

A UNIFYING STANDARD FOR MONOPOLIZATION: “OBJECTIVE ANTICOMPETITIVE PURPOSE”

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Most commentary on the law against monopolization under Section 2 of the Sherman Act highlights the difficulty in distinguishing aggressive competition (which society prizes) from anticompetitive exclusionary conduct (which should be condemned), as well as the controversy created by various tests for monopolization proposed since the turn of the century. This Article seeks to do the opposite. It argues that, despite the apparent differences between the key proposals in this area, a common thread can be identified. In particular, each of the proposed tests for monopolization reveals a central concern, not with the actual effect of the impugned conduct, nor with its profitability for the monopolist or the firm’s subjective intent, but with the objective purpose of the impugned conduct. There is, in fact, a unifying theme, an implicit norm, at work in Section 2 cases and commentary. The implicit norm is that a firm should not engage

in conduct which has the purpose, objectively assessed, of creating, protecting, or enhancing monopoly power by suppressing rivalry without creating proportionate benefits for consumers. The relevance of this type of purpose is reinforced by the key themes in the current, highly contentious, debate about the reform of misuse of market power laws in Australia.

INTRODUCTION

It has become customary, when discussing monopolizing conduct, to begin by applying some disparaging label to the current state of the law. Monopolization under Section 2 of the Sherman Act is said to require proof of two elements: the possession of monopoly power and exclusionary conduct.¹ The standards applicable to the second element, exclusionary conduct, have been variously described as “vacuous,”² “uncertain,”³ “elusive,”⁴ “unclear,”⁵ “unsettled,”⁶ “oxymoronic,”⁷ “in substantial disarray,”⁸ “in dire need of correction,”⁹ and plagued by “serious definitional inadequacies.”¹⁰ Or, as Lambert more recently began,

1. United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966); PHILLIP E. AREEDA & HERBERT HOVENKAMP, 3 ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION ¶ 618 (3d ed. 2008) (describing how a court’s imposition of “something more” on § 2 of the Sherman Act is generally assumed to mean conduct that qualifies as an exclusionary practice); see also 15 U.S.C. § 2 (2012) (penalizing any person or corporation who engages in monopolizing conduct as a felony punishable by a jail sentence of up to 10 years, or a fine of \$100,000,000 if committed by a corporation, or a fine of \$1,000,000 if committed by a person).

2. Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 255, 261 (2003).

3. A. Douglas Melamed, *Exclusionary Conduct Under the Antitrust Laws: Balancing, Sacrifice, and Refusals to Deal*, 20 BERKELEY TECH. L.J. 1247, 1247-48 (2005).

4. Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 ANTITRUST L.J. 3, 3 (2004).

5. Mark R. Patterson, *The Sacrifice of Profits in Non-Price Predation*, 18 ANTITRUST 37, 37 (2003).

6. Steven C. Salop & R. Craig Romaine, *Preserving Monopoly: Economic Analysis, Legal Standards, and Microsoft*, 7 GEO. MASON L. REV. 617, 649 (1999).

7. Alan Devlin, *Analyzing Monopoly Power Ex Ante*, 5 N.Y.U. J.L. & BUS. 153, 155 (2009).

8. Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals’ Costs to Achieve Power over Price*, 96 YALE L.J. 209, 211 (1986).

9. Devlin, *supra* note 7, at 155.

10. *Id.* at 156.

“[t]here is a problem with Section 2 of the Sherman Act: nobody knows what it means.”¹¹

It is true that the law on what constitutes exclusionary conduct under Section 2 remains unsettled, particularly in the absence of unifying guidance from the Supreme Court.¹² It is also true that, since the turn of the century, United States courts and commentators have proposed a variety of tests and definitions for exclusionary conduct in an attempt to resolve this uncertainty.¹³ These include the “consumer harm” test,¹⁴ the “no economic sense” test,¹⁵ the “profit sacrifice” test,¹⁶ the “equally efficient competitor” test,¹⁷ and the “proportionality” definition.¹⁸ Most commentary in this area highlights the difficulty in distinguishing aggressive competition (which society prizes) from anticompetitive exclusionary conduct (which should be condemned), as well as the differences between the major

11. Thomas A. Lambert, *Defining Unreasonably Exclusionary Conduct: The “Exclusion of a Competitive Rival” Approach*, 92 N.C. L. REV. 1175, 1177 (2014).

12. See Elhauge, *supra* note 2, at 257, 262-63 (explaining how the monopoly elements under Section 2 of the Sherman Act suffer from extensive uncertainty and that the Supreme Court’s more general monopolization standards have not provided sufficient guidance in some respects).

13. See, e.g., Herbert Hovenkamp, *The Harvard and Chicago Schools and the Dominant Firm*, in HOW THE CHICAGO SCHOOL OVERSHOT THE MARK 109, 113-114 (Robert Pitofsky ed., 2008) (highlighting questionable tests for exclusionary practices put forth by the Supreme Court and summarizing other proposed tests); Gavil, *supra* note 4, at 5, 52-65 (2004) (referring to the “exclusionary conduct ‘definition’ war” and comparing the “but-for” test, the “sacrifice” test, the “less efficient rival” test, and the “disproportionality-balancing debate” test); Steven C. Salop, *Exclusionary Conduct, Effect on Consumers, and the Flawed Profit-Sacrifice Standard*, 73 ANTITRUST L.J. 311, 312 (2006) (noting the current debate over the proper antitrust liability standard governing alleged exclusionary conduct under Section 2 and discussing the two main competing liability standards and their supporters).

14. Salop, *supra* note 13, at 313-14.

15. Gregory J. Werden, *Identifying Exclusionary Conduct Under Section 2: The “No Economic Sense” Test*, 73 ANTITRUST L.J. 413, 417 (2006).

16. Melamed, *supra* note 3, at 1255-57.

17. RICHARD A. POSNER, ANTITRUST LAW 194-95 (2d ed. 2001).

18. This definition was first put forward in Herbert Hovenkamp, *The Monopolization Offense*, 61 OHIO ST. L.J. 1035, 1042 (2000) (explaining that unlawful monopolistic conduct may be defined by acts that are reasonably capable of creating or increasing monopoly power, and producing damages that are not proportional to the resulting benefits). See PHILLIP E. AREEDA & HERBERT HOVENKAMP, 3 ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION ¶ 651a (2d ed. 2002) (defining proportionality as an element of monopolizing conduct).

approaches proposed for the characterization of exclusionary conduct.¹⁹

This Article seeks to do the opposite. This Article argues that, despite the apparent differences between the key proposals in this area, a common thread can be identified. In particular, each of these proposals reveals a central concern, not with the actual effect of the conduct, nor with its profitability for the monopolist or the firm's subjective intent, but with the *objective purpose* of the impugned conduct. There is, in fact, a unifying theme, an implicit norm, at work in Section 2 cases and commentary. The implicit norm is that a firm should not engage in conduct which has the purpose, objectively assessed, of creating, protecting, or enhancing monopoly power by suppressing rivalry, without creating proportionate benefits for consumers—an objective anticompetitive purpose.

It is necessary to clarify at the outset what is meant by “objective purpose.” A “purpose” is the end or goal which a person seeks to achieve by their act or omission.²⁰ References to purpose or intent in antitrust case law and commentary are generally references to a person's *subjective* purpose or intent. “Subjective purpose” refers to the end that the relevant person actually seeks to achieve.²¹ Proof of subjective purpose requires direct or indirect evidence of that person's actual state of mind.

“Objective purpose,” on the other hand, refers to a purpose determined without the need to refer to the person's mental state.²² It is possible to bypass evidence concerning a person's

19. See Hovenkamp, *supra* note 13, at 114 (discussing the various tests Section 2 scholarship focuses on, including a “sacrifice” test and a “no economic sense” test); see also Elhauge, *supra* note 2, at 267-68 (maintaining that the incoherency of the exclusionary conduct standard has not escaped the Supreme Court and arguing that the Supreme Court needs to provide a sound economic theory that lower courts may easily implement); Salop, *supra* note 13, at 312 (noting the debate over the proper antitrust standard governing exclusionary conduct and discussing the two competing liability tests).

20. *News Ltd v S Sydney Dist Rugby League Football Club Ltd* (2003) 215 CLR 563, 573 (Austl.).

21. Ronald A. Cass & Keith N. Hylton, *Antitrust Intent*, 74 S. CALIF. L. REV. 657, 659 (2001); see *infra* Part IV(D).

22. See Cass & Hylton, *supra* note 21, at 676 (detailing how under an objective approach, specific intent is inferred using evidence indicating a lack of credible efficiency justifications for the conduct); *infra* Part IV(D).

actual state of mind and “*attribute a purpose to an artificial or notional mind* that is deemed responsible for some act or omission.”²³ Objective purpose may be deduced from the nature of the act or omission and the surrounding circumstances.²⁴ To be clear, this is not a matter of using indirect or objective evidence to prove a person’s actual state of mind.²⁵ Rather, under an objective standard, these factors are taken into account *to determine the nature of conduct rather than the mind of actors*.²⁶ Conduct is therefore not absolved on the basis of the dominant firm’s erroneous assessment of the likely impact of its conduct, or because the firm failed to turn its mind to the likely impact of its conduct.

This Article argues that U.S. case law and commentary have been concerned with objective anticompetitive purpose as an *implicit* norm for many years. However, an objective

23. *S Sydney Dist Rugby League*, 215 CLR at 580 (emphasis added). The potential relevance of this type of purpose in the antitrust context has been recognized in the Australian case law on multilateral conduct. *See id.* at 605-06 (advocating an objective “characterization” or “classification” of the relevant purpose); *infra* Part IV(D).

24. *See Dandy Power Equip Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238, 276-77 (Austl.) (distinguishing subjective purpose—“the purpose in the mind of the person who engaged in the relevant conduct”—from objective purpose—“the purpose attributed to the act of engaging in that conduct and to be ascertained from the nature of that act of engaging in that conduct” which is “looked at in the light of the surrounding circumstances”).

25. To clarify, this Article is not concerned with the proof of “specific intent” required to establish attempted monopolization, or a criminal violation of the Sherman Act. *See* Marina Lao, *Reclaiming a Role for Intent Evidence in Monopolization Analysis*, 54 AM. U. L. REV. 151, 152 n.1 (2004) [hereinafter Lao, *Reclaiming a Role*] (contrasting the specific intent required in criminal cases from the relevant intent in civil monopolization cases). Rather, it argues that the purpose of the conduct, objectively assessed, plays a central role in characterizing unilateral conduct as anticompetitive; that is, in distinguishing vigorous competition from anticompetitive exclusion. *Compare id.* at 202-05 (detailing how the defendants’ conduct in *Aspen Skiing*, *Eastman Kodak*, and *Microsoft* were reliable and helped prove the strengths of using objective intent), *with* Marina Lao, *Aspen Skiing and Trinko: Antitrust Intent and “Sacrifice,”* 73 ANTITRUST L.J. 171, 199-201 (2006) [hereinafter Lao, *Antitrust Intent*] (explaining how “objective purpose” indicators, such as the company’s actions, illustrate its intent).

26. *See* Cass & Hylton, *supra* note 21, at 659 (detailing the use of the objective approach); Werden, *supra* note 15, at 416-17, 426 (noting that under his proposed “no economic sense” test for exclusionary conduct, “what matters are the objective economic considerations for a reasonable person” and not the state of mind of any particular decision maker); *infra* Part III(E).

anticompetitive purpose standard should be expressly recognized and articulated. This standard is justifiable as it targets the relevant harm addressed by Section 2 at the same time as improving the administrability of the standard, reducing uncertainty and the risk of over-deterrence.²⁷ Once the true standard for exclusionary conduct is identified, workable tests for applying this standard can be framed.

Laws prohibiting unilateral anticompetitive conduct have been the subject of international debate for decades, as policymakers, antitrust scholars, and agencies continue to disagree over how best to regulate the market conduct of a single firm when that firm enjoys a substantial degree of market power.²⁸

In recent years, Australia, in particular, has witnessed unprecedented controversy concerning its law against misuse of market power, largely as a result of growing dissatisfaction on the part of the competition regulator and small business groups over the operation of this law.²⁹ The debate in Australia has intensified

27. See Hovenkamp, *supra* note 18, at 1039 (advocating that a standard needs to promote social benefits by showing the legitimacy and purpose of a defendant's conduct); *infra* Parts I, V.

28. See UNILATERAL CONDUCT WORKING GRP., INT'L COMPETITION NETWORK, REPORT ON THE OBJECTIVES OF UNILATERAL CONDUCT LAWS, ASSESSMENT OF DOMINANCE/SUBSTANTIAL MARKET POWER, AND STATE-CREATED MONOPOLIES 60-61 (2007) (explaining how Brazil, Chile, France, Germany, and South Korea regulate unilateral anticompetitive conduct); Giorgio Monti, *Unilateral Conduct: The Search for Global Standards*, in RESEARCH HANDBOOK ON INTERNATIONAL COMPETITION LAW 345, 345 (Ariel Ezrachi ed., 2012) (explaining how the European Union attempted to put into law that EU antitrust provisions must prevail over national provisions when both could be applied); cf. ORG. FOR ECON. CO-OPERATION & DEV., OECD REVIEWS OF REGULATORY REFORM: AUSTRALIA 2010, at 22 (2010) (documenting the passage of an Australian law restricting actions by a corporation with substantial market share rather than market power).

29. See, e.g., AUSTRALIAN COMPETITION & CONSUMER COMM'N, REINVIGORATING AUSTRALIA'S COMPETITION POLICY: AUSTRALIAN COMPETITION & CONSUMER COMMISSION SUBMISSION TO THE COMPETITION POLICY REVIEW 78-80 (2014) (explaining how the court's various interpretations of the "take advantage" clause are not an adequate standard because they made it harder to establish when "a misuse of market power" occurred); BUS. COUNCIL OF AUSTRALIA, SUBMISSION ON THE COMPETITION POLICY REVIEW DRAFT REPORT 15-16 (2014) (summarizing how the Business Council of Australia is unsure if the Court is capable of interpreting the "take advantage" clause in a way that would ensure a fair, competitive market); Katharine Kemp, *Uncovering the Roots of Australia's Misuse of Market Power Provision: Is it Time to Reconsider?*, 42 AUSTL. BUS. L. REV. 329, 344-49

since March 2015, when the final report of the Harper Review recommended fundamental and controversial changes to the relevant law, which the government now proposes to adopt.³⁰ This Article argues that the relevance of objective anticompetitive purpose is reinforced by the key themes in the current debate concerning the potential reform of misuse of market power laws in Australia.³¹

(2014) (explaining the Senate Economics References Committee's concern over the limiting interpretation given to "take advantage" in recent Australian cases, and recommendation that the interpretation be expanded); Submission from Stephen Corones, Professor of Law, to the Competition Policy Review Committee 8-9 (Oct. 8, 2014), http://competitionpolicyreview.gov.au/files/2014/11/Corones_S.pdf [<http://perma.cc/BK5V-AMN4>] (explaining how *Rural Press* did not provide any guidance to firms because the High Court held that a well-financed firm whose predatory actions significantly decreased its competition failed to satisfy the "take advantage" clause).

30. See IAN HARPER ET AL., COMPETITION POLICY REVIEW: FINAL REPORT MARCH 2015, at 340-41 (2015) (stating that removing the "take advantage" element and changing the "purpose" test would be effective tools for Australia to utilize to limit unilateral anticompetitive conduct); Marianna Papapakis, *Harper 'Effects Test' Will Hurt Business; Lawyers*, AUSTRALIAN FIN. REV. (Mar. 31, 2015, 5:26 PM), <http://www.afr.com/business/legal/harpers-effects-test-will-hurt-business-lawyers-20150401-1mbnle> [<http://perma.cc/M72H-K3XY>] (explaining how the Harper Review's recommended changes would be easier to prove by making companies bear the burden of proving their innocence); Graeme Samuel & Stephen King, *Let Companies Compete and Consumers Take the Gains*, AUSTRALIAN FIN. REV., <http://www.afr.com/opinion/columnists/let-companies-compete-and-consumers-take-the-gains-20150407-1mfsxn> (last visited Sept. 22, 2016) (praising the Harper report as a whole, but criticizing the change in the construction of "misuse of market power"); Prime Minister Malcolm Turnbull, Joint Press Conference with the Treasurer and Minister for Small Business and Assistant Treasurer (Mar. 16, 2016), <http://www.malcolmturnbull.com.au/media/joint-press-conference-with-the-treasurer-and-minister-for-small-business-a> [<http://perma.cc/EW88-YGAR>] (recommending that the Cabinet change Section 46 to reflect the recommendations in the Harper Review); see also, e.g., Michael Roddan, *Ian Harper Slams 'Effects Test' Reform Critics for Distortion*, THE AUSTRALIAN (Jul. 26, 2016, 12:00 AM), <http://www.theaustralian.com.au/business/companies/ian-harper-slams-effects-test-reform-critics-for-distortion/news-story/88b17e5fc72f568fd15a9de49ee28437> (advocating that the Harper Review recommendations would ensure "competition on its merits" by preventing anticompetitive conduct). Following the Harper Review, the New Zealand government released an issues paper in November 2015 seeking submissions for the purpose of a targeted review of its own misuse of market power prohibition. See N.Z. MINISTRY OF BUS., INNOVATION & EMPLOYMENT, TARGETED REVIEW OF THE COMMERCE ACT 1986: ISSUES PAPER 12-13 (2015) (determining if New Zealand's competition law is effective, what factors New Zealand should use in making its determination, and what alternatives there are to New Zealand's Commerce Act).

31. See *infra* Parts II(A)(5); II(C), III(D).

This Article proceeds as follows. Part I explains the underlying rationale for laws against single-firm, or unilateral, anticompetitive conduct. Part II describes several proposals for “effects-based” tests for exclusionary conduct, which arose around the time of *Microsoft*, as well as the “substantial lessening of competition” test recently proposed to reform the law in Australia.³² It goes on to explain the criticisms of these tests—especially claims of uncertainty and over-deterrence—and responses to those criticisms by advocates of “effects-based” tests. These responses, it is submitted, reveal a fundamental concern with the objective purpose of the conduct.

Part III describes proposals for several “profit-focused” tests for exclusionary conduct, especially following the decision of the Supreme Court in *Trinko*.³³ It argues that a similarly profit-focused test, in the form of the “take advantage” requirement, has been adopted as part of the misuse of market power laws in Australia and New Zealand. While, in the United States, such tests have been proposed as a means of avoiding the uncertainty and over-deterrence of effects-based tests, they have largely been rejected as a general standard for unilateral anticompetitive conduct due to their under-inclusiveness (and sometimes over-inclusiveness). This part goes on to explain that “profit-focused” tests each represent *one method* of identifying the objective purpose of the impugned conduct, but they are too restricted in their scope to capture all significant instances of unilateral anticompetitive conduct.³⁴

Part IV considers other cases in which the case law and commentary have focused on “purpose” in the characterization of

32. See *United States v. Microsoft Corp.*, 253 F.3d 34, 58-59 (D.C. Cir. 2001) (discussing the five principles that prove the backdrop for the “effect-based” test for exclusionary conduct); HARPER ET AL., *supra* note 30, at 340 (proposing the substantially lessening of competition standard); *infra* Part II(A)(4)-(5).

33. See *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 409 (2004) (finding that Verizon's alleged behavior towards its rivals did not amount to a recognized antitrust claim under the Court's current “refusal-to-deal” jurisprudence); *infra* Pt. III(B); see generally Katharine Kemp, “Taking Advantage” of Substantial Market Power, and Other Profit-Focused Tests for Unilateral Anticompetitive Conduct, 41 MONASH U. L. REV. 655, 667 (2015) (explaining the “profit-focused” tests for unilateral anticompetitive conduct that emerged in the United States after the *Trinko* decision).

34. See *infra* Part I.

unilateral conduct. It distinguishes the concept of a “normal business purpose” or “legitimate business purpose” (which has suffered from a lack of definition³⁵), and subjective intent (which has generally been rejected as a basis for liability). It proceeds to explain that the proper focus of the exclusionary conduct standard is objective anticompetitive purpose, which brings the advantages of both a determinate standard and objective analysis. Part V concludes by arguing that, while a concern with objective anticompetitive purpose has been present in case law and commentary for many years as an implicit norm, the objective anticompetitive purpose standard should be expressly recognized and articulated.

I. RATIONALE FOR UNILATERAL ANTICOMPETITIVE CONDUCT LAWS

The objective of the law against monopolization under Section 2 of the Sherman Act is to protect the competitive process in the interests of consumer welfare.³⁶ But this law only applies where the firm possesses “monopoly power” or substantial market power.³⁷ To understand the harm addressed by Section 2 it is important to understand the threat posed by the possession of substantial market power, as well as the reasons that antitrust law nonetheless permits the possession of this degree of market power.

To an economist, “market power” is the ability of a firm to

35. See *infra* Part IV(A).

36. See Salop, *supra* note 13, at 312 (describing the response of the courts and regulators as a “consumer welfare prescription” when dealing with exclusionary conduct). In the Australian context, see for example, *Queensland Wire Indus Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177, 191 (explaining how the purpose of Section 46 is to protect the interests of consumers); *Rural Press Ltd v Australian Competition & Consumer Comm’n* (2003) 216 CLR 53, 94, 101 (explaining how the former Trade Practice Commission would consider if a firm’s actions would negatively limit consumers choice of “price, quality, availability of choice or convenience”).

37. See AREEDA & HOVENKAMP, *supra* note 1 (showing that possessing “monopoly power” is a necessary criteria to trigger prosecution and that case law shows additional behaviors such as “exclusionary practices” are also required to enforce section 2). This Article focuses on the offense of monopolization, as opposed to conspiracy to monopolize or attempted monopolization. See *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 448 (1993) (citing various offenses related to monopolization).

exercise control over price³⁸ that is, to maintain price above the competitive level—or quality below the competitive level—for a sustained period without being undermined by consumers switching or competitors entering the market.³⁹ While almost all firms in modern markets have some ability to control the price they charge,⁴⁰ Section 2 only applies to firms with a substantial degree of market power, or “monopoly power.”⁴¹ Monopoly power generally requires a showing of both a market share above 50 percent and an ability to either influence marketwide prices or impose significant marketwide foreclosure that impairs rival efficiency.⁴²

A firm’s possession of monopoly power is considered to pose several threats to the competitive process and ultimately consumer welfare. First, such firms can limit output and thereby increase price above the competitive level, reducing consumer surplus. This forces some consumers who would otherwise pay a lower price to pay more for the same product, up to their reserve price (or the limit of their individual willingness to pay). There is a wealth transfer from the consumer to the producer.⁴³

Second, and more importantly, some consumers who were willing to compensate the producer for the cost of producing the

38. See Louis Kaplow & Karl Shapiro, *Antitrust 3* (Nat’l Bureau of Econ. Research, Working Paper No. 12867, 2007), <http://www.nber.org/papers/w12867> [<http://perma.cc/UTT2-JTTK>] (defining a firm with some power over price as market power); Geoff Edwards, *The Hole in the Section 46 Net: The Boral Case, Recoupment Analysis, the Problem of Predation and What to Do About It*, 31 AUSTL. BUS. L. REV. 151, 157-58, 161 (2003) (analyzing the *Boral* court’s use of the term “market power”).

