Behavioral Lessons for Antitrust Enforcement

Avishalom Tor
Notre Dame Law School, atortest@nd.edu

Follow this and additional works at: https://scholarship.law.nd.edu/law_faculty_lectures

Part of the Antitrust and Trade Regulation Commons, and the Business Organizations Law Commons

Recommended Citation
Tor, Avishalom, "Behavioral Lessons for Antitrust Enforcement" (2020). Faculty Lectures and Presentations. 61.
https://scholarship.law.nd.edu/law_faculty_lectures/61

This Lecture is brought to you for free and open access by the Faculty Scholarship at NDLScholarship. It has been accepted for inclusion in Faculty Lectures and Presentations by an authorized administrator of NDLScholarship. For more information, please contact lawdr@nd.edu.
Behavioral Lessons for Antitrust Enforcement

Avishalom Tor

Presentation to the DOJ Antitrust Division
June 4, 2020
OVERVIEW

+ Definition and basics
+ Reality check
+ Implications for doctrine / enforcement
+ Why antitrust?

Electronic copy available at: https://ssrn.com/abstract=3681958
DEFINITION

The application of empirical behavioral findings to antitrust law and policy

+ Examining the antitrust implications of recognizing the bounded rationality of real consumers, business managers, regulators, and courts

Electronic copy available at: https://ssrn.com/abstract=3681958
THE BASICS: RATIONALITY ASSUMPTIONS

Antitrust law aims to protect competition among rational suppliers to satisfy the demands of rational consumers

+ Familiar with respect to suppliers (e.g., Matsushita, Brooke Group), which are assumed to be rational profit-maximizers
+ While the basic consumer building block is only occasionally noted (e.g. Brown University), with little consideration of the significance of its rationality assumption for antitrust

Electronic copy available at: https://ssrn.com/abstract=3681958
THE BASICS: RATIONAL CONSUMERS

The standard approach assumes a great deal about consumers…

+ Rational consumer beliefs
+ Rational consumer preferences
THE BASICS: RATIONAL BELIEFS

+ No systematic biases/errors of judgment
  + No biased estimates of product quality
  + No mistaken judgments of absolute or relative prices
  + No erroneous predictions of one’s own future needs / preferences (demand)
THE BASICS: RATIONAL CHOICE

+ **Consistent choice behavior**
  + Complete and orderly preferences
  + Standard axioms of rational choice
    + *E.g.*, Transitivity, Dominance, Regularity (IIA)
  + Implied assumptions of rational choice
    + Description invariance
    + Procedure invariance
    + Context independence

Electronic copy available at: https://ssrn.com/abstract=3681958
THE BASICS: REAL CONSUMERS…

“Did we remember to get that thing we came here for?”
THE BASICS: BOUNDED RATIONALITY (BR)

+ Limited cognitive resources (Simon)
+ Judgment and decision making under uncertainty
  + Reliance on heuristics, environmental cues
+ Impact of motivation and emotion
+ Social preferences

Systematic, predictable deviations from (hypothetical) perfect rationality
THE BASICS: BR CONSUMERS

+ Systematic consumer bias
+ Constructed consumer choice

+ Particularly in the presence of sophisticated sellers that exploit consumers’ bounded rationality
  + Behavioral Industrial Organization

Electronic copy available at: https://ssrn.com/abstract=3681958
Firms designed to maximize profits, but…

+ Human managers—*agency problems*
+ Limits of *incentives* and motivation
+ *Expertise* helps, to a degree
+ Intrafirm *selection* beyond pure competence
  + Commitment, *overconfidence*
+ “Organizational repairs” for routine tasks only
+ Board monitoring/guidance
  + Small group limits; managerial influence
In typical antitrust settings:

+ *Competitive discipline* obviously constrained…
  - And can reward some BR when operates (e.g., entry)
+ *Arbitrage* often impractical
+ Identifying errors and *learning* from them is difficult

Hence, firms better approximate rationality, but only imperfectly
QUESTIONS SO FAR?
REALITY CHECK:

A MORE REALISTIC ASSESSMENT AND PREDICTION OF MARKET BEHAVIOR
REALITY CHECK:
HORIZONTAL RESTRAINTS

+ The real world is “sticky”
  + Established patterns of market behavior more stable than standard models predict
    + Norms, status quo bias/loss aversion, etc.
    + Managerial incentives

+ Suboptimal collaboration (e.g., information sharing) among rival oligopolists

+ Higher likelihood and stability of cartels in some market settings
  + Much evidence from criminal enforcement

Electronic copy available at: https://ssrn.com/abstract=3681958
REALITY CHECK: MARKET POWER

+ Not always fully exploited
  + Reputation with consumers, social norms

+ Somewhat “sticky” market shares
  + Particularly in consumer goods
  + Efficacy of rebates, loyalty programs etc.

