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HOW ENFORCEMENT AGAINST PRIVATE ANTICOMPETITIVE CONDUCT HAS CONTRIBUTED TO ECONOMIC DEVELOPMENT

Contribution from the United States

-- Session IV --

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HOW ENFORCEMENT AGAINST PRIVATE ANTICOMPETITIVE CONDUCT HAS CONTRIBUTED TO ECONOMIC DEVELOPMENT

1. This paper provides brief descriptions of past enforcement actions by the US antitrust agencies and of the economic effects of these actions. The first section describes FTC enforcement in the healthcare sector; the second describes DOJ enforcement in the telecommunications sector.

2. The U.S. Federal Trade Commission's Antitrust Enforcement Program in Health Care: the *American Medical Association Case* and Its Progeny

Introduction

3. One of the most noteworthy developments in U.S. competition policy in the 1970s was the decision of the Department of Justice (DOJ) and the Federal Trade Commission (FTC) to devote significant resources to law enforcement involving restraints of trade in the professions.¹ In a substantial number of antitrust cases initiated in this decade, the federal enforcement agencies opposed restrictions on pricing, advertising, and marketing that associations of professionals imposed upon their members.²

4. As a vehicle for considering the economic impact of antitrust enforcement against private trade restraints, this paper reviews one of the FTC's most influential contributions to competition policy involving the professions -- an administrative case brought in 1975 against the American Medical Association (AMA). The paper first summarizes the content and outcome of the proceeding and then considers its economic consequences.

1. The American Medical Association Litigation

5. Measured by total membership and its influence on the standards of practice for the medical profession, the AMA is the leading U.S. professional association for physicians. As the principal professional group in the field, the AMA and its policies play a major role in determining how markets for health care function in the United States. As described below, the FTC's decision to challenge the AMA's practices had major implications.

1.1 Background and Resolution of the AMA Case

6. In December 1975, the FTC issued an administrative complaint against the AMA and alleged that the association unreasonably had restrained trade by imposing ethical restrictions on advertising, solicitation, and other various activities of its members. Following an elaborate administrative trial and review by the Commission, the FTC found many of the restrictions in question to be illegal horizontal restraints of trade.³ The Commission issued an order that, among other provisions: directed the medical association to cease any actions that forbade members from soliciting clients by advertising or submitting bids; interfered with the setting of fees; characterised as unethical the use of a closed panel or other health care delivery plans; or characterised as unethical the participation by non-physicians in the ownership or management of health care organisations that provide the services of physicians. The FTC decision accompanying the order emphasised that the Commission would not upset AMA initiatives to curb deceptive advertising and marketing activities.

7. The AMA contested the FTC's ruling on two fronts. The first was to seek appellate review in the courts. The Commission's decision was upheld in 1980 by a divided panel of the court of appeals and affirmed by a 4-to-4 vote of the U.S. Supreme Court in 1982.⁴ The second front was to pursue a

legislative exemption from FTC oversight. In the late 1970s and early 1980s, the AMA and various other professional societies mounted a vigorous campaign to persuade the U.S. Congress to withdraw the FTC's jurisdiction to challenge anticompetitive behaviour involving the professions.⁵ Following contentious debate, Congress declined to enact a dispensation for the professional groups.⁶

1.2 Related Developments at the FTC

8. The prosecution of the *AMA* case catalysed far-reaching developments at the FTC. The case led the FTC to devote increasing resources to challenging anticompetitive restrictions imposed by other health care associations and other professionals.⁷ Since the mid-1970s, health care cases have constituted the largest component of FTC non-merger enforcement, and this emphasis endures today.⁸ The concern with competitive restrictions adopted by health care professionals also led the FTC to use its consumer protection authority to adopt trade regulation rules to attack anticompetitive restrictions on advertising. The most important initiative of this type, adopted in the late 1970s, was the "Eyeglasses Rule," which preempted state laws restricting the price advertising of eyeglasses and eye examinations and forbade advertising bans established by professional and trade associations.⁹

2. Economic Consequences of the *AMA* Case and Related Matters

9. The FTC historically has conducted or sponsored relatively few projects to assess the effects of its antitrust cases. In the late 1970s and the early 1980s, the FTC contracted with academic economists to evaluate the effects of several past FTC vertical restraints cases and one dominant firm matter. The Commission published the vertical restraints studies¹⁰ and authorised the author of the dominant firm study to publish his results.¹¹ In the 1990s, the FTC published studies by members of its professional staff concerning FTC merger enforcement in the soft drink industry¹² and the implementation of divestiture decrees obtained by the agency in merger cases.¹³ More recently, FTC staff members or academic consultants have authored or co-authored papers that assess the effects of hospital mergers.¹⁴ The staff of the FTC presently is conducting retrospective assessments of the effects of the agency's merger enforcement policy involving the hospital and petroleum sectors.