39. GUNNAR NIELS ET AL., *ECONOMICS FOR COMPETITION LAWYERS* 116 (2011).

40. Kaplow & Shapiro, *supra* note 38; Elhauge, *supra* note 2, at 330.

41. It is sometimes said that monopoly power is “the power to control prices or exclude competition.” *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956). However, it is submitted that the better view is that market power is the power to price above the competitive level (or reduce quality below the competitive level), and that a firm can price above the competitive level by either restricting its own output or by restricting the output of its rivals. Thomas Krattenmaker et al., *Monopoly Power and Market Power in Antitrust Law*, 76 GEO. L.J. 241, 247-49 (1987).

42. Elhauge, *supra* note 2, at 257.

43. See ALISON JONES & BRENDA SUFRIN, *EU COMPETITION LAW* 9 (4th ed. 2011) (describing how a monopolistic firm’s adjustment of prices and production output adversely affect consumers).

product⁴⁴ will no longer purchase the product at all as the price set by the producer exceeds their reserve price. This type of loss enriches no one. It reduces the producer's sales at the same time as reducing the number of consumers whose wants and needs are satisfied by their product, resulting in a "deadweight loss" for society.⁴⁵

Third, relative to competitive markets, monopolies create productive inefficiency and "X-inefficiency" (or managerial slack).⁴⁶ Fourth, some contend that market power also reduces innovation or dynamic efficiency—the rate at which new products come to market—arguing that the "push of competition generally spurs innovation and investment more than the pull of monopoly."⁴⁷

Given the harm that can be caused by monopoly power, some eminent antitrust scholars and policymakers have argued that it is best to prevent firms from possessing substantial market power.⁴⁸ That is, dominance itself should be prohibited. Surprisingly, in view of the school's later reputation, the high

44. Including a normal profit.

45. *Id.* at 9-10; NIELS ET AL., *supra* note 39, at 14-15.

46. See RENATO NAZZINI, THE FOUNDATIONS OF EUROPEAN UNION COMPETITION LAW: THE OBJECTIVE AND PRINCIPLES OF ARTICLE 102, at 35-37 (2011) (relying on an "X-inefficiency" graph to illustrate a situation in which production is inefficient across the industry); NIELS ET AL., *supra* note 39, at 15 (describing a "quiet life" in which firms may face less pressure to invest or innovate due to lack of rivalry). *But see* Elhauge, *supra* note 2, at 300 (arguing that the benefits of monopoly power arising from innovation will always exceed agency costs).

47. See Jonathan B. Baker, *Beyond Schumpeter vs. Arrow: How Antitrust Fosters Innovation*, 74 ANTITRUST L.J. 575, 585-86 (2007) (showing competition among firms across various industries leads to higher productivity); Jonathan B. Baker, *Preserving a Political Bargain: The Political Economy of the Non-Interventionist Challenge to Monopolization Enforcement*, 76 ANTITRUST L.J. 605, 619 (2010) [hereinafter Baker, *Preserving a Political Bargain*].

48. See HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY § 6.1 (4th ed. 2011) (exempting superior skill or products, natural advantages, economic or technical efficiency, low margins of profit, or legally used patent from liability). Williamson proposed an "expanded market failures" interpretation of dominance, arguing that enduring dominance sometimes results not from any exclusionary conduct by the dominant firm, but from the breakdown of the self-policing properties of markets, such that actual and potential competitors cannot always be relied upon to perform these self-policing functions. Oliver E. Williamson, *Markets and Hierarchies: Analysis and Antitrust Implications*, in THE MAKING OF COMPETITION POLICY: LEGAL AND ECONOMIC SOURCES 447, 450-56 (Daniel A. Crane & Herbert Hovenkamp eds., 2013).

water mark of this “structuralist” thinking came from a group of advisers at the University of Chicago. In 1968, a group of distinguished economists and lawyers led by University of Chicago Law School dean, Phil C. Neal, proposed a Concentrated Industries Act, which would give the U.S. Attorney General power to order divestiture in oligopolistic industries to the extent that no firm would have a market share in excess of 12 percent.⁴⁹ Similar views were held in Europe, particularly in Germany, under the influence of the Ordoliberal school of thought.⁵⁰

However, these views have not been accepted as a general approach to unilateral market power. Modern antitrust laws generally do not prohibit the possession of substantial market power, or even monopoly, by itself.⁵¹ The key reasons for this can be explained as follows. First, as a practical matter, it would be very difficult to determine a level at which market power should be limited: the breaking up of powerful firms would often be arbitrary and prone to dissipate socially beneficial efficiencies.⁵²

Second, some argue that monopolistic markets actually spur innovation even more than competitive markets.⁵³ Importantly, the prospect of pricing above the competitive level gives firms an incentive to outcompete their rivals by making better and cheaper

49. PHIL C. NEAL ET AL., THE NEAL REPORT (1967), *reprinted in* THE MAKING OF COMPETITION POLICY: LEGAL AND ECONOMIC SOURCES, *supra* note 48.

50. Ordoliberalism had its roots in pre-World War II Germany, where a group of professors at the University of Freiburg drafted their *Ordo Manifesto* in 1936 during the rise of National Socialism. Daniel Crane, *Ordoliberalism and the Freiburg School*, in THE MAKING OF COMPETITION POLICY: LEGAL AND ECONOMIC SOURCES, *supra* note 48, at 252; *see also* NAZZINI, *supra* note 46, at 131 n.106 (explaining the view that “avoidable monopolies,” as opposed to “unavoidable monopolies” (natural monopolies), should be required to divest themselves of components of their operations or otherwise eliminate their monopoly positions).

51. *See* UNILATERAL CONDUCT WORKING GRP., *supra* note 28, at 17-18, 40, 59-60 (allowing substantial market power derived from competitive merit with a current focus on limiting anticompetitive conduct).

52. *See* HERBERT HOVENKAMP, THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION 63 (2005) (arguing that judicially mandated breakups could harm the economy as well as grant private plaintiffs too much power to determine the market).

53. *See* JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM AND DEMOCRACY 84, 89-92, 106 (3d ed. 1950) (arguing that monopolistic practices allow for steadier innovation); *see also* David S. Evans & Keith N. Hylton, *The Lawful Acquisition and Exercise of Monopoly Power and Its Implications for the Objectives of Antitrust*, 4 COMPETITION POL’Y INT’L 203, 233-36 (2008) (illustrating examples of innovation being hindered by antitrust laws).

products, and to invest in crucial innovation to the benefit of society in general and consumers in particular.⁵⁴ Substantial market power is often achieved and maintained by a corporation's superior efficiency, innovation, and ability to meet consumer desires.⁵⁵ Third, over time, new or existing rivals will outcompete the dominant firm for the "top spot," or at least force it to compete more vigorously: the market will self-correct.⁵⁶

However, not all threats from dominance can be left to the self-correcting forces of the market. While some firms with substantial market power succeed by offering a better price or product, it is possible for firms to create, protect, or extend their market power through conduct that suppresses the rivalry of their competitors without creating any, or any proportionate, benefit for consumers ("unilateral anticompetitive conduct"). Entrenching market power in this way, through conduct that creates no benefit,⁵⁷ other than the preservation of the firm's market power, goes against the key reasons for tolerating the possession of substantial market power. Such conduct effectively blocks the self-correcting forces of the market and deprives consumers of innovative and superior offers from would-be challengers.⁵⁸ The law against monopolization is intended to

54. See *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 407 (2004); SCHUMPETER, *supra* note 53, at 106 (arguing that perfectly competitive firms are sometimes inefficient, leading to an increase in costs to consumers).

55. See *Verizon Commc'ns, Inc.*, 540 U.S. at 407 (reflecting the economic viewpoint that the prospect of monopoly profits motivates firms to innovate and that such profits are a fair reward unless accompanied by anticompetitive conduct); Herbert Hovenkamp, *Exclusion and the Sherman Act*, 72 U. CHI. L. REV. 147, 159-62 (2005) (maintaining that a dominant firm or one with substantial market power can benefit consumers through raising rival costs by superior efficiency).

56. See Frank H. Easterbrook, *When Is It Worthwhile to Use Courts to Search for Exclusionary Conduct?*, 2003 COLUM. BUS. L. REV. 345, 353 (using the rapid improvement of computer interfaces as an example where competitive firms outcompete a previously dominant firm); Fred S. McChesney, *Talkin' 'Bout My Antitrust Generation: Competition for and in the Field of Competition Law*, 52 EMORY L.J. 1401, 1412 (2003) (predicting that as prices rise due to anticompetitive contracts or practices, new competitors will alleviate or nullify the issue); see also Gavil, *supra* note 4, at 59 (asserting that even the entry of less efficient rivals can stimulate competition against a dominant firm).

57. Or no proportional benefit.

58. See HOVENKAMP, *supra* note 52, at 156 (stating companies initially enter the market using innovative practices but subsequently protect themselves by excluding new competitors); see also Jonathan B. Baker, *Exclusion as a Core Competition Concern*, 78

prevent practices such as these without unduly hindering beneficial competitive activity.⁵⁹

One matter should be clarified here. A “suppression” of rivalry does not occur simply because a rival loses a given sale or sales to the dominant firm. The better view is that the suppression of rivalry occurs when the dominant firm’s conduct significantly impairs its rivals’ ability and/or incentive to compete for future sales, or for sales other than those captured directly by the dominant firm.⁶⁰ This suppression of rivalry tends to preserve or enhance market power and reduce long-term consumer welfare.⁶¹

Inefficient monopoly-preserving conduct wastes the resources of both the excluding firm and the excluded firm.⁶² It also protects or enhances the dominant firm’s substantial market power, such that the firm can act contrary to consumer interests, undeterred by the constraints previously imposed by rivals or potential rivals.⁶³ Having regard to the objective and underlying rationale of unilateral conduct laws, a general rule against unilateral anticompetitive conduct should target conduct that tends to create, protect, or extend substantial market power by suppressing rivalry without creating proportionate benefits for consumer welfare. At the same time, the rule should leave

ANTITRUST L.J. 527, 557 (2013) (discussing a hypothetical soft drink industry that adopts “cartel”-like activity to suppress competition); Krattenmaker & Salop, *supra* note 8, at 234-38 (describing how bottlenecks and foreclosures can raise costs for rivals and suppress competition).

59. Brief of Amici Curiae Economics Professors in Support of Respondent at 3-4, *Verizon Commc’ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682) (distinguishing between anticompetitive and procompetitive conduct is difficult because both conduct is disadvantageous to rivals).

60. See B. Douglas Bernheim & Randal Heeb, *A Framework for the Economic Analysis of Exclusionary Conduct*, in 2 THE OXFORD HANDBOOK OF INTERNATIONAL ANTITRUST ECONOMICS 3, 4-5, 26 (Roger D. Blair & D. Daniel Sokol eds., 2014).

61. See NIELS ET AL., *supra* note 39, at 14-15 (noting that reducing rivalries de-incentivizes innovation while encouraging monopolies to raise prices at the direct expense of consumers).

62. See Richard A. Posner, *The Social Costs of Monopoly and Regulation*, 83 J. POL. ECON. 807, 807-08 (1975) (discussing how “deadweight loss” underestimates a variety of social costs when looking at the impact of monopolies on consumers); HOVENKAMP, *supra* note 48, at 21 (assuming that “dead weight loss” results from suppressing competition).

63. See HOVENKAMP, *supra* note 48, at 21 (looking at how companies use research and development to suppress competition while increasing the cost for consumers).

dominant firms free to exclude rivals through superior efficiency or innovation.⁶⁴

II. “EFFECTS-BASED” TESTS FOR EXCLUSIONARY CONDUCT

A. “Effects-Based” Tests in Case Law and Commentary

1. Salop and Romaine: “Unnecessarily Restrictive Conduct” Test

The early 21st century debate about monopolization standards was sparked by the most scrutinized antitrust case of the late 20th century, *United States v. Microsoft Corp. (Microsoft)*.⁶⁵ In 1998, the U.S. Department of Justice under the Clinton administration brought proceedings against Microsoft alleging that the company had engaged in monopolization and thereby contravened Section 2 of the Sherman Act.⁶⁶ The central allegations concerned various exclusionary practices adopted by Microsoft to protect its dominance in the market for computer operating systems.⁶⁷ The case was finally, and controversially, settled in the first year of the Bush administration.⁶⁸ In the meantime, it gave rise to an enormous volume of commentary on the proper characterization of unilateral conduct.

In 1999, Salop and Romaine responded to the debate surrounding the *Microsoft* case with an in-depth analysis of the conduct in question and its competitive effects, and advocated a test for exclusionary conduct based on a balancing of “motives and effects.”⁶⁹ The authors acknowledged throughout their analysis that unilateral conduct may be ambiguous: the same conduct may

64. NIELS ET AL., *supra* note 39, at 16; *see generally* ORG. FOR ECON. CO-OPERATION & DEV. POLICY ROUNDTABLES: THE ROLE OF EFFICIENCY CLAIMS IN ANTITRUST PROCEEDINGS (2012) (discussing competing efficiency theories and assessments and how they should be carried out).

65. *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001); Mark S. Popofsky, *Defining Exclusionary Conduct: Section 2, the Rule of Reason, and the Unifying Principle Underlying Antitrust Rules*, 73 ANTITRUST L.J. 435, 435 (2006); Salop & Romaine, *supra* note 6, at 617.

66. Baker, *Preserving a Political Bargain*, *supra* note 47, at 607.

67. *See id.* at 621 (summarizing allegations that Microsoft’s marketing and design of its internet browser harmed competition with no other legitimate business purposes).

68. *Id.* at 607.

69. Salop & Romaine, *supra* note 6, at 617-18, 650-51.

give rise to both consumer benefit and consumer harm.⁷⁰ Accordingly, they argued that the best antitrust standard is one that “balances the benefits and harms to consumers in the context of an evaluation of the unnecessarily restrictive conduct.”⁷¹

Salop and Romaine opposed the expansive “avoidable exclusionary conduct” test, adopted in early monopolization cases.⁷² According to this test, the dominant firm’s conduct would infringe if the firm had the ability to forego the exclusionary conduct that raised barriers to competition, such that the barriers (and resulting prices) could be said to be avoidable.⁷³ But the authors also argued against the much narrower “sole purpose and effect test,” under which exclusionary conduct would only be condemned if its sole purpose and effect were to raise barriers to competition.⁷⁴ Under this test, if the conduct had *any* beneficial effects—such as reducing costs or creating a better product—the conduct would be permitted, on the basis that the purpose and likely effect of the conduct was to achieve these efficiency benefits.⁷⁵ This test did not focus on consumer welfare effects at all, but “would condemn only naked exclusionary conduct, and conduct with pretextual or otherwise invalid claimed efficiency benefits.”⁷⁶

Salop and Romaine recommended a third test, the “unnecessarily restrictive conduct test,” as a “middle ground.” According to this approach, unilateral conduct would infringe Section 2 if a rule of reason evaluation established that the conduct was, on balance, likely to harm rather than benefit consumers—if the conduct was “unnecessarily restrictive” or

70. *Id.* at 626-30.

71. *Id.* at 618 (emphasis omitted).

72. *See id.* at 656 (arguing that this test penalizes some conduct that increases consumer welfare and is not likely to provide optimal deterrence).

73. *Id.*

74. *See id.* at 656-57 (concluding that this test is “unlikely to provide optimal incentives or optimal deterrence”).

75. *See id.* at 650 (noting that even though conduct might have both procompetitive and anticompetitive motives and effects, the procompetitive would trump the anticompetitive); *see also* Gavil, *supra* note 4, at 52-53 (supposing that a “pure application” of the Department of Justice’s “but for” test would have a similar result).

76. Salop & Romaine, *supra* note 6, at 657.

“unnecessarily exclusionary.”⁷⁷ This test would weigh “the conflicting motives and effects to determine which has the primary effect on consumers.”⁷⁸ Such a “balancing test,” they argued, would be “[well]-suited to constrain attempts to preserve and extend monopoly power through anticompetitive conduct even while permitting the monopolist to continue to compete and innovate in ways that benefit consumers.”⁷⁹

2. Salop’s “Consumer Harm” Test

Following the 2001 decision of the D.C. Circuit in *Microsoft*⁸⁰ and various proposals for profit-focused tests for unilateral conduct,⁸¹ Salop refined and expanded the approach advocated in the 1999 article. Salop labeled this refined version a “consumer welfare effect” or “consumer harm” test, explaining that this test focused “directly on the anticompetitive effect of exclusionary conduct on price and consumer welfare.”⁸² Unlike profit-focused tests, which look at the impact of the conduct on the defendant firm, the “consumer harm” test concentrates on evaluating the net impact of the conduct on consumers in each case.⁸³ According to this approach, unilateral conduct would violate antitrust laws “if it reduces competition without creating a sufficient improvement in performance to fully offset these potential adverse effect[s] on prices and thereby prevent consumer harm.”⁸⁴

Under Salop’s “consumer harm” test, a comparison is required between the effects or likely effects of the conduct on the relevant markets and the likely state of competition in the absence of the conduct.⁸⁵ The test focuses on identifying the

77. *Id.* at 652.

78. *Id.* at 659; *see infra* Part II(D)(1).

79. *See* Salop & Romaine, *supra* note 6, at 618.

80. *United States v. Microsoft Corp.*, 253 F.3d 34, 58-59 (D.C. Cir. 2001).

81. *See infra* Parts II(A)(4), III(C).

82. Salop, *supra* note 13, at 313-14; *see also* NAZZINI, *supra* note 46, at 92 (stating that the welfare effects of price discrimination depend on factors including the efficiency of intermediate firms as well as whether or not output is higher or lower).

83. Salop, *supra* note 13, at 318, 330-31, 345.

84. *Id.* at 330.

85. *See id.* at 330-31 (explaining that a “consumer harm” standard may be a more appropriate term than a “consumer welfare effect” standard because the analysis inquires if the exclusionary conduct ultimately causes harm to consumers).

counterfactual market price that would occur in the absence of the alleged anticompetitive conduct.⁸⁶ This is not necessarily the price that prevailed *before* the conduct was undertaken.⁸⁷ The counterfactual price may actually be lower than the price occurring before the conduct was undertaken if the firm engages in strategic conduct to maintain its monopoly.⁸⁸ On the other hand, if the conduct in question leads to product or service improvements, those consumer benefits should be compared with the price effect of the conduct to evaluate the net impact of the conduct on the “quality-adjusted price.”⁸⁹

Salop provided examples of how his test would address various types of unilateral conduct. For example, if a dominant firm entered exclusive dealing agreements with critical input suppliers such that its disadvantaged rival would have the incentive to reduce its output and raise its own price,⁹⁰ the conduct would be condemned due to this harmful effect on consumer welfare unless there were benefits—for instance, improvements in consumer information or product quality benefits from the elimination of free-riding—that were sufficient to reverse or offset the higher prices.⁹¹ The dominant firm’s “procompetitive rationales for the conduct” would thereby be taken into account in evaluating the overall competitive impact of the conduct on consumers.⁹² Importantly, Salop’s “consumer harm” test requires a case-by-case assessment of the net effect of the impugned conduct on consumers.

3. Hovenkamp’s “Disproportionality” Definition

Another frequently-cited standard for unilateral conduct was

86. *Id.* at 361.

87. *See id.* at 332 (explaining that courts may forego a determination of the counterfactual market price in favor of raising the competitive benefits standard higher the greater the market power harms shown).

88. *Id.* at 361.

89. *Id.*

90. A case of raising rivals’ costs.

91. *Id.* at 322-23, 336-37.

92. *See id.* at 333-34 (drawing support for this approach from the decision of the D.C. Circuit in *Microsoft*); *infra* Part II(A)(4); *cf.* Popofsky, *supra* note 65, at 445, 448 (looking at how courts identify the effect of a liability test on consumer harm before analyzing the net anticompetitive effects resulting from a firm’s conduct).

proposed by Herbert Hovenkamp, co-author of the *Antitrust Law* treatise.⁹³ In earlier editions of the treatise, the original authors, Areeda and Turner, defined exclusionary conduct as “conduct, other than competition on the merits or restraints reasonably ‘necessary’ to competition on the merits, that reasonably appear capable of making a significant contribution to creating or maintaining monopoly power.”⁹⁴

Defining anticompetitive conduct in this way raises the critical question: What is “competition on the merits”? Areeda and Turner did not offer a general definition, but instead provided a laundry list of conduct that would not offend, including “non-exploitative pricing, higher output, improved product quality, energetic market penetration, successful research and development, cost-reducing innovations, and the like.”⁹⁵

In 2000, the year before the D.C. Circuit’s decision in *Microsoft* was delivered, Hovenkamp proposed a new definition of unilateral exclusionary conduct, suggesting that “monopolistic conduct” be defined as acts that:

- (1) are reasonably capable of creating, enlarging, or prolonging monopoly power by impairing the opportunities of rivals; and
- (2) that either (2a) do not benefit consumers at all, or (2b) are unnecessary for the particular consumer benefits claimed for them, or (2c) produce harms disproportionate to any resulting benefits.⁹⁶

Hovenkamp later explained that this definition was proposed in an attempt to “craft a more general statement” on the meaning of exclusionary conduct which, unlike earlier definitions offered by the *Antitrust Law* treatise, would be capable of being administered.⁹⁷ He emphasized the need for a flexible standard. Single-firm anticompetitive conduct should not be defined too narrowly because “anticompetitive strategic behaviour by

93. *E.g.*, NAZZINI, *supra* note 46, at 93; Gavil, *supra* note 4, at 61-62; Salop, *supra* note 13, at 353.

94. Phillip E. Areeda & Donald Turner, 3 ANTITRUST LAW ¶ 626g(3) at 83 (1978).

95. *Id.* ¶ 626b at 77. These forms of competition might be summarized as low prices (based on costs) and increased output in terms of either quantity or quality.

