DEPARTMENT OF JUSTICE

The Role of Antitrust in Promoting Innovation

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It is a pleasure to be here today. Speaking here at King's College feels a bit like a homecoming. Before I started my current position as Deputy Assistant Attorney General at the U.S. Department of Justice's Antitrust Division, I spent last year here in London as the Director of the University of Notre Dame's London campus, located just a stone's throw away from King's College. I have many fond memories of participating in numerous events at King's College over the years. I join the King's College community in mourning the tragic and untimely death this week of your former law school dean, David Caron, who was a dear friend and colleague of mine.

I am delighted to be here to speak with you today about the topic of innovation. It is a key feature in the discussion of antitrust enforcement. As we all know, the pace of technological change is intense, so intense that many fear enforcers are having a difficult time keeping pace with the changes. In the early stages of innovation, the consequences cannot be fully predicted. One expects that new technologies will be welfare enhancing. But one also recognizes that sometimes new technologies may have unanticipated consequences. And sometimes new technology is consumer welfare enhancing, but also disruptive to incumbents who prefer the *status quo*. The dilemma, as one scholar put it, is that "technology changes exponentially, but social, economic, and legal systems change incrementally."[1]

Some societies approach technology with skepticism, favoring burdensome regulations on the belief that new disruptive innovations should be monitored closely, or even restrained. Other societies have created a legal culture that favors innovation, creating incentives for new technologies to flourish. Innovators recognize these different cultures and respond to the incentives and disincentives as one would expect. As one observer has noted, "innovators can,

[1]Larry Downes, The Laws and Its Enemies: Why People Resist New Technologies 2 (2009).

and will … move to those jurisdictions that provide a legal and regulatory environment more hospitable to entrepreneurial activity. Just as capital now fluidly moves around the globe seeking out more friendly regulatory treatment, the same is increasingly true for innovations."[2]

As we all know, entrepreneurs flock to Silicon Valley and similar innovation hubs because they perceive them to be cradles of creativity. But why? It is fascinating to ask what incentives motivate entrepreneurs around the world to choose one location over another. This point hit home for me this past December, when I was in Paris leading the U.S. delegation to an OECD Global Strategy Group on Digitalization. My placard read *Les Étas Unis*, and those around me from other OECD Member States wanted to talk about U.S. technology companies. There were various topics on the agenda, but there was one central theme: how should the world respond to leading U.S. technology companies? Everyone wants to examine them, many want to emulate them, and some want to regulate or even penalize them. In the current *zeitgeist*, it seems that technological innovation is both favored and feared.

When it comes to new frontiers, the first mover often is not the entrepreneur or the start-up company, but rather the city, province, or nation that promotes a culture of entrepreneurship and innovation.[3] Anticompetitive government regulations are like thousands of Lilliputian threads that tie down economies and stifle creativity. Those countries that have designed their laws and regulations to promote innovation and foster competition are the beneficiaries of innovation arbitrage. Entrepreneurs naturally will embrace warmer climates and avoid the islands of Lilliput that overflow with red tape.

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[2]Adam Thierer, Innovation Arbitrage, Technological Civil Disobedience, and Spontaneous Deregulation, Medium, (Dec. 7, 2016) available at https://medium.com/tech-liberation/innovation-arbitrage-technological-civil-disobedience-spontaneous-deregulation-eb90da50f1e2.

[3]Marc Andreessen, *Turn Detroit into Drone Valley: How To Build Innovation Clusters Beyond California*, Politico (June 15, 2014), available at https://www.politico.com/magazine/story/2014/06/turn-detroit-into-drone-valley-107853#ixzz3LQf5XIiD; Braden Allenby, *The Dynamics of Emerging Technology Systems*, in Innovative Governance Models for Emerging Technologies 33 (Gary E. Marchantet, eds. 2013).

It will not surprise you that according to recent studies, some countries and regions far outpace others in terms of a supportive entrepreneurial framework that encourages innovation. Government policies with respect to taxes and bureaucracy, market burdens, and the commercial and legal infrastructure are all among the critical components for creating an entrepreneurial environment. Recent surveys indicate that North America has the most supportive entrepreneurial conditions in the world, while in Europe, countries such as Estonia, the Netherlands and Switzerland lead the way in creating the conditions to support innovation. By contrast, other countries would be well advised to address their entrepreneurial frameworks if they wish to promote and maintain innovation.[4]

Although there are numerous factors that create a culture of innovation, proper competition law enforcement is a key component. Enforcing competition laws in a way that promotes innovation is something that we take seriously at the Antitrust Division of the Department of Justice. Competition enforcement plays an important role in supporting the free market system by maximizing efficiency, enhancing the integrity of the market, and ensuring the opportunity for everyone to compete on the merits.

