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SUBCOMMITTEE ON ANTITRUST, COMMERCIAL, AND ADMINISTRATIVE LAW

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“Reviving Competition, Part 1:
Proposals to Address Gatekeeper Power and Lower Barriers to Entry Online”

STATEMENT OF
ABBOTT B. LIPSKY, JR.*

Adjunct Professor, Antonin Scalia Law School

* The views expressed herein are personal to the witness. Unless expressly stated to the contrary, they are not intended to represent the views of any other individual or entity, including without limitation the Global Antitrust Institute, Antonin Scalia Law School, or George Mason University.
Chairman Cicilline, Ranking Member Buck, and Members of the Subcommittee:

I am grateful for this opportunity to present my views to the Subcommittee as it begins to explore a number of potential legislative initiatives affecting federal antitrust law enforcement. The series of hearings conducted by the Subcommittee in the previous Congress led to the publication of several staff reports, including the Majority Staff Report and Recommendations ("MSRR"), which included ideas for a wide variety of possible legislative initiatives. This testimony will provide some reactions to certain of these ideas that you have chosen to focus on in today’s proceeding.

The MSRR claimed that the Subcommittee’s investigation established that a number of leading technology companies had obtained significant market power and control of access to important distribution channels in part by engaging in a variety of alleged anticompetitive acts. The MSRR also asserted that the federal antitrust enforcement agencies had failed to prevent such alleged conduct, and that the federal courts had interpreted federal antitrust statutes in ways that are claimed to prevent effective legal challenges to that alleged anticompetitive conduct. At the Subcommittee’s request, Majority Staff identified a number of proposals for legislation that might allow Congress to address these perceived shortcomings in the performance of the federal antitrust agencies and to amend antitrust law in response to certain judicial interpretations of antitrust law identified in the MSRR. These proposals cover a diverse range of ideas and suggestions, from the simple step of enhancing federal antitrust enforcement agency budgets to the more far-reaching possibility of overruling numerous Supreme Court precedents based on more than a century of common-law evolution of antitrust doctrine.

Before addressing some of the specific suggestions identified in the MSRR, I will outline some basic perspectives on the Subcommittee hearings conducted in the last Congress and the conclusions and recommendations contained in the MSRR. First, the MSRR contains some firm conclusions regarding the technology companies’ conduct and their market positions. The MSRR also questions many Supreme Court and other judicial precedents that represent landmarks in the long succession of cases that have gradually refined the interpretation of the antitrust laws as applied to a wide variety of competitive conduct. Looked at from a broad historical perspective, however, there are evident reasons to be skeptical about any claims that the antitrust laws, the antitrust enforcement process, or the common-law development of antitrust doctrine have reached a point of systemic failure, or that they
are in need of fundamental reassessment and redirection. Although it is often useful to conduct a critical review of such an important area as antitrust – which is at its root an exercise of Congress’ constitutionally delegated authority to regulate interstate and foreign commerce – before major changes are proposed or implemented, it is best to be confident of the grounds for such changes and to carefully evaluate both intended and unintended consequences.

First and foremost, the United States has been the world’s leading economic power for decades, and remains the clear leader in innovation not only within the digital technology sector but in most other leading-edge industries. In seeking to identify and remedy serious problems, one does not usually focus on the habits of star performers as a basis for concern. This is not to claim that the U.S. faces no serious economic and technological challenges nor that our private free-market competitive economy cannot be improved by making concrete and practical adjustments in our legal rules and institutions, nor would it immunize or excuse specific instances of anticompetitive conduct that otherwise warrant condemnation under antitrust law. At the same time, however, there is no evident basis for sending signals of alarm or crisis, suggesting that extraordinary, controversial or hastily designed fixes are required. If there is room for improvement of the legal environment in which our private-enterprise competitive economy functions, careful research, due deliberation and a searching analysis of potential consequences are in order.

