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Antitrust: What Counts as Consumer Welfare?

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Introduction

The antitrust laws speak in unmistakably economic terms about the conduct they prohibit. The Sherman Act is directed toward conduct that "restrains trade" or "monopolizes" markets.[1] The Clayton Act prohibits conduct whose effect may be substantially to "lessen competition" or "tend to create a monopoly."[2] Even so, economic effects can be measured in different ways. The dominant view of antitrust law today is its rules should be based on a "consumer welfare" principle. We assume that consumers are best off when prices are low. Dissenters on the right would include seller profits in their conception of consumer welfare. Those on the left would expand antitrust to incorporate political goals, pursue large firm size or industrial concentration for its own sake, or include effects such as wealth or social inequality.

A statement released by the Biden-Sanders Unity Task Force in July, 2020, speaks about the need for greater antitrust enforcement in several areas.[3] It expresses concern about health care mergers that raise price, an acknowledged problem that clearly falls within the consumer welfare principle.[4] It does the same thing for

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[1] 15 U.S.C. §1 (prohibiting contracts, combinations, or conspiracies in restraint of trade); 15 U.S.C. §2 (prohibiting those who monopolize or attempt to monopolize commerce).

[2]All three substantive antitrust sections of the Clayton Act prohibit the conduct they cover when it threatens to "substantially … lessen competition or tend to create a monopoly." See 15 U.S.C. §13 (price discrimination); 15 U.S.C. §14 (tying and exclusive dealing); 15 U.S.C. §18 (mergers).

[3]Biden-Sanders Unity Task Force Recommendations (July 8, 2020), available at https://joebiden.com/wp-content/uploads/2020/07/UNITY-TASK-FORCE-RECOMMENDATIONS.pdf.

[4] *Id*. at 33.

anticompetitive outcomes in agricultural processing.[5] More problematically, it would "Charge antitrust regulators with systematically incorporating broader criteria into their analytical considerations, including in particular the impact of corporate consolidation on the labor market, underserved communities, and racial equity."[6] It also speaks of reversing the impact of Trump-administration mergers "to repair the damage done to working people and to reverse the impact on racial inequity."[7]

The temptation to use antitrust to achieve broader goals is understandable. The broad and brief language of the antitrust laws incorporate an elastic mandate and is directed at the courts. They can become a vehicle for achieving goals through the judicial system that are more difficult to achieve legislatively. By contrast, the consumer welfare principle is a way of limiting the scope of antitrust to a set of economic goals with consumers identified as the principal beneficiaries.

Most descriptions of the consumer welfare principle refer to prices: the goal of the antitrust laws should be to combat monopolistic prices. Articulating the goal in this way raises conceptual problems when we think about suppliers. For example, the antitrust concern with labor is with wage suppression, which means that wages are anticompetitively low. This can collide with a common misperception, which is that low wages invariably produce low consumer prices.

One thing that buyers and sellers have in common, however, is that both are injured by anticompetitive output reductions. Price and output move in opposite directions. While monopoly involves prices that are too high and monopsony (monopoly buying) involves prices that are too low, both require lower output. As a result, when consumer

[5]*Id*. at 52, 68.
[6]*Id*. at 67.
[7]*Id*. at 74.

welfare is articulated in terms of output rather than price, it protects both buyers and sellers, including sellers of their labor.

There are other reasons for preferring output rather than price as the primary indicator of consumer welfare. In most markets, firms have more control over output than they do over price. This is most true in competitive markets, although it is less true as markets are more monopolized. A seller in a perfectly competitive market lacks any control over price bu t usually has full control over output. A corn farmer cannot meaningfully ask "what price should I charge" for this year's crop. She will charge the market price. While she has the power to charge less, she has no incentive to do so because she can sell all she produces at the market price. The one absolute power she does have, however, is to determine output. The decision whether to plant 1000 acres in corn, 500, 100 acres or even zero is entirely hers and depends only on her capacity to produce.