96. Hovenkamp, *supra* note 18, at 1037, 1042.

97. Hovenkamp, *supra* note 55, at 149.

dominant firms comes in many kinds, many of which may not be known or even anticipated today.”⁹⁸

Like Salop, Hovenkamp recognized the often-ambiguous nature of unilateral conduct. Unilateral conduct laws should only condemn business conduct that is likely to create, increase, or prolong monopoly power *without giving significant benefits to society*.⁹⁹ Many competitive practices, such as innovation and aggressive pricing, can create monopoly power, but they do so by creating significant social benefits as well.¹⁰⁰ Anticompetitive conduct, on the other hand, prevents or impairs competition by rivals in a way that either does not benefit consumers or does so in an unnecessarily restrictive way.¹⁰¹

Hovenkamp’s definition of unilateral exclusionary conduct has received attention as an example of an effects-based test and, in particular, a test that considers whether any consumer harm caused by the impugned conduct is disproportionate to any consumer benefits that the conduct creates.¹⁰² However, one of the most interesting points to note about Hovenkamp’s test is that Hovenkamp himself asserts that it is not so much a test as a general *definition* of exclusionary conduct—a series of premises which can be used as a starting point for creating workable and specific tests for specific types of unilateral conduct.¹⁰³ Hovenkamp has stressed that, even if a practice meets his definition for exclusionary conduct, it should not be condemned unless it is “reasonably susceptible to judicial control, which means that the court must be able to identify the conduct as anticompetitive and either fashion a penalty producing the correct amount of deterrence or an equitable remedy likely to improve competition.”¹⁰⁴

98. Herbert J. Hovenkamp, *The Antitrust Standard for Unlawful Exclusionary Conduct* 40 (Univ. of Iowa Coll. Of Law, Univ. of Iowa Legal Studies Research Paper No. 08-28, 2008).

99. HOVENKAMP, *supra* note 52, at 157 (emphasis added).

100. *Id.*

101. Hovenkamp, *supra* note 98, at 27; Hovenkamp, *supra* note 18, at 1042 n.25.

102. Gavil, *supra* note 4, at 61-62.

103. Hovenkamp, *supra* note 55, at 149-51; Hovenkamp, *supra* note 13, at 118.

104. Hovenkamp, *supra* note 55, at 148-49; *see also* HOVENKAMP, *supra* note 52, at 104 (discussing the elements necessary to condemn under antitrust laws).

For Hovenkamp, administrability is key: in his view, “antitrust is a justifiable enterprise only if court intervention can make markets work better,” that is, if intervention can produce higher output and lower prices.¹⁰⁵ In areas where there is significant uncertainty and it is not possible to develop reliable rules or effective remedies, he argues that courts and enforcement agencies should err on the side of caution and decline to intervene. The costs of incompetent intervention are too great.¹⁰⁶ On this basis, Hovenkamp has put forward different tests for different types of conduct, always having regard to his imperative of erring on the side of under-inclusiveness where a more inclusive test might capture procompetitive conduct.¹⁰⁷

4. The D.C. Circuit’s Burden-Shifting Approach in *Microsoft*

In 2001, the D.C. Circuit delivered its *en banc* decision in the appeal by the Department of Justice in *Microsoft* and enunciated an effects-based approach to monopolization claims, often noted for its four-step, burden-shifting process.¹⁰⁸ This approach amounted to a rule of reason analysis. Rather than an open-ended investigation of the various effects of the impugned conduct, however, the court limited the inquiry by specifying the matters for proof and the party who bore the burden of proof at each stage of the analysis.¹⁰⁹ This approach bears some obvious similarities to that advocated by Salop and Romaine in their 1999 article.¹¹⁰

105. HOVENKAMP, *supra* note 52, at 7, 157.

106. *Id.* at 312.

107. See *infra* Part II(D) for further discussion on responses to criticisms of effects-based tests.

108. *United States v. Microsoft Corp.*, 253 F.3d 34, 58-59 (D.C. Cir. 2001). The four-step analysis is as follows: (1) there must be harm to the competitive process; (2) plaintiff must demonstrate the conduct has requisite anticompetitive effect; (3) if plaintiff successfully establishes a *prima facie* case, the monopolist may offer procompetitive justification; and (4) if un rebutted, the plaintiff must demonstrate the harm outweighs the benefit. For additional analysis regarding the *Microsoft* decision, see for example, Salop, *supra* note 13, at 334; Gavil, *supra* note 4, at 21-22.

109. *Microsoft*, 253 F.3d at 58-59.

110. Salop & Romaine, *supra* note 6, at 618, 659; see David McGowan, *Between Logic and Experience: Error Costs and United States v. Microsoft Corp.*, 20 BERKELEY TECH. L.J. 1185, 1187-89 (2005) (arguing that Salop and Romaine’s article is a defense of the Justice Department’s liability theories); *supra* Part II(A)(1).

In *Microsoft*, the Court began by noting the principle, long-established by *United States v. Grinnell Corp.*,¹¹¹ that the offense of monopolization has two elements: (1) the possession of “monopoly power” in the relevant market; and (2) “the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.”¹¹² It also noted that the central difficulty lies in determining when this second element is present, that is, in discerning whether the impugned conduct is exclusionary rather than merely a form of vigorous competition.¹¹³

The Court determined that, from a century of case law under Section 2 of the Sherman Act, several principles emerged. Based on this case law, the Court outlined a four-step approach for determining whether particular conduct by a monopolist violates Section 2.¹¹⁴ The plaintiff must first establish a *prima facie* case that the relevant conduct has an “anticompetitive effect.” The defendant monopolist may then offer a “procompetitive justification” for its conduct. If the plaintiff cannot rebut this justification, the plaintiff must prove that the anticompetitive harm from the conduct outweighs the procompetitive benefit.¹¹⁵

The concept of “anticompetitive effect” was central to the determination of liability in *Microsoft*. According to the Court, the conduct “must harm the competitive *process* and thereby harm consumers.”¹¹⁶ Harm only suffered by one or more competitors will not suffice. The question is whether the monopolist’s conduct

111. *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966).

112. *Id.*; *Microsoft*, 253 F.3d at 50.

113. *Microsoft*, 253 F.3d at 58-59.

114. *Id.*; see Salop, *supra* note 13, at 334 n.93 (comparing the D.C. Circuit’s formulation of this balancing approach and the Second Circuit’s description of the rule of reason analysis under § 1 of the Sherman Act in *United States v. VISA USA, Inc.*, 344 F.3d 229, 238 (2d Cir. 2003)).

115. *Microsoft*, 253 F.3d at 59-60; see ANDREW I. GAVIL & HARRY FIRST, THE MICROSOFT ANTITRUST CASES: COMPETITION POLICY FOR THE TWENTY-FIRST CENTURY 78-80 (2014) (providing a detailed analysis and critique of the *Microsoft* case); see also McGowan, *supra* note 110, at 1198 (pointing out that a defendant can rebut a *prima facie* case of anticompetitive effect from the plaintiff, and the plaintiff must either rebut or offer evidence as to why the harm outweighs the procompetitive benefit).

116. *Microsoft*, 253 F.3d at 58.

on balance harms competition. The Court also emphasized that the focus is on “the effect of that conduct, not upon the intent behind it,” meaning that evidence of intent will only be relevant to the extent that it assists the court in understanding the likely effect of the conduct.¹¹⁷

Further detail of the “anticompetitive effect” concept can be gleaned from the Court’s analysis of the facts in *Microsoft*. From this analysis, it is clear that the Court did not require the plaintiff to prove direct harm to consumers—for instance, higher prices or reduced output. Instead, the court found that there was an anticompetitive effect where the conduct excluded rivals and thereby protected the defendant’s monopoly power.¹¹⁸ Further, it was not necessary to show that the exclusion of competitors led to the actual exit of competitors from the market. It was sufficient that the defendant’s conduct prevented access by competitors to some significant distribution or promotional channel, and/or reduced the usage share of rivals’ products, thereby preserving the defendant’s monopoly.¹¹⁹

To establish an “anticompetitive effect,” however, it was necessary to show something more than exclusionary conduct which preserved the defendant’s monopoly. When finding that the plaintiff had proven an anticompetitive effect, the Court repeatedly referred to the fact that the offending conduct was not “competition on the merits.”¹²⁰ But what meaning did the Court give to “competition on the merits”? At the first stage of the inquiry in *Microsoft*, the Court only held that the plaintiff had failed to establish anticompetitive effect where the conduct amounted to low pricing (based on the firm’s costs) or a pure product improvement.¹²¹ The Court did not, for example, consider the possibility of benefits flowing from exclusivity arrangements at this point.

117. *Id.* at 58-59.

118. *See id.* at 61-78 (examining Microsoft’s restrictions on Original Equipment Managers (OEMs) that prevented them from taking actions that could increase rivals’ share of usage).

119. *See id.* (discussing the court’s satisfaction with evidence that OEMs were unable to take actions that would increase rivals’ share of usage as anticompetitive and did not require the plaintiffs to prove competition had actually left the market).

120. *Id.* at 62, 65, 77.

121. *Id.* at 68, 75.

If the plaintiff proved a prima facie case of anticompetitive effect—that the conduct excluded rivals thereby preserving the defendant’s monopoly, other than by competition on the merits—the defendant might still defend its conduct by advancing a “procompetitive justification.” The Court explained that the defendant’s procompetitive justification must be “a nonpretextual claim that its conduct is indeed a form of competition on the merits because it involves, for example, greater efficiency or enhanced consumer appeal.”¹²² To demonstrate a procompetitive justification, the defendant must show that the conduct has a purpose other than preserving the defendant’s monopoly.¹²³ Preserving monopoly power, in itself, is a “competitively neutral” goal.¹²⁴ Something more—such as greater efficiency or enhanced consumer appeal—is required to demonstrate that that goal is being pursued by way of competition on the merits.

In summary, the *Microsoft* decision put forward a process for characterizing a unilateral practice based on its effects on the relevant markets. This process began with consideration of whether the exclusionary conduct was simply competition on the merits in its clearest form—pure low pricing or a superior product—so that it should be absolved without further analysis. When the conduct involved some restraint or hindrance of rivals beyond this, the burden shifted to the dominant firm to show that the conduct was more than a method of preserving its monopoly power—for instance, that it involved efficiency gains or improved consumer appeal. According to the Court, any substantiated gains should then be weighed against the harm from the enhanced monopoly power to determine the ultimate impact of the conduct on consumers.

5. The Proposal for a “Substantial Lessening of Competition” Test in Australia

In Australia, the prohibition against misuse of market power in Section 46(1) of the *Competition and Consumer Act 2010* (Cth) (“CCA”) currently provides that:

A corporation that has a substantial degree of power in

122. *Id.* at 59.

123. *Id.* at 67.

124. *Id.* at 72.

a market shall not take advantage of that power in that or any other market for the purpose of:

- (a) eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;
- (b) preventing the entry of a person into that or any other market; or
- (c) deterring or preventing a person from engaging in competitive conduct in that or any other market.¹²⁵

Thus, it is necessary for an applicant to prove that the firm in question possessed substantial market power, that it “took advantage” of that power, and that it did so for one of the three proscribed purposes.

This prohibition has been the subject of debate throughout its 40-year history.¹²⁶ More recently, the Competition Policy Review Panel (the “Harper Panel”) conducted the first wholesale review of Australian competition policy in over 20 years, and created significant controversy by recommending substantial changes to Section 46(1).¹²⁷ The Australian Prime Minister has since announced the government’s intention to adopt the central recommendation of the Harper Panel in respect of Section 46(1), which states that the requirement that the relevant firm “take advantage” of its substantial market power should be removed and replaced by a requirement that the firm’s conduct has the purpose, effect, or likely effect of “substantially lessening competition” in the market (“the SLC test”).¹²⁸

The Harper Panel has argued that the proposed amendment

125. *Competition and Consumer Act 2010* (Cth) pt IV div 2 s 46 (Austl.).

126. See, e.g., George A. Hay & Kathryn McMahon, *The “Duty to Deal” Under Section 46: Panacea or Pandora’s Box?*, 17 U. NEW S. WALES L.J. 54, 66-69 (1994) (citing several early cases analyzing non-discriminatory practices of larger firms and concluding that more recent courts have failed to take into account the earlier courts’ analysis); see also HARPER ET AL., *supra* note 30, at 335-36 (outlining the history of proposals for an effects test to be added to Section 46 in Australia); Edwards, *supra* note 38, at 165-70 (identifying problems with Section 46 of the Trade Practices Act regarding catching predatory conduct when the alleged predator does not possess substantial market power at the time of the conduct and gives three possible solutions).

127. HARPER ET AL., *supra* note 30, at 340-45.

128. *Id.* at 344-45; Turnbull, *supra* note 30.

would improve the effectiveness of Section 46(1) in targeting unilateral anticompetitive conduct and bring the Australian law closer to the standards adopted in other comparable jurisdictions.¹²⁹ The Panel also pointed out that the SLC test would have the advantage of creating consistency, since this test is adopted in other key provisions of the CCA in respect of anticompetitive arrangements, exclusive dealing, and mergers.¹³⁰

The SLC test has been analyzed in the case law under these provisions of the CCA, so it is possible to outline some of its likely parameters as a test for unilateral anticompetitive conduct under Section 46(1). As with the other effects-based tests outlined in this Part, the Australian SLC test is not concerned with conduct that harms competitors per se, but with conduct that harms the competitive process. While the conduct must have an impact on actual or potential rivals, it is well established that rivalry is not lessened simply because one or more competitors are harmed or even removed from the field of play.¹³¹ What must be lessened is the “future field of rivalry”¹³² or “rivalrous market behavior,”¹³³ and this is “a process rather than a situation.”¹³⁴

The case law has also established the relevant counterfactual to be considered under the SLC test. Consistent with Salop’s “consumer harm” test, the SLC test requires the court to consider the likely state of competition with and without the impugned

129. HARPER ET AL., *supra* note 30, at 340, 344.

130. *Id.* at 341.

131. See, e.g., *Australian Competition & Consumer Comm’n v Cement Austral Pty Ltd* [2013] FCA 909, ¶¶ 3012-13 (Austl.) (discussing how the effect of competition can still be relevant without having a significant impact on the market itself); *Universal Music Austral Pty Ltd v Australian Competition & Consumer Comm’n* (2003) 131 FCR 529, 585 (Austl.) (finding that for a claim to succeed, the lessening of competition must be adjudged of such seriousness as to adversely affect competition in the marketplace); *Stationers Supply Pty Ltd v Victorian Authorised Newsagents Ass’n Ltd* (1993) 44 FCR 35, 56 (Austl.) (showing that the court was not satisfied with the evidence, which failed to show that the existing market arrangements represented a barrier to entry for other participants).

132. *Cement Austral Pty Ltd*, [2013] FCA at ¶ 3012 (Austl.).

133. *Re Queensland Coop. Milling Ass’n & Defiance Holdings Ltd* (1976) 25 FLR 169, 188 (Austl.).

134. *Id.* at 189.

conduct.¹³⁵ Importantly, this is not a before-and-after test,¹³⁶ but a comparison of the future state of competition with the impugned conduct and the future state of competition without that conduct (which may differ from the pre-existing situation) to determine whether competition is substantially less in the former scenario.¹³⁷

Under the SLC test, the courts have emphasized that the restraints under consideration prevented rivals from offering a better price-product-service package than the firms imposing the restraint.¹³⁸ In these cases, the incumbent's method of winning in the competition for custom was to impair the ability of rivals to compete or that custom. The incumbents interfered with competition by "freezing out realistic competitive offers"¹³⁹ and insulating themselves from the effects of competition.¹⁴⁰ The exclusion of rivalry in these circumstances is likely to lead to higher prices and/or lower quality offerings than those which would be made in the absence of the conduct.¹⁴¹

However, in contrast to the other effects-based tests considered in this Part, the SLC test does not expressly provide that the dominant firm may raise an efficiency defense or justification. Accordingly, to "neutralise concerns about

135. *Stirling Harbour Servs Pty Ltd v Bunbury Port Auth*, [2000] FCA 38 ¶ 113 (Austl.).

136. *See id.* (substituting a "before and after test" with a consideration of a hypothetical future state of events with and without bad conduct).

137. *Id.* ¶¶ 39, 42; *Dandy Power Equip Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238, 259-60 (Austl.).

138. *See Gallagher v Pioneer Concrete (NSW) Pty Ltd* (1993) 113 ALR 59 ¶¶ 205-07 (Austl.) (describing the way in which a party allegedly engaged in conduct that hindered or prevented the supply of services by third party carriers, thereby causing a substantial lessening of the competition in the market).

139. *Australian Competition & Consumer Comm'n v Baxter Healthcare Pty Ltd [No. 2]* (2008) 170 FCR 16, 102 (Austl.).

140. *Cf. Gallagher*, 113 ALR at ¶¶ 204, 207 (describing conduct that restricts supply to competitors as conduct that is engaged in for the purpose of substantially lessening competition in the market).

141. *See Rural Press Ltd v Australian Competition & Consumer Comm'n* (2003) 216 CLR 53, 73 (Austl.) (discussing facts in which the competitive response of a newspaper lowered advertising rates and lessened competition); *Australian Competition & Consumer Comm'n v Cement Austl Pty Ltd* [2013] FCA 909 ¶¶ 3014, 3072, 3087, 3178-80, 3226-27 (Austl.) (concluding that a sales agreement substantially lessened competition by blocking entry into the market by potential competitors).

overcapture,” the Harper Panel proposed that the amended Section 46 should include legislative guidance as to the meaning of the SLC test.¹⁴² This guidance would require the court, in determining whether conduct has the purpose, effect, or likely effect of substantially lessening competition, to have regard to:

- (a) the extent to which the conduct has the purpose, effect or likely effect of increasing competition in the market, including by enhancing efficiency, innovation, product quality or price competitiveness; and
- (b) the extent to which the conduct has the purpose, effect or likely effect of lessening competition in the market, including by preventing, restricting or deterring the potential for competitive conduct in the market or new entry into the market.¹⁴³

B. Common Themes in Effects-Based Tests

The central feature of the effects-based tests outlined in this Part is that they focus on the impact of the impugned conduct on the relevant market, rather than focusing on the dominant firm’s intent, purpose, or incentives. Each of these tests requires proof of a negative impact on actual or potential rivals, but harm to rivals is not sufficient to establish liability. Advocates of effects-based tests agree that low prices based on costs and increases in product quality or innovation are manifestations of vigorous competition, which, by themselves, should not be condemned, even if they cause detriment to competitors.¹⁴⁴ Less efficient competitors should not be protected from the natural outcomes of competition for custom. Before unilateral conduct is condemned, the negative impact on rivals must be such that it amounts to substantial harm to the competitive *process*.

142. HARPER ET AL., *supra* note 30, at 342, 345.

143. *Id.* at 344.

144. *See* HOVENKAMP, *supra* note 52, at 157, 312 (concluding that monopolizing behavior should not be condemned if it gives any significant benefits to society even if the conduct is likely to create, increase, or prolong monopoly power); Salop, *supra* note 13, at 329-31 (describing the consumer standard which refuses to condemn exclusionary conduct if the likely and substantial procompetitive benefits are so strong that consumers are unlikely to be harmed from the behavior).

Harm to the competitive process is likely to occur where conduct constrains actual or potential rivals from making competitive offers to consumers to a substantial degree.¹⁴⁵ These constraints on rivals enhance or maintain the dominant firm's market power, resulting in elevated prices and reduced output to the detriment of consumers. Under most effects-based tests, direct proof of net harm to consumers is usually sufficient, but not essential, to establish liability. The requisite harm may also be demonstrated by proof of substantial or significant foreclosure of rivalry.

Conduct that is likely to significantly enhance or protect the dominant firm's market power without creating any additional benefit for society should be condemned. At the same time, conduct that results in some constraint on rivalry, and thus some increase in the firm's market power, may also give rise to benefits for consumers. Effects-based tests therefore generally permit dominant firms to justify their conduct on the basis that it gives rise to consumer benefits or procompetitive gains, which outweigh any harm to the competitive process.¹⁴⁶

However, the effects-based approaches considered in this Part reveal very different perceptions about the dangers inherent in an effects-based analysis, particularly in the case-by-case assessment of competitive effects.¹⁴⁷ This comparison is extended in the following sections to give consideration to different ways in which the respective effects-based tests address key criticisms, particularly with regard to their administrability, and deterrent effects on socially beneficial dominant firm behavior. These

145. See Salop, *supra* note 13, at 347-48 (using an expected value analysis to show different ways in which a business can be deterred from engaging in certain conduct).

146. See, e.g., *United States v. Microsoft Corp.*, 253 F.3d 34, 58-59 (2001) (holding that the four step test gives the plaintiff an opportunity to prove a *prima facie* case, but gives the defendant the opportunity to prove defendant's conduct was not harmful to the competitive process); Salop & Romaine, *supra* note 6, at 656-57 (characterizing the sole purpose and effects test as one where the procompetitive motive and potential effects trump the anticompetitive ones).

147. See HOVENKAMP, *supra* note 52, at 157, 312 (explaining that a monopolization offense that condemns actions likely to create, increase, or prolong monopoly without giving any benefits to society can result in better results and lower cost in the courts); Hovenkamp, *supra* note 55, at 150-51 (attempting to mitigate the damages by giving a definition to balance the two approaches by focusing on ability to create, enlarge, or maintain market power by excluding rivals).

responses, it is argued, reveal an underlying concern with the objective purpose of the impugned conduct, which may even prevail over evidence of the conduct's actual or likely effect.

C. Criticism of Effects-Based Tests

1. Administrability: Difficulties in Establishing Effects, Causation and “Balancing” Effects

Opponents of effects-based tests in the United States and Australia argue that antitrust authorities and courts (let alone firms) often simply cannot predict or discern the effects of single-firm conduct,¹⁴⁸ at least without incurring costs that greatly exceed any benefit from intervention.¹⁴⁹ Firm behavior and market responses are complex matters. While economic theory might offer some assistance in interpretation and prediction, the discipline is rife with nuance, conflicting views, and theories which cannot be usefully applied by generalist judges to real-world markets.¹⁵⁰ Further, the same practice may have both beneficial and detrimental consequences to consumers, or it might benefit consumers in one market while harming those in another. It is not apparent how such effects might be quantified or balanced against each other.¹⁵¹ In short, an effects-based test

148. See Lao, *Antitrust Intent*, *supra* note 25, at 191-95 (describing the task of predicting competitive effects in markets with significant network characteristics as an extremely speculative exercise); see also Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1, 20-21 (1984) (stating that single firms in the market rarely have any competitive power and when that is the case the market is better than the judicial system process in discerning the beneficial from the detrimental).

