2017

Further Reflections On Antitrust And Wealth Inequality

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FURTHER REFLECTIONS ON ANTITRUST AND WEALTH INEQUALITY

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I. INTRODUCTION

Since I have already published a lengthy academic article on antitrust and wealth inequality,[2] I have the freedom of using this piece to present the key arguments unvarnished by dense citations or technical details (readers interested in those things should consult my earlier article) and to respond to some of the criticisms of my article that have since been levied. My thesis, before and now, is this: claims that antitrust enforcement advances income or wealth progressivity are overstated and rest on simplistic and unrealistic understandings of how antitrust actually operates. While some enforcement actions may generate progressive results, others will generate regressive results, and the net effect is largely unknowable. Therefore, with a few limited exceptions, it would be unwise to cast antitrust as a policy lever for advancing wealth equality.

II. DOES COMPETITION GENERALLY CREATE EQUALITY?

Before getting into the more technical aspects of the issue, consider one important framing question: does the arc of intensive economic rivalry generally bend toward an even or uneven distribution of wealth? If we lived in a world where personal abilities, the vagaries of fortune and kin relationships and family capital were evenly distributed, one might expect that competition would distribute wealth evenly. But that is not the world we live in. People have widely varying natural abilities, the Wheel of Fortune is a fickle and arbitrary patron, and people are born into greatly uneven stocks of economic, social and political capital. Given these background conditions, intensive rivalry will tend toward a grossly unequal distribution of wealth.

If this observation isn't obvious, consider the fact that the Cristiano Ronaldo earns four times the salary of his Real Madrid teammate Marcelo. Ronaldo is not four times better a player than Marcelo, the world's best left back. But the hyper-competitive market for top footballing talent generates immense financial pay-off differences from the comparatively slight differences in the two players' footballing abilities and value to the team. Economy-wide, the variance in natural abilities is many times greater than that between Ronaldo and Marcelo. It is therefore unsurprising that competitive labor markets generate tremendous wage differences.

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2 Crane, *Antitrust and Wealth Inequality*, 101 Cornell L. Rev. 1171 (2016).

Karl Marx makes a very similar point with respect to wage labor. Intense competition among wage laborers, argues Marx, drives the working class to the point of subsistence. The antidote, he argues, is the formation of unions, which enable the workers to thwart labor market competition and bargain collectively for higher wages. We need not accept Marx's wider prescriptions to agree with his observation that fierce economic rivalry creates large divides between the haves and have nots.

Much of the modern regulatory state is built on the assumption that market competition breeds unequal results and that one function of the just state is to redistribute income by taming competitive forces. Minimum wage laws and collective bargaining are squarely premised on the assumption that labor competition suppresses wages below socially desirable levels. Much of consumer protection law worries that competition among consumers for scarce resources will permit sellers to extract too much surplus from buyers.

Given the pervasive background assumption of the modern regulatory state that competition tends toward *inequality*, it is a little surprising to hear prominent public intellectuals assert with such confident authority that weak antitrust enforcement breeds inequality and that enhanced enforcement — leading to intensification of economic rivalry — would cause a more progressive redistribution of wealth. That claim seems to rest on the following simple assumptions: Shareholders are comparatively wealthier than consumers, the exercise of market power tends to transfer wealth from consumers to shareholders, and antitrust enforcement prevents these wealth transfers. While valid in some circumstances, these assumptions are grossly over-simplistic.

At the outset, and to dispel some past criticisms based on misunderstandings of my argument, let me repeat that I accept as a broad proposition that shareholders as a class are richer than consumers as a class.[3] Although tens of millions of comparatively lower-income people participate in shareholders through retirement accounts, direct investments, or things like pension funds, the skewed distribution of shareholding means that, generically, a dollar plucked from the consumer class and deposited into the hands of the shareholder class in proportion to their equity entails an increase in the Gini coefficient. The problem, though, is the assumption that violations of antitrust law generally involve wealth transfers from consumers to shareholders. Sometimes they do, and sometimes they don't.

Any comprehensive analysis of the wealth distribution effects of antitrust violations would need thoroughly to address two issues: (1) who captures the monopoly rents, and (2) who pays for them? To simply plug shareholders into the first category and consumers into the second misunderstands the way that antitrust law, firms and markets actually work.

