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ABSTRACT

Competition Policy as a Political Bargain

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Abstract

Competition policy in the U.S. may be understood as a self-enforcing political bargain emerging from a repeated political interaction between two large and diffuse interest groups, termed consumers and producers. Absent such a bargain, regulatory policy would fluctuate between pro-producer policies that tolerate exercises of market power, and pro-consumer policies that systematically redistribute surplus from producers to consumers. This perspective is consistent with the broad contours of the historical U.S. experience with antitrust, particularly with the continuity in antitrust enforcement and decline in the political salience of competition policy since the 1940s. The adoption of Chicago school views during the late 1970s and 1980s, a notable recent period of discontinuity and heightened political salience, is best understood either as a demonstration that the political bargain is self-enforcing or as reform to increase the efficiency gains, and not as an episode inconsistent with the political bargain perspective. If competition policy reflects a political bargain, then enforcers and courts should seek to maximize aggregate surplus, so long as consumers and producers sufficiently share the efficiency gains, so that neither group can do better by renegeing on the bargain. Current antitrust rules could not easily be exploited by consumers to transfer rents systematically from producers, so the antitrust laws should be enforced today to protect buyers without regard to aggregate surplus, unless the aggregate efficiency costs of doing so would be large.

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Competition Policy as a Political Bargain

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Candidates for President once debated antitrust policy. Disputes about regulating trusts took center stage in the four-way 1912 election campaign among President William Howard Taft, former President Theodore Roosevelt, future President Woodrow Wilson, and socialist candidate Eugene Debs. Moreover, antitrust enforcement in the decades before World War II was marked by sharp pendulum swings. In the early 20th century, the Supreme Court issued decisions breaking up Standard Oil and American Tobacco. Two decades later, during the 1930s, the antitrust laws were effectively repealed – only to be revived over the next decade through a litigation program led by Thurman Arnold at the Justice Department. By contrast, modern Presidential candidates rarely mention the antitrust laws, and speeches by the recent leadership of the Federal Trade Commission have highlighted continuities in antitrust policy over the past quarter-century that are independent of the political party in power.¹

The decline in the political salience of competition policy over the twentieth century is consistent with the political economy explanation for the evolution of U.S. antitrust policy described in this article. According to that explanation, antitrust emerged through a political

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¹ William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 61 *ANTITRUST L.J.* 377 (2003); (FTC Commissioner nominee and former FTC General Counsel) Thomas B. Leary, *The Essential Stability of Merger Policy in the United States*, 69 *ANTITRUST L.J.* 105 (2002) (FTC Commissioner).

bargain between two large and diffuse interest groups, consumers and producers.² Absent such a bargain, governmental regulatory policy toward business, set for the economy as a whole, would not be stable. It would fluctuate between pro-producer policies that tolerate the exercise of market power and pro-consumer policies that redistribute wealth from producers to consumers. An intermediate antitrust policy increases aggregate social wealth by allowing the economy to achieve the efficiency gains available from protecting competition, but it is not as advantageous to the favored interest group nor as disadvantageous to the disfavored group. Antitrust may nevertheless be adopted as an interest group bargain when repeated political interaction takes place between the interest groups. Such a bargain can be self-enforcing: neither group would mobilize politically to replace it for fear of reverting to cycles between pro-consumer and pro-producer redistributive regimes.

In this way, an efficient social institution, here competition policy, can arise from coordinated action among conflicting, self-interested interest groups interacting in the political arena. This result does not arise as the inevitable byproduct of Coasian bargaining among conflicting interest groups or evolutionary selection. Rather, coordination emerges as a possible outcome of repeated interest group interaction.

The political bargain interpretation is consistent with important features of the U.S. regulatory experience with antitrust enforcement, particularly the way that profound disputes over regulatory policy in national politics, most evident during the late 19th and early 20th

² This stylized economic story is formalized and illustrated through a mathematical example set forth in an Appendix.

centuries, were resolved by the 1940s. The claim that the U.S. political system reached a political bargain in favor of competition policy during the 1940s is also consistent with antitrust's Chicago school revolution, a dramatic change in antitrust policy implemented by the courts during the late 1970s and 1980s. The events surrounding the rise of the Chicago school are not interpreted as producers reneging on a political bargain. Instead they are understood as consistent with the existence of such a bargain: either illustrating how the bargain was enforced when some attempted to renege, or else as reform of the method by which the bargain was implemented aimed at increasing the efficiency gains.

The interpretation of antitrust law as a bargain between consumer and producer interests provides a new window into the debate over what welfare standard should be applied in antitrust enforcement. That debate is commonly framed today as a choice between an aggregate surplus standard or a consumers' surplus standard. Viewing antitrust as a political bargain suggests an intermediate position: antitrust enforcers and courts should seek to maximize aggregate surplus, subject to the constraint that consumers and producers sufficiently share the efficiency gains, at least on average, so that neither group thinks it can do better by reneging on the political bargain. In the wake of modifications to antitrust doctrines during the past three decades, which largely remove the practical danger that modern antitrust rules could be exploited by consumers to transfer rents systematically from producers, this perspective implies that antitrust law should be enforced today with a qualified emphasis on consumers: protecting consumers without regard to aggregate surplus unless the aggregate efficiency costs of doing so would be large. Doing so would help protect consumer support for the political bargain in favor of competition policy

without undermining producer support, and thus would help secure most of the economy-wide efficiency benefits available from antitrust enforcement.

