Not Another Drug!
Antitrust for Drug and Other Innovations

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THE SECOND CIRCUIT’S DECISION in New York ex rel. Schneiderman v. Actavis PLC1 shines a spotlight on whether a firm’s conduct to manage a transition to a new product can violate the antitrust laws. The product at issue there is the drug Namenda (chemical name memantine hydrochloride), prescribed to treat moderate-to-severe Alzheimer’s disease and sold by Forest Laboratories, a subsidiary of Actavis. Forest introduced an “extended release” version of the drug (Namenda XR) that is administered daily in place of its “immediate release” twice-a-day version (Namenda IR).2 The district court held that Forest’s actions coerced patients to transition from Namenda IR to Namenda XR, and granted an injunction pending trial on the merits that requires Forest to continue to make Namenda IR tablets available for 30 days following generic entry on the same terms and conditions applicable when Forest first sold Namenda XR.3 The appellate court upheld the district court’s decision.

Actavis is one of a number of antitrust cases that have challenged a firm engaged in conduct associated with the introduction of a new product. Several of these cases are in the pharmaceutical industry, and have earned the moniker of “product hopping.”4 Other cases involve the design of interfaces that defeat interoperability and the supply of integrated products, curtailing demand for one or more of the integrated components.

This article compares the typical allegations in pharmaceutical product hopping cases to other allegations of anticompetitive innovation. Conduct that involves innovation may harm consumers in some circumstances, but antitrust enforcement should not chill incentives for firms to make innovations that contribute to consumer welfare. I propose a framework to compare the costs and benefits of single-firm conduct involving innovation that is a modification of the rule of reason analysis in United States v. Microsoft Corp.5 and offer two suggestions for “almost safe” harbors. One is a transition to a new product that is accomplished without constraining consumer choices among existing products. The court in Actavis characterized such conduct as a “soft switch,” in contrast to a “hard switch” that coerces consumers to purchase a new product.6 Courts have distinguished the com-
petitive implications of soft and hard switches in several contexts involving the introduction of new products.

The second “almost safe” harbor is for the development of an improved product, interface, or design that impacts the supply of complementary products or services, provided that these complements do not offer a pathway for competition that would undermine monopoly power. A monopolist generally has incentives to promote competition in the supply of complementary products and services because lower priced or higher quality complements increase the demand for its own product.

Courts should be skeptical of antitrust cases that allege harm to consumers from conduct associated with the introduction of a new product or design if it occurs in the context of a soft switch or if the new product or design only affects complementors. In these circumstances the potential for significant adverse competitive effects is limited, and aggressive enforcement would risk chilling incentives for innovation. I use the term “almost safe” harbor to note that an antitrust analysis should respect individual circumstances, and conduct that appears innocent may harm consumers in some instances. By the same token, conduct outside these harbors should not be presumed to violate the antitrust laws. This is particularly true for conduct involving innovation given the enormous contributions that innovation has made to consumer welfare and economic growth.

Doing the Product Hop and Other Allegations of Anticompetitive Innovation

Allegations of anticompetitive innovation have appeared in at least four basic contexts or categories of conduct, described below.

**The Product Hop.** Product hopping refers to a strategy in which a firm manages the lifecycle of a product by transitioning consumers to a new version or design. Several product-hopping allegations focus on conduct involving the introduction of incremental changes to patented drugs, but product hopping can occur in other industry contexts in which firms use alleged improvements to extend the life of a product. Potential examples include software upgrades, new versions of microprocessors, and successive generations of telecommunications standards.

Numerous factors make pharmaceuticals a particularly fertile field for incremental innovations to extend market power. The Drug Price Competition and Patent Term Restoration Act (Hatch-Waxman Act) promotes generic substitution by providing a fast track for the approval of drugs that are chemically and therapeutically identical to a reference drug, while state pharmacy laws make it easy for generics to market their drugs by permitting—and in some states requiring—pharmacists to substitute an available generic for a prescription of a branded drug unless the patient objects or the physician indicates otherwise. When pharmacists are free to take full advantage of drug substitution laws, generics typically claim a high fraction of drug sales at a fraction of the price of the branded drug, greatly reducing revenues for the seller of the
branded drug while delivering correspondingly large benefits to health care providers and patients.

