Formalism, Functionalism, and Consensus in Competition Law

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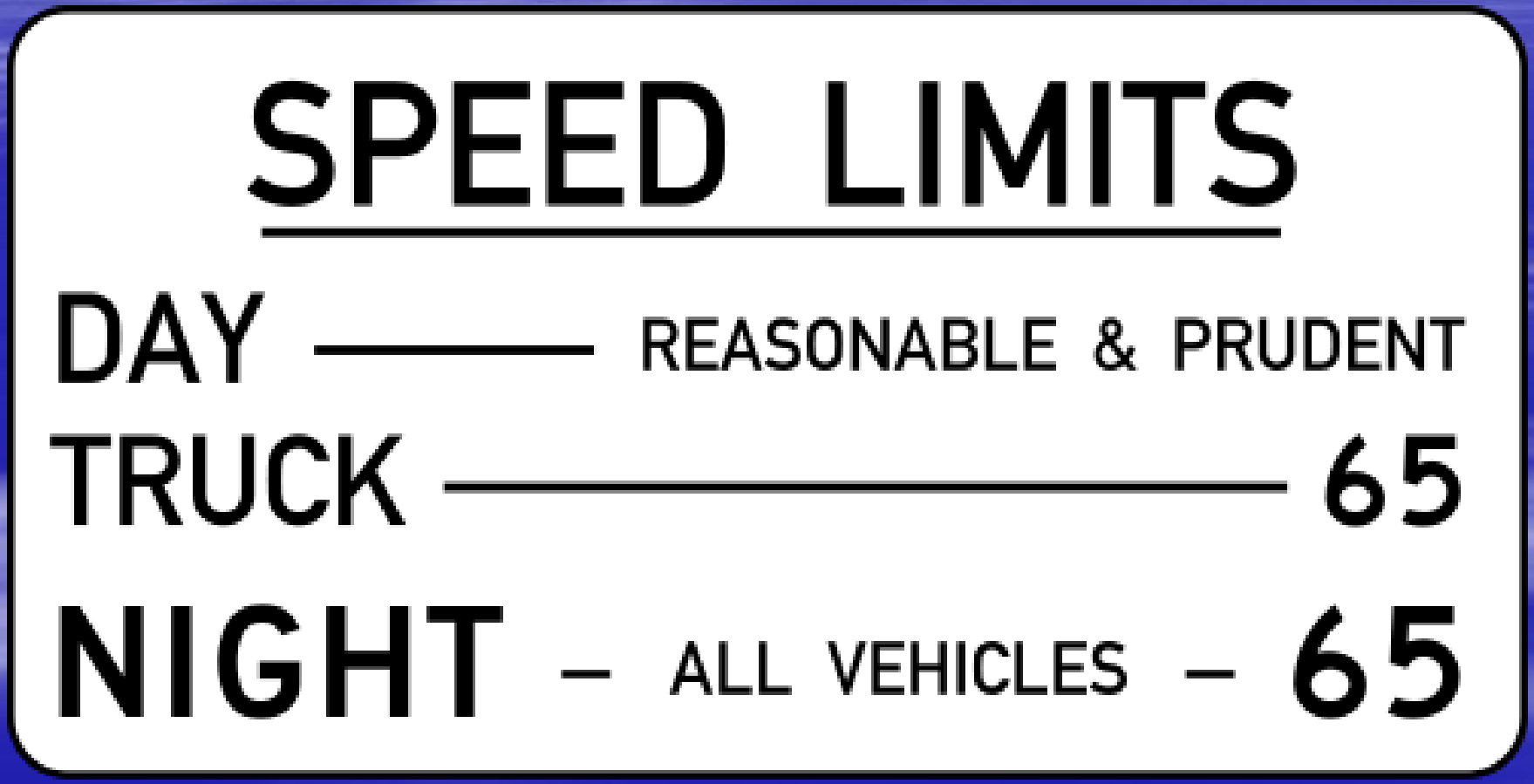
Formalism and Functionalism

- U.S.: Rules (formalism) versus standards (functionalism) in antitrust
  - i.e., “per se” rule (formal) vs “rule of reason”(functional) under Sherman Act § 1
- EU: Form-based (formal) vs effects-based (functional) analysis
  - i.e., Article 102 TFEU