The consumer welfare principle in antitrust is best understood as pursuing maximum output consistent with sustainable competition. In a competitive market this occurs when prices equal marginal cost. More practically and in real world markets, it tries to define and identify anticompetitive practices as ones that reduce market wide output below the competitive level. Output can go higher than the competitive level, but then at least some prices would have to be below cost. As a result, the definition refers to "sustainable" but competitive levels of output. If output is too high some firms will be losing money and must eventually raise their prices or exit.

Consumer welfare measured as output serves the customer's interest in low prices and also in markets that produce as wide a variety of goods and services as a competition can offer. It also serves the interest of labor, which is best off when production is highest. Concurrently, it benefits input suppliers and other participants in the market process. For example, if the output of toasters increases, consumers benefit from the lower prices. Labor benefits because more toaster production increases the demand for labor. Retailers, suppliers of electric components, shipping companies, taxing authorities and virtually everyone with a stake in the production of toasters benefits as well.

Antitrust is a microeconomic discipline, concerned with the performance of individual markets rather than the economy as a whole. It is worth noting, however, that a goal of high output in a particular market contributes to a well-functioning overall economy. For example, macroeconomic measures such as GDP are based on the aggregate production of goods and services in the entire economy under consideration. All else being equal, when a particular good or service market experiences larger competitive output the overall economy will benefit as well.[8] That issue would almost never be relevant in any particular antitrust case, but it can be important at the legislative or policy level. Increasingly people have observed a link between competition policy – particularly high price-cost margins – and the performance of the economy as a whole.[9]

What is not included in consumer welfare under the antitrust laws? First, bigness itself is not an antitrust issue unless it leads to reduced output in some market. That is, the consumer welfare principle is consistent with very large firms. It favors economies of scale and scope.[10] To be sure, very large firms can injure small firms

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[8] For a good introduction to these issues, *see* JOHN BELLAMY FOSTER AND ROBERT W. MCCHESNEY, THE ENDLESS CRISIS: HOW MONOPOLY-FINANCE CAPITAL PRODUCES STAGNATION AND UPHEAVAL FROM THE USA TO CHINA (2017).

[9]For good commentary, *see* Jonathan B. Baker, *Overlapping Financial Investor Ownership, Market Power, and Antitrust Enforcement: My Qualified Agreement with Professor Elhauge*, 129 HARV. L. REV. FORUM 212, 219-225 (2016); Anna Gelpern & Adam J. Letivin, *Considering Law and Macroeconomics*, 83 L. & CONTEMP. PROBS. i (2020); Chad Syverson, *Macroeconomics and Market Power: Context, Implications, and Open Questions*, 33 J. ECON. PERSP. 23 (2019) Tay-Cheng Ma, *Antitrust and Democracy: Perspectives from Efficiency and Equity*, 12 J. COMP. L. & ECON. 233 (2016).

[10] An economy of scale is a cost that declines as a firm produces a larger amount. An economy of scope is a cost that declines as someone produces a

that have higher costs or lower quality products. The impact of the consumer welfare principle on small firms is complex, however, and requires close analysis of individual cases. While small competitors of a large low cost and high output firm can be injured, many other small firms benefit, including suppliers and retailers. A good illustration is Amazon, which is a very large firm that generally sells at low prices and has maintained high consumer satisfaction.[11] Amazon has undoubtedly injured many small firms forced to compete with its prices and distribution. At the same time, however, Amazon acts as broker for millions of small firms who use its retail distribution services.[12] When a very large firm produces more, it creates opportunities for other firms that sell complements, that distribute the products that a large firm produces, or that supply it with inputs. So once again it is important not to paint with too broad a brush. Blowing up Amazon could ruin many small businesses.

