Syllabus: LAW 7221-001

Government Regulation of Business

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This course surveys the legal, economic and policy framework that governs American business. In doing so, it examines the core principles that guide our economy and, against the backdrop of the proposition that non-regulated markets are generally preferred, introduces a number of areas of regulation, including antitrust, securities, environmental, patents, advertising/information and consumer protection. We will critically examine the rationales (market failures of one kind or another, a desire on the part of those regulated to avoid the rigors of the marketplace, etc.), legal ground rules and regulatory models used in various areas of regulation. One objective will be to gain a good understanding of how government intervention has actually played out in selected markets. We will also examine markets that, though once regulated, have since been deregulated.

We will also have a lot of fun. One reason for that is that we will be examining many of the regulatory questions within the context of current “hot” issues—high energy prices, global warming, what to do about health-care services and costs, merger-mania, pending regulatory “reform” proposals, the financing of political campaigns, internet privacy, Wal-Mart’s threats and benefits, run-amuck litigation and the like. Because this is an election year, these topics will be the stuff of a constant stream of information/disinformation in the press, on TV and in campaign speeches that can inform (or at least stimulate) our class discussions.

Readings. Readings for this course will be distributed (Selected Materials), available through TWEN or accessible directly from internet links provided in this syllabus. In addition, there are two sources to which we will refer throughout the course. The first is the April, 2007 Report and Recommendations of the Antitrust Modernization Commission (hereafter, “AMC Report”) (see www.amc.gov/report_recommendation/amc_final_report.pdf). (Because I served as a Commissioner on the AMC, I have been able to secure a hard copy of the AMC Report for each student.) The second is Viscusi, Harrington and Vernon (“VHV”) (4th ed. 2005). (Copies of this and other books referred to in specific class sessions below will be placed on reserve in the law library.) It will also be useful to keep informed on relevant current regulatory issues by reading The Wall Street Journal, Business Week and the like. You will be expected to have read the assigned material before class.

One more thing about the readings. As you’ll see below, this is a “speaking” syllabus, with a brief “teaser” paragraph for each class session designed to stimulate student thinking in advance of class. For some class sessions, the reading list may appear intimidating at first blush. Don’t be intimidated. A lot of readings are just short newspaper articles. Many of the longer readings we will simply skim so that we can discuss certain concepts more profitably in class (with one or two students being assigned to read them and lead the discussion). At the end of each class session, I will provide an overview of upcoming readings to advise which should be skimmed, which should be read more carefully, who will have primary responsibility for certain readings, etc.

Office hours and contact information. Office hours will be each day from 1:30 to 2:30 pm or any time by appointment. My office is Room 410. My email is: dkempf@kempflaw.com. Office phone: 303-492-0119. Cell phone: 303-842-8466.
Class requirements and grading. The course will meet Monday through Friday from 9:00 am though 11:50 am in Room 306. Students are expected to attend all class sessions. Each student will write a paper (approximately ten to twenty pages) related to one of the matters the course will cover; it will count for 40% of the grade. (Students can select their own topic or choose one from a list of suggested possible topics that I will provide.) The final exam will count for 40% of the grade. Finally, class participation will count for 20% of the grade.

Section I. Introduction and overview.

Class #1 (May 12, 2008). The theory of economic regulation: Overview and basics. In its landmark Northern Pacific decision nearly half a century ago, the Supreme Court emphasized that the antitrust laws are bottomed “on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic, political and social institutions.” Sounds good. Yet large chunks of American commerce are not “unrestrained” but rather are regulated. What explains this? Is regulation necessitated by market failures? Are there certain “public goods” that require regulation? And are certain “market goods” such that we as a society are just plain better off if their distribution is determined by regulation rather than the free market? To help us answer these questions, we’ll review some of the basic analytical building blocks used in assessing regulatory issues. Legendary coach Vince Lombardi had his own unique way of emphasizing the importance of continuously re-mastering the basics as a critical first step to success in any endeavor. “Gentlemen,” he began the first practice session each year, “this is a football.” Similarly, Nobel Laureate in Economics George Stigler (in his equally colorful manner) said that consumers “invariably obey one law as universal as any in social life; they buy less of a thing when its price rises.” And its corollary: “people will not buy less, and usually will buy more, of a commodity when its price falls.” Thus, we’ll explore the basics of economic analysis—supply and demand, price theory, economies of scale, the law of diminishing returns, externalities, deadweight loss, public values, price discrimination and the like. We’ll focus in particular on markets. How do you go about identifying and defining “relevant” product and geographic markets anyway? And why is it important that we undertake this exercise? Do some markets behave differently from others? If so, why? Are some goods such that consumers are just not equipped to make sound decisions about them in an unregulated market (thus, necessitating regulation)? Readings:

