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Antitrust Modernization

Laws and Legislation Series

Luigi Ferrigno

Editor

NOVA

LAWS AND LEGISLATION SERIES

ANTITRUST MODERNIZATION

LUIGI FERRIGNO
EDITOR



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PREFACE

First, this book is fundamentally an endorsement of free-market principles. These principles have driven the success of the U.S. economy and will continue to fuel the investment and innovation that are essential to ensuring our continued welfare. Second, this book judges the state of the U.S. antitrust laws as "sound". Certainly, there are ways in which antitrust enforcement can be improved. The book identifies several. Third, the Commission does not believe that new or different rules are needed to address so-called "new economy" issues. That does not mean the Commission sees no room for improvement. To the contrary, the Commission makes several recommendations for change. This book highlights the overview of the Antitrust and the manners in which the Commission intends to improve what requires improvement.

Chapter 1 - This chapter is edited and excerpted written testimony by Deborah A. Garza and Jonathan R. Yarowsky before the Antitrust Task Force of the House Committee on the Judiciary on May 8, 2007.

Chapter 2 - Three years ago, as authorized by statute, this Commission undertook a comprehensive review of U.S. antitrust law to determine whether it should be modernized. It is our pleasure to present the results of that effort, the enclosed Report and Recommendations of the Antitrust Modernization Commission ("Report").

This Report is the product of a truly bipartisan effort. The members of the Commission were appointed by the President and the respective majority and minority Leadership of the House of Representatives and Senate with the goal of ensuring "fair and equitable representation of various points of view in the Commission." In fact, the Commissioners represented a diversity of viewpoints, which were fully and forcefully expressed during many hours of hearings and thoughtful deliberation. As one Commissioner has said, the Commission's recommendations were "fashioned on the anvil of rigorous discussion and debate." The Commission also endeavored at every turn to obtain a diversity of views from the public. In the end, the Commission was able to reach a remarkable degree of consensus on a number of important principles and recommendations.

First, the Report is fundamentally an endorsement of free-market principles. These principles have driven the success of the U.S. economy and will continue to fuel the investment and innovation that are essential to ensuring our continued welfare. They remain as applicable today as they ever have been. Free trade, unfettered by either private or governmental restraints, promotes the most efficient allocation of resources and greatest consumer welfare.

Second, the Report judges the state of the U.S. antitrust laws as “sound.” Certainly, there are ways in which antitrust enforcement can be improved. The Report identifies several. A few Commissioners have greater concerns about aspects of current enforcement, as expressed in their separate statements. On balance, however, the Commission believes that U.S. antitrust enforcement has achieved an appropriate focus on (1) fostering innovation, (2) promoting competition and consumer welfare, rather than protecting competitors, and (3) aggressively punishing criminal cartel activity, while more carefully assessing other conduct that may offer substantial benefits. The laws are sufficiently flexible as written, more-over, to allow for their continued “modernization” as the world continues to change and our understanding of how markets operate continues to evolve through decisions by the courts and enforcement agencies.

Third, the Commission does not believe that new or different rules are needed to address so-called “new economy” issues. Consistent application of the principles and focus noted above will ensure that the antitrust laws remain relevant in today’s environment and tomorrow’s as well. The same applies to different rules for different industries. The Commission respectfully submits that such differential treatment is unnecessary, whether in the form of immunities, exemptions, or special industry-specific standards.

That does not mean the Commission sees no room for improvement. To the contrary, the Commission makes several recommendations for change. A few of these recommendations call for bold action by Congress that likely will require considerable further debate. We look forward to that debate.

The following summarizes some of the more significant changes the Commission recommends.

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Chapter 1

ANTITRUST MODERNIZATION COMMISSION FINDINGS HEARING

Deborah A. Garza

Thank you Chairman Conyers, Ranking Member Chabot, and Members of the Antitrust Task Force of the House Committee on the Judiciary. Three years ago, as authorized by the Antitrust Modernization Commission Act of 2002, the Antitrust Modernization Commission (the “Commission” or “AMC”) undertook a comprehensive review of U.S. antitrust laws to determine whether they should be modernized. It is our pleasure to testify before you today on behalf of the AMC about its findings and recommendations, which were submitted to Congress and the President on April 2, 2007. A copy of the AMC Report and Recommendations (“Report”) was distributed to each member of Congress and is available at http://www.amc.gov/report_recommendation/amc_final_report.pdf.

