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ANTITRUST

IS MORE ANTITRUST THE ANSWER TO WEALTH INEQUALITY?

Market power often serves progressive aims.

BY DANIEL A. CRANE

Wealth inequality has reemerged as a major political issue and may become one of the defining themes of the 2016 presidential election. Progressives claim a broad set of causes for wealth inequality, from tax loopholes favoring the wealthy to the decline of private sector unionization.

Recently, a number of high-profile public intellectuals have begun to finger an additional culprit—lax antitrust enforcement. According to prominent progressives such as Nobel economics laureates Joseph Stiglitz and Paul Krugman, former labor secretary Robert Reich, and Oxford economist Anthony Atkinson, weak enforcement of the antitrust laws has permitted the flourishing of anticompetitive mergers, monopolistic conduct, and other exclusionary and collusive behavior, with the effect of redistributing wealth upward to corporate shareholders and senior executives and away from the less wealthy strata of society. This monopoly regressivity claim is increasingly being repeated in legal and economic scholarship and in the media.

The monopoly regressivity claim may have considerable political appeal, but it is vastly overstated. Although there are surely some violations of the antitrust laws that exacerbate wealth inequality, the generalization that more antitrust enforcement would lead to a more equitable distribution of wealth misunderstands the actual incidence and effects of antitrust enforcement. Exercises of market power have complex, cross-cutting effects, some of which may be regressive, but many of which may also be progressive or distributively neutral. More antitrust is not the answer to wealth inequality.

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THE MONOPOLY REGRESSIVITY CLAIM

There are many good reasons to favor competitive markets, and to think that some degree of antitrust enforcement is necessary to produce such markets. Competitive markets result in innovation, lower prices, and expanded output. This is all good and healthy, but it does not necessarily result in greater income equality. Suppose a more competitive economy results in a 20 percent increase in gross domestic product, with all members of society benefiting, but the wealthiest stratum obtains a greater per-capita share of the wealth than the lower strata. In that case, competition would have resulted in growth and gains for everyone, even while it would have *increased* wealth inequality. More competition does not inherently lead to greater equality.

Indeed, many of the social welfare policy interventions favored by progressives are designed to mitigate the inequality-inducing effects of *competitive* markets. Minimum wage laws require employees to be compensated based on some measure of merit or need rather than the value of their marginal contributions as ascertained in competitive labor markets. Unions had to be exempted from the operation of the antitrust laws because they replaced labor competition with labor cartelization. The entire social welfare state is built on the premise that competitive markets produce socially undesirable outcomes.

So where does the monopoly regressivity claim come from? In the developing world, the claim can frequently be heard from proponents of market liberalization. Such groups as the Organization for Economic Cooperation and Development, United Nations Conference on Trade and Development, and the World Trade Organization argue that the introduction of competition law increases the welfare of the poor. And indeed this story rings true in markets where productive assets are closely held

by a few conglomerate enterprises, labor mobility is low, capital markets are underdeveloped, former or current state-owned enterprises enjoy exclusive legal privileges, and trade barriers are high. Although observe, again, that increasing the wealth of the poor does not necessarily mean a reduction in the Gini coefficient in developing countries, if increased competition also creates a class of *nouveau riche*.

As for the developed world, the story is much more complicated. The argument for the regressivity of monopoly, and hence the progressivity of antitrust enforcement, is predicated on the belief that anticompetitive market conditions systematically divert income toward the wealthy. French economist Thomas Piketty had advanced the much-publicized argument that market-driven economies produce inequality when the return to capital exceeds economic growth. Proponents of the monopoly regressivity claim argue that senior corporate executives and shareholders are the primary beneficiaries of increasing returns to capital and hence the primary group

to absorb monopoly rents generated by lax antitrust enforcement. According to this argument, because senior corporate executives and shareholders are wealthier on average than the general population, antitrust violations leading to monopoly have regressive effects. More antitrust, then, would result in a progressive redistribution of wealth.

For this argument to work, shareholders and senior corporate managers would have to capture the lion's share of monopoly rents, whereas relatively less wealthy consumers would have to pay the brunt of those rents. Is that, in fact, the case?

DO SHAREHOLDERS AND MANAGERS CAPTURE THE RENTS?

