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The Klobuchar Antitrust Bill Is Corporate Welfare that Will Harm Consumers

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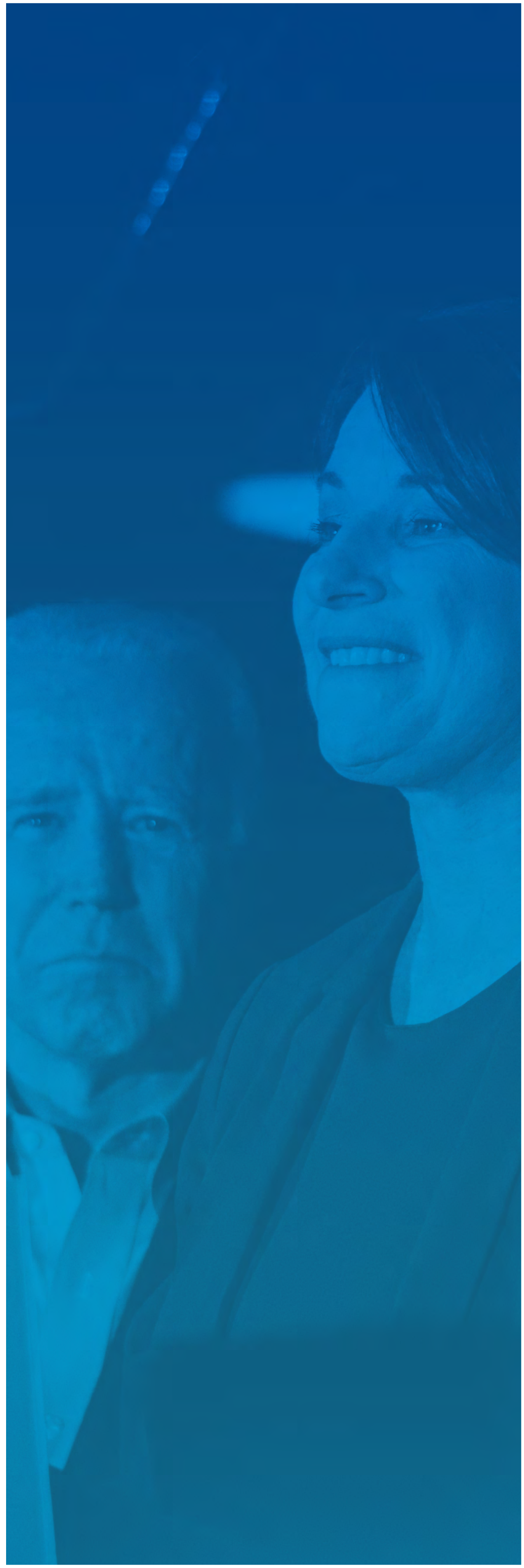

COMMITTEE TO UNLEASH PROSPERITY

"Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer."

- Adam Smith, *Wealth of Nations*

Summary

Antitrust legislation proposed by Senator Amy Klobuchar, combined with regulatory actions taken by the Federal Trade Commission, are an attempt to redefine the core doctrine of antitrust law. The justification for government taking antitrust action against large companies with “monopoly power” was originally that firms with market concentration can limit competition and raise prices, which can harm consumers.

This is called the “consumer welfare standard” of antitrust law. But modern-day global competition and rapid technological innovation dramatically *lower* consumer prices over time, which calls into question whether antiquated antitrust law actions are even necessary. Traditional antitrust law presupposes that market power and concentration always leads to higher prices, but in many industries—particularly the technology sector of the economy—dominant players have tended to lower prices for consumers.

It should be well accepted that if a company is not acting in a way that is harming consumers, then its dominant position should not be regulated or penalized by the government.

Instead, the Klobuchar bill and the FTC actions are broadening antitrust law and enforcement to protect competitors, not consumers. Antitrust in this framework simply adds to government power to inject government into the marketplace and pick industry winners and losers. Instead of building better products to make themselves more competitive, companies will rush to the government to take legal action against their competitors.

This is already happening in many markets. As an example, the FTC is now trying to prevent Google from acquiring an app for physical fitness—even though the fitness industry is one of the most fiercely competitive markets in America.

This study explains the historical rationale for the “consumer welfare standard” and demonstrates the negative implications of the Klobuchar bill and the FTC actions, which would discard this doctrine.

We believe this reinvention of antitrust law will make American companies less competitive against foreign rivals, will reduce funding for startup companies, and will lead to a decline in consumer welfare for American families.