I. THE POLITICAL ECONOMY OF REGULATORY POLICY

From an economic perspective, regulatory policy-making can be understood as the product of interest group competition in the political arena. The most basic difficulty confronting interest groups seeking to influence regulatory policy is to overcome collective action problems arising out of the incentives of individual group members to free-ride on the political participation and lobbying efforts of others.³ Although the determinants of interest group success in overcoming collective action problems are not well understood,⁴ concentrated interest groups are generally considered more likely than large and diffuse interest groups to succeed in doing so.⁵ Yet when economy-wide regulatory policy (as opposed to industry-specific

³ Mancur Olson, *THE LOGIC OF COLLECTIVE ACTION* (1965).

⁴ The positive political theory literature on lobbying does not model how some groups overcome their free-rider problems while others do not, but proceeds by assuming merely that some interest groups are able to organize to influence public good allocation in their favor. Torsten Persson and Guido Tabellini, *POLITICAL ECONOMICS: EXPLAINING ECONOMIC POLICY* 172, 175 (2000); Gene M. Grossman and Elhanan Helpman, *SPECIAL INTEREST POLITICS* 103-04 (2001); *see* Daron Acemoglu, Simon Johnson, and James Robinson, *Institutions as the Fundamental Cause of Long-Run Growth* 4 (NBER Working Paper 10481, May 2004) (the de facto political power of an interest group depends in part on its ability to solve its collective action problems, but “we do not yet have a satisfactory theory” of when groups are able to do so). *But cf.* Gary J. Miller, *The Impact of Economics on Contemporary Political Science*, 35 *J. ECON. LITERATURE* 1173, 1180-81 (1997) (highlighting significance of social incentives associated with group membership as a determinant of individual political participation).

⁵ Mancur Olson, *THE LOGIC OF COLLECTIVE ACTION* (1965).

regulation) is at stake, the relevant interest groups – which we give names like business (producers) and consumers – are best thought of as large and diffuse. How, in such a setting, can the political system arrive at a broad and durable regulatory policy framework, and which interests will benefit?

As will be explained below, competition policy can emerge as a durable bargain among interest groups, even if those groups are large and diffuse. Enforcement presents a key difficulty: such a bargain cannot persist, and consequently is unlikely to be struck, unless it can be enforced. Under some circumstances, such an interest group bargain could be self-enforcing. This possibility is emphasized in the stylized economic story discussed in this part and formalized as a mathematical example in the Appendix. But, as will also be discussed, the idea that competition policy could reflect a political bargain is more general than the particulars of the specific self-enforcement story discussed.

The political bargain story highlighted here views the regulatory policy outcome of the political process as a contest between two large and diffuse interest groups, producers and consumers. With an eye to history, the “producer” category is understood as primarily composed of large firms, with small firms joining consumers, farmers, workers, and others whose lives were disrupted or threatened by the growth of large enterprise in what will be termed the “consumer” interest group.

In this story, the political system selects a regulatory regime from among three options:

competition (protected by antitrust enforcement), market power, and price controls.⁶ In a market power regime, cartels would be permitted and the government would enact barriers protecting incumbent firms against new competition.⁷ In a price controls regime, the government would keep prices low through regulation or legislation with similar effect in redistributing surplus from producers to consumers.⁸ The market power and price controls regimes can be understood as special interest legislation by which either producers or consumers exploit a legislative majority to appropriate rents from the other interest group. By assumption, the competition regime permits the economy to obtain efficiency gains unavailable under the market power or price controls regimes.⁹

The most important economic assumption in the stylized story is that a diffuse interest group, such as consumers or producers, can more easily solve its collective action problems under conditions of adversity than success. This plausible assumption is consistent with

⁶ These possible regulatory regimes should be interpreted as ideal types. In practice, each has a range of variants, as will become evident in the later discussion.

⁷ Absent antitrust laws, market power would result in any given industry with probability, not certainty, so the payoffs in a market power regime are understood as expected profits that account for the possibility that private attempts to exercise market power might fail. The government could improve the odds of success through policies favorable to cartelization, such as government enforcement of private cartel agreements or the exclusion of new competition at the behest of incumbents.

⁸ For example, strongly consumer-oriented regulatory legislation might deconcentrate major industries and simultaneously institute progressive corporate taxation.

⁹ By one estimate, the annual welfare benefits to the U.S. from adopting a competition regime rather than permitting the unchecked exercise of market power could readily exceed 1 percent of GDP, a figure far greater than the likely direct and indirect social costs of antitrust. Jonathan B. Baker, *The Case for Antitrust Enforcement*, 17 *J. ECON. PERSPECTIVES* 27, 45 (2003).

anecdotal evidence.¹⁰ As a leading organizer of large and diffuse political interests explained, “It’s always easier to build a movement when the other side is in power. When your own side is perceived to be in power, it’s more difficult to organize.”¹¹ Accordingly, if the favored regulatory policy of producers, say, is adopted, namely a market power regime, then consumers will find it easier to mobilize politically to overturn that policy.

This assumption is difficult to reconcile with forward-looking expectation formation by informed and rational actors. For such actors, the existing policy regime would not matter in determining the stakes. Rather, each interest group’s valuation of a choice between, say, a price controls regime and a market power regime would depend only on future payoffs under the alternative regulatory regimes, and would not depend upon which regulatory regime is currently in effect. The most promising approach for harmonizing the assumption that adversity facilitates overcoming collective action problems with rational behavior is to postulate greater costs of political mobilization among past winners than among the losers.¹² In any case, this assumption

¹⁰ On the plausibility of this assumption: it is hard to image a Ralph Nader successfully mobilizing consumers politically by writing a book charging that automobiles are presently safe products but soon would not be unless consumers organized, *cf.* Ralph Nader, *UNSAFE AT ANY SPEED: THE DESIGNED-IN DANGERS OF THE AMERICAN AUTOMOBILE* (1965), or a Charles Murray successfully fostering a neoconservative reaction to the welfare state by charging that government regulation had not yet produced adverse unintended consequences but soon would. *Cf.* Charles A. Murray, *LOSING GROUND: AMERICAN SOCIAL POLICY, 1950-1980* (1984).