Rules vs. Standards



Jurisprudential observations

- Advantages of rules
  - Clear notice/transparency
  - Minimize litigation costs
  - Minimize agency/judicial discretion/error
- Advantages of standards
  - Flexibility to “get it right” on individual basis
  - Allows adaptive learning by judicial decision-makers
  - Avoids rigidity, errors
- Legal systems tend to cycle between rules and standards

Definitional problem with rules

- Ludwig Wittgenstein: Rules aren't self-defining
- Must be interpreted based on background assumptions/purposes
- Rules require interpretive rules

Rules

- "No vehicles in the park."
  - Is a bicycle a "vehicle?"
  - What is purpose of rule?
  - Does a bicycle transgress purposes of rule?
  - Promulgation of "interpretive rules"

    rules fragment into standards

Comparison: U.S. and EU

U.S.

- Rule-based approach from early 20th c-1970s
  - RPM
  - Non-price vertical restraints
  - Tying
  - IP licensing
- Chicago School Revolution
  - Everything but hard-core price fixing rule of reason

EU

- Form-based approach
  - Long list of "restrictions by object" under Art. 101
  - Form-based approach for Art. 102
    - i.e., loyalty rebates (Michelin, Virgin Atlantic)
- Now, cautious transition toward effects-based analysis under Art. 102
  - 2008 Guidance Paper

But is the story right?

- U.S.
  - Rule of reason: "euphemism" for per se legality (98% defendant win rate)
  - Formal rules can not only create liability, but immunize against it:
    - No duty to deal
    - No predatory pricing liability for prices above avc
    - Market-power screen for tying
    - Minimum market share of 50% for monopolization
    - Discount-attribution test for bundled or loyalty rebates

Example: Price Squeeze

- *linkLine* (2009)
  - Price-squeeze = duty to deal + predatory pricing
  - No duty to deal, therefore nothing wrong with wholesale price
  - No showing of below-cost pricing, therefore nothing wrong with retail price
- *C.f.* EU cases (i.e., *Deutsche Telekom; TeliaSonera*) finding PS liability based on effects analysis

. . . is the story right?

- EU:
  - Inconsistent treatment of economically similar behavior:
    - Pure exclusive dealing, subject to effects-oriented foreclosure analysis *(Delimitis* (1991); *Van den Bergh* (1998))
    - Loyalty-inducing rebates by dominant firms presumptively unlawful and must be objectively justified *(Hoffman-La Roche (1979); Michelin II* (1983); *Virgin/BA* (2007)
    - Problem: pure exclusive dealing more likely anticompetitive than loyalty rebates, since foreclosure is automatic; only question is degree
  - 2008 Guidance paper recognizes the problem
    - Prescribes effects-based analysis
  - But General Court and ECJ still locked into formalism: (*Tomra* (2010); *Intel* (2014))

Can Rules Work for Antitrust?

- Is the domain determinable by rules?
  - See Wittgenstein.
- Rule of per se illegality for "price fixing"
  - *Chicago Bd of Trade* (1918): Literal price-fixing, but court applies rule of reason
  - *Socony-Vacuum* (1940): Literally not price-fixing, but court applies per se rule
  - *BMI* (1979): Avoid "literalism;" "price fixing" is just a shorthand way of describing certain agreements with no plausible efficiency justifications
  - To determine whether conduct is "price fixing" and hence per se illegal, must inquire into efficiency justifications
    - But then what's point of "per se" rule?
- "Per se" in name, rule of reason in substance
  - Group boycotts,Tying: market power, anticompetitive effects, no efficiencies

But matters to institutional assignments

- Specification of norm as rule or standard often has consequences for delegation of decisional authority
- If rule, application is question of law, therefore more likely . . .
  - Courts on de novo review
- If standard, application is fact-intensive, therefore more likely . . .
  - Agency has discretion
  - Finder of fact (i.e., trial judge or jury in common law system)

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Consensus

- Should antitrust enforcement be driven by consensus?
  - Disciplinary: broad agreement among economists
  - Geographic: overlapping consensus among competition agencies/jurisdictions
- Or should antitrust agencies take risks, explore new angles, innovate?

