Paper Trail: Working Papers and Recent Scholarship

Editor's Note: *John Woodbury reviews two papers addressing the role of consent decrees in particular in resolving anticompetitive concerns.*

Send suggestions for papers to review, or comments, to page@law.ufl.edu or jwoodbury@crai.com.

—William H. Page and John R. Woodbury

Recent Papers

Steven C. Salop, **Modifying Merger Consent Decrees to Improve Merger Enforcement Policy**, Antitrust, Fall 2016, at 15

In this paper, Steven Salop, Professor of Economics and Law, Georgetown University Law Center, and Senior Consultant, Charles River Associates (with which I am affiliated), considers modifications to the merger remedy process (including consent decrees and merger challenges). As is well known, consent decrees in particular provide the antitrust agencies with flexibility in addressing mergers that might otherwise be challenged on the grounds that such mergers would harm consumers and could require extended litigation during which the harm may continue. Joshua Wright and Douglas Ginsburg note that the antitrust agencies "have increasingly moved from actively litigating antitrust cases to settling cases through consent decrees."[1]

But Salop observes that some decrees are robbed of their remedial value, notably (in the extreme) when the consent-mandated divested entities become bankrupt, as happened with the Advantage divestiture in the Hertz/Dollar Thrifty transaction (p. 16). As a result, consumers may well face higher prices with the unexpected reduction in competition. For example, Salop points to the evidence in John Kwoka's recent tome on retrospective merger studies,[2] which (among other things) concluded that mergers allowed to proceed with divestitures have been associated with significant price increases of 6.1 percent on average and a substantial 12.8 percent with conduct remedies.[3] (p. 16)

On balance, Salop argues that consumers likely are harmed within the universe of challenged mergers (which would include those resolved by consent decrees) *if* the agency's expectations are correct.[4] If the agencies succeed in winning an injunction against a perceived anticompetitive

1 Joshua D. Wright & Douglas H. Ginsburg, *The Costs and Benefits of Antitrust Consents* (George Mason University Law and Economics Research Paper Series No. 16-42 (posted Oct. 2016)), https://ssrn.com/abstract=2860174. I discuss this paper below.

2 John W. Kwoka, Jr., Merger Control and Remedies: A Retrospective Analysis of U.S. Policy (2015).

3 Citing the review of the Kwoka book by Robert A. Skitol, *A Harsh Report Card on the Merger Enforcement Process*, Antitrust Source (Feb. 2015), http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/feb15_skitol_review_2_11f.pdf.

4 This obviously is an important "if." If the increased reliance on consents leads to less economic analysis of anticompetitive concerns, one cost of increased reliance on consents could be a higher incidence of false positives. That the underlying economic analysis could be less than complete is a concern of Wright and Ginsburg, discussed below. Having said that, the Kwoka analyses might suggest that that increased incidence of false positives may not be substantial, given the post-merger price increases associated with mergers cleared via consent decrees.

merger, consumers are no better or worse off. If the courts deny the injunction, consumers are worse off. And, judging by the Kwoka study, allowing a merger to proceed via what is ex post an ineffective consent decree will also often harm consumers.

To cure what may be an ineffective remedy ex post, Salop proposes that the agencies should be willing to modify that remedy when its failure becomes evident as well as to revisit a consummated merger where necessary. In particular, he suggests that at least three distinct benefits can flow from a policy of revisiting failed consents. First, the policy will restore much of the competition lost as a result of the ineffective consent. This policy would allow the agencies to revisit consents that appeared effective at the time of the adoption of the consent but subsequently failed to satisfy the agency's expectations. Second, the prospect of a second review will create incentives for the merging parties to develop and propose an economically sound and viable consent to avoid any subsequent review as well as to discourage exaggerated efficiency claims.