As a consequence, sales of branded drugs face a “patent cliff” from generic competition following the expiration of patent protection for these drugs. A manufacturer of a branded drug can avoid this cliff—or moderate its slope—by introducing a new, patented drug for the same or similar indications, and encouraging physicians to move their patients to the new drug. The Hatch-Waxman Act further incentivizes this product switching strategy by providing a patented drug with 30 months of exclusivity if a generic manufacturer employs the provisions of the Act and challenges the brand’s patent. Thus, a new, patented drug can extend the branded drug’s period of exclusivity by an additional minimum of 30 months.

A recent example of avoiding the patent cliff centered on Namenda IR and XR. Faced with imminent generic competition, Forest could avoid or minimize generic competition by switching patients to the new, patent-protected extended release version, Namenda XR, prior to the entry of generic substitutes for Namenda IR. This is the “hop” from a drug about to lose patent protection to a newer, patented drug. Forest initially planned to discontinue Namenda IR prior to generic entry and subsequently planned to provide limited access only to patients whose physicians indicated that the drug was medically necessary. These actions made it more likely that physicians would transition patients to the new drug before generics could enter. Furthermore, there was testimony that after generics entered, most physicians would not write prescriptions for the older drug after their patients become accustomed to the new therapy. Both the district court and court of appeals concluded that this was functionally a “hard switch.”

**New Products that Defeat Interoperability.** Several cases have alleged anticompetitive innovation when a firm with market power changes the design of its product in a way that defeats interoperability with other firms’ products. Examples include the IBM peripherals cases, in which the plaintiffs alleged that IBM destroyed competition in the market for peripherals, such as disk drives that were “plug-compatible” with IBM mainframes, by introducing new designs and protocols for connecting the peripherals to the mainframe. In a similar vein, Berkey Photo sued Kodak when the camera company introduced a new film format for its cameras.

More recent examples of alleged intentional incompatibilities include *C.R. Bard, Inc. v. M3 Systems, Inc.*, which involved the redesign of a biopsy gun that made the gun incompatible with biopsy needles sold by M3 Systems, and *Allied Orthopedic Appliances Inc. v. Tyco Health Care Group LP*, in which a group of hospitals and other health care providers sued Tyco for redesigning its blood oxygenation monitors to make them incompatible with sensors sold by other companies. Other examples include Caldera’s complaint that Microsoft designed the Windows 3.1 set-up program to send an error message if the program detected the
rival DR-DOS operating system, and a lawsuit brought by a class of consumers against Apple for releasing an update of its iTunes software that prevented iPod users from storing music purchased from third parties such as RealNetworks.

*The Technological Tie.* An innovation can take the form of changing the design of a stand-alone product to make it a hardwired component of a bundle. In this scenario, independent suppliers of complements could compete for sales when the product was available in a stand-alone configuration. However, the bundle reduces demand for products sold by these independent suppliers if the bundle includes similar products as hardwired components. Technological tying can take many forms. A firm may change the design of a microprocessor to include additional memory on the same chip, reducing the demand for memory products sold by other suppliers. An exemplar for technological tying is Microsoft’s integration of its operating system and its Internet Explorer browser, which contributed to a much-reduced demand for Netscape’s Navigator Internet browser.

