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DOES ANTITRUST HAVE A COMPARATIVE ADVANTAGE?

FRANK H. EASTERBROOK*

Until the 1970s antitrust law sorted all business practices into two bins. The practices in one bin were declared unlawful *per se*; the practices in the other were evaluated under the rule of reason, which as a practical matter meant that they were declared lawful *per se*, although the attorneys' fees incurred on the way to the ritual absolution were a hefty tax on the lawful conduct.

Per se rules came under attack on the ground that many of the condemned practices might be beneficial, making summary condemnation improvident. Since 1977 (a turning point marked by *Fortner II*,¹ *GTE Sylvania*,² and *Brunswick*³) courts have been willing to indulge explanations for conduct formerly condemned. In 1979, in the *Broadcast Music* blanket-license case,⁴ the Court adapted the *per se* rule to rule-of-reason analysis. That is to say, it inquired into the likely economic effects of a practice before deciding whether it really was the work of a cartel, or instead was beneficial to consumers. At the same time, the rule of reason also became a testing ground for explanations, so that in 1984 the Supreme Court finally declared an important business arrangement illegal under the rule of reason.⁵ Recent decisions continue this move from knee-

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1. *United States Steel Corp. v. Fortner Enters., Inc.*, 429 U.S. 610 (1977).

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

3. *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977).

4. *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1 (1979).

5. *See NCAA v. Board of Regents*, 468 U.S. 85 (1984). The same Term the Court continued what it had begun in *Broadcast Music*, applying a market-power filter, and thus a goodly portion of the rule of reason, to tie-in sales, formerly the domain of *per se* condemnation. *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2 (1984).

jerk reaction to detailed inquiry.⁶ Modern antitrust law thus is a search for economic explanations of problematic conduct. If the explanations show the conduct efficient—and therefore ultimately to consumers' benefit—then the court stays its hand; if not, the court condemns the conduct.

The dominant approach puts us at risk of losing sight of the impetus for *per se* rules: a belief that courts are not very good at divining the reasons for and effects of complex business practices, and a recognition that even when the courts can do this, it takes a long time, during which the problem often resolves itself.⁷ In corporate law the "business judgment rule" insulates most decisions from judicial review because there is little likelihood that systematic judicial intervention would make investors better off. Judges' decrees would increase the riskiness of business decisions without making decisions better. After all, judges are not selected for business acumen and are not penalized for bad decisions. We praise managers who hold the stock of the firms they manage, because this aligns managers' interests with investors' interests; managers and investors do well or poorly together. Self-interest is a powerful spur. A judge who bet on the astuteness of his business judgments by holding stock in the firms that appeared before him would be hustled off to jail. An essential ingredient of interest alignment in the business world is an impermissible lack of disinterest in the judicial world. So we do not trust judges to make business decisions in corporate law. Yet antitrust law now calls for the same sorts of economic judgments. We ought to be skeptical of judges' and juries' ability to give good answers. And this implies being skeptical of antitrust itself, beyond some simple rules such as do not collude.⁸

There is a large difference between corporate and antitrust law. Mistakes in managing a corporation generally harm only people who have elected to affiliate with the firm as investors,

6. See, e.g., *State Oil Co. v. Khan*, 522 U.S. 3 (1997); *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128 (1998); *California Dental Ass'n v. FTC*, 119 S. Ct. 1604 (1999).

7. The ill-fated IBM prosecution (1969-82) is a good example, but only one of many.

8. For two essays that elaborate some of the ideas presented here, see Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1 (1984); Frank H. Easterbrook, *Ignorance and Antitrust*, in *ANTITRUST, INNOVATION, AND COMPETITIVENESS* 119 (Thomas M. Jorde & David J. Teece eds., 1992).

suppliers, or employees. Managers who injure stockholders can expect to receive lower compensation, if not to be given walking papers. Blunders induce automatic penalties, to which legal processes could add little. The “market” — to personify a set of interactions that involve real people protecting their own interests — is the principal safeguard of investors. But managers who monopolize injure customers, who cannot retaliate readily. There are no automatic penalties. These effects on third parties justify a greater judicial role.

In deciding how much greater the role, however, we must inquire into comparative advantage. Comparative advantage in economics means an advantage relative to the cost of the next best alternative. I know a lot about computers, so I can diagnose and fix hardware problems; I may be able to do this in less time than it takes the automation staff at the court. Nonetheless, when my machine breaks I will turn it over to specialists because they have a comparative advantage. If I were to fix the computer, I would have to stop working on opinions and articles; the cost of fixing the machine myself is the loss of whatever else I could accomplish during the time. The value of the hours I would surrender may well be greater than the value (in alternative uses) of the time it takes the computer shop to fix my machine, even if the shop takes more time than I would. So specialists have a comparative advantage over me in fixing computers.

Likewise, although judges may be able to fix markets when they are monopolized, other social institutions may have a comparative advantage. The principal competing institution is the actions of business rivals. If there are monopoly profits to be made, rivals enter the market (or expand their production) and undercut the monopolist. No one doubts that this occurs. The question is, “How long does it take?” Competition is the long-run solution to monopoly. On rare occasions this may not work. Unless we know that it fails, however, judges ought to apply their talents in other fields, where they have a comparative advantage over other institutions. And here’s the big point: *by and large, we can’t know when competition has “failed.”*

Expressing the extent of the law’s comparative advantage over rivalry in undercutting monopoly requires the use of the

social scientist's terms "false positive" and "false negative." If a judge wrongly condemns as monopolistic a business practice that is efficient and beneficial to consumers, that is a false positive. Consumers would be better off if the judge had decided the case the other way. If the judge wrongly excuses conduct that is harmful to consumers, that is a false negative. Litigation produces both false positives and false negatives. The more complex or unusual the conduct, the more false positives and false negatives there will be. And of course the more complex the conduct and the scarcer our knowledge of its consequences, the longer the case will take to conclude, and the more it is apt to cost along the way. All the while competitors will be trying to undercut monopolists.

