

Government Oversight

The Policies And Politics Of Antitrust

Challenges have not always hit the mark, but courts are taking a step in the right direction.

BY C. EVAN STEWART

ALMOST 30 years ago Robert Bork, in his seminal book "The Antitrust Paradox: A Policy at War With Itself," wrote that: "modern antitrust law has so decayed that the policy is no longer intellectually respectable. Some of it is no longer respectable as law; more of it is not respectable as economics;... a great deal of antitrust is not even respectable as politics." Fast forward from 1978 to 2007 and do we find all has become "respectable"? No and yes.

Big Brother I: Microsoft

In the 1990s, the Justice Department brought on civil litigation to break up Microsoft. That litigation (which concerned the company's desktop software portal to the internet—was it a "feature" (Microsoft's position) or was it a "product" (the anti-Microsoft position)) was significant for at least four reasons: (1) the Clinton administration was highly influenced in its enforcement efforts by the views of competitors (to the exclusion of evidence of harm to consumers); (2) the government's litigation was fueled in large measure by the active prompting by various state attorney generals; (3) the fervor of the disparate antitrust enforcers was energized by Microsoft's (and its lawyers') ham-handed mixture of arrogance/contempt (i.e., the government was clueless as to technology issues, the government had no business sticking its big nose into the affairs of the "new" economy's leader, etc.), and ineptitude (i.e., the company had traditionally disdained political influence and was adverse to employing lobbyists, the company's witnesses evidenced defensiveness (or worse) about its documented efforts to out-perform its competitors, etc.); and (4) Judge Bork, who was retained by Microsoft's principal competitor (Netscape), espoused a position 180 degrees different from that which he unambiguously advocated in "The Antitrust Paradox" ("Antitrust should not

interfere with any firm size created by internal growth.")¹

Ultimately, after a fairly messy litigation history in the District of Columbia (which included the U.S. Court of Appeals for the D.C. Circuit removing U.S. District Judge Thomas Penfield Jackson), the government's case was resolved by a fairly benign consent decree in 2002. And a new federal district judge (Colleen Kollar-Kotelly) was charged with overseeing Microsoft's prospective compliance with the 2002 decree.

Big Brother II: Microsoft

Today, a different competitor of Microsoft's—Google—has launched an antitrust challenge to Microsoft's business efforts in a different sphere. Google has lobbied both the federal government and the state attorney generals to put significant restrictions upon Microsoft's Windows Vista operating system which (according to Google) makes it difficult for consumers to use competitors' (read Google) desktop-search application; more specifically, Google's complaints center on software that allows computer users to scan the contents of their hard drives, e-mails, and other personal information (Vista, it is charged, is not interchangeable with similar software from Microsoft's competitors).

Taking a page from Judge Bork (as expressed in "The Antitrust Paradox"—as opposed to when he was an advocate for Netscape), the Justice Department did not cotton much to Google's complaint.² The state attorney generals, on the other hand, picked up the same cudgels they had a decade earlier (then on behalf of Microsoft's competitor Netscape) and indicated that they wanted to pursue antitrust remedies against Microsoft under the consent decree.³

Having learned from its painful experiences from the 1990s (and having become more savvy in the political ways of Washington), Microsoft chose not to play litigation hardball. Instead, the company agreed to make changes to the Vista system, allowing for Vista users to more readily use Microsoft's competitors' software to search through hard drive files. And while this step satisfied the Justice Department and (more importantly) a number of the state attorney generals, it did not satisfy Google and at least one state's attorney general⁴—they asked Judge Kollar-Kotelly to weigh in on Microsoft as being in violation of the consent decree (or at least to extend the duration of the life of the decree, so as to ensure ongoing judicial oversight). The judge—previously skeptical of certain of Microsoft's business practices—has (thus far) not taken the bait.

