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ANTITRUST POLICY AND INEQUALITY OF WEALTH



BY HERBERT HOVENKAMP ¹



All public policies have consequences for the distribution of wealth. Caps on punitive damages in tort law make tort plaintiffs poorer and tort defendants wealthier. Fines for speeding make speeders poorer and state treasuries wealthier. For most legal policy, however, wealth distribution is not a primary or even an explicit goal. Further, the consequences are typically quite random in relation to social class or economic status. For example, fining speeders may not hit one particular economic group harder than another unless poorer people are either more or less likely to speed. Caps on medical malpractice awards may injure those who are sicker or more likely to be injured, but whether this group of victims is poorer or wealthier than society as a whole is hard to say.

Special interest legislation can distribute wealth more explicitly, because often its actual although often unstated goal is to benefit one particular interest group. Antitrust law's Robinson-Patman Act is an example of this.² It was intended to protect small grocers from the rise and development of vertically integrated chain stores such as A&P.³ The intended beneficiaries were small stores. Other victims, perhaps unintended or at least unmentioned, were consumers who would have to pay higher prices. Of course, the supporters of the statute did not articulate its goals as harming consumers with higher prices.

Antitrust law unquestionably affects wealth distribution. Rigorous antitrust enforcement can make condemned price-fixers and monopolists worse off, while benefitting their customers or sometimes competitors. Once again, however, these wealth transfers are not systematically from the rich to the less rich or vice-versa. For example, cartel members need not be rich firms. Many small, family owned companies that produce things such as milk or cement have been prosecuted for price fixing.⁴ Further, cartels often form precisely because the cartel members are losing money as a result of adverse shifts in their industry. The long history of railroad collusion bears this out, but it has shown up in other markets as well.⁵

¹ James G. Dinan University Professor, Penn Law and Wharton Business, University of Pennsylvania. Thanks to Erik Hovenkamp for commenting on a draft.

² 15 U.S.C. §2 (as amended in 1936).

³ See Hansen, *Robinson-Patman Law: A Review and Analysis*, 51 *FORDHAM L. REV.* 1113 (1983); Rowe, *The Evolution of the Robinson-Patman Act: A Twenty-Year Perspective*, 57 *COL. L. REV.* 1059 (1957).

⁴ See Lanzillotti, *The Great School Milk Conspiracies of the 1980s*, 11 *REV. INDUS. ORG.* 413, 440 (1996) (cartels of relatively small dairies); *United States v. Vandebrake*, 679 F.3d 1030 (8th Cir. 2012), cert. denied, 133 S.Ct. 1457 (2013) (cartel of small ready-mixed cement companies).

⁵ HOVENKAMP, *ENTERPRISE AND AMERICAN LAW, 1780-1860* at 313 (1991); Hovenkamp, *Regulatory Conflict in the Gilded Age: Federalism and the Railroad Problem*, 97 *YALE L.J.* 1017 (1988). Other markets have exhibit similar situations. See, e.g. *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 220-221 (1940) (collusion resulting

Why would someone want to use the antitrust laws as a wealth distribution device when far more explicit statutory tools are available for that purpose, including tax law, minimum wage laws, welfare laws and Medicaid, to name a few? One feature of antitrust is its very open-textured, nonspecific statutes that are interpreted by judges. For example, Section 1 of the Sherman Act condemns conduct that “restrains trade,” while the substantive provisions of the Clayton Act reach conduct that “may substantially injure competition,” but leaving all of these terms undefined. The process of definition has been left to the courts. As a result, using antitrust to redistribute wealth may be a way of using the judicial process without having to go to Congress or a state legislature that is likely to be unsympathetic. Of course, a corollary of that position is that someone attempting to use antitrust law to redistribute wealth is going to have to rely on the existing antitrust statutes rather than obtaining a new antitrust provision that is more explicitly distributive. If that is the case, then the question is whether Sections 1 and 2 of the Sherman Act or Sections 3 or 7 of the Clayton Act in their current form are useful wealth distribution tools.