For the law to have a comparative advantage, legal processes must be able to beat market processes to a conclusion in assessing novel business practices. If rivals will undo a monopoly or evade a questionable practice before judges can decide the case, there is little point in incurring the costs of litigation and suffering the inevitable mistaken judgments. (I make an exception for local price-fixing cartels, say in construction markets. These may be stable and resist outside competition because the social relations among the conspirators enable them to resist the urge to cheat.)

If the business practices are long-lived, courts have a comparative advantage only when false positives are few and false negatives will survive competitive pressure. Unless there is a strong reason to suspect that a monopoly or monopolistic practice can survive the attempts of other firms to undermine it, then the costs of inaction (excusing harmful conduct) are low. Unless there is strong reason to suspect that we can identify harmful conduct accurately, then the costs of action (condemning beneficial conduct) are high.

The conditions for useful legal intervention may be met when we know a lot about the practice and can condemn or approve it out of hand. But when we know but little the risk of error goes up, and the risk of false positives may be substantial. People are quick to condemn what they do not understand. Hasty or uninformed judgments may condemn novel practices just because of their novelty. Often it takes a decade or more to determine what a business practice really does. The law moves

too fast for our own good, because courts act in advance of the explanation. Judges move slower than markets but faster than the economics profession, a deadly combination.

It may be prudent for a court to act on limited knowledge if a mistaken condemnation can be washed away as easily as the contrary error would be. Yet there is a bias in the error-correcting devices of the law. Mistakes of *law* are not subject to competitive pressures. If a judge errs in saying that the NCAA's contract with the TV networks for college football is a violation, there is no competitive way to undermine the decision, as there might be a competitive way to undermine the contract. Once the court speaks, the contract is gone. If the prohibition was mistaken, we shall suffer the consequences indefinitely. So, too, if the Supreme Court announces a rule such as the "filed rate doctrine," under which a cartel price is beyond challenge if reflected in tariffs filed with the ICC, or the rule of *per se* illegality for resale price maintenance, there are no automatic market pressures that test the wisdom of the rule. Quite the contrary. After some years have gone by, the Court is apt to declare the rule exempt from further scrutiny.⁹

Law has a comparative advantage over markets, then, when legal processes are rapid, when false positives are rare (or quickly corrected), and when markets are sluggish about correcting false negatives. These criteria are met for naked cartels (which may be condemned quickly and with great assurance that condemnation is appropriate) and for large mergers in markets with serious barriers to entry (the market power from which may take a long time to erode through competitive pressure). They are not met for novel business practices—those that courts are encountering for the first time. The rate of false positives may be particularly high because cases arrive in court ahead of explanations for the practices. It is easier to call practices "abuses" than to understand the real economic effects of novel arrangements. Courts can see the wounded plaintiffs but not the beneficiaries.

9. *See, e.g.,* Square D Co. v. Niagara Frontier Tariff Bureau, Inc., 476 U.S. 409, 424 (1986) (holding the "filed rate doctrine" inviolate). This is not to say that cases are never overruled. *GTE Sylvania* and *State Oil*, referenced above in notes 2 and 6 respectively, are among the handful. But it is to say that these overrulings are few, and that they do not respond to market pressures. Monopoly prices are eroded because of rivals' self-interest; there is no equivalent invisible hand in law.

The difficulty is particularly great in the realm of exclusionary practices. I can't talk about the Microsoft case, which everyone else is eager to discuss, so I invite you to think about *Aspen*,¹⁰ in which the dominant ski lift operator in Aspen changed the terms on which a competing operator's mountain was included in a joint, resort-wide lift ticket. Aspen effectively reduced the rival's share of revenues from the joint ticket, making individual-mountain tickets more attractive to the rival. The jury found this exclusionary and illegal. We should be very suspicious, for the simple reason that we—meaning judges, lawyers, economists, and other professions taken together—know very little about such joint selling arrangements. False positives are apt to be frequent, and it is difficult to undo mistaken condemnations. It is easy to see, however, how a decision like *Aspen* could discourage businesses from entering into beneficial joint operations for fear that they would be exposed to antitrust liability if they should withdraw or change the terms.¹¹

It is also frightening to contemplate businesses using liability for competition as a justification for making or retaining monopolistic joint arrangements—as a form of “mandatory cartelization defense.” As Professor Areeda wrote about *Aspen*: “[t]he monopolist's intent to keep as much of the market as he can for himself is not the kind of exclusionary intent that automatically converts ordinary and useful behavior into unlawful monopolization.”¹² Antitrust law need not contain a bias, with per se rules working only in plaintiffs' favor. If practices that are harmful in eighty percent of the cases should be unlawful per se, then practices that are beneficial in eighty percent of the cases should be lawful per se. More discriminating analysis should be reserved for the rare intermediate case. The practice that is passed over by a rule of per se legality, the false negative, can be taken care of by business rivals. This is the sort of situation in which market forces have a comparative advantage over courts.

10. *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985).

11. This fear explains the decision in *Olympia Equipment Leasing Company v. Western Union Telegraph Co.*, 797 F.2d 370 (7th Cir. 1986), which read *Aspen* narrowly.

12. Phillip Areeda, *Monopolization, Mergers, and Markets: A Century Past and the Future*, 75 CAL. L. REV. 959, 965 (1987).