

# **WHY ANTITRUST MATTERS**

## **by William A. Markham, San Diego Attorney © 2006**

### **The True Purpose of Antitrust Law**

The antitrust laws are supposed to promote and protect competition. This alone is their proper purpose. They are not intended to punish big companies merely on account of their size, nor to serve as surrogate "consumer protection" laws. Most importantly, they have never been anti-market or anti-business in their underlying conception or in their implementation. On the contrary, the antitrust laws are intended to promote market economics and healthy competition in every market, while checking the abuses that sometimes arise in different markets.

The idea behind these laws is that in every market there should be robust competition: If in each market there are many sellers busily competing against one another to sell a particular kind of product or service to paying customers, no one seller will be able to take unfair advantage of the buyers, but rather each seller will be obliged to offer its good or service on attractive terms, and each seller will be responsive and efficient in its dealings with buyers, who otherwise will simply turn to another, better seller.

In other words, vigorous competition in any given market keeps the sellers honest, forcing them to strive continually both to improve their goods and services and to offer them on favorable terms. Customers benefit from this competition. Poorly run companies are run out of business, as they deserve to be. The better run companies, and the most honest ones too, tend to prosper. Society as a whole benefits.

This is nothing other than the glory of marketplace economics working properly and rewarding each of us for our efforts, our talent, and our perseverance. The antitrust laws exist to help marketplace economics to work better.

### **The Origins of the Antitrust Law**

American antitrust laws were intended to break up the enormous family "trusts" that in the late 1800s came to dominate banking, oil production, rail transport, shipping, steel production and a handful of other key industries in the United States.

Many Americans resented the enormous accumulation of power and wealth that this handful of families acquired from their dominance of these key markets, and others grew alarmed that these dominant firms would abuse their market power in order to exact unfair advantages from their customers, doing so precisely because they had eliminated their rivals and now had unchecked power in the different markets that they totally controlled.

### **Anti-Business or Pro-Competition?**

This is where the confusion arises. The antitrust laws were never intended to indulge the clamorings of anti-business populists, such as William Jennings Bryan or his socialist fellow travelers in Europe. To such populists, it was unfair that these industrial barons should have so much affluence and power, while millions of other labored in misery for a pittance, without any social protection or any prospect of improving their sorry lot in a cruel world.

The antitrust laws, although enacted to redress the abuses imposed or threatened by the great trusts, were never intended to accomplish the anti-business, anti-market purposes of the turn-of-the-century populists. Both the populists and the antitrust laws decried the same abuses done by the same trusts, but each had very different purposes in mind.

For the antitrust laws serve to promote and protect market economics, doing so on the theory that society flourishes the most when it is founded on vigorous competition: According to this theory, competition brings forth the best in each of us, keeping each of us on our toes, mindful that if we do not perform well, we will be cast aside for someone else who can perform better. It is a harsh logic, and it works very well because it rightly understands and anticipates actual human nature and human psychology in action.

Promoting competition as an end in itself might be harsh economic policy, but it works better than all the others because it is based on an accurate understanding of what motivates human beings most the time in most their dealings with one another. To paraphrase Adam Smith, the baker does not ask himself whether you might wish to enjoy some of his excellent bread this evening with your meal. No, he wants you to give him money, and thus he strives to make excellent bread so that you will be persuaded to purchase your bread from him and not from some other baker.

The populist, in contrast, expects each of us to be selfless and altruistic, asking ourselves, "what is best for our society as a whole?", and "how can society aid those who are ailing?" He then expects the general population to make sacrifices to give effect to these wonderful, ambitious sentiments. These sacrifices usually come in the form of onerous taxes, which are paid to the government, which uses them in theory to provide social services to the needy and for other worthy social causes.

But this populist approach to inequality and misery, however well-meaning in theory, seems rarely to work in practice: Human beings seem above all to be motivated by selfish behavior, at least in their dealings with strangers. A mother might well love her children so dearly that she will walk through a wall of fire at mortal risk to herself to save one of them from the flames. But when she goes to market to buy her bread for her family, she wants the best bread at the lowest price, and the baker and his family can go to the devil if he cannot provide this for her. (The author of this article would argue that there are certain public services that the government alone is best placed to provide, but that the role of government must always be sensibly limited, and that each of us must be kept constantly on our toes by the demands of marketplace economics.)