149. See, e.g., Easterbrook, *supra* note 148, at 12 (arguing that courts should not be making judgments for difficult economic problems because they are ill-equipped and ill-suited to do so); Patterson, *supra* note 5, at 43 (noting that hypothetical tests are vague, inconclusive, and expensive); Popofsky, *supra* note 65, at 449-51 (stating that legal enforcement is not perfect and imperfect information can create the risk of errors and retard optimal deterrence); see also BUS. COUNCIL OF AUSTRAL., SUBMISSION ON OPTIONS TO STRENGTHEN THE MISUSE OF MARKET POWER LAW 57 (2016) (discussing the accurate assessments of some approaches, but noting the delay and cost associated).

150. See *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 234 (1st Cir. 1983) (discussing that while economic discussions help to inform antitrust laws, these views can actually prove to be counter-productive during application).

151. See ANDREW I. GAVIL ET AL., *ANTITRUST LAW IN PERSPECTIVE: CASES, CONCEPTS AND PROBLEMS IN COMPETITION POLICY* 207 (2d ed. 2008) (criticizing the Rule of Reason balancing test as “perhaps the greatest myth in all of U.S. antitrust law”);

might ask the right question, but it is a question which we will often be incapable of answering.¹⁵² As some would put it, if a question has no answer, that may suggest that it is in fact the wrong question to ask.¹⁵³

Effects-based tests for unilateral conduct have been criticized for requiring courts to “balance” or “weigh” the procompetitive and anticompetitive effects of conduct in a market—or, equally, the different effects which the same conduct may have on different groups of consumers—given that any sensible balancing exercise may be impossible, or at least prohibitively expensive, in practice.¹⁵⁴ Assuming the nature of the respective effects of the conduct can be identified, those effects will often be unquantifiable and incommensurable.¹⁵⁵ Even where balancing of opposing effects is possible, the increased cost of compliance, enforcement, and litigation may well offset the economic benefit of applying such a test.¹⁵⁶

Opponents of effects-based tests draw support for this view from the fact that courts that have purported to apply an effects-based approach have rarely engaged in any actual

Easterbrook, *supra* note 148, at 11 (discussing the difficulty a court faces in balancing the costs and benefits of the effects a business practice has on the market); McGowan, *supra* note 110, at 1188-89 (pointing out that courts should decide to perform a more rigorous cost-benefit analysis or decline to impose liability because of the inherent uncertainty missing from rigorous analysis); Melamed, *supra* note 3, at 1252-55 (identifying problems with balancing tests in the absence of omniscient economic actors and legal professionals); Popofsky, *supra* note 65, at 465 (discussing the difficulty of courts’ engagement in case specific assessments of net effects on consumers).

152. Josef Drexler, *Real Knowledge Is to Know the Extent of One’s Own Ignorance: On the Consumer Harm Approach in Innovation-Related Competition Cases*, 76 ANTITRUST L.J. 677, 677 (2010).

153. Easterbrook, *supra* note 148, at 14.

154. See Melamed, *supra* note 3, at 1252-54 (labeling the balancing test as unworkable because of real-world limitations existing outside of abstract economic theory); Popofsky, *supra* note 65, at 465 (reasoning that a balancing test is too difficult, the stakes are too high, and that the test does not give other economic actors enough assurance);

155. See Richard D. Cudahy & Alan Devlin, *Anticompetitive Effect*, 95 MINN. L. REV. 59, 65 (2010) (establishing a necessary level of residual uncertainty in applying antitrust effects tests).

156. HOVENKAMP, *supra* note 52, at 108; see Hovenkamp, *supra* note 98, at 32 (explaining how courts cannot quantify the economic harm from a defendant’s exercise of market power and balance this against the gains).

weighing of anticompetitive and procompetitive effects.¹⁵⁷ Instead, these courts tend summarily to declare the impugned conduct to be “competition on the merits,” or to arrive at a conclusion regarding the claimed benefits and detriments of the conduct without attempting to weigh those effects against each other.¹⁵⁸ Opponents say this is evidence that the balancing exercise cannot be undertaken in practice.¹⁵⁹ To pretend that it is possible, and that it is being undertaken, only obscures the real, undeclared process by which the court is arriving at its conclusions on the conduct.

2. Over-Deterrence: Reduction of Incentives to Engage in Socially Beneficial Conduct

The risks of adopting an effects-based test extend beyond the risk of “getting it wrong” in individual, litigated cases. The prospect of litigation also affects the behavior of firms who have never been the subject of a complaint.¹⁶⁰ When assessing the risks of engaging in any course of conduct, firms naturally consider the potential for accusation, litigation, and sanctions. Even if one dominant firm has been correctly sanctioned for engaging in certain behavior with an anticompetitive effect, other firms may be deterred from engaging in similar behavior even when that

157. See, e.g., Elhauge, *supra* note 2, at 318-19 (arguing that the D.C. Circuit in *Microsoft* did not actually apply a balancing test, as the court failed to actually consider any anticompetitive effects); Hovenkamp, *supra* note 98, at 32 (stating that the court in *Microsoft* never performed “any real balancing”); McGowan, *supra* note 110, at 1188-89 (arguing that the D.C. Circuit in *Microsoft* applied what seemed more like a market correction approach); Popofsky, *supra* note 65, at 447 (looking at the *Microsoft* court’s recognition that in instances of “competition on the merits,” balancing effects on consumers or rivals is inappropriate); see also *Verizon Commc’ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 407, 414-16 (2004) (reasoning that “the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct”).

158. *United States v. Microsoft Corp.*, 253 F.3d 34, 59 (2001); see Hovenkamp, *supra* note 98, at 32 (arguing that the Court in *Microsoft* avoided any real balancing, but rather accepted the un rebutted justification presented by the defendant).

159. Melamed, *supra* note 3, at 1253-54; Popofsky, *supra* note 65, at 447.

160. See Easterbrook, *supra* note 148, at 2, 6-7 (demonstrating how firms avoid otherwise beneficial practices in fear of facing court-ordered sanctions); McGowan, *supra* note 110, at 1188-89 (finding that the *Microsoft* opinion “often seems confused or contradictory” and the “net result . . . a tepid tapioca pudding” that will do little in guiding the behavior of firms in the future).

behavior would result in important benefits for consumers.¹⁶¹ The fact that the behavior is open to serious antitrust scrutiny may mean that firms will consider it too risky to compete in that way.¹⁶² Low pricing and innovative products are cited as examples, particularly in the current debate in Australia.¹⁶³ The losses from deterring practices such as these, it is said, would be far greater than any benefit from capturing the odd anticompetitive instance.¹⁶⁴

D. Responses to Criticisms of Effects-Based Tests

1. Administrability: “Balancing,” Proportionality and Objective Purpose

The first response to criticisms about the “balancing” requirement of effects-based tests is that, while these tests generally incorporate a final “balancing” or “weighing” stage, the test usually produces a result before this final stage is reached.¹⁶⁵ A balancing exercise is generally only required in cases involving truly exclusionary conduct, which is offset by a compelling efficiency explanation where the impugned conduct is also necessary for the achievement of those efficiencies.¹⁶⁶ This is not

161. Popofsky, *supra* note 65, at 465.

162. BUS. COUNCIL OF AUSTRAL., *supra* note 149, at 26, 57; Easterbrook, *supra* note 148, at 17.

163. See Katharine Kemp, *A Third Way: Objective Anticompetitive Purpose* 14 (Univ. of New S. Wales Sch. of Banking & Fin., Paper No. 2016-22, 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2735898 [<http://perma.cc/6RLV-82JL>] (discussing how low prices and innovative products are essential); Graeme Samuels & Stephen King, *Competition Law: Effects Test Would Have Shackled Competition*, AUSTRALIAN FIN. REV. (Sep. 9, 2015, 8:05 AM), <http://www.afr.com/opinion/competition-law-effects-test-would-have-shackled-competition-20150908-gjqh5l> [<http://perma.cc/6BYL-XP2U>] (arguing the effects-based test would restrict procompetitive effects, such as lower pricing and the creation of innovative products); *infra* Part II(D)(2).

164. Easterbrook, *supra* note 148, at 15-16.

165. See, e.g., Salop, *supra* note 13, at 363-64 (suggesting that there would be no need for balancing if firms could predict the outcome of a design change); Melamed, *supra* note 3, at 1253-54 (purporting that balancing tests would make good sense if economic actors and legal fact finders were omniscient).

166. See Hovenkamp, *supra* note 98, at 32 (asserting that a balancing test will be necessary in instances where conduct causes some benefit but unavoidably threatens harm).

a common scenario.¹⁶⁷ The rarity of cases necessitating a balancing exercise limits the extent of error costs arising from such an exercise and provides some explanation for the absence of balancing in the case law.¹⁶⁸

Nonetheless, there will be some cases where courts must evaluate conduct that creates some benefit for consumers and also unavoidably threatens consumer harm.¹⁶⁹ As to the nature of the balancing exercise, when it is required, Salop argues that it is *not* necessary for courts to *quantify* the various effects of the conduct.¹⁷⁰ What is required is a weighing of *the strength of the evidence* on each side.¹⁷¹ The court should “compare and weigh the magnitude and credibility of evidence on both the procompetitive and anticompetitive sides to evaluate which evidence is stronger on balance.”¹⁷² For example, if the facts in a given case indicate that the exclusionary conduct likely increases or maintains barriers to competition or entry and also leads to higher prices, the conduct would be condemned “unless the evidence of likely and substantial procompetitive benefits is so strong that consumers are unlikely to be harmed.”¹⁷³ Such an approach reveals a focus on uncovering the most likely *explanation* for the impugned conduct.¹⁷⁴

However, complexity arises from the fact that conduct may give rise to substantial increases in one dimension of competition at the same time as it substantially decreases competition in another dimension. As Wright points out:

Firms compete on price, output, reputation, quality, innovation, and cost. In many cases, though not all, these forms of rivalry are negatively correlated. This inverse

167. *Id.*; see also Salop, *supra* note 13, at 363-64 (fending off criticism of the balancing step because it is either easy or unnecessary to apply in the majority of cases).

168. GAVIL & FIRST, *supra* note 115, at 320.

169. Salop, *supra* note 13, at 363-64. See also GAVIL & FIRST, *supra* note 115, at 319 (suggesting that the act of balancing pro- and anticompetitive effects should not be jettisoned simply because it may be difficult).

170. Salop, *supra* note 13, at 331-32.

171. *Id.*

172. *Id.* at 332. It would not generally be necessary, however, for the fact finder to *quantify* precisely the probabilities and strength of evidence on each side.

173. *Id.* at 330.

174. See *infra* Part V(E).

correlation implies that regulators or judges must determine which bundle of competitive forms maximizes efficiency (or consumer welfare) in the face of welfare trade-offs between these activities.¹⁷⁵

Where conduct has substantial but opposing effects on different forms of competition, courts must decide which of these forms of competition should be given priority, having regard to the objective of protecting consumer interests. Given the limits of current economic theory and empirical knowledge, such a decision may amount to little more than the expression of a subjective preference, which may erroneously condemn or deter conduct which is in fact socially beneficial.¹⁷⁶

Given the incommensurability of effects in “mixed” cases, commentators and authorities in the United States and elsewhere have advocated a proportionality inquiry, rather than an attempt to balance effects, in the characterization of unilateral anticompetitive conduct.¹⁷⁷ Under a proportionality inquiry, it would be necessary to ask whether, at the time it engaged in the conduct, the firm’s choice of strategy was proportionate to its claimed benefits with regard to the risk and extent of any exclusion of rivalry. This approach points to the relevance of the

175. Joshua D. Wright, *Antitrust, Multidimensional Competition and Innovation: Do We Have an Antitrust-Relevant Theory of Competition Now?*, in *COMPETITION POLICY AND PATENT LAW UNDER UNCERTAINTY: REGULATING INNOVATION* 228, 231 (Geoffrey A. Manne & Joshua D. Wright eds., 2011).

176. *See id.* at 233-34 (arguing that a deficit of theoretical economic knowledge would produce a capricious treatment of antitrust policy).

177. *See, e.g.*, NAZZINI, *supra* note 46, at 4, 94, 158, 167-69 (explaining how there is a “growing recognition that the balancing” test is more of a “proportionality inquiry”); Gavil, *supra* note 4, at 61-62 (promoting a more dimensional, “disproportionality” test as an initial inquiry in characterizing anticompetitive conduct and noting that this test has been advocated by the government); Salop, *supra* note 13, at 353 (claiming the test could be rephrased in terms of “harms disproportionate to the resulting benefits”); *see also* Donald Robertson, *The Primacy of “Purpose” in Competition Law – Part 1*, 2001 CCLJ LEXIS 4, *25-26 (2002) [hereinafter Robertson, *Primacy of “Purpose” – Part 1*] (demonstrating how countries like the United States and Germany focus on the actor’s purpose in evaluating potentially anticompetitive conduct); Donald Robertson, *The Primacy of “Purpose” in Competition Law – Part 2*, 2002 CCLJ LEXIS 11, *77-78 (2002) [hereinafter Robertson, *Primacy of “Purpose” – Part 2*] (proposing that, rather than balancing immeasurable effects, determining whether potentially anticompetitive behavior is proportional to the objectives to be achieved would be “good reason to think that the balance has been achieved”).

objective purpose of the impugned conduct. In particular, it provides courts with a framework for assessing the reasonableness of the firm's conduct at the outset; for determining whether, objectively speaking, the true purpose of the conduct was to restrict competition or to compete through superior efficiency. A proportionality inquiry also provides dominant firms with a framework for assessing the legality of proposed conduct, which takes into account the reasonably foreseeable competitive impacts of their conduct without requiring precise predictions about actual outcomes which could be affected by factors beyond the firm's control.¹⁷⁸

2. Deterrence: Ex Ante Analysis, Multiple Tests and Objective Purpose

Effects-based tests have also been criticized on the basis that they are likely to capture conduct which is actually procompetitive,¹⁷⁹ and unacceptably reduce the incentives of dominant firms to engage in beneficial competitive conduct.¹⁸⁰ This deterrence results from firms' perceptions on the risk that courts will erroneously condemn conduct which is actually beneficial, particularly where that conduct is new or poorly understood, as well as the risk that firms themselves will incorrectly predict the net competitive impact of their conduct at the outset.¹⁸¹ The effects-based tests considered in this Part take quite different approaches to these risks.

Salop responds to criticisms regarding potential over-deterrence effects by arguing that marginal adjustments

178. See *infra* Part V(D).

179. Easterbrook, *supra* note 148, at 4-8 (listing several examples of judicial economic ignorance which cause effects-based tests to prohibit more than just anticompetitive conduct).

180. See, e.g., Drexler, *supra* note 152, at 677-79 (criticizing an effects-based approach to competition law and arguing that due to the problem of uncertainty, enforcement may chill innovation); Melamed, *supra* note 3, at 1254 (contending that balancing tests that seek to assess the benefits and competitive harms of exclusionary conduct are unlikely to create optimal incentives for marketplace behavior); Popofsky, *supra* note 65, at 465 (cautioning that case-specific assessments of effects on consumers restrict otherwise competitive actions and harm consumers).

181. See Easterbrook, *supra* note 148, at 3-7 (explaining how antitrust regulators and judges struggle to differentiate between firms' practices that are beneficial for consumers and practices that are anticompetitive).

may be made to the “consumer harm” test—for instance, to the standard of proof—to take into account the potential consequences of the test for firm incentives and deterrence in respect of certain types of conduct.¹⁸² Hovenkamp would go further. The risk of deterring socially beneficial conduct is one of the key reasons that Hovenkamp does not in fact recommend the use of an effects-based test, or rule of reason inquiry, in respect of unilateral conduct on a case-by-case basis.¹⁸³ Instead, Hovenkamp advocates what might be called a “meta” rule of reason, or effects-based test, as the over-arching principle for selecting the conduct-specific tests that maximize long-run consumer welfare.¹⁸⁴ In some circumstances, the best solution from a consumer standpoint might be to apply certain simplified screening tests or tests which capture a more limited range of anticompetitive conduct in order to preserve incentives for dominant firms to engage in behavior that ultimately benefits consumers. The difference in these approaches is considered below in the context of one particular area of concern, innovative conduct.

Claims of unilateral anticompetitive conduct often concern novel products, services, or business methods. It is acknowledged that dominant firms may engage in “predatory innovation” which improperly excludes rivals to the detriment of consumers.¹⁸⁵ However, numerous commentators have argued that antitrust rules should err heavily on the side of permissibility in such cases, particularly given the overwhelming economic benefits flowing from innovation and the perverse effects of deterring highly beneficial conduct.¹⁸⁶

182. Salop, *supra* note 13, at 353-54.

183. Hovenkamp, *supra* note 13, at 114, 118, 120-21.

184. Popofsky, *supra* note 65, at 456.

185. Alan Devlin & Michael Jacobs, *Anticompetitive Innovation and the Quality of Invention*, 27 BERKELEY TECH. L.J. 1, 8 (2012).

186. See Drexler, *supra* note 152, at 679-80 (arguing that, especially in innovation-related cases, competition enforcers should not pretend that they can predict consumer preferences and should use specific evidence of consumer preferences cautiously); see also Geoffrey A. Manne & Joshua D. Wright, *Innovation and the Limits of Antitrust*, 6 J. COMPETITION L. & ECON. 153 (2010) (observing that the probability of false positives and social costs are higher in innovation-related cases and identifying filters to minimize these errors); Geoffrey A. Manne & Joshua D. Wright, *Google and the Limits of*

Hovenkamp has recognized that dominant firms may engage in the anticompetitive strategy of selecting technologies or other novel methods of doing business simply to take advantage of the adverse impact on rivals.¹⁸⁷ He also argues that unilateral innovations should only be condemned in the rare situation where the following stringent conditions are met:

- (a) the defendant occupies a very dominant position in the market, sufficient to warrant an inference of serious injury if the firm designs a product that excludes the complementary products of rivals;
- (b) there is no significant actual improvement for which the challenged innovation was necessary; and
- (c) the defendant did not intend, at the outset, to create a better product but only to redesign it in order to exclude a rival, generally by making the rival's product incompatible with its own.¹⁸⁸

Accordingly, an innovative act should never be condemned unless it is a “sham” in the sense that it “does not benefit consumers at all, but is profitable only because it locks consumers into the dominant firm's technology.”¹⁸⁹

Hovenkamp argues that where innovative conduct is actually necessary for *any* significant improvement in the product, it should be absolved. In his view, where there is any significant improvement, the courts are “simply not up to the job of balancing the gains from innovation against the losses from reduced competition.”¹⁹⁰ Even though successful innovations may injure competitors and may create or expand monopoly power, he points out that there is general consensus in the economic literature that

Antitrust: The Case Against the Case Against Google, 34 HARV. J.L. & PUB. POL'Y 171, 183-84 (2011) (discussing how the scrutiny of innovation by antitrust authorities results in a higher likelihood that the given practice will be considered anticompetitive).

187. Hovenkamp, *supra* note 18, at 1039; *see also* Devlin & Jacobs, *supra* note 185, at 8-10 (describing methods of “predatory innovation” used to exclude rivals from the market).

188. Hovenkamp, *supra* note 18, at 1046; Hovenkamp, *supra* note 55, at 158; *see also* Hovenkamp, *supra* note 98, at 23-24 (advocating an *ex ante* analysis of the firm's subjective intent in innovation cases); Devlin & Jacobs, *supra* note 185, at 1 (proposing an alternative approach to predatory innovation claims).

189. Hovenkamp, *supra* note 18, at 1045.

190. *Id.* at 1046.

gains from innovation are likely to be significantly greater than gains from increased competitiveness.¹⁹¹ Accordingly, “[o]ur market system simply places too high a premium on innovation” to condemn such innovations.¹⁹²

Salop’s approach to innovations or product design changes by dominant firms is quite different. Salop would condemn a dominant firm’s product design change if it maintains or enhances the firm’s market power by creating incompatibility with a rival’s product if that incompatibility is not necessary for the improvement of the dominant firm’s product.¹⁹³ However, even if the incompatibility is inextricably linked to the dominant firm’s quality improvement, Salop would find a violation if the dominant firm “consequently gains the ability to raise its price by far more than the [value of the] quality improvement.”¹⁹⁴ Salop would thus have courts compare the additional value or performance benefits to consumers from the design change with the additional price that the consumers would be required to pay. A beneficial design change might still infringe if the resulting price is higher than the quality-adjusted price. The change would be condemned if “the product improvement is valued by consumers, but not by enough when it comes unavoidably bundled with increased barriers to competition that permit such large price increases.”¹⁹⁵

However, Salop adds a qualification which takes into account the potential for over-deterrence. Salop acknowledges that innovative conduct can often have unpredictable results.¹⁹⁶ His solution is that, in such situations, the conduct should be evaluated from an *ex ante perspective* based on the information reasonably available at the time that the innovator made its

191. *Id.* at 1045; see also Herbert Hovenkamp, *The Obama Administration and Section 2 of the Sherman Act*, 90 B.U. L. REV. 1611, 1663 (2010) (“The welfare gains from innovation almost certainly exceed the available gains from squeezing price monopoly out of the economy. An important corollary of this proposition, however, is that the harm caused by an act that restrains innovation can cause far greater harm than a restraint on simple output or pricing.”).

192. Hovenkamp, *supra* note 18, at 1045.

193. Salop, *supra* note 13, at 323-24.

194. *Id.* at 323-25.

195. *Id.* at 338-39.

196. *Id.* at 339.

investment decision.¹⁹⁷ The consumer harm test would therefore only require the firm “to make a good-faith effort to estimate the expected impact of its conduct on consumers,”¹⁹⁸ and the court to “evaluate the likelihood and magnitude of expected consumer benefits or harms based on the information reasonably available at the time that the conduct was undertaken.”¹⁹⁹

It is submitted that both Hovenkamp’s and Salop’s responses to potential deterrent effects—and the possibility of deterring beneficial innovation in particular—demonstrate a concern with the objective purpose of the impugned conduct. In Hovenkamp’s view, the conduct should be condemned if, objectively assessed, the benefit from the innovation at the outset was so minor that it should be regarded as a “sham.” Salop also highlights the importance of considering the purpose of the conduct at the outset by admitting that one should assess the conduct with regard to the information reasonably available to the firm at the time it engaged in the conduct. These matters do not bear on the effect of the conduct, but rather on its purpose. By focusing on the purpose of the conduct in this way, Hovenkamp and Salop (at least implicitly) recognize that conduct initiated *without* an objective anticompetitive purpose should be protected in the interests of social welfare, even if such conduct occasionally gives rise to consumer harm in the event.