10. The FTC has not undertaken an empirical study of the effects of its *AMA* case. Nonetheless, a substantial body of empirical work provides an informative perspective on the economic effects of the FTC's decision to bar the AMA from adopting or enforcing ethical guidelines that forbid advertising or restrict price competition by physicians. Since the early 1970s, a large number of researchers (some affiliated with the FTC, but most being outside academics who published papers based on their own work) have performed empirical studies and have shown that restrictions upon truthful advertising by professions tend to increase the prices for such services.¹⁵ From this body of work one reasonably can infer that the FTC's cases against professional association practices that suppress truthful advertising have tended to benefit consumers.

3. Postscript: The Role of Ex-Post Evaluation in Competition Policy Making

11. Ex-post analysis provides a valuable means for a competition agency to improve the quality of its enforcement program by developing a more confident basis for judging what works and what does not.¹⁶ Nonetheless, for a number of reasons, an agency might regard retrospective assessments with suspicion – because they pose difficult methodological challenges, because evaluations divert resources from new cases or investigations, or because evaluations could show that specific cases had no impact or yielded perverse results. The methodological challenges are formidable, but researchers have made encouraging progress in trying to surmount them. Resource constraints are likewise important, though spending funds on evaluations perhaps ought to be viewed as a necessary element of the enforcement process itself – the

collection of feedback that shows whether the agency's enforcement priorities and analytical tools are sound.

12. The concern that ex-post studies may show that the agency achieved poor results is understandable, but it is not a persuasive basis for declining to ask, and seek answers to, difficult questions about enforcement effects. It would be dismaying to the public and to business operators to know that a competition agency avoided retrospective assessments because it feared the results. A competition agency's conscientious pursuit of an analytically rigorous, well-disciplined system for selecting cases ex ante ought to help ensure over time that evaluations of effects reveal outcomes that, more often than not, improved consumer well-being. As the OECD Secretariat's background note suggests, the long-term legitimacy of a competition system may depend substantially on its willingness to make this dimension (enforcement consequences) of its operation more transparent and to show empirically that enforcement delivers good economic results.¹⁷

Local and Long Distance Telecommunications

13. It is often difficult to identify with specificity the broad economic impact of individual antitrust enforcement actions, particularly in a sector, such as telecommunications, that is characterised by extensive state and federal regulation and in which there are continuous technological advances. That said, sound enforcement of the U.S. antitrust laws has played a critical role in lowering the cost of telecommunications services in the United States; this, in turn, has contributed significantly to economic progress and enhanced consumer welfare. In addition to the role of federal and state regulation, the implementation of consent decrees resulting from Department of Justice antitrust enforcement actions has helped to shape local and long distance telecommunications markets in the U.S. For long distance services, competition was originally fuelled by the 1982 Modification of Final Judgment ("MFJ"), which ended the Antitrust Division's case against AT&T and resulted in spin-offs from AT&T of what became the seven Regional Bell Operating Companies (RBOCs). Among other things, the MFJ prohibited the RBOCs from providing long distance services.

14. Building on the MFJ, the Telecommunications Act of 1996 completely rewrote the landscape. The 1996 Act established a process for the RBOCs to gain authority to provide long distance service to customers within their local areas. Competition has intensified since 2001 as the RBOCs have sought this authority. Consumers have enjoyed a steady decline in prices over time.¹⁸ According to FCC data, average revenue per minute fell from 32 cents at the time of the MFJ to about 10 cents in 2001,¹⁹ even before widespread RBOC entry. While investors worry about the profitability of the long distance services sector, consumers have continued to benefit. The RBOCs have received authority to provide long distance service in 46 (of our 50) states and the District of Columbia since January of 2001. (Authority in New York and Texas was granted earlier.) The Department of Justice has played a major role in this process. First, the Department provided extensive comments to assist the FCC in developing appropriate standards to use in reviewing applications. The Department also interacted with state regulators, competitive local exchange carriers (CLECs), RBOCs, and the FCC to discuss and resolve issues raised in applications, and filed evaluations with the FCC that analysed the potential for competition by examining whether the local market was fully and irreversibly open to competition. Under the Act, the FCC was required to give substantial weight to the Department's evaluations.

15. Since gaining this authority, the RBOCs have captured significant numbers of customers from long distance providers, especially residential customers.²⁰ For example, FCC data shows that from 2000 until 2002, one RBOC's (Verizon's) share of households for long distance services increased from 13 to 28% in the northeast region.²¹ Another RBOC (SBC) increased its share in the Southwest region from 3% to 24% over the same period.²² These regions include the states in which these RBOCs respectively first gained the new long distance authority. Other RBOCs appear to be making similar gains in their regions.²³

The RBOC entry has also stimulated changes in marketing tactics, including the proliferation of bundled offerings by both RBOCs and long distance carriers. Consumers in many areas can now buy local, long distance, and in some cases, high-speed Internet and wireless services from one provider at a discounted, flat rate.