+ Boundedly rational entry
  + Higher rates of entry than assumed
  + But very low success rate, limited mobility
  + Limited short term impact on established incumbents
  + But important long term source of innovation
REALITY CHECK:
MONOPOLIZATION

+ Seemingly irrational predation (e.g., recoupment unlikely) can be rational in fact
  + Investment in predatory reputation with asymmetric information
+ Boundedly rational predation possible in certain circumstances
  + Competition over market share / relative position
  + Loss averse dominant firms losing market share

Electronic copy available at: https://ssrn.com/abstract=3681958
REALITY CHECK: VERTICAL RESTRAINTS

+ Interbrand: Tying, bundling
  + May offer somewhat more effective *foreclosure* in consumer markets due to consumer inertia (status quo bias etc.)

+ Intrabrand: Minimum RPM
  + Mfrs. tend to use excessively
    + Overestimate harms of price cutting, prefer to control retail prices, and more
  + To their own detriment and that of discount retailers
  + Consumer harm only if pervasive in market or mfr. has market power (limited substitutes)
REALITY CHECK: MERGERS

+ **Generally**
  + Many mergers fail to add value
    + Agency problems, managerial hubris
  + Efficiencies often overstated
    + Necessary to justify, desirability bias etc.
  + Accounting for boundedly rational entry

+ **Horizontal**
  + Coordinated effects may be underestimated
    + Cf. criminal collusion cases
QUESTIONS SO FAR?
IMPLICATIONS FOR DOCTRINE AND ENFORCEMENT POLICY
IMPLICATIONS: THE VALUE OF CASE-SPECIFIC EVIDENCE

+ Horizontal restraints
  + The *Matsushita* SJ threshold

+ Monopolization
  + Recoupment (*Brooke Group / Weyerhauser*)

+ Merger enforcement
  + Demand estimation—consumer surveys; simulations
  + Entry
    + Rapid entry
    + Future entry: sufficiency, actual history
  + Efficiencies skepticism

Electronic copy available at: https://ssrn.com/abstract=3681958
IMPLICATIONS: (REASONABLY) SIMPLE ANTITRUST RULES FOR A COMPLEX BEHAVIORAL WORLD

+ Structuring RPM’s ROR
  + Recognizing the prevalence of BR RPM besides traditional pro- and anti-competitive uses
  + Per se illegality/legality / unstructured ROR unjustified
  + *Leegin* factors matter (also for behavioral reasons)
    + Burden on P to show them or direct harm (output reduction)
    + D can rebut, showing RPM necessary to address harm / undermine P’s main case

Electronic copy available at: https://ssrn.com/abstract=3681958
IMPLICATIONS: SUMMARY

+ Greater concern for false negatives when courts / agencies rely on rationality assumptions to ignore factual evidence
+ Improving agency investigations / analysis
+ Tipping the scales in favor of one of the limited number of available rules
+ Helping refine structured inquiries under existing rules
QUESTIONS SO FAR?
WHY ANTITRUST?

Competition → ? → Efficiency Welfare

Electronic copy available at: https://ssrn.com/abstract=3681958
WHY ANTITRUST?

REHABILITATING ANTITRUST

1. Competition *still* *(mostly)* *performs*
2. More competition is *(usually)* *better than its alternatives*
WHY ANTITRUST?
COMPETITION (MOSTLY) PERFORMS (I)

+ Despite prevalent consumer bias
   + Some product markets still reasonably approximate standard model
   + *Heterogeneity in rationality* can reduce market effects of bias (when substantial minority approximates rationality)
   + Deviations diminished where *learning / incentives* to educate consumers exist

Electronic copy available at: https://ssrn.com/abstract=3681958
WHY ANTITRUST?

COMPETITION (MOSTLY) PERFORMS (II)

+ Substantial fraction of approximately-rational preferences remains
  + Within consumers
    + Some extant preferences
    + Many constructed “final” preferences depend on higher-order, more “authentic” preferences
  + Across consumers
    + Heterogeneity in rationality
+ Product-market characteristics
  + Repeat purchases
  + Complexity
WHY ANTITRUST?
COMPETITION (MOSTLY) BETTER

*Increased competition*

*versus what?*

*diminished competition*

(fewer firms w/more market power)

*or*

*more direct regulation*

*of consumer choice*
I. Identify market conditions that determine effects of competition
   - Some markets sufficiently approximate standard model
   - On occasion (more) regulation may perform better
   - Would greater MP sometimes outperform competition?

II. Relate above market conditions to policy
   - Inform antitrust rules / boundaries
     - *Tolerate dominance more* in some settings? (cf. natural monopoly)
     - Support *deference to market-specific regulation*?
     - Innovation and competition—*less deference to IP*?

FINAL WORDS: ANTITRUST AGENDA
THANK YOU!

FOR MORE IN-DEPTH ANALYSIS SEE MY AUTHOR PAGE

Electronic copy available at: https://ssrn.com/abstract=3681958