The State Antitrust Paradox

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EXECUTIVE SUMMARY

American antitrust law is the bedrock of competition policy in the United States. It has also proven among the most intellectually challenging areas of the law for law students and judges alike. For most of its history, the Sherman Act of 1890 was bedeviled by a lack of consensus on what the very *purpose* of the law was. The lack of consensus on the policy behind antitrust law led, predictably, to inconsistent application and incoherent doctrines, a situation that lasted for much of the 20th century.

That all changed—at least at the federal level—with the publication of Robert Bork's *The Antitrust Paradox* in 1978. Judge Bork argued that the only benefit of antitrust law—the only object toward which its design and enforcement should be aimed—was to improve "consumer welfare." Rarely has a single book had such a sweeping impact on the law.

The "consumer welfare" standard advocated by Judge Bork quickly became the consensus goal of antitrust law among federal antitrust enforcers, chiefly at the Department of Justice (DOJ) and the Federal Trade Commission (FTC), and has remained so since. The Supreme Court approvingly quoted Bork when it declared that the Sherman Act is a "consumer welfare prescription." Federal antitrust enforcement, both at the DOJ and the FTC, seemed to gain a new appreciation for market efficiency and consumer interests—and for the dangerous tendency of antitrust enforcement to produce the exact opposite of its intended result.

Alas, state antitrust enforcement was another matter. Too often, state antitrust agencies seem to have more parochial priorities, and have used antitrust laws to shield powerful local constituents from competition. Perhaps the greatest paradox of antitrust—and certainly the most unfortunate—is how consistently government officials employ it for anticompetitive ends. The pattern has been particularly pronounced at the state level, as this report shows.

State policy makers and antitrust enforcers stand to benefit from absorbing some of the key insights of *The Antitrust Paradox*. The most important of these is that consumer welfare is maximized when output increases and prices decrease. That is the appropriate yardstick for measuring both the potential injury of supposedly anticompetitive conduct and the benefits of supposedly procompetitive antitrust enforcement.

This report makes the following recommendations:

- Congress should repeal the Hart-Scott-Rodino Act and preempt states' ability to bring *parens patriae* suits.
- Congress should work to eliminate overlapping areas of federal and state antitrust jurisdiction, by preemption if necessary.
- States should, as a matter of policy, avoid involvement in cases that federal antitrust enforcers are investigating.
- States should use antitrust laws to challenge other states' use of state action to protect their constituents from competition.

STATE ANTITRUST ENFORCEMENT AND THE ENDURING LEGACY OF *THE ANTITRUST PARADOX*

Rarely in the annals of American law has a single book had as much impact on an entire field as Robert Bork's *The Antitrust Paradox* (1978). A graduate of the University of Chicago Law School, where he was deeply influenced by Aaron Director and other founders of the "Chicago School" of Law and Economics, Bork served as solicitor general in the Nixon administration between stints teaching at Yale Law School, before being nominated to the federal bench by President Ronald Reagan. Along with Richard Epstein's *Takings* (1985) and *Bargaining with the State* (1994), Bork's magnum opus exemplified the profound impact that the University of Chicago has had for the better part of a century.

Applying the lessons of economics to law and policy in a rigorous way, the Chicago school approach continues to produce new generations of influential scholars and policy makers from schools across the country.[1] Alas, while it revolutionized federal antitrust enforcement, its impact on state antitrust enforcement has been far more lacking. This report examines the consequences, and suggests ways that the insights of the *Antitrust Paradox* might help inform and improve state antitrust enforcement.

A KEY QUESTION: WHAT IS THE PURPOSE OF ANTITRUST LAW?

Antitrust law is one of the most intellectually challenging classes you can take in law school. There are several reasons for this, starting with the fact that, from the passage of the Sherman Act in 1890 until the publication of Judge Bork's book 80 years later, there was no clear consensus on what the very *purpose* of the law was. Was it to protect mom-and-pop stores from "unfair competition" from larger firms? Was it to prevent any one firm from becoming dominant in a particular sector? Was it to prevent coordination among competitors? The debate over the law's purpose was, as Judge Bork wrote, a "cacophony."[2]

Judge Bork burned through this nettlesome underbrush by advancing a single proposition: The only social benefit of antitrust law—the only object toward which its design and enforcement should be aimed—was to improve "consumer welfare." Hence the yardstick by which to measure antitrust policies was the degree of improvement in the welfare of consumers, normally measured as the greatest output at the lowest price, which—assuming effective internalization of relevant externalities—would lead to the most efficient allocation of resources and the highest aggregate social benefit.

