**Protecting Markets and Consumers in a High-Tech World**

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## I. INTRODUCTION

Thank you. I am delighted to be with you in New York today.

Last September, shortly after I joined the FTC, the agency celebrated its 90th anniversary, having been established pursuant to the FTC Act in 1914. In that year, the United States manufactured almost twice as many horse-drawn vehicles as cars; less than a quarter of all U.S. households had electricity; and only 1 in 10 Americans had a telephone. The first transcontinental phone call was still a year away, and when it was made, it cost $20.70 for the first three minutes (that is nearly $371 in today's money).

Today, this same agency is confronting many of the cutting edge issues affecting the software and other high-tech industries that – if they could have been imagined – would have been the stuff of science fiction when the FTC was created.

Although the agency has had its missteps in the past – like drafting rules prohibiting the use of the term "waterproof" because at some depth even a nuclear submarine will spring a leak, or rules prohibiting the use of the term "automatic" for sewing machines because you could not just turn them on and let them sew – in the main, the reviews at our anniversary seminar were good, even from United States Court of Appeals Judge Richard Posner, who 30 years ago all but

called for the agency's abolition. In sum, although clearly not perfect by any means, the message I heard on the occasion of its anniversary is that the agency is doing a strong job of ensuring that America's model marketplace runs freely, fairly and truthfully to serve American consumers.

The FTC is charged with promoting competition and consumer welfare and enforcing our nation's antitrust and consumer protection laws. Each of its dual missions brings discipline and strength to the other.

A mission that focuses entirely on promoting healthy competition, to the exclusion of consumer protection, can ensure a free market, but perhaps not one that functions as efficiently or robustly as it should. Consumers are less likely to venture into the high tech marketplace if they mistrust the marketing messages they receive, or if they are concerned about their privacy, the integrity of their computer operating systems, or the content of the e-mails their children will be receiving.

To the same degree, a mission that focuses entirely on consumer protection almost inevitably loses sight of the immutable fact that a free, competitive market will best serve the interests of the greatest numbers of consumers. Thus, for example, although consumer concerns about their privacy are real and need to be addressed, a fix for these concerns that hobbles the ability of companies to collect and use information to provide enhanced services to consumers is counterproductive from the standpoint of improving overall consumer welfare. A total ban on the use of "cookies," for example, could inconvenience millions of internet users with little positive benefit.

The FTC functions at its highest level when we have symmetry between our two missions. When the antitrust side was looking at competition in the automobile manufacturing

industry, the consumer protection side was looking at how to encourage greater disclosure of information about defects in cars. When competition advocates were looking at how to break down regulatory barriers to interstate lending, the consumer protection side was looking at how to more meaningfully disclose credit terms to spur greater competition in the marketplace. More recently, as the debate about peer-to-peer file sharing has reached a fever pitch, the FTC convened a public forum to air issues relating to P2P's current or potential impact on competition and consumers.

Today, I will briefly discuss how we are approaching issues that are important to your industry in both the competition and consumer protection programs.

## II. ANTITRUST

### A. Overview

Not surprisingly, antitrust enforcement in technology markets is a large and significant part of the Commission's competition work. (We do, of course, share civil antitrust jurisdiction with the Antitrust Division of the Department of Justice, dividing investigations according to expertise in the product market through a process known in the trade as the "clearance process.") Our antitrust work includes reviewing mergers, evaluating potentially anticompetitive business conduct, engaging in competition policy research and development, and advocating for competition in the courts, in federal and state agencies, in Congress and in state legislatures, and around the world.

#### Standards of Antitrust Analysis

There is no doubt that today's high-tech companies produce products and services that are vastly different than those produced by more traditional "brick and mortar" firms. The mere

speed with which new products and services are introduced, gain acceptance, and then perhaps are overtaken by new offerings can make capturing a market snapshot a genuine challenge. But while enforcing the antitrust laws in these new markets presents new challenges, most of the fundamental principles of antitrust law and economics that we have applied for years are equally relevant to even the newest industries. Because our analysis, done properly, is highly fact-intensive, the unique qualities of any product market can be accounted for. Thus, unlike some commentators heard in the past few years, I do not believe we need to entirely re-write the antitrust laws for the twenty-first century.