1. Is “non-regulation” the greatest thing since sliced bread? Northern Pacific, Selected Materials, p. 1.
2. AMC Report, p. 441.

Section II. The Antitrust Laws.

Class #2 (May 13, 2008). Antitrust: Sherman Act Section 1. The theory is this: Rigorous competition produces the lowest prices, highest quality and best service. If one supplier is “the only game in town,” prices are apt to be higher, quality lower and service worse than if there are two or more competitors all striving to captures the consumer’s business. Competition also spurs
innovation. We want people striving “to build a better mousetrap”—one that is cheaper, one that costs the same but catches more mice or one that is both cheaper and catches more mice. In the auto business, vigorous competition among dealers is what leads to “Mr. Goodwrench,” “overnight loaners” and “the quickest turnaround time in town.” To secure better the benefits of competition, Congress passed the Sherman Act in 1890, making every contract, combination or conspiracy in restraint of trade illegal. But, hey, all contracts are in restraint of trade. That’s why we have contracts. The core objective of contracts—every last one of them—is to restrain trade. What gives?

Readings:

5. D. Kempf, The *per se* rule v. the rule of reason, *Selected Materials*, p. 15.

**Class #3 (May 14, 2008). Monopolization.** How does a company get to be a monopolist anyway? You could do a merger that creates a monopoly (or, as condemned by Section 7, a merger whose effect may be to “tend to create a monopoly”). But how to you recognize that a merger may end up creating a monopoly? Our gut tells us that, if there are only two widget manufactures and they merge, that might well create a monopoly and cause prices to go up. Our gut also tells us that, if there are 100 widget manufacturers (each with 1% of the widget market) and two of them merge, that would likely have no market impact and prices would likely remain the same after the merger as before. But what if there are ten widget makers and two of them merge? Or six widget makers and two of them merge? Or three widget makers and two of them merge? Potential monopoly problems? Another way to end up as a “monopolist,” of course, is to compete well—make the highest quality product efficiently and sell it, along with the very best service possible, at the lowest price. Customers will flock to you, and your market share will skyrocket. But as the great Judge Learned Hand emphasized more than 60 years ago, “the successful competitor, having been urged to compete, must not be turned upon when he wins.” Another way to become a monopolist might be to engage in so-called “predatory conduct”—(say) burning down your competitor’s factory or charging prices so low that your competitor can’t stay in business profitably. But, then again, aren’t low prices the central goal of the antitrust laws? Hello! Readings:

1. *United States v. Aluminum Company of America (Alcoa)*, 148 F.2d 416, 421-432 (2d Cir. 1945) (excepts only); read only those passages highlighted in yellow at [http://hubcap.clemson.edu/~sauerr/classes/425/cases/alcoa.pdf](http://hubcap.clemson.edu/~sauerr/classes/425/cases/alcoa.pdf).