¹¹ Jeffrey H. Birnbaum, *Liberal Praise Drawn from Unlikely Source*, *WASHINGTON POST*, October 18, 2004, at E1, E12 (quoting Richard Viguerie, who has been termed “the funding father of the conservative movement”).

¹² For example, the responsibility of governing that accrues to political winners may raise the costs of organizing to fight the next political battle. Or, in a setting with multiple interest groups divided over multiple issues, political mobilization around one issue could be costly to

is consistent with how collective action is understood in the behavioral and experimental economic literatures.¹³

Three strands of these literatures are consistent with the view that collective action problems among members of diffuse interest groups are more easily solved under conditions of adversity than success. First, surveys of experimental investigations of collective action conclude that individual behavior is better characterized as adaptive and backward-looking than strategic and forward-looking.¹⁴ This characterization is consistent with the idea that members of an interest group that have succeeded in inducing the political system to adopt their favored policy will tend to ignore the implications of increased lobbying by opponents,¹⁵ and will cooperate less than the members of an interest group seeking to overturn that policy.

the extent that it risks undermining a governing coalition by threatening the prospects for political success for cross-cutting interest groups to which the members of a large and diffuse interest group also belong.

¹³ For general surveys of these literatures see Elinor Ostrom, *Collective Action and the Evolution of Social Norms*, 14 *J. ECON. PERSPECTIVES* 137 (2000); Ernst Fehr and Simon Gächter, *Fairness and Retaliation: The Economics of Reciprocity*, 14 *J. ECON. PERSPECTIVES* 159 (2000); John O. Ledyard, *Public Goods: A Survey of Experimental Research*, in *HANDBOOK OF EXPERIMENTAL ECONOMICS* (John H. Hagel & Alvin E. Roth, eds. 1995). For a recent survey of factors affecting the ability of colluding firms to solve collective action problems, see Margaret C. Levenstein and Valerie Y. Suslow, *What Determines Cartel Success?* 44 *J. ECON. LIT.* (forthcoming March 2006).

¹⁴ Frans van Winden, *Experimental Investigation of Collective Action*, in *POLITICAL ECONOMY AND PUBLIC FINANCE: THE ROLE OF POLITICAL ECONOMY IN THE THEORY AND PRACTICE OF PUBLIC ECONOMICS* (S.L. Winer and H. Shibata, eds. 2002) (working paper available at <<http://www1.fee.uva.nl/CREED/pdf/Linz2001.pdf>>); Vjollca Sadiraj, Jan Tuinstra and Frans van Winden, *Interest Group Size Dynamics and Policy Making* 11 (January 2004), available at <http://www.pubchoicesoc.org/papers/tuinstra.pdf>.

¹⁵ That is, group members will tend to act myopically, as though the existing regulatory regime will continue with certainty.

Accordingly, diffuse interest group members will act as though they perceive the stakes in regulatory policy-making to be less when the current policy regime is favorable,¹⁶ even though the actual stakes depend on the expected future regime rather than the current regime. These interest group members will consequently have more difficulty organizing collectively to respond to a gathering threat.

Second, in behavioral analyses of collective action, feelings of unfairness and anger are found to support cooperation;¹⁷ this perspective recalls the historical sociology literature

¹⁶ A high marginal per capita return from cooperation has a strongly positive effect on contributions in the voluntary provision of public goods. John O. Ledyard, *Public Goods: A Survey of Experimental Research*, in HANDBOOK OF EXPERIMENTAL ECONOMICS (John H. Hagle & Alvin E. Roth, eds. 1995) at 149-51. Cf. Roger G. Noll and Bruce M. Owen, THE POLITICAL ECONOMY OF DEREGULATION: INTEREST GROUPS IN THE REGULATORY PROCESS 34, 41-42 (1983) (a group's ability to overcome its collective action problems likely improves as the per capita stakes for its members increase).

¹⁷ Jill Gabrielle Klein, N. Craig Smith, and Andrew John, Why We Boycott: Consumer Motivations for Boycott Participation, 68 J. MARKETING 92 (2004) (working paper available at <<http://facultyresearch.london.edu/docs/02-701.pdf>>); Andrew John and Jill Klein, The Boycott Puzzle: Consumer Motivations for Purchase Sacrifice, 49 MANAGEMENT SCIENCE 1196 (2003); Frans van Winden, *Experimental Investigation of Collective Action*, in POLITICAL ECONOMY AND PUBLIC FINANCE: THE ROLE OF POLITICAL ECONOMY IN THE THEORY AND PRACTICE OF PUBLIC ECONOMICS (S.L. Winer and H. Shibata, eds. 2002) (working paper available at <<http://www1.fee.uva.nl/CREED/pdffiles/Linz2001.pdf>>); Paul M. Romer, *Preferences, Promises and the Politics of Entitlement*, in INDIVIDUAL AND SOCIAL RESPONSIBILITY: CHILD CARE, EDUCATION, MEDICAL CARE, AND LONG-TERM CARE IN AMERICA 204-05 (Victor R. Fuchs, ed., 1996); cf. Simon Gächter and Arno Riedl, Moral Property Rights in Bargaining with Infeasible Claims, MANAGEMENT SCIENCE (forthcoming) (working paper available at <<http://www1.fee.uva.nl/creed/pdffiles/MPRBIC.pdf>>) (labor-management bargaining is influenced by subjective claims of unfairness); but cf. Roger G. Noll, *Comment*, in INDIVIDUAL AND SOCIAL RESPONSIBILITY: CHILD CARE, EDUCATION, MEDICAL CARE, AND LONG-TERM CARE IN AMERICA (Victor R. Fuchs, ed., 1996) (commenting on Romer chapter) (negative voting may best be understood as a way to prevent officials from shirking on their implicit commitments to interest groups rather than as a means by which cooperation among interest group members is facilitated, and in any event any negative voting theory at best explains the behavior only of

describing how a sense of injustice helps diffuse groups solve collective action problems.¹⁸