*Failure to Supply Information that Rivals Desire to Supply Compatible Products.* Sometimes the input that a firm requires to supply a competitive product is information about the design of a complementary product or the interface necessary to connect with the complementary product. If the supplier of the complement refuses to supply this information or changes the design without supplying the information in a timely fashion, the result can damage the ability of another firm to be an effective competitor. The failure to supply timely information to enable interoperability can attract antitrust scrutiny if it maintains or extends monopoly power. The Federal Trade Commission alleged that Intel harmed competition by withholding information and creating other obstacles to impede the interoperability of non-Intel graphic processing units with Intel’s microprocessors.

The cases in these categories share important characteristics. In each, the defendant provides a product or information that other firms rely on to sell their products, either as a direct input or as a complementary product or service. All involve a new product or design that renders some other firms’ products less attractive alternatives in the marketplace, if not altogether obsolete. As noted above, the switch to the new product or design can be “hard” or “soft.” For product hopping, the switch is hard if the introduction of a new product is accompanied by measures to make the older product unavailable. For incompatibilities, the switch is hard if the defendant no longer supports the older product or interface protocol. In this respect, a hard switch has characteristics of a refusal to deal in the supply of the old product or interface. Refusals to deal can raise competition concerns, but they also can have related benefits by promoting the creation and adoption of new products and encouraging competition in new technologies.

**Anticompetitive Refusals to Deal and Procompetitive Benefits**

Courts that have addressed allegations of anticompetitive...
innovation generally recognize that it is the curtailment of alternatives—not the innovation—that is of potential antitrust concern. For example, the complaint in *Schneiderman v. Actavis (Actavis)* did not challenge the innovation of Namenda XR itself, but rather focused on the reduction in consumer choice when Forest planned to remove Namenda IR from the market, thereby frustrating generic substitution. The challenged conduct was “the combination of Defendants’ withdrawal of IR and introduction of XR in the context of generic substitution laws that places their conduct beyond the scope of their patent rights for IR or XR individually.”

Yet antitrust scholarship and the law remain conflicted as to whether a firm—even one with monopoly power—has an obligation to supply a product that other firms desire. The Report and Recommendations of the Antitrust Modernization Commission concluded, “In general, firms have no duty to deal with a rival in the same market.” In *Verizon v. Trinko*, the U.S. Supreme Court affirmed that, “as a general matter, the Sherman Act ‘does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.’”

The deference to independent discretion expressed in *Trinko* can be distinguished from the obligation to supply a product in a case such as *Actavis*. The antitrust laws do not require a firm that has achieved a dominant position as a consequence of a superior product, business acumen, or historic accident to share the fruits of its efforts with others. However, the allegation in *Actavis* is that Forest did not maintain its dominant position in the market for memantine hydrochloride by competing on the merits of Namenda XR, but rather by coercing patients to switch to Namenda XR through the planned curtailment of Namenda IR as a reference for generic substitution. Indeed, the district court in *Actavis* emphasized that a firm’s right to choose with whom it will deal includes the qualification, “‘[i]n the absence of any purpose to create or maintain a monopoly.’”

Although in some contexts a “hard” switch can be characterized as an anticompetitive refusal to deal, it can also have significant consumer welfare benefits. Suppressing the availability of an older product makes it easier for a firm to overcome consumer inertia that often slows the adoption of a new product—even one that offers significant consumer benefits. In turn, this increases incentives to improve products and can be an important element in the incentive for innovation in the first place. Pharmaceutical companies might not invest to develop critical therapies, or might invest less, if not for the expectation of a profitable product roadmap that includes product line extensions.

To be sure, the consumer benefits from product extensions may be small and the ability to upsell consumers to a new product can lead a firm to invest in incremental improvements instead of more significant innovations that do not require coercing consumers to accept the new product. Nevertheless, courts should not ignore the potential benefits
from these improvements.

Courts have resorted to various rules or standards to assess when the transition to a new product may violate the antitrust laws. The next section briefly reviews some of the analytical frameworks that courts have applied and their limitations.