In contrast, in Australia the proposed SLC test would apply uniformly to all dominant firm conduct, requiring the court to determine the effect or likely effect of the conduct on rivalry in the particular case which is before the court. If a plaintiff succeeded in proving a rare instance of anticompetitive above-cost pricing or an innovative design change that disproportionately excluded rivalry and enhanced the dominant firm’s market power, the court would be required to find an infringement without regard to the disincentive effects of such a finding on low pricing and innovation in general.²⁰⁰ In this respect, the

197. *Id.*

198. *Id.* at 365.

199. *Id.* at 341.

200. Where a dominant firm’s new product or design change excludes rivalry *without* giving rise to any benefit to consumers, the innovation may be found to have substantially lessened competition. Accordingly, strategic behavior or “sham” design changes by

Australian SLC test is a much blunter instrument than other effects-based tests considered in this Part, which may discourage some good conduct with the bad. Accordingly, the SLC test has been criticized for its over-deterrent effects.²⁰¹

III. “PROFIT-FOCUSED” TESTS FOR UNILATERAL CONDUCT

A. *Introduction to “Profit-Focused” Tests*

Given the uncertainty and potential over-deterrence of effects-based tests for unilateral anticompetitive conduct, some courts and commentators have sought to explain the distinction between “competition on the merits” and exclusionary conduct by asking instead why the relevant conduct was profitable for the dominant firm.²⁰² In particular, they focus on the connection between the profitability of the relevant conduct for the firm and the firm’s market power. In this Article, these tests for unilateral anticompetitive conduct are referred to as “profit-focused” tests.²⁰³ Unlike effects-based tests, which depend on an accurate

dominant firms may be captured by the Australian SLC test. Importantly, however, the SLC test might also give rise to liability where a dominant firm’s product design change was genuinely intended to create benefits for consumers, but the intended benefits ultimately failed to materialize. In this respect, the court would not be required to consider the dominant firm’s intent or purpose in introducing the design change if the conduct in fact gave rise to a substantial lessening of competition. Nor would the court be permitted to take into account the fact that condemning such conduct may affect the incentives of dominant firms to invest in innovative conduct more generally.

201. See Kemp, *supra* note 163, at 15 (naming four main weaknesses in the Harper Proposal); BUS. COUNCIL OF AUSTRAL., *supra* note 149, at 57 (explaining how the uncertainty associated with an effects-based approach can deter firms from engaging in lawful conduct).

202. See, e.g., *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 608, 610-11 (1985); ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 144-45 (1978); Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975); Janusz A. Ordover & Robert D. Willig, *An Economic Definition of Predation: Pricing and Product Innovation*, 91 YALE L.J. 8, 15 (1981).

203. This Part draws on the author’s analysis of such tests in Kemp, *supra* note 33, at 660-78. To be clear, these courts and commentators do not focus on the economic profit of the firm as an indication of the *existence* of monopoly power. Rather, they consider how the firm’s profit is likely to be affected by the impugned conduct, and particularly the relationship between that profit and the firm’s resulting market power, in assessing whether that conduct should be regarded as anticompetitive.

analysis of the likely effect of the impugned conduct in the relevant markets, profit-focused tests concentrate attention on the impact of the conduct on the firm undertaking the conduct to determine *how* the firm profited, or was likely to profit, from the conduct.²⁰⁴ In short, they rely on the premise that exclusionary conduct which is not profitable apart from its effect in extending market power is not competition on the merits. Conduct that would be profitable in the absence of this extension of market power should be protected as competition on the merits.²⁰⁵

In the United States, profit-focused tests came to the fore in the 1970s as a means of identifying specific categories of anticompetitive conduct.²⁰⁶ Around the turn of the century, however, some courts and commentators attempted to synthesize and expand these tests as a general standard for unilateral anticompetitive conduct—a necessary condition for liability, rather than a sufficient condition for the existence of anticompetitive behavior.²⁰⁷ Importantly, these tests also share a similar rationale, with each profit-focused test representing one method of identifying the objective purpose of the impugned conduct.²⁰⁸ The unfolding of these proposals and the reasons for their rejection as a general standard for exclusionary conduct in the United States are explained in the following sections.

204. *Id.* at 676.

205. See Brief of Amici Curiae Economics Professors in Support of Respondent at 7, *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682) (acknowledging that the purpose of the “sacrifice test” is to provide protection to ordinary businesses, including alleged monopolists, to ensure that its conduct is promoting social welfare).

206. See, e.g., BORK, *supra* note 202, at 144-45 (explaining profit-motives theory in the context of defining predation); Areeda & Turner, *supra* note 202, at 709-18 (looking at marginal cost pricing and the average variable cost test in relation to predatory pricing); Ordover & Willig, *supra* note 202, at 20-24 (referring to predatory profit sacrifice and predatory product innovations).

207. Sherman Act Section 2 Joint Hearing: Academic Testimony Before the U.S. Dept. of Justice & Federal Trade Commission, 27-30 (2007) (testimony of Aaron Edlin); Jonathan M. Jacobson & Scott A. Sher, “No Economic Sense” Makes No Sense for Exclusive Dealing, 73 ANTITRUST L.J. 779, 783 (2006).

208. See *infra* Part III(E).

B. Profit Sacrifice in the Case Law

The use of profit-focused tests, or at least profit-focused reasoning, has been evident in the case law on monopolization under Section 2 of the Sherman Act, especially in predatory pricing cases. In *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*,²⁰⁹ for example, the Supreme Court endorsed, in general terms, the below-cost pricing requirement advocated by Areeda and Turner in their seminal article on predatory pricing.²¹⁰ The Court noted the significance of a firm setting its price at a level that deliberately sacrifices profits, stating that an “agreement to price below the competitive level requires the conspirators to forgo profits that free competition would offer them” in the hope of obtaining “later monopoly profits.”²¹¹ Later, in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, the Supreme Court held that predatory pricing requires proof of the dominant firm pricing “below an appropriate measure of cost” (without specifying what that measure should be), as well as a reasonable prospect or a dangerous probability of the firm recouping its investment in below-cost prices.²¹² Subsequently, in *United States v. AMR Corp.*, the District Court of Kansas applied the Areeda-Turner test, using average variable cost as a proxy for marginal cost, to determine whether prices had fallen below an “appropriate measure of cost.”²¹³

But on occasion courts have also referenced the way in which exclusionary conduct becomes profitable in cases that do not involve predatory pricing.²¹⁴ For example, in *William Inglis &*

209. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986).

210. *Id.* at 589, 594; Jacobson & Sher, *supra* note 207, at 783.

211. *Matsushita*, 475 U.S. at 588-89.

212. *Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222, 224 (1993).

213. *United States v. AMR Corp.*, 140 F. Supp. 2d 1141, 1203 (D. Kan. 2001); *see also* *Cargill, Inc. v. Monfort of Colo., Inc.*, 479 U.S. 104, 117-18 (1986) (explaining how predatory pricing below the appropriate measure may eliminate competitors in the short run and reduce competition in the long run).

214. *See, e.g.*, *Covad Commc'ns Co. v. Bell Atl. Corp.*, 398 F.3d 666, 670 (D.C. Cir. 2005) (explaining how Bell Atlantic's failure to share its facilities and certain network elements was inadequate to violate the Sherman Act); *MetroNet Servs. Corp. v. Qwest Corp.*, 383 F.3d 1124, 1132-33 (9th Cir. 2004) (holding that Qwest did not violate the monopolization provision of the Sherman Act when Qwest set per location pricing even

Sons Baking Co. v. ITT Continental Baking Co., the Ninth Circuit explained that, to violate Section 2 of the Sherman Act, conduct “must be such that its anticipated benefits were dependent upon its tendency to discipline or eliminate competition and thereby enhance the firm’s long-term ability to reap the benefits of monopoly power.”²¹⁵ That is, the profitability of the conduct depends on its tendency to perpetuate monopoly power by excluding rivalry.

The Supreme Court also pointed to the relevance of profit sacrifice in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*²¹⁶ This case did not concern a predatory practice, but instead a firm’s refusal to deal by terminating a joint venture in the provision of ski lift passes.²¹⁷ Nonetheless, the Court noted that the evidence supported an inference that the defendant “was not motivated by efficiency concerns [but] that it was willing to sacrifice short-run benefits and consumer goodwill in exchange for a perceived long-run impact on its smaller rival” and that the defendant “was more interested in reducing competition in the Aspen market over the long run.”²¹⁸ Later advocates of profit-focused tests have relied on this passage in support of their arguments, while other commentators have asserted that the Court in *Aspen* relied on an effects-based test.²¹⁹

Subsequently, in *Neumann v. Reinforced Earth Co.*, Judge Bork employed a profit-focused test for monopolization, outlining a similar definition of predation to that which he had put forward in *The Antitrust Paradox*, that:

predation involves aggression against business rivals through the use of business practices that would not be considered profit maximizing except for the expectation that (1) actual rivals will be driven from the market, or the entry of potential rivals blocked or delayed, so that

though it was unprofitable for a period of time).

215. *William Inglis & Sons Baking Co. v. ITT Cont’l Baking Co.*, 668 F.2d 1014, 1030 (9th Cir. 1981).

216. *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 610-11 (1985).

217. *Id.* at 603-04.

218. *Id.* at 608, 610-11.

219. Sherman Act Section 2 Joint Hearing: Academic Testimony Before the U.S. Dept. of Justice & Federal Trade Commission, 30-31 (2007) (testimony of Aaron Edlin); Patterson, *supra* note 5, at 39.

the predator will gain or retain a market share sufficient to command monopoly profits, or (2) rivals will be chastened sufficiently to abandon competitive behavior the predator finds threatening to its realization of monopoly profits.²²⁰

Such conduct is only profitable because it preserves the dominant firm's monopoly profits by excluding or disciplining rivals. Here, the outlines of the "but for" test, later advocated by the Antitrust Division of the U.S. Department of Justice, are apparent. In 2003, the Antitrust Division referred to this line of cases and proposed a new "screen" for monopolization cases under Section 2 of the Sherman Act,²²¹ noting that it often found it useful, in the context of monopolization claims, to ask if the impugned conduct "make[s] economic sense for the defendant but for its elimination or lessening of competition" (the "but for" test).²²² The resemblance to Bork's test is evident.²²³

The Antitrust Division advocated its "but for" test in a number of enforcement actions at that time.²²⁴ In one of these cases, *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko LLP* ("*Trinko*"), the Supreme Court demonstrated a clear preference for a restricted interpretation of Section 2 and expressed the view that the earlier successful refusal to deal

220. *Neumann v. Reinforced Earth Co.*, 786 F.2d 424, 427 (D.C. Cir. 1986).

221. R. Hewitt Pate, Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, *The Common Law Approach and Improving Standards for Analyzing Single Firm Conduct*, Address Before the Thirtieth Annual Conference on International Antitrust Law and Policy 8 (Oct. 23, 2003), <http://www.usdoj.gov/atr/public/speeches/202724.pdf> [<http://perma.cc/74XT-AWGQ>].

222. *Id.*

223. Compare BORK, *supra* note 202, at 144 (characterizing predation as conduct that would not maximize profits except for the expectation of (1) driving players out of the market or (2) causing rivals to abandon competitive efforts) with Pate, *supra* note 221 (stating that the Antitrust Division asks whether conduct would make not make economic sense but for its elimination or lessening of competition).

224. See, e.g., *United States v. Microsoft Corp.*, 253 F.3d 34, 57, 62, 107 (D.C. Cir. 2001) (finding that the district court expressly did not adopt the position that Microsoft would have lost its position in the OS market but for its anticompetitive behavior); see also Brief for the United States and the Federal Trade Commission as Amici Curiae Supporting Petitioner at 15, *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682) (explaining that conduct is exclusionary only if it would not make economic sense but for the tendency to impair competition).

claim in *Aspen* lay at the outer limits of Section 2 liability.²²⁵ The Court distinguished the facts in *Trinko* from *Aspen Skiing*, in part, on the basis that, in its view, a key element of the liability finding in *Aspen Skiing* was the defendant's "willingness to forsake short-term profits to achieve an anticompetitive end."²²⁶ In this way, the Court highlighted the importance of profit sacrifice in monopolization claims beyond predatory pricing. The Antitrust Division considered this decision to be an implicit endorsement of its "but for" test.²²⁷

C. *Proposals for a Profit-Focused Test for Unilateral Conduct Generally*

Following the Antitrust Division's support for a "but for" monopolization screen and the Supreme Court's comments in *Trinko*, some antitrust commentators began to endorse the expansion of similar profit-focused tests to unilateral anticompetitive conduct claims in general.²²⁸ There was, at this time, vigorous debate about what kind of test might be adopted as a universal standard for unilateral anticompetitive conduct.²²⁹

225. *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 399 (2004)

226. *Id.* at 409. *See also* *Covad Commc'ns Co. v. Bell Atl. Corp.*, 398 F.3d 666, 676 (D.C. Cir. 2005) (noting that Bell Atlantic's actions indicated a potential willingness to sacrifice immediate profits in the attempt to drive Covad out of the market).

227. J. Bruce McDonald, Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dep't of Justice, Antitrust Division Update: *Trinko* and *Microsoft*, Remarks Before the Houston Bar Association Antitrust and Trade Regulation Division 11 (Apr. 8, 2004); *cf.* Eleanor M. Fox, *Is There Life in Aspen After Trinko? The Silent Revolution of Section 2 of the Sherman Act*, 73 ANTITRUST L.J. 153, 168 (2005) (explaining how lower courts are confining the *Aspen* exception to cases of prior voluntary dealing, with some assuming that sacrifice-of-profits is necessary for a Section 2 violation).

228. *E.g.*, Patterson, *supra* note 5. There had, however, been some earlier advocacy for this approach. *See, e.g.*, Thomas A. Piraino Jr., *Identifying Monopolists' Illegal Conduct Under the Sherman Act*, 75 N.Y.U. L. REV. 809, 845 (2000) (proposing a new standard which would focus on the substantive purpose of the monopolist and which would make the conduct illegal if it made "no economic sense other than as a means of perpetuating or extending monopoly power").

229. There was also debate concerning the appropriate tests for unilateral anticompetitive conduct in the European Union, including consideration of profit-focused tests. *See, e.g.*, Philip Marsden, *Exclusionary Abuses and the Justice of "Competition on the Merits,"* in *THE REFORM OF EC COMPETITION LAW: NEW CHALLENGES* 411, 414-16 (Ioannis Lianos & Ioannis Kokkoris, eds., 2010) (examining the resulting different

Some claimed that a test that focused on the likely source of the dominant firm's gain would provide greater predictability and administrability while reducing error costs;²³⁰ others, following the dicta of the D.C. Circuit in *United States v. Microsoft Corp.*,²³¹ proposed a test that considered the net effect of the conduct on competition in the relevant market(s).

Melamed, for example, proposed a "profit sacrifice" test as a general test for unilateral anticompetitive conduct, although he distinguished his test from the profit sacrifice concept familiar in predation cases on the basis that his test avoided the temporal dimension of identifying "a short-term sacrifice in search of a long-term, anticompetitive payoff."²³² The test proposed by Melamed focused instead on whether the conduct was profitable because it excluded rivals and thereby preserved or enhanced the firm's market power.²³³ If the conduct would not be profitable for the firm in the absence of the resulting preservation or enhancement of market power, it should be regarded as anticompetitive.²³⁴

Melamed's test compared the incremental costs of the conduct²³⁵ with the benefits resulting from the conduct—including variable cost savings, revenues from additional units sold, increased revenues from quality improvements, and increased demand—to determine whether it would be profitable absent an exclusionary effect.²³⁶ "The relevant benefits did *not* include the ability to charge higher prices, or to shift the variable cost curve downward, as a result of the conduct's exclusionary

enforcement approaches, and the merits of each); John Vickers, *Abuse of Market Power*, 115 *ECON. J.* 244, 253-56 (2005) (discussing various tests based on profit sacrifice, productive efficiency, and consumer harm).

230. See *supra* Part II.

231. *United States v. Microsoft Corp.*, 253 F.3d 34, 58-59 (D.C. Cir. 2001).

232. Melamed, *supra* note 3, at 1255; see also A. Douglas Melamed, *Exclusive Dealing Agreements and Other Exclusionary Conduct – Are There Unifying Principles?*, 73 *ANTITRUST L.J.* 375, 393 (2006) (arguing that the sacrifice test provides "simple, effective, and meaningful guidance" to firms so they can avoid liability without having to avoid procompetitive conduct).

233. Melamed, *supra* note 3, at 1255.

234. *Id.*

235. Here, incremental costs are the costs, including opportunity costs, that the defendant would not incur but for the conduct.

236. *Id.* at 1256.

effect, since these would be benefits derived from maintaining or augmenting market power.”²³⁷ As with the earlier tests, this test considers the likely source of the dominant firm’s gain to draw an inference about the firm’s purpose or intent in engaging in the conduct. As Melamed explained, the test condemns “only conduct that makes no sense apart from exclusion and resulting market power” and thereby “ensures that the antitrust laws condemn only conduct from which an anticompetitive intent can unambiguously be inferred.”²³⁸

At about the same time Melamed published his proposal, Werden proposed a slightly different version of a profit sacrifice test, which he called the “no economic sense” test.²³⁹ When applying Werden’s test, the court should ask “whether challenged conduct would have been expected to be profitable apart from any gains that conduct may produce through eliminating competition.”²⁴⁰ The test is whether the conduct that allegedly creates or maintains a monopoly by its tendency to exclude existing or potential competition would have been profitable if those competitors were not excluded and the monopoly was not created or maintained.²⁴¹ Like Melamed’s test, the “no economic sense” test requires consideration of the gains from the conduct, ignoring those that stem from eliminating competition, and the costs of undertaking the conduct.²⁴²

D. The “Take Advantage” Test in Australia and New Zealand

As noted earlier, in Australia, Section 46(1) of the CCA prohibits a corporation with substantial market power from “taking advantage” of that power for one of three proscribed purposes.²⁴³ The “take advantage” element is intended to play a central role in distinguishing between vigorous,

237. Kemp, *supra* note 33, at 668.

238. Melamed, *supra* note 3, at 1257. *See also* Piraino, *supra* note 228 (“Conduct should be illegal under Section 2 if it makes no economic sense other than as a means of perpetuating or extending monopoly power.”).

239. Werden, *supra* note 15, at 414-15.

240. *Id.* at 414.

241. *Id.* at 415.

242. *Id.* at 416.

243. *Competition and Consumer Act 2010*, (Cth) pt IV div 2 s 46 (Austl.).

efficiency-enhancing competition and anticompetitive conduct.²⁴⁴ It has been interpreted in case law as a requirement that the dominant firm “used” its substantial market power to engage in the impugned conduct.²⁴⁵ This “use” of substantial market power will be established if the plaintiff shows that the dominant firm engaged in conduct that it would not, or could not, engage in if it did not possess substantial market power.²⁴⁶

In Australia, the “take advantage” standard has not generally been explained as a profit-focused test of the kind described here.²⁴⁷ But it is submitted that the “take advantage” element bears striking similarities to the profit-focused tests advocated in the United States. Like them, the “take advantage” element has been applied by Australian courts to take account of the profitability of the conduct for the dominant firm rather than the effect of the conduct on the competitive process: the focus is on the relationship between the likely profitability of the conduct for the dominant firm and the firm’s market power. More specifically, in determining whether the firm has taken advantage of its market power, the Australian courts have assessed the likely profitability of the impugned conduct for a firm with substantial market power and for a firm in a competitive market, or a firm without

244. Philip L. Williams, *Should an Effects Test Be Added to s46?*, Paper Presented at the Competition Law Conference, Sydney (May 24, 2014); Kemp, *supra* note 29, at 344.

245. *Queensland Wire Indus Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177, 191 (Austl.) (noting that determination as to whether a firm has “taken advantage” of its position of control in a market requires no hostile intent but simply that the firm “has used that power”); *cf. Universal Music Austl Pty Ltd v Australian Competition & Consumer Comm’n* (2003) 131 FCR 529, 563 (Austl.) (discussing that it is necessary to determine not only the existence of market power, but that it has been abused).

246. “In determining for the purposes of this section whether, by engaging in conduct, a corporation has taken advantage of its substantial degree of market power in a market, the court may have regard to any or all of the following:

- (a) whether the conduct was *materially facilitated* by the corporation’s substantial degree of power in the market;
- (b) whether the corporation engaged in the conduct *in reliance* on its substantial degree of power in the market;
- (c) whether it is likely that the corporation *would have engaged in the conduct if it did not have* a substantial degree of power in the market;
- (d) whether the conduct is *otherwise related to* the corporation’s substantial degree of power in the market.” *Competition and Consumer Act* pt IV div 2 s 46(6A) (emphasis added);

247. Kemp, *supra* note 33, at 669.

substantial market power.²⁴⁸

Where the Australian test diverges from the profit-focused tests in the United States is in its explanation of the requisite relationship between market power and profit. The U.S. tests ask whether the conduct would make business sense in the absence of the *resulting* market power.²⁴⁹ In contrast, the “take advantage” test asks whether the conduct would make sense in the absence of the firm’s *ex ante possession* of substantial market power, essentially asking if it would have been profitable for the firm to proceed with the conduct if it did not possess substantial market power *before* it engaged in the conduct.²⁵⁰ This question is often answered by posing a counterfactual in which a firm engages in the same conduct in a competitive market: the “competitive market” counterfactual.²⁵¹

The underlying assumption of the “take advantage” standard is that firms in a competitive market are likely to engage in efficient conduct since non-efficient conduct will be sanctioned by the competitive process; thus, conduct that is likely in a competitive market is efficient conduct.²⁵² It follows that conduct that is profitable on the part of a firm without substantial market power is always competitive conduct, no matter the market conditions under which that conduct is in fact undertaken. The U.S. profit-focused tests do not make this assumption. Instead of hypothesizing a market in which the dominant firm does not possess substantial market power, the U.S. tests hypothesize a situation in which the conduct does not exclude competitive behavior.²⁵³ Rather than considering a “competitive market”

248. *Australian Competition & Consumer Comm’n v Cement Austral Pty Ltd* [2013] FCA 909, ¶ 4 (Austl.); *Melway Publ’g Pty Ltd v Robert Hicks Pty Ltd* [1999] FCR 128, 135 (Austl.); *Commerce Comm’n v. Telecom Corp. of N.Z. Ltd.* [2010] NZSC 111 at [31] (N.Z.).

