

## **Economics 335**

### **Economics of Regulation and Antitrust**

Dr. David Loomis  
Fall 2016

TR 11 a.m.-12:15 p.m.  
STV 234

Office: STV 428  
Office Hours: TR 2-3:30 pm and by appointment  
Phone: 438-7979  
E-mail: dloomis@ilstu.edu

Course Prerequisites: ECO 101 or 105 and ECO 240

#### **REQUIRED RESOURCES:\***

Required Text: **W. Kip Viscusi, John M. Vernon, and Joseph E. Harrington, Jr.**  
*Economics of Regulation and Antitrust 4<sup>th</sup> Ed.*, Cambridge, Mass.: MIT Press, 2005.  
(Abbreviated VVH)

*Papers referenced in the syllabus will be on ReggieNet.*

ReggieNet will be used as our course management system. On ReggieNet, you will find the following:

- A current copy of this syllabus,
- Class Announcements,
- Problem Sets,
- Lecture Notes (PPT), and
- Links to useful websites.

#### **COURSE OBJECTIVES:**

This course covers the origins, aims, methods and effects of economic regulation and antitrust. The course will provide the theoretical foundation for economic analysis while allowing the student to apply sound reasoning to actual legal cases or case studies. The study of legal cases and case studies will be done primarily through in-class discussions.

Students will learn to use economic criteria for judging the applicability of regulation to different industries. Since this is the first course in the Master's Degree sequence in Policy Studies in Electricity, Natural Gas, and Telecommunications, there will be an emphasis on case studies in these industries. Current events in these and other industries will be analyzed with the economic framework developed in class.

---

\* Any student needing to arrange a reasonable accommodation for a documented disability should contact Disability Concerns at 350 Fell Hall, 438-5853 (voice), 438-8620 (TDD).

By the conclusion of the course, students should be able to

- understand the reasons for regulation and antitrust,
- determine when antitrust and/or regulation is an appropriate remedy,
- give the relative merits of various regulatory schemes, and
- provide a brief industry background for electricity, natural gas, and telecommunications.

## **COURSE REQUIREMENTS**

There will be 2 midterms and a final. *No make-up exams will be given unless arrangements have been made prior to the exam and approved by the instructor.* The final will be comprehensive in the sense that material from earlier in the class is needed to understand later material. The final will focus on material from the last 1/3 of the class.

Problem Sets will be given throughout the semester, usually one per week or two. Problems will include the use of spreadsheet analysis, preferably using Microsoft Excel. If you have never used spreadsheets, please seek out resources (i.e. books, people) to help you learn how to use the software. Instructional Technology regularly schedules a basic Microsoft Excel course for the fall semester.

Regular attendance is expected and class participation counts towards the final grade. A paper will be due towards the end of the semester. *The topic must be approved by the instructor in advance.*

Graduate students will have additional assignments throughout the semester and will not always be graded on the same scale as undergraduate students. Graduate students are expected to attend the *Institute for Regulatory Policy's* fall workshop. Transportation, lunch and registration will be provided. A short paper reviewing the workshop will be assigned.

Class Participation grades will be determined at the end of the semester based on the following criteria:

Points	Characteristics
50	This student always attends class, is always prepared for class and regularly makes positive major contributions to class discussion
40	This student always attends class, is mostly prepared for class and frequently makes positive major contributions to class discussion
35	This student regularly attends class, is sometimes prepared for class and occasionally makes positive major contributions to class discussion
25	This student mostly attends class, is sometimes prepared for class and occasionally makes some contribution to class discussion
10	This student misses class frequently, is sometimes prepared for class and occasionally makes some contribution to class discussion
0	This student misses class frequently, is rarely prepared for class and rarely makes a contribution to class discussion

The final grade will be based on the following point scheme:

Midterm #1	100 points
Midterm # 2	100 points
Problem Sets	100 points
Class Participation	50 points
Paper	50 points
<u>Final</u>	<u>100 points</u>
TOTAL	500 points

The following point scale will be used to evaluate your performance:

<u>Grade</u>	<u>Total Points</u>
A	450 or above
B	400 or above
C	350 or above
D	300 or above
F	less than 300

## KEYS TO SUCCESS

This course has a large volume of reading. Some of the reading is technical, focused on economic theory and some of the reading is narrative, focused on actual case studies. ***It is imperative that you read the assigned material in both areas.*** Because the class is discussion oriented, you will not maximize your classroom learning if you have not read the material in advance. In addition, ***participating in classroom discussion will help you clarify your own thinking as we review cases.*** As you listen to others' economic reasoning and express your own ideas, true learning takes place. The goal of this course is not to memorize a set of facts the night before the exam but to develop economic reasoning in the area of regulation and antitrust. This cannot be done by cramming the night before the exam!! Finally, ***do the problem set independently so that you know not only the correct answer but also how to arrive at the correct answer.*** Many exam questions will be similar to problem set questions, so view problem sets as practice exams.

