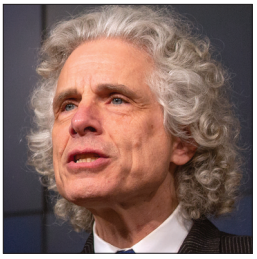

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MAY/JUNE 2018 VOL. XL NO. 3

Big Tech's Big-Time, Big-Scale Problem

BY GEOFFREY A. MANNE AND JUSTIN (GUS) HURWITZ

High-tech and network industries have a long history of evoking populist scrutiny. New technologies frequently disrupt incumbent, often less centralized, business models and interfere with existing relationships between sellers and consumers. Inevitably, the paradigmatic small-town buggy manufacturer displaced by technological advance directs his ire against the large, distant car companies that make the automobiles responsible for his demise. Even consumers and business owners who benefit from enhanced efficiency or entirely new and beneficial products often end up feeling dependent on them. Adding to that a distrust of firms that operate in geographies or at scales that are distant from typical consumer experiences, critics express their concerns about firms with a single heuristic: big is bad.

Although often framed in more complex antitrust terms—large firms are accused of employing anticompetitive business practices, including the development of "predatory" innovations designed to expand their reach and thwart potential competition, for example—populist antipathy is, at root, fundamentally about the "bigness" of these high-tech firms. Companies that owe their success—and their size—to clever implementations of innovative technologies are ultimately decried not for their technology or their business models but for their expansive

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In a photo tweeted by Sen. Orrin Hatch (R-UT) and later featured on *Meet the Press*, the senator holds up a T-shirt inspired by Cato trade policy analyst Scott Lincicome. Over 700 of these shirts have been sold since a pro–free trade Twitter quip from Lincicome went viral. See page 16.

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operations. Standard Oil, AT&T (in the early 20th century), IBM, AT&T (in the late 20th century), Microsoft, and, most recently, Google, Facebook, Amazon, and (once again) AT&T have regularly found themselves in the crosshairs of antitrust enforcers for growing large by besting (and, often, buying) their competitors.

The size of these companies—among the largest in the American economy—endows them with the superficial appearance of market power, providing competitors and advocates with a rhetorical basis for antitrust action against them. But their problems also extend beyond mere allegations that they are too large: in each case, these companies have also engaged in some conduct disfavored by powerful political actors. The appearance of market power and the firms' problematic-to-some conduct give rise to calls to use antitrust law to regulate their behavior—or, perhaps most troubling, to constrain their perceived power by breaking them up.

This article is not an apologia for the bad acts of the modern tech industry. There is no question that some of today's largest companies have transformed society and the economy over the years (not necessarily always for the better) and have engaged in arguably troubling conduct in the process. But whatever the beliefs of those calling for the breakup of Big Tech, the question remains whether it is wise to shoehorn broader social and political concerns into the narrow, economic remit of antitrust law.

By and large, the market is sufficiently powerful to constrain potentially problematic conduct. Consider the discussion that has developed since the disclosure of Facebook's relationship with Cambridge Analytica. Mark Zuckerberg has been scrambling to make public amends and to stave off a potentially devastating regulatory response, even going so far as to suggest that perhaps platforms like Facebook should be subject to some regulation. Despite those efforts, the reality is

> "By and large, the market is sufficiently powerful to constrain potentially problematic conduct."

that the market is the most effective regulator, and at the time of this writing Facebook has lost over $75 billion in value.

Alas, the urge to treat antitrust as a legal Swiss Army knife capable of correcting all manner of social and economic ills is apparently difficult to resist. Conflating size with market power, and market power with political power, many recent calls for regulation of the tech industry are framed in antitrust terms. Sen. Elizabeth Warren (D-MA) is one of the worst offenders in this regard:

> Today in America competition is dying. Consolidation and concentration are on the rise in sector after sector. Concentration threatens our markets, threatens our economy, and threatens our democracy.

For Senator Warren the antidote is clear: "It is time to do what Teddy Roosevelt did: pick up the antitrust stick again."

And she is not alone. Abetted by a growing chorus of advocates and scholars on both the left and right, proponents of activist antitrust are now calling for invasive, "public-utility-style" regulation or even the dissolution of the world's most innovative companies essentially because they seem "too big." Unconstrained by a sufficient number of competitors, the argument goes, these firms impose all manner of alleged harms—from fake news to the demise of local retail to low wages to the veritable destruction of "democracy." What is needed, they say, is industrial policy that shackles large companies or that mandates more, smaller firms.

This view contradicts the past century's worth of experience and learning. It would require jettisoning the crown jewel of modern antitrust law—the consumer welfare standard—and returning antitrust to an earlier era in which inefficient firms were protected from the burdens of competition at the expense of consumers. And doing so would put industrial regulation in the hands of would-be central planners, shielded from any politically accountable oversight.