Soon after publication of *The Antitrust Paradox*, the "consumer welfare" standard became the consensus goal of antitrust law among federal antitrust enforcers, chiefly at the Department of Justice and the Federal Trade Commission (FTC), and has remained so since.[3] However, as noted, there is an area of antitrust law where progress toward prioritizing consumer interests and economic efficiency has been more limited: antitrust enforcement by state governments. Therefore, state policy makers stand to benefit from absorbing some of the key lessons from *The Antitrust Paradox*.

Consumer Welfare as the Measure of Antitrust Law's Benefit

Since its beginnings, American antitrust law has been plagued by confusion as to both the problems it was designed to fix and how the proposed remedies were supposed to fix them. A pattern quickly emerged of antitrust enforcement attacking instances of monopolization and restraints on trade that, on closer inspection, were more imagined than real, and doing so with remedies that had unintended negative impacts on competition.

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Bork's insight was a long overdue corrective to the paradoxically anticompetitive doctrines that had arisen in support of America's competition policy. Indeed, many of these doctrines were not just anticompetitive, they were, as Bork put it in *The Antitrust Paradox*, "ultimately incompatible with the preservation of a liberal capitalist social order."[4]

Since the 1970s, federal enforcement agencies and federal courts have largely accepted the basic propositions of Bork's *The Antitrust Paradox*. These are as follows:

- Consumer welfare should be the overriding goal of antitrust law.
- Consumer welfare is maximized when markets increase output and lower prices.

- Efficiencies that lead to increased output and lower prices are good for consumers and competitors alike, even when they result in market concentration or economic losses to less efficient competitors.
- Many practices formerly thought to be "anticompetitive" are actually procompetitive and pro-consumer, even when they leave certain competitors worse off.

As scholars and jurists—and eventually the Supreme Court—absorbed Bork's insights, federal antitrust enforcers started walking away from the quaint mid-20th century goals of preventing "unfair competition" and excessive "market power." A year after publication of *The Antitrust Paradox*, the Supreme Court quoted Bork when it declared that the Sherman Act is a "consumer welfare prescription."[5] Federal antitrust enforcement, both at the Department of Justice and the Federal Trade Commission, seemed to gain a new appreciation for market efficiency and consumer interests—and for the dangerous tendency of antitrust enforcement to produce the exact opposite of its intended result.

As former FTC commissioner Christine Wilson explained in a 2019 speech:

> The consumer welfare standard equates with consumers' surplus in economic terms— technically, the difference between what each consumer actually pays and what he or she would be willing to pay. Generally speaking, conduct is evaluated only by looking at the surplus that goes to consumers, ignoring what goes to sellers. For instance, in a merger analysis, the gains to the merging

producers do not count; only the effect on consumer prices is relevant.[6]

State antitrust enforcers often seem to have other priorities, however. When Andrew Cuomo, then attorney general (AG) of New York, sued Intel for antitrust violations in 2009, the complaint presented scant evidence of consumer harm.[7] But page after page of the complaint described alleged harms to Intel's competitor Advanced Micro Devices, which just a few years earlier had announced plans to construct a multi-billion-dollar facility in New York state, after the state agreed to extend record-breaking incentives.[8]

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A BRIEF HISTORY OF STATE ANTITRUST ENFORCEMENT

Competition policy is arguably the most essential aspect of economic regulation in a democracy. It is at the root of the Constitution's federal structure, its guarantees of freedom of contract, and its protection of property rights.

In America, the original constitutional understanding made protecting the people's health and safety the province of state and local governments, under what were known as general "police powers," while the federal government was empowered to regulate commerce among the states. That gave the federal government jurisdiction over transactions that actually crossed state lines, but not over purely intrastate transactions.

The New Deal promised, in essence, to protect the right to work by limiting the right to work, and the right to farm by limiting the right to farm.