As the MSRR acknowledges, although the leading technology companies scrutinized during the hearings held in the last Congress are among the largest, most profitable and successful private firms in history, they “once were scrappy, underdog startups that challenged the status quo . . . .” MSRR at 6. Indeed, these firms were scrappy, underdog startups relatively recently. Google was founded in 1998 by a pair of Stanford grad students offering a superior internet search engine that they had devised. Facebook was founded in 2004 by a few college students who perceived a need for an online school directory and undertook to provide it. Amazon was founded in 1994 by a single entrepreneur working out of his garage, financed by his parents, to pioneer the business of online book sales. Apple was another garage-based effort founded in 1976 by a few PC enthusiasts, but it teetered on the edge of failure as recently as 1997. After rehiring one of its exiled founders, Steve Jobs, Apple produced an extraordinary series of innovative products and services – including the iMac, iTunes, iPhone, iPad, iBook and the App Store – to become the largest private enterprise in history (over $2 trillion in market capitalization at this writing).
Although the visible success of these companies invites comparison to the industrial giants that emerged during the Second Industrial Revolution – Standard Oil and others – there are key differences in their legal environments and their industrial origins. The firms that drew the greatest concern in the late 19th and early 20th centuries were not only manifestations of rapid growth made possible by dramatic improvements in technology, but were also shaped to a profound degree by efforts to form trusts, cartels and other anticompetitive collaborations that we now recognize as competitively harmful, and which are now severely condemned under antitrust provisions, including a wide range of powerful criminal-law enforcement tools that are still aggressively enforced. Standard Oil, for example, may have been an innovator in the emerging petroleum industry, but the public alarm that led to passage of the Sherman Act as well as the antitrust case that led to the breakup of Standard Oil in 1911 was fueled by the brazen scheme of its founder and leader, John D. Rockefeller, to obtain decisive advantages over his competitors by obtaining exclusive transportation concessions from the railroads in return for critical assistance by Standard Oil in stabilizing the railroad’s own pernicious cartel. Elizabeth Granitz and Benjamin Klein, Monopolization by 'Raising Rivals' Costs': The Standard Oil Case, 39 J.L. & Econ. 1 (1996).

There can be no question that the companies now under scrutiny “... have delivered clear benefits to society...”, as the MSRR acknowledges. MSRR at 6. Unlike the situation prior to 1890, firms operating now and throughout the digital age are and have been constantly exposed to powerful antitrust constraints. Thus, rapid and widespread consumer and user acceptance of new products and services – internet search, social media, internet-connected devices and applications, and e-commerce – have been the leading drivers of success for these new technology firms. The main propellant of the competitive success of today’s major technology firms has not been cartelization. It can be misleading, therefore, to draw a straight line from the most successful technology firms of today to those of the Second Industrial Revolution over a century ago, and conclude that audacious new legal approaches are required to ensure that such firms operate within effective legal constraints.

It is prudent also to recognize that the beneficial results of economic growth and innovation we are witnessing today confirm the wisdom of key decisions made by the 51st Congress in implementing

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1 Quantitative estimates of these benefits are provided in Avinash Collis, Consumer Welfare in the Digital Economy, in THE GAI REPORT ON THE DIGITAL ECONOMY (2020).
the world’s first functional antitrust enforcement system by passing the Sherman Act, and by subsequent Congresses in trusting the courts to formulate and implement specific rules to construe and apply the fundamental antitrust prohibitions on anticompetitive conduct in the myriad of specific cases and diverse circumstances encountered in antitrust litigation. Rather than attempt to anticipate the limitless range of competitive market circumstances and business practices that might be challenged in the future, the substantive provisions of the Sherman Act were stated generally but targeted on the key concept of anticompetitive conduct – anticompetitive agreements and monopolization. This focus on condemning anticompetitive conduct was maintained in subsequent antitrust legislation that governs mergers, acquisitions and other structural transactions, including the 1914 Clayton Act and the 1950 Cellar-Kefauver amendments that significantly strengthened the Clayton Act. That being so, Congress wisely left to the federal courts the task of determining precisely which forms of conduct would be deemed anticompetitive. With the common-law tradition of case-by-case analysis and the federal judiciary’s strong safeguards for rights of defense and the independence and impartiality of judges and Justices, the federal judiciary was well situated to implement the broad ambitions embodied in the antitrust laws in a balanced and effective manner.

As the law evolved, the wisdom of these substantive and institutional choices has been fully demonstrated by the emergence of American economic and innovation leadership. In the early years of Sherman Act interpretation, the Supreme Court fashioned the rule of reason as the main approach to determine the legality of business conduct. As Justice Louis Brandeis stated in what is still considered to be the classic formulation of the rule of reason:

The true test of legality is whether the restraint imposed is such as merely regulates, and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition. To determine that question, the court must ordinarily consider the facts peculiar to the business to which the restraint is applied, its condition before and after the restraint was imposed, the nature of the restraint, and its effect, actual or probable. . . .

Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918). The only exceptions to this approach involved application of a per se rule – a rule of automatic illegality – to classic cartel restraints and to vertical price fixing (the latter having since been overruled). This basic configuration remained more-or-less intact until the 1940’s. Departures from this basic approach arose in the New Deal years, as FDR sought to rescue the U.S. economy from the Great Depression. Among FDR’s leading policy initiatives was the National Industrial Recovery Act, signed into law at the very end of FDR’s legendary first 100
days in office in 1933. The NIRA was the antithesis of competition subject to antitrust law – it suspended antitrust law so that industry-wide “fair competition codes” could be enacted across many sectors of the economy. These codes, which were actually industry cartels, had a further restrictive effect on trade and employment, and in any event the NIRA’s key provisions were declared unconstitutional by the Supreme Court in Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935). Forced to change his approach, FDR was eventually convinced by Robert Jackson and other advisers to reinvigorate antitrust enforcement, rather than to abandon the root concept of private free-enterprise competition as the main organizing principle for productive activity in America.

Beginning from the time that Jackson served as FDR’s Assistant Attorney General for Antitrust, and continuing until the early 1970’s, the federal courts – at the urging of the federal antitrust agencies – discarded the rule of reason with regard to a widening range of competitive practices, and declared most forms of competitive conduct to be illegal per se. Horizontal restraints, vertical restraints and intellectual property licensing practices were all decreed to be illegal regardless of any proffered defense. Although never designated per se illegal as such, the Court’s adoption of heavy structural presumptions against mergers and other structural transactions, and application of such presumptions to competitively inconsequential mergers, were the functional equivalent of a per se rule against such transactions. This was the meaning of Justice Potter Stewart’s sardonic dissent in United States v. Von’s Grocery Co., 384 U.S. 270, 301 (1966), that “the Government always wins” merger cases.

Similarly, firms with monopoly power were presumed guilty of monopolization unless they could meet the burden of proving that their superior market position had been “thrust upon” them, even if their conduct had been otherwise lawful and “honestly industrial.” This placed major constraints on innovative firms and steered U.S. antitrust enforcement into a policy realm where superior productivity and innovation were being punished rather than encouraged. Judge Learned Hand warned in United States v. Aluminum Co. of America, 148 F.2d 416, 430 (2d Cir. 1945), “The successful competitor, having been urged to compete, must not be turned upon when he wins.” But Judge Hand acted in apparent disregard of this warning, ordering that Alcoa be broken up primarily because it consistently expanded capacity to ensure that it could meet rising demand. A similar fate awaited the most innovative shoe machinery firm in the world when, after more than two decades of antitrust proceedings, the Supreme Court ordered its dissolution. United States v. United Shoe Machinery Corp., 391 U.S. 244 (1968). This per se/structuralist trend reached its high-water mark when the Supreme Court openly mocked the idea
of using economic analysis to analyze territorial restraints ancillary to a procompetitive joint venture. United States v. Topco Assocs., Inc., 405 U.S. 596, 609-10 n.10 (1972).

Fortunately, however, the common-law process eventually led the Supreme Court to end the series of repeated extensions of the per se rule, its adherence to rigid structural formulas and its categorical rejection of economic analysis outside the cartel domain. Due in part to the decades-long trend of agency and judicial hostility to fact-based antitrust defenses and economic analysis, severe economic headwinds pushed the United States into an extended period of stagflation in the 1970’s. Unemployment, interest rates and inflation reached record levels by the time of the Carter-Reagan transition. Fortunately, a number of federal policies – including among many others competition-limiting sectoral regulation of basic industries (transportation, energy, communications) and limits on intellectual property protection – were reexamined and reformed in light of the nation’s worsening economic performance. The Supreme Court began to accept economic arguments in non-cartel cases, notably in United States v. General Dynamics Corp., 415 U.S. 486 (1974), and Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977). Critically, in Sylvania the Court observed that antitrust rules should be based on “demonstrable economic effect” rather than “formalistic line drawing”. Id. at 59.