The Commission’s Report is the product of a truly bipartisan effort. The members of the AMC were appointed by the President and the respective majority and minority Leadership of the House of Representatives and Senate with the goal of ensuring “fair and equitable representation of various points of view in the Commission.”¹ In fact, the Commissioners represented a diversity of viewpoints, which were fully and forcefully expressed during many hours of hearings and thoughtful deliberation. As one Commissioner has said, the Commission’s recommendations were “fashioned on the anvil of rigorous discussion and debate.” The Commission also endeavored at every turn to obtain a diversity of views from the public. In the end, the Commission was able to reach a remarkable degree of consensus on a number of important principles and recommendations.

First and foremost, the Report is an endorsement of free-market principles. These principles have driven the success of the U.S. economy and will continue to fuel the investment and innovation that are essential to ensuring our continued national economic welfare. They remain as applicable today as they ever have been. Free trade, unfettered by either private *or* governmental restraints, promotes the most efficient allocation of resources and greatest consumer welfare.

Second, the Report judges the state of the U.S. antitrust laws as “sound.” Certainly, there are ways in which antitrust enforcement can be improved. The Report identifies several. A few Commissioners have greater concerns about aspects of current enforcement, as expressed in their separate statements. On balance, however, the Commission believes that U.S. antitrust enforcement has achieved an appropriate focus on (1) fostering innovation, (2) promoting competition and consumer welfare, rather than protecting competitors, and (3) aggressively punishing criminal cartel activity, while more carefully assessing other conduct that may offer substantial benefits. The laws are sufficiently flexible as written, moreover, to allow for their continued “modernization” as the world continues to change and our understanding of how markets operate continues to evolve, through decisions by the courts and enforcement agencies.

Third, the Commission does not believe that new or different rules are needed to address so-called “new economy” issues. Consistent application of the principles and focus noted above will ensure that the antitrust laws remain relevant in today’s environment and tomorrow’s as well. The same applies to different rules for different industries. The Commission respectfully submits that such differential treatment is unnecessary, whether in the form of immunities, exemptions, or special industry-specific standards.

That does not mean the Commission sees no room for improvement. To the contrary, the Commission makes several recommendations for change. A few of these recommendations call for bold action by Congress that likely will require considerable further debate. We look forward to that debate.

The following summarizes some of the more significant changes the Commission recommends.²

SUBSTANTIVE ANTITRUST STANDARDS (MERGERS AND MONOPOLY)

The Commission does not recommend legislative change to the Sherman Act or to Section 7 of the Clayton Act. There is a general consensus that, while there may be disagreement about specific enforcement decisions, the basic legal standards that govern the conduct of firms under those laws are sound.

The Commission nevertheless makes several recommendations in the area of merger enforcement. The purpose of these recommendations is to ensure that policy is appropriately sensitive to the needs of companies to innovate and compete while continuing to protect the interests of U.S. consumers. In particular, the Commission urges that substantial weight be given to evidence demonstrating a merger will achieve efficiencies, including innovation-related efficiencies. The Commission also recommends that the federal enforcement agencies continue to examine the basis for, and efficacy, of merger enforcement policy. We urge the agencies to further study the economic foundations for merger enforcement policy, including the relationship between market performance and market concentration and other factors. We also recommend increased retrospective study of the effects of decisions to challenge or not challenge specific transactions. Such empirical evidence, although difficult to gather, is critical to an informed and effective merger policy.

With respect to monopoly conduct, the Commission believes U.S. courts have appropriately recognized that vigorous competition, the aggressive pursuit of business

objectives, and the realization of efficiencies are generally not improper, even for a “dominant” firm and even where competitors may lose. However, there is a need for greater clarity and improvement to standards in two areas: (1) the offering of bundled discounts or rebates, and (2) unilateral refusals to deal with rivals in the same market. Clarity will be best achieved in the courts, rather than through legislation. The Commission recommends a specific standard for the courts to apply in determining whether bundled discounts or rebates violate antitrust law.

REPEAL OF THE ROBINSON-PATMAN ACT

The Commission recommends that Congress finally repeal the Robinson-Patman Act (RPA). This law, enacted in 1936, appears antithetical to core antitrust principles. Its repeal or substantial overhaul has been recommended in three prior reports, in 1955, 1969, and 1977. That is because the RPA protects competitors over competition and punishes the very price discounting and innovation in distribution methods that the antitrust laws otherwise encourage. At the same time, it is not clear that the RPA actually effectively protects the small business constituents that it was meant to benefit. Continued existence of the RPA also makes it difficult for the United States to advocate against the adoption and use of similar laws against U.S. companies operating in other jurisdictions. Small business is adequately protected from truly anticompetitive behavior by application of the Sherman Act.