If, after reading the assigned material, participating in class discussion and working independently on problem sets, you are not achieving the level of success that you expect of yourself, please come to see me regularly during office hours. My goal as your professor is to see you succeed. If you are doing your best to learn, I will do my best to help you learn.

<b>Schedule</b>		
<b>Date</b>	<b>Topic</b>	<b>Problem Set Due</b>
August 23	Why Regulate?	
August 25	Why Regulate?	
August 30	Monopoly	
September 1	Monopoly cases	
September 6	Monopoly cases	#1
September 8	Monopoly cases	
September 13	Oligopoly	
September 15	Oligopoly cases	
September 20	Merger/ Merger cases	#2
September 22	<b>Exam #1</b>	
September 27	Guest Lecture	#3 Paper Topic
September 29	NO CLASS IRPS Conf.	
October 4	Price Discrimination	
October 6	Price Discrimination cases	
October 11	Vertical Restraints	
October 13	Vertical Restraints cases	#4
October 18	Natural Monopoly	
October 20	Natural Monopoly	
October 25	Optimal Pricing	#5
October 27	Optimal Pricing	
November 1	Optimal Pricing / Review	#6
November 3	<b>Exam #2</b>	
November 8	Rate of Return Regulation	
November 10	Rate of Return Regulation	
November 15	Rate of Return Regulation	
November 17	Rate of Return Regulation	Paper Due
November 22-24	NO CLASS - THANKSGIVING	
November 29	Telecommunications	
December 1	Electricity	
December 6	Natural Gas	#7
December 8	<b>Review</b>	
Finals Week	<b>FINAL TBD Exam #3</b>	

## **COURSE OUTLINE** (Readings with \* are required)

### I. Introduction and Review

### II. Government vs. Markets

- \* VVH Chap. 1

### III. Why Regulate? /Who controls whom?

- \* VVH Chap. 2&3
- \* Posner, Richard A., "Theories of Economic Regulation," Bell Journal of Economics, Autumn 1974, pp. 335-358.
- \* Peltzman, Sam, "Toward a More General Theory of Regulation," Journal of Law and Economics, 1976, pp. 211-240.
- \* <http://www.antitrust.org/>
- \* Posner, Richard A., *Antitrust in the New Economy*, 68 Antitrust L.J. 925 (2001);
- \* Tirole, Jean, "Market Failures and Public Policy, 105(6), American Economic Review, June, 2015, pp. 1665-1682.

### IV. Monopolization

- \* VVH Chap. 4 & 9 (pp. 293-304; 332-342)
- \* Direct Testimony Of Franklin M. Fisher, U.S. vs. Microsoft, Civil Action No. 98-1232.
- \* Direct Testimony of Richard L. Schmalensee, U.S. vs. Microsoft, Civil Action No. 98-1232.
- \* Keyte, James A. and Neal R. Stoll, "Markets? We Don't Need No Stinking Markets! The FTC and Market Definition, Antitrust Bulletin, Vol. 49 No. 3, Fall 2004, pp. 593-632.
- \* Carlton, Dennis W., "Does Antitrust Need to be Modernized?" Journal of Economic Perspectives, Vol. 21 No. 3, Summer, 2007, pp. 155-176.
- JEP, Spring 2001 Symposia "The Microsoft Case"
- Waldman, Donald E., "The duPont Cellophane Case Revisited," Antitrust Bulletin, Winter 1980, pp. 805-830.

### V. Oligopoly and Collusion

- \* VVH Chap. 5-6
- \* Stigler, George J., "A Theory of Oligopoly," Journal of Political Economy Vol. 72, pp. 44-61.
- \* Carlton, Dennis W., Gustavo E. Bamberger, and Roy J. Epstein, "Antitrust and Higher Education: Was There a Conspiracy to Restrict Financial Aid?", RAND Journal of Economics, Vol. 25 No. 1., Spring 1995, pp. 131-147.
- \* Gilbert, Richard J., "E-books: A Tale of Digital Disruption," Journal of Economic Perspectives, Vol. 29 No. 3, Summer 2015.