Since Sylvania the Supreme Court – supported by a broad consensus among scholars of antitrust law and economics, as well as enforcement agency officials and other members of the antitrust community – has consistently focused on protecting the dynamic competitive process from anticompetitive conduct, rather than insulating competitors or other stakeholders from the consequences of competition on the merits. As the Court had stated in Northern Pacific R. Co. v. United States, 356 U.S. 1, 4-5 (1958),

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 . . ..

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2 This long-term economic slowdown was the product of a wide variety of policies in addition to the antitrust enforcement approach of that time.
This passage effectively describes what is now referred to as the “consumer welfare” standard. Its broad reference to the key benefits of competition demonstrates that current antitrust law does not focus narrowly on lowering consumer prices as an independent objective, as is often alleged nowadays. Indeed, the Court has condemned anticompetitive buyer conduct involving only producers as both buyers and sellers – even in cases where the conduct in question involved no direct impact on consumers. Mandeville Island Farms v. American Crystal Sugar, 334 U.S. 219 (1948) (condemning monopsony conduct among sugar-beet refiners directed against sugar-beet producers).

This is not the first time that Americans have heard proposals to apply the existing antitrust laws or extend them to limit or reduce perceived excessive concentrations of economic power. In the 1970’s, legislation was discussed that would have established principles of “no-fault monopolization”, allowing the break-up of firms without any demonstration that they had engaged in “culpable” conduct.\(^3\) Although such legislation did not make significant progress in Congress, at about the same time the federal antitrust agencies pursued a variety of efforts to “deconcentrate” specific economic sectors. Major litigation was initiated by the FTC to require vertical separation of the integrated petroleum companies, and to address perceived oligopolistic conduct in the breakfast cereal industry. In 1969 the Antitrust Division began major monopolization litigation in the general-purpose computer industry, challenging what it perceived as anticompetitive conduct by IBM Corp., and in 1974 the Division initiated monopolization litigation against the former Bell System. Many of the themes found in the Subcommittee’s MSRR were also present in these earlier government challenges to some of the leading technology firms of that earlier time. The 1969 Complaint filed against IBM Corp. attempted to paint a sinister picture of the threat posed by IBM’s strong position in the emerging computer industry, describing how IBM had sold thousands of computers and obtained revenues in the hundreds of millions of dollars. Of course, these figures seem absurdly small by the standards of the present-day technology sector.

Most of these deconcentration efforts ended badly. The FTC proceedings against the integrated petroleum companies and the breakfast cereal producers were eventually terminated. The Antitrust

Division dismissed its monopolization case against IBM without prejudice in 1982, the industry having shifted so dramatically since the filing of the complaint (thirteen years earlier) that it was highly unlikely that any further proceedings were needed to protect the public interest in maintaining vigorous competition in the computer sector. William E. Kovacic, Failed Expectations: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration, 74 Iowa L. Rev. 1105 (1989).

By contrast, the case begun in 1974 against the former Bell System terminated in a consent decree implementing the largest divestiture in history. Although the path to resolution of the case (from the filing of the complaint in 1974 to the entry of the decree in 1982, terminating in the 1996 legislation that finally resolved many of the major competitive issues affecting the industry) was littered with a variety of difficult legal and practical complexities and obstacles, in hindsight the overall venture must be judged a resounding success of antitrust enforcement – arguably its greatest success since the Standard Oil case. The U.S. telecommunications sector was transformed from a regulated nationwide monopoly that innovated slowly and usually only with aggressive prodding, and at the end of the legal and legislative saga (following the 1996 legislation) the nation was being served by an enormous variety of new and vastly superior technologies supplied not only by the corporate successors to the former Bell System but by numerous successful new players in mobile, internet and other sectors of the industry. Once the sector was opened to the possibility of innovations independent of regulatory approval, huge advances such as cellular and other forms of mobile and wireless communication, fiber optics and packet switching assured that the public would benefit from aggressive competition. Other forces – including for example the astounding progress achieved in the design and production of semiconductors – made major contributions to these developments, but it seems unlikely that the beneficial changes in the information technology industry that occurred in the last forty years would have been as profound or as rapid without the Antitrust Division’s successful pursuit of the Bell System divestiture.

