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How To Measure Success: Agency Design and the FTC at 100

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I. Introduction

Good morning. Thank you to Howard Feller and the ABA for inviting me to participate in the Fall Forum, and to David Wales and Jamillia Ferris for organizing one of the Section's signature annual events. I am delighted to be here. With the Federal Trade Commission's one hundredth birthday upon us, I would like to spend a few minutes this morning discussing the unique role the agency plays in promoting competition and to emphasize how the agency's unique design contributes to its success.

These are issues I have spent many years thinking about – from my early days advising Commissioner Swindle to my time working on the FTC at 100 Report[2] as Director of the Office of Policy Planning under Bill Kovacic to the many months during which I reflected on how I would approach being a Commissioner between my nomination and confirmation by the Senate.

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[1] The views expressed in these remarks are my own and do not necessarily reflect the views of the Federal Trade Commission or any other Commissioner. I am grateful to my advisor, Alexander Okuliar, for his invaluable assistance in preparing this speech.

[2] WILLIAM E. KOVACIC, CHAIRMAN, FED. TRADE COMM'N, THE FEDERAL TRADE COMMISSION AT 100: INTO OUR SECOND CENTURY, THE CONTINUING PURSUIT OF BETTER PRACTICES (Jan. 2009), *available at* http://www ftc.gov/reports/federal-trade-commission-100-our-second-century-continuing-pursuit-better-practices-report.

But, this year in particular, I have had good cause to again reflect seriously on what we do at the FTC, our institutional strengths, and how to successfully leverage those strengths for the good of consumers and the country in the century ahead. My remarks this morning include only my opinions and are not meant to reflect the views of the Commission or any other Commissioner – although I bet they would agree that the agency is a paradigm of success.

II. What is Success?

But, how should we define success? In a recent article, former Chairman Bill Kovacic and Professor David Hyman identify the three most important factors to predict the long-term success of agency design: consistent political support, policy coherence, and the capacity and capability to handle the agency's mission.[3] Let's take a look at each of these for a minute and see how the FTC measures up.

a. Political Support

As a threshold matter, an agency needs consistent political support, or, as Kovacic and Hyman call it, "political implications." They note that this is the most important of the factors for success. In their words, "An agency is doomed if it lacks a supportive constituency, or if the performance of its duties generates crippling political opposition. More broadly, an agency will not be able to operate effectively if its structure raises serious doubts about its legitimacy or increases the vulnerability to political pressure that the performance of its duties will arouse."[4]

This first factor speaks directly to the FTC's origins and the stability of its structure as a bipartisan entity. The FTC was born from early twentieth century dissatisfaction with the way the

[3] David A. Hyman & William E. Kovacic, *Why Who Does What Matters: Governmental Design, Agency Performance, the CFPB, and PPACA*, GW Legal Studies, Research Paper No. 2014-2, at 36 (Jan. 6, 2014).

[4] *Id.*

Department of Justice was enforcing – or, really, not enforcing – the Sherman Act.[5] As many of you know, in the Gilded Age years preceding the FTC's creation, the country underwent a massive wave of corporate consolidation.[6] In the decade straddling the turn of the twentieth century there were 42 deals producing companies controlling over 70 percent of their respective industries.[7] During the peak of this merger boom, from 1898 to 1902, at least 303 companies disappeared each year and in 1899, over 1208 were merged out of existence.[8] For several years, the government offered essentially no meaningful response.

The leadership at DOJ was not entirely to blame for this situation. It was a product of many factors, including the underdeveloped understanding about the economic implications of corporate consolidations, political indifference (or worse), and a Supreme Court that had expressly called into question whether the Sherman Act applied to mergers. Many of you may recall from law school the Supreme Court's 1895 decision in *United States v. E.C. Knight Co.*[9] The Court rejected the government's attempt to stop the sugar trust from buying four Pennsylvania plants, even though it would give the trust a 98 percent share of the national market.[10] The Court read the Commerce clause to exclude transactions from federal law, because they impact commerce "only incidentally and not directly."[11] In addition, since the trust was mainly a manufacturer, the Court noted that, "Commerce succeeds to manufacture, and is not part

[5] David A. Hyman & William E. Kovacic, *Institutional Design, Agency Life Cycle, and the Goals of Competition Law*, 81 Fordham L. Rev. 2163, 2167 (2013).

[6] Marc Winerman, *The Origins of the FTC: Concentration, Cooperation, Control, and Competition*, 71 ANTITRUST L. J. 1, 17 (2003).

[7] *Id.* at 7.

[8] *Id* at 6.

[9] *United States v. E.C. Knight Co.*, 156 U.S. 1 (1895).