249. Melamed, *supra* note 3, at 1257.

250. Or if the conduct occurred in a competitive market. See *Commerce Comm’n v. Telecom Corp.* [2010] NZSC at [13].

251. *E.g., id.*; *Cement Austral Pty Ltd*, [2013] FCA at ¶ 3013. In New Zealand, this is the only method of proving “taking advantage” which is recognized by the courts. N.Z. MINISTRY OF BUS., INNOVATION & EMPLOYMENT, *supra* note 30, at 21-22.

252. See *Dowling v Dalgety Austral Ltd* (1992) 34 FCR 109, 144 (Austl.) (noting that Section 46 discourages conduct “which would not be possible in a competitive market, thereby promoting competitive conduct”)

253. The profits that a firm can derive while its rivals continue to impose the same

counterfactual, the U.S. tests ask whether the conduct would have remained profitable even if competition by rivals were not excluded or disciplined.²⁵⁴

E. The Common Concern of Profit-Focused Tests: Objective Purpose

Each of the tests outlined in this Part requires consideration of the likely source of the dominant firm's profit as a result of the impugned conduct, and the relationship between that profit and the firm's market power. These tests also appear to share a similar rationale for focusing on the connection between profit and market power, explaining the objective *purpose* underlying the conduct in question, and particularly whether the conduct was designed to create profit only by suppressing the competitive responses of the dominant firm's rivals.²⁵⁵ As Lao explains the "profit sacrifice" test:

[B]usinesses do not generally engage in strategies that are unprofitable or otherwise contrary to their economic interests. Therefore, if a monopolist engages in an unprofitable refusal to deal, we assume that the firm has taken that course of action only because it believed and expected the refusal to increase barriers to competition, which would allow it to earn greater monopoly profits in the future. In other words, *the defendant's likely purpose*

level of competitive constraint must result from the superior efficiency of the incumbent and not simply from the preservation or enhancement of the incumbent's monopoly power. See Ordovery & Willig, *supra* note 202, at 10 (clarifying that the profit sacrifice test does not punish an incumbent for legitimate competitive responses to rival action).

254. Kemp, *supra* note 33, at 677.

255. See, e.g., BORK, *supra* note 202, at 144 (explaining that, under the predation theory, rivals will be driven from the market, leaving the predator with a market share sufficient to command monopoly profits); Keith N. Hylton, *The Law and Economics of Monopolization Standards*, in *ANTITRUST LAW AND ECONOMICS* 82 (Keith N. Hylton, ed. 2010) (noting that the specific intent approach condemns monopolizing acts when it appears that the dominant firm's sole purpose is to destroy competition); Gavil, *supra* note 4, at 52 (applying the but-for test to determine if the monopolist would have undertaken the conduct but for its anticompetitive effects); Piraino, *supra* note 228, at 845 (arguing that courts should focus on a monopolist's purpose for its conduct to ensure there is a consistent standard and to avoid deterring legitimate competitive conduct); Salop, *supra* note 13, at 355-56 (emphasizing that the key antitrust issue is competitive effect, even though it may give insight into the monopolist's intent).

in refusing to deal *was not to enhance its own efficiency but to invest in future monopoly profits through excluding or disadvantaging its rivals.*²⁵⁶

With regard to the nature of the conduct, its likely effects, and surrounding circumstances, the purpose of the conduct was to perpetuate the firm's monopoly power by suppressing rivalry.

A concern with objective purpose can also be discerned in the Australian “take advantage” test, where the courts seek a “business rationale” for the conduct which is “independent of market power”—if the conduct is only profitable because the firm possesses market power, the underlying rationale for the conduct must have been anticompetitive.²⁵⁷ Similarly, tests for predatory pricing in the United States reveal a focus on the objective purpose or rationale of the conduct.²⁵⁸ These tests for predatory pricing proceed from the assumption that all firms seek to maximize their profits.²⁵⁹ Given this assumption, a firm that *sacrifices* profits in the short term raises the suspicion that it is acting with the ultimate purpose of maximizing its profits by preventing rivals from competing in the longer term.²⁶⁰

Later profit-focused tests have applied this logic to competitive conduct more broadly. In Melamed's words, one of the benefits of his more general “profit sacrifice” test is that

by condemning only conduct that makes no sense apart from exclusion and resulting market power, the sacrifice test ensures that the antitrust laws condemn only conduct from which *an anticompetitive intent can*

256. Lao, *Antitrust Intent*, *supra* note 25, at 187 (emphasis added).

257. See Robertson, *Primacy of “Purpose” – Part 1*, *supra* note 177, at *43 (noting that anticompetitive purpose should be used to determine if conduct is efficiency enhancing or destructive of the competition process); see also *Australian Competition & Consumer Comm'n v Australian Safeway Stores Pty Ltd* (2003) 129 FCR 339, 408 (Austl.) (finding it “necessary to look at not only what the firm did, but why the firm did it”).

258. See Salop, *supra* note 13, at 314-15 (noting the Supreme Court's two-part liability standard for predatory pricing, applicable to all exclusionary conduct, which looks at below-cost pricing and the likelihood of recoupment).

259. Areeda & Turner, *supra* note 202, at 702-03.

260. Brief of Amici Curiae Economics Professors in Support of Respondent at 4-5, *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682); LAWRENCE ANTHONY SULLIVAN, *HANDBOOK OF THE LAW OF ANTITRUST* 113 (1977).

*unambiguously be inferred.*²⁶¹

But the relevant intent is not the firm's subjective intent. As Werden explains:

In applying the no economic sense test, *what matters are the objective economic considerations for a reasonable person*, and not the state of mind of any particular decision maker. The test does not condemn conduct undertaken because of an unreasonable belief that the conduct would have an exclusionary effect. Nor does it condemn conduct because the decision maker did not clearly focus on, or even was unaware of, what were sound economic reasons for undertaking the conduct.²⁶²

Rather than focusing on the “subjective motivation” for the conduct, the test asks “whether the conduct would have been rational but for any payoff from eliminating competition.”²⁶³

Werden also emphasizes that the “no economic sense” test “inquires into the reasonably anticipated impact of the challenged conduct when undertaken, and not into the actual impact of the conduct.”²⁶⁴ Conduct should not be condemned on the basis of consequences—including its ultimate profitability or unprofitability—that could not be anticipated at the time the conduct was undertaken. This accords with Salop's view that an *ex ante* assessment of conduct, based on information reasonably available at the outset, is more appropriate in cases involving conduct with unpredictable outcomes.²⁶⁵ Advocates of the “take advantage” test in Australia similarly argue that this test permits dominant firms to plan their conduct based on information reasonably available to them at the outset, rather than requiring firms to predict the actual market outcomes of their conduct.²⁶⁶ All of these views point to the relevance of the purpose of the conduct when it was initiated.

261. Melamed, *supra* note 3, at 1257 (emphasis added).

262. Werden, *supra* note 15, at 416-17 (emphasis added) (footnotes omitted).

263. *Id.* at 426.

264. *Id.* at 416 (footnote omitted).

265. Salop, *supra* note 13, at 313-14, 339.

266. *Id.* at 341-42.

F. Criticisms of Profit-Focused Tests

Notwithstanding these arguments in favor of profit-focused tests, the use of profit-focused tests as a general standard for unilateral anticompetitive conduct has generally been opposed on the basis that they would be under-inclusive in this role.²⁶⁷ This has been one of the main criticisms of Werden's "no economic sense" test and Melamed's "profit sacrifice" test.²⁶⁸

Even the Antitrust Division, while acknowledging the usefulness of these tests in some circumstances, did not ultimately adopt a profit-focused test for all unilateral conduct cases. It noted that these tests focus only on the effect of the impugned conduct on *the dominant firm*, such that they may excuse some practices that have an anticompetitive effect on the relevant markets and ultimately consumer welfare.²⁶⁹ Similarly, in Australia, the Australian Competition and Consumer Commission, the Harper Panel, and some commentators have argued that the "take advantage" test has proved under-inclusive as a test for unilateral anticompetitive conduct because it fails to take into account the impact of the conduct on the relevant markets, resulting in the absolution of plainly anticompetitive

267. *E.g.*, Brief of Amici Curiae Economics Professors in Support of Respondent at 5-6, *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682); U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT 42 (2008), <https://www.justice.gov/sites/default/files/atr/legacy/2009/05/11/236681.pdf> [<http://perma.cc/DC5H-P7LE>]; Salop, *supra* note 13, at 14. In fact, Ordover and Willig, together with other prominent economics professors, vigorously opposed the use of their "profit sacrifice" test as a general standard in monopolization cases, stating that, "there undeniably are circumstances where business conduct can be damaging to the public welfare even though it passes the sacrifice test." Brief of Amici Curiae Economics Professors in Support of Respondent at 6, *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682). Thus a requirement that such a test should be satisfied in all unilateral conduct cases "could immunize from antitrust scrutiny a wide range of conduct that can only be viewed as reducing overall consumer welfare." *Id.* at 16. The authors listed instances of unilateral conduct not captured by the "profit sacrifice" test. *Id.* at 20-21. Ordover and Willig make particular reference to conduct that is otherwise unlawful, as well as examples of "cheap" exclusion, also explained in this section. *Id.* at 18; *see also* Gavil, *supra* note 4, at 56 (explaining that the sacrifice test is flawed in its assumption that predation is not a concern if it is costless); Lao, *Antitrust Intent*, *supra* note 25, at 188 (expounding on the under-inclusive nature of profit sacrifice tests).

268. Hovenkamp, *supra* note 13, at 115-16; Jacobson & Sher, *supra* note 207, at 786.

269. U.S. DEP'T OF JUSTICE, *supra* note 267, at 41-42.

conduct in some cases.²⁷⁰

Profit-focused tests may, for example, be under-inclusive when applied to “mixed” conduct—conduct that produces some gains from improved efficiency as well as gains from increasing or augmenting market power.²⁷¹ In this respect, the “no economic sense” test and its variants may be particularly unhelpful in cases concerning tying and exclusive dealing.²⁷² These practices will almost always have some efficiency justification—they will make at least some “economic sense.” However, by focusing solely on the internal costs and benefits of the conduct for the defendant, profit-focused tests may neglect the net harm caused by the conduct to the competitive process and consumer welfare.²⁷³

Profit-focused tests in general have also been criticized for failing to capture cheap exclusion.²⁷⁴ Cheap exclusion has been defined as “conduct that costs or risks little to the firm engaging in it, both in absolute terms and when compared to the gains (or potential for gains) it brings.”²⁷⁵ While some unilateral anticompetitive conduct (such as predatory pricing) entails substantial costs and uncertain gains even for a dominant firm, cheap exclusion is attractive because it involves very low costs and little or no sacrifice of profits. Consider, for example, threats of predation made to deter the entry of a new rival,²⁷⁶ abuse of governmental processes,²⁷⁷ abuse of standard-setting

270. AUSTRALIAN COMPETITION & CONSUMER COMM’N, *supra* note 29; Submission from Stephen Corones, *supra* note 29, at 7-10; Kemp, *supra* note 29, at 344-49.

271. Gavil, *supra* note 4, at 52-54; Popofsky, *supra* note 62, at 476; Salop, *supra* note 13, at 356, 361.

272. Hovenkamp, *supra* note 98, at 12; Jacobson & Sher, *supra* note 207, at 786.

273. Hovenkamp, *supra* note 98, at 12; Jacobson & Sher, *supra* note 207, at 784, 788-92.

274. *E.g.*, Brief of Amici Curiae Economics Professors in Support of Respondent at 18-19, *Verizon Commc’ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682); Elhauge, *supra* note 2, at 280-82; Gavil, *supra* note 4, at 56-57; Jacobson & Sher, *supra* note 207, at 784, 790-92; Salop, *supra* note 13, at 357.

275. Susan A. Creighton et al., *Cheap Exclusion*, 72 ANTITRUST L.J. 975, 977 (2005).

276. Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263, 282 (1981) (looking at the implicit threat of predation along with the monopolist’s reputation to persuade rivals either to stay out of the market or to stop competing with the monopolist).

277. BORK, *supra* note 202, at 347.

processes,²⁷⁸ “gaming” of patent regulations to stall the introduction of generic rivals,²⁷⁹ and fraudulent acquisition of a patent.²⁸⁰ Cheap exclusion is often also “plain” exclusion²⁸¹ in the sense that it is anticompetitive exclusion that lacks any efficiency justification.²⁸²

On the other hand, there is an argument that some profit-focused tests are *over*-inclusive in respect of conduct—for example, investing in a new factory or in research to create a patentable product—that requires a sacrifice of short-run profits and depends on an increase in market power for its profitability, but which overwhelmingly benefits consumers in the long term.²⁸³ But as Elhauge argues, “[d]elayed gratification is not an antitrust offense.”²⁸⁴ Treating it as such could have “disastrous *ex ante* effects” on dominant firm incentives, and particularly dynamic efficiency, or the rate of innovation in a market.²⁸⁵

G. Responses to Criticisms of Profit-Focused Tests

Advocates of profit-focused tests have responded to these criticisms. Melamed is confident that his “profit sacrifice” test would not result in false negatives arising from “mixed” conduct (conduct that gives rise to gains from increased efficiency as well as gains from exclusionary effects).²⁸⁶ By weighing the incremental costs of the conduct against the incremental gains

278. *Market Forces, Competitive Dynamics, and Gasoline Prices: FTC Initiatives to Protect Competitive Markets, Before the H. Subcomm. on Oversight & Investigations, Comm. on Energy & Commerce*, 110th Cong. 10 (2007) (prepared statement of the Federal Trade Commission).

279. Creighton et al., *supra* note 275, at 983-84 (illustrating an example of gamesmanship in the approval of generic drugs).

280. Baker, *supra* note 58, at 539.

281. *Id.* at 544.

282. See Creighton et al., *supra* note 275, at 982 (noting that cheap exclusion involves opportunistic or otherwise harmful behavior for both parties and consumers alike).

283. U.S. DEP’T OF JUSTICE, *supra* note 267, at 41; Elhauge, *supra* note 2, at 274-75, 278-79.

284. Elhauge, *supra* note 2, at 279.

285. *Id.* at 275.

286. See Melamed, *supra* note 3, at 1257-58 (arguing that market-wide balancing tests are more difficult to administer and have perverse incentive effects in comparison to the sacrifice test).

from the conduct,²⁸⁷ Melamed claims to be able to identify conduct that depends upon an exclusionary effect for its profitability.²⁸⁸ Critics, on the other hand, argue that, in practice, determining which gains arise from increases in efficiency and which gains result from an increase in market power may be near impossible.²⁸⁹

By contrast, Werden recognizes that his “no economic sense” test may not be useful in these circumstances and acknowledges that a different type of test may be needed to assess such conduct.²⁹⁰ He has acknowledged, in particular, that his test might not be feasible in circumstances where “the conduct generates legitimate profits as well as profits from eliminating competition,” as, for example, in some cases involving bundled rebates.²⁹¹

With regard to cheap exclusion, Werden considers that such conduct would be captured by his “no economic sense” test since it assesses whether the conduct creates a profit because of its exclusionary effect alone, whether or not it involves any short-run sacrifice.²⁹² Melamed, on the other hand, acknowledges that his “profit sacrifice” test might not capture certain cheap or plain exclusion,²⁹³ but argues that such conduct could be condemned in any case, without the need for his “profit sacrifice” test, an effects-based test, “or any other elaborate inquiry.”²⁹⁴

These responses by proponents of profit-focused tests acknowledge that such a test will not capture all significant instances of unilateral anticompetitive conduct, meaning that supplementary tests may be necessary. But how do we frame these supplementary tests? Responses to the possibility of “plain”

287. *Id.* at 1256.

288. *Id.* at 1256-57.

289. *See, e.g.*, Popofsky, *supra* note 65, at 464 (noting that the profit-sacrifice test may not be applicable in many cases); Salop, *supra* note 13, at 323 (explaining that the profit sacrifice test may classify profits as both procompetitive and anticompetitive).

290. Werden, *supra* note 15, at 414.

291. *Id.* at 421 (citing *LePage’s Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003) (en banc), *cert. denied*, 542 U.S. 952 (2004)).

292. *See* Werden, *supra* note 15, at 425-26 (discussing a hypothetical scenario in which his “no economic sense” test accounts for instances of cheap exclusion).

293. Melamed, *supra* note 3, at 1257-58.

294. *Id.* at 1260.

exclusion are particularly revealing in this respect. Melamed contends that such conduct “can be condemned as anticompetitive conduct without need for the sacrifice test, market-wide balancing, or any other elaborate inquiry.”²⁹⁵ In one sense, Melamed has a point. There is substantial consensus that “plain” exclusion should be condemned without the need for a detailed analysis of its actual or probable effects.²⁹⁶ In short, such conduct is so lacking in any value to society that a less costly, truncated analysis is justifiable: there is a negligible risk that imposing liability in these cases will deter beneficial behavior.²⁹⁷

Other commentators have also set this type of exclusion apart, arguing that “plain” or “naked” exclusion “may be easily condemned without reference to any test for unreasonably exclusionary conduct.”²⁹⁸ But it is submitted that this exceptional treatment of plain exclusion misses an important opportunity. It is precisely when all parties agree that “of course” such conduct should be condemned that we should inquire after the norm on which we rely. In this case, the unspoken norm is that a dominant firm should not be permitted to engage in conduct which, objectively assessed, has no purpose other than the suppression of rivalry to preserve market power; or conduct with an objective anticompetitive purpose. It would be a waste of resources to engage in an effects analysis of conduct with such a uniformly detrimental purpose. It is submitted that this implicit norm should be recognized rather than dismissed for its obviousness.

With regard to the potential *over*-inclusiveness of profit-focused tests, the flipside of this norm is apparent. Werden contends that the “no economic sense” test should not be applied to conduct which is generally socially beneficial such as “improved product quality, energetic market penetration, successful research and development, cost-reducing innovations, and the

295. *Id.*

296. *E.g.*, NAZZINI, *supra* note 46, at 101; Gavil, *supra* note 4, at 62; Krattenmaker & Salop, *supra* note 8, at 282; Popofsky, *supra* note 65, at 464; Salop & Romaine, *supra* note 6, at 664; A. Douglas Melamed, Principal Deputy Assistant Attorney Gen., Antitrust Div., U.S. Dep’t of Justice, Exclusionary Vertical Agreement, Address Before the American Bar Association Antitrust Section (Apr. 2, 1998), <http://www.usdoj.gov/atr/public/speeches/1623.htm> [<http://perma.cc/NUK8-GM3L>].

297. Hovenkamp, *supra* note 98, at 31.

298. Lambert, *supra* note 11, at 1183.

like,” but instead that such conduct should be the subject of prudential safe harbors on the ground that it is “overwhelmingly likely to enhance consumer welfare.”²⁹⁹ But, as Elhauge argues, this approach fails to reveal precisely what normative criteria determine when the profit-focused test would apply and when it would not. Instead it relies on implicit normative criteria.³⁰⁰

It is submitted that the implicit norm at work in these instances is the opposite of that mentioned above—that a firm should be permitted to engage in conduct with the purpose of protecting or enhancing its market power by impairing the ability of its rivals to compete, *if at the outset, and objectively assessed, that conduct had the purpose of creating benefits for consumer welfare which were at least proportionate to any consumer harm likely to be created by the exclusion.*

IV. PURPOSE AND INTENT IN THE CASE LAW

A. *Introduction to Purpose and Intent*

Since the passage of the first unilateral conduct laws, courts, commentators, and legislators have given consideration to the purpose or intent of a dominant firm when characterizing its exclusionary behavior.³⁰¹ In more recent decades, this focus on purpose or intent has been criticized as irrelevant and misleading, particularly since the late 1970s, when the Chicago School began to exert its influence on the field.³⁰² Competition

299. Werden, *supra* note 15, at 419.

300. Elhauge, *supra* note 2, at 278.

301. *E.g.*, *N. Pac. Ry. Co. v. United States*, 356 U.S. 1, 8 (1958); *Chi. Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918); *Standard Oil Co. v. United States*, 221 U.S. 1, 76 (1911); *United States v. Am. Tobacco Co.*, 221 U.S. 106, 182 (1911); *A-G (Cth) v The Adelaide Steamship Co Ltd* (1913) 18 CLR 30, 30-31 (Austl.); *Adelaide Steamship Co Ltd v The King* (1912) 15 CLR 65, 65 (Austl.); Barry E. Hawk, *Attempts to Monopolize – Specific Intent as Antitrust’s Ghost in the Machine*, 58 CORN. L. REV. 1121, 1125 (1973).

302. *Ball Mem’l Hosp., Inc. v. Mut. Hosp. Ins. Inc.*, 784 F.2d 1325, 1339 (1986); *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 232 (1983); *see, e.g.*, RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 189-90 (1976) (noting that ascertaining the intent of a major corporation through litigation can be very difficult as the availability of evidence of improper intent is often a function of luck and of the defendant’s legal sophistication); Hovenkamp, *supra* note 18, at 1037-38 (criticizing the historical role of intent in monopolization cases); *see also* *United States v. Microsoft Corp.*, 253 F.3d 34, 59 (D.C. Cir. 2001) (explaining that the courts concentrate on the effect of the content rather

law, it is said, is not concerned with morality or subjective perceptions of commercial motives, but with the actual or likely economic effect of firm conduct.³⁰³ Unlike a firm's subjective intentions, the *effect* of a firm's conduct can also be measured with the assistance of expert economists, at least in theory. Nonetheless, courts and commentators continue to refer to the purpose or intent that underlies the unilateral conduct in question.³⁰⁴

The relevance of purpose or intent in characterizing unilateral conduct has been debated in the antitrust commentary. Opinions are divided between those who consider that purpose or

than the intent, where evidence of intent is only used to help explain the likely consequence of the anticompetitive behavior); Eleanor M. Fox, *What is Harm to Competition? Exclusionary Practices and Anticompetitive Effect*, 70 ANTITRUST L.J. 371, 378 (2002) (purporting that the Chicago School's solution to their criticism of over-regulation was that conduct should not be regulated unless there was clear proof of inefficient activity); C. Scott Hemphill, *Less Restrictive Alternatives in Antitrust Law*, 116 COLUM. L. REV. 927, 966 (2015) (explaining that intent is given little significance in antitrust examinations because examiners can be confused by colorful language); Lao, *Reclaiming a Role*, *supra* note 25, at 164 (discussing how the role of intent evidence in monopolization analysis became marginalized when the Chicago School's analysis emerged in the late 1970s); Robertson, *Primacy of "Purpose" – Part 2*, *supra* note 177, at *5 (contending that an increasing emphasis on "manifestations" rather than "motivations" was evident from the time of Smith and Marshall).