Third, even if the consent is seemingly ineffective or the merger is erroneously cleared without remedial conditions (a false negative), the merged firm may nonetheless refrain from raising prices or otherwise harming competition to avoid another agency review. The possibility of ex post reviews "in principle . . . might permit the agencies to demand smaller divestitures or other relief in certain cases, knowing that there can be further adjustments later, if needed [or] allow the agencies to forgo challenging some very 'close-call' mergers that otherwise would be challenged." (p. 16) Nonetheless, Salop urges caution in concluding that in "close-call(s)," the agencies should forgo litigation "only in the most limited circumstances. . . . Post-consummation reviews may be imperfect and remedial choices will be more limited." (pp. 16–17)

Salop proceeds to outline a framework for the implementation of the consent review, and that framework includes the following (among others):

- Language in the consent that specifically provides for such a post-merger review.
- A non-exclusive list of the types of events that could trigger such a review.
- A requirement that the merging parties (and other competing firms) provide ordinary course of business documents to allow the agencies to track prices, margins, shares, and quantities on an annual basis.
- A sunset provision for the ex post review, possibly one that occurs within, e.g., 3 to 4 years after court approval of the decree or the clearance of the merger.[5]

Salop acknowledges that in considering ex post adjustments to remedy any consumer harm, "[i]t can be difficult to unscramble the eggs. However, analysis . . . suggests that there would be substantial benefits by restoring competition and increasing deterrence through alternative modifications." (p. 18)

Salop highlights other possible second-review remedies where divestitures are not practical, including (where appropriate) the licensing of intellectual property at zero or below market rates, reducing the length of customer contracts or allowing customers to renegotiate contracts (to reduce entry barriers), or requiring (where relevant) a set price differential between captive customers (who would experience the more substantial post-merger price increases) and others. If these remedies are not available, Salop suggests that the merged firm could be required to divest in other markets where the merged firm competes and has market power (but is unaffected by the merger), thereby tending to offset in part the market power resulting from an ineffective

[5] However, Salop notes that "[i]f there is evidence that the merged firm subsequently raised prices as a result of market power flowing from or enhanced by the merger, the period may be lengthened somewhat or there might be a second review." (p. 17)

initial consent decree. Alternatively, monetary penalties could be imposed that reflect the value of current and/or expected profits as a deterrent to the exercise of market power.

If none of these remedies are viewed as possible, practical, or effective, Salop proposes that as a "remedy of last resort" (p. 18), the court (or some other agency) monitor and regulate the prices of the merged firm if the merger creates durable market power. Salop notes that "[w]hile ongoing oversight of prices may create great discomfort for antitrust practitioners, commentators, and the regulated firms, paying monopoly prices creates great discomfort for consumers, who are entitled to protection by the antitrust laws." (p. 18)

Salop has no illusions that this would be a costless endeavor. He acknowledges that (among other costs) there may be false positives associated with the consent review. As one example, any observed post-merger price increases may be attributable to unrelated cost and demand factors rather than market power. Further, any price increases may reflect quality improvements. But he notes that comparing current with but-for (nominal or quality-adjusted) prices is within the expertise of the agencies. Given the fact that consumers currently bear the downside risk of challenged mergers, Salop notes that "[a]sking the merging firms to 'put their money where their mouth is' can both partially insure consumers against the downside risk and facilitate a more efficient merger enforcement process." (p. 19)

I share Salop's view that in principle, the merger enforcement process and consumers can benefit from an agency's willingness to review consent decrees that appear ineffective and thus cause consumer harm. Importantly, the modifications would create incentives for the merging parties to develop an effective remedy. But the devil ultimately is in the details. As Salop recognizes, a second bite at the apple by the agencies should occur infrequently. It would be useful if the circumstances under which such a review would be triggered—and the degree of certainty one would have that in modifying the decree, consumers would be better off—were carefully specified.[6] Otherwise, the risk that such modifications—particularly ones involving an ongoing review of pricing by the merged firm, divestitures in unrelated markets, or interfering in the firm's contractual relationships—may have adverse effects on the very competition that the modifications seek to enhance.

As Salop recognizes, many antitrust practitioners would be at least somewhat concerned with some of the suggestions in his proposal.[7] Such ex post remedies as the prospect of essentially regulating prices (using rate-of-return regulation, price caps, or even benchmark pricing) or requiring divestitures in unrelated markets, will surely give many antitrust practitioners pause, given, e.g., the extent to which price regulation has been associated with substantial market inefficiencies.

And there remains the practical question of costs to the agencies and firms of such a proposal. Salop argues that these increased costs would be limited because "not all mergers would be reviewed in detail and detection of remedial failure would necessarily be imperfect." (p. 19) In addition, as noted above, a concern that the agencies may take a second bite at the apple will

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[6] For example, suppose that the agency were to find that there was a statistically significant increase in the post-merger price, but that the increase was quantitatively small. Putting litigation costs aside, would that small increase trigger a process to modify the consent decree? Or would the trigger depend on the total overcharge to consumers being above some threshold level? Put differently, would there be safe harbors for mergers or practices that require a second look?

