. at 412-15; *see Kansas v. Utilicorp United, Inc.*, 497 U.S. 199, 211-12 (1990) (regulatory remedies are reason to reject new exception to indirect purchaser bar).

[43] 915 F.2d at 25, 28.

[44] The Supreme Court has found even the demanding immunity standard of strong incompatibility met without trial. *E.g.*, *United States v. National Ass'n of Securities Dealers*, 422 U.S. 694 (1975); *Gordon v. New York Stock Exchange*, 422 U.S. 659 (1975).

5. A network's refusal to interconnect is not an antitrust violation.

At a previous hearing before this Commission, Commissioner Carlton asked whether a dominant network that refuses to interconnect with a smaller rival network is committing an antitrust offense. The answer is "no." *Trinko* itself involved an alleged denial of "interconnection services."[45] Having an antitrust court set the price and terms for forced interconnection presents problems of deterring investment and the courts' inability reliably to set price and terms. And expanding antitrust into new territory is unnecessary because there is already a regulatory requirement that telecommunications carriers must interconnect.[46]

There is empirical evidence involving network-to-network interconnection in areas where the 1996 Act's regulatory duty to interconnect has not been applied that provides reason for optimism that interconnecting parties will tend to work out proper terms without intervention from antitrust courts. Diverse email networks, which started as separate closed systems unable to communicate with each other, developed common standards for exchanging messages and then interconnected so that their customers can send emails between networks. Diverse internet backbones interconnected through arrangements known as "peering" and "transit" so that the users connected directly or indirectly to one backbone can access websites on other backbones. Diverse wireless telephone systems interconnected through arrangements known as "roaming" so that a subscriber to one network can make calls when outside the area his or her network covers. In each instance, the interconnecting networks worked out for themselves problems of pricing, measuring the burden the networks place upon each other, capturing billing information, deterring fraud, and a host of other issues. Even a look at some of the failures of different networks to interconnect does not suggest that an antitrust court or jury applying general standards could reliably improve matters. For example, the FCC unsuccessfully sought to force AOL's Instant Messenger service to interconnect with other services.[47] Despite the lack of interconnection with

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[45] 540 U.S. at 407.

[46] 47 U.S.C. § 251(a)(1) (requiring "[e]ach telecommunications carrier" "to interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers").

[47] Mem. Opinion & Order, Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc., Transferors, to AOL Time Warner Inc., Transferee, CS Dkt No. 00-30, ¶¶ 128-200 (released Jan. 22, 2001) (imposing restrictions); Mem. Opinion

other instant messenger services, AOL's market power is abating while Google, MSN, and Yahoo services are gaining market share.[48]

6. Antitrust should not condemn dominant firms for pro-competitive behaviors.

I want to revisit and emphasize a final point. Regulation sometimes inhibits dominant firms from engaging in pro-competitive behaviors such as cutting prices, innovating, and investing. There is a popular view that antitrust, too, should specially scrutinize these behaviors by dominant firms because cutting prices, etc. can injure rivals.

That view is wrong. As a general rule, when non-dominant firms are observed commonly engaging in a particular form of conduct in the marketplace, such conduct should be presumptively permissible for a dominant firm also:

> If the practice is one employed widely in industries that resemble the monopolist's but are competitive, there should be a presumption that the monopolist is entitled to use it as well. For its widespread use implies that it has significant economizing properties, which implies in turn that to forbid the monopolist to use it will drive up his costs and so his optimum monopoly price.[49]

& Order, Petition of AOL Time Warner for Relief from the Condition Restricting Streaming Video AIHS, 29 Comm Reg (P & F) 1291 (released Aug. 20, 2003) (lifting restrictions).

[48] Mem. Opinion & Order, Petition of AOL Time Warner for Relief from the Condition Restricting Streaming Video AIHS, 29 Comm Reg (P & F) 1291, ¶ 6 (released Aug. 20, 2003) (noting AOL's IM market decline). After the FCC lifted its requirement that AOL interconnect its Instant Messenger service with others, AOL voluntarily interconnected with Reuters' service. *See* America Online and Reuters Link IM Networks, Information Week, Sept. 9, 2003.

[49] Richard A. Posner, Antitrust Law 253 (2d ed. 2001); *see* Richard A. Epstein, *Monopoly Dominance or Level Playing Field? The New Antitrust Paradox*, 72 U. Chi. L. Rev. 49, 60 (2005) ("[T]he appropriate assumption is that these practices offer some efficiencies that improve the gains from trade, even if a reviewing court cannot quite understand exactly why these practices survive or how they work."); David S. Evans & A. Jorge Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 81 (2005) ("[N]ondominant firms regularly engage in unilateral practices challenged under the antitrust laws. These include tying; vertical restraints such as exclusive contracts and exclusive territories; nonlinear pricing, including loyalty discounts; and aggressive price cutting. Practices that generate efficiencies where firms lack market power logically should generate those same efficiencies where firms possess market power. There is no economic reason to believe that these efficiencies become less important as firms acquire market power. We therefore presume these practices are procompetitive, even if practiced by firms with monopoly power, unless shown otherwise."); *Brooke Group Ltd. v. Brown*

Monopolists, of all firms, should be *encouraged* to lower prices, invest, and innovate because by definition full market pressure to do so is missing, and the monopolist has more customers who stand to benefit. Similarly, allowing a monopolist to become more efficient is a good thing to be encouraged. When a monopolist's costs go down, the self-interested monopolist will pass some of the cost savings on to consumers because its total profits go up when consumers buy the increased volume.

& Williamson Tobacco Corp., 509 U.S. 209, 223-26 (1993) (adopting predatory pricing test for measuring the legality of single-product discounts by dominant firms); U.S. Br. in *3M v. LePage's*, 10 n.6, 14 n.11 (U.S. filed May 2004) (*Brooke Group* "plainly" applies to dominant firm pricing).