Department of Justice

COMPETITION POLICY AND ECONOMIC EFFICIENCY:

PROVIDING THE FRAMEWORK

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Mr. Secretary-General, Chairman Stockmann, fellow members of the OECD committee on Competition Law and Policy, and distinguished guests, I am very happy to have this opportunity to address you this morning. I consider myself privileged to speak to you about antitrust policy, a subject that is crucial to the economic vitality of the United States and other countries.

I approach with some diffidence the prospect of talking about antitrust in the context of developing economies. I make no claim to being expert in the field of developmental economics; and I will not presume this morning to prescribe the wholesale incorporation of United States antitrust rules into the laws of nations whose economies are at a very different stage of development than our own.

On the other hand, it is sometimes said that in the United States antitrust is more than a set of laws, and more than an aspect of economic policy. Some observers have gone as far as describing the American belief in competition principles, embodied in our antitrust laws, as having almost a religious aspect. I readily admit to being a disciple of the faith in competition.

If U.S. antitrust policy can be said to have a summary text, it might be found in the words of the Supreme Court of the United States, when it said some 30 years ago that:

> The Sherman Act [-- the principal American antitrust law --] 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, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions. 1/

Although this statement of the aims of competition policy is an American one, the idea it expresses is broadly accepted among the OECD countries. But while some antitrust laws have been in place for as long as a century -- Canada celebrates the centennial of its law this year, and we will mark the 100th anniversary of our Sherman Act next year -- specific antitrust rules have continued to evolve, and will continue to do so. There has never been a more widely perceived need than there is today to assure that our competition policies are structured to promote their underlying goals. National policy makers are more conscious than ever that they operate in a world of scarce resources that must be efficiently used, and of international

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1/ Northern Pacific Railway Co., v. United States, 356 U.S. 1, 4-5 (1958).

competition that forces national industries to be more productive, more cost-effective, and more innovative than ever.

These are basic themes that other Symposium participants will develop in more detail. As I said a moment ago, I do not suggest that the U.S. approach, or any other single approach, provides a model that is perfect in all its details for adoption by developing countries. But I have no hesitation about recommending the competitive model as by far the best path to an efficient economy -- or about an antitrust framework along the lines of those that have evolved in the United States and other OECD countries as the best way of securing and preserving the competitive markets that are the best assurance of economic efficiency.

My aim this morning is to introduce four of the central concepts and critical choices of approach that define an antitrust framework: the structure of antitrust laws; competition policy and monopoly; treatment of agreements among competitors; and competition policy and other social goals. I will discuss these concepts from the perspective of the long U.S. experience with them.

The Structure of Antitrust Laws

One of the first decisions that policymakers have to make in enacting a competition law is what the law should look like. Should the law's language sweep broadly, or should it forbid or permit only precisely defined business conduct? OECD members take differing approaches to this question. The new Canadian competition law, for example, speaks with some precision to what conduct is illegal and what legal defenses are permitted. The U.S. antitrust laws, in contrast, broadly prohibit agreements "in restraint of trade" and monopolization, but do not define those terms, which obviously could be deemed to encompass a very wide range of business conduct.

The expansiveness of our statutory language has been praised by our Supreme Court for being written with a "generality and adaptability comparable to that found to be desirable in constitutional provisions." 2/ Conversely, this same expansiveness sometimes is criticized by confused businessmen who complain about having to hire expensive antitrust counsel to help them understand how this broad language applies to their particular business dealings. In any case, the unquestioned advantage of the U.S. approach has been to permit our courts and enforcement agencies flexibly to apply U.S. antitrust laws to the myriad business situations that

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2/ Appalachian Coals v. United States, 288 U.S. 344, 359-360 (1933).

legislatures could never hope to anticipate in narrowly-drawn statutes. Moreover, our approach has permitted us readily to adapt our antitrust policy to a changing economy on the basis of practical experience.