In 1890 Congress passed the Sherman Act, which prohibited monopolization and restraints on trade at the federal level. At that time, most states had some version of antitrust laws. Major jurisdictional disputes and conflicts between state and federal antitrust laws were largely avoided because there was little overlap between state and federal authority in the regulation of commerce, which included competition policy.[9] If it crossed state lines, the federal government could regulate it and the states generally could not; if it did not cross state lines, the states could regulate it and the federal government generally could not. That understanding also applied to antitrust laws.[10]

President Franklin D. Roosevelt's New Deal changed all that. In response to the Great Depression, his New Deal program involved a dramatic expansion of the government's power to regulate commerce at both the federal and state level. A central purpose of the New Deal was to protect the vulnerable from the purported ravages of unfettered competition. It sought to accomplish this through a constitutional transformation, which, for the first time, gave the federal government the power both to both create cartels and monopolies across every sector of commerce and enforce those created by the states.

The general theme was support for higher wages and prices. The New Deal accomplished this by restricting the supply of two key production factors: agriculture and urban labor. Farm prices were to be raised by restricting farm production; wages were to be raised through union laws constricting the supply the labor. The New Deal promised, in essence, to protect the right to work by limiting the right to work, and the right to farm by limiting the right to farm.

Federal and state regulation now substantially overlap over whole swaths of economic activity.

The Supreme Court resisted at first, but after Roosevelt threatened to pack it with additional justices, the Court relaxed the limits on the federal commerce power, deciding, in cases from *NLRB v. Jones & Laughlin Steel Co.*[11] to *Wickard v. Filburn,*[12] that the federal government could regulate any activity that might have a substantial effect on interstate commerce in the aggregate across the country. Thus, the Court abdicated its vital role as guardian of the framework of limited and enumerated federal powers. It paved the way for the New Deal's expansion of federal power over purely intrastate transactions, without diminishing the states' power to regulate the same transactions in any way. As a result, federal and state regulation now substantially overlap over whole swaths of economic activity.

Though the early progressives thought of themselves as fervent opponents of corporate power, the reforms they introduced paved the way for corporations and special interests to capture government regulatory bodies for the purposes of erecting cartels and monopolies that would benefit them at the expense of consumers. In the area of antitrust the results were particularly counterproductive, with enforcers routinely attacking imaginary cartels and monopolies, and in the process creating real ones.

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federal regulations of commerce, when the federal antitrust laws were originally passed, they applied only to transactions that crossed state lines. But after the Court's New Deal-era expansion of the commerce power, federal antitrust law applied to practically every transaction under the Sun. The Court's vast and apparently unintentional expansion in the reach of the federal antitrust laws created an equally unintentional conflict between those laws and the states' ability to cartelize markets for their own political purposes.

The conflict came to a head in the 1943 case *Parker v. Brown*. At issue was a California raisin marketing program that limited the production and sale of raisins. The program was designed to sustain producers' profits and impose the resulting costs on out-of-state consumers—a cartel arrangement made possible by the fact that California produced 95 percent of the nation's raisins at the time.[13] The Supreme Court upheld the California law, reasoning that the federal antitrust laws were not intended to apply to state regulatory action.[14]

The Court was technically correct on that score. No federal regulation of commerce enacted before the New Deal was supposed to apply to state regulation, which could not cross state lines and therefore could not normally come within the reach of the federal commerce power as originally understood. The fact that federal antitrust laws might now apply to cartels and monopolies created by state governments was yet another indication that in expanding the reach of the federal commerce power, the Court had inadvertently extended the reach of countless federal laws, thereby creating overlapping authorities where Congress had intended none. The result was a massive overlap of federal and state authority over most commerce that is arguably incompatible with the constitutional design, and its separate spheres of state and federal authority.

In an efficient market, it is difficult to enforce cartel arrangements or exclude new competitors.

Unwilling to revisit its recent Commerce Clause decisions, the Court proceeded to make matters considerably worse: In *Parker* it looked at the cartels and monopolies created by state governments and declared them not to be cartels and monopolies, as if by waving a wand it could transform black into white. Thus was born the "*Parker* state action doctrine."[15]

The net result eliminated the one potential benefit of extending federal antitrust laws to intrastate activity. Antitrust laws are rarely necessary in the case of purely private monopolies and cartels because, in an efficient market, it is difficult to enforce cartel arrangements or exclude new competitors. Monopolies and cartels that charge prices much above competitive levels tend to lose market share, as new market entrants—or cartel participants sensing competitive opportunity—seek to increase market share by exploiting the difference between the competitive price (theoretically equal to the marginal cost of production) and the supra-competitive cartel or monopoly price. Eventually, such competitive pressures cause cartels and monopolies that seek to charge supracompetitive prices to reduce prices or break down.