As for labor and antitrust, that relationship is also complex and has changed over time. During the early years of Sherman Act enforcement organized labor was widely believed to be a source of monopoly. Many of the earliest antitrust criminal prosecutions were directed at labor unions.[13] For example, Eugene Debs went to prison in 1895 as a result of a conviction under the Sherman Act.[14] Congress

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larger variety of products, or in a larger number of places. For example, because of joint costs a firm might be able to produce toasters and space heaters out of the same plant more cheaply than two firms that each produced one of the two products.

[11]*See* Jon Markman, How Amazon.com Remains the Ruler of Retail, FORBES (Jan. 30, 2020) (Amazon #1 in consumer satisfaction for three consecutive years).

[12]For statistics, see https://www.feedbackexpress.com/amazon-1029528-new-sellers-year-plus-stats/#:~:text=Amazon%20US%20stats,and%20more%20than%2060%20countries. (last visited July 20, 2020) (noting that Amazon has 5 million independent sellers, with 1.7 million currently listing products for sale).

[13]*See, e.g.*, Herbert Hovenkamp, *Labor Conspiracies in American Law*, 66 TEX. L. REV. 919 (1988).

[14]*See in re* Debs, 158 U.S. 564, 596-600 (1895); and Hovenkamp, *Labor Conspiracies*, *id*. at 920.

came to labor's rescue during the New Deal,[15] and the result was the development of a complex labor immunity that today reaches even agreements among employers, provided that they are part of the collective bargaining process.[16]

But years of anti-union activity largely deprived the unions of the economic power and turned the tables. Most of the antitrust concerns about labor today are with anticompetitive practices that suppress wages, not with worker power to extract higher wages.[17] Agreements among employers not to hire away one another employees ("anti-poaching" agreements) are unlawful per se.[18] Today a fair amount of litigation is directed at overly broad use of labor noncompetition agreements, which are formally vertical but subject to antitrust attack when they are used by many firms in a market to impede worker mobility.[19]

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[15]*Id*. at 928, 929, 962.

[16]Brown v. Pro Football, Inc., 518 U.S. 231 (1996) (extending labor antitrust immunity to agreement among multiple NFL team owners involved in collective bargaining). *See* 1B PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶¶255-257 (5th ed. 2020).

[17]*See* Ioana Marinescu and Herbert Hovenkamp, *Anticompetitive Mergers in Labor Markets*, 94 IND. L.J. 1031 (2019); Herbert Hovenkamp, *Competition Policy for Labour Markets*, OECD Directorate for Financial and Enterprise Affairs (5 June 2019), available at https://one.oecd.org/document/DAF/COMP/WD(2019)67/en/pdf. *See also* Suresh Naidu, Eric Posner & E. Glen Weyl, *Antitrust Remedies for Labor Market Power*, 132 HARV. L. REV. 537 (2018).

[18]*See* the Justice Department's statement, "No More No-Poach: The Antitrust Division Continues to Investigate and Prosecute "No Poach" and wage-Fixing Agreements," available at https://www.justice.gov/atr/division-operations/division-update-spring-2018/antitrust-division-continues-investigate-and-prosecute-no-poach-and-wage-fixing-agreements#:~:text=When%20companies%20agree%20not%20to,compete%20for%20those%20employees'%20labor.&text=Naked%20no%2Dpoach%20and%20wage,product%20prices%20or%20allocate%20customers. (spring 2018).

[19]*E.g.*, Deslandes v. McDonald's USA, LLC, 2018 WL 3105955 (N.D. Ill. June 25, 2018) (parallel use of noncompetition agreements among

Are there situations in which a practice that the consumer welfare principle would approve might nevertheless harm labor? Yes, when the practice in question reduces the demand for labor as a result of cost savings rather than a decrease in output. Consider the merger between Chrysler and Jeep, two producers of automobiles.[20] The merger was small as automobile mergers go and was lawful under the antitrust laws. Nevertheless, a likely result of such a merger would be consolidation of dealerships and some elimination of duplicate jobs. After the merger it is cheaper for Chrysler and better for consumers if Chryslers and Jeeps are sold through a common dealership. Sales and service can be performed by a common staff, reducing the number of employees to less than the number required by two separate facilities. At the same time, however, the overall automobile market remains competitive on both the consumer side and the input (labor) side. To the extent this consolidation reduces Chrysler/Jeep's costs, output of automobiles would go up.