303. See HOVENKAMP, *supra* note 52, at 51 (contending that antitrust law only considers whether conduct is anticompetitive, not if conduct is ethical); Hemphill, *supra* note 302, at 968 (discussing Justice Brennan's suggested approach and how it can be adapted to focus on effect, giving the example of how a defendant will choose an action that harms consumers rather than the alternative because of the gain it expects to receive, rather than being concerned with acting in an ethical manner); Kathryn McMahon, *Church Hospital Board or Board Room?: The Super League Decision and Proof of Purpose Under Section 4D*, 1997 CCLJ LEXIS 6,*4 (1997) (noting that the objectives of the misuse of market power provision are economic in nature); Robertson, *Primacy of "Purpose" – Part 2*, *supra* note 177, at *5, *15-16 (noting that competition law, such as the Trade Practices Act, is a form of economic regulation and therefore requires an economic method of analysis but that within economic theory there is "little place for subjective values"); Donald Robertson, *Taking Advantage of Market Power in a Modern Economy*, 10 N.Z. BUS. L.Q. 26, 56 (2004) (describing two approaches where both questions were about examining the effect of the conduct of the firm, not the subjective purpose).

304. See, e.g., Cass & Hylton, *supra* note 21, at 657, 659-60 (noting those that suggest that evidence of subjective intent is relevant); Lao, *Reclaiming a Role*, *supra* note 25, at 202 (discussing two modern monopolization cases where intent influenced the outcome); McMahon, *supra* note 303, at *11-12 (detailing cases in which courts considered subjective purpose when analyzing anticompetitive conduct); Robertson, *supra* note 303, at 35 (noting courts' continued emphasis on subjective purpose).

intent has a critical, but currently underrated, role to play in the characterization of unilateral anticompetitive conduct,³⁰⁵ and those who argue that considerations of purpose or intent are at best a distraction and at worst a ground for wrongly condemning procompetitive conduct.³⁰⁶ Other commentators concede that a dominant firm's subjective purpose may occasionally prove a useful consideration, especially where the competitive impact of the conduct is ambiguous.³⁰⁷

It is submitted that, once more precise terminology is adopted and the relevant commentary more carefully analyzed, there is actually significant consensus about the role of purpose or intent in the assessment of unilateral conduct. At the outset, it is generally accepted that liability should not be based on a firm's subjective intention to harm or eliminate rivals alone, since this intention may be consistent with procompetitive conduct.³⁰⁸ Even if the test is reframed to consider whether the firm acted with the purpose of harming the competitive *process*, focusing on subjective purpose still gives rise to difficulties in proving corporate intention.³⁰⁹ There is also the more fundamental

305. See, e.g., Cass & Hylton, *supra* note 21, at 658 (justifying the intent analysis in antitrust law); Lao, *Reclaiming a Role*, *supra* note 25, at 202-03 (arguing that intent evidence can be objective and plays an important role in antitrust cases); McMahon, *supra* note 303, at *2 (noting how courts manipulate purpose to achieve specific outcomes in cases).

306. See, e.g., RICHARD A. POSNER, ANTITRUST LAW 214-15 (2d ed. 2001) (explaining that rules which rely on proof of intent will be applied capriciously); Frank H. Easterbrook, *Monopolization: Past, Present, and Future*, 61 ANTITRUST L.J. 99, 102-03 (1992) (contending that searching for some intent is a wasted effort); Michael C. Quinn, Note, *Predatory Pricing Strategies: The Relevance of Intent Under Antitrust, Unfair Competition, and Tort Law*, 64 ST. JOHN'S L. REV. 607, 617, 628 (1990) (noting the Chicago School's view that the focus should not be on a defendant's subjective intent, which may help prevent the federal courts from being clogged with insubstantial allegations).

307. See, e.g., Lao, *Reclaiming a Role*, *supra* note 25, at 158 (purporting that subjective statements, so long as they have some credibility, can be helpful in interpreting the objective steps taken by a firm); David McGowan, *Networks and Intention in Antitrust and Intellectual Property*, 24 J. CORP. L. 485, 516 (1999) (arguing that in cases where the evidence is unclear, intent should be considered a relevant factor).

308. E.g., PHILLIP AREEDA & HERBERT HOVENKAMP, 3A ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION ¶ 806e (2d ed. 1986), NAZZINI, *supra* note 46, at 64; POSNER, *supra* note 306, at 214-15; Robertson, *Primacy of "Purpose" – Part 2*, *supra* note 177, at *30.

309. See McGowan, *supra* note 307, at 514-15 (discussing the issues with

problem that the actual state of mind of the relevant agents of a corporation is not a consistent predictor of the type of harm that unilateral conduct rules are intended to address.³¹⁰ However, this does not mean that all considerations of purpose are redundant. On the contrary, an analysis of the underlying rationale for unilateral conduct rules and the tests which purport to characterize unilateral conduct reveal a fundamental concern with the *objective* purpose or rationale of the conduct.

Unilateral conduct rules are not intended to condemn the possession of substantial market power, but only a certain method of preserving or enlarging that power which is considered to damage social welfare—the extension of market power by the suppression of competitive responses by the firm’s rivals or potential rivals and not by improvement of the firm’s efficiency, performance, or innovation to the benefit of consumers.³¹¹ The adoption of such a method of maintaining market power is evident in the inherent design of the conduct.³¹² It can be ascertained objectively, with regard to the nature of the conduct in the relevant market context. The optimal standard for unilateral anticompetitive conduct should depend on the identification of such an objective anticompetitive purpose.³¹³

B. Subjective Purpose or Intent to Harm Competitors

Antitrust courts and commentators have often disparaged considerations of a dominant firm’s subjective intent as potentially misleading in unilateral anticompetitive conduct cases.³¹⁴ Fact finders may be overly impressed by evidence of

determining intent of a firm with case examples); Robertson, *Primacy of “Purpose” – Part 2*, *supra* note 177, at *25-27 (noting that subjective purpose is difficult to prove because of the lack of single purpose and because some firms will be better at hiding evidence from these individuals than others).

310. See POSNER, *supra* note 302, at 214-15 (considering how misleading the comments of sales executives are because they can sound like “evidence of predatory intent to the naïve”); Werden, *supra* note 15, at 416-17 (discussing the advantages of the no economic test because it does not consider the subjective state of mind of decision makers).

311. Lao, *Reclaiming a Role*, *supra* note 25, at 155.

312. *Dandy Power Equip Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238, 277 (Austl.).

313. See *supra* Part I for the definition of “unilateral anticompetitive conduct.”

314. Cass & Hylton, *supra* note 21, at 675-76; see POSNER, *supra* note 302, at 214-15

aggressively competitive intent and misconstrue it as an indication of an anticompetitive plot.³¹⁵ Some commentators concede that there may be a role for subjective purpose in a limited range of unilateral conduct cases, as explained in the following section.³¹⁶ However, there is substantial consensus that antitrust liability should not generally be triggered by a certain *type* of purpose or intent, particularly a dominant firm's subjective purpose or specific intent to damage or eliminate its competitors ("eliminary purpose or intent").³¹⁷

A number of monopolization cases have emphasized that evidence of a firm's eliminatory intent is not only insufficient to establish antitrust liability, but may also be entirely consistent with the very competition that antitrust legislation seeks to promote.³¹⁸ Indeed, from the tone of these cases, a proper savaging of one's rivals might actually be applauded.

In *Ball Memorial Hospital, Inc. v. Mutual Hospital Insurance, Inc.*, the Seventh Circuit Court of Appeals pointed out that harm to rivals is an inevitable side effect of procompetitive behavior:

Competition is a ruthless process. A firm that reduces cost and expands sales injures rivals—sometimes fatally. The firm that slashes costs the most captures the greatest sales and inflicts the greatest injury. The deeper the injury to rivals, the greater the potential benefit.

(explaining how sales executives are likely to use language that appears to be anticompetitive when bragging about their "competitive prowess"); Hovenkamp, *supra* note 13, at 120 (describing how when intent and materiality are weighed, this approach reestablishes the issues with pre-*Matsushita* antitrust litigation); Lao, *Reclaiming a Role*, *supra* note 25, at 152-53 (arguing that going through business records to find evidence that is misleading also increases litigation costs and creates more inaccurate decisions).

315. See HOVENKAMP, *supra* note 52, at 178 (explaining how injuries caused by anticompetitive behavior can be confused with injuries caused by aggressive competition that antitrust encourages); Cass & Hylton, *supra* note 21, at 711-12 (providing an example of how corporate memoranda could be misconstrued as evidence in a subjective inquiry, leading to false convictions).

316. See *supra* Part IV(C).

317. See POSNER, *supra* note 306, at 214 ("Any doctrine that relies upon proof of intent is going to be applied erratically at best."); Cass & Hylton, *supra* note 21, at 712, 715 (describing doubts that a subjective intent test could be applied in a predictable fashion and that a number of scholars believe it should have no place in antitrust analysis).

318. See, e.g., *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 232 (1st Cir. 1983) (arguing that looking for an intent to harm is too vague a standard).

These injuries to rivals are byproducts of vigorous competition, and the antitrust laws are not balm for rivals' wounds.³¹⁹

It is acknowledged that rivals will be harmed by competitive behavior and aggressive competitors are aware of this as a likely outcome. As the Seventh Circuit stated in *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*:

Rivalry is harsh, and consumers gain the most when firms slash costs to the bone and pare price down to cost, all in pursuit of more business. Few firms cut price unaware of what they are doing; price reductions are carried out in pursuit of sales, at others' expense. . . . If courts use the vigorous, nasty pursuit of sales as evidence of a forbidden "intent", they run the risk of penalizing the motive forces of competition. . . . Almost all evidence bearing on "intent" tends to show both greed-driven desire to succeed and glee at a rival's predicament.³²⁰

Even the fact that a firm is motivated by hostility or "pure malice"³²¹ towards its rivals does not distinguish anticompetitive conduct from procompetitive.³²²

Even those who advocate a central role for purpose in the assessment of unilateral conduct acknowledge that eliminatory intent alone should not be a ground for liability.³²³ The critical

319. *Ball Mem'l Hosp., Inc. v. Mut. Hosp. Ins., Inc.*, 784 F.2d 1325, 1338 (7th Cir. 1986).

320. *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1401-02 (7th Cir. 1989).

321. *Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 225 (1993).

322. *Olympia Equip. Leasing Co. v. W. Union Tel. Co.*, 797 F.2d 370, 379 (7th Cir. 1986); see also Easterbrook, *supra* note 306, at 102-03 (describing how the same elements of greed exist in anticompetitive and procompetitive conduct, including where a firm wants to grow and beat its rivals).

323. *William Inglis & Sons Baking Co. v. ITT Cont'l Baking Co.*, 668 F.2d 1014, 1028 (9th Cir. 1981); Paul G. Scott, *The Purpose of Substantially Lessening Competition: The Divergence of New Zealand and Australian Law*, 19 WAIKATO L. REV. 168, 180-81 (2011); see Okeoghene Odudu, *The Role of Specific Intent in Section 1 of the Sherman Act: A Market Power Test?*, 25 WORLD COMPETITION 463, 484 (2002) (noting that others have tried to erase intent from antitrust law); Robertson, *supra* note 303, at 35 (describing how the courts' emphasis of the subjective purpose test causes them to be distracted from the true objective of the legislation—to punish conduct that is not welfare-enhancing).

point is that vigorous, socially beneficial competition necessarily harms, and may ultimately exclude, less efficient competitors.³²⁴ The fact that a dominant firm acts with the specific intent to achieve, or the subjective purpose of achieving, this end does not distinguish anticompetitive conduct from procompetitive conduct. A test that relies on eliminatory intent is not a sound basis for a unilateral conduct rule.

C. *Subjective Purpose of Hindering the Competitive Process*

While competitors may be harmed by vigorous competition, they are also harmed when a dominant firm adopts strategies aimed at hindering the competitive process. Some commentators have therefore argued that evidence of a dominant firm's subjective purpose to harm the competitive *process* plays a useful role in characterization in particular kinds of unilateral conduct cases.³²⁵ Such evidence may be especially relevant where objective evidence concerning the impact of the impugned conduct is ambiguous: that is, where it is difficult to discern the likely outcome of the conduct from an effects analysis alone.³²⁶ For example, when considering whether a firm accused of predatory pricing will be able to recoup its losses from below-cost pricing by charging supracompetitive prices, it may be relevant, at least in close cases, that the firm itself was aware that it was pricing below cost and expected to profit from it.³²⁷ In these

324. BORK, *supra* note 202, at 39.

325. See, e.g., Cass & Hylton, *supra* note 21, at 658 (noting that scholars have urged courts to focus on the monopolist's subjective intent); Daniel J. Gifford, *The Role of the Ninth Circuit in the Development of the Law of Attempt to Monopolize*, 61 NOTRE DAME L. REV. 1021, 1021 (1986) (suggesting that a defendant's intent explains the defendant's behavior); Lao, *Reclaiming a Role*, *supra* note 25, at 158 (indicating that the subjective intent of a dominant firm can be deciphered by the factfinder).

326. HOVENKAMP, *supra* note 52, at 52; Geoff Edwards, *The Perennial Problem of Predatory Pricing: A Comparison and Appraisal of Predatory Pricing Laws and Recent Predation Cases in the United States and Australia*, 30 AUSTRALIAN BUS. L. REV. 170, 191 (2002); Hemphill, *supra* note 302, at 968; see also Lao, *Reclaiming a Role*, *supra* note 25, at 178 (arguing that consideration of intent would complement expert testimony, making it more applicable). *But see* Gifford, *supra* note 325, at 1049 (indicating that courts prefer evidence of conduct to verify intent).

327. John R. Allison, *Ambiguous Price Fixing and the Sherman Act: Simplistic Labels or Unavoidable Analysis*, 16 HOUS. L. REV. 761, 767 (1979); Edwards, *supra* note 326, at 191.

circumstances, the alleged predator may be in the best position to predict the likely losses from its below-cost pricing and its chances of profiting from the strategy.

Evidence that the firm possessed the subjective purpose of harming the competitive process might also be relied on as a *substitute* for proof of anticompetitive effect in cases where there is a high risk of under-deterrence from a rule that requires a demonstration of anticompetitive effect.³²⁸ This category of conduct includes certain types of “plain” or “naked” exclusion, where the dominant firm engages in exclusionary conduct with the sole purpose of suppressing rivalry.³²⁹ In these circumstances, it may be unreasonably costly to prove the actual harm caused by the conduct where there is no plausible procompetitive justification for the conduct.³³⁰

On the other hand, some have argued that it would be reasonable to require proof of subjective purpose *in addition to* proof of likely anticompetitive effect in cases where there is a high risk of over-deterrence. As noted earlier, Hovenkamp contends that proof of subjective intent to harm to the competitive process should be required in cases concerning product design changes which both create some improvement for consumers and exclude rivals to a certain extent.³³¹ He argues that innovative activity of this kind is valuable to society, and the potential cost of “false convictions” so great, that the conduct should only be condemned if it is established that the design change was a sham intended to hamper rivalry in the market.³³²

Notwithstanding the recognition of the potential role of subjective purpose or intent in these limited situations, the weight of academic opinion is against a general requirement of subjective purpose or intent in all cases.³³³ At the outset, a general

328. See NAZZINI, *supra* note 46, at 61 (stating that inquiring into the impact on price and output of a dominant firm’s conduct can be wasteful and create risks of under-deterrence).

329. *Id.* at 60-61; *see supra* Part III(F).

330. NAZZINI, *supra* note 46, at 61.

331. Hovenkamp, *supra* note 18, at 1046.

332. *Id.* at 1045; *see also* NAZZINI, *supra* note 46, at 60 (arguing that proof of intent will encourage “thorough market inquiry” which will in turn prevent false convictions).

333. Lao, *Reclaiming a Role*, *supra* note 25, at 152; NAZZINI, *supra* note 46, at 65; Cass & Hylton, *supra* note 21, at 715-16.

test based on subjective purpose is not well aligned with the central objective of competition law, namely the protection of the competitive process.³³⁴ Expressions of the state of mind of the relevant actors rarely address the critical question of whether the proposed conduct is likely to extend the firm's market power by suppressing the competitive responses of rivals, but are instead more likely to relate to the firm's eliminatory intent or a desire to protect its market share, both of which may cause no harm to the competitive process.³³⁵

A rule that conditions liability on proof of subjective purpose in all cases may also fail to capture important instances of anticompetitive conduct and create perverse incentives for dominant firms. Under a subjective purpose test, plaintiffs face the evidentiary hurdle of proving corporate intent in circumstances where evidence of the intentions and purposes of various employees and officers of the firm often vary considerably.³³⁶ Requiring proof of subjective anticompetitive intent or purpose may also create the wrong incentives for dominant firms by encouraging firms to conceal evidence of anticompetitive plans and adopt "correct" semantic descriptions for their strategies, rather than alter the substantive nature of those strategies. In this way, a subjective purpose test is said to favor sophisticated, well-counselled firms over the more naïve.³³⁷

More importantly, the mental states of the dominant firm's officers and employees—their own perceptions of the competitive impact of the firm's conduct—do not determine the likelihood that the firm's conduct will have an adverse effect on the competitive

334. See, e.g., *News Ltd v S Sydney Dist Rugby League Football Club Ltd* (2003) 215 CLR 563, 579, 605 (Austl.) (finding that an objective interpretation of section 4D seems more in accord with the legislation's goal of promoting competition).

335. See POSNER, *supra* note 306, at 214-15 (explaining how evidence of improper intent is usually a "function of luck" and of "the defendant's legal sophistication").

336. McGowan, *supra* note 307, at 514 ("More generally, what one identifies as 'the firm's' intention in the run of cases will probably depend on who is asked, and even then the answer of one individual may not be worth much.").

337. POSNER, *supra* note 306, at 214; Cass & Hylton, *supra* note 21, at 732; see also Mark Berry, *Competition Law*, N.Z. L. REV. 599, 608-09 (2006) (indicating that a subjective purpose inquiry is problematic because "win at all costs" language is common and often made by those not responsible for formulating strategy).

process.³³⁸ The critical issue is the nature of the conduct in the context of the relevant market and not the dominant firm's awareness of the nature of that conduct.³³⁹ Conduct should not be absolved on the basis of the dominant firm's erroneous assessment of the likely impact of its conduct or because the firm failed to turn its mind to the likely impact of its conduct.

D. Subjective and Objective Purpose Distinguished

To be sure, a firm's subjective purpose or intent may sometimes be determined by reference to indirect or objective evidence. Even where there is direct evidence of the relevant person's intention, subjective purpose may be inferred from conduct,³⁴⁰ its effect or likely effects, and the circumstances surrounding the relevant conduct.³⁴¹ In fact, some courts have recognized that the best evidence of subjective purpose may be provided "by looking at what was actually done," bearing in mind the relevant experience, knowledge and expertise of the person in question,³⁴² or by determining the objective effect or likely effect of the relevant conduct.³⁴³

However, it is submitted that the distinction between subjective and objective purpose is nonetheless significant. Although under both standards courts may have regard to objective factors, such as the nature and likely effect of the conduct within the context of the relevant market, this does not mean that the standards are equivalent. In particular, it is submitted that the nature of the ultimate inquiry under each standard is different. Each takes account of similar evidence for

338. See Cass & Hylton, *supra* note 21, at 712 (stating that the inquiry into subjective intent would result in random punishment); Easterbrook, *supra* note 306, at 106 (detailing how the Court in *Matsushita* used objective criteria to determine any injury to consumers).

339. Robertson, *Primacy of "Purpose" – Part 2*, *supra* note 177 at 25-26.

340. *Dowling v Dalgety Austl Ltd* (1992) 34 FCR 109, 143 (Austl.)

341. *Universal Music Austl Pty Ltd v Australian Competition & Consumer Comm'n* (2003) 131 FCR 529, 589 (Austl.); *Hughes v W Australian Cricket Ass'n Inc* (1986) 19 FCR 10, 38 (Austl.); Lao, *Reclaiming a Role*, *supra* note 25, at 158, 202;

342. *Asx Operations Pty Ltd v Pont Data Austl Pty Ltd [No. 1]* (1990) 27 FCR 460, 482.

343. Cf. Lao, *Reclaiming a Role*, *supra* note 25, at 208 (noting that subjective steps can be useful for the interpretation of objective steps, even when ambiguous).

a different purpose.

Under an objective standard, objective factors are taken into account to attribute a state of mind to a notional person standing in the shoes of the respondent, based on the nature of the impugned conduct in its context.³⁴⁴ The focus is on determining “the nature of conduct rather than the mind of actors.”³⁴⁵ According to Robertson’s description of objective purpose:

The ultimate issue for determination when a court is assessing purpose is: What is the economic actor *really* trying to do in commercial or economic terms? We are concerned with the commercial, not the criminal context. We are not trying to discern what people mean by having a “purpose” in everyday commercial conversations. In asking this question we are asking for an *explanation* of commercial conduct—to make the best sense we can of the conduct—not a psychological analysis of the minds of the economic agents.³⁴⁶

In contrast, under a subjective standard, objective factors are taken into account to determine the actual state of mind of the person engaging in the conduct. The evidence may be objective, but it is nonetheless used to reach a conclusion about the subjective intent of the relevant person, or “the purpose of the particular respondent.”³⁴⁷ In this case, the focus is on testing the plausibility of any direct evidence regarding purpose.³⁴⁸

In a given case, the court may be satisfied that the direct evidence establishes that the subjective purpose of the particular corporation was not anticompetitive: for example, where there is “a single directing mind” and clear evidence of his or her purpose.³⁴⁹ If the direct evidence of the corporation’s subjective purpose is strong, the fact that the conduct *by its nature* has an

344. Cass & Hylton, *supra* note 21, at 659.

345. *Dandy Power Equip Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238, 277 (Austl.).

346. Robertson, *Primacy of “Purpose” – Part 1*, *supra* note 177, at *62 (footnote omitted).

347. *Universal Music Austl Pty Ltd v Australian Competition & Consumer Comm’n* (2003) 131 FCR 529, 589 (Austl.).