So what does all the foregoing tell us? Well, for one thing, antitrust enforcement by elected officials seems not a whole lot more principled in 2007 than it was in 1978 (or in the 1990s). Politics, rather than economics and consumer-based concerns, seem at least as front and center as ever. Perhaps that is inescapable. But in the high-tech/cyberspace

economy, we should evaluate politicians attempting to apply traditional antitrust concepts with a healthy degree of skepticism, given market fluidity, low (or non-existent) barriers to entry, and lightning changes in innovation.⁵

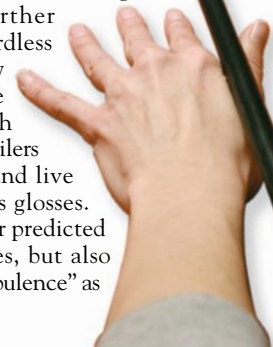
Supreme Court (Part I)

As opposed to government regulation, antitrust policy as recently decided on by the U.S. Supreme Court has shown much greater progress toward what Judge Bork would deem "respectability."

On June 27, 2007, the Supreme Court struck down an antitrust precedent dating from 1911: Justice Charles Evans Hughes' decision in the *Dr. Miles* case—that vertical price fixing (a/k/a resale price maintenance) is illegal per se. In *Leegin Creations Leather Products, Inc. v. PSKS, Inc.* (2007-1 CCH trade cases, ¶75,753), the Court (by a 5-4 decision) ruled that a "rule of reason" standard should be applied when manufacturers establish and enforce minimum prices for their products downstream in the marketplace (e.g., discount retailers); put another way, minimum price agreements may run afoul of the antitrust laws if they are determined to be anti-competitive, but such arrangements are not automatically illegal.

The five Supreme Court justices sided with Judge Bork's view that retail price maintenance does not restrain or restrict output, but rather "promote[s] effective distribution and marketing," which are "beneficial to consumers." And since the "sole consideration" of the antitrust laws should be "the maximization of consumer welfare" (according to Judge Bork), the majority of the justices voided years of tortured glosses on *Dr. Miles*, glosses which attempted to thread a needle between a "fixed" economic arrangement (historically, anything "fixed" had been deemed illegal) and the freedom of manufacturers to unilaterally price their products and deal with retailers as they saw fit.⁶

Justice Stephen G. Breyer (the Court's antitrust expert), for the dissent, contended that no compelling reason had recently come to the fore requiring the overruling of *Dr. Miles*. He further contended that, regardless of the doctrinal purity advocated by Judge Bork (and others),⁷ both manufacturers and retailers had come to accept and live with *Dr. Miles* and its glosses. As such, Justice Breyer predicted not only higher prices, but also "considerable legal turbulence" as



federal judges will now be prospectively determining the appropriateness of resale price maintenance agreements, agreements re-drafted in light of the majority's decision.

Will the dire consequences predicted by Justice Breyer come to pass? As to the issue of guaranteed higher prices, most economists would say no; but what will happen in the real world remains to be seen.⁸ Most (but not all) market participants doubt that there will be a huge gravitational shift in the balance of power to manufacturers (and their ability to increase prices with no push back). As to federal judges having trouble with prospective antitrust litigation, that seems doubtful.⁹ But even if we get different jurisprudential results in the near term, that is simply a regular feature of our current, balkanized judicial system. In any event, the heavily glossed law that developed because of *Dr. Miles* had led to many decades of federal judges struggling with conflicts involving vertical business arrangements. Perhaps now that that slate has been wiped clean, we (and the federal judiciary) can do better.

Supreme Court (Part II)

Among other key antitrust decisions rendered by the Court in this past session was its June 17, 2007, decision in *Credit Suisse Securities (USA) LLC v. Billing*.¹⁰ The issue in *Billing* was the applicability of the doctrine of implied immunity—whether conduct impermissible under the antitrust laws may be non-actionable if conflicting regulatory prerogatives of the Securities and Exchange Commission have been (are or could be) put at issue.