Consolidations can reduce the demand for labor even though the firms could not possibly injure competition in any market. For example, if two pediatricians in New York City should form a partnership they might decide to share a single secretary or assistant. A job would be eliminated, but without any competitive harm to any market. So the consumer welfare principle does not condemn every practice that reduces the demand for labor, but only those practices that do so monopolistically, by suppressing the demand for labor rather than by reducing the amount of it that a firm needs. It is not antitrust's purpose to subsidize employment by requiring firms to use employees that they do not need. The merger that reduces the demand for labor through efficient consolidation is no different in principle than any

McDonald's franchsees). *See* HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE §4.1d (6th ed. 2020).

[20]The acquisition, which occurred in 1987, was with American Motors, which at that time had already acquired Jeep. See "Chrysler is Bying American Motors," NEW YORK TIMES (March 10, 1987), available at https://www.nytimes.com/1987/03/10/business/chrysler-is-buying-american-motors-cost-is-1.5-billion.html.

other production change that requires less labor – for example, when a manufacturer shifts from a labor intensive assembly process to a more automated one that requires fewer employees.

If we really wanted to protect jobs from all changes that reduce the demand for employment we would do better to change the patent laws rather than antitrust law. Changes in technology almost certainly have greater and more explicit effects on labor than do mergers or other procompetitive antitrust practices. For example, a "Job Protection from Innovation Act" might provide that patent applications must show as a condition of patentability that their invention will not lead to a loss of jobs. No one advocates for such a statute because its economically harmful implications are too clear.

Distinguishing pro- from anti-competitive reductions in labor is not always easy. Most of the time the difference can be inferred from market structure. For example, if two small firms in a large field merge and eliminate a certain number of duplicate jobs, the reason is highly likely to be more efficient use of resources. As the employee-side market share of the two firms becomes larger, however, anticompetitive explanations become more plausible. Then it becomes necessary for a tribunal to investigate whether efficient consolidation or inefficient labor suppression is going on.[21]

[21]*Cf*. United States v. Anthem, Inc., 855 F.3d 345, 371-374 (D.C.Cir. 2018) (then Circuit judge Kavanaugh, dissenting, noting dispute about whether lower provider rates result from hospital merger would result from increase efficiency or anticompetitive suppression of input prices). *See also* Elena Prager & Matthew Schmitt, *Employer Consolidation and Wages: Evidence from Hospitals* (SSRN working paper Jun 2019), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3391889 (citing evidence that hospital mergers in concentrated markets can result in wage suppression for employees such as nurses and that the dominant explanation if employer power over labor).

Getting to Consumer Welfare

Antitrust policy has not always articulated a consumer welfare principle. It is largely a creature of the 1960s and after.[22] Historically, economists almost always used "welfare" to describe "general" or "total" welfare, which was the welfare of all participants in the economy. For example, Pareto optimality assesses equally everyone who is affected by an economic action, producers as well as consumers. The same thing is true of Kaldor-Hicks efficiency, which assesses welfare changes by comparing the welfare of all gainers against the welfare of all losers. A change is a welfare improvement if the gainers gain enough to compensate fully the losers out of their gains.[23]

Oliver Williamson advocated a so-called "welfare tradeoff" model for antitrust in the 1960s,[24] and Robert Bork popularized it in the 1970s.[25] The Williamson proposal was a variant of the total welfare model. It proclaimed an antitrust practice such as a merger to be competitively harmful if the welfare losses that it produced exceeded any welfare gains.[26] Bork in particular used the model to offset gains