The exceptions to the rule are monopolies and cartels enforced by state governments, which can enforce internal discipline and exclude new entrants by law. Ironically, by exempting state regulations from federal antitrust laws, the Supreme Court ensured that those laws would not apply to the most dangerous cartels and monopolies—those created and enforced by government power.

THE PROBLEMS OF STATE ANTITRUST ENFORCEMENT

For nearly 50 years following the New Deal's vast expansion of federal power, the federal antitrust laws largely obviated state antitrust enforcement. But the Hart-Scott-Rodino (HSR) Act of 1976 created a compelling new opportunity for rent-seeking by state officials. The law allowed state attorneys general to sue under federal law as *parens patriae* ("parent of the country"). In the decades since, this enhanced state antitrust enforcement has proven superfluous at best and anti-competitive at worst.

Competition and Consumer Welfare

One of the most contentious issues in antitrust law is how to define "market power." Courts traditionally begin an antitrust analysis by defining the relevant market, in terms of both product category and geography, after which they seek to determine who the competitors are within that market.[16] They must then assess whether those charged with violations of antitrust laws have, or could have, the necessary market power to engage in conduct that has injurious anticompetitive effects.

Nowadays, a determination of "anticompetitive conduct" usually requires a finding of restriction of output, increases in prices, or both. But in a normally functioning market, restricting output or increasing prices almost always creates opportunities for competitors to jump into the market at a lower price or with additional supply.

Higher output and lower prices arise from increased efficiency in the allocation of human and material resources.

Courts have had enormous difficulty in distinguishing between anticompetitive conduct and conduct that is merely commercially risky but could have procompetitive effects. Higher output and lower prices arise from increased efficiency in the allocation of human and material resources, which is how society creates surplus and wealth. In a properly functioning market, the acquisition of large market share is almost impossible to achieve except by efficiency and internal growth, both of which benefit society. Yet the temptation of seeing anticompetitive harm in every instance of a company having a large market share has proven difficult to resist, regardless of whether the increased market share tends to benefit competition and consumers.

As a result, for most of the 20th century, courts applied antitrust laws in ways that achieved anticompetitive outcomes, created special advantages in the name of eliminating them, and hurt consumers in the name of helping them. The doctrines they developed were applied in an increasingly wide array of cases that showed the absurdity of the doctrines.

For example, the 1962 case *Brown Shoe v. United States*[17] concerned a merger between the country's third and eighth largest shoe manufacturers. The Supreme Court noted that in 47 urban markets the combined market share of the two firms would barely exceed 5 percent

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in an industry with countless participants, of which the 24 largest represented a mere 35 percent of the national market. The Supreme Court nevertheless held the merger illegal, despite the industry's remarkably flat and diverse market structure, because of what it saw as an anticompetitive trend in the industry. As a result, the antitrust laws prevented a consolidation that would almost certainly have increased output while reducing prices.

In recent decades, courts, influenced by Judge Bork, have retreated from many of these excesses. They have been increasingly wary of curtailing private parties' freedom of contract in cases where conduct and structures once thought to run afoul of the antitrust laws may prove procompetitive. Hence, federal courts and enforcement agencies have pulled back from interfering with commercial arrangements they had long viewed with suspicion, where it is clear that such arrangements are driven by efficiency and can increase consumer welfare.

It is increasingly clear that interfering with such transactions achieves the exact opposite of what antitrust law was designed to achieve. In this respect, the modern understanding of antitrust policy reflects the insight that the best way to protect the public from the dangers of monopoly and restraints on trade is by preserving free competition. That is the essential insight of *The Antitrust Paradox*. Unfortunately, as the next section shows, state legislators and officials have shown great difficulty in absorbing that insight.

Monopolies and Oligopolies

As the U.S. Supreme Court stated in *United States v. Grinnell Corp.*, a monopoly position attained by efficiency and internal growth "as a consequence of a superior product, business acumen, or historic accident," does not violate the antitrust laws.[18] What the antitrust laws prohibit is not monopoly but *monopolization*. Section 2 of the Sherman Act prohibits (1) the use of improper tactics to achieve a monopoly position (attempted monopolization), and (2) the use of improper tactics to maintain or strengthen a monopoly position (monopolization).

Any judge can decide that some conduct has no business rationale if he or she lacks enough understanding of economics or of a given industry to see one.