16. At the time of the 1996 Act, the RBOCs provided virtually all local telecommunications services. The advent of competition in this sector has been slow but steady.²⁴ FCC figures suggest that by 2002, CLECs served over 13% of local lines nationwide.²⁵ This represents all modes of entry allowed by the Act, including resale, use of unbundled network elements ("UNEs"), and facilities-based. In many areas and for some customers, the numbers are significantly higher. In some states, CLECs now serve over 33% of business customers using their own facilities.²⁶

NOTES

1. The origin of these initiatives is difficult to identify precisely, but a formative event was the lawsuit initiated by DOJ in the first half of the 1970s to challenge restrictions on competitive bidding by a major professional association, the National Society of Professional Engineers. The DOJ case generated a landmark ruling of the U.S. Supreme Court that, in the course of striking down the challenged restrictions, expressed acute skepticism about the defendant's arguments that the competition ethic embodied in the U.S. antitrust laws posed a serious social and economic danger if it were allowed to govern the supply of professional services. *See* National Society of Professional Engineers v. United States, 435 U.S. 679, 692-96 (1978) (considering and rejecting the argument of the defendant professional association that uninhibited competitive bidding "would lead to deceptively low bids, and would thereby tempt individual engineers to do inferior work with consequent risk to public safety and health." The decision marked a major turning point in modern U.S. horizontal restraints jurisprudence and the application of competition policy to professional groups. The significance of these developments in modern U.S. competition law is examined in William E. Kovacic & Carl Shapiro, *Antitrust Policy: A Century of Economic and Legal Thinking*, 14 *Journal of Economic Perspectives* 43 (2000).
2. *See* William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 71 *Antitrust Law Journal* 377, 426-30 (2003) (highlighting the DOJ and FTC's professions cases of the 1970s as a major ingredient of the U.S. trend toward making horizontal restraints the centerpiece of government civil non-merger enforcement).
3. American Medical Association, 94 F.T.C. 701 (1979).
4. American Medical Association v. Federal Trade Commission, 638 F.2d 443 (2d Cir. 1980), *aff'd by an equally divided Court*, 455 U.S. 676 (1982).
5. The lobbying campaign by the AMA and other professional associations to persuade Congress to exempt them from FTC jurisdiction is described in Joe Sims & Tom Smith, *FTC Assault: A Modern-day Roman Circus*, *Legal Times*, Dec. 10, 1979, at 18.
6. The main legislative proposal would have terminated pending FTC matters (including the AMA case) involving the legal, medical, and dental professions. *See* Senator Proposes Limitations on FTC's Jurisdiction Over Professional Groups, 938 Bureau of National Affairs Antitrust & Trade Regulation Reports A-22 (Nov. 8, 1979). The professional associations marshaled substantial political support. The measure to deny the FTC jurisdiction over the professions failed by two votes to gain the approval of the U.S. Senate. *See* William E. Kovacic, *The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement*, 17 *Tulsa Law Journal* 587, 664-67 & n. 442 (1982) (describing legislative deliberations).
7. Several FTC cases inspired by the AMA litigation deeply affected U.S. jurisprudence. *See, e.g.*, California Dental Ass'n v. Federal Trade Commission, 526 U.S. 756 (1999) (rejecting FTC attack on advertising restrictions imposed by dentists' group); Federal Trade Commission v. Superior Court Trial Lawyers Ass'n, 493 U.S. 411 (1990) (upholding FTC decision to condemn boycott by attorneys seeking to force local government to raise fees paid for representing indigent criminal defendants); Federal Trade Commission v. Indiana Federation of Dentists, 476 U.S. 447 (1986) (upholding FTC ban upon professional association's efforts to prevent its members from fulfilling requests of insurance companies to obtain patient x-rays to evaluate insurance claims).
8. *See* Timothy J. Muris, Chairman, U.S. Federal Trade Commission, "Everything Old Is New Again: Health Care and Competition in the 21st Century" (Nov. 7, 2002) (remarks before 7th Annual Competition in Health Care Forum, Chicago) (reviewing FTC competition policy health care agenda), *available at* <http://www.ftc.gov/speeches/muris/murishealthcarespeech0211.pdf>.