Competition Policy and Monopoly

Few concepts seem as antithetical to one another -- as a matter of both theory and experience -- as those of competition and monopoly. In the United States, the antitrust laws were an outgrowth of popular hostility to late 19th-century cartels that took the legal form of "trusts" -- hence the term "antitrust," which is universally understood as referring to laws that deal with anticompetitive conduct. You might be interested to know that much of the public passion of the day was directed at trusts that had been formed in the oil, corn and whiskey markets -- the last of these trusts, apparently, having been a particular threat to consumer welfare in late 19th-century America. The famous American general, William Tecumseh Sherman, once said "[w]ar is hell;" in 1890, his brother, Senator John Sherman, the chief sponsor of our first antitrust law, determined to ensure that U.S. markets would be, if not warlike, then at least competitive. As Senator Sherman warned, without antitrust legislation there would soon be "a trust for every production and a master to fix the price for every necessity of life." The law that emerged to deal with monopolies, Section 2 of the Sherman Act, outlawed monopolization, attempts to monopolize, and conspiracies to monopolize. Many OECD countries have more-or-less similar provisions in their laws dealing with abuse of dominant position.

It is important to observe that the Sherman Act and analogous provisions in other nations' laws do not prohibit a company from having a monopoly. A law designed to promote competition must, of course, allow for the possibility that a firm will be so much more efficient or innovative than its competitors that it will achieve a monopoly for those reasons alone. To punish such a firm would eliminate the incentives the law is designed to preserve.

Similarly, a law aimed at monopolization has to distinguish between conduct that is exclusionary and anticompetitive, on the one hand, and conduct that simply reflects aggressive competition, on the other -- even if that aggressive competitive behavior disadvantages less competitive firms or even leaves them unable to remain in the market. A fundamental and long-recognized principle of antitrust law, at least as it has evolved in the United States, is that its purpose is to protect the process of competition, not to protect individual competitors at the expense of efficiency and innovation.

The evolution of these rules in the U.S. is illustrated in the differing approaches to monopolization taken by a single U.S. appellate court over time. In the Alcoa decision of 1945 3/ -- a case that is perhaps known more widely abroad for having established the extra-territorial reach of U.S. antitrust law -- our Court of Appeals for the Second Circuit held that the Alcoa aluminum company had been guilty of monopolization, in part for expanding its capacity to meet anticipated demand. The court's opinion suggested that to avoid being guilty of monopolization, Alcoa should have restrained its capacity, in order to leave unfilled demand that would induce competitors to come into the market.

Thirty-five years later, that same court reflected a rather different attitude toward the kinds of competitive activities in which a firm with a dominant market share could legitimately engage. As the court said in the Berkey Photo case:

> A large firm does not violate section 2 simply by reaping the competitive rewards attributable to its efficient size. . . . So long as we allow a firm to compete in several fields, we must expect it to seek the competitive advantages of its broad-based activity -- more efficient production, greater ability to develop complementary products, reduce transaction costs, and so forth. These are the gains that accrue to any integrated

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3/ U.S. v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945).

firm, regardless of its market share, and they cannot by themselves be considered users of monopoly power. 4/

In other words, as time has passed, U.S. courts have come to a better understanding of the fact that when U.S. antitrust law looks at the big economic picture -- competition -- it will reach results more in keeping with its efficiency-enhancing purpose then if it fixates on short-term effects on individual competitors.

Agreements Among Competitors

Antitrust law provisions aimed at monopolization, or abuse of dominant position, are generally designed to prevent individual firms from gaining market power -- that is, power over price -- through anticompetitive means. Most competition laws have separate provisions aimed at anticompetitive agreements among two or more firms. In the United States, as I have noted above, Section 1 of our Sherman Act prohibits contracts, combinations and conspiracies in restraint of trade. Similarly, Article 85 of the Treaty of Rome prohibits agreements whose purpose or effect is to restrain competition.

4/ Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 276 (2d Cir. 1979), cert. denied, 444 U.S. 1093 (1980).

As in the case of laws on monopolization or abuse of dominant provision, the crucial task for competition policy in applying laws against anticompetitive agreements has been interpreting these provisions to distinguish between conduct or arrangements that restrain competition, and those that do not. The approach that has evolved in the United States has been to establish a category of agreements that, based on analysis and experience, restrain competition and are unlikely to serve any productive, efficiency-enhancing purpose. Agreements among competitors to fix prices, divide markets, or allocate customers are examples of conduct that falls into this category, and that is impermissible per se. No extensive case-by-case analysis of purpose or effect is required to establish that these practices, if they occur, are unlawful and, if we discover them, they will lead to criminal prosecution.

