

Complexity in Antitrust: The Accuracy-Simplicity Tradeoff

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Insights from Economics and Business Strategy

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Epiphany via anecdotes

- **Judge Diane Wood on specialized antitrust courts**
 - Against because if a federal judge can't understand antitrust, how can businesses?
- **Commissioner Sheridan Scott on the ABA Spring Meeting crowd**
 - If antitrust was understandable, would all of these lawyers and economic consultants be necessary?
- **Should antitrust expand its objectives, replace some with others, or shrink?**

Merger Guidelines questions

- 1982, 1984: A step toward clarity
 - Standardized and prominent market definition
 - Concentration criteria
- 1992, 1997 revisions
 - “Game theory guidelines”
 - “Lawyer and Consultant Full Employment Act”
- 2010 edition
 - The fall of “market definition”
 - We like economic efficiency (mostly on consumer side, but ...)
 - Here’s a laundry list of what we’ll listen to
 - And if it ain’t on here, we’re still listening

In what sense are these still “guidelines”?

- Carl Shapiro recently celebrated this multiplicity
- But apply it in other contexts: speed limits
- Could post a speed limit – a “guideline”
- Or, say that “the police will be maximizing consumer welfare, and will be taking all evidence one might offer, those on our list and those others can think of, before writing a ticket”
 - Econometric estimations, driving simulation models welcome
- Which tells drivers what to do? What provides the most useful “guidance”?
- Is the only constraint *Daubert*?
 - Whose academic literature counts?

What makes a guideline? Simplicity as a virtue

- **Accuracy has costs**
 - Marginal cost of reducing error goes up as error shrinks
 - Hard to go from a 95 to a 99
 - Tools needed to be more accurate less accessible
 - Increase in ambiguity of tools and results: How to check which set of arcane tools give the right answer?
- **Simplicity has benefits**
 - Business people have a greater chance of figuring out the rules
- **Avoiding litigation**
 - Litigation as Coasian failure
 - Litigation occurs when
Difference of optimistic opinion x Stakes > Litigation cost
 - Reduce ambiguity => reduce differences of opinion

Need simplicity imply lenience? Well, it *could* ...

- “Chicago” virtues, even if not accurate
- Some, I’ll confess, I’m inclined to adopt
- A “simple” high bar for predation: A price cut is OK unless there’s *no* circumstance under which that would be a response to competition
 - Permits any above cost pricing.
 - Acknowledge that above cost pricing can have predatory effects
 - But can anyone determine in advance when?
- The “first” of any purely vertical restraints
 - Exclusive dealing with the 2nd complement supply horizontal: more below
 - Non-exclusionary restraints, e.g., exclusive territories (although could be upstream exclusive dealing)

On the other hand: Merger options

- **Geoff Shepherd (2001):**
 - “The Guidelines should restore the tight focus on the merging firms’ market shares, just as all smart business leaders and observers do. That refocusing would make the Guidelines reliable, crystal-clear and useful. It would also reduce various economic losses that are caused by the vagueness and bloat of the current Guidelines.”
- **Malcolm Coate findings (2005)**
 - 3 to 2 or worse bad, 4 to 3 need “hot documents”
 - John Kwoka (2013) recently found less of a “line”
- **However, some merger aspects irremediably empirical**
 - Who competes with whom, and how much
 - The connection to this conference: How is competition seen?
 - Can this be simplified?

On the collusion side: *per se* rules

- Relatively clear lines regarding (horizontal) price-fixing, market allocation
- Worthwhile exception: Something like a “product disappears without” test
 - ASCAP, BMI
 - Some sports league, NCAA rules
- Strategic analysis weakens *per se* rules
 - The agency arguments in favor of RPM, exclusive territories are not inherently intrabrand
 - Show the consumer how *any* food processor works
- Implication: *Per se* rules appeal to simplicity over accuracy

On the monopolization side

- **Predation perhaps simple on the legality side**
 - *Brooke Group*
 - Interpretation: If pricing, output expansion, etc. *could* be a response to competition, it's OK
 - Covering incremental cost of response, and maybe not even that
 - Chilling effect dominates, even if one could get anticompetitive predation
- **The mishandling of exclusion cases**
 - To raise rivals' costs, need to raise price they pay
 - Suppressing horizontal competition in complement market
 - Most if not all exclusion cases involve competing complement providers – they win, not lose
 - Make simple: “As if” merger in complement market

Leave externalities out of competition policy

- Sometimes output reductions are a good thing, but does that excuse mergers, collusion?
 - Beer, if there's too much drinking and drunk driving?
 - Steel, if there's too much air pollution?
- An oldie but goldie: TV commercials
 - The NAB case in the 1980s
 - Broadcaster self-imposed limits on commercial time
 - Market failure: Absence then of a direct viewer-pay TV market
 - Undersupply of programming
 - Harmed by commercial interruptions
 - Audience has low propensity to respond to ads
 - Audience could out bid advertisers
 - But is best response collusion?

