Welfare Standards in U.S. and E.U. Antitrust Enforcement

Roger D. Blair
D. Daniel Sokol

University of Florida Levin College of Law, sokold@law.ufl.edu

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The potential goals of antitrust are numerous. Goals matter to antitrust. We believe that it is total welfare rather than consumer welfare that should drive antitrust analysis. We use this Article as an opportunity to explore both a comparative analysis of welfare standards across E.U. and U.S. competition systems and the impact of welfare standards on global antitrust systemwide welfare.

In this Article, we analyze two types of situations in which there would be a different outcome based on the goal implemented. One scenario involves resale price maintenance (RPM). For RPM, we argue that even if there were a different welfare standard across jurisdictions as between Europe and the United States, in practice, it would have very little global impact. The second scenario involves merger control. We analyze a divergence in welfare standards between merger regimes where the use of efficiencies might play out differently across Europe and the United States depending on the welfare standard used. Under this second scenario, the welfare standard matters globally as to business outcomes in a way in which it does not under the first scenario. If one major merger regime blocks the merger, it effectively blocks the merger globally. Finally, we provide our concluding thoughts on the future and desirability of convergence around total welfare as the sole goal in the practice of competition economics globally.
INTRODUCTION

Goals matter to antitrust.1 While proponents of antitrust (in the United States) and competition law (most of the rest of the world) may have had multiple goals when initially enacting legislation,2 two goals predominate modern academic and policy discourse: total welfare (the overall surplus from producers and consumers) and consumer welfare (the surplus only from consumers).3 Much of the time these goals are indistinguishable in practice, because behavior that violates antitrust law often reduces both consumer and total welfare. However, there are certain situations in which the behavior in question violates only one of these goals. In those situations, the goal selected matters to the execution of antitrust law, particularly when there are not per se legal rules regarding legality or illegality.4

1. ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 50 (1978). Ambiguity about the goals (a distinction between rules and standards) or inconsistency among goals may be costly. Indeed, divergence among standards across countries is costly, and we believe that total surplus is the superior standard.


3. We note that there is a difference between welfare and surplus, but we use the term “welfare” as shorthand throughout this Article because the debate has been framed as between consumer welfare and total welfare. For a discussion of the difference between welfare and surplus, see Barak Y. Orbach, The Antitrust Consumer Welfare Paradox, 7 J. COMPETITION L. & ECON. 133 (2010).

4. See Roger D. Blair & D. Daniel Sokol, The Rule of Reason and the Goals of Antitrust: An Economic Approach, 78 ANTITRUST L.J. 471, 498–502 (2012) (providing examples of joint ventures, mergers, bilateral monopolies, physician cooperative bargaining, all-or-none offers, two part pricing, and bid rigging in English auctions, in which a different welfare standard may lead to divergent outcomes for the same type of behavior).
As we have argued elsewhere, we believe that it is total welfare rather than consumer welfare that should drive antitrust analysis. This is not a new position within antitrust scholarship. Indeed, it seems to be the dominant one. Under a total welfare standard, any behavior that reduces total welfare would be deemed unlawful, whereas any behavior that does not would be lawful.

As part of the total welfare analysis, we utilize the Kaldor-Hicks compensation principle to assess the impact that various practices would have on total welfare. The strength of Kaldor-Hicks is its ability to provide an economically sound methodology for separating objectionable and unobjectionable business behavior. For example, a merger may be Kaldor-Hicks efficient if the winner (the monopolist) is able to compensate the loser (consumers) and still have profits left over.

Welfare standards within antitrust have been studied in great depth within a single jurisdictional setting. Most of the time, the battle over welfare standards has been overblown, and there is no difference in outcome. We use this Article as an opportunity to explore both a

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5. See generally id.


8. See Blair & Sokol, supra note 4, at 483–89.

comparative analysis of welfare standards across E.U. and U.S. competition systems and the impact of welfare standards on global antitrust systemwide welfare. This analysis provides an opportunity to discuss situations in which the difference between different standards—consumer versus total welfare versus non-antitrust political factors—may lead to disparate outcomes. The analysis’s comparative element is distinct from its international element in that a difference across antitrust systems may have a global impact. When there is a disagreement across antitrust regimes as to welfare standards that have global impact, there may be, for example, behavior that is forbidden even when it enhances total welfare globally and should be permitted based upon the strictest major antitrust jurisdiction to review the merger. This is only a small set of situations, most notably efficiencies in a merger or joint venture context. Most of the time, the welfare standard does not matter.

In any discussion across legal systems about the goals of antitrust, one must ask if there is substantive convergence, and if there is, is it a good thing. The answer to the first question is both yes and no. There is some global substantive convergence around the goals of antitrust. We believe that this convergence is happening around a narrow competition economics vision of the goals of antitrust, as we explore in Part I.

The process of antitrust convergence across countries is not easy. Institutional structures are a function of both the time in which they were set up and the institutional development based upon this initial endowment. This creates path dependence to institutional development that makes the integration of new learning more difficult for some antitrust


11. For a general conceptualization of regulatory competition, see Francesco Parisi et al., Two Dimensions of Regulatory Competition, 26 INT’L REV. L. & ECON. 56 (2006).


systems (primarily agencies and courts) than others. Different path dependencies complicate the possibility of convergence across systems for any potential singular goal of antitrust.

Consequently, a number of factors are at play regarding antitrust convergence. Law matters, macro level political economy factors matter, as do the quality and ability of courts and agencies to shape doctrine into policy. In the European Union and United States comparison, a number of developments in the U.S. institutional framework are different from those of Europe. They include private treble damages, a robust system of class actions, and a judicial-based enforcement system (unlike the European administrative-based competition system).

Private remedies do not exist in a meaningful way in Europe, which might explain stronger E.U. remedies by government enforcement if one assumes that total enforcement (public and private) should be roughly the same between the two jurisdictions.

Other factors also shape the institutional path dependency of antitrust. To a certain extent, it is history and politics, rather than efficiency, that explain divergent antitrust systems, although economics’ application to antitrust also plays a role. For example, many of the assumptions in the

24. See DAVID J. GERBER, GLOBAL COMPETITION: LAW, MARKETS, AND GLOBALIZATION (2010); DAVID J. GERBER, LAW AND COMPETITION IN TWENTIETH CENTURY EUROPE: PROTECTING PROMETHEUS (1998); Arthur, supra note 21. There is a similar discussion in
United States and its antitrust system—with a history of limited government regulation and a dearth of state ownership—do not provide a direct analogy to the competition regimes in Europe, which had more state intervention. European competition law also has specific provisions regarding state aid\(^{25}\) (subsidies) and provisions specific to public undertakings.\(^{26}\)

An additional policy, unique to the supranational nature of the European Union, adds richness to European competition law goals. The initial focus of the European competition system and European Union overall was to integrate the economies of the member states. Moreover, competition policy in Europe has had a more distributive flavor than its American counterpart. There has been far more concern in European case law about choices for consumers,\(^ {27}\) even if preserving choice has translated into enforcement policies that disfavor more efficient competitors.\(^ {28}\)

We recognize that institutions vary and that the current set of institutions both within the United States and European Union (let alone other competition systems) are not easily calibrated to ensure that total welfare could be utilized as the singular value of antitrust/competition law. Indeed, if anything, it seems to be consumer welfare that is the standard on which there is increasing international convergence. However, the purpose of this Article is to note that, because of the misalignment of institutional capabilities and goals, certain fault lines emerge between competing economic goals of antitrust as well as between political and economic goals. We articulate where these fault lines are currently. We also note corporate law regarding comparative corporate governance systems. See Mark J. Roe, Strong Managers, Weak Owners: The Political Roots of American Corporate Finance (1994) (describing a political and historic view of what shapes corporate governance in the United States); Donald C. Clarke, "Nothing but Wind"? The Past and Future of Comparative Corporate Governance, 59 AM. J. COMP. L. 75 (2011) (providing an overview of comparative corporate governance scholarship); Mark J. Roe, Legal Origins, Politics, and Modern Stock Markets, 120 HARV. L. REV. 460 (2006) (explaining comparative corporate governance through political economy and historical factors); Andrei Shleifer & Robert W. Vishny, A Survey of Corporate Governance, 52 J. FIN. 737 (1997) (discussing how law matters to corporate governance).

25. Consolidated Version of the Treaty on the Functioning of the European Union art. 107, Mar. 3, 2010, 2010 O.J. (C 83) 91 [hereinafter TFEU] (limiting "any aid granted by a Member State . . . in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the internal market"). For analysis, see Kelyn Bacon, European Union Law of State Aid (2d ed. forthcoming 2013).


particular situations in which a divergence of welfare standards either matters or does not matter globally.29

This Article analyzes the United States and European Union because at present, global antitrust is bipolar. That is, a global business strategy that one of the U.S. antitrust agencies or the European Commission (EC) successfully challenges may have global repercussions and may spell the end to such a strategy in ways that would not be true if other jurisdictions were to challenge a global deal. Future growth of Chinese and possibly Indian economic power may impact the antitrust setting.30 The result may be the creation of a multipolar world of antitrust for which a successful agency action by either the United States, Europe, India, or China may derail a business strategy whether it be via conduct or merger.31

Part I of this Article discusses the importance of the development of economic analysis in U.S. and E.U. competition law to better explain how the choice of an economic welfare standard has fundamentally become the choice of a goal for antitrust/competition law. This discussion sets up our substantive analysis of goals, where we analyze two types of situations in which there would be a different outcome based on the goal implemented. In Part II, we discuss the first scenario. This scenario involves resale price maintenance (RPM). For RPM, we argue that even if there were a different welfare standard across jurisdictions, it would have very little global impact. In Part III, we analyze the question of different global standards with regards to merger control. In this second scenario, we analyze a difference in welfare standards between merger regimes where the use of efficiencies might play out differently between the European Union and the United States depending on the welfare standard used. Under this second scenario, the welfare standard matters globally as to business outcomes in a way that it does not under the first scenario. If one major merger regime blocks the merger, it effectively blocks the merger globally.32

29. Conceptually, total welfare of a given country actually means the sum of consumer surplus and domestic firms’ profits. See, e.g., Pedro P. Barros & Luis Cabral, Merger Policy in Open Economies, 38 EUR. ECON. REV. 1041 (1994). If, however, the consumer welfare standard is adopted, then all firms should be treated equally.


32. See Sokol, supra note 15, at 1094 (“On an international level, a key concern is when one of the major powers in antitrust, the European Union or the United States, has a lower standard for a finding of wrongdoing than other countries. The lower standard effectively operates as the global standard because remedies often have global implications.”); D. Daniel Sokol, Monopolists Without Borders: The Institutional Challenge of International Antitrust in a Global Gilded Age, 4 BERKELEY BUS. L.J. 37, 62 (2007) (“A single country
provides our concluding thoughts on the future and desirability of convergence around total welfare as the sole goal in the practice of competition economics globally.