These emotions are more likely to be found among members of an interest group that has lost recent major policy debates than among the winners, suggesting that the losers will be better able to solve collective action problems. Third, based on considerations like these, some behavioral economists have come to model political participation among members of an interest group as based in part on a reference or aspirational utility level, not just actual utility and costs of participation.¹⁹ This approach is consistent with the view that individual political action (including action in the presence of individual incentives to free-ride) is determined importantly by dissatisfaction with existing governmental policies – as is more likely the case when an interest group has been unsuccessful in its past efforts to influence government policy than when it has succeeded.

In order for a heightened sense of grievance to facilitate collective action by a diffuse interest group, moreover, a diffuse interest group that succeeds politically must be unable to lock-in its success permanently by making it difficult for its unsuccessful rival interest group to mobilize in the future. Many have observed a contrary dynamic in the wake of political success

voters relatively uncommitted to a political party).

¹⁸ Barrington Moore, Jr., *INJUSTICE: THE SOCIAL BASES OF OBEDIENCE AND REVOLT* (1978).

¹⁹ *E.g.* Vjollca Sadiraj, Jan Tuinstra and Frans van Winden, *Interest Group Size Dynamics and Policy Making* (January 2004), *available at* <http://www.pubchoicesoc.org/papers/tuinstra.pdf>; *see* Daniel Kahneman, Jack L. Knetsch and Richard Thaler, *Fairness as a Constraint on Profit-Seeking: Entitlements in the Market*, 76 *AM. ECON. REV.*, 728 (1986) (firms gauge fairness in terms of reference transactions).

by *concentrated* interest groups;²⁰ the assumption made here that adversity facilitates collective action takes the view that *diffuse* interest groups are unable to behave similarly. This assumption is plausible because voters that are members of large and diffuse interest groups would be expected to have multiple interest group allegiances, and have difficulty negotiating complex cross-issue political compromises.²¹ In consequence, they may find themselves able to reach agreement only on a narrow political program, such as the common denominator of their shared interests. If alterations in procedural rules would affect differentially the prospects of political success for the cross-cutting interest groups to which the members of the large and diffuse interest group also hold allegiance, such procedural modifications are unlikely to be included in the political program of the diffuse interest group.²²

²⁰ Concentrated interest groups that succeed in inducing the political system to adopt their favored policy are sometimes able to compound their success by creating procedural roadblocks to impede opposing interests from overturning that outcome in the future. *See, e.g.* Roger G. Noll and Bruce M. Owen, *The Political Economy of Deregulation: Interest Groups in the Regulatory Process* 34, 39 (1983); Terry M. Moe, The Politics of Bureaucratic Structure, in *Can the Government Govern?* (John E. Chubb and Paul E. Peterson, eds. 1989) (analyzing methods currently advantaged groups employ to build agencies that are difficult for opposing groups to gain control over later); *cf.* Forrest Maltzman and Charles R. Shipan, Continuity and Change: The Evolution of the Law (August 12, 2005), *available at* <http://www.uiowa.edu/~c030310/Research.html> (analyzing factors affecting durability of laws). As with regulatory capture theories generally, however, this dynamic is more plausible with respect to single industry regulation, in which the political contest involves one or more concentrated interest groups, than with respect to economy-wide regulation among diffuse producer and consumer interests.

²¹ Consistent with this perspective, the mathematical example set forth in the Appendix treats the choice of regulatory policy as the only issue that the political system must resolve, thereby ruling out the possibility of cross-issue bargaining in the interest group interaction.

²² *Cf.* Daron Acemoglu, Simon Johnson, and James Robinson, Institutions as the Fundamental Cause of Long-Run Growth 48-48 (NBER Working Paper 10481, May 2004)

The political contest between producers and consumers over choice of regulatory regime analyzed here thus takes place under two conditions: that these diffuse interest groups can more readily solve their collective action problems under conditions of adversity than success, and that a political success for one interest group does not go so far as to create procedural hurdles that would make it difficult for a competing interest group to organize. Under such circumstances, as the Appendix shows with an example, the one-shot political interaction regarding economy-wide regulatory policy between producers and consumers would be expected to lead to regulatory cycles.²³ When consumers get the upper hand, they institute price controls in order to extract rents from producers; when producers control the political system, they obtain the ability to exercise market power. Political victories are temporary: the losing group is motivated by adversity to mobilize its political resources more effectively and overturn the undesirable

(“institutional changes that do not strengthen strong opposition groups or destabilize the political situation are more likely to be adopted”); *but cf.* Jacob S. Hacker & Paul Pierson, *OFF CENTER: THE REPUBLICAN REVOLUTION AND THE EROSION OF AMERICAN DEMOCRACY* (2005) (describing efforts of a diffuse national governing coalition to discourage political mobilization by opponents).