III. WHO CAPTURES MONOPOLY RENTS?

First, who captures the monopoly rents associated with antitrust violations? To the extent that the antitrust violator is a corporation, "the firm" may be said to capture the rents, although even that claim may be overstated. As Posner has long argued, firms spend a considerable share of their expected monopoly rents to become and stay monopolists. But even assuming that "the firm" captures most of the rents, it's facile to assume that shareholders, or even wealthy senior managers, capture the lion's share. Some conventional antitrust wisdom should give us pause about making that assumption: For example, midlevel managers and other firm employees may expend considerable firm resources to exclude rivals simply to obtain Hicks's famous "quiet life"[4] or internally expend monopoly profits through the wastefulness and sloth qualities of monopoly identified by Judge Learned Hand in his famous *Alcoa* decision.[5] Indeed, it is a common assumption in antitrust law that many monopolists do not show high economic profits on their balance sheets, as *Alcoa* did not, but rather internally dissipate monopoly rents through

3 Elhauge seems to think that my earlier paper claimed that shareholders capturing monopoly profits does not create regressive results since shareholding is widely distributed. Elhauge, *Horizontal Shareholding*, 129 Harv. L. Rev. 1267, 1294 (2016). To the contrary, while noting that widely distributed nature of shareholding needs to be taken into account in any argument about market power's regressive effects, my paper made clear that "corporate shareholding is disproportionately concentrated in the hands of the very wealthy." Crane, supra note 2 at 1187.

4 Hicks, *Annual Survey of Economic Theory: The Theory of Monopoly*, 3 Econometrica 1, 8 (1935) ("[Monopolists] are likely to exploit their advantage much more by not bothering to get very near the position of maximum profit, than by straining themselves to get very close to it. The best of all monopoly profits is a quiet life.").

5 *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 427 (2d Cir. 1945) ("Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone.").

complacency. A long-standing empirical literature has searched with indeterminacy for evidence that dominant firms produce greater returns on capital to their shareholders. As Roe has argued, "rents give managers slack and attract grabs by players inside the firm."[6] Empirical evidence evidences a monopoly labor-wage premium for ordinary employees, but little evidence that the senior managers of dominant firms earn more in compensation than their counterparts in more competitive markets. Union support for arguably anticompetitive mergers in recent years (such *AT&T/T-Mobile* and various airline mergers) suggests that blue collar workers may expect to extract a significant share of the monopoly rents. Thus, without denying that monopoly firms sometimes pass on a large share of their rents to comparatively wealthy shareholders or senior managers, we need to question the generality and magnitude of that effect.

Moreover, the assumption that antitrust law mostly mediates wealth transfers between corporations and consumers ignores the very significant role that antitrust plays in policing anticompetitive conduct in middle-class professions. A long litany of antitrust actions against doctors, dentists, engineers, lawyers, real estate brokers, stock brokers, music teachers, mechanics and all sorts of middle class professions and trade associations makes it challenging to predict what effect on wealth distribution would result from even more enforcement.

Consider, for example, the Justice Department's 2005 action enjoining the National Association of Realtors from preventing its members from using password-protected Internet sites that enabled the brokers' customers to search for and receive real estate "multiple listing services" listings over the Internet.[7] If the Justice Department's factual allegations were correct, the Association's restriction inhibited competition among brokers that would have "place[d] downward pressure on brokers' commission rates." In other words, the restriction facilitated a wealth transfer from home sellers to realtors. The median income of home sellers, who typically bear the incidence of real estate commissions, is approximately $97,500[8] and that of realtors is $43,430.[9] Thus, on average, higher commissions would allow realtors to extract income from clients with more than double their income. The effect of the antitrust enforcement decision was to redistribute that income back up to the sellers.

The effects of antitrust enforcement on noncorporate, middle-class actors cannot be dismissed as insignificant. In the Realtors case, the Justice Department alleged that virtual office website brokers, whose activities the challenged rule tended to suppress, had offered discounted commission rates that had saved their customers tens of millions of dollars in commissions.[10] Given the sheer volume of existing home sales in the United States — $1.2 trillion per year[11] — even a comparatively small change in broker commission rates due to increased competition would have very significant economic effects. For example, a reduction in the average broker commission from 5.5 percent to 4.5 percent[12] would redistribute $12 billion annually from brokers to their clients with strongly regressive effects.