The Klobuchar bill would increase the FTC budget by nearly $300 million a year—a near doubling of the resources and lawyers available to the agency’s chairman, super-regulator Lina Kahn. These resources would enable the FTC to challenge nearly every major merger and acquisition that is proposed between American companies. This would run contrary to the free market agenda of deregulation central to a prosperous economy.

Nothing good can come from hiring thousands of additional regulators to snoop on business.

The Essential Facilities Doctrine

The foundation of Senator Klobuchar's antitrust legislation is that the targeted companies—Amazon, Apple, Facebook, Google, and Microsoft—should be subject to what's known as the "essential facilities" doctrine.

Under this doctrine, some large entities are deemed to be so "essential" to the industry in which they operate that they need to be treated as analogous to public utilities. And that means they would be required to open their platforms (and even proprietary information and data) to their smaller competitors, which can then use these platforms for their own commercial purposes.

The implications of this for innovation are breathtaking. Apple's App Store would need to accept virtually any app that a developer wanted to have sold through the platform. Similarly, Amazon's Prime marketplace would have to accept any and all products that sellers requested.

As the Information Technology & Innovation Foundation points out, such unfettered access "opens the door for almost any competing business user to demand access to core functionality of large platforms, even if it would significantly harm consumers."

Implementation of the essential facilities doctrine would be a brazen move that vests regulators with extraordinary power to make arbitrary and potentially ill-advised decisions. As Justice Scalia pointed out in a 2004 Supreme Court decision, the "enforced sharing" at the heart of the doctrine "requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing–a role for which they are ill-suited."

The doctrine's implementation would also create powerful disincentives for companies to strive to innovate and achieve dominant positions in the industries in which they operate. Why would they spend many years, and make massive investments, attempting to realize strong growth if the price of success could be sweeping government interference that rewards their smaller, less successful competitors? Indeed, a **study** looking at European countries where the essence of the doctrine was applied in the telecom sector, via mandated access, found that investment dropped off.

A commissioner on the Federal Trade Commission, Christine Wilson, **notes** that, "The incentive to risk investment in research and development is weakened with the threat that rivals successfully could demand access to costly developments. In this context, competitors would no longer need to out-compete their rivals because they could take some of what their competitors built."

At an even more fundamental level, relying on the essential facilities doctrine is striking because there's no allegation that these large entities are depressing consumer welfare or limiting access to new products. These are industries where consumer choice is king.

A basic flaw in the essential facilities doctrine is the supposition that because these technologies exist, they should be shared with rivals. This is reminiscent of the lecture by then-President Obama to corporate America that they should be more public-spirited because "you didn't build that."

But companies often spend billions of dollars to develop new technologies that never existed before. So companies *did* build these services and products. They are not public goods. Google did invent its own search function. Facebook did invent its social network. Apple did invent the iPhone. It is contrary to the fundamental concept of private property rights and patent rights that what you create is *yours* – and that others aren't permitted to take it from you for free.

In other words, if the so-called "essential facilities" never get developed, and consumers never realize the benefits that come from the efficiencies created, then consumers suffer substantial harm – not benefit – from this new doctrine.

For example, if a new cancer drug that could save 100,000 lives a year was considered to be an "essential service" once invented and therefore to be made available at no cost to cancer patients, what are the chances that the treatment would be developed in a timely manner at all? And how many more people will die under this alternative scenario?

In sum, the essential facilities doctrine will reduce innovation, which will depress consumer welfare and reduce American living standards.

Historical Perspective on Antitrust Legislation

The Sherman Antitrust Act arrived more than 130 years ago on a wave of "Progressive" Era economic populism. Small farmers and businesses surfaced concerns about the dominance of big business in the 1880s. The legislation was based more on a perceived fairness to small businesses rather than any economic evidence of a lack of competition or efficiency.

The Sherman Act forbade monopolization as defined in the following ways: Section 1 of the Sherman Act outlaws "every contract, combination, or conspiracy in restraint of trade," while Section 2 bars any "monopolization, attempted monopolization, or conspiracy or combination to monopolize."

The Sherman Act was first effectively leveraged against labor unions (most labor activity was exempted by statute from antitrust law decades later), though the first widely heralded monopolization victories involved the breakup of Standard Oil and the American Tobacco Company in 1911. Despite these victories, "Progressive Era concerns that the Sherman Act was insufficiently effective in constraining market concentration of power led (1) to the Clayton Act, which specifically targets anticompetitive mergers and forbids certain types of agreements, and (2) to the Federal Trade Commission Act, which empowers a board of government experts to study business practices and curtail unfair competitive abuses."

