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AEI-BROOKINGS JOINT CENTER FOR REGULATORY STUDIES

**Comment on the Federal Trade Commission's  
Strategic Plan for 2003-2008**

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## **Executive Summary**

This comment assesses some important economic consequences of the Federal Trade Commission's approach to strategic planning. We recommend that the FTC evaluate cases based on their impact on consumer benefits, and that the FTC develop a formal "Investigation Impact Statement" for each case to better manage resource allocation within the agency.

## Comment on the Federal Trade Commission's Strategic Plan for 2003-2008

Robert W. Hahn, Robert E. Litan, and Roger G. Noll

We are submitting this comment for the Federal Trade Commission (FTC) in response to the publication of the *Federal Trade Commission Strategic Plan: Fiscal Years 2003-2008*.

Although our organizations are not listed as among the “stakeholders” for this comment, as scholarly research institutions that engage in extensive research on antitrust and economic policy analysis, we have a strong interest in promoting efficient enforcement of antitrust laws and the development of useful performance measures for antitrust enforcement agencies. The American Enterprise Institute-Brookings Joint Center for Regulatory Studies is a research center that is devoted to improving the efficiency of regulatory policy and, in particular, working with government agencies to improve the use of cost-benefit analysis and other economics research tools in regulatory policy. The Stanford Institute for Economic Policy Research undertakes research on economic policy, including antitrust.

Our comments are directed at the section of the *Preliminary Strategic Plan* that deals with performance measures, especially pages 12-15. We strongly endorse the goal of the Commission “to focus our investigative resources on those activities most likely to harm consumers” (p. 12). We also agree with two very important statements in the report that ought to constitute the guideline for developing performance measures. First, pertaining to mergers, “enforcement saves consumers money by preventing price increases that likely would have occurred due to the loss of competition had the merger gone forward unchallenged” (p. 13). Second, pertaining to other enforcement activities, “enforcement similarly benefits consumers by stopping anticompetitive activity that raises prices or otherwise restricts competition” (p. 14).

As implied by these statements, the best measure of the benefits arising from enforcement activity is the improvement in the welfare of consumers, or the expected increase in “consumers’ surplus,” that is caused by enforcement. FTC enforcement activities increase consumers’ surplus by reducing prices and/or increasing product quality and variety.

The *Preliminary Strategic Plan* proposes to measure the direct benefits of enforcement by determining the “amount of commerce involved in the markets in which the agency takes an enforcement action” (p. 13). The indirect benefits from deterrence will be measured “by multiplying the indirectly affected volume of commerce by one-third in most cases” (p. 15).

While we are sympathetic to the view that accurately measuring the consumer benefits from enforcement actions is difficult and “can be subject to many variables,” (p. 13) we nevertheless believe that replacing a good-faith, well-documented attempt to measure consumer benefits with an arbitrary number is a mistake. Clearly the magnitude of commerce in the market is a vast overstatement of the stakes for consumers in an enforcement action. But the main problem with this measure is that it creates an incentive structure among the Commission’s staff that could seriously distort the case selection process in favor of investigations of relatively minor actions by companies in very large markets. Moreover, this approach gives investigators an incentive to devote excessive resources to cases involving a company in a large market for the purpose of obtaining a consent agreement, however minor, so that the magnitude of business in that market will be chalked up as a “benefit” of the investigation. Facing costly and time-consuming litigation over a minor issue, companies will be likely to settle such cases even if the questioned practice is benign. Thus, the use of this measure could lead to misleading assessments of the efficiency of the FTC’s priorities and resource allocation among potential cases.

We recommend that the FTC continue to seek to evaluate cases on the basis of their impact on consumer benefits. To do so requires estimating the magnitude of the price and other effects of a merger or other anticompetitive practice. While such estimates are bound to contain errors, the appropriate method for dealing with this problem is to describe in detail the assumptions and methods that were used to generate these estimates, and to make the estimation procedures publicly available for comment and peer review. Indeed, without such estimates the FTC cannot effectively establish case priorities and allocate its enforcement resources. Moreover, by producing a historical record of the estimated effects of enforcement action, the FTC will create useful information to compliment its ongoing process of retrospective reviews of the effects of past actions.

We also recommend that the FTC develop a formal "Investigation Impact Statement" (IIS) to be completed at the point at which a case is terminated. This statement would contain the information about consumer impact (the expected direct and indirect effect on consumers' surplus), the cost of the investigation to the FTC and to the respondents, and the outcome of the case. The last item would focus on (1) what was learned by the investigation and (2) any changes in market structure or business practices that emerged from the case. To assure consistency of methods for evaluating investigations, the FTC should create guidelines that set forth standard assumptions and methods for an IIS.

IIS reports could be very brief (a few pages), but invaluable in managing resource allocation in the agency. In some cases an investigation inevitably will result in no action because a suspicious merger or business practice proves to be beneficial to consumers. *These investigations should not necessarily be regarded as failures because no action ensued.* By describing the circumstances that gave rise to the investigation and the reasons for concluding that no action was warranted, the FTC can create an important source of information about both business practices and the methods for evaluating them that can improve the efficiency of subsequent Commission enforcement activities.