Suppose that a telephone company achieves a monopoly of the local fiber-optic network. The company will violate antitrust laws if it uses its position to require customers to purchase all their telephones from it, thereby monopolizing the local market for telephones. Here, it is not the company's monopoly of the local network that is illegal, but rather its *monopolization* of the telephone market. Notably, it can run afoul of the antitrust laws even if its monopolization does not result in market concentration.

In applying Section 2 of the Sherman Act, courts have looked for conduct that seems to have no lawful business rationale and instead relies on an anticompetitive effect in order to be profitable. The problem with this approach should be obvious: Any judge can decide that some conduct has no business rationale if he or she lacks enough understanding of economics or of a given industry to see one. That, indeed, is an apt description of most 20th century federal antitrust cases.

An oligopoly resembles a monopoly in that barriers to entry by new competitors are high, but the market is dominated by a few firms rather than a single firm. Courts and enforcement agencies sometimes confuse oligopolies and cartels, but they are not necessarily the same. Oligopoly describes a legal market structure in which entry to competitors is limited by barriers to entry, whereas a cartel describes an illegal agreement among existing competitors (usually in an oligopoly) to restrict output, raise prices, or both.

A natural barrier to entry is most often simply the challenge of achieving a competitive economy of scale. A college graduate trying to decide between launching a food cart and launching an airline will no doubt be discouraged by the barriers to entry in the airline industry, but that does not make the airline oligopoly illegal or even undesirable. Where the entry of competitors is simply a matter of the time it takes to launch a firm with the scale and resources necessary to be competitive, there is no violation of the antitrust laws. But where existing firms take advantage of such natural barriers to entry in order to cartelize a given market, most courts agree that enforcement is appropriate.

In cases where firms achieve monopoly or oligopoly through efficiency and growth, any antitrust enforcement designed to “deconcentrate” the market can only hurt competition and consumers. A monopoly based on efficiency has very little room to restrict output and raise prices before new entrants appear. This can be seen in an example given by Judge Bork in *The Antitrust Paradox*:

> If the law dissolved a firm having a 100 percent monopoly [as a result of efficiency] into five approximately equal parts, the economic forces that led to monopoly would still be operative and would lead in that direction again.
>
> Let us suppose, however, that the law announced a policy of dissolution of any firm that exceeded 50 percent of the market. When one of the new firms approached that size once more, it would have every incentive to restrict its output in order avoid the penalties of the law, and so the law would produce the evil of resource misallocation in the attempt to avert it.[19]

Where federal agencies have declined to act, there may still be dozens of state attorneys general with jurisdiction over a given company.

In other words, antitrust enforcement can create an artificial cartel that injures the public in the place of a natural monopoly that benefits the public.

Institutionally, the overlapping jurisdiction of state and federal antitrust enforcers raises a clear risk of erroneous enforcement: Where federal agencies have declined to act, there may still be dozens of state attorneys general with jurisdiction over a given company. The risk that one of them will see potential antitrust injury where there is only a perfectly innocuous and beneficial market concentration is a significant concern.

State attorneys general sometimes seek to justify their involvement in antitrust matters on the basis of their greater knowledge of local industry conditions. But the lead enforcer in these cases is almost always the U.S. Department of Justice or the Federal Trade Commission, *A proper division of labor between federal and state governments would significantly diminish states' involvement in monopoly cases.*

which makes it difficult to understand what is so indispensable about state antitrust enforcement.

As a general principle, a state attorney general should only get involved in antitrust enforcement when the state takes the lead in a case—that is, in matters where the private parties are local. The agreements that govern the division of labor between states and federal enforcement agencies should be modified so as to eliminate overlapping enforcement. Federal agencies should not concern themselves with purely local matters, and the states should only concern themselves with purely local matters.

However, given modern supply chains and the mobility of capital and labor, few antitrust concerns are purely local. As a practical matter, a proper division of labor between federal and state governments would significantly diminish states' involvement in monopoly cases.

The current system is rife with opportunities for rent-seeking. As in New York's 2009 case against Intel, state attorneys general who pursue antitrust actions are often acting mostly to protect local businesses from out-of-state competition. State officials also commonly pursue enforcement actions purely on the basis of percentage of market share, as supposed evidence of "market power," without bothering to identify the narrow circumstances—usually the result of prior government intervention or regulation—that would make it sustainable for a company in that industry to monopolize a dominant market share by restricting output or raising prices.