Standards to Evaluate Anticompetitive Innovation

Courts have invoked different standards to evaluate when conduct in the context of new product introductions may be unlawful. In *Allied Orthopedic Appliances v. Tyco Health Care Group*, the Ninth Circuit held that “a design change that improves a product by providing a new benefit to consumers does not violate Section 2 absent some associated anticompetitive conduct” and “[t]here is no room in this analysis for balancing the benefits or worth of a product improvement against its anticompetitive effects.” Thus, the Ninth Circuit in essence applied a rule of per se legality, provided that the new product has consumer benefits and the defendant does not engage in conduct that would otherwise offend the antitrust laws, such as entering into exclusive dealing arrangements.

By contrast, in *C.R. Bard, Inc. v. M3 Systems, Inc.*, the Federal Circuit focused on the intent of Bard’s redesign of its biopsy gun, inquiring whether the purpose was to injure competition rather than to improve the product. Despite evidence that the redesign was an improvement, the Federal Circuit upheld a jury finding that Bard violated the antitrust laws because its intent was to injure competition.

Neither the standard of per se legality for valid innovations nor the intent test addresses the key issue of whether the defendant’s conduct is likely to harm or benefit consumers. Furthermore, other tests for “predatory” innovation only indirectly address consumer welfare, such as those that focus on the profit sacrificed by the innovator to introduce a new product or whether its introduction makes any economic sense. As a consequence, these tests can condemn innovations that have net consumer benefits or fail to identify conduct that harms consumers, even if the fact finder has good information about the nature of the new product and the competitive effects from the firm’s conduct.

A different approach is set forth in *United States v. Microsoft*, where the D.C. Circuit proposed a step-wise rule of reason analysis that asks first whether conduct by a defendant with market power has anticompetitive effects. If so, the defendant can respond with procompetitive justifications. If the plaintiff establishes harm and the defendant has cognizable justifications, the plaintiff must then demonstrate that the anticompetitive harm outweighs the procompetitive benefit. The district court in Actavis accepted, and the Second Circuit affirmed, this approach. Both courts also focused on whether the introduction of a new product involved coercion. Citing *Berkey Photo v. Eastman Kodak*, the Second Circuit stated, “When a monopolist combines product withdrawal with some other conduct, the overall effect of which is to coerce consumers rather than persuade them on the
merits, and to impede competition, its actions are anticompetitive under the Sherman Act.”

At issue in *Actavis* was an injunction to prevent the withdrawal or curtailment of Namenda IR until generics had entered. Although the district and appellate courts considered the effects of the conduct, it was not a full trial on the merits. One can predict how the *Microsoft* rule of reason analysis would proceed in a trial on the merits for a product-hopping case that alleges the exclusion of generic competitors. If the plaintiff establishes the usual predicates of monopoly power, efforts to discontinue or significantly reduce the availability of a drug that is eligible for generic substitution would likely trigger the first step in the *Microsoft* approach. Conduct that impedes generic substitution may cause significant harm to competition, although the analysis should consider the alternatives available for rivals to market their products as well as other sources of competition before reaching that conclusion.

Moving to the second step of the *Microsoft* rule of reason framework, the defendant in a product-hopping case is likely to argue that impeding generic competition has a procompetitive justification. Of course, the mere prospect of increasing revenues that can be spent on research and development is not a salve for anticompetitive conduct. A defendant would have to demonstrate benefits from transitioning consumers to a new product or show that the potential for incremental invention was instrumental to the success of a research program. In particular, the defendant would have to show that the suppression of competition promoted the realization of these procompetitive benefits.