One possible lever for redistributive antitrust is a link between market competitiveness and wealth equality. Some literature suggests that competitive markets are conducive to the more even distribution of wealth.⁶ To the extent this is true we might use antitrust to equalize wealth distribution simply by making markets more competitive. Of course, the antitrust laws already have a generally agreed upon goal of increasing competition. The most defensible goal for the antitrust laws is prohibition of practices that serve to reduce output anticompetitively, which is simply a statement of the consumer welfare principle. An output reduction is anticompetitive if its profitability depends on the higher margins.

The same thing is true about the use of antitrust to protect jobs. In general, increased employment results from either higher output, which requires more labor; or else inefficiency, which requires more labor per unit of output. Antitrust encourages greater employment by promoting increased output, but not by decreasing efficiency.

For a long time people have debated the merits of two different welfare goals for the antitrust laws: “general” welfare and “consumer” welfare.⁷ General welfare is the ordinary measure that neoclassical economists use to talk about the economy. It calculates the amount of welfare (surplus) enjoyed by everyone, not only consumers and producers, but also competitors, employees, and anyone else who is affected. The general welfare test may approve some practices that harm consumers, provided that the benefit to producers (and others) is greater than consumer losses. For example, suppose a merger results in a price increase that injures consumers in the aggregate by \$100,000,000, but also produces production efficiencies of \$120,000,000 that accrue to the merging parties and are not passed on via lower prices. That merger is general welfare increasing, because producers are benefitted by a greater amount than consumers are injured.

Under a consumer welfare standard this merger would be condemned, however, because consumers are harmed and we do not count the benefits to producers. This strikes some people as wrong, but I believe it is the best approach to antitrust analysis and the only one that is capable of reasonable implementation. The arguments for an antitrust consumer welfare approach are of three general kinds – those derived from legislative history, those derived from principle and those derived from administrative concerns. The legislative history makes a weak case for consumer welfare, but as between consumer welfare and general welfare the former is a clear winner. Second, the arguments from principle do not get us anywhere because they are very sensitive to assumptions. Third, the arguments from administrability strongly favor a consumer welfare approach. Finally, however, as a practical matter selection of a standard as between general and consumer welfare rarely makes a difference, certainly not often enough to justify the greatly increased cost of antitrust analysis under a general welfare standard.

from excess capacity and distress in oil industry); *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 273 (6th Cir. 1898) (similar; cast iron pipe). Cf. *United States v. Apple, Inc.*, 791 F.3d 290, 332 (2d Cir. 2015), cert. denied, 136 S. Ct. 1376 (2016) (speaking of ruinous competition in book industry); *General Cinema Corp. v. Buena Vista Distribution Co., Inc.*, 532 F.Supp. 1244 (C.D.Cal. 1983) (rejecting ruinous competition defense to market division agreements in motion picture screening).

6 See Khan & Vaheesan, *Market Power and Inequality: the Antitrust Counterrevolution and its Discontents*, 11 HARV. L. & POL'Y REV. 235 (2017); Baker & Salop, *Antitrust, Competition Policy, and Inequality*, 104 GEO. L.J. 1 (2015).

7 See Dameron, *Present at Antitrust's Creation: Consumer Welfare in the Sherman Act's Statutory Forerunners*, 125 YALE L.J. 1072 (2016); Hovenkamp, *Implementing Antitrust's Welfare Goals*, 81 FORDHAM L. REV. 2471 (2013); Alan J. Meese, *Debunking the Purchaser Welfare Account of Section 2 of the Sherman Act: How Harvard Brought Us a Total Welfare Standard and Why We Should Keep It*, 85 N.Y.U. L. REV. 659, 690-98 (2010).

First, a fair reading of the legislative history of the Sherman Act suggests that it was dominated by two concerns. One is high prices and the other is protection of smaller competitors from what was regarded as the emerging threat of large businesses, or trusts.⁸ Neither of these concerns strongly suggests a general welfare approach. The concern with higher prices is at least consistent with a consumer welfare concern. Further, the legislative history of the Clayton Act (1914), Robinson-Patman Act (1936), and the Celler-Kefauver Amendments to the merger statute (1950) indicate that to the extent Congressional concerns changed over time it was in the direction of greater concern for the protection of smaller rivals.⁹

The framers of the Sherman Act clearly did not want to punish someone for being more efficient than rivals. For example, they praised and would have exonerated the rancher who was better than anyone else at producing shorthorn cattle, and thus got the “whole business.”¹⁰ But that is hardly the same as supporting a general welfare test. A general welfare test has its bite in situations where consumers are actually injured, whether by higher prices or lower quality, but this injury is more than offset by producer gains. That is hardly the situation when someone gets the whole business by being better than anyone else. Someone does that by benefitting rather than injuring consumers, and nothing in the legislative history account suggests to the contrary. Someone who got the whole business of producing shorthorn cattle because he was better than everyone else was hardly injuring consumers.