I. ECONOMIC ANALYSIS IN ANTITRUST VERSUS OTHER GOALS AND DIFFERENCES BETWEEN THE UNITED STATES AND THE EUROPEAN UNION

This part explores the importance of goals in the implementation of antitrust law and policy. It begins with an overview of the different types of goals in antitrust. It then examines the shifts in goals over time in both the United States and Europe. In the long run, antitrust goals have narrowed to ones based on industrial organization economics. This is without question the current state of play in the United States. In Europe, the shift to industrial organization economics based goals is less well developed.

A. Goals

The potential goals of antitrust are numerous. Moreover, the goals of antitrust in any given antitrust system may change over time.33 A current snapshot of the different goals of the International Competition Network (ICN) members shows the diversity and, at times, overlapping or conflicting nature of the goals of antitrust. These goals include: ensuring an effective competitive process, promoting consumer welfare, enhancing efficiency, ensuring economic freedom, ensuring a level playing field for small and mid-sized enterprises, promoting fairness and equality, promoting consumer choice, achieving market integration, facilitating privatization and market liberalization, and promoting competitiveness in international markets.34

Noneconomic goals may play a role in some antitrust regimes. This discussion is similar to the choice of goals in economic regulation generally. There may be other areas of economic regulation in which other legitimate factors get included in the goal. Regulation frequently seeks to address issues relating to externalities, health and safety, industrial policy,
distributive justice, or financial stability among others. At times, some of the goals are prone to risk of capture and present problems familiar within the public choice literature. It is just that these other regulatory goals are not considered in an industrial organization antitrust analysis, nor do we think that they should be.

We believe that there are better mechanisms for achieving distributive effects than antitrust. By distributive goals within antitrust, we mean either distributive goals via the implementation of a consumer welfare standard or through justifications that are not economics based within antitrust law. Other mechanisms for distributive concerns, such as taxation, would be more effective. As for the achievement of multiple goals that include the promotion of competition concurrently with goals that may be pursued through sector regulation, we believe that sector regulation is better suited to address political tradeoffs because of its broader goals, such as "public interest," than is antitrust.

Antitrust, as practiced in the modern, advanced jurisdictions, is more predictable and better able to produce welfare-enhancing results than a system based upon public interest concerns, in which interest group clashes may predominate. This economic effects based form of antitrust is antitrust technocracy. We prefer that the antitrust system be technocratic in the sense that antitrust be defined narrowly to examine only those issues that are purely within antitrust's ability to be measured and understood using industrial organization as the basis for economic analysis. This technocratic approach moves noncompetition economic considerations to areas such as sector regulation, the legislative process, or executive fiat. Such areas are better equipped than antitrust to deal with political trade-offs between law

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and policy because of their ability to deal with conflicting policy issues, whether based on legitimate goals or rent seeking.

There has been, and continues to be, convergence around the use of industrial organization/competition economics as the basis for the analysis of competition law/antitrust. We believe that it is merely a matter of time until all of the major established antitrust regimes come to a point in their institutional and case law development in which the only choices among the goals of antitrust will be industrial organization based goals of total and consumer welfare. Essentially, nonindustrial organization economic goals and political goals will be pushed so far to the margin as to become inconsequential. Developments to date suggest that this movement has not been uniform, but the trend in many countries suggests that this is in fact what is occurring.

B. U.S. Goals

In the United States, several goals have defined antitrust law as it has developed, from those of the Sherman Act to the goals contained in current case law and agency thinking. Over time the discussion of the goals of antitrust has shed its overtly political elements in favor of goals that are based on different economic welfare standards, largely as a result of the Chicago Revolution.

U.S. competition law enforcement and the institutions that support it are evolutionary. The evolution occurs along a number of dimensions, such as shifts in judicial interpretation, economic thinking, and government policy. The evolution of antitrust policy is a complex process influenced by various factors, including economic theories, judicial interpretations, and political considerations. The evolution of antitrust policy is a dynamic process that continues to shape the legal landscape of competition law.


41. However, it remains unclear whether different antitrust systems will choose total welfare, the policy choice we believe to be superior. This is the subject for a different article.


44. See Bork, supra note 1.

As the antitrust statutes are purposely vague, courts have developed and refined antitrust jurisprudence through the common law and have increasingly used economic analysis to drive this refinement.

The judiciary is a key player in the U.S. antitrust system through its review of antitrust cases. By reviewing agency actions, the judiciary has power to ensure that legal actions are upheld and enforced through injunctive relief, disgorgement, and financial penalties. The more recent focus on economics has reduced the areas of per se illegality and increased the areas where the rule of reason operates because of procompetitive justifications for the business behavior. A similar move has been underway in the merger control area.

With a shift to the rule of reason, courts now provide more in-depth analysis. But even these courts have failed to understand how critical the welfare standard is in this analysis. Thus, given the welfare standard, courts (including the Supreme Court) remain confused as to how to implement the rule of reason. This confusion creates circumstances in which the use of a different welfare standard might lead to a divergent outcome as between total and consumer welfare.

As a result of shifts in agencies and courts, sophisticated economic analysis is now at the forefront of antitrust in the United States. Perhaps

48. See Kobayashi & Muris, supra note 43, at 152–53 ("One result of the incorporation of economics into antitrust law has been the widespread rejection of broad rules of per se illegality.").
50. The prohibitions in sections 1 and 2 of the Sherman Act appear to be both categorical and uncompromising: "Every contract, combination in the form of trust or otherwise, or conspiracy" that restrains trade appears to be condemned under section 1. 15 U.S.C. § 1 (2006). "Every person" who monopolizes a market appears doomed by section 2. Id. § 2. But the Supreme Court soon recognized that a literal interpretation of the statutory language was both unwise and unworkable. The test of illegality quickly centered on "reasonableness." In United States v. Joint Traffic Ass'n, 171 U.S. 505, 558–60 (1898), a section 1 case, and Standard Oil Co. v. United States, 221 U.S. 1, 81–82 (1911), a section 2 case, the Court found only unreasonable restraints or business practices to be unlawful under the Sherman Act. This, of course, raises the obvious question of how reasonableness should be determined; that is, what benchmarks or standards should be used to distinguish the reasonable from the unreasonable? For the contemporary analysis of the rule of reason, see, for example, Andrew I. Gavil, Moving Beyond Caricature and Characterization: The Modern Rule of Reason in Practice, 85 S. CAL. L. REV. 733 (2012).
51. See Blair & Sokol, supra note 4, at 474–81.
52. Liran Einav & Jonathan Levin, Empirical Industrial Organization: A Progress Report, 24 J. ECON. PERSP. 145, 152 (2010) ("Thirty years ago, it was common for antitrust arguments to rest on simple summary measures of industry structure such as concentration
unique among legal fields, antitrust is one in which the Supreme Court regularly cites not merely to law journal articles that employ economic analysis but to economics journal articles. In its 2007 *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* decision, the Supreme Court cited to an economic textbook and articles from the *Journal of Law and Economics, RAND Journal of Economics, Quarterly Journal of Economics,* and the *Journal of Political Economy.*

One anecdote illustrates the change within the United States perhaps better than any other. When Richard Posner wrote his antitrust book in 1976, its title reflected the tension within antitrust legal scholarship and policy of the time. Its title was *Antitrust Law: An Economic Perspective.* This was a provocative title. As one prominent scholar wrote in his review of the book, "[Posner’s *Antitrust Law*] comes at a time when the limits of traditional microeconomics as a tool of antitrust policy have become starkly apparent, limitations which suggest that antitrust law should be moving outside the economist’s world rather than burrowing more deeply into it." By the time of the second edition in 2001, Posner’s title had been abridged to *Antitrust Law.* The economic revolution was so complete that all antitrust analysis has become economics based and it was superfluous to mention the economic perspective in the title.

The change in discourse to one based on economics has framed antitrust scholarship such that any goal other than total welfare must be framed within an economic analysis lens. Many of those who embrace a consumer welfare standard may do so based on their broad reading of the multiple ratios and Herfindahl-Hirschman indices. Nowadays, the Department of Justice and the Federal Trade Commission, which are tasked with reviewing proposed mergers, commonly undertake sophisticated econometric studies to define industry boundaries and to assess the likelihood of price increases or collusive behavior following a merger. These exercises often draw on academic research, and in turn have motivated the development of new empirical models.); Vivek Ghosal, *Regime Shift in Antitrust Laws, Economics, and Enforcement,* 7 J. COMPETITION L. & ECON. 733 (2011) (providing empirical support of the shift to economic analysis); Barak Orbach & D. Daniel Sokol, *Antitrust Energy,* 85 S. CAL. L. REV. 429, 439 (2012) ("The evolution of antitrust has been shaped by changing lines of economic thinking and ideologies.").

54. *Id.* at 890–92, 921.
57. *See* POSNER, supra note 6.
goals of antitrust.\textsuperscript{60} From its inception, there were numerous goals of the Sherman Act. As noneconomic goals of antitrust have been removed from the U.S. discussion as a result of the ascendancy of the Chicago School, the ideological fight over promotion of economic goals versus other goals has given way to a debate about different economic conceptualizations of welfare effects that approximate the more "populist" notions of competition within an economics framework. In this current populist formulation, it is consumer welfare that would be maximized at the expense of producer-and-consumer welfare.