In sum, when antitrust violations disperse monopoly rents, they are not uniformly or even predominantly captured by wealthy shareholders or senior corporate managers. Many other interested parties, many of them less wealthy than the people paying the bill, have their finger in the till.

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6 See Roe, *Rents and Their Corporate Consequences*, 53 Stan. L. Rev. 1463, 1465 (2001)

7 Amended Complaint at ¶¶ 2, 5–6, *United States v. Nat'l Ass'n of Realtors*, No. 05 C 5140 (N.D. Ill. Oct. 4, 2005), http://www.justice.gov/atr/case-document/amended-complaint-6 [http://perma.cc/ZH5U-WNL6].

8 Nat'l Ass'n of Realtors, Home Buyer and Seller Generational Trends 77 Exhibit 6-2 (Mar. 2014), http://www.realtor.org/sites/default/files/reports/2014/2014-home-buyer-and-seller-generational-trends-report-full.pdf [http://perma.cc/5459-M6A9].

9 *Occupational Outlook Handbook: Real Estate Brokers and Sales Agents*, Bureau of Labor Statistics (Dec. 17, 2015), http://www.bls.gov/ooh/sales/real-estate-brokers-and-sales-agents.htm [http://perma.cc/L4JF-2CSF].

10 See Competitive Impact Statement at 7, *Nat'l Ass'n of Realtors*, No. 05 C 5140, http://www.justice.gov/atr/case-document/competitive-impact-statement-160 [http://perma.cc/BC89-RRX2].

11 Yun et al., Nat'l Ass'n of Realtors, 2014 Profile of International Home Buying Activity: Purchases of U.S. Real Estate by International Clients for the Twelve Month Period Ending March 2014, at 3 (June 2014) (reporting a U.S. existing home sale market of $1.2 trillion during the period of April 2013 through March 2014).

12 Home Prices and Commissions Over Time, U.S. DEP'T OF JUSTICE (July 2, 2015), http://www.justice.gov/atr/home-prices-and-commissions-over-time [http:// perma.cc/5AVJ-8PKR] (reporting steady average commission of 5.5 percent to 5.0 percent over the last decade and observing that if competition among brokers were effective, commission rates should have declined as home values increased).

IV. WHO PAYS FOR MONOPOLY RENTS?

Let's turn now to the other side of the ledger — the issue of who pays monopoly rents. The progressive critique of antitrust laxity as contributing to wealth inequality has relatively poor consumers paying the lion's share of the rents. As with respect to who captures the rents, this characterization of who pays them is grossly overstated.

First, observe that — depending on your country — a quarter or more of all economic activity is financed by the government. In large slices of the economy — much of healthcare, defense spending, education, public infrastructure, etc. — the government is the payer. If an antitrust violation produces market power in, say, defense contracting or public works, the government bears the rents. Of course, the government is just a pass-through for taxpayers, hence taxpayers pay the rents. In the United States and most OECD countries, the tax system is at least mildly progressive. To the extent that taxpayers are funding monopoly rents, the effect is generally progressive, since rich taxpayers are contributing a higher share of their income to the effort than are poorer people.

The same holds true in many other segments of the economy where consumer purchasing is mediated through structures or institutions that re-distribute costs on a progressive basis. For example, most health-care spending in the United States is mediated through a health insurance system designed by law to be progressive — to have the relatively more affluent subsidize the relatively less affluent. Overcharges due to the exercise of monopoly power therefore extract a higher share of income from the wealthy than the less wealthy, and have a progressive wealth distribution effect. Against this baseline, antitrust enforcement correcting the competitive failure would have a regressive effect.

Another flaw in the assumption that relatively poor consumers tend to bear the brunt of monopoly rents concerns the nature of inter-corporate wealth transfers. Many antitrust violations occur far upstream from retail consumers. Although end consumers may end up bearing some of the overcharge, much of it may also be borne by upstream corporate interests and not passed on. If corporations representing relatively poorer interests extract rents from corporations representing relatively wealthier interests, the net effect on wealth distribution could be progressive. Again, antitrust enforcement to correct these wrongs would be regressive.