Second, the arguments from principle are based mainly on standard models of neoclassical economics, such as Pareto efficiency or Kaldor-Hicks efficiency,¹¹ that measure the efficiency of an economy but purport to be indifferent to how wealth is distributed. These models are valuable for the function that they perform, which is to measure the economy’s overall efficiency. Whether they are the best models for assessing the legality of competitive behavior is a different question.

Bork famously used the term “consumer welfare” when he really meant “total surplus,” which is general welfare.¹² Bork generally assumed that what drives economic assumptions about efficiency is its benefits to consumers. To the extent that is true, there is very little tension between a general welfare and a consumer welfare test for antitrust policy. Bork’s efficient producer is the legislative history’s producer of shorthorn cattle, who “got the whole business” because no one could do it better than he could.¹³ Importantly, that piece of legislative history was discussing superior performance by a single actor. It was not discussing mergers, which can present different issues.

In his highly influential “welfare tradeoff” model, Oliver E. Williamson essentially set competition policy scholars off on a wild goose chase looking for practices such as mergers or joint ventures that simultaneously injure consumers while producing efficiencies that exceed consumer losses. In one of the most storied portrayals in antitrust economics, Williamson illustrated a merger that increased prices but also led to productive efficiencies. He then showed how the size of the efficiencies could exceed that of the consumer losses from the price increase.¹⁴

In the subsequent literature, this welfare tradeoff conception became the norm for thinking about efficiencies. In fact, most of the “general welfare” vs. “consumer welfare” debate since that time has swirled around it by focusing on what we should do when a practice produces both productive efficiency gains to producers and allocative efficiency losses that

8 See, e.g. Bork, *Legislative Intent and the Policy of the Sherman Act*, 9 J.L. & ECON. 7 (1966) (general welfare); Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: the Efficiency Interpretation Challenged*, 34 HASTINGS L.J. 65 (1982) (consumer welfare); Stigler, *The Origin of the Sherman Act*, 14 J. LEGAL STUD. 1 (1985) (small business protectionism); HOVENKAMP, *THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION*, ch. 2 (2005) (small business protectionism).

9 For a summary, see HOVENKAMP, *FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE*, Ch. 2 (5th ed. 2015).

10 See 21 Cong. Rec. 3151-3152 (1890) (exchange among Senators Kenna, Edmunds and Hoar concluding that the statute’s monopolization provision would not condemn someone who “got the whole business because nobody could do it as well as he could. . .”).

11 A state of affairs is Pareto efficient if no change can benefit someone without making at least one other person worse off. A state of affairs is Kaldor-Hicks, or “potential” Pareto efficient even if it produces both gainer and losers, but only if the gainers gain enough fully to compensate the losers, leaving them indifferent.

12 Bork, *Legislative Intent*, supra note 8 at 10; and see Ginsburg, *Legislative Intent and the Courts*, 71 ANTITRUST L.J. 941, 942 & n. 11 (2014) (collecting sources).

13 Bork relies on this passage in BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 12, 28-31, 138 (1978). See Hovenkamp, *Distributive Justice and the Antitrust Laws*, 51 GEO. WASH. L. REV. 1, 18 (1982).

14 Williamson, *Economies as an Antitrust Defense: the Welfare Tradeoffs*, 58 AM. ECON. REV. 18, 21 (1968).

accrue to consumers. The answer under the general welfare approach is that we condemn the practice only if the productive efficiency gains are smaller than the consumer losses. The answer under the consumer welfare approach is that we condemn the practice whenever consumer harm has occurred and we do not offset the gains in productive efficiency.