\section*{C. E.U. Goals}

There is a rich literature of the goals of European competition law.\textsuperscript{61} Though in the space of this Article we cannot do justice to various approaches suggested, for purposes of this Article we do not need to. We merely note that there is a difference in how competition law has been conceptualized in Europe (and we exclusively deal with the E.U. level rather than at the level of national competition authorities) and the various goals to which competition law has been and continues to be applied. We

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provide a basic overview merely, first, to set up our discussion of how different goals may have an international dimension when goals are not aligned and, second, to note what seems to be an increasing (though still somewhat nascent) shift to a true consumer welfare standard.62

Unlike in the United States, the divide in Europe has not been between total welfare and consumer welfare.63 Instead, the divide is between different visions of competition—one based exclusively upon industrial organization economics versus a mix of industrial organization economics and noneconomic political goals. The latter mix encompasses an industrial policy that favored European over non-European firms64 and a focus on "fairness" that includes competitor effects and consumer choice.65 E.U. competition law is one of a number of competing goals under the treaty and these are bound together by the single market imperative.66 It was also influenced by the Ordo-Liberal tradition.67

Although there is no explicit discussion of the goals of antitrust within the current Treaty Establishing the European Community or its predecessors,68 the Lisbon Treaty overall has certain goals, such as a unified market, that at times work within a traditional competition economics analysis for antitrust goals but at other times might lead to a divergence.69 Some of these important factors suggest a focus other than consumer welfare.70 However, since the E.U. competition system has been modernized to reflect, among other things, an analysis more heavily based on economics, the focus increasingly has been on consumer welfare,71 even

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62. Bork sowed significant confusion with his use of "consumer welfare," which in his formulation was not consumer welfare at all but total welfare. See BORK, supra note 1, at 81–115.
63. But see NAZZINI, supra note 61, at 102 (arguing that dominance in Europe is based on a total welfare goal).
65. See TFEU pmbl.; see also id. arts. 119–120. For academic commentary, see AMATO, supra note 61, at 2 (discussing consumer choice) and DAVID J. GERBER, LAW AND COMPETITION IN TWENTIETH CENTURY EUROPE: PROTECTING PROMETHEUS 37–38 (1998) (discussing the ordoliberal tradition and fairness). There is a certain similarity between these conceptualizations and that of U.S. cases that have now been discredited such as Brown Shoe Co. v. United States, 370 U.S. 294 (1962).
66. This is reflected in the fact export bans (i.e., preventing a distributor in one member state from selling to customers in another) are treated as an 'object' agreement (as serious as price fixing).
68. Laura Parret, The Multiple Personalities of EU Competition Law, in THE GOALS OF COMPETITION LAW, supra note 37, at 61, 63.
69. GERBER, supra note 65; VAN ROMPUY, supra note 61.
70. Parret, supra note 68, at 64–74.
71. For a general discussion, see PINAR AKMAN, THE CONCEPT OF ABUSE IN EU COMPETITION LAW: LAW AND ECONOMIC APPROACHES (2012). For a discussion on both procedural and substantive modernization, see David J. Gerber, Two Forms of
if some suggest that a consumer welfare rationale within European competition law might be at odds with the European Community Treaty.\textsuperscript{72}

To the extent that the case law is shifting (as opposed to agency decisions, guidelines, and discussion papers), the move to a serious economic analysis is still at an early stage. To our knowledge, the first time that the European Court of Justice (ECJ) ever used the term "consumer welfare" was in its \textit{Post Danmark A/S v. Konkurrencerådet} ruling of 2012.\textsuperscript{73} While Pinar Akman's impressive work argues that total welfare was closer to what the drafters had in mind when they drafted the Treaty provisions,\textsuperscript{74} this interpretation of the goal of European competition law remains a minority position.\textsuperscript{75} It also seems not to have been adopted by E.U. case law. Rather, most court decisions formulate the goals of E.U. competition law differently. In \textit{GlaxoSmithKline Services v. Commission},\textsuperscript{76} the ECJ noted:

62. With respect to the Court of First Instance's statement that, while it is accepted that an agreement intended to limit parallel trade must in principle be considered to have as its object the restriction of competition, that applies in so far as it may be presumed to deprive final consumers of the advantages of effective competition in terms of supply or price, the Court notes that neither the wording of \textit{[Treaty on the Functioning of the European Union (TFEU) 101(1)]} nor the case-law lend support to such a position.

63. First of all, there is nothing in that provision to indicate that only those agreements which deprive consumers of certain advantages may have an anti-competitive object. Secondly, it must be borne in mind that the Court has held that, like other competition rules laid down in the Treaty, \textit{[TFEU 101]} aims to protect not only the interests of competitors or of consumers, but also the structure of the market and, in so doing, competition as such. Consequently, for a finding that an agreement has an anti-competitive object, it is not necessary that final consumers be deprived of the advantages of effective competition in terms of supply or price.


73. Case C-209/10, 2012 ECI EUR-Lex LEXIS 2559, ¶ 42 (Mar. 27, 2012) ("[I]t is for the dominant undertaking to show that the efficiency gains likely to result from the conduct under consideration counteract any likely negative effects on competition and consumer welfare in the affected markets, that those gains have been, or are likely to be, brought about as a result of that conduct, that such conduct is necessary for the achievement of those gains in efficiency and that it does not eliminate effective competition, by removing all or most existing sources of actual or potential competition." (emphasis added)).


75. \textit{DAMIEN GERADIN ET AL., EU COMPETITION LAW AND ECONOMICS} 21 (2012) ("[This approach] finds no clear-cut support in the wording of the Treaty . . . .").

64. It follows that, by requiring proof that the agreement entails disadvantages for final consumers as a prerequisite for a finding of anti-competitive object and by not finding that that agreement had such an object, the Court of First Instance committed an error of law. 77

A broader review of case law suggests multiple goals, both economics based and noneconomics based.

The *T-Mobile Netherlands BV v. Raad van bestuur van de Nederlandse Mededingingsautoriteit* decision 78 provides another recent formulation of the multiple goals of European competition law. It states, “[TFEU 101], like the other competition rules of the Treaty, is designed to protect not only the immediate interests of individual competitors or consumers but also to protect the structure of the market and thus competition as such.” 79 In *Konkurrensverket v. TeliaSonera Sverige AB*, 80 the court explained in the dominance context:

> Article 102 TFEU is one of the competition rules referred to in Article 3(1)(b) TFEU which are necessary for the functioning of that internal market. The function of those rules is precisely to prevent competition from being distorted to the detriment of the public interest, individual undertakings and consumers, thereby ensuring the well-being of the European Union. 81

Similarly, in the dominance context, the court has explained that “[TFEU 102] thus refers not only to practices which may cause damage to consumers directly, but also to those which are detrimental to them through their impact on competition.” 82 This formulation seems to show concern for competitors, consumers, and the functioning of the internal market. These goals may at times be at odds with each other.

The ECJ has taken similar positions regarding multiple goals in *Sot. Lelos kai Sta EE v. GlaxoSmithKline AEVE Farmakeftikon Proionton* 83 and *T-Mobile Netherlands*. 84 Some of the recent case law in the Article 102 TFEU context suggests the protection of rivalry as a value in itself. These cases include *Konkurrensverket v. TeliaSonera Sverige AB* 85 and *Visa Europe & Visa International Service v. Commission*. 86 The move within E.U. courts now seems at times even more expansive. Decisions emphasize that the purpose of E.U. competition law is “to prevent competition being distorted to the detriment of the public interest, individual undertakings and consumers,” 87 thereby ensuring the “well-being of the European Union”

77. *Id.* ¶ 62–64 (citations omitted).
79. *Id.* ¶ 38.
81. *Id.* ¶ 22–23.
83. Joined Cases C-468/06 to C-478/06, 2008 E.C.R. 7139.
84. Case C-8/08, 2009 E.C.R. I-4529.
both in TFEU 101 and TFEU 102 contexts. Whatever the mix of these multiple goals, it is certainly not total welfare and not even clearly consumer welfare.

Where there has been a noticeable change to embrace consumer welfare, it has been from EC’s Directorate-General for Competition (DG Competition) itself. Its Merger Guidelines make explicit the goal of consumer welfare.\(^8\) The Commission similarly did so in its Article 82 Guidance.\(^9\) Overall, the shift towards consumer welfare exists both at the level of top management\(^9\) and from the work product of the DG Competition itself.\(^9\) It may very well just be a matter of time before European courts embrace what is a clear attempt by DG Competition to refine and narrow the goals of competition to the singular purpose of consumer welfare. This same trend should shift, with time, convergence among the national competition authorities toward the DG Competition formulation of welfare goals.

### D. Convergence of Economics in Antitrust Law

Even though a convergence of U.S. and E.U. case law towards a unified economic-based standard remains distant, this divergence is not the case in the academy, which has moved closer since the 1970s. The “A” publications for European industrial organization economists are the same for U.S. equivalents. Faculties attend the same conferences, write joint papers, and teach together. The most important revolution in industrial organization in the past thirty years has been the game theory revolution. From this standpoint, it is interesting to note the fact that Jean Tirole originally wrote his textbook—the standard graduate level economic textbook around the world—in French rather than English.\(^9\) Thus, to a certain extent, economic analysis of antitrust has already converged.\(^9\)

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93. This is true not only in Europe and the United States but elsewhere such as Australia, Canada, Chile, China, Israel, Korea, and Japan, to name just a few other jurisdictions. See,
Where there are differences, they seem to be at the margin—although hotly contested in these areas.\textsuperscript{94}

Differences remain in the use of economic analysis within the legal scholarship across the Atlantic. First, the publication outlets are different in the United States than in Europe. Second, economic analysis of law within this field seems to be, on the whole (with some notable exceptions), less used in Europe as European competition law scholarship is far more doctrinal.\textsuperscript{95} The way in which law is taught contributes to this. There is far less economic analysis of the cases in the leading European competition law casebooks than in their U.S. antitrust law counterparts. Indeed, every single major U.S. casebook has a Ph.D. economist among the casebook authors.\textsuperscript{96} This development is not unique to the field of antitrust/competition law. Europe in general has been less receptive than the United States to the economic analysis of law among law professors, although in Europe economic analysis of law is more significant among economists.\textsuperscript{97}

A snapshot of the current European law reviews provides evidence of the different approaches to economic analysis of antitrust/competition law. We compared the articles from the August 2012 issues of the \textit{European Competition Journal}\textsuperscript{98} and the \textit{Antitrust Law Journal}.
\textsuperscript{99} Of six articles and a book review in the \textit{European Competition Journal}, three articles reference an economics journal in the footnotes and two of those articles have economists as the author or coauthor. Of the remaining articles, only one article referenced any economics journals. Compare this to the \textit{Antitrust

Law Journal, in which ten of eleven articles cited at least several economics papers, and the one article that did not reference an economics article was a short afterword that summed up most of the other articles.

The lack of significant economic analysis within European law schools means that the pipeline of both ideas and practitioners of economic analysis in competition law is weaker in Europe than it is in the United States. In the United States, it was the law-and-economics academy that first transformed the analysis of antitrust, starting in the 1950s. The courts followed, responding to the emerging scholarship. Courts began to shift antitrust doctrine from per se to rule of reason (and greater economic analysis) starting in the late 1970s, while at the same time transforming procedural standards. These changes next influenced the antitrust agencies, which in turn further strengthened the changes within the courts.

In Europe, where the legal academy has not been the driver of economic analysis, the sequence has been different. It has been DG Competition and the courts rather than the legal academy that have promoted greater use of economic analysis of antitrust in Europe. However, all is not lost regarding convergence of economic analysis of law. Indeed, the trend is positive even within the European legal academy. Additionally, practitioners have acted as catalysts of convergence in Europe. Law firms and economic consulting firms have offices on both sides of the Atlantic and try to coordinate theories and analyses across antitrust agencies and before courts.