Mergers and Acquisitions

As a matter of basic economics, mergers and acquisitions among competitors are indistinguishable from natural growth through efficient capital investments. When such a transaction shows a positive return on investment, the result is an efficient wealth-creating reallocation of resources across the economy as a whole. If the transaction shows a positive return on investment, it is because the efficiency and capacity of the firm—and hence also of the overall market—have increased. Gains in efficiency and capacity can only exert downward pressure on prices and benefit consumers.

Unfortunately, U.S. antitrust policy has long failed to recognize this economic reality. Like the *a priori* fear of monopolies, the particular scrutiny accorded to mergers and acquisitions under the antitrust laws is founded on the *a priori* fear of market concentration, and is subject to the same concerns of unintended impacts arising from misguided enforcement actions. In addition, mergers and acquisitions raise problems of their own, because of the special treatment accorded to them by the antitrust laws and the inordinate attention they receive from antitrust enforcers, particularly at the state level.

There are three basic kinds of mergers:

- Horizontal mergers among competitors;
- Vertical mergers between suppliers and purchasers; and
- Conglomerate mergers between companies in different markets.

Antitrust enforcement should not be concerned with vertical or conglomerate mergers at all, because such mergers can never injure competition or harm the consumer on their own absent some horizontal effect or some other separate violation of the antitrust laws. Vertical mergers present no more concern than any company with a vertically integrated supply chain. And even horizontal mergers, which receive the most scrutiny, have significant potential for increased efficiency and consumer welfare. They should be scrutinized only in special circumstances—usually the result of prior government regulation—where it is clear that competitors have colluded, or are likely to collude, to restrict output and raise prices.

Antitrust enforcement imposes significant costs on merger activity because federal premerger notification requirements are costly, and can turn into far more costly investigations. Under Section 7A of the Clayton Act (updated in Hart-Scott-Rodino), most mergers must be submitted to the Department of Justice and the Federal Trade Commission. Those two agencies then decide which of them will conduct the approval process on behalf of the federal government.

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However, state attorneys general can still seek injunctive relief to block a merger transaction under Section 7 of the original Clayton Act, so the merging parties' federal premerger notice often leads state attorneys general to open investigations of their own. In a typical case, a party will offer to turn over to the state AG any waivers of confidentiality with respect to the federal filings, in exchange for confidentiality agreements regarding the investigation. The state AG then issues a kind of subpoena called a "civil investigative demand" to obtain additional information.[20] This can quickly turn into a fishing expedition.

Antitrust enforcers' concern with horizontal mergers—as former Assistant Attorney General John H. Shenefield and American Enterprise Institute scholar Irwin M. Stelzer note—are typically founded on one of three potential anticompetitive effects: "first the surviving firm may have assembled the instruments of dominance; second, the market, with uncertainty reduced, is more susceptible to collusion; and third, the merged firm itself may be able to raise prices unilaterally."[21]

These supposed anticompetitive effects typically cannot occur in a market free of government interference because raising prices or reducing output will almost always attract new market entrants. It is in heavily regulated industries—such as health care and telecommunications—that special market conditions create potential problems of concern to antitrust regulators. The health care area raises unique public policy concerns because it is not merely competition that suffers when output is restricted, but also public health. Unsurprisingly, these are the mergers that tend to receive the most scrutiny, particularly from state attorneys general.

In keeping with economic rationality, vertical and conglomerate mergers are virtually always approved by the relevant federal agency as a matter of course, and few lawsuits, whether brought by agencies or by private parties, prosper on allegations of injury from vertical or conglomerate mergers. The ability of states to pursue injunctive relief under Section 7 of the Clayton Act and block vertical and conglomerate mergers is correspondingly limited. Accordingly, the focus of antitrust enforcement in this area is overwhelmingly on horizontal mergers. Still, as New York's case against Intel shows, the potential for abusive and costly state investigations piggybacking on federal actions is evident, even where the state would be highly unlikely to prevail in court.[22] In addition, states are routinely involved in mergers that do not rise to the level of Hart-Scott-Rodino review.

Companies contemplating mergers reportable under Hart-Scott-Rodino routinely share HSR reports with every potentially concerned state attorney general pursuant to confidentiality agreements, as previously mentioned. When the state attorney general decides there are problems in a proposed merger, the remedy is typically to block the merger or to require the parties to modify the intended transaction, sometimes through extensive divestitures, modifications of existing executory contracts, and even substitution of different parties for the original ones. In cases where the premerger review leads to litigation, any of these outcomes may result, whether by settlement or by court decree.