WILSON, BRANDEIS, AND THE IGNORANT CONSUMER

American antitrust law began with the Sherman Antitrust Act of 1890. The Sherman Act, named for Ohio Senator John Sherman, prohibited agreements "in restraint of trade" (that is, collusion) and "monopoliz[ation], or attempt[s] to monopolize." Importantly, and contrary to common understandings on both the left and right, the purpose of the Sherman Antitrust Act was never particularly clear.

There is ample evidence that it was intended both to proscribe business practices that harmed consumers and to allow politically preferred businesses to maintain high prices in the face of competition from politically disfavored businesses—never mind that modern economics roundly tells us that these two goals are incompatible. This ambiguity isn't entirely surprising, both because Senator Sherman was fickle and petty in his own purposes for introducing the legislation and because the regnant economic theory of the day was relatively unsophisticated and would remain so for at least another several decades.

The years surrounding the adoption of the Sherman Act were characterized by dramatic growth in the high-tech industries of the day—most notably manufacturing/refining, railroads, and telecommunications—as well as corporate and conglomerate consolidation. For many, the purpose of the Sherman Act was to stem this growth—to prevent low prices and large firms from "driving out of business the small dealers and worthy men whose lives have been spent therein," in the words of one of the early Supreme Court decisions applying the act. It failed to do so, however, and by the time of the presidential election of 1912, concern

about large firms had developed as a divisive, populist issue. Woodrow Wilson was elected president largely on a big-is-bad antitrust platform.

The key architect of that platform was Louis Brandeis. Brandeis played an important role in reshaping antitrust and industrial policy in the United States, helping to design the Clayton Antitrust Act and the Federal Trade Commission in 1914, both of which dramatically expanded federal antitrust law. Brandeis's views were informed by a strong belief that large firms could become large only by illegitimate means and could not be trusted. Large firms, unlike their Main Street, mom-and-pop counterparts, operated primarily by deceiving consumers into buying unnecessary and lower-quality products. Stated bluntly, Brandeis's views were informed by a belief that consumers were (in his own words) "servile, self-indulgent, indolent, ignorant."

THE RISE AND FALL OF MID-CENTURY ANTITRUST

As the 20th century progressed, antitrust economics and the study of industrial organization grew increasingly sophisticated. The most prominent early advance in antitrust economics was the development of the Structure-Conduct-Performance (SCP) paradigm, associated with University of California, Berkeley, economist Joe Bain. SCP held that the conduct of firms in an industry, and ultimately their performance, was a function of the overall structure of the industry. One of the predictions of the SCP model is that more-concentrated industries are inherently less competitive, allowing firms to employ anticompetitive conduct (like collusion) to raise prices. Profitability and market performance, in this view, are a function of market structure, not the relative efficiency of competing firms. SCP therefore generally prescribed reducing concentration—for instance, by breaking up firms or challenging mergers—as a way of making industries more competitive. Ultimately, the SCP model proved to be overly simplistic and fell out of favor relatively not long after it was popularized.

> "Size simply does not correlate with anything recognizable as 'consumer harm.'"

Both SCP and the Brandeisian view of antitrust espouse a preference for smaller firms, though they diverge on the harm of "bigness." The Brandeisian view holds that big is bad per se, whereas SCP suggests that a market comprising multiple competing smaller firms is comparatively better than a highly concentrated one (which implies larger firms). Neither approach readily admits the possibility that big could be better under appropriate conditions, however.

Yet the weight of subsequent economic research holds that large firms are frequently ideal economic actors for maximizing consumer welfare. Since the Industrial Revolution, and especially in the Information Age, it's not unusual for efficient, competitive markets to comprise only a few big, innovative firms. Unlike the textbook models of monopoly markets, these markets tend to exhibit extremely high levels of research and development, continual product evolution, frequent entry, almost as frequent exit—and economies of scope and scale (i.e., "bigness"). Size simply does not correlate with anything recognizable as "consumer harm."

While perhaps counterintuitive, this observation means that, in many cases, modern antitrust law actually condones bigness—or, put differently, without additional factors to substantiate potential concern, antitrust law is fundamentally agnostic about the size of firms or the extent of market concentration.

The classic example of the problem with the Brandeisian and SCP approaches to antitrust analysis is the 1966 *Von's Grocery* case. In *Von's Grocery*, the Supreme Court addressed the government's challenge of the 1960 merger of Von's Grocery and Shopping Bag Food Stores, two grocery chains in southern California that were succeeding in a rapidly changing and increasingly concentrated market for grocery stores. Together, these chains controlled less than 8 percent of a grocery market that was increasingly dominated by a smaller number of big-box supermarkets that were coming into existence as a result of business model innovation, changing demographics, affordable automobiles, and economies of scale enabled in part by new technology.