PATENTS AND ANTITRUST

Patent protection and the antitrust laws are generally complementary. Both are designed to promote innovation that benefits consumer welfare. In addition, a patent does not necessarily confer market power. Nevertheless, problems in the application of either patent or antitrust law can actually deter innovation and unreasonably restrain trade. Many of the Commission’s recommendations relating to the Sherman Act address the antitrust side of the balance. On the patent side, the Commission urges Congress to give serious consideration to recent recommendations by the Federal Trade Commission (FTC) and National Academy of Sciences designed to improve the quality of the patent process and patents. The Commission also recommends that the joint negotiation of license terms within standard-setting bodies ordinarily should be treated under a rule of reason standard, which considers both potential benefits of such joint negotiation to avoid “hold up” and the possibility that such joint negotiation might suppress innovation.

IMPROVING THE ENFORCEMENT PROCESS

To be effective, any enforcement regime must be clear, fairly administered, and not unreasonably burdensome. Several of the Commission’s recommendations are designed to improve current processes to better meet these goals.

Eliminate Inefficiencies Resulting from Dual Federal Enforcement

Except in the area of criminal enforcement (which is the responsibility of the Justice Department), federal antitrust law is enforced by both the Justice Department (DOJ) and the FTC. Both agencies, for example, are equally authorized to review mergers under the Hart-Scott-Rodino Act (HSR Act), which essentially requires all mergers valued at above \$59.7 million to be notified to the agencies and suspended until the expiration or termination of certain waiting periods. The Commission does not believe it would be feasible or wise to eliminate the antitrust enforcement role of either agency at this time. However, we make a number of recommendations designed to eliminate inconsistencies and problems that may result from dual enforcement.

Merger Clearance

The agencies have done a good job minimizing problems that can result from dual enforcement. But there is room for improvement that can only be achieved with the help of Congress. At the time of her confirmation, the current head of the FTC was asked to agree not to pursue a global merger clearance agreement between the agencies. The Commission calls on the appropriate congressional committees to revisit that position and authorize the DOJ and FTC to implement a new merger clearance agreement based on the principles of the 2002 clearance agreement between the agencies. It is bad government for mergers to be delayed by turf battles between the agencies. Such battles undermine confidence in government, damage agency staff morale, and potentially delay the realization of significant merger efficiencies without good reason. The Commission recommends that Congress revise the HSR Act to require the DOJ and FTC to resolve all clearance requests under the HSR Act within a short period of time after the parties report their transaction.

The Commission also recommends changes to ensure that mergers are treated the same no matter which agency reviews them. Specifically, the Commission recommends that Congress amend Section 13(b) of the FTC Act to prohibit the FTC from pursuing administrative litigation in HSR Act merger cases. The Commission further recommends that the FTC adopt a policy that when it seeks to block a merger in federal court, it will seek both preliminary and permanent relief in a combined proceeding where possible.

Improve the HSR Act Pre-Merger Review Process

The DOJ and FTC should continue to pursue reforms to their internal review processes that will reduce unnecessary burden and delay. The Commission also makes a number of specific recommendations designed to reduce the burden of HSR merger reviews and increase the transparency of government enforcement. For example, the Commission recommends that the agencies update their Merger Guidelines to explain how they evaluate non-horizontal mergers as well as a proposed merger's potential impact on innovation competition. The Commission also recommends that the agencies issue statements explaining why they have

declined to take enforcement action with respect to transactions raising potentially significant competitive concerns.

Improve Coordination between State and Federal Enforcement

State and federal enforcement can be strong complements in achieving optimal enforcement. But the existence of fifty independent state enforcers on top of two federal agencies can, at times, also result in uncertainty, conflict, and burden. The Commission encourages state and federal enforcers to coordinate their activities to seek to avoid subjecting businesses to multiple, and potentially conflicting, proceedings. We make a number of specific recommendations in this regard. In addition, the Commission believes States should continue to focus their efforts primarily on matters involving localized conduct or competitive effects. In addition, state and federal agencies should work to harmonize their substantive enforcement standards, particularly with respect to mergers.