9. On the FTC Eyeglasses Rule, see Dorsey D. Ellis, Jr., *Legislative Powers: FTC Rule Making*, in *The Federal Trade Commission since 1970: Economic Regulation and Bureaucratic Behavior* 161, 166-68 (Kenneth W. Clarkson & Timothy J. Muris eds., 1981).
10. See Federal Trade Commission, *Impact Evaluations of Federal Trade Commission Vertical Restraints Cases* (Ronald N. Lafferty et al. eds., 1984) (vertical restraints studies).
11. See Timothy Bresnahan, *Post-Entry Competition in the Plain Paper Copier Market*, 75 *American Economic Review* 15 (May 1985) (presenting results of impact evaluation sponsored by FTC concerning consequences of abuse of dominance case brought against Xerox).
12. Harold Saltzman et al., *Transformation and Continuity: The U.S. Carbonated Soft Drink Bottling Industry and Antitrust Policy Since 1980* (Bureau of Economics Staff Report, FTC, Nov. 1999), *available at* <http://www.ftc.gov/reports/softdrink/softdrink.pdf>.
13. Staff, Bureau of Competition, Federal Trade Commission, *A Study of the Commission's Divestiture Process* (1999), *available at* <http://www.ftc.gov/os/1999/9908/divestiture.pdf>.
14. See Martin Gaynor & William B. Vogt, *Competition Among Hospitals*, 34 *RAND Journal of Economics* 764 (2003) (effects of hospital merger in California); Michael G. Vita & S. Sacher, *The Competitive Effects of Not-for-Profit Hospital Mergers: A Case Study*, 49 *Journal of Industrial Economics* 63 (2001) (effects of consummated hospital merger in California).
15. See, e.g., Lee Benham & Alexandra Benham, *Regulating Through the Professions: A Perspective on Information Control*, 18 *Journal of Law & Economics* 421 (1975) (prices were 25-40% higher in markets with greater professional information controls, including advertising restrictions); Ronald S. Bond et al., *Staff Report on Effects of Restrictions on Advertising and Commercial Practice in the Professions: The Case of Optometry* (Bureau of Economics, Federal Trade Commission, Sept. 1980) (price for combined eye exam and glasses was \$29 less in cities with least restrictive advertising regimes); Roger Feldman & James Begun, *The Welfare Cost of Quality Changes Due to Professional Regulation*, 34 *Journal of Industrial Economics* 17 (1985) (total consumer welfare loss from state regulations governing optometrists that, *inter alia*, banned price advertising was \$156 million); Deborah Haas-Wilson, *The Effect of Commercial Practice Restrictions: The Case of Optometry*, 29 *Journal of Law & Economics* 165 (1986) (prices were 26-33% lower in which markets in optometrists advertised using price and non-price media); William W. Jacobs et al., *Staff Report on Improving Consumer Access to Legal Services: The Case for Removing Restrictions on Truthful Advertising* (Bureau of Economics, Federal Trade Commission, Nov. 1984) (restrictions on attorney advertising resulted in prices that were 5-10% higher); John E. Kwoka, Jr., *Advertising and the Price and Quality of Optometric Services*, 74 *American Economic Review* 211 (1984) (prices of eye exams were \$11-\$12 lower in markets with advertising than in markets with advertising restrictions); James H. Love & Frank H. Stephen, *Advertising, Price and Quality, in Self-Regulating Professions: A Survey*, 3 *International Journal of Econ. Bus.* 227 (1996) (reviewed 17 studies; restrictions on advertising generally found to have effect of raising prices paid by consumers).
16. The discussion here draws upon the rationales presented in William E. Kovacic, *Evaluating Antitrust Experiments: Using Ex Post Assessments of Government Enforcement Decisions to Inform Competition Policy*, 9 *George Mason Law Review* 843 (2001).
17. See Robert A. Katzmann, *Regulatory Bureaucracy: The Federal Trade Commission and Antitrust Policy* 205 (1980) (“[W]ithout studies indicating whether antitrust policy is technologically capable of achieving various economic goals, government is vulnerable to the charge that antitrust is a charade or a lightning rod that absorbs the frustrations of those who might otherwise push for greater state intervention in the economy.”).
18. FCC, *Trends in Telephone Service*, Report at 13-6 Table 13.4 (August 7, 2003).

19. *Id.*
20. FCC, *Statistics of the Long Distance Telecommunications Industry*, Report at 29 Table 15 (May 2003).
21. *Id.*
22. *Id.*
23. Griff Witte, *An Evolutionary Edge; Local Phone Firms Pass Long-Distance Companies*, Wash. Post, Dec. 3, 2003, at E1.
24. FCC, *Local Telephone Competition: Status as of December 31, 2002*, at Table 1 (June 2003) (for 1999-2002, CLECs shares calculated as percentage of total ILEC and CLEC end users switched access lines); FCC, *Local Competition: August 1999*, at 23; and FCC, *Local Competition*, at 6 (December 1998).
25. *Id.*
26. *See, e.g.*, U.S. Department of Justice Section 271 Evaluation for New Mexico, Oregon, and South Dakota, Feb. 20, 2003; U.S. Department of Justice Section 271 Evaluation for Minnesota, May 2, 2003.