One of the ways we are attempting to promote innovation and foster economic growth is by taking a fresh look at anticompetitive regulations. Last month, Assistant Attorney General Makan Delrahim announced a number of roundtables to address the intersection of antitrust law and deregulation. Among the roundtables that we have proposed is one dealing with the consumer costs of anticompetitive regulations. On the agenda is the question of how lawmakers can do a better job of ensuring that government action supports, rather than impairs, the operation of free markets. Another roundtable will focus on regulatory exemptions and

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[4] Global Entrepreneurship Monitor, Global Report 2017/18, 18 (2017), available at http://gemconsortium.org/report.

immunities to antitrust laws. Recognizing that antitrust laws enable markets with limited regulation, how should we view express or implied exemptions? A third roundtable will focus on deregulation with respect to antiquated antitrust consent decrees. What is the appropriate response to over 1,300 long-standing decrees on the books?[5]

Let me make a few comments regarding the relationship between innovation and merger review. As recent surveys indicate, the United States plays a major role in protecting markets from anticompetitive mergers, with seventy-one percent of the value of all frustrated deals in the world attributed solely to challenges by the U.S. competition agencies.[6] In the United States, we strongly believe that evidence-based assessment of anticompetitive harm should be conducted before we undertake to challenge a merger. And in doing that assessment, we recognize the many different ways that innovation plays a role in antitrust analysis – the differing effects a merger can have on incentives to innovate, as well as the effect innovation may have on the markets under review.

Antitrust law enforcement in the United States has long taken account of the range of potential competitive effects a merger may have on innovation. Our Horizontal Merger Guidelines provide a framework for analyzing when a merger is "likely to diminish innovation competition by encouraging the merged firm to curtail its innovative efforts below the level that would prevail in the absence of the merger."[7] Among the harms we consider under the Guidelines are reduced incentives to innovate in existing products and effects on incentives to develop future lines of business. On the other hand, the Horizontal Merger Guidelines also

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[5] Remarks of Assistant Attorney General Makan Delrahim at the New York State Bar Association (Jan. 25, 2018), *available at* https://www.justice.gov/opa/speech/remarks-assistant-attorney-general-makan-delrahim-delivered-new-york-state-bar.
[6] Allen & Overy, Global Trends in Merger Control Enforcement, 6 (Feb. 2018).
[7] U.S. DEP'T OF JUSTICE AND FEDERAL TRADE COMMISSION, HORIZONTAL MERGER GUIDELINES (2010), Section 6.4, *available at* https://www.justice.gov/atr/horizontal-merger-guidelines-0.

recognize that some mergers can enhance innovation by bringing together capabilities that could not otherwise be combined, by increasing a firm's ability to conduct R&D, or by enabling firms to enhance the benefits from their investments.[8]

Enforcers must ensure that their theories of innovation are tested against the factual evidence on a case-by-case basis. As our Guidelines suggest, the relationship between competition and the pace of innovation is complex. There is no one-size-fits-all approach to how a merger will affect innovation. In analyzing the likely impact on innovation in a particular case, the Antitrust Division looks at the factual and economic evidence. For example, is there evidence that pre-merger, the parties can produce better, faster or different solutions in response to a rival's innovation? Is there evidence that innovative efforts are largely duplicative? Do innovations quickly swing market share to the innovator? Or, are the innovations rapidly duplicated by others in the industry? These are just a few examples of the many questions we have explored in conducting merger reviews.

There are no shortcuts to answering these types of questions. Instead, they require factual investigation, including careful economic analysis, a review of relevant documents, and interviews of the parties, customers and competitors. We must assess the import of intellectual property with similar rigor. For example, patent counts can be misleading, as short-run differences that may signal an important advantage in one industry are irrelevant to another industry. And it can sometimes be difficult to associate patents with a particular business segment, let alone a particular product line. Without a fact-based investigation of the impact that a proposed merger will have on innovation, there is a significant risk that the enforcer will ask the wrong questions or reach the wrong conclusions.

[8] *Id.* at Section 10.

Enforcers must be willing to expose their conclusions on innovation effects to challenge. At the investigative stage, this means that at the appropriate time agencies should be transparent with the parties as to possible theories of harm. Moreover, as the investigation proceeds, we must be open to evidence that may challenge our initial conclusions. In the face of such evidence, sometimes we will reach a different result than we originally expected. For example, when the Antitrust Division reviewed the proposed merger of Expedia and Orbitz in 2015, we conducted a six-month investigation in which we reviewed tens of thousands of business documents, analyzed transactional data from the merging companies and from other industry players and interviewed over 60 industry participants.[9] After reviewing the evidence, however, we concluded that the transaction would not substantially lessen competition in online travel booking, in part because of new and emerging competitors who were innovating in the market. At other times the opposite occurs. After subjecting our theories to challenge we sometimes emerge from the investigation with a stronger case for harm.