[7] In an earlier version of this paper, Salop notes that when presenting it at the 2016 ABA Antitrust Section's Spring Meeting, his proposal "was (I hope) jokingly characterized as a 'communist plot.'" Steven C. Salop, Modifying Merger Consent Decrees: An Economist Plot to Implement Merger Enforcement Policy 1 (Apr. 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2768143.

itself create incentives for the merging parties to fashion a consent decree that is realistic and effective. Still, if the scope of agency merger control broadens substantially, one would expect, as Salop notes, that additional agency resources would be required to better insure that the costs of any particular ex post intervention is worth the benefits. Regardless of whether one agrees with Salop, he has focused on an ex post issue worthy of consideration. For those looking for a thoughtful and provocative read, this paper is an ideal candidate.

Joshua D. Wright & Douglas H. Ginsburg, The Costs and Benefits of Antitrust Consents
(George Mason University Law and Economics Research Paper Series No. 16-42 (posted Oct. 2016),
https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2860174

In this paper, Joshua Wright and Douglas Ginsburg (WG) consider the costs and benefits of increased reliance on consent decrees rather than litigation to address perceived consumer harm from mergers or other anticompetitive practices.[8] At the outset, WG observe that in the U.S., "over the last three decades the Agencies have resolved nearly their entire civil enforcement docket by consent decree . . . ." (p. 1), which has resulted in what they call a "culture of consent." (p. 1) The goal of the paper is to "document the costs and benefits of a shift from a litigation-oriented regime to a regulatory regime." (p. 2)

While aknowledging that any antitrust policy would include some optimal mix of consent decrees and litigation to address anticompetitive harms, WG highlight what they regard as the significant costs in moving from litigation to consents. First, WG argue that increased reliance on consent decrees "results in less litigation of important issues that would stimulate the healthy development of antitrust jurisprudence." (p. 4) Among other effects, WG contend that the use of consent decrees diverts resources from gathering and evaluating evidence that a merger or a business practice is anticompetitive to designing and negotiating the consent.

WG argue that by contrast, litigation provides the opportunity for the agencies to reaffirm or develop new antitrust legal rules that "provide the parties with some degree of certainty about the boundaries of lawful business conduct . . . . As our understanding of economics evolves, repeated litigation allows courts to adapt to changes in our economic knowledge and empirical learning." (p. 5) WG contend that increased reliance on consent decrees, implemented as they are on a case-by-case basis, provide guidance on only what kind of conduct is unlawful rather than conduct that is lawful. Further, whatever guidance consent decrees provide is further reduced, according to WG, because the nature of the decrees can vary with the changing composition of the agencies.

A second cost from a shift towards consents is the failure of the agencies to involve economists in the process of consent design and implementation. WG argue that the collateral damage from increased reliance on consents relative to litigation is that the agencies will fail "to collect the data and evidence required for economic analysis if it assumes that cases will typically be resolved by a negotiated consent decree." (p. 7)

WG identify a third cost of increased consents as one that reduces "the cost to the agency of straying from its core antitrust mission." (p. 8) As one example of a "misuse of agency power"

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[8] Joshua Wright is University Professor, Antonin Scalia Law School, George Mason University, and Senior of Counsel, Wilson, Sonsini, Goodrich & Rosati. Douglas Ginsburg is Senior Judge, U.S. Court of Appeals for the District of Columbia Circuit, and Professor of Law, Antonin Scalia Law School, George Mason University.

(p. 9), WG cite the FTC's consent decree with Intel that (among other things) prevented Intel from making design changes that, in the FTC's view, generate few consumer benefits but could be used to fortify Intel's market power.[9] In another example cited by WG (n.17), the Nevada Attorney General conditioned its approval of a merger on the merged firm's dollar contributions to certain activities favored by the state, a condition exceeding the scope of what many would consider as appropriate antitrust policy.

Finally, WG point to a fourth cost of consents as how they affect the conduct of non-party firms: "Businesses make note of the consent decrees entered into by firms in their industry [but] generally have no way of knowing which facts or modes of economic analysis were influential in the settlement process." (p. 11) In other words, the consent decrees are not transparent, creating uncertainty in firms deciding whether to engage in conduct that could be procompetitive.[10]

Against those costs, WG consider the benefits from a consent. First, WG note that consents can be "convenient" to the agencies because "entering into consent decrees can substantially shorten the duration of an investigation [and] need not exhaust its resources preparing for litigation and instead can focus on a broader set of activities." (p. 14) In addition, "an agency may be able to narrow the theory of harm in a complex case without fully establishing a violation of the law." (p. 14) In doing so, WG urge the agencies to focus on only those consents that advance the welfare of consumers.