Whether we are looking at supermarkets or semiconductors, the Commission applies a consistent analytical framework for antitrust enforcement. This framework is grounded in microeconomics, and guided by the policy goal of preventing conduct that substantially reduces competition and, by extension, consumer welfare.

During the past few years, of course, merger activity has been relatively slow. Although you know better than I, it appears that merger activity finally is on the upswing, as high-profile mergers are being announced and Hart-Scott-Rodino ("HSR") filings have increased so far in this fiscal year. In fact, we received 55 new merger filings just last week. When we review mergers, we ask whether the deal is likely to reduce competition in a way that likely will lead to price increases or reduced output. The review is highly fact-intensive. We gather detailed information from the parties under investigation, as well as from their customers, their competitors, and other market participants. Quite often, we collect substantial amounts of empirical data, which is then subject to economic and statistical analyses. The legal and economic standards we use to evaluate the facts are well-known. Our analysis accounts for the effects of consolidating the

assets of the merging parties and the likely reaction, if any, of other competitors to the merger, including any enhanced ability for firms to coordinate prices and output. The analysis also considers whether new competitors are likely to enter the relevant markets, and if so, when and to what degree. And, of course, we consider the likely efficiencies that the merger will produce.

The consistent refrain from the business community is that the merger review process takes too long and imposes too many burdens. I agree that we can do better – and so can the private sector. If we are not sufficiently disciplined and rigorous in collecting and dissecting information during the merger review process, then we are not spending the taxpayer's dollar appropriately. Similarly, if firms are not appropriately cooperative and responsive during this process, then they are wasting the shareholder's dollar. In each instance, consumers lose. Accordingly, one of my most important objectives for 2005 is to determine what has and has not worked in merger review and implement measures for improvement. One specific focus will be the production of electronic documents.

I must emphasize that I firmly believe that merger process reform must be a two-way street. For example, for the FTC staff to more effectively limit their requests for information, they must have confidence that the parties will fully cooperate in responding to those narrowed requests.

In business conduct investigations, we seek to separate anticompetitive conduct from aggressive competition, often no simple task. Fundamental to our free market system is the assurance that competitors are permitted, indeed, encouraged, to compete fiercely on the merits. In a recent speech, a European head of state made the following perplexing statement: "[L]et us favor competition. Not wild competition, which destabilizes whole fields and endangers

economic sectors, but rather regulated competition, to give more purchasing and economic power to consumers."[1] His statement contains a false premise: that consumers generally will be better off if competition is tamed through regulation. In the crucible of the marketplace, companies may succeed by beating their competitors in price or quality, and perhaps even driving them out of business. In most instances, such market results are and should be perfectly legal. We focus on protecting competition, not competitors. It is only when firms seek to "stack the deck," by taking actions outside the realm of competition on the merits, that the antitrust laws must be invoked. "Free" market does not mean free of responsibility.

Of course, software is not soybeans. And it is vitally important for sound antitrust enforcement in the technology markets that, in applying our fact-intensive approach, we recognize and account for the characteristics of high-tech industries. I will briefly mention three challenging characteristics that often are present in high-tech sectors. First, in many technology markets, there is often no easily classified "product" in the traditional sense of the word. Instead, the consumer is often buying functionality or services, not a particular physical item that is easily identifiable, such as a car or a washing machine. (Of course, a car provides functionality as well, but there are more easily observed limits to what can economically substitute for a car.) Thus, determining which emerging technology services compete or will likely soon compete with the services offered by the parties under investigation is a potentially challenging task.