The antitrust laws exist not to help populist business-bashers dismantle successful, prosperous companies, even the most dominant global monopolies of the era. Rather, these laws are meant to redress or temper the fundamental flaw that seems inherent to unbridled competition. A word of explanation is in order. Competition is the best market system for human beings, so the theory goes, because each of us goes to market to do selfish bidding for ourselves and our families. We will produce the best goods and services, doing so at the best prices, only because if we fail to do so our customers will abandon us and buy from another; and when we ourselves buy goods or services, we will look to the seller who can provide them on the most favorable terms, taking into account considerations of quality, price, and delivery, etc. Thus antitrust laws promote market economics and are never to be confused with antimarket economics. Antitrust laws do not punish big businesses merely because they are big and successful. Success rather is the proper reward to those who labor well or who provide excellent goods and services to their customers. This is what motivates

us in the first place to do well. Success must be encouraged, not envied or resented, much less punished by government confiscation (i.e., taxation and redistributive policies).

### **The Besetting Flaw of Market Economics**

Rather than punish successful firms or proscribe free markets, as the populists seem to want, the antitrust laws seek instead to perfect the markets by "correcting" the inherent contradiction of market economies, which is as follows: In many key markets, one firm or a clutch of major firms often come to dominate the entire market. Once this happens, competition in this market ceases altogether or at best becomes a pale shadow of its former self. If, say, one company alone sells computer operating software for nearly all personal computers, the users of personal computer find themselves too much at its mercy and too vulnerable to its depredations. The dominant company might well have become dominant because it makes a better or less expensive product or has been more astute at spotting and exploiting commercial opportunities. But once this firm becomes the only competitor, it will no longer be kept on its toes by the threat of superior competition. It will find that "it is the only show in town", and it will naturally look for ways to exact bigger profits and more onerous concessions from its captive customers. The law of tendencies makes clear that it is only a matter of time before the dominant firm abuses its customers. Over time the market controlled by a single firm or handful of firms will no longer enjoy the expected, ordinary benefits of robust competition – competitive pricing, quality in production, superior service, and constant, impatient innovation.

The antitrust laws serve to check and redress the abuse of market dominance. It punishes (1) those who acquire market dominance by improper means, and (2) those who, having acquired market dominance by proper means, have abused it since obtaining it. It also punishes the conspiracies, both express and tacit, that powerful firms sometimes try to impose across entire markets in order to consolidate market power and exact unfair benefits. These are the true purposes of the antitrust laws.

Put another way, the antitrust laws presuppose that unrestrained market competition is the best method of promoting lasting prosperity and wealth for the greatest number. But unrestrained competition, put into practice, often leads to the emergence of stultifying monopolies and oligopolies that take unfair advantage of their customers while hindering innovation and commercial excellence. This is the great and eternal contradiction of market economics, and it is this contradiction that the antitrust laws seek to redress.

It is a difficult task precisely because it arises from a fundamental contradiction: Markets should be left alone and left to regulate themselves, save when a market becomes corrupted by a predatory monopoly or is harmed by predatory trade impositions – both of which seem inevitably to occur in unregulated markets of certain kinds. The underlying logic of the antitrust laws would seem to arise from this very contradiction, and can be summarized as follows: Leave the markets alone, knowing that in time the winners will abuse their victorious position, and then regulate or punish the victors; and always punish those who collude to impose trading shams. The antitrust laws should serve to regulate or punish the offending monopoly or trade practices.

### **What Antitrust Laws Try to Accomplish**

Antitrust laws, properly understood, are intended to grapple with this market contradiction. In particular they forbid any improper monopoly or any attempt to obtain a monopoly by improper means (i.e., a monopoly obtained or attempted by a firm that on purpose has

destroyed or tried to destroy its competitors, using anticompetitive tactics whose sole purpose has been to undermine competitor businesses). These laws also forbid dominant firms to act in collusion in order to impose unfair commercial practices that impose upon any market that they dominate or aim to dominate by means of the improper practice, and they also outlaw various kinds of recognized commercial fraud that are always deemed to be so anti-competitive as to be per se unlawful (i.e., bid-rigging, price-fixing, etc.).

### **The Charter Principles of Antitrust Law**

The antitrust laws strive to set forth a series of general propositions that serve as the "charter principles" of marketplace economics in the United States. I think these charter principles and their corollaries can be summarized as follows:

1. It is always improper to acquire monopoly power by means of business practices whose only purpose is to undermine or destroy business rivals. If your computer software is so good or so inexpensive that everyone buys only from you, then you have won in the marketplace and have obtained a proper monopoly. If you use business methods calculated to crush rival makers of software, and if by such methods you acquire or perpetuate your monopoly, you have committed an antitrust offense.
2. It is also improper to attempt to acquire a monopoly by means of such predatory or anti-competitive business practices, and it is likewise improper to conspire with others to try to do so or to succeed at doing so. Any such effort constitutes an antitrust offense.
3. It is likewise improper for two or more firms to act in concert or conspire in order to impose predatory or anti-competitive schemes in a market in which they jointly wield significant power or control. The litany of such abuses is as long as the imagination of the wily managers of the bigger firms in each market. But any time two or more firms collude to impose unfair trade restraints in a market that they control, their effort constitutes an antitrust offense, or least arguably constitutes such an offense.
4. It is always improper for two or more ostensible competitors to agree in secret to set prices (price-fixing), pre-arrange competitive bids (bid-rigging), divvy up customers in a market by pre-arrangement (horizontal market allocation), or provide a necessary product or service only on condition that the buyers also purchase another product or service (unlawful tying). Any such practice, however ingeniously characterized, is an antitrust offense if it is detected and proven.
5. There are other, more technical wrongs that likewise constitute antitrust offenses: For example, it is an antitrust offense for two firms to agree to an exclusive supplier or exclusive dealer arrangement, if the arrangement unreasonably harms competition or tends to give rise to a monopoly.
6. It is sometimes improper for two competitors, however honest, to merge or otherwise unite, if by so doing they significantly diminish competition in markets in which they have been competitors. A proposed merger or acquisition, if it is large enough, must therefore usually obtain advance clearance from antitrust authorities, such as the Federal Trade Commission (this is another topic, fit for a book or volumes of books all on its own).

These then would be the grand principles of the marketplace enshrined in the antitrust laws that have served us so well for more than a century.

### **How Some Other Countries Approach the Same Issues**

The author of this article would argue that "competition authority" in Europe is too inclined to regulate and lay a restraining hand on marketplace economics, but it seems to be improving over time, and it has certainly played a useful role in penalizing national discrimination by one EU country against firms from other EU countries.

Mexico in contrast suffers from a dearth of competition law: It too much resembles a "corporatist" society in which key industries are utterly controlled by a clutch of inter-connected firms. The new president, Felipe Calderon, has made some excellent comments on the subject and appears far more inclined than any of his predecessors to redress the abuses and price manipulations imposed by the hitherto unchallenged oligopolies in telecommunications, construction, retailing, banking, and financial services.

The United States seems to do very well in comparison to either Mexico or the European Union, but our antitrust laws rely too much on criminal law enforcement, which should be reserved only to punish outright fraud, such as bid-rigging, extortion, and price-fixing by cartels.

The antitrust laws of Canada are similar to our own laws, but have less emphasis on criminal punishment. The Canadian competition authorities treat competition issues as matters best suited for private litigation and civil decrees, not criminal enforcement, which seems to be sensible. On the other hand, the Canadians have mostly copied our antitrust innovations and then devised clever modifications of them. We have been the ones to lead the way.

### **Curse or Blessing?**

Critics of the antitrust laws plausibly argue that these laws serve in the end merely to punish, restrain and burden the most successful competitors of every market, thereby causing enormous injury to competition. They thus argue that the antitrust laws are harm the very thing they say they are intended to protect – competition in the marketplace.

For these critics, the antitrust laws are self-contradictory, self-defeating nonsense. Worse than that, they are an expensive nuisance and a crippling burden to our most successful firms, and our economy cannot afford such burdens in this new era of globalization and outsourcing.

The critics have a point. Antitrust laws are uncertain in their application, and compliance with them can be onerous and expensive. If a firm is sued in antitrust case, it will likely be obliged to pay substantial or onerous sums to its attorneys and experts, and some of its key officers will have to devote much of their time to preparing the firm to defend itself in the case. In the meantime, the firm will likely suffer bad press. Even if the firm at length "wins" the case (i.e., is exonerated of any liability for antitrust misconduct), it will find that it has lost money, effort, time and goodwill. This scenario brings to mind the old saw about lawsuits: "I have been twice ruined in my career; once when I went to the courts and lost; and a second time when I went to the courts and won!"

But the alternatives are worse. If there were no antitrust laws, a dominant firm or handful of firms would emerge in many markets, especially the really important ones, such as

telecommunications, energy markets and various others in which there are significant "barriers to entry". These firms would not only exclude all other competitors, but also tend to impose unfair trading terms on their business partners and ultimate customers, while failing to keep fit and responsive because of the dearth of competition from rivals.

Unfettered competition leads to monopolies in too many kinds of commerce. Monopolies in turn tend to become unresponsive to customers, less efficient, and more likely to impose abusive trading terms in the markets that they control. The antitrust laws provide remedies for such anti-competitive behavior: Stiff damages and fines, injunctions, consent decrees and various other measures.

We need antitrust laws to redress this fundamental contradiction of marketplace economics (see above). Yes, the antitrust laws are horrible, ruinous abominations that arise from an inextricable contradiction that they do not resolve, and they involve us all in wasteful litigation and suffering. But as Winston Churchill might have said, the antitrust laws have the benefit of being better than all the alternatives.

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