**Class # 4 (May 15, 2008). Mergers.** If it is sound antitrust policy to prevent mergers that are anticompetitive, then isn’t it also sound antitrust policy to encourage mergers that are pro-competitive? One would think so. Still, Section 7 is often referred to as the “anti-merger law.” And mergers are routinely blamed by politicians and others for a wide assortment of economic and other ills—everything, it sometimes seems, save the common cold. Proposed legislation is almost always pending that aims to block all kinds of mergers—big ones, media- or petroleum-related ones, etc., etc., etc. Passions run strong in the merger area. Fear of the aggregation of “power,” concern over possible oligopolistic behavior, a desire to return to “a nation of shopkeepers,” you name it. What explains all this? And how the heck do you tell when a proposed merger really poses a threat to competition anyway? Another thing: on the way to addressing broader issues, merger law has lots of important “technical” issues. How do you decide what the relevant “line of commerce” and “section of the country”—the product and geographic markets—are? How do you handle a proposed merger involving a “failing company” that is going to disappear from the market under any circumstance. What about joint ventures? In analyzing mergers, do “efficiencies” count as a good thing or a bad thing? What are the “Merger Guidelines” and what role do/should they play in merger analysis? Readings:

1. VHV, pp. 203-09 (merger theory) and pp. 299-300 (the early days) (skim).


5. Simplified charts for use with the Merger Guidelines (*Selected Materials*, p. 30):
   a. Measuring market concentration/Herfindahl-Hirschman Index
   b. The 1968 DOJ Merger Guidelines.
   c. Professor Steven C. Salop (Georgetown and CRA) (1999).


7. The Whirlpool-Maytag merger:
   b. Market shares in key home appliance industry markets (as set forth in D. Moss, “Antitrust Analysis of Whirlpool’s Proposed Acquisition of Maytag,” Tables 1 and 2, pp. 4, 13 (January 17, 2006)), *Selected Materials*, p. 36.
8. The Whole Foods-Wild Oats merger:


Class # 5 (May 16, 2008). Antitrust revisited: (1) Exemptions and immunities. Nearly all politicians regularly sing the praises of the antitrust laws, call for stiffer penalties for their violation and urge that there be no exemptions or immunities from the antitrust laws. Yet those same politicians also regularly pass legislation granting all sorts of exemptions and immunities. Why? And when it comes to getting rid of exemptions and immunities, where a politician stands depends on where he sits. Will a Democrat from an industrial state vote for repeal of the labor exemption? Will a Republican from an agricultural state vote for repeal of food and dairy exemptions? And because it is thus a bipartisan issue/problem, almost no exemption ever gets repealed: “I’ll let you keep your exemption, if you’ll let me keep mine.” Congress is always willing to listen to special pleas from special interests who argue that the antitrust laws should not apply to them. Does this imply that we should also abolish the so-called *per se* rule and let courts do the same? After all, the test is: Is this an “unreasonable” restraint of trade? And what about various specific exemptions—labor, agriculture, insurance, baseball, petitioning the courts or legislatures, exports, state-action . . . and the list goes on. (2) Misuse of antitrust. Over the years, some have sought to use the antitrust laws as an instrument for lessening competition rather than for protecting and enhancing it. For judges (and others), it can be difficult at times to tell whether a particular course of conduct or proposed transaction is pro-competitive or anticompetitive. Congress too has enacted “special” antitrust laws that many view as at odds with the Sherman Act and aimed at thwarting competition rather than advancing it. In Europe these days, antitrust enforcers are increasingly attacking large companies for “abuse of dominance.” Are such challenges designed to protect competition or prevent it? Readings:

   a. 253 F.3d 34, 45-48, 50-59. 78 (“Course of Conduct”), 82-85, 95-97(DC Cir. 2001)

10. VHV, pp. 343-44, 350-52.

Section III. Regulation In Our Economy.

**Class # 6 (May 19, 2008). Patents.** The granting of patents (and all that follows from that) is one form of regulation that has always been a big deal in America. The first antitrust law wasn’t enacted until 1890. The Constitution, however, from the get-go, provided for the enactment of patent laws. There is, of course, a tension between the antitrust laws and the patent laws: the former condemn monopolies, while the latter grant them. Each set of laws has its advocates, and they argue about where the line should be drawn to balance the interests each set of laws serves. Should a patent holder, for example, be prohibited from seeking to “extend” his monopoly to non-patented products? By “bundling”? By “tying”? And do we need “reforms” of the patent laws to prevent people from gaining patents too easily for things that don’t really deserve to be patented? Are some patented items so important that there should be compulsory licensing of the patents for them? All these questions reflect the reality that patents raise a multitude of “public goods” issues. Readings:


**Class # 7 (May 20, 2008). Environment-related regulation.** Pollution control—whether involving automobiles, coal-fired power plants or factories—raises a host of challenging legal and regulatory issues. How do we best go about it? Do we want prescriptive-based regulation or incentive-based regulation? The carrot or the stick? Do we prohibit (or limit) emissions? Or auction off “rights” to pollute? Or what? And when do we act? Now, for the sake of future
generations? Or only after we’ve got rock-solid evidence that our particular concerns are well founded? Does the global warming debate ring a bell? Readings:

1. VHV, pp. 691-96, 703-05, 745-51, 757-60, 775-76, 785-86.
8. Global warming.
   a. An Inconvenient Truth: http://www.youtube.com/watch?v=TUiP6dqPynE (Trailer for movie.). (If there’s sufficient student interest (and I hope there is), we will schedule an evening to watch the full movie and have dinner afterwards.)
   d. Article, “Gore Slams Global Warming Critics” (June 20, 2006), Selected Materials, p. 186.

Class # 8 (May 21, 2008). (1) Advertising and information regulation. Effective advertising can impact markets. As David Ogilvy sums up in his wonderful book Ogilvy on Advertising (1983, p. 7), “I do not regard advertising as entertainment or an art form, but as a medium of information. When I write an advertisement, I don’t want you to tell me that you find it ‘creative.’ I want you to find it so interesting that you buy the product. When Aeschines spoke, they said, ‘How well he speaks.’ But when Demosthenes spoke, they said, ‘Let us march against Philip.’” But advertising is not without regulatory controversy and issues. Is it designed to inform or to persuade? (Or trick? Or create artificial demand?) Advertising regulation has been both limiting and proscriptive. Some advertising is banned; some is limited to certain media
only. Some is required to contain disclaimers—or even warnings. (Interestingly, in at least one area, in recent commercials, the warning has become part of the sales pitch.) Some consider regulations banning (or limiting) certain advertising as simply another example of price fixing.

(2) Regulation for consumer protection. “Consumer protection” efforts have had a mixed reception—as captured nicely in the title of a 2002 conference hosted by the Manhattan Institute, “Unfair Competition and Consumer Fraud Statutes: Recipe for Consumer Fraud Prevention or Fraud on the Consumer.” Still, some have been unqualified successes—the establishment of the FTC’s do-not-call registry, for example, which has been called “the greatest government program since the Elvis stamp.” The competing rights of privacy and free speech raise a host of constitutional and regulatory issues in the currently-hot area of internet privacy. And regulation with respect to the providing of financial support for political activities—so-called “campaign contribution reform” efforts—have always been greeted with legal challenges. Readings:

7. VHV, pp. 576-78.
   b. Online Interactive Forum, “Ask the White House” (interview with FTC Chairman Muris} (June 27, 2003), Selected Materials, p. 67.
10. The internet.
11. Political campaign finance reform.
   d. F. Schouten, “Maxed-out donors shift to state politics,” USA Today, p. 5A (November 13, 2007); Selected Materials, p. ??.
Early on, the Supreme Court held that certain formal markets (securities, commodities, etc.) involve unique characteristics that warrant special treatment under the antitrust laws. The Securities and Exchange Commission has general oversight for the securities of all issuers and particular regulatory supervisory authority over securities exchanges and securities firms. The principal theme of securities regulation has been disclosure. Recent corporate scandals have led to regulatory reforms in the securities arena—such as the passage of the Sarbanes-Oxley law—(with, among other things, new and expanded disclosure requirements). The SEC’s oversight of securities firms is supplemented by an extensive “self-regulation” regime—the NYSE, NASD and others. With securities firms now being subjected to actual, active direct regulation by the SEC, does the SRO scheme still make sense? High profile trials for alleged frauds on the public (Enron) or on the corporation (Tyco) have ensured that all these issues remain very much on the front-burner. The corporate scandals of the past several years have also led to demands for so-called “corporate governance” reforms. Readings:

1. United States v. Chicago Board of Trade, 246 U.S. 231 (1918).
4. Hedge Funds.
   b. AP, “Most sweeping changes since Great Depression,” MSNBC.com (March 30, 2008); Selected Materials, p. ??.
6. Corporate Governance.
   a. A. Murray, “Corporate Governance Concerns are Spreading, and Companies Should Take Head,” The Wall Street Journal (April 12, 2006), Selected Materials, p. 96.
Section IV. Regulatory Institutions.