De-link Agency Funding and HSR Act Filing Fees

HSR Act filing fees are used to fund DOJ and FTC antitrust enforcement activity. These fees are a tax on mergers, the vast majority of which are not anticompetitive. They do not accurately reflect costs to the government of reviewing a given filing, nor do they confer a benefit on notifying parties. But they set a precedent for other countries with merger control regimes. In the past, moreover, dips in merger activity (and filing fees) have threatened to affect the level of appropriations available for critical agency activities. The Commission recommends that Congress de-link agency funding from HSR Act filing fee revenues.

PRIVATE LITIGATION

Uniquely in the United States, private litigation has been a key part of antitrust enforcement. Under current rules, private plaintiffs are entitled to recover three times their actual damages, plus attorneys' fees. Defendants are jointly and severally liable for alleged conspiracies. There is no right of contribution among defendants. There is also only a limited right of claim reduction when one or more defendants settle. The combined effect of these rules is that one defendant can be liable for nearly all of the damages caused by an antitrust conspiracy. Defendants thus face significant pressure to settle antitrust claims of questionable merit simply to avoid the potential for excessive liability. While the rules can maximize deterrence and encourage the resolution of claims through quick settlement, they can also overdeter conduct that may not be anticompetitive.

The Commission recommends no change to the fundamental remedial scheme of the antitrust laws: the treble damage remedy and plaintiffs' ability to recover attorneys' fees. On balance, the current scheme appears to be effective in enabling plaintiffs to pursue litigation that enhances the deterrence of unlawful behavior and compensates victims. However, the Commission recommends that Congress enact legislation that would permit non-settling

defendants to obtain a more equitable reduction of the judgment against them and allow for contribution among non-settling defendants.

Indirect and Direct Purchaser Litigation

There are different rules at the federal level and among the states as to whether both direct purchasers of price-fixed goods or services and indirect purchasers may sue to recover damages. Under federal court law, only direct purchasers can sue (this is commonly known as the rule of *Illinois Brick*). Defendants cannot argue that direct purchasers have “passed on” any amount of the overcharge to indirect purchasers (this is commonly known as the rule of *Hanover Shoe*). In thirty-six states and the District of Columbia, however, indirect purchasers can sue under state law providing that *Illinois Brick* does not apply to state court actions.

As a result, there is typically a morass of litigation in various state and federal courts relating to a single alleged conspiracy. Injured parties are treated differently depending on where they reside and defendants are subject to suit in multiple jurisdictions. In addition, federal *Illinois Brick/Hanover Shoe* policy provides a “windfall” to purchasers who have passed on an overcharge, while depriving any recovery at all to purchasers who actually bear the overcharge.

Such a system that compensates the uninjured and denies recovery to the injured seems fundamentally unfair. The Class Action Fairness Act may ameliorate some of the administrative issues caused by conflicting federal and state rules by facilitating the removal of state actions to a single federal court for pre-trial proceedings. However, that Act applies only to pre-trial proceedings and does nothing to address the fairness issues associated with current federal policy. The Commission believes it is time to enact comprehensive legislation reforming the law in this area.

The Commission recommends that Congress overrule the Supreme Court’s decisions in *Illinois Brick* and *Hanover Shoe* to the extent necessary to allow both direct and indirect purchasers to recover for their injuries. Other aspects of the Commission’s recommendations are designed to ensure that damages would not exceed the overcharges (trebled) paid by direct purchasers, that the full adjudication of such claims occur in a single federal forum, and that current class action standards would continue to apply to the certification of direct purchasers regardless of differences in the degree to which overcharges may have been passed on to indirect purchasers.

CRIMINAL PENALTIES

There is a strong consensus worldwide favoring vigorous enforcement against cartels. Cartels offer no benefit to society and invariably harm consumers. Sentencing and fines under the Sherman Act are generally determined by the courts based on guidance in the Sentencing Guidelines issued by the U.S. Sentencing Commission. The Sentencing Guidelines employ a proxy of harm from cartels based on twenty percent of the volume of commerce affected. This twenty percent proxy is based on an assumed average overcharge of ten percent, which is doubled to account for dead-weight loss to society. The Commission recommends that the

Sentencing Commission evaluate whether it remains reasonable to assume an overcharge of ten percent (*i.e.*, whether it should be higher or lower) and the difficulty of proving actual gain or loss in lieu of using a proxy. It also recommends that the Sentencing Guidelines be amended to make explicit that the twenty percent proxy may be rebutted by proof by a preponderance of evidence that the actual amount of overcharge was higher or lower where the difference is material.