International antitrust norms through international organizations such as the Organisation for Economic Co-operation and Development (OECD) and ICN support some legal convergence around economic analysis. The dynamics of these organizations allow them to help foster convergence among countries around the world. Convergence within the international antitrust realm has tended to be stronger around procedural rather than substantive matters. Nevertheless, in those substantive areas in which


101. See Kobayashi & Muris, supra note 43; Kovacic, supra note 47.

102. RICHARD A. POSNER, THE PROBLEMATICS OF MORAL AND LEGAL THEORY 229 ("More judges and lawyers learned the rudiments of antitrust economics, and antitrust economists became more effective as consultants and expert witnesses. It is fair to say that at the beginning of its second century antitrust law has become a branch of applied economics, has achieved a high degree of rationality and predictability, and is a success story of which all branches of the law and allied disciplines can be proud."); Richard A. Posner, Introduction to Baxter Symposium, 51 STAN. L. REV. 1007, 1007–09 (1999); Richard Schmalensee, Bill Baxter in the Antitrust Arena: An Economist's Appreciation, 51 STAN. L. REV. 1317, 1323–30 (1999).

103. Elhauge, supra note 43.

104. See supra notes 88–91 and accompanying text.

105. See Oliver Budzinski, International Antitrust Institutions, in OXFORD HANDBOOK OF INTERNATIONAL ANTITRUST ECONOMICS, supra note 32; Sokol, supra note 32.
convergence is possible, these organizations have helped foster convergence around best practices, which allows for integration within existing legal systems.\textsuperscript{106}

Is this convergence a good thing? The answer is not straightforward. Convergence is not the same as uniformity. Indeed, it would be naive to think that antitrust has reached an end of history in which every country interprets the same goal and applies it uniformly. Competitive pressures do exist regarding ideas, and over time populist noncompetition economic theories of antitrust have dwindled and been moved to other areas of regulation across jurisdictions. However, this has not led to a uniform standard, just as complex businesses themselves do not all share the same internal organizational structures.\textsuperscript{107} Antitrust will not reach a single global goal based on some sort of economic Darwinism where the marketplace of ideas will eventually lead to the total elimination of competing theories.\textsuperscript{108}

From an economic standpoint, convergence is positive if it leads to the same analytical economic approach across jurisdictions, since this provides for a certain level of predictability in both process and outcome.\textsuperscript{109} Without convergence, developments in Europe will affect business behavior in the United States. However, convergence may be problematic if it leads to suboptimal enforcement or if there is convergence around a suboptimal standard. Thus, convergence around a better substantive standard would allow for "trading up" and a race to the top, whereas bad standards would force some countries to trade down and create a race to the bottom with respect to regulatory standards.\textsuperscript{110}

Below, we explore two situations in which there is a divergence in the welfare standard for behavior between the United States and the European

\textsuperscript{106} John Fingleton, The International Competition Network: Planning for the Second Decade, Address at the 9th Annual Conference in Istanbul, Turkey 4–5 (Apr. 27, 2010), available at http://www.internationalcompetitionnetwork.org/uploads/library/doc617.pdf ("The ICN has proven successful in developing international best practices in relation to substantive standards, as we have seen in the areas of mergers and cartels, discussed above. Similarly, the ICN provides a forum to discuss differences, a 'marketplace for ideas'. The ICN has also provided part of the underlying infrastructure for many bilateral and regional improvements . . . .")


\textsuperscript{108} See MILTON FRIEDMAN, ESSAYS IN POSITIVE ECONOMICS (1953) (providing a classic analysis).

\textsuperscript{109} See David S. Evans, Why Different Jurisdictions Do Not (and Should Not) Adopt the Same Antitrust Rules, 10 CHI. J. INT’L L. 161, 162 (2009) ("Divergence is hardly a happy state of affairs for companies that compete in multiple jurisdictions. It is also a source of tension among competition authorities that are working from different rulebooks, as they jointly regulate the game of competition among firms playing on a world stage."); Gifford & Kudrle, supra note 92, at 695.

Union and the implications of those divergences. We begin with RPM and then examine merger efficiencies.

II. TREATMENT OF RPM

There are some restraints that have been condemned under the antitrust laws despite having ambiguous welfare effects. A prominent example is RPM, which is when a supplier sells its product to a distributor on the condition that the product not be resold below some specified minimum price.\textsuperscript{111} The difference between the U.S. and E.U. approaches regarding RPM has to do with the legal presumptions underlying each\textsuperscript{112}—in the United States, RPM is not presumptively illegal while in Europe it is. In the verticals setting, there is no global systemwide antitrust problem. The least common denominator problem tends not to be as significant because a distribution strategy for end goods tends to be national.

A. U.S. Treatment

It has been argued that RPM can be used to facilitate a horizontal conspiracy among manufacturers or among distributors.\textsuperscript{113} These cartels are clearly undesirable and should be condemned. As price rises and quantity falls, both consumer welfare and social welfare may be reduced. Without some colorable claim of enhanced efficiency, the practice will have no redeeming virtue and will fail a rule of reason test. But the existence of an RPM program is not evidence of a horizontal price fixing conspiracy among manufacturers or distributors.

The U.S. Supreme Court found RPM to be illegal per se in\textit{ Dr. Miles Medical Co. v. John D. Park & Sons Co.}, a 1911 decision.\textsuperscript{114} After nearly 100 years, the Court overturned \textit{Dr. Miles} in its \textit{Leegin} decision.\textsuperscript{115} The

\begin{itemize}
  \item[\textsuperscript{111}] Prohibitions on resales above a \textit{maximum} price do not have ambiguous welfare effects. Such restraints promote both consumer welfare and social welfare. See Roger D. Blair & John E. Lopatka, \textit{The Albrecht Rule After Khan: Death Becomes Her}, 74 NOTRE DAME L. REV. 123, 168–69 (1998). This restraint is subject to the rule of reason. See generally State Oil Co. v. Khan, 522 U.S. 3, 22 (1997).
  \item[\textsuperscript{112}] See Ulf Bernitz, \textit{Resale Price Maintenance in Comparative Perspective, in Research Handbook on International Competition Law, supra} note 30, at 441–50.
  \item[\textsuperscript{113}] RPM supports a cartel by making it more difficult to cheat. Lester G. Telser, \textit{Why Should Manufacturers Want Fair Trade?}, 3 J.L. & ECON. 86, 96–99 (1960) (explaining the cartel motivation for RPM and pointing out the weaknesses in those uses of RPM). Herbert Hovenkamp examines the background of \textit{Dr. Miles Medical Co. v. John D. Park & Sons Co.} and argues that there was a widespread conspiracy among distributors that explained the use of RPM in that case. See \textit{Enterprise and American Law: 1836–1937}, at 342 (1991).
  \item[\textsuperscript{114}] 220 U.S. 373 (1911). This decision has received a good deal of scholarly criticism that began long ago. For an account of the early reactions, see William Breit, \textit{Resale Price Maintenance: What Do Economists Know and When Did They Know It?}, 147 J. INSTITUTIONAL & THEORETICAL ECON. 72 (1991).
  \item[\textsuperscript{115}] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007). There has been a wealth of commentary on this decision. For a sampling, see Special Issue, \textit{Antitrust Analysis of Resale Price Maintenance After Leegin}, 55 ANTITRUST BULL. 271 (2010), available at http://www.federallegalpublications.com/antitrust-bulletin/201007/ab-2010-55-2-antitrust-bulletin-vol-55-no-2-summer-2010, as well as Thomas C. Arthur, \textit{The Core of}
weight of scholarly research, as discussed in the *Leegin* opinion, revealed that RPM was neither invariably anticompetitive nor invariably procompetitive. Consequently, a rule of reason analysis seemed necessary to determine whether a particular instance of RPM was lawful or unlawful. This is what *Leegin* now requires.

**B. E.U. Treatment**

In theory, RPM is not per se illegal under Article 101. However, it has been treated as such under the block exemption and so, in practice, it has the same effect as a per se violation under Article 101(1) (even though the 2010 block exemptions recognize for the first time some form of efficiencies argument under Article 101(3), which companies could in theory use).

The EC adopted its most recent vertical block exemption in 2010. A block exemption in relation to vertical agreements did exist before 2010. What preceded that (pre-1999) was a messy system of individual exemptions (through a notification system) and an inefficient system of black and white listed clauses.

Though the 2010 block exemption came out after *Leegin*, the EC took a different approach to RPM. The block exemptions are more restrictive in some sense than U.S. measures. Under the block exemption, no distinction is made between express RPM on the one hand and measures that may serve to influence RPM on the other. Both are restricted where there is "a minimum or fixed sale price as a result of pressure from, or incentives offered by, any of the parties." Restricting both types of behavior is different from the approach used in the United States, where many price-
affecting measures, including RPM, are presumptively legal. The differences are not limited to price restraints but also include non-price restraints where Europe (but not the United States) has drawn distinctions in a number of areas, such as selective versus exclusive distribution and online versus brick-and-mortar sales.

One reason for the different treatment of vertical restraints in Europe may have been the historic and path dependent concern about market integration. This remains the case for the ECJ in its recent competition vertical rulings; noncompetition economic arguments regarding market integration trump all else in both *Football Ass’n Premier League Ltd. v. QC Leisure* and *GlaxoSmithKline*. However, at the lower level, the General Court in its *GlaxoSmithKline* decision has been more open to competition economics based arguments, so perhaps over time a change might be possible in European case law.

### C. Promotional Uses of RPM

Several procompetitive motives have been offered for RPM. These uses of RPM are promotional in nature and are intended to cause the

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123. Block Exemption, supra note 119, art. I(1)(e).


demand function to shift rightward. The increase in demand will increase the supplier's profits, but it may also improve consumer welfare even though the price rises. Under other circumstances, however, it will not increase consumer welfare and may even reduce total welfare.

