# The FTC's Challenge to Intel

## Predictions of Doom Are Exaggerated and Misplaced—the FTC Has a Straightforward Case

**By David Balto | April 6, 2010**

The Obama administration has promised more aggressive antitrust enforcement. In its first action under new leadership, the Antitrust Division of the U.S. Department of Justice abandoned a report issued during the previous administration that blessed a broad range of conduct by dominant firms. Both the Federal Trade Commission and DOJ have promised stronger enforcement efforts against anticompetitive mergers. The most significant challenge has been an enforcement action against Intel Corp. by the FTC challenging a wide variety of anticompetitive conduct in critically important markets for microprocessors.

As with any major antitrust action, the FTC's suit has sparked significant controversy. After all, Intel is a powerful corporation with enormous resources. In public comments, it has responded that the prices of microprocessors have plummeted and output has increased. It has also claimed that there have been dramatic increases in innovation accompanied by increasing expenditures in research and development.

And some commentators attack the FTC's use of Section 5 of the FTC Act: The agency is alleging not only that Intel has engaged in exclusionary conduct in violation of the Sherman Act but also (as explained in further detail below) that it has engaged in "unfair methods of competition" and "unfair acts or practices" in violation of Section 5, as an additional, stand-alone violation. Thus, Intel supporter Robert Litan claimed in a paper that, if the FTC prevails, it will result in a "radical and sweeping reinterpretation of this nation's antitrust laws." Robert Litan, "Piling on Intel: The FTC's Radical Application of Section 5" (Charles River Associates, Feb. 17, 2010).

These predictions of doom are exaggerated and misplaced. The reality is far more straightforward. Intel has been clearly dominant in the market for central processing units (CPUs) with between 80 percent and 98 percent of the market. The practices at issue in the FTC litigation have been condemned by the Japan Fair Trade Commission in March 2005, by the Korean Fair Trade Commission in June 2008 and by the European Commission in May 2009. In the United States, Advanced Micro Devices Inc. (AMD), Intel's sole significant rival, sued Intel for a broad range of exclusionary practices in 2005. The New York attorney general brought its own action in November 2009.

Intel has had its day in court in proceedings before the three foreign commissions—and lost. Each of those tribunals found that Intel engaged in severely anti-competitive practices that protected its central processing unit monopoly and excluded its only real CPU rival, AMD.

Second, Intel's rebate schemes with computer manufacturers and retailers severely limited consumer choice. Instead of providing consumers with the option of choosing AMD-based computers, retailers and computer manufacturers were effectively constrained by exclusionary rebates and other devices to offer only Intel's CPUs. As each enforcer concluded, Intel—through its exclusive rebate scheme—paid computer manufacturers to buy Intel's more expensive, less technologically advanced CPUs, resulting in turn in consumers paying higher prices for computers.

Not surprisingly, the foreign regulators imposed severe penalties. The European Commission penalized it more than $1.45 billion, the largest fine in that commission's history. And earlier last year, Intel settled the AMD litigation for $1.25 billion, also one of the highest antitrust settlements in history.

## Why the FTC action?

In light of these enforcement actions and settlements, why then was an FTC action necessary? By any measure there is reason to see a highly problematic course of conduct that has not been completely addressed by these other enforcers.

First, the FTC complaint challenges exclusionary conduct in the emerging and critically important graphic processing unit (GPU) market, a market not addressed in the other actions. GPUs have remarkably powerful processing capability such that they perform many key tasks far more rapidly and effectively than CPUs. The complaint alleges that Intel has sought to thwart competition from GPU manufacturers because "these products have lessened the need for CPUs, and therefore pose a threat to Intel's monopoly power." In order to diminish the potential competitive threat from GPU manufacturers, according to the complaint, Intel engaged in deception, degraded connections between GPUs and CPUs, refused to deal with a key GPU manufacturer (Nvidia Corp.) and unlawfully bundled Intel's GPUs with its CPUs, resulting in below-cost pricing.