The market share of the merged chains was insufficient to have any meaningful effect on prices, but it might have been sufficient to give the resulting retail chain the scale it needed to compete. Yet despite the lack of evidence of any anticompetitive effect from the merger, the Supreme Court affirmed the government's challenge, adopting the SCP presumption against increased concentration even where there was no anticompetitive harm.

In *Von's Grocery*, this decision meant breaking up a merger that did not harm consumers, on the one hand, while preventing firms from remaining competitive in an evolving market by achieving efficient scale, on the other. As Justice Stewart noted in dissent:

> In fashioning its per se rule, based on the net arithmetical decline in the number of single store operators, the Court completely disregards the obvious procreative vigour of competition in the market as reflected in the turbulent history of entry and exit of competing small chains. . . . The Clayton Act was never intended by Congress for use by the Court as a charter to roll back the supermarket revolution.

In other words, by adopting a formalistic rule against increased concentration, the analysis in *Von's Grocery* disregarded the more nuanced market dynamics that justified the merger, thus harming consumers, competitors, and dynamic competition.

In the 1970s, antitrust economists increasingly questioned the small-is-good bias of

Brandeisian and SCP antitrust. Prompted by cases like *Von's Grocery*, antitrust economists realized that small is good as an antitrust ethos lacked empirical and intellectual justification. Moreover, preferring firm size as an analytical dimension for applying antitrust laws could often lead to perverse outcomes in which consumers were harmed and smaller, less efficient competitors were protected. Rather than focusing on naive proxies for conduct and performance, more probing analysis was needed.

ANTITRUST'S PARADOX: PROTECTING COMPETITORS HARMS CONSUMERS

Robert Bork famously synthesized the lessons of these economists in *The Antitrust Paradox*, the 1978 *urtext* of modern antitrust. Bork argued that the best understanding of the purpose of American antitrust law is the protection of consumers against anticompetitive business practices, and that success on this front is best measured in terms of consumer welfare. Under the consumer welfare standard, we are not concerned with the structure of an industry in the abstract; we are concerned only with the extent to which particular actions of firms within that industry are likely to harm consumers.

But Bork's normative focus wasn't merely the meaning of the Sherman Act or the significance of the consumer welfare standard. For Bork, the paradox of antitrust is that antitrust law, meant to shield *consumers* from anticompetitive business practices, had come to be used to shield *competitors* from competition, at the expense of consumers' welfare.

By its nature, competition disrupts incumbent firms and existing markets. Firms develop new technologies or processes that allow them to offer better products or lower prices than their rivals. This benefits consumers and successful firms alike. Sometimes firms develop new products that disrupt markets entirely, putting a whole generation of firms out of business—again benefitting consumers and successful firms. Horses and buggies are replaced by cars; small grocers are replaced by supermarkets.

> "The story of antitrust law for most of the 20th century was one of standard-less enforcement for political ends."

What Bork saw was that antitrust law was used by unsuccessful firms to constrain the competitive efforts of their rivals. Under the Brandeisian and SCP models, firms that sought to evade the pressures of competition and managers who preferred to extract easy rents than to give their customers better products or lower prices could point to virtually any threat to the status quo as evidence of anticompetitive conduct. If a firm developed a better product, the law could be used to punish its success if the firm grew too large. If a firm developed a better process that enabled it to offer lower prices, competitors could allege that such conduct was illegal because it was "predatory."

THE POLITICAL ECONOMY OF ANTITRUST REGULATION

Perhaps the greatest virtue of the consumer welfare standard is not that it is the best antitrust standard (although it is)—it's simply that it *is* a standard. The story of antitrust law for most of the 20th century was one of standard-less enforcement for political ends. It was a tool by which any entrenched industry could harness the force of the state to maintain power or stifle competition.

This is because competition, on its face, is virtually indistinguishable from anticompetitive behavior. Every firm strives to undercut its rivals, to put its rivals out of business, to increase its rivals' costs, or to steal its rivals' customers. The consumer welfare standard provides courts with a concrete mechanism for distinguishing between good and bad conduct, based not on the effect on rival firms but on the effect on consumers. Absent such a standard, any firm could potentially be deemed to violate the antitrust laws for any act it undertakes that could impede its competitors.

Compounding the problem, the operative text of the Sherman Act comprises about 170 frustratingly ambiguous words. It is difficult to escape the sense that advocates of the elimination or dilution of the consumer welfare standard seek to co-opt the act's terse ambiguity to invent a sort of "meta-legislation" effectively to enact social preferences that they couldn't convince Congress to adopt outright.