[10] Winerman, *The Origins of the FTC, supra* note 6 at 8.

[11] *Id.*

of it."[12] Hence, you can see my point about a relatively unsophisticated view of law, economics, and antitrust in that era. These years of unchecked consolidation and competitive excesses triggered an era of public agitation that aided President Roosevelt in expanding the antitrust laws, pushing to establish the Sherman Act's coverage of consolidations, and culminated more than a decade later with Wilson's signing of the FTC Act and Clayton Act.

But this turn-of-the-century consensus for additional competition enforcement was not reflected in a uniform vision for a new competition agency. Rather, two camps formed. The first believed Congress should create a new agency to be a law enforcer similar to the DOJ, but politically independent and with flexible substantive jurisdiction to allow it to proactively shape business behavior. The second camp, on the other hand, wanted to move away from the DOJ model and create an independent policy body, similar to Roosevelt's new Bureau of Corporations within the Department of Commerce and Labor.[13] This policy agency would have special power to work with the business community, research competition issues, and then issue reports, regulations, and guidelines that would help shape industry's conduct. [14]

The FTC was created as a compromise between these polarized views – we are an independent, bipartisan, policy-oriented, research-based, enforcement agency. The bipartisan design insulates us to some extent from being buffeted by political winds. Combining this bipartisan leadership with the agency's research and policy functions results in relatively steady and disciplined stewardship of our merger review mandate and conduct enforcement, which other than some notable missteps about thirty years ago, has often been a source of broad political support over the last few decades. I assume that this support is at least in part because even the

[12] *Id.*

[13] Hyman & Kovacic, *Institutional Design*, *supra* note 5, at 2167.

[14] *Id.*

out-of-power party continues to have a serious voice in U.S. competition policy and enforcement decisions.

b. Policy Coherence

This leads me to the next most important factor for agency success – policy coherence – something that Kovacic and Hyman note is similar to identifying, "[i]n economic terms, [whether] the [agency's] functions [are] complements or substitutes[.]"[15] They further observe, "Synergies and efficiencies are more likely to result if there are commonalities among the functions…."[16] Again, the FTC's design offers strong policy coherence because of its dual mandate for competition and consumer protection. These are different, but equally-important complementary tools for the agency to help promote fairness in our markets and thereby promote consumer welfare.[17] Each tool protects consumers in different ways, and each has its limitations, allowing one to offer relief where the other cannot.

Competition is the first line of defense – a competitive market is a welfare-enhancing one for consumers. Aggressive competitors fight for consumers using price and quality as their weapons, including the quality of service. They work hard to protect their reputations because they know that a dissatisfied customer can easily turn to alternatives. But there are limits to this – as former FTC Chairman Tim Muris once wryly observed, "the commercial thief loses no sleep over its standing in the community."[18] Some companies engage in fraud, dishonesty, unilateral breach of contract, or other conduct that hurts consumers, with little regard for their reputations or the possibility of being put out of business. Because a competitive market sometimes cannot

[15] Hyman & Kovacic, *Why Who Does What Matters*, *supra* note 3, at 21.

[16] *Id.*

[17] Timothy J. Muris, *The Interface of Competition and Consumer Protection*, Fordham Corporate Law Institute's Twenty-Ninth Annual Conference on International Antitrust Law and Policy (Oct. 31, 2002).

[18] *Id.* at 4.

discipline these behaviors, we also use our consumer protection authority.[19] But these missions are aligned, which allows the agency to apply them cohesively and imbues all Commission Staff with a sense of common purpose – to protect consumers.

c. Capacity and Capability

So, we come to the third most important factor, agency capacity and capability. Capacity refers to resources, which in large part hinges on an agency's credibility with Congress. Capability, according to Kovacic and Hyman, is slightly different, turning on "whether an agency has the tools to make good decisions, and does so."[20] Over the years, I have read arguments challenging the FTC's capability to make good decisions on competition matters. These arguments usually turn to historical FTC losses in appellate courts as examples of our failure. I will focus the remaining few minutes of my remarks explaining why, based on our design protocol, the agency is doing exactly what it was meant to do – identifying competition problems in the economy, developing proof of the problems, debating the evidence of harm and proper course internally, and then leading by example outside the agency with every advocacy, enforcement, and regulatory tool at its disposal. And contrary to what you may be hearing, our efforts do pay off, just not always right away. But that's sometimes the risk of leading.

III. Intellectual Leadership Is the True Measure of Agency Success

The agency's design gives it the singular ability to identify a potential competition problem in the market, develop empirical research to determine whether the problem actually exists, and then plan and execute a multi-year advocacy and enforcement agenda to rectify the problem – in other words, the FTC is designed specifically to lead others in the continuous development of competition law to accurately reflect changing economic conditions. It is in the

[19] *See* Timothy J. Muris, *Principles for A Successful Competition Agency*, 72 U. CHI. L. REV. 165, 173-76 (Winter 2005).