The lesson of this history is not that the antitrust laws are ineffective or weakly enforced, which would have made the Bell System divestiture impossible – but that the appropriate outcome of specific cases depends on the nature of the industry and the other particular facts and circumstances applicable to each case – the factors that were itemized in Justice Brandeis’ description of the rule of reason in Chicago Board of Trade. The IBM case was properly dismissed, but the case against the Bell System was properly litigated to a conclusion involving profound realignment of an entire industry. The existing institutional structure of our antitrust enforcement system is purpose-built to ensure that cases are
properly evaluated and that they reach the conclusions warranted by the law and the specific facts in evidence. The U.S. is uniquely fortunate to have a federal judicial system whose Article III judges are protected by a wide variety of constitutional and other safeguards, so that they can provide independent and objective assessments of cases and balanced and judicious development of legal doctrine. The elaborate system of federal rules regarding evidence, procedure, appeal and review, as well as rules of judicial and attorney conduct, are all focused on assuring that the federal courts render decisions that are objective and impartial. The system is not perfect, and it may occasionally fail, but the practice of requiring antitrust complaints – with potentially enormous remedial consequences for the accused – to be assessed through this rigorously structured system involving presentation of evidence and argument to a neutral and independent decision maker is the best system yet devised for this purpose. The spectacular success of the American economy and specifically the continuing American leadership in innovation is a testament to the wisdom of the choices made by the 51st Congress and subsequent Congresses (as well as to the constitutional design of our federal judiciary).

For these and other reasons, the case for major change in these rules and institutions is not well-supported by the evidence now of record. The legislative approach to examination of the competitive and antitrust issues posed by the history and conduct of specific firms within particular economic sectors, while based on Congress’ constitutional authority, is bound to be less effective than litigation of specific cases subject to the numerous safeguards characteristic of litigation before Article III courts. A broad-brush approach to the diverse firms and industries considered by the Subcommittee in the previous Congress is a less refined tool than case-by-case examination within the usual context of federal agency investigation, case development and litigation, to say nothing of the “private attorneys general” or “parens patriae” litigation that may be brought before the federal judiciary. Indeed, there is ongoing antitrust litigation of every type involving each of these companies, based on the same concerns that motivated the Subcommittee’s hearings in the previous Congress. Congressional intervention at this point seems to suggest mistrust of the federal judicial process, and therefore should be regarded as both unwarranted or at least premature.

Let me conclude with some observations intended to address some of the specific proposals included in the MSRR’s recommendations section. As you may now infer from my testimony, I would oppose any legislative effort to implement an across-the-board requirement for structural separation or imposition of line-of-business restrictions for the technology companies examined in the MSRR. These
are extraordinary remedies and they have the clear potential to impose enormous costs on the sectors involved, to needlessly confine the development and evolution of leading technology firms in arbitrary and uneconomic ways and ultimately to deprive users and consumers of the benefits of innovation and competition. Our existing enforcement institutions are fully capable of ferreting out any anticompetitive conduct and implementing appropriate and feasible remedies within the existing framework provided by the federal judicial system. Without a full airing of the basic issues before neutral and objective decisionmakers – specifically, Article III judges – there is no way to obtain adequate assurances that the relevant facts and arguments have been fairly and thoroughly aired and resolved.

That having been said, the suggestions contained in the MSRR for addressing certain aspects of the technology sector that may be inhibiting entry should not be dismissed on the basis of the considerations discussed above. The possibility of taking action to promote interoperability of different systems or reducing the friction and cost inherent in user and consumer interbrand switching by establishing “portability” protocols, merits further thought. At first encounter these proposals sound somewhat similar to the notion of standard setting, which has long been recognized as beneficial when carried out by private entities that are structured and guided by careful antitrust analysis. Indeed, Congress has enacted legislation recognizing the beneficial character of standard setting, and has provided specific antitrust protections for the collective conduct of standards-development organizations that meet specified criteria.4

The world-leading performance of the U.S. economy and the clear achievements of its dynamic technology sector are sound testaments to the wisdom of the fundamental principles of the antitrust statutes, the leading Supreme Court precedents and the common-law process that unfolds within our carefully structured federal judicial system. This of course would not excuse illegal conduct within our technology sector if such has occurred, but for the time being Congress should continue to repose trust that the existing principles and institutions that constitute our present antitrust-law enforcement system stand the best chance to resolve specific cases appropriately. While some of the ideas contained

in the MSRR may deserve further exploration, wholesale changes in the essential guideposts of antitrust-law interpretation are not warranted based on the existing record.