The same high-tech, scale industries that are likely to evoke superficial big-is-bad antitrust concerns are also likely to raise important social, legal, and political questions. The telephone and the railroad reshaped society; the computer began a reshaping of society that the *personal* computer continued and that is still ongoing in today's internet era.

Adapting to the changes wrought by these industries is one of the defining challenges of the 21st century. It could well be the case, as Mark Zuckerberg suggests, that it's time to regulate all or part of these industries. If so, the shape and scope of that regulation is a matter for political debate and social response. But antitrust law is not the proper vehicle for addressing open-ended issues related to social and political values, disconnected from the economic effects of restraints on competition.

One major risk of addressing these concerns through antitrust law—and of weakening the consumer welfare standard in the process—is that applying antitrust law short-circuits the social and political processes that are better suited to addressing the concerns.

Another risk is that such a standard-less antitrust law could be used to impose arbitrary market controls subject only to political whim. The earliest, worst impulses of American antitrust law catered to the would-be industrial planners of the early 20th century. Contemporary calls to weaken the consumer welfare standard are motivated by the demands of

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another case, "the FCC voted to grant a company a TV license, and the staff wrote up an order of more than 100 pages explaining it. For reasons undisclosed, the FCC reconsidered and switched licensees. The staff dutifully revised its order using the original draft as a template, producing an equally glowing public interest justification for the new winner." I think that makes it critical for us to focus on the facts, to think about principles of economics and to have a view as to consumer welfare as opposed to whatever parochial interest might be badgering us for this or that regulatory favor.

The professor, as I said, offers some great insights, and I would like to think that over the last year and change we have tried to incorporate some of those insights in terms of structure and policy. Last year, I introduced my proposal to create an Office of Economic Analysis. Our hope is to make sure that economic reasoning is not just an afterthought at the FCC, but a *central* thought as we make our decisions. That is one way to insulate the agency from that kind of "ends justify the means" decisionmaking that I just described.

Additionally, we are giving teeth to Section 7 of the Communications Act. No longer will an innovator have to sit around waiting for years for the FCC to figure out whether or not an invention is in the public interest. We now have a one-year deadline for making these determinations. And we are adopting more market-based solutions—flexible spectrum use, for example, has been a profound benefit to consumers the world over. Instead of determining what the spectrum shall be used for, dictating it from on high and expecting entrepreneurs to make use of it, we let innovators make that decision. And the results speak for themselves. The fact that we have smartphones speaks to the fact that innovators have been able to devote the spectrum to its highest-valued use.

Additionally, we want to minimize infrastructure burdens. Increasingly this is where the rubber meets the road. Next week, for example, we are going to be voting on an order modernizing our regulations to recognize that the networks of the future won't look like the networks of the past. The small cells of the future and all the guts of the 5G networks need to be evaluated under a regulatory rubric that is different from the one that applied in decades past to 200-foot cell towers.

Our hope is that both in terms of structure and in terms of policy we can make sure that we make decisions that are right for the American people, produce more consumer welfare, and most importantly ensure that when the sequel to this book is written, Chairman Ajit Pai is not going to be featured whatsoever. Except for, hopefully, as an example of something that went right. ■

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similar would-be planners to reshape American industry in their own idiosyncratic image. Regardless of whether that image for the American economy is good (it is not), such designs should be made through the legislative process, not by hollowing out the core of antitrust law and parasitically repurposing it for political purposes.

Today's promoters of breaking up or strictly regulating Big Tech companies are primarily motivated by political concerns. These undeniably large and pervasive companies have social influence and economic power that rivals and therefore threatens would-be regulators who have spent their careers positioning themselves to wield the power of the state to advance what Thomas Sowell has dubbed the "vision of the anointed." Thus, Amazon threatens to undermine an aesthetic vision of "local self-reliance;" Facebook and Google are "information gatekeepers" with the power to undermine preferred political narratives; Uber exploits workers, evades social regulation, and threatens to hasten the decline of labor unions (and their campaign contributions).

Ultimately, from Louis Brandeis to Elizabeth Warren, those who cloak their approach to market regulation in the cloth of "consumer protection" instead of "consumer welfare" start from the premise that consumers *need* protection—from both the market and from themselves—and that learned regulators are best situated to offer this protection. A consumer protection standard is inherently ambiguous, affording regulators the power to structure markets in whatever manner they deem best for consumers. The consumer welfare standard, on the other hand, restricts the conduct of firms and regulators alike, ensuring that both operate in the objective best interest of consumers.

Properly construed, antitrust law has one focus: protecting consumers from anticompetitive conduct. This goal is encapsulated in the consumer welfare standard, and that standard accomplishes it well. We should not jeopardize that function merely for political expedience, let alone to hastily and surreptitiously implement a particular, politicized industrial policy. ■