But this entire “welfare tradeoff” debate depends on the existence of a non-empty, verifiable set of instances in which a practice simultaneously injures consumers by reducing output and benefits producers by yielding productive efficiencies. Without denying that such situations occur, the fact is that in 125 years of antitrust litigation, no American court has yet identified one. In virtually every case where a practice has been proven to yield efficiencies it has also been shown to leave consumers unharmed – or perhaps to say it more accurately, it has not been shown to harm them.

Welfare tradeoff modeling appears most frequently in analysis of horizontal mergers. The reason is not hard to identify: mergers have a tremendous capacity to cause significant changes in market structure in a short period of time. The union of two relatively large firms can threaten the immediate creation of market power. Offsetting this, the same union can do a number of things that reduce production costs or improve product quality. Given the amount of merger litigation and the legal and economic resources poured into it, we should have a relatively substantial database of cases requiring tradeoff. But in fact we do not, even though the so-called efficiency defense is raised in a high percentage of litigated merger cases. Courts sometimes cite efficiencies as justifying a merger after holding that the merger is not anticompetitive, meaning that there was no consumer harm.¹⁵ They also sometimes dismiss efficiency claims after finding that the merger is anticompetitive.¹⁶ One thing they have not done, however, is identified a merger that both reduced output and raised prices, but that produced offsetting efficiencies that were thought sufficient to justify it.

The only cases where the choice of a welfare standard makes a difference are when the challenged practice, whether merger or otherwise, actually reduces output. The biggest efficiency gains to come from challengeable antitrust practices such as mergers is economies of scale, but except in idiosyncratic situations these are achieved under higher, not lower, output. The set of efficient but output reducing practices is not necessarily empty, but it is probably not very large. I am not aware of a single antitrust decision in the United States in which a court has found actual consumer harm from reduced output or higher prices, but then went ahead to approve the practice because producer gains exceed consumer losses.¹⁷ In sum, once all the facts are known it is virtually never necessary to apply the welfare tradeoff model, because there is nothing to trade off.

The third consideration is administrability. How we assess situations in which both consumer harm and efficiency gains are possible depends critically on which measure of welfare we choose. Under a general welfare test, consumer losses would first have to be quantified fairly precisely, at least in close cases. This is true because their size needs to be measured against the size of any efficiency gains that accrue to producers. Consumer losses consist of two parts. First is the output reduction and the amount of lost consumer surplus that each lost unit represents. This loss is depicted by the “deadweight loss” triangle in the standard monopoly graph. So making that measure requires a fact finder to know the size of the output reduction and the size of the surplus that each lost unit represents. The other part of consumer losses accrues to those customers who stay in the market but pay a higher price. Their loss, roughly estimated in antitrust damages actions, is the number of units consumers actually purchase during the monopoly/cartel period multiplied by the price increase. As a general matter, we need not worry about these consumer losses under a general welfare test, because they are precisely offset by producer gains.¹⁸

15 E.g. *United States v. Carilion Health Sys.*, 707 F.Supp. 840 (W.D. Va. 1989), *aff'd mem.*, 892 F.2d 1042 (4th Cir. 1989) (finding efficiencies, but also that government failed to prove its structural case).

16 *Saint Alphonsus Medical Center-Nampa, Inc. v. St. Luke's Health sys., Ltd.*, 2014 WL 407446 (D.Id. Jan. 24, 2014), *aff'd*, 778 F.3d 775 (9th Cir. 2015); *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 721-722 (D.C. Cir. 2001).

17 Canadian antitrust law, which adopts a total welfare approach, includes one widely debated decision, *Comm'r of Competition v. Superior Propane, Inc.*, (2003) 23 CPR (4th) 316 (FCA) (approving a merger of producers of liquefied gas because, while it led to reduced output and higher prices, efficiency gains more than offset these losses). For commentary, see Neher, Russo & Zona, *Lessons from the Superior-ICB Merger*, 12 GMU L. REV. 289 (2003); Gifford & Kudrie, *Rhetoric and Reality in the Merger Standards of the United States, Canada, and the European Union*, 72 ANTITRUST L.J. 423 (2005); Zerbe, Jr. & Knott, *An Economic Justification for a Price Standard in Merger Policy: the Merger of Superior Propane and ICG Propane*, 21 REC. L. & ECON. 409 (2004).