Following the passage of the Sherman Act, several Supreme Court decisions noted concerns of protecting small businesses. Examples are *United States v. Trans-Missouri Freight Ass'n*, in which the Court expressed a desire to protect "small dealers and worthy men." Other examples include Brown Shoe and Alcoa.

In 1912, the Court's decision in *United States v. Terminal Railroad Ass'n of St. Louis* brought to the legal forefront the essential facilities doctrine, a legal concept that is predicated on the concept that "big is bad." The essential facilities doctrine is the proposition "that antitrust laws require a single firm in control of a facility essential to its competitors to provide reasonable access to the facility, if possible."

The Terminal Railroad Association had "organized a coalition of 14 railroads lines to acquire every railroad facility at an important junction where 24 railroad lines concluded." The Court believed ownership of every facility by one firm restrained trade and was an attempt at monopolization, thereby violating Sections 1 and 2 of the Sherman Act. But rather than dissolve Terminal Railroad, as a solution the Court invoked the essential facilities doctrine, ordering the Terminal Railroad Association to provide its competitors "reasonable access to its facilities."

Again, the railroads' "essential" transportation lines didn't exist before the railroads built them. Nothing prevented other companies the right to build their own railroads, just as today no one is prevented from forming a new airline or a new social media platform.

The period from the end of World War I through the late 1930s witnessed little antitrust enforcement and was characterized by moderate merger enforcement and some attention to joint ventures, trade associations, and resale price maintenance (when a manufacturer dictates to a dealer the retail sale price for its product). Federal agencies largely ignored collusion among competitors, reflecting a fear that aggressive competition would stall growth and prolong the Great Depression. "By the late 1930s, enforcement against price fixing picked up, as did actions against discounting by big businesses that threatened the viability of less efficient small competitors. Anti-discounting lawsuits, brought under the Robinson-Patman Act of 1936, sought to protect small businesses from competition, but their benefit ultimately came at the expense of the consumer and efficient new business models. They were later totally discredited by economists, and due to many successful defenses against the Robinson-Patman Act, the FTC no longer considers anti-discounting laws to play a meaningful role in federal antitrust enforcement.",

After a World War II hiatus, postwar antitrust policy increasingly sought to limit the power of industry leaders under a "big is inherently bad" mindset. Academic economists mistakenly coalesced around the belief that high market concentration inevitably leads to anticompetitive conduct and poor economic performance. And no longer content just focusing on size, decisions limited other "practices such as 'tying', i.e., the practice of tying the sale of one good or service to the purchase of another good or service) and nonprice vertical restraints (i.e., manufacturer limitations on the terms of marketing a product by downstream distributors)." A 1950 amendment that tightened the Clayton Act's "limitation on mergers led to increased and predominantly successful government lawsuits against mergers along horizontal, vertical, and conglomerate dimensions (that is, among direct competitors, among firms at different levels of distribution, and among firms in different industries)."

The postwar view towards antitrust law may be summarized by the following passage from Alden Abbot at the Mercatus Center:

> "A focus on the perceived evils of increased concentration led to the nearly automatic judicial condemnation of horizontal mergers among competitors, even in industries where there were huge numbers of firms with small market shares. This led Supreme Court Justice Potter Stewart to state that the sole consistency in these merger cases was that "the Government always wins.""

The economic turbulence of the 1970s led to a shift in perspective. Advances in economic theory and empirical research, primarily by the Chicago school, identified "benign explanations for highly concentrated markets" and "broke from prior work that was suspicious of concentration." While previous efforts largely assumed that concentration fostered collusion and predatory behavior, this new body of research indicated scale fostered considerable efficiency, leading to increased output and lower prices. In addition, groundbreaking research on historical cases revealed that Standard Oil did not actually engage in predatory pricing to eliminate competition prior to its dissolution. Just the opposite was true: energy prices *fell* during the summit years of this so-called monopoly.

Such was the intellectual climate in which Robert Bork developed the consumer welfare standard in *The Antitrust Paradox*. *The Antitrust Paradox* described what may have already become apparent to the reader: that legislation written based on claims to protect the consumer rarely do so in practice. In the course of also trying to protect everything under the sun, the cost to efficiency leads to reduced output and higher prices—and the consumer suffers.

Why The Consumer Welfare Standard Matters

The FTC's Christine S. Wilson has summarized the guiding principle of the consumer welfare standard in the following way: "Under the consumer welfare standard, business conduct and mergers are evaluated to determine whether they harm consumers in any relevant market. Generally speaking, if consumers are not harmed, the antitrust agencies do not act."