Contrary to the claim that senior corporate managers are the primary beneficiaries of monopoly, the literature on the relationship between product market competition and executive compensation is ambiguous. No general case can be made from the literature that chief executive officer compensation goes up

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as product market competition softens. Indeed, some empirical studies show the opposite—that CEO compensation *declines* in less competitive markets. The intuition explaining this effect is that CEO talent may be less valuable to the corporation in a monopoly market, where earning high profits may be easier than in a more competitive market.

What about shareholders? Certainly, shareholders capture some gains from monopoly rents, but that does not necessarily make antitrust violations regressive. Shareholding is widely distributed in the United States, with 88 million participants in 401(k) or similar retirement plans and pensions controlling 16 percent of domestic corporate equities. So, directly or indirectly, many middle-class interests are represented among the ranks of shareholders.

Proponents of the monopoly regressivity theory point to studies showing that shareholding is disproportionately concentrated in the hands of the very wealthy. But do shareholders reap a significant portion of the monopoly rents generated by the corporation? While they surely obtain some of the rents, it is far from clear that they reap the lion's share.

It has long been understood that various interests within the firm and outside its borders compete to appropriate any monopoly rents generated by the corporation. Monopoly profits often do not show up on corporate balance sheets (where they would benefit shareholders) because they are eaten up within the firm. A standard trope in antitrust law concerns the fat, lazy monopolist internally consuming its monopoly profits through sloth and lack of incentive. As Judge Learned Hand famously remarked in his landmark *Alcoa* decision, “Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift, and depresses energy; that immunity from competition is a narcotic.” Or, as Nobel laureate John Hicks remarked, “The best of all monopoly profits is a quiet life.”

Workers are one of the groups well documented to benefit from monopoly power. Empirical studies have shown a monopoly wage premium for both unionized and non-unionized workers across a wide range of industries, and also the tendency for unionization to increase with increases in employer market power. Blue collar workers are thus able to appropriate some of the monopoly rents generated by their employers.

Consistent with this economic literature, labor unions and other progressive-leaning groups have sometimes supported large corporate mergers that raised serious antitrust questions. The Communications Workers of America supported the AT&T-T-Mobile merger that was eventually blocked by the U.S. Justice Department and Federal Communications Commission, and three airline employee unions supported the controversial (and now widely derided) merger of American Airlines and USAir.

Prominent civil rights organizations have supported such corporate mergers as Comcast-NBC and SIRIUS-XM. Whether or not those mergers should have been blocked as anticompetitive, many organizations ostensibly representing the interests of workers, minorities, and other arguably disadvantaged groups saw benefits to their constituencies.

A final straw for the claim that shareholders and CEOs are the chief beneficiaries of anticompetitive behavior arises from the fact that antitrust law applies to non-corporate actors as much as to corporate ones. Many of the “producers” whose commercial agreements have been challenged by antitrust

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authorities are not corporate at all, but rather sole proprietors or middle-class professionals. For example, in 2014 the Federal Trade Commission brought an enforcement action against an association of music teachers over an association rule prohibiting teachers from soliciting clients from rival teachers. According to the U.S. Bureau of Labor Statistics, music teachers earn a squarely middle-class annual income of \$66,000. In the last two years, the FTC also brought enforcement actions against other middle-class professions, including property managers, legal support professionals, lighting and sign managers, and ice skating coaches.

Another case against middle-class professionals, this one brought by the Justice Department, showcases the potential for antitrust enforcement to have regressive rather than progressive wealth distribution effects. In 2005, the Justice Department brought an antitrust challenge against the National Association of Realtors based on restrictions on the ability of home buyers to search for real estate listings over the Internet. According to the Justice Department, the effect of this restriction was to inflate realtor commissions. If that allegation was true, then the enforcement action likely had highly regressive effects. The median income of realtors is \$41,990, and that of home sellers (who typically pay commissions) is \$97,500. Any rent extraction by realtors would be progressive. Further, given the magnitude of existing home sales (\$1.2 trillion annually), the magnitude of this progressive effect (and, conversely, the regressive effect of antitrust enforcement) could be measured in the billions of dollars.

To be clear, my point is not to condemn the Justice Department's enforcement action for its regressivity. Rather, it is to point

out that increased antitrust enforcement cannot be easily equated with progressive wealth distribution effects.

DO POOR CONSUMERS BEAR THE BRUNT?