INTERNATIONAL ANTITRUST

The United States was once the only major country actively enforcing a comprehensive set of antitrust laws. Today, more than 100 countries have adopted competition laws. On the one hand, this development has helped the United States in its fight to stamp out international cartels. It has also benefited world trade by opening up markets to competition. On the other hand, the proliferation of competition authorities has increased the risk of burden, inconsistency, and even conflict. There is some concern about the potential effect on U.S.-based companies of differences in the way that other countries treat so-called dominant firm behavior and the exploitation of rights in intellectual property.

The Commission recommends a number of steps to address these concerns. First, “as a matter of priority” the DOJ and FTC should study and report to Congress on the possibility of developing a centralized international pre-merger notification system that would ease the burden of companies engaged in cross-border transactions. Second, the DOJ and FTC should seek procedural and substantive convergence around the world on sound principles of competition law. Third, the United States should pursue bilateral and multilateral cooperation agreements with more of its trading partners. These agreements should explicitly recognize that conflicting antitrust enforcement can impede global trade, investment, and consumer welfare. They should also promote comity by providing for the exercise of deference where appropriate, the harmonization of remedies, consultation and cooperation, and benchmarking reviews. Fourth, the DOJ and FTC should be provided with direct budgetary authority to provide antitrust technical assistance to other countries for the purpose of enhancing convergence and cooperation.

Cooperation from other countries can be essential to punishing international cartels that exact hundreds of millions of dollars from U.S. consumers. But the United States has had limited success in entering Antitrust Mutual Assistance Agreements (AMAAs) with other countries. Many believe this is because U.S. law appears to require that those nations agree to allow the United States to use confidential information obtained under such agreements for non-antitrust enforcement purposes. The Commission recommends that Congress amend the International Antitrust Enforcement Assistance Act to clarify that it does not require such a commitment as the cost of entering into an AMAA.

Finally, the Commission recommends that, as a general principle, purchases made outside the United States from sellers outside the United States should not give rise to a cause of action in U.S. courts. The Commission was split as to whether this principle should be codified through amendment to the Foreign Trade Antitrust Improvements Act.

IMMUNITIES AND EXEMPTIONS

Free-market competition is the foundation of our economy, and the antitrust laws stand as a bulwark to protect free-market competition. Nevertheless, we have identified thirty statutory immunities from the antitrust laws. The Commission is skeptical about the value and basis for many, if not most or all, of these immunities. Many are vestiges of earlier antitrust enforcement policies that were deemed to be insufficiently sensitive to the benefits of certain types of conduct. Others are fairly characterized as special interest legislation that sacrifices general consumer welfare for the benefit of a few. Congress is currently considering the repeal of several immunities, including those covering the business of insurance and international shipping conferences. The Commission strongly encourages such review.

The Commission believes that statutory immunity from the antitrust laws should be disfavored. Immunities should rarely (if ever) be granted and then only on the basis of compelling evidence that either (1) competition cannot achieve important societal goals that trump consumer welfare, or (2) a market failure clearly requires government regulation in place of competition. The Commission recommends a framework for such a review and recommends that Congress consult with the DOJ and FTC about the likely competitive effects of existing and proposed immunities. In those rare instances in which Congress does grant an immunity, the Commission recommends (1) that it be as limited in scope as possible to accomplish the intended objective, (2) that it include a sunset provision pursuant to which the immunity would terminate at the end of a specified period unless renewed, and (3) that the FTC, in consultation with the DOJ, report to Congress on the effects of the immunity before any vote on renewal.

The judicial state action doctrine immunizes private action undertaken pursuant to a clearly articulated state policy deliberately intended to displace competition. In addition, the state must provide sufficient “active supervision” to ensure that conduct is truly a manifestation of state policy rather than private interests. A recent report by the FTC staff raises concern that courts have been applying the doctrine without sufficient care to ensure that private anticompetitive conduct has actually been authorized by the state pursuant to a clear policy to displace competition. The Commission agrees that courts should adhere more closely to Supreme Court state action precedents. It recommends that the doctrine should *not* apply where the effects of conduct are not predominantly intrastate. In addition, the doctrine should equally apply to governmental entities when they act as participants in the marketplace.

REGULATED INDUSTRIES

During the early part of the 20th century, several industries—including electricity, natural gas, telecommunications, and transportation—were thought to be natural monopolies or at risk of “excessive competition.” Since then, however, technological advancement and changed economic precepts have led to substantial deregulation. The unleashing of competition in these industries has greatly increased efficiency and provided substantial benefits to consumers. The Commission believes the trend toward deregulation should continue.