If the exclusion of competition promotes a social benefit from the new product, an antitrust evaluation of product-hopping under the *Microsoft* framework would move to the third step in the rule of reason analysis—i.e., the weighing of anticompetitive harm and procompetitive benefit. In many cases this will be a difficult balancing. Suppose a new drug extends life or improves the quality of life for some patients, possibly because it is in a form that improves patient compliance. How should courts compare this benefit to the anticompetitive harm from the exclusion of competition? One approach to this balancing would be to put a price on human life, but it is far easier to calculate the increase in costs from excluding competitors than it is to calculate the value from better drug compliance of additional months of life. [Q: IN THIS CASE, QUALITY OF LIFE RATHER THAN EXTENSION OF LIFE?] without the deepening ravages of a disease like Alzheimer’s. Moreover, an incremental invention can have spillover benefits for other products or methods of manufacture. The rule of reason analysis should take these spillover consumer benefits into account, but a reliable estimate of these benefits is likely unavailable in many circumstances.

The rule of reason approach in *United States v. Microsoft* is embedded in antitrust jurisprudence and properly focuses on the net effects of conduct on consumer welfare. However, in the context of innovation, the issues are particularly com-
plex, and antitrust enforcement is vulnerable to costly errors. Here I suggest a variant of the Microsoft rule of reason analysis that provides a cushion to protect against errors that might condemn procompetitive innovations and chill incentives for invention.

**A Weighted Rule of Reason.** In an ideal, and entirely abstract, world all conduct should be evaluated based on its expected consumer welfare effects. The rule of reason analysis in *United States v. Microsoft* encompasses both the potential harms from exclusion of older products or methods of production and the procompetitive benefits from the introduction of a new product and, in this respect, is theoretically sound. However, the *Microsoft* methodology is fraught with analytical hazards that can condemn conduct that involves innovation. The harms from the introduction of a new product are relatively easy to identify. It is not particularly difficult to discern whether competitors are excluded because an older product or interface is no longer available and to measure the effects. It is more difficult to determine the value of an innovation, particularly over the longer term, including any spillover benefits for other technologies.

To the extent that such a balancing is feasible, in my view the scale should be biased in favor of innovation benefits. I therefore propose a “weighted” rule of reason analysis for innovation. The weight refers to the evidentiary requirements to establish innovative benefits versus anticompetitive harms. If both the benefit from an innovation and the harm from excluded competition could be calculated with a tolerable level of precision, my proposed rule of reason analysis would account for them equally. However, in many situations the benefits from an innovation are uncertain. In those instances, the fact-finder should credit the innovation with an additional weight to reflect the likelihood that the fact-finder may underestimate its societal contribution.  

A weighted rule of reason does not provide a free pass to conduct that involves a discrete product improvement. Rather, the approach allows for a comparison of benefits and harms, while easing the evidentiary burden for proof of innovation benefits. This approach guards against condemning procompetitive innovations, but it is not immune to error and is likely to be difficult to implement in many circumstances. Importantly, a rule of reason analysis for innovation, even with appropriate evidentiary weights, risks chilling procompetitive innovative conduct by not providing clear signals about the types of conduct that may incur antitrust liability. For these reasons it is desirable to define limits to the rule of reason analysis for unilateral conduct involving innovation by identifying market circumstances in which such conduct is unlikely to impose significant harms to competition. The next section describes two areas that should qualify for “almost safe” harbors, with the qualification that it is unwise to adopt conventions that entirely insulate conduct from antitrust scrutiny because competitive effects depend on particular circumstances.
“Almost Safe” Harbors
This section describes certain characteristics of markets and firm conduct that mitigate potential adverse consumer outcomes associated with the introduction of a new product. These characteristics may not be so determinative as to establish immunity from the antitrust laws for new product introduction, but they warrant consideration for antitrust enforcement. For this reason I refer to them as “almost safe” harbors.

Soft Switches. As discussed, courts in both product-hopping and interoperability cases have distinguished hard switches from soft switches. The Second Circuit emphasized this distinction in Actavis and pointed to precedent in Berkey Photo, where Kodak continued to sell and support the older film formats. Other courts have rejected allegations of anticompetitive product hopping when the switch was soft and there was no evidence of coercion.