²³ Political cycles (and even more complex dynamics) similarly arise out of endogenous variation in the propensity of individuals to participate in collective action in Vjollca Sadiraj, Jan Tuinstra and Frans van Winden, *Interest Group Size Dynamics and Policy Making* (January 2004), *available at* <http://www.pubchoicesoc.org/papers/tuinstra.pdf>. These authors relate the participation propensity to a reference utility level, in order to implement an assumption similar to one made here, that dissatisfaction with governmental policies is a determinant of political action. They do not, however, consider the possibility that repeated play could support coordinated outcomes, the theme emphasized here. Political cycles can also arise for other reasons. For example, it is well known that outcomes resulting from majority voting can cycle because group preferences may be intransitive even if individual voters have transitive preferences; this phenomenon is known as a Condorcet cycle. *See generally*, Kenneth A. Shepsle & Mark S. Bonchuck, *ANALYZING POLITICS: RATIONALITY, BEHAVIOR, AND INSTITUTIONS* (1997).

regulatory regime. Hence, much political debate would be expected to revolve around regulatory policy.²⁴

In contrast, if producers and consumers come to recognize that they interact politically in repeated play, another outcome is possible: a competition policy bargain. As the example in the Appendix also shows, the two diffuse interest groups can bargain to achieve a regulatory regime in which antitrust enforcement ensures competition among firms. The efficiency gains from competition would then be split between producers and consumers.

If these groups are able to bargain politically to achieve competition, moreover, that regime may be self-enforcing. Absent changes in the discount rate or the payoffs, neither interest group would have an incentive to encourage the political system to deviate from a competition regime, as both would do better with competition than they would were regulation to revert to cycles. Under such circumstances, economy-wide regulation would no longer be found at the top of the political agenda for either interest group.

A durable competition policy could result from interest group bargaining even if the

²⁴ Cycles between pro-producer and pro-consumer regimes sometimes appear in industry regulation, as has occurred with the regulation of both cable television and natural gas. *See, e.g.*, Gregory S. Crawford, *The Impact of the 1992 Cable Act on Household Demand and Welfare*, 31 *RAND J. ECON.* 422 (2000); M. Elizabeth Sanders, *THE REGULATION OF NATURAL GAS: POLICY AND POLITICS, 1938-1978* (1981). Unlike economy-wide regulatory regimes, regulation in these industries does not involve bargaining between diffuse interests. Rather, the regulatory contest in these industries involves more than one concentrated interest group with adverse interests: cable and broadcast in the case of cable television, and natural gas and oil in the case of natural gas regulation. Regulatory cycles may be possible in these settings because the political power of the second concentrated interest group can prevent the regulated industry from locking in temporary regulatory victories.

specific enforcement mechanisms suggested by the stylized story do not apply in all particulars.²⁵ For example, a competition policy bargain between interest groups, once reached, could also be self-enforcing for a reason that does not require the threat of reversion to regulatory cycles: the diffuse distribution of economic and political power across individual consumers, or across individual firms, may mean that neither group could mobilize politically to undermine the bargain. Given the “public good” nature of a political bargain to effectuate competition policy, by which consumers and firms share the efficiency gains, no individual firm or consumer may have sufficient incentive on its own to bear the costs of shifting governmental policy toward a pro-producer or pro-consumer regime, respectively.

Moreover, self-enforcement is not the only mechanism available to enforce a competition policy bargain. Another possibility is that the interest groups striking the bargain can take steps to insulate it by creating institutions that would make competition policy difficult to undermine. In particular, one could interpret a number of institutions as structural impediments to the dismantling of U.S. competition policy. These include the fabric of judicial cases elaborating

²⁵ Even if the threat of reversion to regulatory cycles is an important mechanism for enforcement of a competition policy bargain, moreover, other enforcement methods may also matter because deviation from such a bargain may be easier than the stylized story suggests. In particular, the example set forth in the Appendix ignores differences among members of the consumer and producer groups (such as differences within the consumer coalition between individual consumers, small firms, and farmers; possible differences in discount rates between young and old consumers; and differences in the long term prospects of individual industries) that may exacerbate collective action problems in reaching and enforcing an interest group bargain. In addition, the example treats the regulatory policy decision as a choice among three discrete alternatives. The actual availability of a more complex set of alternatives may similarly make any particular bargain more difficult to sustain.

antitrust rules in a legal system that values consistency with precedent, the establishment of multiple agencies with antitrust enforcement responsibility (particularly the Justice Department's Antitrust Division and the Federal Trade Commission, but also state attorneys general), the well-developed norm by which specific enforcement decisions by the federal antitrust agencies are protected from political influence, and the availability of private rights to challenge antitrust violations in court. These institutions would not be impervious to a legislative assault, were Congress minded to reduce the scope of the antitrust laws, restrict access of certain potential plaintiffs to the courts, and decrease the budget of the federal enforcement agencies. Nor would they be impervious to a judicial assault, were the Supreme Court to choose to reinterpret precedents to undermine a competition bargain, as some suggest was threatened during antitrust's Chicago school revolution. Still, the inertia for competition policy undoubtedly created by the presence of these institutions makes clear that a competition policy bargain could be enforced through a number of mechanisms, and the plausibility of such a bargain is not tied to the specifics of the self-enforcement mechanism emphasized above.

