Before the
Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, D.C. 20580

August 15, 2018

In the Matter of	)	
	)	
Competition and Consumer Protection	)	FTC Docket No.2018-0048
in the 21st Century	)	
	)	

Comments of the Innovation Defense Foundation

The Innovation Defense Foundation is a project of the Method Foundation, a registered tax-exempt nonprofit organization under 26 U.S.C. §501(c)(3) based in Washington, D.C. The Foundation is a nonprofit, nonpartisan, research and issue-advocacy institution focusing on "permissionless innovation,"[1] seeking to address unnecessary legal or regulatory impediments to innovation. The Innovation Defense Foundation is actively involved in several issues relating to competition policy and is particularly interested in the technology sector and the role of disruptive innovation in expanding competition and increasing consumer welfare.

With respect to competition policy, the Innovation Defense Fund is concerned that, if misapplied, antitrust laws can actually limit competition and innovation, the benefits of which inure to consumers as a whole. To avoid unnecessary impediments on dynamic market competition, the Innovation Defense Foundation urges to the Commission to focus its antitrust enforcement actions specifically on those cases where there is demonstrable consumer harm.

In a review of the history and practice of antitrust, Harold Demsetz makes the point that competition is a complex process that occurs through many dimensions beyond simply price competition. Because competition can take many forms, Demsetz argues that antitrust laws should focus on the broader mix of competitive processes.[2] This is a clearly different and more challenging task than simply eliminating monopolies or reducing market concentration. Regulating competition along one dimension, such as price will have implications for competition on other margins, which poses challenges for antitrust policy. As Demsetz notes:

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[1] Adam Thierier, *Permissionless Innovation: The Continuing Case for Comprehensive Technological Freedom*, Mercatus Center (April 2016), https://tinyurl.com/y7tyu8m2.
[2] Harold Demsetz, "How Many Cheers for Antitrust's 100 Years?" *Economic Inquiry*, Vol. XXX, April 1992, pp. 207-217.

> [The perfect competition model] is not very useful in a debate about the efficacy of antitrust precedent. It ignores *technological competition* by taking technology as given. It neglects *competition by size of firm* by assuming that the atomistically sized firm is the efficiently sized firm. It offers no productive role for *reputational competition* because it assumes full knowledge of prices and goods, and it ignores *competition to change demands* by taking tastes as given and fully known.[3]

Focusing exclusively on monopoly or concentration necessarily overlooks other aspects of competition that also affect consumer welfare. Because consumer welfare is central and responsive to all forms of competition, it remains an important measure in determining whether markets are competitive or anti-competitive. As Abbot B. Lipsky, Jr. recently testified, "no alternative criterion comes close to being a plausible candidate to be the guiding principle for construction and application of antitrust law."[4]

The Commission should assess antitrust policy based on a broader notion of efficiency and competition, instead of a narrow emphasis solely on price competition. Focusing on consumer welfare will facilitate this broader view and help ascertain the effects of current competitive practices. Empirical findings and economic analysis can help guide the Commission's assessments of competition and anti-competitive practices.

This framework allows a better understanding of the competitive forces at work in any given market. Several aspects of antitrust law can be reviewed from this perspective to ensure that the FTC's policies promote competition and consumer welfare to the greatest extent possible. Accordingly, it may be useful to address the following aspects of antitrust law:

1. Tying and Bundling Arrangements.

Recent actions against Google by the European Commission were justified in part by asserting that tying is an anti-competitive practice.[5] The question of tying is particularly important in the technology sector, where products are continually updated in a dynamic marketplace. As products are modified, the question arises of whether a new feature is viewed as an enhancement of an existing good or a new good that is bundled with an existing good. Economist Kevin Lancaster made clear that a good or service is defined by the various attributes the good provides to maximize utility.[6] Enhancing the

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[3] *Ibid.*, p. 209.

[4] Testimony of Abbot B. Lipsky before the Committee on the Judiciary Subcommittee on Antitrust, Competition and Consumer Rights, December 13, 2017, available at: https://www.judiciary.senate.gov/imo/media/doc/12-13-17%20Lipsky%20Testimony.pdf

[5] European Commission, "Antitrust: Commission Fines Google €4.34 Billion for Illegal Practices Regarding Android Mobile Devices to Strengthen Dominance of Google's Search Engine," July 18, 2018, available at http://europa.eu/rapid/press-release_IP-18-4581_en.htm.

[6] Kelvin J. Lancaster "A New Approach to Consumer Theory," *The Journal of Political Economy*, Vol. 74, No. 2, April 1966, pp.132-157.

attributes of a good or service, or adding new attributes to that good or service increase its value to consumers. This is especially important to acknowledge when assessing competition in the technology sector, where products can be readily modified with new features in a very short timeframe.

Typically, antitrust law has viewed tying as anticompetitive because it may allow a firm with market power in one area to extend that power to other market segments. Yet there are cases where there are unambiguous increases in consumer welfare due to tying, and in these instances anti-tying laws can actually thwart innovation and harm consumers. This is especially true when there are complementarities in production or consumption. Antitrust policies that focus mainly on concentration may inhibit firms with a degree of market power from pursuing product design decisions that would actually enhance consumer welfare.