Second, and related to the first, a consent decree allows the agency to act more quickly than the courts when the market is dynamic. By the time the case winds its lengthy way through the court system, WG note that the conditions that led to the original anticompetitive concerns may no longer exist: "The ability of agencies to intervene more quickly through settlement may increase the chance of successful enforcement by restoring effective competition in the market faster." (pp. 16–17)

WG also note that despite the fact that consent decrees do not establish legal precedents, the consent decree "signal[s] an agency's enforcement goals [that] can help an industry quickly understand the prevailing logic and inner workings of the agency." (p. 17)

Third, WG note that consent decrees "have the ability to tailor remedies to the particular facts of individual cases and are thus able to address allegedly anticompetitive behavior more precisely." (p. 18) But WG again caution that such remedies can be "detrimental to consumer welfare or . . . could not lawfully be obtained in litigation." (p. 18)[11]

WG conclude that when considering a consent decree as a remedy, the "agencies must be aware of the social costs associated with over reliance upon settlements rather than upon litigation to promote competition policy." (p. 20)

It does not take much of a leap to infer that WG regard the current use of consent decrees by the agencies as being excessive in that the incremental gains from consents are outweighed by the incremental costs. But some of the costs described by WG may be difficult to accept on faith.

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[9] Intel Corp, FTC Docket No. 9341 (2010), https://www.ftc.gov/enforcement/cases-proceedings/061-0247/intel-corporation-matter.

[10] Concern about the lack of transparency seems, at least superficially, at odds with a benefit of consents highlighted by WG and noted below in the text, that consents can send a clear signal to market participants about the agency's enforcement policies. But, to be sure, the judicial system provides more durable guidance, one that does not depend on the changing composition of the agency heads or staff.

WG also express concern that if the "culture of consent" were to be adopted by other countries, antitrust policies internationally will fail to converge to a common framework. (pp. 12–13)

[11] Of course, it is quite possible that the remedy would advance consumer welfare and not be one that would be readily obtainable from the courts because, e.g., the court decisions do not yet reflect modern antitrust thinking.

As one example, WG claim, in effect, that if a consent decree is in the offing for a matter, both the investigation of the alleged harm and the underlying economic analyses will become a much more casual affair. Certainly, there may well be consent decrees that are ill-suited as remedies to address the alleged harm. But a general statement that a key cost of relying on consent decrees entails "less formality" (p. 14) in the analyses would seem to require greater substantiation (which I grant may be a mission impossible). Still, former Commissioner Wright is certainly in a better position than many others (including myself) to identify this as an important source of collateral damage. To the extent that economists in particular are not part of the process leading up to a decree, the remedy is for the agency itself to appreciate the risks of developing a decree that lacks a grounding in economics and so may harm consumers and competition.

As noted above, WG regard the consent decree addressing Intel's alleged anticompetitive behavior as an example of agency abuse of the consent decree process. While I offer no opinion on the decree itself or the underlying allegations, I certainly would be concerned if this remedy was fashioned with little or no economics input. And I suspect that some antitrust practitioners would regard that part of the decree addressing design changes as one that was tailored to the alleged anticompetitive harms. One may view the allegations against Intel as being unfounded or that the decree was too regulatory in nature (with costs not fully appreciated by the FTC), but that is a different issue from whether or not the consent was an effective remedy (meaning that it cured the anticompetitive conduct), assuming the FTC's views were correct.[12] Interestingly, I observe that this consent would seem to fit the general circumstances in which WG might think the consent decrees are more appropriate in that the "market" for computer chips is one that is dynamic.

While WG appreciate that consent decrees can be useful remedies, WG raise reasonable arguments in cautioning against an immediate resort to consent decrees to resolve anticompetitive harms, and those lessons should be taken to heart by the agencies. I certainly agree that any analyses in support of a consent should be complete and not the result of casual economics. Another paper worth reading.

—JRW

[12] I do agree that using consent decrees to extort conditions unrelated to the perceived harms (as in the Nevada matter cited above in the text) does not obviously advance the interests of consumers or serve to protect competition.