This interpretation of the development of competition policy in the U.S. views the choice of regulatory regime, an economic institution, as the product of a political interaction among self-interested interest groups. In this respect, it takes a similar perspective to the modern economic literature on the endogenous development of economic institutions.²⁶ The broader literature

²⁶ *See generally*, Daron Acemoglu, Simon Johnson, and James Robinson, *Institutions as the Fundamental Cause of Long-Run Growth* (NBER Working Paper 10481, May 2004); *cf.* Gary J. Miller, *The Impact of Economics on Contemporary Political Science*, 35 *J. ECON. LITERATURE* 1173, 1197 (1997) (surveying examples of political institutions developed through negotiation by rational actors cognizant of the distributional implications of institutional change).

originally emphasized the hypothesis that competition among alternative ways of organizing institutions would tend to weed out those institutions that do not capture efficiencies, and that in consequence, institutional arrangements would tend toward those that allow social groups to obtain efficiencies.²⁷ But that provocative hypothesis foundered. For example, Douglass North “abandoned the efficiency view of institutions” when he recognized that “[r]ulers devised property rights in their own interests and transactions costs resulted in typically inefficient property rights prevailing.”²⁸ One central difficulty was identifying a mechanism, comparable to price, that would signal the availability of efficiency gains to social actors and induce them to alter institutions in order to achieve them. Accordingly, the modern literature on the endogenous development of economic institutions has a different emphasis: it highlights the likelihood that an inefficient outcome will arise out of the political interaction, for example because political actors have difficulty making commitments to compensate others in the future or to take future

²⁷ This perspective was advocated in various forms in, for example, Armen A. Alchian, *Uncertainty, Evolution and Economic Theory*, 58 *J. POL. ECON.* 211 (1950); Harold Demsetz, *Toward a Theory of Property Rights*, 57 *AM. ECON. REV.* 347 (1967) (Papers and Proceedings); Richard A. Posner, *Some Uses and Abuses of Economics in Law*, 46 *U. CHI. L. REV.* 281 (1979); Lance E. Davis and Douglass C. North, *INSTITUTIONAL CHANGE AND AMERICAN ECONOMIC GROWTH* (1971); and Gary S. Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 *Q. J. ECON.* 371 (1983); Gary S. Becker, *Public Policies, Pressure Groups, and Dead Weight Costs*, 28 *J. PUB. ECON.* 329 (1985).

²⁸ Douglass C. North, *INSTITUTIONS, INSTITUTIONAL CHANGE AND ECONOMIC PERFORMANCE* 7 (1990). Similarly Richard Posner is reportedly now “distinctly skeptical” about the related claim that the common law tends toward rules that ensure economic efficiency. Jürgen G. Backhaus, *Efficient Statute Law*, in 2, *THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW* 24 (Peter Newman, ed. 1998).

actions that would not be in their interest *ex post*.²⁹ Self-enforcing agreements, such as the competition policy bargain discussed here, are dismissed as generally implausible.³⁰

From this perspective, one contribution of this article is to rehabilitate the possibility that interest group bargaining may lead to the development of welfare-enhancing institutions. But unlike the earlier efficiency view, this outcome is not regarded as the inevitable product of Coasian bargaining among conflicting interest groups or evolutionary selection. It is merely one possible outcome, which may arise when coordination is made possible by repeated interaction.

II. DID THE U.S. STRIKE A POLITICAL BARGAIN IN FAVOR OF COMPETITION POLICY?

The economic stylized story of how competition policy could emerge politically through repeated interest group interaction, set forth above, is consistent in broad outline with the

²⁹ See Daron Acemoglu, Simon Johnson, and James Robinson, *Institutions as the Fundamental Cause of Long-Run Growth* (NBER Working Paper 10481, May 2004) at 37-47 (explaining how social conflict among interest groups making conscious choices can cause underdevelopment).

³⁰ See generally Daron Acemoglu, *Why Not a Political Coase Theorem? Social Conflict, Commitment and Politics*, 31 J. COMPARATIVE ECON. 620 (2003). Acemoglu emphasizes the absence of an impartial third party that can be relied upon to enforce political bargains and highlights reasons why self-enforcing agreements (incentive-compatible promises) would not be reached or would fall short of achieving the efficient outcome. *But cf.* Avner Greif, *INSTITUTIONS AND THE PATH TO THE MODERN ECONOMY: LESSONS FROM MEDIEVAL TRADE* (forthcoming 2005) (draft available at <http://www-econ.stanford.edu/faculty/Greif_Institutions/GreifBook.html>) (studying self-enforcing institutions, by which rules conditioning the behavior of optimizing actors and the beliefs of individual actors supporting those rules are simultaneously in equilibrium).

historical evolution of antitrust in the United States.³¹ This consistency suggests that the story captures an important aspect of that history. However, it does not explain every nuance; the historical record is richer and more complex throughout than the stylized story would presume.

The question of how to regulate big business was hotly debated for decades during the late 19th and early 20th centuries, without clear resolution, notwithstanding that the political branches enacted, interpreted and enforced the primary antitrust statutes during these decades.³² Over this period, horizontal agreements, from loose pools to tighter trusts, emerged in major industries including railroads, steel and sugar, and large firms like American Tobacco and Standard Oil came to dominate their markets.³³ When regulation was adopted in response, it took more than one form: public utility regulation for some industries, particularly railroads and

³¹ Modern antitrust enforcement arose first in the United States, and until the last decades of the 20th century, was not central to regulatory policy in most other nations. *Cf.* Morton Keller, *The Pluralist State: American Economic Regulation in Comparative Perspective, 1900-1930*, in *REGULATION IN PERSPECTIVE* 65 (Thomas K. McCraw, ed. 1981) (“Nowhere did large enterprise take root so readily or flourish so luxuriantly as in the turn-of-the-century United States. And in no other country was there so strong a political, legal, and regulatory response. The land of the trust was also the land of antitrust.”); Tony Freyer, *REGULATING BIG BUSINESS: ANTITRUST IN GREAT BRITAIN AND AMERICA, 1880-1990* (1992) (tracing the causes and consequences of differing competition policies in the two nations). Moreover, the adoption of competition policy elsewhere in the world undoubtedly owes much to the example and influence of the U.S. Accordingly, the stylized story of competition as a political bargain set forth here is compared with the historical record in the U.S. only.