The specific matter was teed up by charges that the initial public offering (IPO) process and its aftermarket had been illegally manipulated to the detriment of investors who had purchased securities brought to the capital markets between 1997 and 2000. More than 1,000 securities class actions charging illegal/fraudulent manipulation(s) in the IPO process were brought under the federal securities laws; those cases were consolidated in the Southern District of New York before Judge Shira Scheindlin.¹¹

Based upon exactly the same conduct, nine consolidated antitrust actions were brought on against various securities underwriters; these were also initiated in the Southern District of New York, and were before Judge William Pauley. One of Judge Pauley's initial steps was to determine whether these antitrust claims could go forward independent of the separately filed securities claims (i.e., whether the doctrine of implied immunity was applicable). The SEC weighed in on that subject, arguing to Judge Pauley that implied immunity was clearly applicable in light of the SEC's (and NASD's) regulation of the underwriting process. The Justice Department did, as well, arguing the opposite to Judge Pauley.¹²

Defendants moved to dismiss the antitrust actions, and Judge Pauley granted the motion. Based upon the record before him, Judge Pauley was persuaded that:

- the SEC expressly regulates the underwriting syndicate process;
- the SEC expressly regulates the "road show" process;
- the SEC expressly allows for underwriter communications (through the rules of the various self-regulatory organizations (SROs)—e.g., the NASD); and

• the SEC, both previously and contemporaneously, had considered (and was considering) rules specifically addressing the alleged misconduct at issue.

In light of the foregoing, Judge Pauley held that implied immunity was called for because "the SEC, both directly and through its pervasive oversight of the NASD and other SROs, either expressly permits the conduct alleged or has the power to regulate the conduct[,] such that a failure to find implied immunity would 'conflict with an overall regulatory scheme that empowers the [SEC] to allow conduct that the antitrust laws would prohibit.'"¹³

Happily, I had predicted the result determined by Judge Pauley.¹⁴ Unhappily, the U.S. Court of Appeals for the Second Circuit took a different view on implied immunity and reversed Judge Pauley; and while I publicly criticized the Second Circuit's analysis and outcome, that is where matters stood until the Supreme Court granted certiorari to review the Second Circuit's decision.¹⁵

By 7-1, the Supreme Court reversed the Second Circuit and reinstated Judge Pauley's dismissal.¹⁶ Writing for the Court, Justice Breyer opined that allowing for civil liability under both the antitrust and securities laws would constitute an improper legal whipsaw, with "conflicting guidance, requirements, duties, privileges or standards of conduct...[that] would threaten serious harm to the efficient functioning of the securities markets."

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Applying prior Supreme Court precedent in this area (with which the Second Circuit had some difficulty), Justice Breyer's focus was on the issue of whether any conflict between the two legal schemes rose to the level of incompatibility. Not only did he find a high level of incompatibility, Justice Breyer (i) found pervasive regulation of the underwriting process by securities regulators, (ii) observed that drawing a line between permissible and impermissible activities in that process in antitrust cases would be extremely difficult and "could seriously alter underwriter conduct in undesirable ways," and (iii) noted that investors harmed by improper underwriter conduct were not without a remedy—they had the ability to seek full redress under the securities laws and did not need a second bite of the same apple under the antitrust laws.

Justice Breyer's analysis was right on and was fully consistent with the Court's prior precedent. By removing the liability whipsaw created by the Second Circuit, Justice Breyer's ruling will give a helpful predictive boost to securities industry actors who want to know where the liability lines are (and are not). Chalk *Billing* up as one for the good guys.

Conclusion

The foregoing shows conflicting trends: antitrust policy in the hands of the executive branch seems to be determined in large part based upon politics and personnel; antitrust policy in the hands of the judicial branch, on the other hand, seems to have moved

in the direction of antitrust theory, economics, and efficient regulatory oversight. This latter trend may not reflect heaven on earth, but it would seem to indicate a bit of progress in the right direction.

1. The record evidence before Judge Jackson showed: (i) no injury(ies) to consumers; (ii) no monopoly pricing by Microsoft (in fact, prices were dramatically dropping); (iii) significant product innovation; and (iv) no barriers to entry preventing Microsoft competitors from coming up with a product superior to Microsoft's. Thus, what Microsoft had achieved was a result of superior skill, experience, drive, etc.—all the things Judge Bork wrote should never be penalized under the antitrust laws.