A second challenge presented by high-tech markets is that they often are characterized by

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[1] Allocution de Monsieur Jacques Chirac, President of France, Jan. 4, 2005, *available at* http://www.elysee.fr/magazine/actualite/sommaire.php?doc=/documents/discours/2005/05VXFV.html.

more rapid and less predictable change than traditional sectors of the economy. Consequently, we take care to determine whether any impact on competition produced by a merger of (or conduct by) high-tech companies is merely a brief transitory blip or more sustained competitive harm. Markets are usually self-correcting. In some technology markets, a market may correct itself in a shorter period of time than is required to prosecute an antitrust case.

Finally, as you know, technology markets often are characterized by what economists call "network effects." Network effects are produced when one person's use of a product or service increases the value to another person of using the same product or service. At an early point in time, there may be several different technologies that can (or have the potential to) provide a particular functionality at comparable prices – *e.g.*, VHS and Betamax. If one of those technologies, however, becomes an industry standard, and if there are considerable costs to adoption and to after-the-fact switching, the provider of the chosen technology may obtain substantial after-the-fact market power – especially if the licensees failed to anticipate that result and negotiate a price before the adoption. Determining whether or not the provider of the technology did anything other than compete to acquire such market power requires careful analysis. Because the acceptance of a single standard may spawn efficiency benefits for consumers, we must tread cautiously before condemning the provider of the "winning" standards technology.

### B. Examples Of The FTC's Recent Antitrust Work In High-Tech Markets

Clearly, an ever increasing percentage of the value of U.S. companies is comprised of various forms of IP and human capital, rather than hard assets, and the FTC's recent work reflects that shift. You may know that in December, the Commission resolved its challenge to

AspenTech's acquisition of the Hyprotech software assets, just weeks before the scheduled start of an administrative trial.[2] The consent order resolving the matter requires AspenTech to divest the intellectual property rights to the Hyprotech products, and the Commission has approved Honeywell's acquisition of these rights.[3] Under the order, AspenTech is permitted to license back the rights to these products so that it too can remain a viable competitor. (The consent order also requires Aspentech to divest its integrated engineering software business to Bentley Systems.)[4] The Commission's handling of the AspenTech matter is an excellent example of how a detailed fact-intensive investigation led to a highly-tailored solution that will preserve competition in an important software market.

An illustrative, ongoing, non-merger case is the *Rambus* matter, which also puts the focus on intellectual property rights, rather than hard assets. The staff's Complaint in *Rambus* alleged that Rambus had engaged in unlawful exclusionary conduct by failing to disclose to a standard-

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[2] Decision and Order, *Aspen Technology Inc.*, Docket No. 9310 (Dec. 20, 2004), *available at* http://www.ftc.gov/os/adjpro/d9310/041221do.pdf.

[3] Letter from Donald S. Clark, Secretary, Federal Trade Commission to George S. Cary (Dec. 20, 2004), *available at* http://www.ftc.gov/os/adjpro/d9310/041221ltr.pdf.

[4] To ensure restoration of pre-merger competition levels, however, the order goes beyond simply requiring divestitures. With respect to the process engineering software assets purchased by Honeywell, the order also requires AspenTech to, among other requirements: (1) divest a related operator training business; (2) allow current customers to void their current contracts; and (3) support the assets divested to Honeywell for two years. In addition, for five years, AspenTech must provide Bentley with updates, upgrades, and new releases of AspenTech's engineering and other products on terms as favorable to those provided to other persons. The consent order further directs AspenTech to provide both Honeywell and Bentley with lists of relevant employees, remove impediments deterring current AspenTech employees from switching to either buyer, and, for two years, refrain from soliciting any former AspenTech employees who choose to work for the buyers. Decision and Order, *Aspen Technology Inc.*, Docket No. 9310 (Dec. 20, 2004), *available at* http://www.ftc.gov/os/adjpro/d9310/041221do.pdf.

setting organization in which it participated that it had obtained "blocking" patents with respect to a computer memory standard under evaluation by the organization. After a two-month trial, the Administrative Law Judge agreed with *Rambus* and held that the staff had not proven the case.[5] The matter is now before the full Commission for decision.