³² The statutory framework for federal competition policy in the U.S. was largely settled by 1914. Sherman Act was enacted in 1890. The Clayton Act and Federal Trade Commission Acts were enacted in 1914.

³³ *See generally*, Naomi R. Lamoreaux, *THE GREAT MERGER MOVEMENT IN AMERICAN BUSINESS, 1895-1904* (1985).

electric power,³⁴ and antitrust for others. But big business had defenders, who argued that large scale enterprise was inevitable and beneficial to the economy.³⁵

Once enacted, the federal antitrust laws were enforced inconsistently. Few cases were brought during the Sherman Act's first decade. In 1895, the Supreme Court held that a government challenge to a combination of manufacturing capacity in the sugar industry was beyond the reach of federal commerce power, and consequently beyond the reach of the Sherman Act,³⁶ though the Court liberalized its jurisdictional view a few years later.³⁷ In 1899, the Court confirmed that naked price-fixing violated the Sherman Act,³⁸ but shortly after that decision, the colluding firms were allowed to merge into a single firm without government challenge. In 1904, the Supreme Court established that substantial horizontal mergers violated the Sherman Act,³⁹ slowing the pace of industrial consolidation. Standard Oil was broken up as a result of a high-profile Supreme Court decision in 1911, but in doing so the Court set forth a then-

³⁴ See generally, Thomas K. McCraw, *PROPHETS OF REGULATION* (1984). Railroads were also subject to the antitrust laws. *E.g.* *United States v. Trans-Missouri Freight Ass'n*, 166 U.S. 290 (1897); *United States v. Joint Traffic Ass'n*, 171 U.S. 505 (1898).

³⁵ James May, *Antitrust in the Formative Era: Political and Economic Theory in Constitutional and Antitrust Analysis, 1880-1918*, 50 *OHIO STATE L. J.* 257, 285 (1989).

³⁶ *United States v. E.C. Knight Co.*, 156 U.S. 1 (1895).

³⁷ *Addyston Pipe & Steel Co. v. United States*, 175 U.S. 211 (1899). The Supreme Court expanded its view of federal commerce clause power during the 1940s, after which *E.C. Knight* was overruled. *Mandeville Island Farms v. American Crystal Sugar Co.*, 334 U.S. 210 (1948).

³⁸ *United States v. Addyston Pipe & Steel Co.*, 175 U.S. 211 (1899) (affirming 85 F. 271 (6th Cir. 1898)) (Taft, J.).

³⁹ *Northern Securities Co. v. United States*, 193 U.S. 197 (1904).

controversial framework for antitrust analysis which accepted that restraints of trade by large firms, even when they led to market dominance, could be found reasonable.⁴⁰

Two broad coalitions of diffuse interests contested economy-wide regulatory policy during the late 19th and early 20th centuries,⁴¹ each seeking to appropriate the rents of the other (regardless of the costs of redistribution to aggregate social wealth).⁴² The Populist and Progressive accounts of politics as a struggle between the people and the interests captures an important aspect of debates over economy-wide regulatory policy during that era.⁴³ The

⁴⁰ *Standard Oil Co. v. United States*, 221 U.S. 1 (1911).

⁴¹ *Cf.* James Q. Wilson, *BUREAUCRACY* 78 (1989) (when the costs and benefits of governmental action are both widely distributed, as with the passage of the Sherman Act and antitrust enforcement generally, “no one organizes” to seek the benefits or to avoid the costs and the regulatory regime is said to have been produced by “majoritarian” politics); Samuel P. Hays, *THE RESPONSE TO INDUSTRIALISM, 1885-1914* 138 (1957) (at time the Sherman Act was passed by Congress, “antitrust agitation” was neither “well organized” nor “particularly strong”). The political impetus for antitrust during the late 19th and early 20th centuries came importantly from politically mobilized farmers. Elizabeth Sanders, *ROOTS OF REFORM: FARMERS, WORKERS, AND THE AMERICAN STATE, 1877-1917* (1999); Donald J. Boudreaux, Thomas J. DiLorenzo, and Steven Parker, *Antitrust Before the Sherman Act, in THE CAUSES AND CONSEQUENCES OF ANTITRUST: THE PUBLIC CHOICE PERSPECTIVE* 255 (Fred S. McChesney and William F. Shugart II, eds. 1995).

⁴² *Cf.* William W. Lewis, *THE POWER OF PRODUCTIVITY: WEALTH, POVERTY, AND THE THREAT TO GLOBAL STABILITY* (2004) (documenting higher productivity in the U.S. relative to other nations; attributing that difference to greater product market competition among firms in the U.S.; and attributing greater domestic U.S. competition to the success of consumer interests in opposing producer and worker interests, in part through antitrust enforcement).