348. *Id.*

349. *Id.* at 587; e.g., *Dowling v Dalgety Austl Ltd* (1992) 34 FCR 109, 143 (Austl.).

anticompetitive purpose will not be determinative.³⁵⁰ A corporation may escape liability for conduct which is, by its nature, objectively anticompetitive, on the basis of its own actual but misguided assessment of the competitive nature of the conduct. More importantly, it is submitted that the subjective purpose approach overlooks the superior logic of using objective purpose to characterize unilateral anticompetitive conduct.³⁵¹

E. “Normal Business Purpose”

The intuition that underlying purpose or rationale is critical to the characterization of unilateral conduct is evident in the case law on monopolization. In both the United States and Australia, a number of cases concerning single-firm conduct have considered whether the defendant firm acted with an acceptable purpose or rationale, often described as a “legitimate business purpose.”³⁵² In these cases, courts have asked whether there is a “legitimate” explanation for allegedly anticompetitive conduct such that it should be absolved.³⁵³ The requisite explanation has been variously described as a “normal business purpose,”³⁵⁴ “legitimate business reasons,”³⁵⁵ a “valid business reason,”³⁵⁶ and “legitimate purposes.”³⁵⁷

All of these labels make clear that the courts are concerned to the underlying purpose or rationale of the impugned conduct. And yet, in the absence of further explanation as to the *type* of purpose which should absolve a dominant firm, these phrases merely beg the question, what is it that makes a purpose “normal” or “valid” or “legitimate” in this context?³⁵⁸ The fact that it is considered to

350. Cf. McMahon, *supra* note 303, at *5 (arguing that, in certain cases, Australian courts have failed to take this approach, essentially applying an objective purpose test under a “subjective purpose” label).

351. See *infra* Part V.

352. *E.g.*, Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 597 (1985); Eastman Kodak Co. v. Image Tech. Servs. Inc., 504 U.S. 451, 483 (1992); *Queensland Wire Indus Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177, 193 (Austl.).

353. *Queensland Wire*, 167 CLR at 193.

354. *Aspen Skiing Co.*, 472 U.S. at 608.

355. *Id.* at 597.

356. *Eastman Kodak Co.*, 504 U.S. at 483 (1992).

357. *Id.* at 502.

358. Elhauge, *supra* note 2, at 265.

be a “business” purpose cannot be determinative. Anticompetitive practices are undertaken in the course of “business” as surely as procompetitive practices. It is submitted that the relevant, absolving purpose is improved efficiency, innovation, or quality, which creates proportionate benefits for consumers, as opposed to the suppression of rivalry by competitors.³⁵⁹ The importance of this particular distinction, and the objective quality of the relevant purpose, can be discerned in the jurisprudence on legitimate business purpose in the United States and Australia.

In *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, the Supreme Court found that the defendant ski field operator had contravened Section 2 of the Sherman Act by terminating its joint venture with the operator of a neighboring ski field, a joint venture which had previously enabled consumers to purchase an “all-Aspen ticket” providing entry to all of the ski fields in the area.³⁶⁰ In reaching its conclusion, the Court stated that perhaps the most significant evidence of monopolization was the defendant’s failure to persuade the jury that its conduct was “justified by any normal business purpose.”³⁶¹

The Court in *Aspen* emphasized the short-term sacrifice by the defendant inherent in the impugned conduct as well as the defendant’s failure to provide any convincing “efficiency justification” for the conduct. It held that, in the circumstances, the jury might well have concluded that the defendant had elected to forego the short-run benefits of offering the all-Aspen ticket “because it was more interested in reducing competition in the Aspen market over the long run by harming its smaller competitor.”³⁶² That is, the objective purpose of the termination of the multi-ticket arrangement was not to improve the dominant firm’s efficiency or performance but to suppress the rivalry offered by its erstwhile joint venture partner.³⁶³ It was this purpose—this

359. See *Data Gen. Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147, 1183 (1st Cir. 1994) (noting that business justifications are usually valid so long as they are connected to the enhancement of consumer welfare).

360. *Aspen Skiing Co.*, 472 U.S. at 610.

361. *Id.* at 608.

362. *Id.*

363. *But see* Easterbrook, *supra* note 306, at 107 (offering an alternative view on the nature of the conduct in *Aspen*, namely that a lack of enough tourists who could use a multiple-mountain pass resulted in squandered economies of scale).

method of preserving market power—which was objectionable.

Cass and Hylton have drawn on the decision in *Aspen* and other U.S. authorities concerning the relevance of “valid business reasons,” to argue that an “objective specific-intent standard” is the proper standard for determining monopolization claims under Section 2 of the Sherman Act.³⁶⁴ They explain that this objective approach asks what state of mind can reasonably be attributed to the defendant in light of its actions, rather than asking for direct evidence of what the defendant had in mind.³⁶⁵ In their view, the current law on Section 2 suggests that the plaintiff must prove that the defendant acted “solely or primarily out of intent to gain or to maintain monopoly power.”³⁶⁶ “Objective specific intent” is inferred on the basis of evidence indicating the “absence of credible efficiency justifications for the monopolist’s conduct.”³⁶⁷

A similar process of reasoning is evident in certain Australian decisions under Section 46(1) that have referred to the *Aspen* decision.³⁶⁸ In *Australian Competition & Consumer Commission v Safeway*, for example, Justices Heerey and Sackville rejected the primary judge’s finding that, because a non-dominant firm might just as easily have engaged in the impugned conduct, Safeway had not infringed Section 46(1).³⁶⁹ According to Justices Heerey and Sackville, the primary judge’s approach overlooked the critical issue of the defendant’s purpose or rationale in engaging in the conduct:

In our view, this analysis ignores the question of *why* Safeway engaged in the impugned conduct. This is not the same question as to whether one or more of the

364. Cass & Hylton, *supra* note 21, at 659, 675.

365. *Id.* at 659.

366. *Id.* at 673, 708.

367. *Id.* at 676.

368. See *Australian Competition & Consumer Comm’n v Boral Ltd.* [1999] FCA 1318, ¶ 158 (Austl.) (noting that a firm with substantial market power does not take advantage of its power by following a course of action ordinarily taken by firms without substantial market power); *Melway Publ’g Pty Ltd v Robert Hicks Pty Ltd* [1999] FCR 128, 135 (Austl.) (citing and discussing the Supreme Court’s decision in *Aspen*); *Queensland Wire Indus Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177, 193 (Austl.) (arguing that BHP did not provide a legitimate reason for its refusal to sell).

369. *Australian Competition & Consumer Comm’n v Australian Safeway Stores Pty Ltd.* 129 FCR 339, 407-08.

statutorily proscribed purposes existed. Before reaching that point it is necessary to look at not only what the firm did, but why the firm did it. That is why a business rationale for the conduct, independent of the question of market power, is relevant. . . . The rationale for the conduct is critical.³⁷⁰

Their Honours went on to examine the rationale or purpose of the defendant's conduct with reference to the objective circumstances of the case by asking whether a firm would be likely to behave in the same way if it did not possess market power.³⁷¹ The relevant conduct here was Safeway's termination of supplies from bakery suppliers—"plant bakers"—who supplied bread to rival supermarkets at a discount. According to their Honours:

Its reason for doing so was to induce the plant baker to cease supplying discounted bread to an independent retailer in competition with a Safeway supermarket. As we have explained, there would have been no purpose in Safeway acting in this manner in a competitive market. On the contrary, had Safeway done so it would have inflicted economic harm on itself for no gain.³⁷²

In the absence of market power, a firm engaging in the same conduct "would have produced harm for itself without any countervailing benefit,"³⁷³ meaning that the non-dominant firm would have lost sales without any prospect of profiting by preserving its substantial market power. The critical consideration was the objective purpose of the conduct, inferred from the surrounding circumstances.³⁷⁴ Implicitly, the conduct was condemned because its underlying purpose was the suppression of rivalry from competing supermarkets selling discounted bread to preserve the dominant firm's market power.³⁷⁵ Similar references to the objective purpose or rationale underlying the impugned conduct form a common thread

370. *Id.* at 408.

371. *Id.*

372. *Id.* at 409.

373. *Id.*

374. *Id.*

375. *Id.* at 410.

throughout the jurisprudence on unilateral conduct.³⁷⁶

While these cases make the argument that the purpose or rationale underlying the conduct is critical, they have not clarified whether the mere existence of *some* “business” explanation should absolve conduct even if that conduct is also likely to cause substantial harm to the competitive process. In contrast, the objective anticompetitive purpose standard proposed in this Article clarifies that the mere existence of a “normal business purpose,” or efficiency justification, does not automatically exempt unilateral conduct from antitrust scrutiny. Even if conduct is likely to give rise to some improvement to the firm’s efficiency or the quality of its product, the conduct may have an anticompetitive purpose if its designed restraint of rivalry by competitors is disproportionate to those improvements. Thus a proportionality enquiry will sometimes be necessary to determine the firm’s objective purpose.³⁷⁷

V. THE RATIONALE FOR AN OBJECTIVE ANTICOMPETITIVE PURPOSE STANDARD

A. *Signposts in the Existing Law*

As explained throughout this Article, the existing case law and commentary on the characterization of unilateral anticompetitive conduct repeatedly point to the importance of objective anticompetitive purpose in this process, although this is rarely articulated. The common thread of objective purpose can be discerned in the following areas:

- (a) Advocates of an effects-based test, or “consumer harm” test, recognize that an *ex ante* assessment, having regard to information reasonably available to the dominant firm at the time it engaged in the conduct, may be required in cases where the outcomes of conduct are unpredictable at the outset. This is not because the direct effect of such conduct is necessarily less harmful to consumers, but because it is desirable to protect conduct which, objectively speaking, was initiated with a

³⁷⁶. See cases cited *supra* note 368.

³⁷⁷. See *infra* Part V(D).

procompetitive purpose.³⁷⁸

- (b) Profit-focused tests—including the “no economic sense” test, the “profit sacrifice” test, the Areeda-Turner test for predatory pricing, and the Australian “take advantage” test—each represent *one method* of proving objective anticompetitive purpose in some cases, but they do not cover the field and are therefore under-inclusive as a general standard for unilateral anticompetitive conduct.³⁷⁹
- (c) References in the case law to “normal business purposes” or “valid business reasons” highlight the significance of the underlying purpose or rationale of the conduct, but generally fail to articulate what makes a business purpose legitimate or illegitimate.³⁸⁰
- (d) There is general consensus that “naked” or “plain” exclusion should be condemned without the need for any detailed effects analysis. This is not because, as some assert, “no test is needed” in these cases, but because courts and commentators are applying an unspoken test, based on objective anticompetitive purpose.³⁸¹

B. A Return to the Rationale for Unilateral Conduct Rules

While a concern with objective anticompetitive purpose has been present in case law and commentary for many years as an implicit norm, it is submitted that the objective anticompetitive purpose standard should be expressly recognized and articulated. To understand the significance of objective purpose in the application of unilateral conduct rules, it is necessary to return to the rationale that underlies these rules and antitrust’s treatment of unilateral market power generally.

While monopolies are acknowledged to cause some harm, the competitive process by which monopolies are created, defended, and superseded is believed to produce redeeming benefits which

378. *See supra* Part II(D)(2).

379. *See supra* Part III(D).

380. *See supra* Part IV(E).

381. *See supra* Part III(G).

outweigh the potential harm.³⁸² Nonetheless, it is also possible for firms to achieve or maintain a monopoly position or substantial market power by another method—not by outcompeting their rivals, not by offering consumers a better product or service, but by preventing rivals from offering consumers a better product or service.³⁸³ If a dominant firm can hamstring its rivals' attempts to compete, it can enjoy its position of power without creating any benefits for consumers and deprive consumers of the benefits of increased rivalry. In these circumstances, society suffers the harms inherent in the possession of substantial market power without enjoying any of its redeeming side effects. Unilateral conduct rules therefore target this method of maintaining or enhancing market power—conduct that is designed to substantially suppress rivalry without creating proportionate benefits for consumers.

C. The Role of Objective Purpose in Characterizing Unilateral Conduct

From these foundations, the proper role for purpose in unilateral conduct rules can be discerned. The mere fact that a dominant firm acts with the goal or purpose of achieving, maintaining, or enhancing substantial market power should not be sufficient to attract condemnation. Moreover, evidence that the firm purported or intended to cause harm to its rivals is, in itself, irrelevant. What is important is the *method* adopted by the firm in pursuit of these goals. One method (superior performance and efficiency) gives rise to benefits for society, while another (suppression of competitive responses by rivals) is detrimental to society. The social disadvantages inherent in substantial market power should only be tolerated if that power is achieved by the former method, with its redeeming side effects. If market power is achieved by the latter method, both the process and the end result are harmful.

The particular method adopted by a firm might be discerned by assessing the effect of the impugned conduct on the relevant

382. See *supra* Part I.

383. See Hovenkamp, *supra* note 18, at 1038 (presenting the tactic of attempting to exclude others from markets rather than offering a superior product or service).

market or markets.³⁸⁴ If it is apparent that the conduct has substantially excluded competition without creating any proportionate benefits for consumers, it may be concluded that the firm has sought to enhance its market power by obstructing the competitive process.³⁸⁵ But it is submitted that the firm's method may also be discerned by considering the *design* inherent in the impugned conduct itself: that is, by considering whether, objectively speaking, the conduct had the purpose of hindering the competitive process to prolong or enhance the firm's market power.

Antitrust is not concerned with ethics, but with economic objectives.³⁸⁶ Its central economic objective is to increase the welfare of society as a whole and consumers in particular.³⁸⁷ In the context of unilateral conduct, the greatest threat to this goal occurs when firms with substantial market power adopt a certain method of protecting or enhancing that power, namely the suppression of competitive responses by rivals or potential rivals. The fact that a firm has adopted such a method is generally evident from the conduct itself. The firm's acts or omissions, in context, disclose their objective.

For these reasons, a dominant firm should be prevented from engaging in conduct that has the objective purpose of substantially hindering the competitive process (substantially suppressing the competitive responses of its rivals) to prolong or enhance its market power. It is not sufficient to demonstrate that the firm acted with the purpose of protecting or increasing its market power alone; nor is it sufficient to prove that the firm intended to harm or eliminate its rivals.³⁸⁸ What is required is

384. *See supra* Part II.

385. Exclusionary conduct has been defined as those acts furthering monopoly and which are either unnecessary for society's benefit, not beneficial to society at all, or cause harm to society disproportionate to their benefit. AREEDA & HOVENKAMP, *supra* note 18); Hovenkamp, *supra* note 18, at 1041.

386. John B. Kirkwood & Robert H. Lande, *The Fundamental Goal of Antitrust: Protecting Consumers, Not Increasing Efficiency*, 84 NOTRE DAME L.R. 191, 194.

387. *Id.* at 192.

388. *See* Ball Mem'l Hosp., Inc. v. Mut. Hosp. Ins., Inc., 784 F.2d 1325, 1339 (1986) (noting that vigorous competition tends to harm rivals, and "to penalize this intent is to penalize competition"); NAZZINI, *supra* note 46, at 218 (noting that the Court was wrong to hold that intent to harm rivals was insufficient).

proof that the dominant firm acted with the objective purpose of substantially suppressing rivalry by its competitors to prolong or enhance its market power without creating proportionate benefits for consumers.³⁸⁹

D. Improved Certainty and Administrability

A standard that expressly focuses on objective anticompetitive purpose improves certainty and administrability relative to effects-based tests in particular. Since this standard requires an *ex ante* assessment of the purpose of the conduct, with regard to information available at the time the firm engaged in the conduct, firms are better able to predict the lawfulness of their conduct. Firms will not be confronted with the difficulty of predicting the actual effects of their conduct, which could be affected by factors beyond the firm's control. Courts should not adopt the circular reasoning that, in these circumstances, the dominant firm should bear the burden of the uncertainty created by its anticompetitive conduct: after all, under an effects-based analysis, the conduct cannot be characterized as anticompetitive until the court establishes that the conduct created an anticompetitive effect.³⁹⁰ It is the information available to the firm at the time it engaged in the conduct which is relevant.

Relative to effects-based tests, an objective anticompetitive standard also improves certainty and administrability by permitting the court to focus on the proportionality of the impugned conduct, rather than engaging in any fine balancing of the mixed outcomes of that conduct. As noted earlier, a number of commentators and authorities have advocated a proportionality enquiry in the characterization of unilateral anticompetitive conduct.³⁹¹ Under a proportionality enquiry, it would be necessary to ask whether, at the time it engaged in the conduct, the firm's choice of strategy was proportionate to its claimed benefits, with regard to the risk and extent of any exclusion of rivalry.

389. See *supra* Part I.

390. See McGowan, *supra* note 110, at 1198 (pointing out that if a defendant can rebut a *prima facie* case of anticompetitive effect from the plaintiff, the plaintiff must either rebut or offer evidence why the harm outweighs the procompetitive benefit).

391. See sources cited *supra* note 177.

A proportionality inquiry provides courts with a framework for assessing the reasonableness of the firm's conduct at the outset to determine whether, objectively speaking, the true purpose of the conduct was to restrict competition or to compete through superior efficiency. A proportionality inquiry also provides dominant firms with a framework for assessing the legality of proposed conduct, which takes into account the reasonably foreseeable competitive impacts of their conduct without requiring precise predictions about actual outcomes which could be affected by factors beyond the firm's control. Under a proportionality approach, dominant firms should consider at the outset:

- (a) whether the conduct plausibly creates any benefits for consumer welfare;
- (b) whether there are significantly less restrictive alternatives which could achieve the same benefits;³⁹² and
- (c) whether any restriction of rivalry which might arise from the proposed strategy is disproportionate to the plausible improvements in long term consumer welfare which the strategy is designed to achieve.³⁹³

This last inquiry does not require firms to balance precisely the procompetitive and anticompetitive effects of the strategy, but to give proper consideration to the importance, extent, and plausibility of the various potential consequences for competition in the market, bearing in mind the objective of protecting long-term consumer welfare.

In short, a proportionality inquiry provides greater certainty and fairness for dominant firms, in that it does not require any "crystal ball" skills in predicting actual outcomes or determining the likely effect on competition as a result of mixed outcomes. This improved certainty is likely to reduce the over-deterrent effects of the legal standard. At the same time, a proportionality approach ensures that a dominant firm will not be permitted to rely on an efficiency justification for its conduct where it was apparent at

392. Guidance on the Commission's Enforcement Priorities in Applying Article 82 of the EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings, 2009 O.J. (C 45/02) ¶ 30.

393. Robertson, *Primacy of "Purpose" – Part 2*, *supra* note 177, at *58.

the outset that the firm was, in effect, using a sledgehammer to crack a nut—that its strategy would tend to cause disproportionate harm to consumer welfare as a result of its tendency to restrict rivalry, relative to its tendency to create benefits for consumer welfare. Of course where there is *no* plausible efficiency justification for conduct, it should be condemned without the need for any proportionality inquiry.³⁹⁴

E. Reduced Error Costs and Deterrent Effects

Finally, an objective anticompetitive purpose standard reduces the error costs inherent in profit-focused tests.³⁹⁵ While profit-focused tests may provide evidence of anticompetitive conduct in some cases, they do not capture all significant instances of anticompetitive conduct. By contrast, an objective anticompetitive purpose standard is able to take account of the outcomes of profit-focused tests at the same time as identifying the relevant purpose beyond these cases, for instance, in the case of ‘naked’ or ‘plain’ exclusion. At the same time, this standard avoids the potential *over*-inclusiveness of some profit-focused tests since it acknowledges that conduct is not anticompetitive if plausible gains for consumer welfare are at least proportionate to the plausible harm from the conduct at the outset.³⁹⁶

In short, an objective anticompetitive purpose standard targets harmful conduct, while absolving procompetitive conduct. Conduct that is initiated without an objective anticompetitive purpose is generally socially beneficial conduct. Even if such conduct occasionally causes unforeseeable harm to the competitive process and a net detriment to consumer welfare, the detriment from subjecting all conduct to an *ex post* effects analysis is likely to outweigh the benefit of capturing the occasional instance of anticompetitive effect.³⁹⁷

On the other hand, conduct that is initiated with an objective anticompetitive purpose is generally detrimental to social welfare, even if there are some cases where the anticompetitive

394. *See supra* Part III(G).

395. *See supra* Part III(E).

396. *See supra* Part III(F)-(G).

397. Hovenkamp, *supra* note 18, at 1039.

plot does not succeed or where its actual effects cannot be proved on the balance of probabilities. In particular, conduct with this purpose is likely to waste social resources (both those of the dominant firm and its rivals), exclude competitors who are equally efficient, and increase market power in the absence of superior efficiency.³⁹⁸

CONCLUSION

In the assessment of unilateral conduct, the critical task for the court is to discover the most plausible explanation for the exclusionary act in its context, to determine the end which that conduct is designed to achieve and, if that end is alleged to be the creation of benefits for consumers, whether the conduct is a proportional means of achieving that end. As Hovenkamp has argued, we should use Occam's razor to strip away "those explanations that are implausible or unproven until we have a 'core' left that characterizes the practice as pro or anticompetitive."³⁹⁹

A dominant firm's *subjective* purpose or intent is not the proper focus of unilateral conduct standards: we are not concerned with the firm's consciousness of wrongdoing. Rather, society has an interest in a dominant firm being able to plan its market conduct within the bounds of the law, with regard to information reasonably available to the firm at the outset about the likely competitive impact and proportionality of its strategy. The proper standard for unilateral anticompetitive conduct therefore focuses on the objective purpose of the impugned

398. See Brief of Amici Curiae Economics Professors in Support of Respondent at 5, *Verizon Comm'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (No. 02-682) (suggesting that in economic terms, the ramifications must be economic inefficiency because the act must produce more costs than consumer benefits, creating a presumption that social welfare is injured by an uptick in monopoly power and loss of competition); BORK, *supra* note 202, at 144 (explaining that the intention behind this conduct can be thought of as a deliberate attempt to increase market power through unconventional means); Areeda & Turner, *supra* note 202, at 712 (noting that monopolists not only cause private harm but also waste social resources when marginal costs exceed value and extinguish rivalries when pricing below marginal costs).

399. HOVENKAMP, *supra* note 52, at 108; see also Cass & Hylton, *supra* note 21, at 677 ("[T]he credible efficiency justification is one that seems likely to explain actions under the actual conditions.").

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conduct. It requires an assessment of the underlying rationale of the conduct to determine whether, objectively speaking, the act in its context was designed to extend the firm's substantial market power by stifling the competitive responses of rivals without creating proportionate benefits for consumers. This is the common thread running through the case law and commentary on monopolization in both the United States and Australia, and the standard for exclusionary conduct that should now be expressly acknowledged.