To complement our work on individual matters, the Commission, together with the Antitrust Division, has devoted substantial resources to learning more about how intellectual property rights impact competition. In October 2003, the FTC issued a 300-page report on patents and competition, entitled "To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy."[6] It was based on over twenty-four days of hearings, with more than 300 stakeholder panelists and roughly 100 written submissions.

The hearings confirmed that patents play different roles, and thus may pose different competitive issues, in different industries. Pharmaceutical companies reported that patents were indispensable to protect the enormous financial investments required by innovation toward drug products containing new chemical entities. Similarly, biotech companies spoke about the crucial importance of patents in attracting venture capital to fund the extremely costly, high-risk R&D that biotech involves. Computer hardware and software and Internet companies highlighted the special issues that arise in industries characterized by incremental, cumulative innovation and by products requiring a great many, separately held patents. Panelists described thickets of overlapping patents through which firms must maneuver to achieve product commercialization.

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[5] Initial Decision, *In the Matter of Rambus Inc.*., Docket No. 9302 (Feb. 23, 2004), *available at* http://www.ftc.gov/os/adjpro/d9302/040223initialdecision.pdf.

[6] *To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy* (Oct. 2003), *available at* http://www.ftc.gov/os/2003/10/innovationrpt.pdf.

They noted the increase in defensive patenting – that is, developing many patents of your own, not necessarily to protect your product innovations, but rather to keep as trading chips to use when other companies demand that you license their patents to avoid alleged infringement.

The FTC proposed ten recommendations to improve patent quality. In particular, we recommended the use of administrative post-grant review of patents and the imposition of certain limits to liability for willful infringement, as well as adequate funding for the PTO – a recommendation on which everyone agreed.

In April 2004, the FTC continued its intellectual property focus when it co-sponsored a conference on patent reform with the National Academies' Board on Science, Technology, and Economic Policy (STEP), and with the Berkeley Center for Law and Technology. The debate and discussion begun there will continue at four patent reform meetings that the FTC is co-sponsoring with the NAS STEP Board and the American Intellectual Property Law Association (AIPLA). Sessions in a town meeting format, with much of the time set aside for audience participation, will be held in San Jose (February 18), Chicago (March 4), and Boston (March 18), with a final meeting in Washington, D.C. (June 9). We hope that the many businesses that would be affected by patent reforms will send representatives, so that we can hear from all of those who have a stake in patent reform.

In all of this, our aim is to add our voice and to stimulate dialogue. In that vein, please do not hesitate to bring me your views, your concerns, and your questions about what we can do to better protect competition and promote innovation.

## III. CONSUMER PROTECTION

### A. Introduction to Consumer Protection

On the consumer protection side, as on the competition side, no single approach will effectively and efficiently solve the problems posed by new technologies. The rapid development of new technology has created enormous benefits for consumers. It has changed the way we communicate and redefined how we collect, use, and store information. But in some cases, the tremendous benefits of new technology have also created risks for consumers.

To protect consumers, we use a three-pronged strategy that incorporates aggressive law enforcement, consumer and business education, and research. Balancing this strategy with sound competition policy is bringing us closer to the appropriate solutions to the problems without hindering competition or impeding the development of new technology. In the rapidly changing high-tech environment, however, industry is generally better positioned to develop solutions to respond to consumer demand than government. I will talk briefly about three related issues: spam, spyware, and information security.

### B. Spam

Spam, a topic highlighted today on page 1 of the *New York Times*,[7] is one of the most intractable consumer protection problems that the Commission – like you and computer users – has ever faced. The extremely low cost of sending email makes it an appealing marketing channel even for legitimate companies. Unfortunately, low cost combines with anonymity, making spam an ideal vehicle for con artists as well. Indeed, a 2003 staff survey revealed that

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[7] Tom Zeller, Jr., *Law Barring Junk E-Mail Allows a Flood*, N.Y. TIMES, Feb. 1, 2005, at A1.

two-thirds of spam in our sample contained facial indications of falsity.[8] I do not have to tell you about the significant costs spam imposes on consumers and businesses; indeed, many of you have helped educate us on these issues.