Sen. Lee, who has proposed the TEAM Act, robust antitrust legislation that increases funding to the FTC to monitor, enforce, and punish monopolies in violation of antitrust laws, provided the following about the consumer welfare standard in the most recent edition of *The Antitrust Paradox*:

> "As Judge Bork explained, antitrust law prior to 1978 wrongly focused on firm size and industry concentration (i.e., allocative efficiency) and ignored the productive efficiencies, whether gained through merger or internal growth, that increased benefits for consumers. Focusing only on allocative efficiency willfully ignores economic reality in order to pursue political goals-goals which are nowhere to be found in the statutory language, or even the legislative history—of the antitrust laws. Put briefly, it is the belief, against all economic evidence to the contrary, that big is always bad."

Bork argued the prevailing view frequently led courts to make decisions that ultimately harmed the consumer, by "repeatedly rejecting claims of efficiencies that would result in lower prices or better products and services, even going so far as to pejoratively label those "competitive advantages" that harmed rivals and therefore violated the antitrust laws." He also cautioned that the overemphasis on economic analysis would only continue to lead regulators astray, instead advising a single-mindedness with antitrust evaluation [emphasis ours]:

> **"Antitrust must content itself with the identification of attempts to restrict output and let all other decisions, right or wrong, be made by the millions of private decision centers that make up the American economy."**

The consumer welfare standard became part of the free-market Chicago school influence on legislative and judicial activity, as well as economic policy, for the next several decades. The merits of the consumer welfare standard earned broad influence across the political spectrum. Earlier case law decisions that punished big business and stressed the protection of small businesses were largely ignored and landmark judicial decisions began to "eliminate *per se prohibitions* unrelated to hardcore cartel conduct, to grant monopolists greater freedom of action to engage in aggressive competition, and to enunciate standards that maintain incentives for business conduct that actually benefits consumers."

Though influence would ebb with some elements of the progressive left and tech-skeptics on the right, the modern state of judicial antitrust philosophy in the years prior to the Biden Administration are best explained by Alden Abbot at the Mercatus Center:

> "Although the courts have never specifically defined the consumer-welfare standard, leading commentators see it as focused on behavior that tends toward maximizing output (taking into account quantity, quality, and innovation) in a way that is consistent with sustainable competition. Modern antitrust law condemns business behavior that is not "competition on the merits" (aggressive behavior that harms rivals without plausibly benefiting consumers or improving a firm's efficiency) as illegal "exclusionary conduct" that undermines consumer welfare. Antitrust law does not, however, require firms to show that their practices will guarantee the greatest amount of consumer welfare. Rather, antitrust law today generally allows businesses substantial leeway to shape their commercial agreements as they see fit to obtain profits, as long as they avoid per se illegal behavior and other exclusionary conduct."

The influence of the consumer welfare standard and the century-plus evolution of U.S. antitrust policy have led the Court to distinguish between the mere presence of a single industry leader and *monopolistic behavior* that harms the *competitive process*:

> "…the Sherman Act has long been construed by the courts as not condemning monopolies themselves, but as barring only "exclusionary" conduct (specific business behavior not involving competition on the merits that creates, enhances, or protects monopoly power). Thus, for example, in the famous 2001 case *United States v. Microsoft*, the US Court of Appeals for the DC Circuit did not condemn Microsoft for obtaining monopoly power in PC operating systems, but rather for engaging in a variety of "bad" practices that precluded potential competitors from legitimately challenging its monopoly. The most frequently quoted standard for what constitutes a section 2 violation is found in the 1966 case *United States v. Grinnell*, in which the Supreme Court defined illegal monopolization as having two required elements: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."

Conclusions

The Klobuchar Bill would open the floodgates to a tidal wave of new litigation against American tech companies (and others). They would be punished for innovation, research and development, and product superiority over their competitors. It would arm the FTC with massive resources to harass successful American businesses that have gained market share by providing American consumers with products and services at low prices—particularly in the tech sector of the U.S. economy, where prices have been falling and where consumer welfare has produced gains in the trillions of dollars.

Shifting away from the consumer welfare standard of antitrust would only empower the companies competing with successful U.S. businesses—without any regard to how consumers would fare. This study shows that consumers will be the victims—not the beneficiaries—of this shift in legal doctrine. As such, we believe the harm to consumers could be in the hundreds of billions of dollars, by reducing innovation as well as the development of new products and services available to consumers throughout the country. Competition, not regulation, is the key to continued American economic superiority in technology, social media, and other 21st century industries.

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