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[22]Robert Bork used the term in 1960s, but in a way that referred to general welfare. *See* Robert H. Bork, *Resale Price Maintenance and Consumer Welfare I*, 74 YALE L.J 775 (1965); & II, 77 YALE L.J. 950, 950 (1968); Robert H. Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division II*, 75 YALE L.J. 373 (1965). The phrase had a few earlier uses, but none that became popular. Perhaps the most important is Arnold C. Harberger, *Monopoly and Resource Allocation*, 44 AM. ECON. REV. 77 84 (1954) (monopoly harms consumer welfare). *See also* Covey T. Oliver, *The Fair Trade Acts*, 17 Tex. L. Rev. 391 (1939) (arguing that resale price maintenance ("fair trade") harms consumer welfare).

[23]*See, e.g.*, RICHARD POSNER, THE ECONOMICS OF JUSTICE (1981); Jules L. Coleman, *Efficiency, Exchange, and Auction: Philosophic Aspects of the Economic Approach to Law*, 68 CAL. L. REV. 221 (1980).

[24]Oliver E. Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoffs*, 58 AM. ECON. REV. 18 (1968).

[25]ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 107-112 (1978).

[26]Bork, *id*. at 107 (discussing Williamson, *supra* note __ at 21).

and losses as between consumers and producers, not giving much attention to effects on third parties.

One particularly damaging feature of the welfare tradeoff model was that a relatively small profit increase for producers was sufficient to offset rather large price increases to consumers. As a result, even practices that raised price significantly were thought to promote welfare. For example, Williamson concluded that under typical assumptions about elasticities of demand a cost reduction of 1% - 4% would be sufficient to offset a price increase of about 20%.[27] "More generally it is evident that a relatively modest cost reduction is usually sufficient to offset relatively large price increases."[28] This led Williamson to conclude that "a merger which yields non- trivial real economies must produce substantial market power and result in relatively large price increases for the net allocative effects to be negative."[29] What he did not acknowledge was the severe measurement difficulties that would accompany most attempts to measure the size of welfare gains against welfare losses.

Williamson did acknowledge that a merger or other practice that resulted in both efficiencies and a price increase would also reduce output. That is true of any price-increasing practice. However, he did not consider where these efficiencies would come from. Two of the most important sources of efficiency are economies of scale in production and purchasing economies for inputs. However, these occur only at higher rates of output and, thus, of purchasing. So the fact that output goes down takes away the most important sources of efficiencies. To be sure, there are exceptions that can result from reorganization of production. For example, suppose one merging firm is producing 50 washers and 50 dryers at an inefficiently low rate and the other merging firm is also producing 50 washers and dryers inefficiently. After the merger the two firms might be able to switch

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[27] Williamson, *Economies*, *supra* note__ at 22.
[28] *Ibid*.
[29] *Id*. at 23.

their production so that all of the washers are produced in one plant and all of the dryers in the other. Further, it might reduce output to 90 units of each, reflecting its increased market power, and still produce them more efficiently than it did before. But this would require not merely a merger but also significant reorganization or production.

Some efficiencies are so substantial that post-merger prices are lower than they were prior to the merger. In that case, however, there is nothing to trade off. That merger would be lawful under the consumer welfare test because it benefits rather than harms consumers. The Government's Horizontal Merger Guidelines take this approach, permitting an efficiencies defense to a merger only if efficiencies are so significant that output is at least as high after the merger as before.[30]

Other types of efficiencies can conceivably be attained at lower output levels, such as increased technological complementarity, access to IP portfolios, or redeployment of management. But merger law also requires that these efficiencies be "merger specific," which means that they cannot reasonably be attained except through merger.[31] Talent can be hired and IP can be licensed. In sum, the range of merger specific efficiencies that can result from an output reducing practice is very likely extremely small.