Let me touch briefly on innovation in the context of digitalization and online platforms. There is no doubt that digitalization, including the aggregation and commercial use of large quantities of data, has created a multitude of dynamic product offerings that deliver incredible benefits to consumers. And there also is no doubt that these products are technologically complex and rapidly evolving. But there is no reason to think that the lessons we have learned over the past several decades about the role of antitrust enforcement in protecting and respecting innovation do not apply to the digital marketplace. Quite the opposite: there is a strong case to be made that years of consistent application of antitrust law, with innovation as a key concern, fueled the growth of digital companies in the first place.

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[9] Press Release, "Justice Department Will Not Challenge Expedia's Acquisition of Orbitz." (September 16, 2015), *available at* https://www.justice.gov/opa/pr/justice-department-will-not-challenge-expedias-acquisition-orbitz.

As in other contexts, when evolving technology is involved, evidence-based investigations are better than static, one-size-fits-all solutions. It is for this reason that we do not employ the term "Big Data." We view that term as ill-defined and vague, and too blunt to capture the nuances of the modern information-based marketplace. It is not even clear in the taxonomy of markets whether *Magnus Notitia* is a species, genus, or family. As Commissioner Margrethe Vestager has stated, it is important to keep the conversation complicated, because when you oversimplify the term "Big Data" you miss some of the real benefits and opportunities that it may have to offer.[10]

With respect to a firm's unilateral business conduct, if we abandon the approach of carefully assessing the facts on a case-by-case basis in favor of a one-size-fits-all approach that presumes anticompetitive effects simply because of the nature of the industry, there is a genuine risk of reaching the wrong conclusion. When a major antitrust agency rushes to judgment in challenging a digital market competitor, one can be confident that other agencies will follow in its footsteps. The price of a poor enforcement decision is not borne only by the companies under investigation, it is also borne by consumers, who suffer when incentives to innovate are diminished. So it is critical that we are careful in how we proceed in analyzing digital markets.

With perfect information, a competition agency would challenge only anticompetitive behavior and would never challenge pro-competitive behavior. But in the real world, there is sometimes informational uncertainty, which can pose risks of over-enforcement and under-enforcement. Sometimes promoting innovation means taking enforcement action. For example, the U.S.'s *Microsoft* case in 1998 illustrates that companies sometimes try to preserve their

[10] Competition Policy from a European Perspective: A Conversation with Margrethe Vestager, American Enterprise Institute (Sept. 18, 2017), *available at* http://www.aei.org/events/competition-policy-from-a-european-perspective-a-conversation-with-eu-commissioner-for-competition-margrethe-vestager/.

monopoly positions by excluding innovators that might displace their incumbency. As AAG Delrahim has emphasized, moreover, collusion among implementers of technological standards can push down patent licensing rates and thereby diminish incentives to innovate. In such cases, enforcing the antitrust laws protects not only consumers but also the incentives of innovators.

Harm to incentives to innovate is a particular concern where enforcers consider forced data sharing as a remedy. For this reason, U.S. antitrust law generally does not impose a duty to share one's assets with competitors. Whether the asset is data or intellectual property or another type of property, we need to be skeptical of the notion that companies have an overarching duty to deal with their competitors.

A brief word is also in order regarding the increased use of pricing algorithms and recent concerns that have been expressed in the antitrust community about the potential for easier or more effective collusion. Where firms agree to set their pricing algorithms to coordinate on price, this is a traditional Section 1 violation. This was the case, for example, in the DOJ's successful prosecution of the online Wall Décor cartel.[11] But in the absence of evidence of concerted action, we cannot presume the simple use of pricing algorithms is an antitrust violation. Any approach that bypasses proof of concerted action risks false prosecution of potentially pro-competitive pricing decisions. Misplaced enforcement efforts have the potential to discourage innovation and deter efficiency-enhancing pricing.

The need to ensure evidence-based decision-making throughout our enforcement activities is particularly acute when our goal is to protect innovation. Otherwise, we risk supplanting the functioning of the market with our own judgments. As we have learned time and again in antitrust law, there are significant adverse repercussions from an approach that discourages

[11] Press Release, "Online Retailer Pleads Guilty For Fixing Prices of Wall Posters," *available at* https://www.justice.gov/opa/pr/online-retailer-pleads-guilty-fixing-prices-wall-posters.

rather than incentivizes innovations. More intensive innovation contributes to higher competitiveness which in turn leads to higher per capita GDP and greater sustainable development.[12] So the stakes could not be greater in deciding whether or not we will enforce antitrust laws to promote innovation.

Thank you.

[12] Global Entrepreneurship Monitor, Global Report 2017/18, 40 (2017), available at http://gemconsortium.org/report