39. Antitrust

Congress should

- repeal the Sherman Act of 1890, the Clayton Act of 1914, the Federal Trade Commission Act of 1914, the Robinson-Patman Act of 1936, the Celler-Kefauver Act of 1950, the Antitrust Procedures and Penalties Act of 1975, and the Hart-Scott-Rodino Act of 1976;
- pending repeal, require that the Department of Justice and the Federal Trade Commission (a) weigh long-range incentive effects before intervening to reshape private markets and (b) show that proposed remedies will materially advance legitimate antitrust objectives;
- amend the antitrust laws to provide explicitly that their goals are not to insulate competitors or appease special interests but to protect private property and enhance consumer welfare;
- legalize tying arrangements, unless it can be proven that (a) the tying company has a monopoly in the tying market, (b) the tie-in produces no substantial economic efficiencies, and (c) the likely result will be to harm consumers; and
- enact legislative guidelines focusing on barriers to entry rather than market share as the key criterion of market power.

Antitrust is thought by some to be the bulwark of free enterprise. Without the continued vigilance of the Justice Department and the Federal Trade Commission, so the argument goes, large corporations would ruthlessly destroy their smaller rivals and soon raise prices and profits at consumers' expense. At a time when business combinations valued at nearly $1 trillion have already been announced and news of yet another megamerger grabs headlines almost daily, the importance of vigorous antitrust law enforcement seems to be obvious.

But antitrust has a dark side. Opposition to mergers, tying arrangements, and other business practices—in theory based on worries that competition may be impaired—typically arises, not from consumers whose interests antitrust is supposed to defend, but from competitors seeking protection from aggressive rivals. Antitrust authorities often respond to the demands of competitors, labor unions, and other well-organized special-interest groups that have a stake in stopping business practices that promise to increase economic efficiency. Instead of preventing prices from rising, antitrust intervention frequently keeps them from falling.

The politicization of antitrust is not just a matter of historical curiosity. Politics stalks many of the high-profile cases brought by President Clinton's trustbusters. When the antitrust authorities intervene to reshape markets at the behest of competitors, private decisions about how best to organize production are displaced by government decisions. Innovative firms are penalized, economies of scale are lost, and competition is thwarted, not enhanced.

Weigh Long-Range Incentive Effects

Responding to competitive market forces unleashed by the rapidly changing global economy of the late 20th century, leading American firms in the automobile, telecommunications, defense weapons systems, pharmaceuticals, and financial services industries, among others, have moved aggressively to consolidate their resources and to diversify their operations in order to compete more effectively on an international scale.

At the same time, antitrust law enforcement has exhibited renewed vigor under President Clinton's appointees to leadership positions at the Justice Department's Antitrust Division and the Federal Trade Commission, who seem to be wary of (if not openly hostile to) the self-correcting forces of unfettered markets. Concerned for much of this century that market power might result in prices that are too high, antitrust enforcers increasingly summon images of the Gilded Age to insist that firms will relentlessly exploit economies of scale to dominate their markets by charging prices that are too low. Like the great muckraker Henry Demarest Lloyd—and Karl Marx—law enforcers nowadays seem to think that competition leads inevitably to monopoly.

For the last 20 years, financial economists have seen mergers and acquisitions as productive entrepreneurial activities that improve the control and management of assets and help to deploy resources to more valuable uses. Nonetheless, the antitrust agencies persist in intervening to

block large numbers of proposed business combinations on the unsupported theory that competition will be impaired. The result has been to forestall reductions in production or distribution costs associated with economies of scale, adoption of more efficient production or organizational technologies, more effective utilization of production capacities, displacement of incumbent management, and other synergies.

One particularly egregious example is premerger notification rules, implemented in 1978 as part of the Hart-Scott-Rodino Act, that have imposed a duty on the managers of acquiring firms to announce publicly the discovery of previously hidden profit opportunities. Other suitors, unaware of the existence of undervalued assets, are given time to step forward with takeover offers of their own. The HSR process thus allows rival suitors to free ride on the information revealed by the premerger announcement.