States' involvement in premerger reviews is entirely superfluous and fraught with the potential for mischievous interference in private transactions that show a positive return on investment and a net benefit to society.

This is an area where federal enforcement is also arguably superfluous. Congress should revisit the HSR premerger notification and review requirements. There is little justification for adding to the burdens on private business combinations in the service of a prophylactic that almost never proves justifiable. Mergers and acquisitions may pose some danger in heavily regulated industries—almost invariably as a direct result of such regulations. But in markets that are functioning properly and free of government interference, merger activity is a vital pillar of the dynamic allocation of human and material resources upon which a free society depends for competition, innovation, and wealth.

In markets that are functioning properly and free of government interference, merger activity is a vital pillar of the dynamic allocation of human and material resources.

Horizontal Restraints on Trade

In a typical market, cartel discipline is impossible to maintain because (1) individual cartel members have an inherent incentive to break with the cartel and increase output and (2) the higher prices draw in new market entrants offering lower prices. But the existence of supracompetitive prices—prices above what may be sustained in a competitive market—may not always be immediately apparent to potential entrants, enhancing the incentive to collude on price among existing competitors.

The antitrust laws take an especially harsh view of such cartel behavior, which can remain undetected by potential entrants even as it injures consumer welfare. Thus, virtually all agreements among competitors that have an effect on price—whether explicit or tacit—have been made per se illegal, and are the particular focus of criminal antitrust enforcement by federal and state agencies.

Price-fixing occurs whenever there is an agreement relating to price among competitors. The price itself doesn't matter. As in other areas, *Not all agreements among competitors that have an effect on prices necessarily constitute price-fixing.*

antitrust enforcement here often targets behavior that is not harmful to anyone.[23] On the other hand, price-fixing is clearly dangerous in certain circumstances. Bid-rigging is a particularly problematic because the contractual "offer" has already been made by the "purchaser" in the expectation of a competitive bid, and sometimes under circumstances that legally require competitive bidding. Hence, price-fixing in the context of a bid is particularly difficult to distinguish from ordinary fraud.

Public policy is especially concerned with bid-rigging in the award of government contracts. State and federal criminal laws properly empower state attorneys general to prosecute such cases. It is over bid-rigging on government contracts that state attorneys general most often sue or prosecute on their own behalf rather than as *parens patriae*.

However, not all agreements among competitors that have an effect on prices necessarily constitute price-fixing. If the agreement has a valid objective protected by the law, and incidentally affects prices, courts will not consider it a per se violation of the antitrust laws and will instead apply a "rule of reason" analysis, which requires a showing of anticompetitive injury. The question over the states' role arises where the states sue in these close cases as *parens patriae* on behalf of state residents.

In terms of anticompetitive injury, horizontal market division and collective refusals to deal can constitute the economic equivalent of price-fixing. Market divisions are agreements to divide up a product or geographic market—or the customers themselves. Such agreements are per se illegal restraints on trade. A superficially analogous situation is presented by covenants not to compete between a business and a former employee.[24] Such covenants usually have a valid legally protected purpose, such as the protection of intellectual property or trademarks, and are treated as "ancillary restraints on trade" under the rule of reason.

An example of a collective refusal to deal is a situation in which a supplier and certain purchasers agree to exclude certain other purchasers who depend on that supplier. As the Supreme Court held in *Northwest Wholesale Stationers v. Pac. Stationery*, collective refusals to deal are only anticompetitive in highly particular situations such as unusual "market power or exclusive access to an element essential to effective competition."[25] This situation arises most often as a result of government regulation. Otherwise, under the rule of reason, such cases are rarely sustained, and are usually considered ancillary restraints.

State authorities should focus their antitrust enforcement on cartel and other horizontal restraint cases—which tend to be the most local of the various kinds of antitrust cases and are generally the cases where antitrust enforcement is most easily justified—and pursue criminal prosecutions only when a criminal case can be made out. Here, as elsewhere, there is little justification for states' authority to pursue cases as *parens patriae*.

Vertical Restraints on Trade

For much of the 20th century, antitrust enforcement intervened heavily in the category of routine business practices known as vertical restraints on trade. These include resale price maintenance, vertical market divisions, tying arrangements, exclusive dealing arrangements, price discrimination, and vertical refusals to deal. This is one area of antitrust law where the modern revision of antitrust and free market economics has had a major impact.