Class #10 (May 23, 2008). Regulation by litigation (or the threat thereof). Litigation can be high stakes indeed. In the antitrust field, in addition to suits by the DOJ or FTC, private plaintiffs can bring cases as so-called “private attorneys general.” Not only that, but, if they win, they can recover treble damages and attorney’s fees. Often antitrust and securities private lawsuits are brought as class actions. In some areas of the law, the corporation may also face exposure to punitive damages. Potential class-action, treble damage or punitive damage exposure in such cases can run into the billions of dollars. And in our “federalism” system, it is possible that firms might face the prospect of both federal actions and state actions. In some industries, an adverse court finding (or governmental administrative ruling) can result in the loss of the company’s license to do business. And does a firm really want to go to war with a regulator that has continuing oversight over all (or most) aspects of its business? No wonder many such situations are referred to as “bet-the-company” cases. One outgrowth of all this is that litigation settlements can achieve “regulatory reform” that might not have been able to have been accomplished through the regulatory processes itself. Readings:

2. AP story, “Spitzer files suit against AIG, former CEO” (May 26, 2005), Selected Materials, p. 120.
6. AMC Report, pp. 251-56, 400 (first paragraph only), 417-19 (contribution and carve-out).
7. The Milberg Weiss Indictments.
   a. DOJ Press Release, “Milberg Weiss law firm, two senior partners, indicted in secret kick-back scheme involving named plaintiffs in class-action lawsuits” (May 18, 2006); Selected Materials, p. 131.
   f. D. Kempf, “The new class representatives: Wise and helpful heroes or foolish and harmful dupes?” (2008) (discussion draft only); Selected Materials, p. ??.
g. DOJ Press Release, “Melvyn Weiss, co-founder of Milberg Weiss law firm, agrees to plead guilty to federal racketeering charge,” (March 20, 2008); Selected Materials, p. ??.

Class # 11 (May 27, 2008). Regulation v. deregulation: (1) Regulation: we can do it better. Ronald Reagan often said that “the nine most terrifying words in the English language are ‘I’m from the government and I’m here to help.’” Yet government is the original and enduring growth industry. Indeed, it even remained so during Reagan’s presidency. Thus, in politics, reducing the size of government has come to mean increasing the size of government, but reducing the rate of increase in the size of government. Similarly, reducing the deficit has come to mean increasing the deficit, but reducing the rate of increase in the deficit. Over the years (and continuing to today), economists have published a great deal on whether to regulate and, if so how. (2) Deregulation: trust the markets. Sometimes a consensus is reached that a market that is regulated isn’t working all that well and that it should be deregulated. Many factors can contribute to reaching of this consensus, including a sense that the regulating body has effectively been “captured” by those being regulated. In Europe, many countries have taken industries that were both owned and operated by the government (the ultimate form of government regulation) and “privatized” them. (In the former communist countries, much of the economy has gone through this process.) In the United States, perhaps the poster child for deregulation has been the airlines industry. Interestingly, while we generally associate deregulation with Republicans, it was three Democrats who were most instrumental in bringing about airline deregulation—Sen. Ted Kennedy, Professor Alfred Kahn and a then-young Senate staffer named Stephen Breyer. How has it worked out? There are far fewer airlines today; does that mean there’s been a “lessening” of competition? And those that have survived seem to go in and out of bankruptcy proceedings on a regular basis. And what do we learn from the new entrants—Southwest, Jet Blue, etc.? One interesting experience with deregulation is the situation where an industry operates at several levels and only one level is deregulated. This has happened in the energy field. We end up with markets that are part regulated and part not regulated. What follows? Readings:

1. Regulation.
   a. VHV, pp. 375-92 (skim).
   c. AMC Report, pp. 357-63.
I. The mortgage/housing “crisis.”
   iii. R. Thaler and C. Sunstein, “The psychology of the housing mess,” USA Today, April 24, 2008); Selected Materials, p. ??.