Second, there are the important institutional advantages to a suit by the FTC. Unlike private parties, the FTC can bring its cases before an FTC administrative law judge in an administrative proceeding, as it has done here. The FTC administrative process has clear time limits that promise a resolution typically in just more than one year. In fact, the case is scheduled to go to trial in September—only nine months after the filing of the complaint. Such speed is especially useful in addressing alleged anti-competitive conduct of dominant firms in dynamic, fast-changing high-tech markets; the comment is sometimes heard that

judicial resolution is just too slow to provide a proper, timely remedy that can both promote innovation and protect competition in such markets. Furthermore, the FTC has particular expertise in antitrust matters and is far more capable than a generalist federal court to grapple with the complex issues posed by Intel's conduct.

Third, the FTC is not only bringing a traditional monopolization case under Section 2 of the Sherman Act; it is also challenging the conduct under Section 5 of the FTC Act, 15 U.S.C. 45. Section 5 allows the FTC to prohibit "unfair methods of competition...and unfair acts or practices." The U.S. Supreme Court has held that the reach of the FTC's powers under Section 5 extends somewhat beyond the antitrust laws—the FTC Act was designed to "stop in their incipiency acts and practices which, when full blown, would violate those Acts...as well as to condemn as 'unfair methods of competition' existing violations" of those acts. Despite its characterization by some opponents as "radical," the FTC's assertion of an independent Section 5 enforcement power in this case is not new. As current FTC Chairman Jon Leibowitz has observed in his concurring decision in In re Rambus, FTC No. 9302 (Aug. 2, 2006), "Section 5 was intended from its inception to reach conduct that violates not only the antitrust laws themselves, but also the policies that those laws were intended to promote."

The action could stand on the Section 2 claims alone—as the conduct constitutes "exclusionary conduct" within the meaning of Section 2—but there are aspects of Intel's conduct (e.g., certain unfair and deceptive practices) that make the application of Section 5, in addition, wholly appropriate. The FTC alleges certain types of deception of customers, such as deception relating to competitors' efforts to enable their GPUs to interoperate with Intel's newest CPUs. Section 5, which condemns unfair practices, may in fact be a stronger, more specifically targeted tool for condemning these practices.

Moreover, Section 5 enables the FTC to go beyond narrow competition concerns. As the Supreme Court has held in FTC v. Sperry & Hutchinson Co., 405 U.S. 233 (1972), "like a court of equity, the Commission may consider public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws." Here, the FTC asserts that conduct that falls within the scope of Section 5 includes "deceptive, collusive, coercive, predatory, unethical, or exclusionary conduct or any course of conduct that causes actual or incipient harm to competition."

Finally, the most straightforward reason why FTC enforcement is necessary is that, although AMD settled its long-running suit challenging the conduct condemned by the three foreign commissions, it was largely a monetary settlement. Just because AMD has resolved its concerns does not mean that consumers are protected, and the AMD settlement does not address the critical issues in the GPU market.

The FTC's action is perhaps most important for its focus on dynamic competition. Innovation is central to the growth of the U.S. economy. Exclusionary conduct that dampens innovation extracts a significant cost on the economy.

Consider the allegations concerning the restrictive practices that diminish the competitive impact of GPUs. Not only does Intel's conduct threaten competition in the GPU market, but the emergence of GPU competition also threatens Intel's CPU monopoly. Indeed, in a publicly available document prepared by one of Intel's senior officials, the threat of GPU competition was highlighted with the observation: "YIKES!" Intel's actions aimed at GPU competition, as alleged in the FTC's complaint, soon followed.

In this way, the FTC's case is similar to the U.S. Department of Justice's case against Microsoft Corp. in the late 1990s. That case focused on Microsoft's exclusionary practices in the Internet browser market directed at thwarting a "middleware" threat posed by Netscape's browser and SunMicrosystem's Java as a platform for competition to the Windows monopoly. However, whereas the middleware threat in Microsoft was arguably somewhat speculative, here the threat of commoditization of CPUs through the processing power of GPUs is quite actual and the threat to Intel is thus far more immediate than that faced by Microsoft. The reasoning behind the government's monopolization claim in Microsoft therefore certainly applies with even more reason to Intel's conduct.

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