The distinction between hard and soft switches is important. If a switch is soft, acceptance of a new product depends on its relative merits and not on the restriction of alternatives. A soft switch, by definition, does not coerce consumers to choose the new product. For pharmaceutical product hopping, a soft switch does not constrain physician choice or the availability of an older therapy. In the case of interoperability, a soft switch allows a firm to continue to connect using established compatibility protocols.

Yet a determination of whether a particular switch is hard or soft depends on economic circumstances and does not necessarily admit a simple classification. A switch to a new drug may involve incentives, such as attractive pricing, advertising, and promotion, that blur the distinction between “soft” and “hard.” The distinction can also be difficult in other industries. The publisher of software that interfaces with other software products may introduce an incompatible upgrade while continuing to offer the older product for sale or lease. The continued sale or lease of the old product suggests that the switch is soft. However, the software may require extensive support to be commercially useful, which the publisher may or may not continue to supply in a manner that is timely and informative. Without sufficient support, the switch may effectively coerce the suppliers of complementary software products to redesign their products to be compatible with the new version.

Importantly, a switch does not necessarily foreclose meaningful competition merely because it is “hard.” Generic companies can develop and promote their own branded versions of off-patent drugs such as Namenda IR, although intense competition can make such efforts unprofitable if their products are not differentiated. Third-party payors, such as pharmacy benefit managers, can promote the use of generic drugs, including branded generics, without the benefit of automatic substitution at the pharmacy counter. Remedies that compel pharmaceutical companies to maintain historical levels of generic competition can have undesirable disincentive effects by discouraging generic companies from introducing their own branded products and by reducing incentives for innovation more generally.
Complementors. Virtually all cases alleging anticompetitive innovation involve the supply of an input in the form of a product, interface, or design that firms desire to compete. In this respect all of these cases have a vertical dimension. Nonetheless, they differ because in some cases the firms impacted by the innovative conduct supply complementary components, while in others they are direct competitors. Biopsy needles do not compete with biopsy guns. Peripherals do not compete with mainframe central processing units. These are examples that involve the supply of complements. In contrast, generics compete with branded drugs, although there is still a complementary dimension because they rely on the reference branded drug for pharmacy substitution.

Cases that have alleged anticompetitive innovation can be categorized as primarily involving conduct affecting complementors or competitors. Competition concerns are mitigated in cases involving complementors because a monopoly supplier should benefit from competition in the supply of a complementary product or service. Cheaper and better biopsy needles allow the monopolist to charge more for the biopsy gun. The “competition is good for the monopolist” argument does not apply to cases involving direct competitors, such as pharmaceutical product hopping, where the conduct impedes competition from generic suppliers. Firms have incentives to advantage themselves at the expense of their competitors, and the key issue is whether their conduct better reflects competition on the merits or efforts that harm competition.35

While the supplier of a product like a biopsy gun can benefit from competition in the supply of another complement like biopsy needles, the supplier may choose to thwart competition in the market for the complement for at least three reasons. First, the manufacturer may be constrained in the amount that it can charge for its product or in the amount that it can charge complementors for the right to access its product. If the manufacturer of a biopsy gun cannot charge a monopoly price for the gun, it has an incentive to offer a system consisting of the gun and the needles if, by doing so, it can charge a price that is closer to the monopoly price. A firm’s decision to supply a biopsy gun that can use only its own needles is similar in some respects to a decision to vertically integrate. Whether such conduct harms consumers depends on a host of factors that are commonly encountered in the evaluation of vertical mergers.