18 For a graphic and more detailed explanation, see Hovenkamp, *Progressive Antitrust*, ___ ILL. L. REV. ___ (2018) (forthcoming), available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2892336.

Under a general welfare test, consumer losses would have to be offset against the productive efficiency gains that accrue to producers. In the simplest cases where the product is not changed but production costs are lower, these would be assessed as the cost savings per unit. That would require the fact finder to discover how many units per time period the firm produced and how much were the efficiency-induced cost savings on each unit. If efficiency gains show up in other ways, such as improvements in product quality, this calculation would be more difficult because some value would have to be put on the quality increase.¹⁹ For example, if a merger led to both higher prices and an improved product, someone would have to be able to calculate how much of the price increase is a consequence of the output reduction and how much is a function of consumer response to a better product.

By contrast, under a consumer welfare test the fact finder need answer only one question: has output been reduced? We need not know the amount, as long as we can determine that there was a non-trivial output reduction. So if the output consists in a decline in product quality rather than number of units, the fact finder need not measure the decline but only identify that it has occurred. Once we know that output has declined and can infer that this happened for an anticompetitive reason, then we know that there is consumer harm. Of course, damages measurement in a private plaintiff action would still require consumer losses to be quantified, as we already do in damages actions for price fixing.²⁰

In sum, assessing welfare losses under a consumer welfare test is much, much easier than under a general welfare test. In fact, assessing effects under a general welfare test in a moderately close case would be heroic. Considering administrability, the best choice for a welfare standard for antitrust is consumer welfare as measured by output.

That then leaves one question pertaining to wealth inequality. Suppose we start out with the premise that antitrust harm consists in a market-power-driven output reduction. Accepting that competitive markets are conducive to greater wealth equality, hasn't antitrust already done all it can do? To ask the question somewhat differently, are there any situations that warrant antitrust intervention on distributive grounds even though intervention would push market output lower rather than higher?

One case that comes to mind as an example is *Brown Shoe*, where the Supreme Court gave effect to a district court decision that condemned the Brown-Kinney Shoe merger precisely because the merger would lead to lower prices, and these would put increased pressure on smaller, independent shoe sellers who were already struggling.²¹ We might take the same approach with the Amazons of the twenty-first century world – condemn their actions precisely because their lower prices attract so many consumers that smaller competitors might be unable to survive.²²

There are a couple of things worth noting about this approach. First, it clearly injures rather than benefits consumers. They are being robbed of the larger firms' lower prices. Second, there is no obvious way of limiting its application. Should antitrust condemn every practice that reduces the defendant's prices or costs, or improves the quality of its product when rivals are injured or suppliers are worse off? That policy would rather quickly drive the economy back into the Stone Age, imposing hysterical costs on everyone. To be sure, there might be ways of limiting the rule. For example, we might say that lower prices or higher quality ought to be condemned only when it creates or threatens to create a monopoly. That approach might not be quite as bad, but it would be a strong barrier to innovation, and particularly to market shifting innovations that result in dominant firms. There would go Ford, Bell, IBM, Kodak, Polaroid, Xerox, Microsoft, Google, Apple and numerous others.

19 Ibid.

20 Damages actions based on an overcharge would not require measurement of efficiency gains *per se*. However, to the extent that efficiency gains reduced the size of the overcharge damages would be correspondingly reduced. See HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE §17.5 (5th ed. 2016).

21 *United States v. Brown Shoe*, 179 F. Supp. 721, 738 (E.D.Mo. 1959), aff'd, 370 U.S. 294 (1962) (approving district court decision that merger was bad because it led to "lower prices or higher quality for the same price," and thus injured small rivals).