For the monopoly regressivity claim to work, not only would shareholders and senior corporate executives have to be capturing the preponderance of the monopoly rents, but relatively poorer consumers would need to be paying for them. The argument for regressivity on the payer side mirrors the arguments that sales taxes are regressive: since the wealthy save at a higher rate than the less wealthy, a smaller percentage of the wealthy's income is exposed to the tax. But this argument falls apart when it comes to antitrust enforcement, for two reasons.

First, household consumers are not the purchasers of large swaths of economic activity covered by the antitrust law. General government final consumption—government purchases of goods and services—accounts for 16 percent of GDP. An anti-competitive defense industry merger, bid rigging by contractors building schools, roads, or bridges, or monopolistic practices by pharmaceutical companies selling directly or indirectly to governmentally sponsored health programs result in overcharges to taxpayers. Because the U.S. tax system is progressive, those overcharges result in progressive wealth redistribution (at least on the payer side).

The same holds true in much of the \$1 trillion private health insurance market, which, particularly because of the Affordable Care Act, is highly progressive in redistributing wealth. Monopolistic overcharges to third-party payers are passed on progressively to household consumers, hence the overall effect of monopoly could be progressive.

Intercorporate effects also mitigate the ostensible regressivity of antitrust violations. Many antitrust violations happen far upstream of household consumers. For example, only about 10 percent of cartels sell directly to retail customers. Most occur in intermediate manufactured goods, up many levels of manufacturers, assemblers, wholesalers, and retailers from household consumers. Even if much of the overcharge is eventually passed downstream to consumers, the absorption of some of the overcharge in the distribution chain can mitigate any ultimate regressive effect.

There are two additional reasons why the analogy of antitrust enforcement and regressivity to sales taxes falls apart. First, the regressive effect of the sales tax arises because unspent wealth is not subject to the tax. But where monopoly conditions prevail in banking and financial services (areas where proponents of the monopoly regressivity claim have leveled much of their wrath), rents can be extracted from unspent money as well—for example, through inflated service fees, deflated interest rates, and the like.

Second, the regressivity of the sales tax depends on its flat rate, but monopolists do not extract equal proportions of wealth from rich and poor consumers. Economic theory holds that market power facilitates price discrimination, and that price discrimina-

tion often has progressive wealth redistribution consequences. In a world of lax antitrust enforcement leading to greater market power, producers would extract a higher share of monopoly rents from low-elasticity wealthy consumers than from high-elasticity poorer consumers.

ANTITRUST AND PRIVATE EQUALITY INITIATIVES

An additional insight into the problem of monopoly and wealth effects concerns the fact that antitrust enforcement not infrequently impedes efforts to address issues of inequality through private coordination. If, as previously argued, untempered market forces generally tend toward inequality, then private actors committed to redistributing wealth may need to subvert market forces. In a variety of cases, such efforts have met with hostility from antitrust institutions.

An important example involves diversity and access to higher education. Between 1958 and 1991, the eight Ivy League universities and the Massachusetts Institute of Technology participated in an “Ivy Overlap Group” that involved financial aid personnel from the schools agreeing on the financial need profile of any student admitted to two or more Ivy League Schools and guaranteeing that student an adequate financial aid package at whatever school he chose to attend. The schools' goal was to shift from merit-based financial aid, which allocated scarce financial aid resources to privileged applicants who often didn't need the money, to need-based aid. The schools reported significant increases in income, racial, and demographic diversity because of the Overlap program.

In 1991, the Justice Department brought an antitrust challenge that resulted in the abandonment of the Overlap program. For better or worse, antitrust killed a program ostensibly designed to redistribute wealth and opportunity progressively.

The Overlap case is by no means unique. The currently pending class action challenge to National Collegiate Athletic Association rules limiting player compensation could well result in the enrichment of a handful of star male football and basketball players at the expense of less popular athletic programs and women's sports. U.S. garment manufacturers have cited antitrust fears in declining to organize collectively to pressure their global suppliers to improve labor conditions. In many other cases, antitrust law's insistence on competition and market-determined allocation of resources flies in the face of private efforts to achieve a more equitable distribution of wealth or related social justice objectives.

CONCLUSION

Again, none of this should be taken as an indictment of antitrust enforcement. There are many legitimate reasons other than wealth inequality to take on monopolies and cartels. But it is time for progressives to remove antitrust from their wealth inequality playbook. In a time of anti-corporate sentiment, that theme may play well politically, but it cannot withstand serious scrutiny. 