Virtually every kind of "vertical restraint on trade" is something a company would be legally free to do if it acquired the relevant purchasers and integrated them into its distribution system. It may be less efficient to have the distribution coordinated among various suppliers and purchasers, but it is hard to argue that a diffuse distribution network is more anticompetitive than a vertically integrated company. For that reason, courts and enforcement agencies have been especially willing to revise their prior doctrines on vertical restraints, and the rule of per se illegality is nowadays applied far more narrowly and less often than before. As the Supreme Court held in 1977 in *Continental TV, Inc. v. GTE Sylvania, Inc.*: "Interbrand competition is the competition among the manufacturers of the same generic product … and that is the primary concern of the antitrust law."[26] Hence, intra-brand competition receives much less scrutiny.

Tying arrangements are a somewhat special case. They are called restraints on trade, but they are potentially anticompetitive only in circumstances closely analogous to monopolization. In the typical case, the firm has a monopoly—or "market power"—over a product in one market and uses its position to force customers to purchase a second product over which it does not have a monopoly if the customer wants to purchase the first product at all.

The anticompetitive effect theoretically results from a cross-subsidy: The firm artificially raises the price of the monopoly product in order to depress the price of the tied product to a point that undercuts competitors in the second product's market. The case should depend on whether the artificially higher prices of the monopoly product are sustainable due to special circumstances such as prohibitively costly barriers to entry. As discussed above in the section on monopolies, prices much higher than marginal cost almost always draw new market entrants. Hence, tying arrangements are normally not sustainable because the higher price of the tying—monopoly—product is not sustainable.

Federal agencies nowadays rarely insinuate themselves into these types of cases. The concern with the role of state attorneys general is that they have not caught up to modern law and economics, and that, motivated by local bias, they may tend to use their enforcement powers in ways that injure interstate competition, as New York's case against Intel shows. The bar should be especially high for any state involvement in this category, as antitrust enforcement with respect to vertical restraints has perhaps the highest potential for injury to the public.

Manipulations of State Government Power against Nonresident Competitors

Federal law exempts broad categories of federal and state regulation that would otherwise be illegal under the antitrust laws. The classic examples are government-created cartels, such as the agriculture and labor union cartels that arose out of the New Deal. These cartels function at both the federal and state levels.

At the state level, firms sometimes seek cartel protection from nonresident competitors by gaining special advantages from their respective local governments, such as the state raisin cartel in *Parker*. Under the *Parker* doctrine, such government-created preferences are shielded from the antitrust laws.

But the *Parker* doctrine has been somewhat narrowly drawn, and state attorneys general still have not used the antitrust laws to challenge the anticompetitive practices of other states. This is an area where more involvement by state attorneys general could have procompetitive effects. Instead of using the antitrust laws to protect local constituents from out-of-state competitors, states should use the antitrust laws to challenge the state-created cartels and monopolies of other states.

RECOMMENDATIONS

- The Hart-Scott-Rodino Act should be repealed. At the very least, Congress should eliminate states' ability to bring *parens patriae* suits.
- Congress should work to eliminate overlapping areas of federal and state antitrust jurisdiction. States should, as a matter of policy, avoid involvement in cases that federal antitrust enforcers are investigating.
- Rather than try to shield their constituents from competition, states should use antitrust actions to challenge other states' use of state action to protect their constituents from competition.

CONCLUSION

Many government policies have undesirable unintended consequences. Few, however, consistently produce the very opposite of the intended consequence. Alas, it is in this respect that American antitrust law has been truly outstanding.

As Judge Robert Bork showed over four decades ago, most areas of antitrust enforcement are highly problematic and exhibit a strong tendency to injure both competitors and the public. Antitrust enforcement by states exhibits these problems in spades.

After a century of state-level antitrust enforcement, it is clear that the New Deal's expansion of the federal commerce power to the ends of the Earth should have resulted both in the preemption of state-level antitrust enforcement—except in criminal cases like conspiracies to defraud the public—and in the application of federal antitrust law to the monopolies, cartels, and restraints on trade created by state governments.

Viewed in this light, it is hard to think of a Supreme Court decision since the Civil War that has caused so much injury to the public as *Parker v. Brown*. Generations of Americans should be grateful to Judge Bork for shining such clear light on the state action doctrine, and the many other problems of America's anticompetitive competition policy. State policy makers should take special heed.

NOTES

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