## VI. Mergers and Acquisitions

- \* VVH Chap. 7 & 8 (pp. 235-256)
- \* Dalkir, Serdar and Frederick R. Warren-Boulton, "Prices, Market Definition, and the Effects of Merger: Staples-Office Depot," in *The Antitrust Revolution: Economics, Competition, and Policy*, (ed. by Kwoka and White), New York: Oxford University Press, 1999

## EXAM #1

## VII. Price Discrimination

- \* VVH Chap. 9 (pp. 305-331)
- \* Bowman, Ward S., "Restraint of Trade by the Supreme Court," Yale Law Journal, 1967, pp. 70-85.

## VIII. Vertical Restraints and Advertising

- \* VVH Chap. 8 (pp. 257-292)
- \* Baldwin, William L., "The Feedback Effect of Business Conduct on Industry Structure," The Journal of Law and Economics, 1969, pp. 123-144.
- \* Ahlborn, Christian, David Evans & Jorge Padilla , "The Antitrust Economics of Tying: A Farewell to Per Se Illegality," The Antitrust Bulletin, Spring 2004, pp. 287-341.
- \* Gilbert, Richard J., "Networks, Standards, and the Use of Market Dominance: Microsoft," in *The Antitrust Revolution: Economics, Competition, and Policy*, (ed. by Kwoka and White), New York: Oxford University Press, 1999

## IX. Natural Monopoly Regulation

- \* VVH Chap. 10 & 11
- \* Demsetz, H., "Why Regulate Utilities?", Journal of Law and Economics, 1968, pp. 55-65.
- \* Berg, Sanford V. and John Tschirhart, "A Market Test for Natural Monopoly in Local Exchange," Journal of Regulatory Economics, 1995, pp. 103-124.

## XI. Rate Cases and Optimal Pricing

- \* VVH Chapter 12

## EXAM #2

## XII. Rate-of-Return Regulation/Regulatory Strategies and Alternatives

- \* VVH Chap. 13 & 14
- \* Braeutigam, Ronald E. & John C. Panzar, "Effects of the Change from Rate-of-

Return to Price-Cap Regulation," American Economic Review, May 1993, pp. 191-198.

- \* Joskow, Paul and Richard Schmalensee, "Incentive Regulation for Electric Utilities," Yale Journal on Regulation, Vol. 4 1986, pp. 1-49.
- Averch, H. And L.L. Johnson, "Behavior of the Firm Under Regulatory Constraint," American Economic Review, 1962, pp. 1052-1069.
- Johnson, L.L., "Behavior of the Firm Under Regulatory Constraint: A Reassessment," American Economic Review, Vol. 63 No. 2, May 1973.

### XIII. Regulation and Fairness

- \* Zajac, Edward E., *Political Economy of Fairness*, Chapter 7, 11, 12.
- \* Loomis, David G., "The FCC Price Cap Regulation Proposal: A Fairness Analysis," October, 1989.

### XIV. Industry Studies

- \* VVH Chap. 15 & 18 (pp. 663-688)
- \* *Economic Report of the President*, Chapter 6, US Government Printing Office, 1996

#### A. Telecommunications

- \* Sappington, David E. M. and Dennis L. Weisman, "Today's Telecommunications Industry," Chapter 2 from *Designing Incentive Regulation For the Telecommunications Industry*, MIT Press, Cambridge, 1996.

#### B. Electricity

- \* Brennan, Timothy J., Karen L. Palmer, Raymond J. Kopp, Alan J. Krupnick, Vito Stagliano, and Dallas Burtraw, *A Shock to the System: Restructuring America's Electricity Industry*, Washington, DC: Resources for the Future, 1996, Chapter 1 and 2.
- \* Joskow, Paul L., "Restructuring, Competition and Regulatory Reform in the U.S. Electricity Sector," Journal of Economic Perspectives, Summer 1997, pp. 119-138.
- \* Eckert, Toby, "Unplugging the Electric Power Monopolies," Illinois Issues, January 1997, pp. 12-15.

#### C. Natural Gas

- \* Dreyfus, Daniel A., "Deregulation of Utilities: The Natural Gas Experience," Business Economics, April 1989, v. 24 n. 2, pp. 41ff.
- \* Barcella, Mary L., "Natural Gas in the Twenty-First Century," Business Economics, October 1996, v. 31 n. 4, p. 19ff.

### FINAL EXAM