We are devoting significant resources to aggressive law enforcement against spammers. Since 1997, the Commission has been ferreting out fraudulent offers sent via spam, and more recently, spam messages that violate the CAN-SPAM Act. To date, we have filed 66 spam-related cases against 192 individuals and companies. The number of consumers who received spam from these malefactors is mind-boggling. We continue to receive 300,000 new spam messages per day in our spam database (known as our refrigerator), and, together with our law enforcement partners, we will use this information to go after more spammers. The biggest problem we face is tracing the spammers.

We cannot solve the problem with new laws and law enforcement alone. First, we must educate consumers and businesses, not just in the United States, but around the world, about how to protect themselves and others from unwanted spam. The campaign against "phishing" is a prime example of a problem that is best addressed by consumer education. Identifying individual "phishers" is extremely difficult; but if consumers know not to provide financial information through email in response to a pop-up solicitation or email inquiry, they themselves can effectively stop this criminal activity.

Second, this is also a technological problem, and it requires a technological solution. The FTC, of course, cannot develop the technological solutions to mitigate the problem. But we are

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[8] *See False Claims in Spam* staff report, available at www.ftc.gov/opa/2003/04/spamrpt.htm (April 2003).

working to encourage and facilitate private market innovations. Last November, the Commission convened an Email Authentication Summit, cosponsored by the National Institute of Standards at the Commerce Department.[9] The Summit enabled the Commission to gather a wide spectrum of interested parties, capable of finding a solution to the problem of email anonymity, with the goal of invigorating the search for and agreement on an authentication standard.

I implore the industry to quickly put aside differences and work diligently in developing a compatible authentication standard that will provide accountability for email communication. The stakes are high, and all involved have an interest in ensuring the continuing viability of email communications.

### C. Spyware

Just when we were getting a good start on addressing spam, spyware popped up. The term spyware may be amorphous, but there is no doubt that its negative impact is real. It is hard to find any computer user who has not struggled for hours to remove spyware from his computer.

Like spam, much harmful spyware is distributed illegally. We filed our first spyware case in October 2004,[10] and more are in the pipeline. In that law enforcement action, we challenged spyware that changed consumers' home pages, changed their search engines, and triggered a barrage of pop-up ads. According to our complaint, the spyware also installed additional software, including spyware that can track a consumer's computer use. As a result of the

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[9] *See* www.ftc.gov/bcp/workshops/e-authentication/index.htm.

[10] *FTC v. Seismic Entertainment Productions, Inc.*, Civil No. 04-377 (D. N.H. filed October 6, 2004), available at *available at* www.ftc.gov/opa/2004/10/spyware.htm.

spyware and other software the defendants installed, many computers malfunctioned, slowed down, or crashed, causing consumers to lose data stored on their computers. Then, after having created these serious problems for consumers, the defendants offer to sell them a solution – for $30. We charged that these practices were unfair and violated the FTC Act. A district court has granted our request for a preliminary injunction. While these cases are difficult to develop, we are giving them top priority, and we welcome technological assistance in developing them.

We are educating consumers about spyware and anti-spyware tools, as well. We have issued a Consumer Alert specifically on spyware, as well as four additional Alerts addressing other online security issues such as viruses.[11] The media quote from these often, and are driving traffic to our website. We logged more than 150,000 hits to these publications last fiscal year.

And, last spring, we sponsored a public workshop on spyware to explore what it is, how it is distributed, and how much harm it causes.[12] We used that information to start developing cases, and equally important, to start the discussion of what technology is or may be available to protect consumers. Here again, we believe a critical role for government is to encourage technological solutions to help reduce spyware problems. We will shortly issue a report on the spyware workshop.