All agreements that are not unlawful per se are judged under what is referred to in U.S. antitrust law as the "rule of reason." The rule of reason, in its broadest and most general meaning, is simply the notion that a practice that has some potential for fostering competition or efficiency must be examined in context, with a view to its purposes and effects, to decide whether it amounts to an unlawful restraint of trade.

The terms "*per se*" and "rule of reason" are, I believe, used only in U.S. law; but the type of distinction they signify is reflected in the competition laws of many countries. And, as has been the case in the United States, views on what practices should be automatically condemned and what practices should be analyzed more fully have, over time, become more informed by experience and more economically sound.

The general tendency of U.S. courts and enforcement agencies has been to narrow the category of *per se* offenses and to broaden the category of conduct judged under the rule of reason. The reason for this trend is quite simple. There has been increasing and widespread recognition that some practices formerly condemned under the *per se* rule are not necessarily anticompetitive, but in fact may foster competition and create efficiencies.

To illustrate how competition policy has come to recognize efficiencies in arrangements that were once condemned as unqualifiedly anticompetitive, let me give a brief example from the U.S. courts. At one time, agreements between a manufacturer and its distributors limiting the territories into which the distributors could sell were considered unlawful *per se*. Our Supreme Court took this view in the 1960s, when it concluded that restraints of this kind unreasonably limited the distributors' freedom to sell goods they owned. 5/ Then, in 1977, the Court reconsidered its view and decided that it had been wrong. 6/ The Court realized that a manufacturer might want to provide its distributors with exclusive territories to induce them to promote its product more vigorously, and that doing so could benefit, rather than harm, consumers by increasing competition between different brands. In general, decisions by our Supreme Court since this 1977 Sylvania case have interpreted the antitrust laws in ways that further their fundamental efficiency-enhancing purposes.

Competition Policy and Other Social Goals

Up to now, I have talked about competition policy principles that are most likely to promote the objective of economic efficiency. There is a fundamental issue of a different kind, however, that any nation adopting or altering competition laws must face: how to deal with conflicts between competition policy and the competing demands of other policies

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5/ United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967).

6/ Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977).

and interests. What priority will competition policy have, and who will resolve the inevitable conflicts between competition and other interests? These are important choices that can significantly affect the extent to which competitive markets have an opportunity to work and to contribute to the health of one's economy.

The answers that the U.S. has given to these questions are clear. Competition is a -- indeed, the -- fundamental economic policy of the United States, and our Congress is presumed to have intended any legislated exceptions to this policy to be construed very strictly. By the same token, our courts, in interpreting the antitrust laws, are permitted to consider only competition concerns. They are not free to conclude that other social goals (*e.g.*, employment or international trade concerns) should be given greater weight in deciding a particular antitrust case.

But different choices are reflected in different antitrust regimes represented in this room. In the United Kingdom, for example, practices generally are condemned under competition law only if they are inconsistent with a broad "public interest" standard, although the government's policy is that competition effects are to be the predominant consideration. In the Federal Republic of Germany, the Federal Cartel Office is charged with making decisions exclusively on competition grounds, but in certain circumstances its decisions can be overridden by the Economics Minister on other economic policy grounds. Other OECD member states have made still other choices of criteria and have allocated decisionmaking responsibility in other ways.

I strongly believe that the priority given to competition policy as embodied in the antitrust laws is the right choice for the United States, and has benefitted us to an enormous extent over the years. Such a choice can have as great an impact on the effectiveness of one's competition policy as does the decision about which practices to permit and which to prohibit, and that it should be made with full awareness of that fact.

Conclusion

This morning, I have meant to share views with you, and not to preach a sermon. I hope that I have conveyed to you something of the antitrust tradition in the U.S., some of the antitrust policy choices that we have made and continue to face, and my own strong feeling that the century-old U.S. policy of insisting on unfettered competition has played a crucial role in enhancing the efficiency of the market economy upon which our economic prosperity is based. Thank you.