Free riding lowers the value of information about profit opportunities. Moreover, the waiting periods imposed on merger transactions under HSR raise the cost of corporate takeovers by giving target firms opportunities to implement defensive strategies. Both of those effects reduce incentives for entrepreneurs to search out information about undervalued productive assets.

Stop Appeasing Special Interests

The antitrust laws, like government regulation generally, can be exploited by special interests to thwart competition. Laws that declare certain business practices illegal where they would substantially lessen competition are also laws that can be used strategically by politically well connected firms to obtain competitive advantages over their rivals. When a competitor is confronted with the prospect that a merger will create a larger, more effective rival, what better victory than to have antitrust authorities intervene to stop the transaction, or let it move forward only if key assets are divested?

Rather than imitate the organizational innovations that the merger partners plan to implement, or take other steps to lower their own costs, hard-pressed rivals complain that the merger will substantially lessen competition, thereby violating antitrust law. Almost certainly, they will be joined by workers who may lose their jobs and, if plants are slated for closure, by local public officials who could face higher unemployment rates and smaller tax bases.

It is conceivable, of course, that competitors' opposition to a proposed merger might be prompted by a public-spirited desire to protect consumers from the harmful effects of imminent monopoly. After all, who besides rivals has access to the specialized industry information necessary to distinguish between efficiency-enhancing and market-power-increasing motives for merger? Surely, the antitrust authorities can see through and reject competitors' complaints that are nothing more than self-serving attempts to handicap their rivals.

Systematic studies of merger law enforcement by the Justice Department and the FTC suggest that competitors, not consumers, are the chief beneficiaries of the regulation of mergers by antitrust means. One need only to have witnessed the feeding frenzy triggered by WorldCom's acquisition of MCI Communications Corp. to appreciate the constellation of identifiable interests attempting to influence the outcome. The coalition of groups opposed to the acquisition—supposedly concerned about the purely formal economic problem of assessing the merger's impact on competitive market conditions—included GTE Corp. (one of the disappointed suitors), Bell Atlantic (another corporate rival), the AFL-CIO and the Communications Workers of America (two labor unions harboring fears that the merged firm will be nonunion), the Reverend Jesse Jackson (who claimed that WorldCom-MCI will cater to business customers ''at the expense of low income and minority residential customers''), consumer activist Ralph Nader, and the United Church of Christ. Among other things, lobbyists for those organizations applied pressure on the White House, took out large ads in newspapers, and showered journalists and Congress with antimerger material.

Competitors' opposition to mergers is understandable. Indeed, such opposition is prima facie evidence that the planned combination is procompetitive, promising lower costs and lower prices. Silent acquiescence by rivals would be expected if a merger foreshadowed higher prices and profits. As the WorldCom-MCI case illustrates, however, the antitrust laws have become a weapon of convenience for special pleaders of all stripes, who are apparently willing to go to almost any length to protect their interests. The only response that seems to be off the table in this politicized antitrust environment is the one demanded by competitive market forces—namely, for rivals to work harder to use resources efficiently and to do a better job of satisfying consumers' wants.

Protect Private Property

The latest Department of Justice crusade against Microsoft is a prime example of misapplied antitrust law. Instead of vindicating property rights and advancing consumer welfare, the department has politicized competition—enlisting the public sector in pursuit of private, parochial interests. In essence, the government seeks to transform Microsoft's private property into something that belongs to the public, its products designed by bureaucrats and sold on terms congenial to competitors who are bent on Microsoft's demise. Some members of Congress, purported advocates of the free market, endorse that foolishness, evidently oblivious to the destructive implications of stripping private property of protection against confiscation.

The principles are these: No one other than Microsoft has a right to the operating system that it created. Consumers can't demand that it be provided at a specified price or with specified features. Competitors aren't entitled to share in its advantages. By demanding that Windows be exploited for the benefit of competitors, or even consumers, our politicians encourage those who debase private property and do an enormous disservice to the rest of us who still have a healthy respect for free markets and a free society.