A clear case is illustrated in Figure 1, where $D_1$ represents final good demand without any promotional services and the supply is represented by $S_1$. In Figure 1, we analyze a simple case of unit demand. This is the case in which a consumer will buy only one unit of the good in question.\footnote{In Figure 5, we assume that $D_2$ is parallel to $D_1$, which means that every consumer places an equal value on the promotional services. This, of course, may not be accurate; we deal with that possibility below.} In this case, the quantity sold also tells us how many consumers are in the market. In the absence of promotional services provided by the distributors, the equilibrium price and quantity will be $P_1$ and $Q_1$, respectively. Now, suppose that the manufacturer wants its distributors to provide promotional services that increase the demand for its product. For many consumers, the promotions increase the value of the product. Because the value of the product increases when these promotional services are performed, the demand shifts from $D_1$ to $D_2$.\footnote{If this were not the case, the manufacturer would not push the promotional services because it would not be profitable to do so. The derived demand for the product by the dealers would fall rather than rise, and the manufacturer's profits would suffer. Frederic M. Scherer and David Ross point out that such services will be expanded until no further gains exist. See F.M. Scherer & David Ross, Industrial Market Structure and Economic Performance 541-48 (3d ed. 1990). At this point, the increased cost of additional services will be precisely equal to the increased value of the product resulting from the increased services.} Of course, these promotions are costly and, therefore, the supply curve will shift from $S_1$ to $S_2$ to reflect the increased cost. The new equilibrium is $P_2$ and $Q_2$. In this case, the promotion not only leads to an increase in price from $P_1$ to $P_2$, but quantity also increases from $Q_1$ to $Q_2$ because the vertical shift in demand exceeded the vertical shift in supply.\footnote{Triangles $abP_2$ and $cdP_1$ are similar because the corresponding angles are equal. Since the base of $abP_2$ is larger than the base of $cdP_1$, the area of the former must be larger than that of the latter. This will always be the case with a parallel shift in demand.}

In this case, consumer welfare is unambiguously enhanced. Without the promotion, consumer welfare is given by the triangular area $cdP_1$. With those promotions, however, consumer welfare rises to area $abP_2$. This is clearly larger—and always will be—as long as the shift in demand is parallel and results in a quantity increase.\footnote{RPM is a means of correcting an incentive alignment problem. This is highlighted in Richard E. Romano, Double Moral Hazard and Resale Price Maintenance, 25 RAND J. ECON. 455 (1994).} Without promotion, producer welfare is given by the triangular area $deP_1$. With promotions, producer welfare increases to triangle $bJP_2$. This will also be larger as long as the shift in supply is parallel and results in an increase in quantity. Consequently, total welfare is given by the area of triangle $cde$ without
promotion. With promotion, total welfare expands to area \( abf \). In this context, RPM is used in a way that improves both consumer welfare and the manufacturer's profits. This use of RPM would be lawful under a rule of reason analysis regardless of whether the court is pursuing consumer welfare or social welfare.

In the United States, the use of RPM depicted in Figure 1 would pass muster; but in the European Union it would not. From an economic perspective, this is a curious result. Consumers are clearly better off as a result of \( Q_2 - Q_1 \). More people will consume the product; among consumers, no one is worse off. Producer welfare also rises, so there is no loss there. There are no losers, so a Kaldor-Hicks tradeoff is unnecessary.

This raises an obvious question: assuming that policymakers in the European Union understand the economic analysis, what goals are they pursuing? It could very well be that because of the vertical guidelines, treatment of RPM may be framing the discussion in a way that it would not otherwise be if one were to create a new block exemption from scratch. It also may be that the nonindustrial organization economics goals may play a larger role even in court cases. Because of the historic harsh treatment of RPM, there is less empirical work in this area than other areas involving vertical restraints, but the work to date suggests that the European approach is not borne out by the economic evidence, and so European policy in this area seems to accept noneconomic goals.

Below we show graphically the difference of outcomes across U.S. and E.U. systems.

134. For a discussion of the empirical RPM work to date, see Benjamin Klein, *Online Resale Price Maintenance*, in *OXFORD HANDBOOK OF INTERNATIONAL ANTITRUST ECONOMICS*, supra note 32; Francine Lafontaine & Margaret E. Slade, *Franchising and Exclusive Distribution: Adaptation and Antitrust*, in *OXFORD HANDBOOK OF INTERNATIONAL ANTITRUST ECONOMICS*, supra note 32.
In Figure 1, the parallel shift in demand from $D_1$ to $D_2$ indicates that all consumers value the promotion equally (i.e., each consumer's willingness to pay increases by the same amount). This, however, may not necessarily be the case, as all consumers may not value the promotions equally. In our economic model, this means that the shift in demand will not be parallel. In Figure 2, the promotion leads to a rotation of demand from $D_1$ to $D_2$. We have constructed this example so that the increase in price from $P_1$ to $P_2$ and the increase in quantity from $Q_1$ and $Q_2$ in Figure 2 are precisely the same as the corresponding prices and quantities in Figure 1. In this case, consumer welfare without the promotion is equal to area $acP_1$ and with the promotion equal to area $abP_2$. In some cases (like the one depicted in Figure 2) consumer welfare will decline even though RPM is being used for promotional purposes. In other cases, however, it will increase. Thus, the impact on consumer welfare is ambiguous on a priori


136. As a result, the appropriate antitrust policy is unclear. See Roger D. Blair & James M. Fesmire, *The Resale Price Maintenance Policy Dilemma*, 60 S. ECON. J. 1043 (1994). Richard Posner does not believe that this refinement can be handled in a judicial setting and, therefore, should be ignored. See Posner, *supra* note 6, at 176. Judge Posner may be right as a practical matter, but ignoring this refinement necessarily abandons the consumer welfare standard.
grounds. As a result, the effect of RPM on consumer welfare is an empirical matter. For all practical purposes, however, estimating the effect of RPM on consumer welfare while controlling for all other influences is problematic at best.

Figure 2: RPM May Improve Total Welfare but Reduce Consumer Welfare

In Figures 1 and 2, all of the corresponding prices and quantities are equal. As a result, RPM can lead to identical price and quantity increases but different outcomes for consumer welfare. In Figure 1, RPM is clearly reasonable because both consumer welfare and total welfare increase due to RPM and, therefore, is presumably lawful in the United States. In contrast, the RPM plan depicted in Figure 2 is unreasonable in the sense that consumer welfare declines, but may not be unreasonable on total welfare grounds. Consequently, it is crucial to have a clear antitrust goal: consumer welfare or total welfare. Without such clarity, policy prescriptions are murky at best. Producer welfare is the same in Figures 1 and 2 since the relevant areas are the same in both figures. Thus, the impact on social welfare depends on the impact on consumer welfare. If RPM causes consumer welfare to rise, then total welfare rises and vice versa. It is therefore critical to determine the effect of RPM-induced promotion on consumer welfare.

Determining the economic effect of RPM on either consumer welfare or total welfare is complicated by the fact that there are no simple tests. It is clear that neither an output test nor a price test provides an answer to the
question of reasonableness. RPM is supposed to lead to higher prices, but higher prices alone do not tell us what happens to welfare. As the results in Figures 1 and 2 show, somewhat surprisingly, an output test also fails to distinguish the effects on consumer welfare. Thus, it will be necessary to embark on a difficult econometric journey to resolve the reasonableness inquiry. It would seem that whoever bears the burden of proof will lose the battle.

There is another circumstance that poses a severe challenge for the rule of reason. Suppose that the producer introduced a new product and sold it to distributors subject to an RPM policy. In that event, all we would know is the price and quantity associated with the RPM-induced promotion. There would be no information regarding the price and quantity that would have resulted in the absence of the RPM-induced promotion. In that event, we could measure consumer welfare, at least in principle, with RPM and the promotion but not without the promotion. Thus, a rule of reason analysis would be impossible, because there would be no way to determine the effect of RPM on consumer welfare.

**D. The OTCs and RPM**

Online travel companies (OTCs), such as Expedia, Hotels.com, Orbitz, Priceline, and Travelocity, provide information on flight schedules, airfares, hotel room rates, and car rentals. In many respects, OTCs are travel agents that are open twenty-four hours a day and, therefore, offer a more convenient service than the traditional travel agent. As OTCs have grown in importance, several legal issues have arisen. For the most part, OTCs have attracted the attention of tax-starved states and municipalities over forgone tax revenues. Most recently, however, RPM issues have surfaced. These price restraints may receive different antitrust treatment in the United States and the European Union.

Consumers may consult various OTCs when searching for hotel accommodations. These sites provide information on availability and rates in the destination city. The consumer may then contact the hotel’s reservation system and book a room for, say, one hundred dollars. If the applicable tax rate were 12 percent, the consumer would pay one hundred and twelve dollars to the hotel, which would keep one hundred dollars and transmit twelve dollars to the taxing authority.

The consumer could also book the room through the OTC. The hotels provide discounts to the OTC of, say, 20 percent. In our example, the OTC would pay eighty dollars for the room along with nine dollars and sixty cents (i.e. 12 percent of eighty dollars) in taxes. The consumer would still pay one hundred and twelve dollars pursuant to an agreement between the

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137. See James Mak, *What Should Be the Appropriate Tax Base for OTCs' Hotel Room Sales*, 65 ST. TAX NOTES 775, 775–86 (2012).

hotel and the OTC that the OTC will not undermine the hotel by competing with it through discounting. On this booking, the OTC will earn a gross profit of twenty dollars through the discounted room rate and another two dollars and forty cents because it pays taxes of nine dollars and sixty cents while collecting one hundred and twelve dollars from the consumer. This lost tax has been subject of much litigation.139

For our purposes, however, we are interested in the agreement between the hotel and the OTC that the OTC will not use the discount to undercut the hotel’s reservation system. In effect, the hotel sells the room to the OTC at a wholesale price on the condition that the OTC not resell the room below a specific price set by the hotel. This, of course, is RPM. There are several antitrust issues surrounding these business practices.

First, the vertical agreements between a hotel and each of the OTCs appear to be bilateral. That is, there is no evidence of agreement among various OTCs. But may one infer agreement under the logic of Interstate Circuit, Inc. v. United States140 in the United States or Toshiba Corp. v. Commission in the European Union?141 Second, since the hotel is engaged in a form of dual distribution, is it unreasonable for the hotel to avoid competing with itself? In other words, is it unreasonable as that term is used in the antitrust context to refrain from competing with the OTCs?

As described above, the hotel is engaged in dual distribution. It produces hotel accommodations for travelers and sells directly to the consumer. It also sells hotel rooms through the OTCs. In doing so, it hope to increase its occupancy rates. But the hotel runs the risk of competing with itself, which it wants to avoid through an RPM agreement with the OTC. This agreement clearly restrains the OTC’s ability to reduce the price to the consumer, but is that unreasonable? Presumably, the hotel would argue that the OTC has reduced consumer search costs, which is a procompetitive benefit of the dual distribution. It would also argue that it would abandon dual distribution if it could not protect itself with the RPM agreement. This argument (or one similar) may persuade a jury that the RPM agreement is a reasonable restraint.

Now, suppose that the hotel has similar agreements with all of the major OTCs. As long as these agreements are truly bilateral, each agreement can

139. See Mak, supra note 137.
141. Case T-113/07, ¶ 82 (July 12, 2011), http://curia.europa.eu/juris/document/document.jsf?docid=107961&mode=lst&pageIndex=1&dir=&occ=first&part=1&text=&doc lang=EN&cid=1021087 ("[T]he Commission cannot be required to produce documents expressly attesting to contacts between the traders concerned. The fragmentary and sporadic items of evidence which may be available to the Commission should, in any event, be capable of being supplemented by inferences which allow the relevant circumstances to be reconstituted. The existence of an anti-competitive practice or agreement may therefore be inferred from a number of coincidences and indicia which, taken together, can, in the absence of another plausible explanation, constitute evidence of an infringement . . . ."); see also Joined Cases C-204/00 P, C-205/00 P, C-211/00 P, C-213/00 P, C-217/00 P & C-219/00 P, Aalborg Portland A/S v. Comm’n, 2004 E.C.R. I-123; Case C-199/92 P, Hüls AG v. Comm’n, 1999 E.C.R. I-4287.
be supported by the same claim of reasonableness. To the extent that each OTC honors its agreement with the hotel, there will be no price competition among the OTCs. This, however, should not undermine the reasonableness of the RPM agreements.