2. In the words of the head of the Justice Department's Antitrust Division (Thomas Barnett), "The purpose of the consent decree was to prevent and prohibit Microsoft from certain exclusionary behavior that was anti-competitive in nature. It was not designed to pick who would win or determine who would have what market share." S. Labaton, "Microsoft Finds Legal Defender in Justice Department," *The New York Times*, A1 (June 10, 2007).

3. As stated by Richard Blumenthal (Connecticut's Attorney General), "In concept, if not directly word for word, it is the Microsoft-Netscape situation. The question is whether we're seeing déjà vu all over again." S. Labaton, "Microsoft Finds Legal Defender in Justice Department," *The New York Times*, A1 (June 10, 2007).

4. Connecticut Attorney General Richard Blumenthal.

5. See C. Stewart & P. Tozzi, "Antitrust Enforcement in the Millennium—Back to the Future," *BNA Mergers & Acquisitions Law Report*, Vol. 4, p. 222 (Feb. 26, 2001). Microsoft is not lily pure itself on this score, having lobbied the government to give close antitrust scrutiny to Google's acquisition of DoubleClick.

6. Compare *Dr. Miles Medical Co. v. John D. Park & Sons*, 220 US 373 (1911), with *United States v. Colgate*, 250 US 300 (1919), with *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 740 US 211 (1951), with *White Motor Co. v. United States*, 372 US 261 (1963), with *United States v. Arnold, Schwinn & Co.*, 388 US 365 (1967), with *GTE Sylwania, Inc.*, 433 US 36 (1977). As a prelude to *Leegin*, the Supreme Court 10 years ago struck down per se treatment for maximum retail price maintenance agreements. *State Oil Co. v. Khan*, 522 US 3 (1997).

7. The Justice Department and the Federal Trade Commission filed an amicus brief urging that *Dr. Miles* be overturned.

8. At oral argument Justice Breyer presumed that higher prices would automatically flow from the Court's decision. That recalls Justice William J. Brennan's observation in *White Motor* (concurring opinion) that resale price maintenance almost invariably reduces price competition; according to Judge Bork, that "observation runs counter to theory and experience." And as one former CEO from the fashion world has noted, moreover, the antitrust laws at the end of the day "have questionable efficacy because...supply and demand determines what price is." E. Clark & K. Ellis, "Retailer vs. Vendor: Supreme Court Mulls Power of Price Fixing," *WWD.com* (June 19, 2007) (comments of J. Aronson).

9. In point of fact, it is pretty unlikely that courts will find many resale price agreements violative of the antitrust laws under the rule of reason standard. Only where a manufacturer has dominant market power could one foresee this standard coming into play.

10. Another recent Supreme Court case of significant antitrust jurisprudence (but beyond the scope of this article) is *Bell Atlantic Corp. v. Twombly*, 2007-1 CCH Trade Cases ¶75,709 (merely alleging parallel conduct was held to be insufficient as a matter of pleading an antitrust conspiracy in order to survive a motion to dismiss under the Federal Rules of Civil Procedure).

11. See *In re Initial Public Offering Securities Litigation*, 241 FSupp2d 281 (S.D.N.Y. 2003).

12. Interestingly, federal regulators frequently have taken contrary (and often inconsistent) views on the issue of implied immunity.

13. 241 FSupp2d at 523 (quoting *In re Stock Exchange Options Trading Antitrust Litigation*, 317 FSupp 134, 149 (2d Cir. 2003)).

14. See C. Stewart, "Securities Regulations and the Antitrust Laws: Navigating the Law Enforcement Schemes," 35 *Sec. Reg. & L. Rep.* (BNA) 196 (Feb. 3, 2003).

15. 426 F3d 130 (2d Cir. 2005). See C. Stewart, "A Dangerous Intersection of the Securities and Antitrust Laws," 38 *Sec. Reg. & L. Rep.* (BNA) 1 (Jan. 9, 2006); C. Stewart, "'Carnacking' the Future," *New York Law Journal* (Feb. 15, 2007).

16. Justice Clarence Thomas dissented; Justice Anthony M. Kennedy declined to participate in the case.

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