The market has begun responding to consumer concerns. The anti-spyware tools and technologies that AOL, Earthlink and other ISPs are providing to their subscribers are

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[11] The consumer alerts are available at www.ftc.gov/bcp/conline/pubs/alerts/spywarealrt.htm; www.ftc.gov/bcp/conline/pubs/alerts/idsalrt.htm; www.ftc.gov/bcp/conline/pubs/buspubs/secureyourserver.htm; and www.ftc.gov/bcp/conline/pubs/buspubs/security.htm.

[12] *See* www.ftc.gov/bcp/workshops/spyware/index.htm.

encouraging. We encourage industry to give priority to developing easy-to-use technology to ensure that consumers maintain control over their own computers.

### D. Information Security

Finally, the FTC has given priority to protecting consumers' privacy, and nothing today is more fundamental to privacy than information security. We have brought a series of cases challenging allegedly false security claims. In each of the cases, we charged that the companies promised that they would take reasonable steps to protect sensitive information obtained from consumers, but failed to do so.[13] With an estimated 9 million cases of identity theft last year, quite frankly, it is alarming to see, in two of the FTC's enforcement actions, allegations of websites with unencrypted credit card information or without defenses to even the most basic hacker attack. We also are bringing cases against companies that have failed to comply with the security requirements of the Gramm Leach Bliley Act.[14]

We have promoted information security through a practical and plain language consumer and business education campaign, which includes outreach through the FTC's website, through speeches, "news you can use" alerts, and participation in joint initiatives with other government agencies and private groups.[15] Many of you have heard first-hand the passion that my colleague, Commissioner Orson Swindle, has brought to the issue of improving information security both here and abroad.

We have conducted research and surveys, and held workshops to educate ourselves and

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[13] *See* www.ftc.gov/privacy/privacyinitiatives/promises_enf.html.

[14] *See* www.ftc.gov/opa/2004/11/ns.htm.

[15] *See* www.ftc.gov/bcp/conline/edcams/infosecurity/index.html.

the public about emerging issues in the privacy and security arena. In 2003, for example, we held a two-session workshop, "Technologies for Protecting Personal Information: The Consumer and Business Experiences," to examine the challenges and possible technological solutions to protecting consumers' personal information.[16] What emerged from the workshop was a basic agreement that privacy solutions depend on four critical elements working in sync: people, policies, process, and technology.[17]

Time and again, we are told that if protective technology is to be effective for consumers, it has to be easy. And it should be comprehensive. Although from a policy development standpoint, we discuss online security as discrete topics – viruses, spam and spyware -- consumers do not. Many consumers will not adequately protect their computers if they have to shop around for separate security products, read complex user manuals, and even change the default settings to their systems. They just want to be able to surf and use the Internet safely. Now, one can argue that consumers should be taking greater responsibility for their own computer safety. But I would think that the important point for you is not whether they should; it is whether they actually will, if securing themselves is not made easy. Given that we all have a tremendous stake in the security of – and consumer confidence in – the online world, it seems that making that world safer should be a priority for all stakeholders.

For our part, we are taking a big-picture look at how we communicate with consumers about online security, privacy, and fraud. Since the beginning of January, we have conducted

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[16] *See* www.ftc.gov/privacy/privacyinitiatives/promises_wkshp.html.

[17] *See Staff Workshop Report: Technologies for Protecting Personal Information*, available at www.ftc.gov/bcp/workshops/technology/finalreport.pdf.

about three dozen interviews with representatives of trade associations, consumer advocates, other federal agencies, and corporations – including several of your member companies – to get a sense of what messages and tactics are most effective for reaching consumers. What we have learned has confirmed that consumer education is a key part of the solution. We heard time and again that we need to keep it simple. In the coming weeks, we are going to develop a plan for the next phase of our consumer education program on online issues. I hope that you will find the themes, strategies, and outreach tools that we develop to be useful in your own consumer outreach activities. We certainly would like to continue working with you.

## IV. CONCLUSION

Thank you again for the opportunity to speak to you today about the FTC's competition and consumer protection work in high-tech markets.