

## Unit 9

# **Antitrust and Information Policy**

# Anti Trust Laws and Policy

- Statutes developed by the U.S. Government to protect consumers from predatory business practices by ensuring that fair competition exists in an open-market economy
- Also referred to as "competition laws"
- Since the government's rules inevitably affect industry participants, no executive in the network economy can afford to be ignorant of government information policy

# Policy overview

- We have developed three major themes in this book, each of which raises questions for government policy
  - **Differentiation of products and prices**
  - **Lock-in**
  - **Positive feedback**

- **Differentiation of products and prices.**
  - The high first-copy costs of information and information technology inevitably lead to price and product differentiation.
  - Strategies involving mass customization, differential pricing, personalized content, and versioning are natural outcomes in such industries.
  - However, these strategies raise antitrust issues about fair competition.
    - Is it discriminatory to charge different users different prices for essentially the same product?

- **Lock-in**

- Since information products work together in systems, switching any single product can be very costly to users. The lock-in that results from such switching costs confers a huge competitive advantage on firms that know how to take advantage of it.
- This leads to concerns about the nature of competition.
  - What tactics are counted as "fair" and "unfair" competition with lock-in?
  - Will you be branded an aftermarket “monopolist” under antitrust law if you are the sole supplier to some locked-in customers?
  - If you are such a "monopolist," how will your strategic choices be limited?

- **Positive feedback.**

- Winner-take-all competition and standards battles are common as rivals fight for temporary market control.
- If you agree to cooperate with your rivals to establish standards, you run the risk of violating laws against cartels.
- Alternatively, if you compete and win, you may be guilty of monopolization, depending on the tactics you employed to gain or keep control over the market.
- Even if you avoid antitrust entanglements, you may have to deal with regulatory agencies.

# Price differentiation

- Robinson - Patman Act of 1936 says
  - Price discrimination is illegal if it "effectively lessens competition,"
- Many antitrust cases have been brought on these grounds.
  - For example, a group of pharmaceutical drug manufacturers has been facing a massive antitrust action the past several years in part because they each set drug prices lower for hospitals and HMOs than for retail drug stores.
- There are three primary legal arguments that render the vast majority of price differentiation immune from successful legal challenge:
  - You are allowed to set lower prices that result from lower costs.
  - You are allowed to set differential prices to meet the competition.
  - Differential pricing is only questionable if it "lessens competition."

# Price differentiation

- Differential pricing itself should not be taken as primary evidence of anticompetitive behavior
- Price discrimination for information goods is often positively beneficial to groups receiving discounts
- Price discrimination may be a necessary strategy to recover costs
- Differential pricing allows the producer to sell to markets that otherwise would not be served
  - If film producers had to set one price for first-run movies in all countries, only the high-income countries could afford to go to the movies



# Competition policy

- The Sherman Act (1890) makes it illegal to "monopolize" a market.
- The Clayton Act (1914) prevents mergers likely to "substantially lessen competition."
- FCC regulations refer to the "public interest."

- The underlying principle guiding antitrust law is the protection of competition as a *process*.
- Congress's judgment in passing the Sherman Act in 1890 was that this competitive process would ultimately be best to spur economic growth and protect consumers' interests.

- But how does the government and legal system respond when our cherished free market economy spawns a powerful monopolist?
  - First, the government can sit back and do nothing
  - Second, the government can attack the monopoly as illegally obtained
  - Third, the government can directly regulate the monopoly. This is the approach that has been taken for decades to the local telephone business as well as other utilities such as electricity

# *Implications for Strategy*

- unpleasant surprises that firms operating in information technology businesses commonly face:
  - 1. Virtually any acquisition or merger will be reviewed by the antitrust authorities. If you are joining forces with a rival, making your case will require careful planning, antitrust lawyers, and detailed economic analysis.
  - 2. Antitrust sensitivities are raised whenever you meet and talk with your rivals—for example, for standard-setting purposes.
  - 3. You may be accused of being a monopolist, especially if some of your consumers are locked in.
    - To defend yourself, you will need to establish either that you lack genuine and lasting monopoly power or that your conduct was legitimately competitive, not exclusionary or predatory.

# ***Mergers and Joint Ventures***

- Mergers and joint ventures that "may substantially lessen competition" are illegal
- Mergers involving direct rivals are typically subjected to antitrust review by the Justice Department
- There is no antitrust immunity for software mergers
  - Threat of high consumer switching costs and the intellectual property rights of incumbents
  - Adobe/Aldus in graphics software, Microsoft/Intuit in personal financial software

# ***Cooperative Standard Setting***

- The public policy concern is that participants will use the opportunity of meeting to stifle competition.
- Federal antitrust authorities must ask themselves: is this a standard-setting process, or is it a cartel?
- The antitrust authorities and the courts are likely to look with disfavor on negotiations that go beyond an agreement on product standards
- But once the rules of play have been established, you have to go out onto the field of play and compete vigorously and independently.

# ***Single-Firm Conduct***

- Hard to distinguish the firm that successfully competes, and thus gains a very large market share, from the firm that somehow crosses the line and gains a monopoly using tactics that are unfair, inefficient, or harmful to consumers, and thus illegal.
- *A monopolist who insists* that its customers not deal with its competitors is in for some tough questions

- *Tying is another suspect practice: a monopolist who insists* that customers take another product if they want the monopolized
  - Was it tying when Ford decided to put radios in its cars, thus posing a grave threat to the independent companies that had previously sold radios for installation into Ford cars?



- We can say no more, except to question whether these disputes are best handled in the courtroom with a lay jury or through some more sophisticated forum for dispute resolution.

# End of Unit 9