Given the possibility of pro-competitive and welfare enhancing aspects of tying, a rule of reason is preferred over per se illegality when assessing the benefits and costs of tying, especially in the technology sector. A thorough economic analysis of the efficiencies and consumer benefits should be included in any evaluation of tying, allowing the Commission to weigh any benefits against the charges of anticompetitive behavior. In fact, per se legality, tempered by empirical evidence may be the appropriate baseline.

2. Network Effects and Path Dependency

In the technology sector, networks and network effects have raised new issues for antitrust policy. In particular, with the dominance of large platforms, there have been concerns about the harmful effects of lock-in and path dependency. Some view these issues as anticompetitive practices that limit market competition to the detriment of consumers. Yet demonstrating these adverse outcomes can be difficult in practice. In fact, network effects can be pro-competitive and yield consumer benefits. It is therefore prudent for the Commission to carefully evaluate any claims of anticompetitive outcomes due to network effects. As Max Schanzenbach notes, "…network effects do not necessarily have clear cut implications for antitrust analysis, and strong affirmative defenses are possible when there is a charge of network predation."[7]

While network effects and lock-in have drawn the attention of economists and antitrust practitioners, the evidence of adverse impact has been limited. Consumers have demonstrated their willingness to abandon "path dependent" technologies for superior alternatives. Consider, for example, the transition from analog to digital music, or the many dominant platforms that no longer exist, including MySpace, AOL, and Blackberry, to name a few. Markets are dynamic and competition remains fierce, even in the face of a dominant platform as consumers search for the product that best serves their needs.

[7] Max Schanzenbach, "Network Effects and Antitrust Law: Predation, Affirmative Defenses, and the Case of *U.S. v. Microsoft*. *Stanford Technology Law Review*, vol 4., 2002, at http://stlr.stanford.edu/STLR/Articles/02_STLR_4

More recently, "big data" has been cited as a further source of market power that is anticompetitive and harms consumers. However, the empirical evidence has yet to demonstrate the anticompetitive effects of big data. As David S. Evans and Richard Schmalensee note: "The point isn't that big data couldn't provide a barrier to entry or even grease network effects. As far as we know, there is no way to rule that out entirely. But at this point there is not empirical support that this is anything more than a possibility, which one might explore in particular cases."[8] The Commission, therefore, should rely on a rule of reason and the application of empirical analysis when addressing claims of big data's adverse effects.

3. State Antitrust Enforcement

A number of legal scholars, including Richard Posner, have reviewed the role of states with respect to antitrust law, concluding that the duplicative nature of state antitrust actions with respect to federal antitrust actions can be burdensome and hamper the competitive process.[9] As the scope of competitive markets has expanded, responding to competition policy crafted by the various states in addition to the federal government can be costly and inefficient. Given both the legal and administrative burdens state antitrust laws can impose, the Commission should examine the potential impact of eliminating *parens patriae* suits filed by states attorney generals. If this is too much of a political challenge , the Commission can recommend limits on these lawsuits. For example, states can be preempted from pursuing antitrust lawsuits that have been addressed at the federal level. If a case has come before the Federal Trade Commission or the Department of Justice and it has been dismissed or pursued by the agency, then state attorneys general would be preempted from filing suit. This would focus scarce legal resources on their most efficient use while minimizing costs.

4. International Challenges to Competition Policy

Fueled by rapid advances in communications technologies and the inherently borderless nature of the internet, globalization has emerged as one of the central issues of our times. Not surprisingly globalization also has raised a number of formidable challenges and problems for the efficient application of competition law across borders. Pursuing international cooperation and harmonization of antitrust laws is becoming an import issue, and the Commission should work to ensure that, where possible, U.S. standards of antitrust laws are adopted.

Increasingly, the EU and other nations have adopted laws that have a significant impact on U.S. companies. If the Commission engages in efforts to harmonize antirust laws, it should advocate strongly for policies based on a standard of consumer welfare.

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[8] David S. Evans and Richard Schmalensee, "Debunking the 'Network Effects' Bogeyman, *Regulation,* Winter 2017-2018, pp. 36-39.

[9] Richard A. Posner, "Federalism and the Enforcement of Antitrust Laws by States Attorneys General," 2 *Georgetown Journal of Law and Public Policy* 5, 2004. .

Key areas of interest with respect to harmonization include merger reviews, predatory pricing, and monopoly leveraging. In all of these instances, a consumer welfare standard would promote efficiency and long-term economic growth.

There is a substantial body of research evaluating competition policy and the consumer welfare standard in the United States. The Commission should rely on this to promote all forms of competition in any proceedings on international convergence and harmonization.

Finally, it is worth reiterating a point raised by Carl Shapiro. Specifically, antitrust must remain focused exclusively on competition and long-term economic growth. Economic populism has pressed to transform antitrust into a tool for shaping broader social policies, from the political power of large corporations to income inequality. While these may be valid issues of concern, they are beyond the scope of antitrust policy. As Shapiro states, "…it is important to recognize that antitrust cannot be expected to solve the larger political and social policies facing the United States."[10] Antitrust is a mechanism designed for competition policy, and extending its use to achieve other policy objectives can harm consumer welfare, innovation, and economic growth. Antitrust laws should remain focused on consumer welfare, identifying the least-cost methods for enhancing consumer welfare and promoting long-run economic growth.

Respectfully submitted,

Wayne T. Brough

[10] Shapiro, Carl, Antitrust in a Time of Populism (October 24, 2017). Available at SSRN: https://ssrn.com/abstract=3058345 or http://dx.doi.org/10.2139/ssrn.3058345, p. 29.