Contrary to this hypothetical, however, suppose that there is an agreement among the OTCs not to compete with one another. This would make these bilateral agreements a horizontal agreement that unreasonably denies consumers the benefits of price competition and should therefore be deemed unlawful under section 1 of the Sherman Act.142

Another complicating factor is that the major hotels that presumably compete with one another have similar RPM agreements with the OTCs.143 This in itself is not indicative of horizontal collusion among the hotels but may suggest to some that there is a restraint on competition.

E. Recent Litigation Regarding RPM and OTCs

In the United Kingdom, the Office of Fair Trading (OFT) has filed a Statement of Objections against IHG and others that challenges the RPM agreements that prevent OTCs from undercutting the hotel reservations systems. These supposedly bilateral agreements will prevent price competition among the OTCs.144 There are complaints from smaller OTCs that the larger OTCs demand that the hotels prevent discounting. This alone, however, is not suspicious. After all, if a large OTC honors its bilateral agreement with a hotel, it necessarily will resent being undercut by another OTC that is not honoring a similar agreement.

In the United States, a consumer class action has been filed alleging that the RPM agreement is rigorously enforced against smaller OTCs so that the larger OTCs do not face price competition.145 In essence, the complaint alleges a horizontal rather than a vertical restraint. If such an agreement is proven, it will violate section 1 of the Sherman Act. If, however, the RPM agreements between each OTC and each hotel are simply a collection of bilateral agreements, then the RPM agreements will have to be proven to be unreasonable.

III. MERGERS

In this part, we give a historic overview of the development of merger enforcement in the United States and European Union and examine the legal context of merger efficiencies. Thereafter, we provide an analysis of how a proposed merger might be impacted by disparate merger standards

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143. Posner has found industry-wide use of RPM suspicious. Posner, supra note 6, at 67–68.
across major jurisdictions. The difference in outcomes can be seen through the example of the use of efficiencies arguments in case law regarding mergers. In both cases, the dominant approach seems to be consumer welfare in both the United States and the European Union.

Oliver Williamson first identified the efficiency trade-off raised by merger-specific efficiencies that may accompany an increase in monopoly power postmerger.\textsuperscript{146} There are some instances in which a business practice improves efficiency (i.e., reduces costs of production and/or distribution). The easy case is one in which the merger does not enhance market power. As a result, cost savings from the merger will be passed on to some extent to consumers in the form of lower prices. This case is easy because the merger increases both consumer welfare and total welfare.

The more difficult case occurs when the improved efficiency accompanies increased market power postmerger that leads to a price increase above the previous level. This situation creates a need to weigh the benefits of improved efficiency against the costs of allocative inefficiency, since this merger should be allowed on total welfare grounds but not on consumer welfare grounds. Before we examine these cases, we provide a review of how merger analysis has developed.

\textbf{A. Merger Goals, Efficiencies, and Antitrust Systems}

This section traces the development of merger control in the United States, the first antitrust system to create a robust merger-control regime that includes merger guidelines to shape practice before agencies and courts. This section then examines the development of U.S. merger case law regarding efficiencies. Thereafter, it undertakes a similar analysis regarding European merger-efficiencies case law before noting areas of divergence between the two systems. Finally, the section explains the economics of how different welfare standards could lead to disparate outcomes in the decision to allow or block a merger and how this might have a global impact.

1. Historic Overview of U.S. Mergers

Perhaps more than any other antitrust system, the United States' experience with merger control has shown the most dramatic shift from the influence of overt political factors to sole primacy of industrial organization economics considerations.\textsuperscript{147} Antitrust case law began to reflect the shift


\textsuperscript{147} For example, in the United States, even though the economic understanding of cases such as *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962), and *United States v. Philadelphia National Bank*, 374 U.S. 321 (1963), is retrograde by today's standards, agencies still cite to them when they want to block a merger. The latest methods in industrial organization recommend the least amount possible of political intrusion specific to industrial organization economics into antitrust policy. See ULRICH SCHWALBE & DANIEL ZIMMER, *LAW AND ECONOMICS IN EUROPEAN MERGER CONTROL* (2009); Mats A. Bergman et
from political factors to industrial organization economics in the late 1970s, although the change specifically in merger case law lagged a bit relative to the abolition of per se rules regarding conduct. As Judge Ginsburg has noted in the case law development,

Even in such cases where there is no consensus among economists, there is, nevertheless, virtually universal agreement among antitrust economists and lawyers alike, that the Court should answer questions of antitrust law with reference to economic competition—matters of consumer welfare and economic efficiency—rather than make political judgments about such economically irrelevant matters as the "freedom of traders," or "the desirability of retaining 'local control' over industry and the protection of small businesses."

Classic merger cases such as Brown Shoe Co. v. United States, United States v. Von's Grocery Co., and United States v. Philadelphia National Bank would be decided quite differently both in approach and outcome today. Moreover, changes in priorities became embedded not merely in the case law but also in the agencies with the rise in the importance of economics.

The introduction of economically informed merger guidelines has created a framework to analyze mergers, and the approach of writing and operationalizing guidelines has been copied in many of the world's jurisdictions. The importance of the merger guidelines to antitrust merger and the use of various economic theories and approaches have been tremendous. There has been an iterative process of tweaking the guidelines as the economics of the time have changed. This has been true in the United States with each iteration of the merger guidelines—1968, 1982, 1984, 1992, 1997, and 2010. This economic approach based upon the merger guidelines has become embedded within U.S. case law.

Scholars have quantified the shift of merger enforcement. Indeed, there is much empirical literature examining the political economy of federal government antitrust enforcement. Judge Posner first set the stage by examining data on the Department of Justice antitrust litigation. Others


148. See Greene, supra note 49.


154. See generally Greene, supra note 49.

have since updated, revised, and extended his work. Collectively, the empirical evidence shows that (1) there is no consistent relationship between the party of the President and federal antitrust enforcement, and (2) the relationship between aggregate economic activity and federal antitrust case-activity is ambiguous—the typical finding being a weak-positive or no link. Empirical work suggests that overt industrial organization economics based politics has, for the most part, become a nonissue in U.S. merger enforcement in recent decades (1990s onwards). As Malcolm Coate states, "Populism was forced to a fringe position." This is a change from earlier studies of U.S. merger control that examined the 1980s and suggested that there were noneconomic factors at play in merger control.

Examining even earlier merger enforcement, and given the current state of industrial organization economics, U.S. merger enforcement and case law from the 1950s and 1960s is an intellectual embarrassment. The agency priorities and case law reflected the idea that big was bad and that the protection of competitors mattered more than some notion of efficiency. In a large sense, overt noneconomic political factors mattered most within antitrust merger analysis.

2. E.U. Mergers Historic Overview

Empirical work that analyzes the pre-"effects based" period of European merger enforcement shows that protectionism existed in merger control in terms of deals challenged. The analyses show that DG Competition had a


159. FTC v. Procter & Gamble Co., 386 U.S. 568, 574–75 (1967); In re Foremost Dairies, Inc., 60 F.T.C. 944, 1084 (1962). This approach was not limited to mergers, but also applied in the monopolization setting. See United States v. Aluminum Co. of Am., 148 F.2d 416, 428 (2d Cir. 1945) ("[G]reat industrial consolidations are inherently undesirable, regardless of their economic results.").

higher probability of intervention against non-European firms when there were European competitors in the same market.\footnote{161} This supports the view that the welfare standard (at least at that time) was not a traditional consumer or total welfare standard but one that included non-antitrust economic factors.

Things have changed in Europe. Empirical work that focuses on more recent European merger control suggests that protection of European firms from non-European firms is no longer a factor within European level merger control.\footnote{162} With time, European merger analysis has improved, as European merger law has increasingly featured economic analysis as a result of certain doctrinal and structural changes.\footnote{163} Changes have included reform via the 2004 Horizontal Merger Guidelines,\footnote{164} which made economic analysis a more vital part of merger analysis, case law developments (\textit{Airtours/First Choice}, \textit{Schneider/Legrand},\footnote{166} and \textit{Tetra Laval/Sidel}\footnote{167}),\footnote{168} and the creation within DG Competition of the chief economist position and an economics group that is not subservient to the legal team in its analysis.\footnote{169}

\begin{itemize}
  \item \footnote{163} Nicholas Levy, \textit{Evidentiary Issues in EU Merger Control}, in \textit{ANNUAL PROCEEDINGS OF THE FORDHAM COMPETITION LAW INSTITUTE: INTERNATIONAL ANTITRUST LAW & POLICY} 81 (Barry E. Hawk ed., 2009); Orbach & Sokol, \textit{supra} note 52, at 446.
  \item \footnote{164} Guidelines on the Assessment of Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings, 2004 O.J. (C 31) 5, 14.
  \item \footnote{165} Case IV/M.524, 2000 O.J. (L 93) 1, \textit{overruled by} Case T-342/99, Airtours v. Comm’n, 2002 E.C.R. II-2585.
  \item \footnote{166} Case COMP/M.2283, 2004 O.J. (L 101) 1, \textit{overruled by} Case T-310/01, Schneider Electric SA v. Comm’n, 2002 E.C.R. II-4071.
  \item \footnote{168} \textit{See} ULRICH SCHWALBE & DANIEL ZIMMER, \textit{LAW AND ECONOMICS IN EUROPEAN MERGER CONTROL} (2009); Mark Leddy et al., \textit{Transatlantic Merger Control: TheCourts and the Agencies}, 43 \textit{CORNELL INT’L L.J.} 25, 42 (2010); Duso et al., \textit{supra} note 147.
  \item \footnote{169} Luke M. Froeb et al., \textit{The Economics of Organizing Economists}, 76 \textit{ANTITRUST L.J.} 569 (2009). A similar trend occurred earlier in the United States. Oliver Williamson notes, "Taken together, the creation of the position of Special Economic Assistant and the decision to staff the evaluation section with young lawyers who bought into the idea that economic reasoning should be featured more prominently in antitrust enforcement were important 'organizational innovations.'" For those who were a part of this transition, these were
Since that time, the role of economics (and economists) has grown both within DG Competition and among economic experts who regularly appear before Commission staff. Yet, the earlier case law and institutional approaches have impacted the current structure and nature of merger enforcement in Europe in terms of state intervention. Quantitative research supports that, at present, Europe is a stricter enforcer of merger regulation than the United States.