Second, the gun manufacturer may be better able to price discriminate if it is also a monopoly supplier of needles. The monopolist can use the price of needles to “meter” demand and extract more surplus, much the way that sellers of ink jet printers offer the printer at a low price and charge high prices for the ink jet cartridges. Price discrimination can harm consumers in some, but not all, circumstances. A price that depends on demand can allow a firm to serve consumers who otherwise would be excluded if the firm charged everyone the same price.36

Third, the supply of a complement can provide a pathway to competition that can benefit consumers. Production of the
Complement can facilitate entry into the market for the monopoly product. The component can be the first step in a two-step pattern of market entry. By manufacturing peripheral devices, such as disk drives that are plug compatible with mainframe computers, a firm might better amortize research and development costs and eventually become a competitor in a market for computing systems. Components can facilitate competition in other ways. In United States v. Microsoft, Microsoft engaged in conduct to limit the adoption of Netscape’s Internet browser product because it feared that Netscape’s browser would evolve to become a platform for applications that would undermine Microsoft’s operating system monopoly. In other circumstances, limiting competition in the supply of complementary products could prevent the emergence of an ecosystem of component suppliers that can be a source of robust innovation and ultimately produce new competitors that could challenge the status of a dominant firm. For example, the owner of a platform may want to manage the supply of complementary applications out of concern that one or more app developers may evolve to become competitors of the platform.

Thus, while innovations that only affect competition in the supply of a complement need not raise antitrust concerns, conduct that excludes actual or future competition for the monopoly product does not deserve immunity from the antitrust laws, even if it involves the introduction of a new product. In some situations, a dominant firm has no incentive to harm the supplier of a complement, and antitrust enforcement should take this into account. However, other situations blur the distinction between complementors and competitors, and this too should be a factor in antitrust enforcement.

A balancing of the likely harm to competition against the benefits from new products or services favors almost safe harbor treatment for soft switches and conduct that only affects complementors and not competitors. This does not imply that a soft switch eliminates the possibility of consumer harm. It does not. However, the balance of enforcement risks favors shielding soft switches from aggressive antitrust enforcement. Similarly, innovative conduct that adversely affects complementors can raise prices and harm consumers. However, innovators have incentives to protect the supply of efficient complementors, and exclusionary conduct that enables more effective price discrimination can benefit as well as harm consumers. Absent special circumstances, when the introduction of a new product or design occurs in the context of a soft switch or only affects complementors, the risk of chilling procompetitive innovation from antitrust enforcement likely outweighs the risk of harm from too little enforcement.

**Going Forward**
Innovation benefits consumers and powers economic growth, but some conduct that occurs along with the introduction of a new product or service may warrant antitrust condemna-
tion. Although courts have articulated different standards to assess when conduct that involves innovation may offend the antitrust laws, in most cases the defendant has prevailed when it offers a discrete improvement in quality, performance, or cost and there is no other exclusionary conduct. For innovations of questionable value, courts have looked to evidence of intent to exclude rivals. But, as a matter of antitrust policy, it should not be relevant whether the defendant’s claims mask its true intent; the relevant issue is whether the conduct promotes consumer welfare.

The rule of reason analysis described in United States v. Microsoft permits an evaluation of both the costs of anticompetitive conduct and the benefits for innovation that such conduct may facilitate. However, the benefits from innovation are particularly difficult to measure, as they may occur well in the future, have intangible consequences such as improved quality of life, and have value for firms and consumers in other market activities. For these reasons, I propose a modification to the Microsoft rule of reason analysis that eases the evidentiary burden to demonstrate innovation benefits.

This weighted rule of reason provides a cushion to avoid condemning procompetitive innovation. Nonetheless, the outcome of such an analysis is uncertain, and that unpredictability may chill incentives to innovate. It is therefore useful to delineate safe harbors when consumer costs are unlikely to be large relative to the benefits from new products or services. Soft switches and conduct that affects complements do not qualify as perfect safe harbors because a switch may appear to be soft yet still exclude competitors, and complements can facilitate competition or evolve to become direct competitors themselves. Nonetheless, these “almost safe” harbors should mitigate concerns that consumers may be harmed in the course of introducing a new product or service. Of course, conduct is not anticompetitive merely because it falls outside these harbors.