Legalize Tying Arrangements

Underlying the Microsoft litigation is the government's contention that Microsoft illegally ties its Internet Explorer browser to its Windows operating system. Supposedly, say Microsoft's critics, tying arrangements are inherently coercive. They force consumers to purchase a tied product that, at best, the consumer would prefer to buy from someone else or, at worst, the consumer does not want at all.

Courts have held that tying arrangements are per se illegal if (a) they involve two separate products, (b) the defendant has a monopoly in the tying (e.g., operating system) market, and (c) commerce in the tied market is "not insubstantial." That standard has it exactly backwards. Tying arrangements should be presumptively *legal*, unless the government can demonstrate not only that the defendant has a monopoly but also that the tie-in produces no substantial economic efficiencies and is likely to harm consumers. No such showing is possible in the Microsoft case.

First, the corollary to Microsoft's 85 to 90 percent share of the operating system market is that one customer in eight does not use a Microsoft system—not a huge number, but neither is it inconsequential. Alternatives

are available—MacOS, Unix, Linux, and OS/2, to name a few. Second, it's not just existing but potential competition that matters. Over the near term, network computers and consumer electronics could radically affect the nature and scope of the operating system. When it comes to PC software, market power is likely to be here today, gone tomorrow.

Most important, Microsoft of the future must compete against a company that controls nearly 90 percent of PC operating systems—namely, Microsoft of today. Even if the company were to go out of business this afternoon, all of its installed systems would continue to function indefinitely. To sell any new product—Windows 98, for example—Microsoft must convince its customers to pay more money, learn a new system, and take a chance that other software applications won't work. It is utterly inconceivable that Microsoft would employ coercive tactics on the very consumers on whom it must rely for its new sales.

In short, the major competition for Windows 98 is Windows 95, just as Windows 95 had to capture market share from Windows 3.1. That process, still unfolding, exerts a powerful discipline on Microsoft's behavior. Windows 95 has roughly 33 percent of the market. If Microsoft had coercive power, and attempted to exercise that power, the company would surely have been able to persuade more than a third of its customers to upgrade to its flagship product.

Finally, Microsoft's tie-in of its browser and operating system generates efficiencies that promote consumer welfare. At the top of the list, PC users demand integration. Integrated systems are less expensive to produce and distribute, easier to use and document, and cheaper to debug. Globally, millions of software developers have created thousands of compatible products thanks to the standardized platform that Windows affords.

Eliminate Barriers to Entry

At root, the question is whether there are barriers to entry that protect a company from competition. In our largely—but not wholly—free-enterprise system, true barriers arise not out of private market power but out of government misbehavior—special-interest legislation or a misconceived regulatory regimen that insulates existing producers from potential rivals.

When cable companies, electric utilities, and telephone companies are issued ''certificates of public convenience and necessity'' or their equivalent, monopolists are born and nurtured at public expense. When government offers tax benefits, subsidies, insurance, or loans to specific businesses or erects trade barriers designed to protect a U.S. firm from foreign

competition, the effect is frequently to foster the same sort of anti-competitive environment that the antitrust laws were meant to foreclose. The obvious answer—which has little to do with the antitrust laws—is for politicians to stop doing those things.

Repeal the Antitrust Laws

The time for modest reform of antitrust policy has passed. Root-and-branch repeal of what Federal Reserve chairman Alan Greenspan a generation ago referred to as a ''jumble of economic irrationality and ignorance''—and what modern scholarship has shown over and over again to be a playground of special pleaders—is called for.

As long as government has the power to help or hurt various interests by regulating merger activity and other business practices, the groups that have a stake in law enforcement outcomes will rationally strive to shape those outcomes in their own favor. It is not the special-interest groups that are to blame but the state's jealously guarded regulatory power. Adam Smith's oft-quoted line, ''People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public or in some contrivance to raise prices,'' has become a defense of vigilant antitrust intervention. What almost everyone ignores is Smith's warning in the next sentence: ''It is impossible indeed to prevent such meetings, by any law which either could be executed, or would be consistent with liberty and justice.''

Suggested Readings

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