[20] Hyman & Kovacic, *Why Who Does What Matters*, *supra* note 3, at 27.

agency's DNA, so to speak, from the open-ended drafting of our statutory authority over "unfair methods of competition" in Section 5 of the FTC Act to our research and report-writing in Section 6 of the Act, which permits us to "gather and compile information" and make public "such portions … as are in the public interest."[21] The Commissioners sometimes disagree about how the agency should pursue its mandate – for instance, I have said we should set out guidance for application of our standalone Section 5 authority, whereas others prefer a different path forward – but that debate, too, and the necessary negotiation and compromise that come with a Commission structure is another invaluable part of our Commission design. It is among the reasons studies have shown that the agency's merger enforcement does not wax and wane with the election cycles in Washington, D.C.[22]

Over the years the FTC has made vital contributions in doctrinal grey areas. On the merger side, the agency has most notably introduced new concepts or new ways of analyzing hospital mergers, potential competition issues, and dynamic markets. On the conduct side, the FTC has been at the forefront of developing invitations to collude, patent ambush in standard setting as a form of monopolization, the proper extent of competitor collaborations in cases like *Polygram*, and, of course, reverse payment settlement agreements. The agency also has had a major impact on developing the outer bounds of antitrust, particularly with respect to the scope of exemptions and immunities like *Noerr*, the filed-rate doctrine, and state action. For example, in

[21] 15 U.S.C. § 46(a), (f) (2005).

[22] *See, e.g.*, Malcolm B. Coate, *Bush, Clinton, Bush: Twenty Years of Merger Enforcement at the Federal Trade Commission* 24 (Working Paper Sept. 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1314924 (noting "Little evidence can be found to suggest that the enforcement regime changed in response to … political control …").

the past 29 years the FTC is the only antitrust agency that has appeared before the Supreme Court as a party, and our six cases in that period demonstrate our impact on doctrinal developments.[23]

Importantly, most of our doctrinal contributions have depended on broad use of all our agency functions – research, advocacy, administrative litigation, and federal court enforcement – and several have first been met with failure in the courts – sometimes repeated failure – before realizing wider success. Two examples include our efforts revitalizing hospital merger enforcement and pursuing reverse payment settlements. I will say a few words about each.

a. Hospital Merger Enforcement

In 2002, on the heels of an eight-year period in which the FTC and Justice Department had lost seven consecutive hospital merger challenges, former FTC Chairman Timothy Muris announced a hospital merger retrospective project. The goals of the retrospective were to study consummated hospital mergers to determine whether any of them had resulted in higher prices and to update the agency's prior assumptions about the nature of health care competition. This project, and other subsequent work, helped show empirically that hospital consolidation could indeed lead to higher prices and lower-quality care. It also led to the application of new thinking, like two-stage competition and willingness-to-pay models, that allowed the FTC to step up its enforcement program.

The hospital retrospective that we then applied in the *Evanston* administrative litigation and subsequent cases, deserves a lot of credit for not only our recent Supreme Court victory in *Phoebe Putney* but also several other favorable decisions in our hospital merger challenges, including federal court victories in cases like *St. Luke's* and *ProMedica* and abandoned mergers in

[23] *See F.T.C. v. Indiana Federation of Dentists*, 476 U.S. 447 (1986); *F.T.C. v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990); *F.T.C. v. Ticor Title Ins. Co.*, 504 U.S. 621 (1992); *California Dental Ass'n v. F.T.C.*, 526 U.S. 756 (1999); *F.T.C. v. Phoebe Putney Health System, Inc.*, 133 S.Ct. 1003 (2013); *F.T.C. v. Actavis, Inc.*, 133 S.Ct. 1522 (2013).

many other matters. This work is critical to protecting an area of the economy that is known for its high costs and its tremendous personal significance to all consumers.

b. Reverse Payment Settlements

Another similar example is the FTC's work in the pharmaceutical space. In 1984, Congress struck an important balance in passing the Hatch-Waxman Act. The Act facilitates competition by lower-priced generic drugs, while maintaining incentives for pharmaceutical companies to invest in developing new drugs. In so doing, it resolved several problems with the drug approval process that existed before it was passed. But, as we now know, the Act also created incentives for branded drug makers to file and then settle patent infringement claims by offering large reverse payments to generic drug makers to keep them out of the market.