Finally, to the extent that consumers do bear the incidence of monopoly rents, are the net effects regressive? In my prior paper, I presented a long list of cases involving antitrust violations in luxury goods or services catering to the wealthy, where it is a fair bet that the economic profile of the antitrust violator was less wealthy than that of the clientele. There are counter-examples, of course, but the incidence of monopoly on consumers does not merely involve a consumer-to-producer transfer. There are also important intra-consumer effects, the most significant one being price discrimination. As considered at length in the 2010 Horizontal Merger Guidelines, anticompetitive mergers may create the potential for price discrimination, which usually has progressive wealth effects, since the wealthy are less price elastic than the poor for most goods and services.[13] As firms acquire market power through anticompetitive acts and begin to increase their prices, they often do so employing pricing schemes that extract significantly more monopolistic rents from the wealthy than from the poor. To the extent that antitrust enforcement creates more competitive markets and more competitive markets diminish price discrimination, the effect in many instances could be to decrease the prices paid by the rich while reducing less, keeping flat, or even decreasing the prices paid by the comparatively less wealthy.

13 See Tirole, The Theory of Industrial Organization 139 (1988).

V. RESPONDING TO CRITICS

I will now respond briefly to some of the critics of my earlier papers or talks on this subject.

Elhauge dismisses my observation that firms with market power do not necessarily show higher returns on capital to shareholders with the assertion that "this claim really goes to the issue of whether there are anticompetitive profits, not who captures them."[14] No, the previously cited observation made by Hicks and Hand is that firms may capture monopoly rents but consume them internally — i.e. not return them to shareholders. In that case, (1) the paradigm on which the market power regressivity claim is premised — rich shareholders further enriched — would be falsified, and (2) other interests within the firm, including perhaps lower income interests, could be capturing those rents, further confounding the income equality effects of monopoly.

Several critics have disputed my observation about taxpayers bearing a significant share of the burden of monopoly, contending that one needs to take into account the possibility that governments would respond to their higher procurement costs by cutting other government spending, including programs that benefit the poor.[15] Once we are talking about these kinds of speculative dynamic effects, we are just underlining my overall point that the wealth distribution effects of antitrust enforcement and monopoly are almost impossible to know systematically or to generalize. As discussed in my earlier paper, social science literature suggests that increases in market power increase the political demand for higher tax rates. It is entirely possible that the long-run effect of a "rising tide of concentration" is a more aggressive and redistributive tax system. Or, governments concerned about the incidence of the tax burden on the wealthy could, as the Reagan administration did, deploy antitrust law aggressively in the public procurement sector to prevent progressive effects of market power.

Khan & Vaheesan dispute my observation about the role of health care intermediaries, believing that I had asserted that health care monopoly charges are borne by wealthy insurance companies rather than insureds.[16] To the contrary, my point was that that, particularly due to mandatory structures implemented by the Affordable Care Act, the health insurance system acts to distribute wealth from the comparatively more affluent to the comparatively less affluent. To the extent that health insurers incur monopoly overcharges and pass those along to insureds, rich people pay a comparatively larger share of those than poorer people, hence the effect is, in economic terms, progressive. Conversely, antitrust enforcement action to prevent those overcharges would be, in economic terms, regressive since it would allow the rich to keep more of their money while offering a comparatively smaller benefit to the poor.

The most salient response I have received is along the following lines: Admittedly, it cannot be said that antitrust enforcement is *generally* progressive in its wealth redistribution effects, for many of the reasons set forth in my paper. However, when one stacks up all of the progressivity effects of market power exercises outlined in my paper and weighs them against the fact that shareholding is so disproportionately held in rich hands, simple order of magnitude intuitions inform us that the latter must outweigh the former. Even if many other interests within the firm capture a share of monopoly rents, shareholders capture enough of them to skew this one effect to such a degree that it necessarily outweighs all countervailing effects.

Maybe. I don't know. Nor, I suspect, do the people making this assertion. And that's my point. Before turning to antitrust as a lever to fight income inequality, we need to admit a degree of modesty about what we really know and don't know. The story is not so simple as it is made to seem.

14 Elhauge, supra note 3 at 1294.

15 See, e.g. Elhauge, supra note 3 at 1296; Kukovec, *Economic Law, Inequality, and Hidden Hierarchies on the EU Internal Market*, 38 Mich. J. Int'l L. 1, 8 n.36 (2016).

16 Khan & Vaheesan, *Market Power and Inequality: The Antitrust Counterrevolution and Its Discontents*, Harv. L. & Pol'y Rev. 248, 235 (2017).