3. Examples of Merger Divergence

It has been quite some time since the substantive merger standard has mattered across regimes. What we have seen overall is that after a period of substantive divergence in merger control as it relates (in part) to economic analysis, increasingly there is convergence between the United States and the European Union as to substantive analysis of mergers. Yet, a number of high profile cases regarding mergers that involved significant merger scrutiny over a decade ago demonstrated that the more stringent legal regime could have global consequences. These included most notably Boeing/McDonnell Douglas, General Electric/Honeywell, and Oracle/PeopleSoft. In each of these three cases, had either the United States or the European Union blocked the merger, the deal would have had to be abandoned as a condition of closing. Of these three deals, the one that created the greatest transatlantic rift was GE/Honeywell, which the United
States approved but the European Union blocked. The effect of the E.U. action was to block the deal globally.

We will now review these mergers to demonstrate that a divergence in merger standards can have global results in a way that a divergence in RPM standards cannot. We begin with a short review of GE/Honeywell.

The proposed GE/Honeywell deal received merger clearance in the United States but was blocked within Europe based on the theory of a bundling of GE’s engines with its financial services at a price that was below what its rivals could offer. Third-party complaints drove much of the hostility of the EC but so did a path dependency based on political considerations on the view of competition in Europe. European competition policy, at the time, was far more likely to be about the preservation of competitors than that of the United States. Thus, even if there were not some overt public choice explanation for the strategic use of antitrust, institutional factors also pushed DG Competition to block the deal in Europe and, in effect, to block the deal globally.

In Oracle/PeopleSoft, the EC approved the merger but did so using the same unilateral effects theory that the U.S. Department of Justice (DOJ) had suggested to block the deal. Unlike Boeing/McDonnell Douglas and GE/Honeywell, the Europeans agreed with the market definition employed by DOJ and yet somehow still cleared the merger after DOJ had lost its merger challenge to the deal before a district court. This is puzzling since, if DG Competition accepted the DOJ market definition, the three-to-two merger most probably should have been challenged by DG Competition based on a unilateral effects theory.

Politics seems to have played a role in the decision not to challenge the Oracle/PeopleSoft merger in Europe. Because of the very thorough opinion that would have made an appeal incredibly difficult to win, DOJ decided not to appeal the ruling. Had economic analysis been at the forefront of the European decision making, this would have created a potential problem. By challenging a deal that could proceed in the United States, the EC would only increase transatlantic tensions, just as Commissioner Monti’s term was to come to a close and just as efforts on best practices in the ICN for merger control were taking shape. These political factors seem to have been in play in the EC’s decision to clear Oracle/PeopleSoft. DOJ’s loss in the district court provided cover for the Europeans not to challenge the deal aggressively so that Commissioner Monti would not leave a political bomb

178. Id.
for his successor Commissioner Kroes and another potential transatlantic rift.\textsuperscript{181} Having described past divergence, we now examine the present and future use of efficiencies in merger law and economics and how there might be divergence between the United States and Europe. With the political issues resolved and closer day-to-day coordination between U.S. and E.U. agencies, the type of political divergence between merger deals may be a thing of the past. Consequently, we lay out a hypothetical merger based on purely economic factors that might lead to divergent outcomes.

\textbf{B. U.S. Efficiencies in Merger Law}

Efficiencies in mergers went through a significant transformation over a period of thirty years between the 1960s and 1990s. In the 1960s, efficiencies were treated with some hostility under U.S. case law. In \textit{In re Foremost Dairies},\textsuperscript{182} a violation of section 7 of the Sherman Act would include a firm’s “over-all organization [that] gives it a decisive advantage in efficiency over its smaller rivals,”\textsuperscript{183} while in \textit{Philadelphia National Bank},\textsuperscript{184} the Supreme Court noted that “a merger the effect of which ‘may be substantially to lessen competition’ is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial.”\textsuperscript{185} Technically, the Court has never renounced its earlier view on mergers efficiencies in its more modern antitrust jurisprudence, largely because there has not been a substantive merger case before the Court in over a generation.

Though efficiencies arguments began to emerge as part of the rule of reason analysis in conduct cases, its adoption in earnest within the area of mergers came later. Starting in the 1980s, the rewriting of the efficiencies analysis, as part of the 1984 Horizontal Merger Guidelines, moved efficiencies from being a defense to part of the competitive effects.\textsuperscript{186} Certain cases along the way, such as \textit{United States v. General Dynamics Corp.},\textsuperscript{187} also helped.\textsuperscript{188}

\textsuperscript{181} Christian Duvernoy \& Sven Völcker, \textit{Oracle in Brussels}, 5 M&A J. 1, 15 (2005), available at http://law.bepress.com/cgi/viewcontent.cgi?article=1022&context=wilmer (“One theory is that after GE/Honeywell, the Commission was making a political decision and hiding that fact: ‘Let’s look different and independent, but let’s also come out with the same result.’”). Commissioner Kroes soon created a number of transatlantic political crises of her own without the help of Monti.

\textsuperscript{182} 60 F.T.C. 944 (1962).

\textsuperscript{183} \textit{Id.} at 1084.

\textsuperscript{184} 374 U.S. 321 (1963).

\textsuperscript{185} \textit{Id.} at 371.

\textsuperscript{186} U.S. DEP’T OF JUSTICE, MERGER GUIDELINES § 3.5 (1984), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,103.

\textsuperscript{187} 415 U.S. 486 (1974).

This brief historic overview of merger efficiencies allows us to move to the present legal regime for merger analysis of efficiencies—the 2010 Merger Guidelines, which for the most part adopted the 1997 version of the efficiencies section. What the language of the 2010 Merger Guidelines suggests at first blush is an unambiguous support of a consumer welfare standard. Efficiencies are treated under a "sliding scale" approach. The 2010 Merger Guidelines explain:

The Agencies will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market. To make the requisite determination, the Agencies consider whether cognizable efficiencies likely would be sufficient to reverse the merger's potential to harm customers in the relevant market, e.g., by preventing price increases in that market. In conducting this analysis, the Agencies will not simply compare the magnitude of the cognizable efficiencies with the magnitude of the likely harm to competition absent the efficiencies. The greater the potential adverse competitive effect of a merger, the greater must be the cognizable efficiencies, and the more they must be passed through to customers, for the Agencies to conclude that the merger will not have an anticompetitive effect in the relevant market.

The 2010 Merger Guidelines add that "[i]n adhering to this approach, the Agencies are mindful that the antitrust laws give competition, not internal operational efficiency, primacy in protecting customers." Courts have responded to this language by adopting a true consumer welfare standard with regard to efficiencies. Indeed, most of the litigated cases before the courts do not rest strongly on an efficiency argument, but this has not


193. 2010 MERGER GUIDELINES, supra note 189, at 31.

194. Kolaszky & Dick, supra note 188, at 232 ("The courts have largely adopted the analytical framework for evaluating efficiency claims that is set out in the Guidelines."); see also Greene, supra note 49 (describing the adoption of the merger guidelines by courts).
stopped various courts in dicta from reiterating the importance of consumer welfare in the efficiencies context.\textsuperscript{195} However, as the expression goes, the devil is in the details. In our case, that detail is footnote fifteen of the efficiencies section of the 2010 Merger Guidelines, which provides for the possibility of the use of a total welfare standard for merger efficiencies.\textsuperscript{196} In that footnote, the 2010 Merger Guidelines explain, "The Agencies also may consider the effects of cognizable efficiencies with no short-term, direct effect on prices in the relevant market."\textsuperscript{197}

This attention to detail also opens up the possibility of some ambiguity within case law as to what welfare standard might come into play regarding a case that substantively may be litigated upon efficiency grounds. To date, there has been only one case in which there was a significant discussion of efficiencies under the modern Merger Guidelines, a merger known commonly as the "baby foods case" and officially as FTC\textsuperscript{v.} H.J. Heinz Co.\textsuperscript{198} The case involved a proposed three-to-two merger between Heinz and Beech Nut, the number two and number three firms in the baby food market.\textsuperscript{199} The merging parties argued that the merged company would provide efficiencies to more effectively compete with the market leader, Gerber.\textsuperscript{200}

According to the D.C. Circuit in Heinz, to prove the case for accepting the efficiencies argument of the parties, given the high level of concentration of the merged firm, would require extraordinary efficiencies. However, the court did not make clear what it meant by extraordinary efficiencies. From the standpoint of welfare standards, the court was also silent as to whether extraordinary efficiencies should be measured using consumer welfare or total welfare (the district court had been similarly silent as to the standard). Unfortunately, the only guidance as to the welfare standard for extraordinary efficiencies comes in the form of dicta via a

\begin{footnotes}
\item 195. FTC\textsuperscript{v.} Arch Coal, Inc., 329 F. Supp. 2d 109, 153 (D.D.C. 2004) ("The existence of such efficiencies, therefore, remains relevant to an assessment of the post-merger market and the potential benefits to consumers from cost reductions and increased competition."); FTC\textsuperscript{v.} Cardinal Health, Inc., 12 F. Supp. 2d 34, 62 (D.D.C. 1998) ("The FTC does not contest that the mergers will result in large-scale efficiencies, some of which will be passed on to the consumer."); United States\textsuperscript{v.} Long Island Jewish Med. Ctr., 983 F. Supp. 121, 137 (E.D.N.Y. 1997) ("In sum, to sustain an 'efficiencies defense,' the defendants must clearly demonstrate that the proposed merger itself will create a net economic benefit for the health care consumer."); FTC\textsuperscript{v.} Staples, Inc., 970 F. Supp. 1066, 1090 (D.D.C. 1997) ("The Court has no doubt that a portion of any efficiencies achieved through a merger of the defendants would be passed on to customers.").
\item 196. 2010 MERGER GUIDELINES, supra note 189, at 31 n.15.
\item 197. Id.
\item 198. 246 F.3d 708 (D.C. Cir. 2001).
\item 200. H.J. Heinz Co., 246 F.3d at 720.
\end{footnotes}
citation to FTC v. University Health.201 The Heinz D.C. Circuit decision quoted the proposition in University Health that "a defendant who seeks to overcome a presumption that a proposed acquisition would substantially lessen competition must demonstrate that the intended acquisition would result in significant economies and that these economies ultimately would benefit competition and, hence, consumers."202 The problem with this statement is that it muddled what goal might be reached. It could be that what might benefit competition (total welfare) may be at odds in some set of cases with what might benefit consumers (consumer welfare) in the situation of extraordinary efficiencies.203 One could imagine a hypothetical two-to-one firm merger in which prices might not fall, but the combined firm conducts research and development more efficiently.204 Under a total welfare standard, such a merger should be allowed even though under a consumer welfare standard the outcome might be more ambiguous. In such circumstances, prices may go up for a number of years before going down many years later, if at all.205