In response to the concerns about reverse payment settlements, the agency began to research and challenge them in the late 1990s. In 2001, OMB approved a Commission study of generic drug entry that was published in 2002.[24] With this new body of evidence about the effects of generic drug competition, and with additional studies over the years, the FTC pursued reverse payment settlements nationally, with investigations, lawsuits, and advocacy as an amicus in existing private litigation. And, we lost. Over and over again. From the beginning of our work in this area until just last year, the overwhelming trend in federal courts was to find these agreements, or many of them anyway, lawful because they fell within the scope of the branded drug owners' patent. That is until, of course, the Third Circuit in *K-Dur* rejected the Eleven Circuit's scope-of-the-patent approach and held that pay-for-delay settlements were presumptively anticompetitive.[25]

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[24] FED. TRADE COMM'N, *Generic Drug Entry Prior to Patent Expiration: An FTC Study* (July 2002), *available at* http://www ftc.gov/sites/default/files/documents/reports/generic-drug-entry-prior-patent-expiration-ftc-study/genericdrugstudy_0.pdf.

[25] *See In re K-Dur Antitrust Litigation*, 686 F.3d 197 (3d Cir. 2012).

The Supreme Court granted certiorari in our case against *Actavis* for its drug Androgel to resolve the conflict between the circuit courts. The rest, as they say, is history. The Court decided *Actavis* in June 2013, rejecting both the Eleventh and the Third Circuits' approaches in favor of a rule of reason analysis. In essence, the Supreme Court agreed with the FTC that pay-for-delay agreements can harm consumers and violate the antitrust laws.

IV. Chief Justice Edward Douglass White and the Rule of Reason

I want to close with a story that was wonderfully recounted by Bill Kolasky as part of his Trustbuster series in Antitrust Magazine and that I think about when I hear claims that the FTC is incapable of making good competition law decisions because of its win/loss record in court. It is the story of Chief Justice Edward Douglass White and his work to introduce the rule of reason into the Sherman Act.[26] Justice White was appointed to the Court in 1894.[27] A few years later, the Court encountered its second antitrust case, *Trans-Missouri Freight Association*,[28] in which the United States sued to stop a railroad association from jointly setting rates. The majority, in its analysis, adopted a literal reading of the Sherman Act and condemned the association activity.[29]

Justice Peckham, writing for the Court, reasoned that when the "plain and ordinary" language of a statute "pronounces as illegal every contract or combination in restraint of trade or commerce . . . all contracts are included in such language, and no exception or limitation can be added without placing in the act that which has been omitted by Congress."[30]

Justice White exposed this remarkably constricted logic, explaining it contradicted "the plain intention" of the Sherman Act "to protect the liberty of contract and the freedom of trade"

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[26] William Kolasky, *Chief Justice Edward Douglass White and the Birth of the Rule of Reason*, 24 ANTITRUST 7, Summer 2010.

[27] *Id.* at 78.

[28] *United States v. Trans-Missouri Freight Assoc.* 166 U.S. 290 (1897).

[29] *Id.* at 328.

[30] *Id.*

and ignored the common law handling of the term, "restraint of trade" under a reasonableness standard.[31] He argued, "If the rule of reason no longer determines the right of the individual to contract . . . what becomes of the liberty of the citizen or of the freedom of trade?"[32]

Despite the obvious failings of the majority approach, Justice White would not be fully vindicated for fourteen years, when, as *Chief* Justice, he authored the Court's landmark 1911 opinions in *Standard Oil*[33] and *American Tobacco*[34] and set out in detail the rule of reason test we still use today. The moral of the story is, of course, that leadership requires risking failure, as well as vision not always available to everyone.

V. Conclusion

I leave you with a few closing thoughts on success and agency design. First, a leading competition agency like the FTC must have the courage to fail from time to time. Second, the FTC is well-suited to this leadership role in large part because of its design, which has played a significant role in its contributions to difficult competition issues. It has afforded the agency bipartisan political support, a coherent policy framework to protect consumers with complementary tools, and the capacity and capability to invest in resolving novel competition issues with long-range plans relying on outreach, research, advocacy, and enforcement. And, finally, the real key to successful agency design, in my opinion, is the ability to attract and retain great people. Judging by the people I have met in my years at the FTC, we are a runaway success. I hope everyone enjoys the Fall Forum and is able to make it to the special FTC at 100 dinner tonight. Thank you very much.

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[31] *Id.* at 355 (White, J., dissenting); *Kolasky*, *supra* note 26, at 78.

[32] *Trans-Missouri,* 166 U.S. at 355.

[33] *Standard Oil Co. v. United States*, 221 U.S. 1 (1911).

[34] *United States v. Am. Tobacco Co.*, 221 U.S. 106 (1911).