22 E.g. Khan, *Amazon's Antitrust Paradox*, 126 YALE L.J. 710 (2017).

Finally, it is hardly clear that this antitrust policy of condemning firms that produce lower prices or higher quality than their rivals would yield a more attractive distribution of wealth than a policy of simply encouraging maximum, competitive output. To be sure, stockholders of the target of an antitrust prosecution would be worse off. The less competitive rivals who no longer have to compete with lower prices or better products will be better off, but without knowing something about their starting position there is no reason to classify them as relatively “poor” and the antitrust defendant as “wealthy.” Indeed, often highly innovative firms are relatively young upstarts facing older money and established technology. For example, one of Amazon.com’s principal targets – most likely to be injured by the *Amazon/Whole Foods* merger – is Wal-Mart, which is substantially owned by the wealthiest family in the United States.²³

Much the same thing is true of impact on employment. One component in the antitrust attack on Amazon, as well as other tech firms, is that they are job killers, and that this should be an antitrust problem. As a matter of historical fact, these complaints have surfaced time and again when market shifting technologies were introduced and have always proved wrong. Second, a policy of facilitating higher output almost always produces more jobs. For example, to the extent that Amazon sells products designed and produced by others, the effect of its lower prices is simply higher output, which is conducive to greater employment.

One thing that does not necessarily produce more jobs, at least in the short run, is increased productive efficiency, which can result in higher output with less labor. Should we have a goal of condemning efficient practices that result in job-reducing labor savings? As a matter of principle, I believe the answer is a robust no. As a matter of management, antitrust is a very poor tool for preserving jobs by making production less efficient. We would do that much more effectively by limiting productive efficiency directly. For example, we could amend the Patent Act so as to deny patents to things whose deployment threatens reduced need for labor. Or perhaps we should have a policy of simply identifying labor saving technologies directly and limiting their deployment. Antitrust reaches these technologies only indirectly because it reaches only the practices that are challengeable under the antitrust laws, and even then only when they limit competition. Just stating the alternatives, however, should suggest how ridiculous they are as a matter of policy.

Another alternative is that we might decide that the low prices charged by Amazon or other very large firms are a temporary illusion. Perhaps Amazon is engaging in predatory behavior by charging very low prices today and intends to recoup monopoly profits later. Or perhaps it is exercising monopsony power by suppressing buying prices. If these things occur then antitrust can be brought to bear. But such claims need to be more than asserted as an abstract proposition. They need to be proven. The law of predatory pricing is designed to identify instances in which predatory pricing is a plausible strategy.²⁴ We might dispute the correctness of those legal rules, but that dispute occurs equally among those who believe general welfare or consumer welfare should be the guiding antitrust principle. In the case of Amazon, almost nothing about its market positions suggests that it would be able to sustain monopoly pricing without producing so much consumer defection or competitor entry that the price increase would be unprofitable.

And what about the complaint that Amazon engages in monopsony buying, forcing its suppliers to sell to it at anticompetitively low prices? The telltale sign of monopsony is suppression of output, something that requires both market power in the purchasing market and evidence that the buyer is seeking to keep market wide output down. In hard, competitive bargaining a buyer obtains lower prices by getting a better deal, often by increasing the amount purchased. By contrast, a monopsonist forces buying prices down by limiting market-wide purchases. That is, monopsony, just as monopoly, is an output reducing strategy. On casual observation, that hardly seems to be true of Amazon.²⁵

23 The Walton family, which owns roughly half of Wal-Mart. See: <https://www.forbes.com/profile/walton-1/>.

24 See 3A AREEDA & HOVENKAMP, ANTITRUST LAW, Ch. 7C (4th ed. 2015).

25 See BLAIR & HARRISON, MONOPSONY IN LAW AND ECONOMICS (2011); HOVENKAMP, FEDERAL ANTITRUST POLICY, note 19, §1.2b (5th ed. 2016).

Finally, the one class of people that would clearly be injured by a policy of advocating lower output on distributional grounds is consumers. They would pay higher prices. Other losers include employees whose jobs would disappear in a lower output market; creditors, landowners, tax authorities, distributors and retailers, all of whom face reduced business when output goes down.²⁶ In sum, it seems unlikely that a policy of condemning firms who charge lower prices or produce higher quality goods would yield a distribution of wealth any more desirable than a policy of maintaining high output by condemning anticompetitive restraints.

²⁶ While all of these various groups would be injured, most are denied standing to sue for an antitrust violation because their injuries are considered “derivative.” See 2A AREEDA & HOVENKAMP, ANTITRUST LAW ¶¶350-353 (4th ed. 2014).