C. E.U. Efficiencies in Merger Law

Whereas E.U. competition law was a part of the Treaty of Rome in 1957 with regard to conduct, merger control at the E.U. level came about relatively late in 1989 with the EC Merger Regulation (ECMR), which went into effect in 1990.206 An amended ECMR went into effect first in 1998 and then in its current form in 2004.207

201. Id.
202. Id. (quoting FTC v. Univ. Health, 938 F.2d 1206, 1223 (11th Cir. 1991)).
203. The Merger Guidelines suggest that consumers are the net beneficiaries, although this has not come up in a court context. 2010 MERGER GUIDELINES, supra note 189, at 30–31.
205. Gregory Werden et al., The Effects of Merger Efficiencies on Consumers of Differentiated Products, 1 EURO. COMPETITION J. 245 (2005) (discussing how to conceptualize potential pass through to consumers). We assume away the problem that it may be difficult to quantify efficiencies effectively. For this critique, see Frédéric Jenny et al., Substantive Standards for Mergers and the Role of Efficiencies, in INTERNATIONAL ANTITRUST LAW & POLICY: ANNUAL PROCEEDINGS OF THE FORDHAM CORPORATE LAW INSTITUTE 301, 343 (Barry Hawk ed., 2003) ("We can't solve this. Economists, the system, auditoriums full of well-educated competition analysts, cannot actually overcome the essential unpredictability of the future."). For discussions of dynamic merger efficiencies, see Michael L. Katz & Howard A. Shelanski, Merger Analysis and the Treatment of Uncertainty: Should We Expect Better?, 74 ANTITRUST L.J. 537 (2007) and Gary L. Roberts & Steven C. Salop, Efficiencies in Dynamic Merger Analysis, 19 WORLD COMPETITION 4 (1996).
The ECMR explicitly recognizes efficiencies as of the 2004 revisions. It notes, “In order to determine the impact of a concentration on competition in the common market, it is appropriate to take account of any substantiated and likely efficiencies put forward by the undertakings concerned.” This is based upon “the development of technical and economic progress provided that it is to the consumers’ advantage and does not form an obstacle to competition.” The EC Horizontal Merger Guidelines note that an efficiencies defense will work in situations where

the Commission is in a position to conclude on the basis of sufficient evidence that the efficiencies generated by the merger are likely to enhance the ability and incentive of the merged entity to act pro-competitively for the benefits of consumers, thereby counteracting the adverse effects on competition which the merger might otherwise have. Furthermore, efficiencies must “benefit consumers.” As a result of the language from the ECMR and the Merger Guidelines, it seems to be the case that the welfare standard for an efficiencies defense in Europe is consumer welfare.

European merger cases support this view of a consumer welfare standard. In Inco/Falconbridge, the EC rejected an efficiencies defense (although conditioned approval of the merger-based remedies proposed) because the efficiencies of the proposed merged firm would not be passed through to consumers. Similarly, regarding Ryanair/Aer Lingus, the EC rejected an efficiencies defense in part because it believed that the efficiencies would not be passed on to consumers. In a more recent airlines case, Lufthansa/SN Airholding, the EC approved a merger but rejected the efficiencies defense because the efficiencies could not be passed through to consumers.

Adding an analytical twist to the European approach is that, unlike the United States, the European Union has relatively recent merger guidelines that apply in cases of conglomerate effects and vertical

208. Id. ¶ 29, recital 29.
209. Id. art. 2(1)(b).
211. Id. ¶ 78.
mergers. These European nonhorizontal guidelines make clear that "the fact that rivals may be harmed because a merger creates efficiencies cannot in itself give rise to competition concerns." Efficiencies seem to take a consumer welfare approach under these guidelines as well. In the Tom Tom/Tele Atlas case, the EC took a consumer welfare approach to efficiencies in a detailed discussion of efficiencies, even though the EC found that the efficiencies were irrelevant to the decision to approve since the deal did not present anticompetitive concerns.

D. Economics of Merger Efficiencies

Having discussed divergence in the case law, we move to an economic analysis of merger efficiencies and illustrate how a change in welfare standard might lead to divergent outcomes in the United States and the European Union. Efficiency that flows as a result of a merger may justify mergers and joint ventures under antitrust law. The Williamsonian tradeoff of merger specific efficiencies may lead to situations where the merged firm is able to pass on the merger specific cost savings to consumers. However, the efficiency tradeoff may result in an increase of monopoly power. In those circumstances in which the increase in market power still leads to lower prices, there is no antitrust problem regardless of the welfare standard used. There will, however, be a problem in those situations in which the efficiencies enhance total welfare but reduce consumer welfare through higher prices.

In Figure 3, the premerger price and quantity are represented as $P_1$ and $Q_1$. What determines $P_1$ and $Q_1$ are the equality of demand (represented as $D$) and the competitive supply, which the figures shows as $MC_1 = AC_1$. The model in the figure assumes that the industry’s marginal cost (represented as $MC_1$) and average cost (represented as $AC_1$) remain constant. The merger will increase efficiency. We reflect this as the decrease in costs from $MC_1 = AC_1$ to $MC_2 = AC_2$. If market power due to the merger does not increase, the cost savings will be passed on to consumers. Postmerger, the price will fall to $P_2$ and the quantity will rise from $Q_1$ to $Q_2$. Under this scenario, the merger should not raise competition law concerns since the

217. Id. ¶ 16.
218. Id. ¶ 31 ("As indicated above, for input foreclosure to lead to consumer harm, it is not necessary that the merged firm’s rivals are forced to exit the market. The relevant benchmark is whether the increased input costs would lead to higher prices for consumers. Any efficiencies resulting from the merger may [sic], however, lead the merged entity to reduce price, so that the overall likely impact on consumers is neutral or positive.").
219. See Case No. COMP/M.4854, TomTom/Tele Atlas (May 14, 2008), http://ec.europa.eu/competition/mergers/cases/decisions/m4854_20080514_20682_en.pdf (declaring a concentration to be compatible with the common market and the EEA Agreement).
220. Id. ¶ 250.
221. Due to the perfectly elastic competitive supply curve, all of the cost saving is passed on to consumers when the market remains competitive. If the supply were positively sloped, not all of the cost saving would be passed on, but output would still rise and price would still fall.
welfare effects are positive—both consumer welfare and total welfare increase.222

Figure 3: Mergers Specific Efficiencies: the Welfare Tradeoffs

Under an alternative scenario, there is a merger in which market power increases as a result of an efficiency-enhancing merger. In Figure 3, let us assume that the merger leads to the same cost savings as before. However, unlike before, the exercise of the market power that results from the merger leads to an increase in price from $P_1$ to $P_3$. This leads to a corresponding decrease in quantity from $Q_1$ to $Q_3$. From a consumer welfare framework, the merger is undesirable. The consumer has experienced an increase in the price paid. Moreover, the consumer also does not appear to benefit from the cost reduction that has occurred as a result of the merger. Figure 3 measures this as the allocative inefficiency resulting from market power postmerger that causes consumer welfare to fall from area $acP_1$ to area $abP_3$. If the lawfulness of the merger under the legal regime is determined solely on the basis of consumer welfare, the result is that in this market, the merger would be unlawful.

Examining the same scenario but from the lens of total welfare, the lawfulness of the merger may be different. Two issues arise in this context.

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222. For a similar result, see Motta, supra note 6, at 261–62.
First, whether total welfare rises or falls depends on the relative magnitudes of the allocative inefficiency and the cost saving. In Figure 3, we represent the allocative inefficiency by the triangular area bcd. The postmerger profit to the sellers is equal to the rectangle $P_3beP_2$. Part of this, area $P_3bdP_1$, is a transfer from consumers to producers, while rectangle $P_1deP_2$ represents the cost saving. Given how Figure 3 has been drawn, the cost saving as a result of the merger appears to be larger than the allocative inefficiency from the merger. When this is the result of a merger, the merger should be lawful under a system that follows a total welfare standard because the benefits of the cost saving outweigh the allocative inefficiency. Indeed, from a Kaldor-Hicks cost-benefit analysis, under this scenario the merger is efficient because the winners of the merger (the producers) would be able to compensate the losers of the merger (the consumers) and still be better off.$^{223}$

This possible outcome is not the only one that could arise after the merger. There may be circumstances in which the allocative inefficiency will outweigh the postmerger cost saving. Under such circumstances, the merger will reduce both consumer welfare and total welfare. As a result, the joint venture will be inefficient on the Kaldor-Hicks criterion because it will not be possible for the winners of the merger (producers) to profitably compensate the losers of the merger (consumers). Under both a total welfare and consumer welfare standard the merger should be unlawful and forbidden.

Even if the welfare standard is exclusively consumer welfare, it is important to note that the cost savings of the merger described above benefit consumers generally. It is the case that these cost savings will improve the sellers’ profits in this market. However, an inference that would dismiss these cost savings as inconsequential to consumers would be mistaken.$^{224}$ The costs of production that sellers face decrease as fewer of society’s scarce resources are needed to produce the output being sold.$^{225}$ Consequently, these resources are available to be redeployed to produce goods and services in other markets. Even though the consumer benefits that flow from these cost savings may be diffused throughout the economy, they still exist.$^{226}$

This economic analysis shows that it is possible for a merger to be allowed under a total welfare standard but blocked under a consumer welfare standard. If this merger is efficiency enhancing both domestically


224. We are not counting the cost savings twice. One may dismiss them as beneficial to the sellers, but they should be considered for their benefits to consumers.

225. We are not referring to the resources not being used because output has been reduced from $Q_1$ to $Q_2$. We are instead referring to the resources now needed to produce $Q_3$.

and globally, it could still be blocked in Europe but not in the United States, given existing case law. Thus, a merger that enhances total welfare globally may not go through (even if it is total welfare enhancing in each jurisdiction) because the welfare standards of the two antitrust powers differ with regard to merger efficiencies.

CONCLUSION

Divergence across goals of antitrust impact both antitrust law and policy. In the United States, goals of antitrust are exclusively economic ones. In Europe, there are some political noneconomic goals in addition to economic goals. Over time, E.U. case law and policy will recognize that the only goals that will impact antitrust are economic ones. This seems to be the trend within DG Competition, although the courts and legal academics have not yet followed this trend as strongly. However, the transition to exclusively economic goals across jurisdictions is not without peril. Welfare standards as between total welfare and consumer welfare are not always clear. Moreover, the choice of welfare standards might lead to divergent outcomes both within a single antitrust system and across antitrust systems. We demonstrate how such divergence plays out in the examples of RPM and merger efficiencies.

In a best-case worldwide scenario, we believe that total welfare should guide antitrust. However, when given the choice between political factors playing a role in antitrust analysis versus a standard of consumer welfare, we choose consumer welfare as a second best standard to bring economic clarity to the law and policy of antitrust globally.
Notes & Observations