1 New York ex rel. Schneiderman v. Actavis PLC, 787 F.3d 368 (2d Cir. 2015).
4 E.g., Actavis, 787 F.3d at 643; Actavis, 2014 WL 7015198, at *9.
6 See Actavis, 787 F.3d at 647–48.
7 In addition to Actavis, cases in the pharmaceutical industry that have alleged anticompetitive product hopping include Abbott Laboratories v. Teva Pharmaceuticals USA, Inc., 432 F. Supp. 2d 408 (D. Del. 2006), see id. at 413–18, 422–24; Mylan Pharmaceuticals, Inc. v. Warner Chilcott Public Ltd.


9 Actavis, 787 F.3d at 648 (agreement with mail-order pharmacy effectively withdrew Namenda IR from the market); see id. at 653–54; Actavis, 2014 WL 7015198, at *23–24, *40.

10 See, e.g., Telex Corp. v. IBM Corp., 510 F.2d 894, 903, 925 (10th Cir. 1975); Cal. Computer Prods., Inc. v. IBM Corp., 613 F.2d 727, 743–44 (9th Cir. 1979); Memorex Corp. v. IBM Corp., 636 F.2d 1188, 1188 (9th Cir. 1980) (per curiam); Transamerica Computer Co. v. IBM Corp., 698 F.2d 1377, 1382–83 (9th Cir. 1983).


13 Allied Orthopedic Appliances Inc. v. Tyco Health Care Group LP, 592 F.3d 991 (9th Cir. 2010).


16 See Microsoft, 253 F.3d at 64–67.


18 Actavis, 787 F.3d at 660.


21 Actavis, 2014 WL 7015198, at *37 (quoting Colgate & Co., 250 U.S. at 307 (emphasis added)).

22 Allied Orthopedic Appliances, 592 F.3d at 998–99.

23 Id. at 1000.

24 See C.R. Bard, 157 F.3d at 1381–83.


27 See Microsoft, 253 F.3d at 58–59.


29 See Actavis, 2014 WL 7015198, at *40; Actavis, 787 F.3d at 652–55.

30 Actavis, 787 F.3d at 654 (citations omitted) (citing Berkey Photo, 603 F.3d at 274–75, 287).

31 There is precedent in merger policy for holding efficiencies to a different standard than competitive effects. See U.S. Dep’t of Justice & Federal Trade Comm’n, Horizontal Merger Guidelines 30–31 (2010), https://www.ftc.gov/system/files/documents/public_statements/804291/100819hmg.pdf (In their merger evaluations, “the Agencies are mindful that the antitrust laws give competition, not internal operational efficiency, primacy in protecting customers”). See also Daniel A. Crane, Rethinking Merger Efficiencies, 110 MICH. L. REV. 347, 348 (2011) (“[M]erger law implicitly requires a greater degree of predictive proof of merger-generated efficien-
cies than it does of merger-generated social costs.”).

32 See Actavis, 787 F.3d at 652–53 (citing Berkey Photo, 603 F.3d at 287 & n.39).


34 Alan Devlin and Michael Jacobs argue that regulatory constraints undermine the utility of antitrust analysis for product hopping in the pharmaceutical industry. See Alan Devlin & Michael Jacobs, Anticompetitive Innovation and the Quality of Invention, 27 Berkeley Tech. L.J. 1, 51 (2012) (“The problem, if one exists, is that antitrust rules are designed to operate in unregulated markets in which companies enjoy equality of opportunity. The key insight here is that policymakers should not distort well-established antitrust rules in order to solve what is, at heart, a regulatory problem. . . . Product hopping in the pharmaceutical industry is an excellent candidate for such a solution.”).

35 My focus is on the competitive effects of the alleged conduct and not on whether it fits into a particular enforcement box. In particular, I do not consider whether a redesign that defeats interoperability implements a tied sale, for example by obligating a purchaser of a biopsy gun to purchase needles from the gun manufacturer.


37 See Microsoft, 253 F.3d at 50, 59–64.