2. Deregulation.
   a. Airlines.
   c. Energy.

Section V. Regulation and the Future.

**Class #12 (May 28, 2008).** Health-care regulation. The issue today is whether there should be universal, government-provided (or government-supported/mandated/regulated) health care. We already have pretty extensive—and expensive—government health-care programs—Medicare and Medicaid. Not too long ago, of course, we had no such programs at all. None. How on earth did we survive? As we listen to the debate on this subject this fall and beyond into the next Congressional session, things to focus on include the coverage (universal v. poor-only; all ills v.
selective ills, etc.), the cost (who gets what; who pays for what) and is-there-a-better-way-to-do-this (including: perhaps-we-shouldn't-do-“this”-at-all). The poster-child for the unfortunate who have no medical insurance coverage is always the unfortunate person who recently lost a job. As it turns out, however, many of those in this category are healthy young Yuppies who’ve simply decided they’d rather use the money on monthly payments on a Ferrari than on monthly payments on medical insurance they don’t need or want. What do we do with them? Readings:

1. The SCHIP debate.

2. Political positions.

3. The Massachusetts experience.

Class # 13 (May 29, 2008). (1) Globalization and Its Critics: Of NAFTA and the like. Ross Perot came back from the sidelines during the debate over Congressional ratification of the NAFTA treaty to coin a memorable phrase about “the giant sucking sound” that would be heard if NAFTA was ratified. As he saw it, jobs in America would be lost in the wake of the passage of NAFTA as work was “sucked” out of the United States and transplanted to foreign countries. How do international trade disputes get addressed and resolved? WTO? NAFTA panels? And what, if anything, do we do about “global warming”? Especially, elsewhere throughout the world? And how do we go about doing whatever it is we decide should be done? And where? What do we learn (or make use of) from the Kyoto Protocols? (2) Wal-Mart. Is Wal-Mart the greatest things since sliced bread? Or the worst thing since the plague? Economic regulation often involves a struggle between the head and the heart. Everyone prefers the warmth and friendliness of the Ma-and-Pa corner grocery store to the coldness and piped-in Muzak at the supermarket. Or at least they say they do. But they vote with their feet. So the Ma-and-Pas are vanishing and the supermarkets are growing like weeds. Lately, some have sought to address this issue via regulation. Wal-Mart decided it would like to enter the banking business. Because banking is extensively regulated, Wal-Mart would have had to go through a lengthy and contentious approval process. As you might expect, many came forward to urge the regulators not to let Wal-Mart into banking. It got pretty ugly; finally, Wal-Mart just gave up. Others have sought to restrain Wal-Mart’s growth through legislation. Some communities, for example, have passed laws effectively banning Wal-Mart from opening a store there—by (say) prohibiting store-size from exceeding 75,000 square feet. And Maryland passed a law requiring Wal-Mart to allocate a certain percentage of its profits to health care benefits for its employees. Great humanitarian legislation or thinly disguised effort to keep Wal-Mart from doing business in the state? Readings:

1. International.
   a. T. Friedman, The World is Flat (Farrar, Straus and Giroux 2005); see the summary list of what Friedman identifies as “the ten forces that flattened the
world,” Selected Materials, p. 171. (skim pp. 3-47, 225-236 so that we can discuss Friedman’s “ten forces”)
c. International trade disputes.
d. AMC Report, pp. 213-16.
e. VHV, pp. 769-71.

2. Wal-Mart.
c. Legislative Efforts to keep Wal-Mart out of certain areas.
d. Wal-Mart’s efforts to go into banking.
e. The attack on Wal-Mart’s labor practices.