State of Play

U.S.

- Economic consensus
  - RPM (*Leegin*)
  - Presumption of market power from patents (*Independent Ink*)
  - FTC hearings on loyalty rebates: Is there consensus among economists?
- Not terribly interested in global consensus

Developing jurisdictions

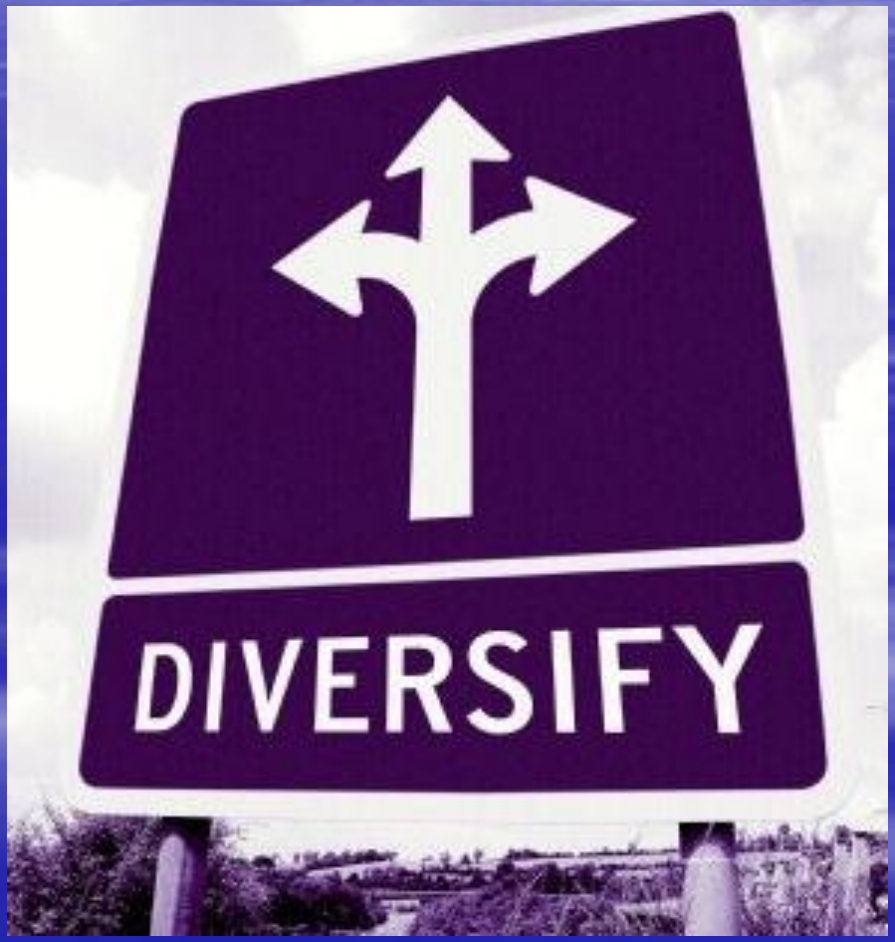
- What are global best practices?
- What are practices universally condemned practices?
  - Price-fixing cartels
  - Mergers to monopoly

Enforcement by consensus can stifle innovation and discovery

- Practices that were unknown 20 years ago:
  - Anticompetitive branded/generic pharmaceutical settlements
  - Patent ambush following product standardization
  - Self-preferential design of Internet search engines
  - Technology companies as “frenemies”

Agency Risk Diversification

- Core portfolio of consensus cases—pick the low-hanging fruit
- Judicious exploration of novel theories
- But (circling back) use of standards rather than rules
  - I.e., *Microsoft* (2001): No per se illegality for technological tying



Four Take-Aways

- 1. Use prohibitory rules when there is broad consensus that the practice is anticompetitive and the rule can be predictably applied in paradigmatic cases. (i.e., price fixing).
- 2. Use immunizing rules to create safe harbors from liability where costs of false positives are high and/or there are reasons to worry about commitment of decision to particular institutional actors.
- 3. In all other cases, use standards.
- 4. Expect to see vacillation between rules and standards over time.

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