Since you asked: Leave out cognitive limitations

- A longer critique of behavioral econ., beyond antitrust
- It's not really economics, but psychology
- Undercuts all policy assessment
 - Benefits, costs measured assuming revealed willingness to pay equals actual willingness to pay
- Proponents justify technocratic usurping of democracy
 - Sunstein: BE rationalizes benefit-cost analysis because people don't make sensible voting decisions
 - Doesn't say how to do BCA when the data are inherently trustworthy
- Cooper, Kovacic: Aren't policy makers biased, too?

Antitrust policy and BE

- Incorporated in the empirical part
 - Market definition, diversion based on consumer behavior
 - If quarts of milk aren't close substitutes for pints in practice, even if they're perfect substitutes in theory ...
- Handle other places: Why we have a BCP
 - Again, not every problem is an antitrust problem
 - Canada "FBP" story: Distorting competition to favor bad guys
- BE vs. consumer choice: Worse off with more options?
- Aren't higher prices good for things consumers shouldn't buy? (Another reason to allow beer mergers?)
- If not efficiency, what's else? "Liberty" interest?
- Lesson: May be true, but adoption entails real costs

Speaking of psychology: An aside on intent

- Popular view—intent to harm rivals
- Leaving aside whether that's a bad thing in a generally competitive economy ...
- Why should antitrust be about mind reading?
- Shouldn't the goal be (at least up to now) consumer welfare?
- Should a restraint of trade, monopolization, or merger that tends to inhibit competition be excused because “they didn't mean to harm anyone”?
- Civil vs. criminal

Does simplicity imply economic pre-eminence?

- Richard Hofstadter, “What Happened to the Antitrust Movement?” 1964 [HT to Crane and Hovenkamp]:
 - “The [original Congressional] goals of antitrust were of three kinds. The first were economic; the classical model of competition confirmed the belief that the maximum of economic efficiency would be produced by competition The second class of goals was political; the antitrust principle was intended to block private accumulations of power and protect democratic government. The third was social and moral; the competitive process was believed to be a kind of disciplinary machinery for the development of character

Among the three, the economic goal was the most cluttered with uncertainties, so much that it seems to be *no exaggeration to regard antitrust as being essentially a political rather than an economic enterprise.*” [emphasis added]

The “competitive process”?

- Justice Black in *Northern Pacific Railway Co. v. U.S.* (1958)
[HT to Greg Werden]:
 - The Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade. It rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices,, the highest quality and the greatest material progress, while at the same time providing an environment conducive [sic] to the preservation of our democratic political and social institutions. *But even were that premise open to question, the policy unequivocally laid down by the Act is competition.* [emphasis added]
- William Letwin: pre-Sherman Act common law on the right to ply one’s trade

Management theory: Is the First Theorem wrong?

- Bringing us to the theme of the conference
- The First Theorem of Antitrust: “If a competitor complains about X, X must be good”
 - Calling low prices “predatory”
 - Merger-created efficiencies
 - [Aside: Consistent with complement market monopolization view of exclusion]
- But are there management strategy considerations economics misses?
- Competitor self-interest consistent with a good, simple way to tell if a practice should be illegal?
 - Political clout as zero-sum game?

My (not necessarily your) bottom line

- No matter what, simplicity deserves more respect
- Prefer economics-based static efficiency
 - Not axiomatic, ideological (I hope), legislative history
 - But because static efficiency has no other policy instrument
 - Rationality failure, externality, innovation, macro: Elsewhere
- Principles
 - Sec 1: Keep *per se* rules for horizontal agreements
 - Sec 2: High bar for predation, vertical restraints; exclusion lower
 - Sec 7: Empirics important, but perhaps simpler numerical rules
 - Allow first vertical merger, subsequent view as horizontal
- But should a limiting principle come business, politics?
- I'm staying tuned!

A final word:

“The explanation requiring the fewest assumptions is most likely to be correct.”

William of Ockham