Bork's approach to the welfare tradeoff problem was also unique in another and quite damaging way. He disagreed with Williamson about the wisdom of measuring a welfare tradeoff, asserting that efficiencies simply cannot be measured. Using economies of scale as an example, he concluded that the problem of efficiency measurement is "utterly insoluble."[32] Rather, efficiencies should be taken on faith. When market power is completely lacking efficiencies can be inferred, because they are the only explanation that

[30]Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines §10 (August, 2010), available at https://www.justice.gov/atr/horizontal-merger-guidelines-08192010.
[31]*Ibid*.
[32]BORK, ANTITRUST PARADOX, *supra* note __ at 126.

makes a practice profitable. For example, when the two New York pediatricians form a partnership and move into a single building they could not be exercising market power. Their union is profitable only if it reduces costs or improves the quality of their services. But that argument falls apart in the presence of any amount of market power. Then the action can be profitable if it *either* reduces costs or raises prices to noncompetitive levels.

Importantly, however, Bork's idea that efficiencies are impossible to measure permits someone to look at the alarming increase in price-cost margins over the last several decades and dismiss them as reflecting nothing more than efficiencies – simply by not requiring evidence. Under Bork's tutelage we have seen a dramatic rise in margins, and thus in the presence of monopoly power, over the past forty years.

Bork also did antitrust an important disservice by naming his version of the welfare tradeoff approach "consumer welfare," even though it expressly took into account the combined welfare of consumers and producers.[33] That conception of "consumer welfare" haunts antitrust to this day. Under it, for example, the dissenters in the Supreme Court's *Actavis* decision could speak of antitrust as adhering to a consumer welfare principle even as they would have approved a practice (pay-for-delay) that resulted in very substantially higher prices to consumers.[34] Or in the *American Express* decision the majority could profess adherence the consumer welfare principle even as they were approving a practice that resulted in higher consumer

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[33]*See, e.g*., Daniel A. Crane, *The Tempting of Antitrust: Robert Bork and the Goals of Antitrust Policy*, 79 ANTITRUST L.J. 835, 836 (2014) ("Bork shifted from consumer welfare to total welfare without changing labels, hence equating antitrust policy with efficiency while continuing to package it in a consumer welfare pill that courts would easily swallow.")

[34]*See* FTC v. Actavis, Inc., 570 U.S. 136, 161 (2013) (Roberts, C.J., dissenting, along with Justices Scalia and Thomas).

prices every time it was applied.[35] In both cases the practice was highly profitable to producers, and that was all that mattered.

Conclusion: Maximum Sustainable Output

We live in an era when monopoly profits are very high,[36] when labor's share of the returns to production has declined sharply,[37] when overall economic growth is significantly smaller than it was in the mid-twentieth century,[38] and economic inequality is near an all-time high.[39] Antitrust is not a cure-all for these problems, but it does have its role. It does best when it sticks to its economic purposes and lets other legislative agendas handle the rest. Even so, pushing output back up to competitive levels can do a great deal of good and, along with other policy choices, can assist in addressing all of these problems.

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[35] Ohio v. American Express, 138 S.Ct. 2274, 2290 (2018) (Thomas, j., for the majority). *See* HOVENKAMP, FEDERAL ANTITRUST POLICY, *supra* note __, §10.10. The challenged practice forbad merchants from offering customers a lower price in exchange for using a cheaper credit card.

[36]*See* Herbert Hovenkamp & Carl Shapiro, *Horizontal Mergers, Market Structure and Burdens of Proof*, 127 YALE L.J. 1996 (2018).

[37]David Autor, et al, *Concentrating on the Fall of the Labor Share*, 107 AM ECON REV: PAPERS AND PROCEEDINGS 180, 181-83 (2017).

[38]*See* https://tradingeconomics.com/united-states/gdp-growth-annual.

[39]*See* LARRY M. BARTELS, UNEQUAL DEMOCRACY: THE POLITICAL ECONOMY OF THE NEW GILDED AGE (2d ed. 2018).