⁴³ *See generally* Richard Hofstadter, *THE AGE OF REFORM* 234 (1955) (describing “a widespread and urgent fear of business consolidation and private business authority”); Robert H. Weibe, *THE SEARCH FOR ORDER, 1877-1920* 45, 52-53 (1967) (anti-monopoly sentiment was the “most common means of expression” of a widespread “desire for community self-determination” in the face of “threats to local autonomy” from “great corporations”; the Sherman Act seemed to “appear from nowhere” in order to reflect that “consensus”); *cf.* Mark T. Law and Gary D. Libecap, *The Determinants of Progressive Era Reform: The Pure Food and Drugs Act of 1906*

introduction of competition policy can reasonably be understood as the product of a political contest involving broad coalitions of opposing interests.⁴⁴ As historian Richard Hofstadter explained, during the Progressive era, Americans “stopped viewing political issues solely from the standpoint of the producer” and instead exhibited “an equal concern with consumption as a sphere of life.”⁴⁵ This development of a “consumer consciousness,” and the concomitant emergence of consumers as an interest group, “gave mass appeal and political force to many Progressive issues,” including the desire to regulate monopoly.⁴⁶

On the other hand, the asserted division of the polity into two broad interest groups, here termed producers and consumers, downplays important distinctions within these aggregates.⁴⁷

(Nov. 17, 2004), *available at* http://entrepreneurship.eller.arizona.edu/docs/fac_pubs/Libecap_PureFoodDrugsAct_2004.pdf (tracing the influence of producer and consumer groups in Progressive era food and drug regulatory legislation). A rhetorical distinction between the people and corporate interests was also employed by Franklin Roosevelt, in his attacks on “economic royalists,” and continues to be adopted by some liberal politicians today.

⁴⁴ Certain industries are subject to antitrust exemptions or special antitrust rules. These include exemptions for labor unions, the business of insurance, and agricultural cooperatives. These exemptions and rules are generally the result of lobbying by concentrated interest groups rather than diffuse interests, and for that reason are closer to industry-specific regulation than to the economy-wide regulatory policy outcomes studied here. Moreover, the success of antitrust has created concentrated interest groups with a stake in preserving its institutions, including plaintiff and defense lawyers with antitrust practices, consulting economists, and federal and state enforcement agencies. But these small interest groups have little influence on economy-wide regulatory policy.

⁴⁵ Richard Hofstadter, *THE AGE OF REFORM 172-73* (1955).

⁴⁶ *Id.*

⁴⁷ *Cf.* James May, *The Factional Foundations of Competition Policy in America 1888-1992*, 42 *ANTITRUST BULL.* 239 (1997) (evaluating the claim that competition policy in the U.S. is the product of an ongoing interaction between two factions, one committed to protection from

The terms “producer” and “consumer” do not fully reflect the nature of the two political coalitions that debated economy-wide regulatory policy. For example, agrarian interests played a key role in the pro-antitrust “consumer” coalition during political debates over antitrust legislation during the late 19th and early 20th centuries.⁴⁸ Similarly, the sweeping producer category ignores the historically important distinction between small business and big business. Small business interests were actually important members of the “consumer” political coalition seeking to regulate large firms during the late 19th and early 20th centuries.⁴⁹

Moreover, it can be difficult to categorize any individual or entity as associated uniquely

excessive private economic power and the other committed to protection from excessive government regulation) (reviewing Rudolph J.R. Peritz, *COMPETITION POLICY IN AMERICA 1888-1992: HISTORY, RHETORIC, LAW* (1996)).

⁴⁸ Elizabeth Sanders, *ROOTS OF REFORM: FARMERS, WORKERS, AND THE AMERICAN STATE, 1977-1917* 267-313 (1999).

⁴⁹ Cf. Robert H. Weibe, *THE SEARCH FOR ORDER, 1877-1920* 45-46 (1967) (during the late 1800s, local entrepreneurs particularly resented large firms and feared that the great corporations were “stifling opportunity”); Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 447 (1966) (“... the bulk of [Thurman] Arnold’s support came not from any uprising of consumers, but from smaller businessmen or dissatisfied business groups unable to compete successfully with their larger rivals ...”); Samuel P. Hays, *Political Choice in Regulatory Administration*, in *REGULATION IN PERSPECTIVE: HISTORICAL ESSAYS* 136 (Thomas K. McCraw, ed., 1981) (the “real world of continuous antitrust politics” during the 1920s lay not in a battle between consumers and producers but “within the business community between those who bought and those who sold”). Accordingly, antitrust law and policy have historically incorporated provisions favored particularly by small sellers seeking to compete with large rivals, most notably statutory prohibitions against price discrimination, exclusive dealing, and tying. In contrast, by the start of antitrust’s Chicago school revolution, the small-businessman had “all but disappeared” as “a partner in the American liberal coalition,” and “with him has gone much of the pristine anti-bigness feeling of the Progressive tradition.” Richard Hofstadter, *What Happened to the Antitrust Movement?*, in *THE PARANOID STYLE IN AMERICAN POLITICS, AND OTHER ESSAYS* 221 (1979). Today, regulatory policies aimed at protecting small businesses are no longer reflexively regarded as in the interests of consumers.

or even primarily with the producer or the consumer category. Individual voters may be consumers at home, but they may associate themselves with producer interests when worrying about continued employment or the value of the stock holdings in their retirement assets. Firms, which are not directly represented in the legislature but are widely acknowledged to have political influence, may also be difficult to categorize. They may be producers when transacting in their output markets, but they are also consumers of inputs, including the output of other firms. In addition, political debates over regulatory policy took place in a range of settings, not just within the federal legislature but also within the federal executive and judicial branches, and in the states.⁵⁰ Notwithstanding these qualifications, it appears reasonable to treat the development of antitrust policy as the product of a political interaction among two large and diffuse interests groups.

Through the early 20th century, political debates over regulatory policy focused on the “monopoly problem” created by the rise of the large corporation and its economic power generally, and the development of industry-wide trusts in particular.⁵¹ By 1912, historian Ellis Hawley concludes, “three broad approaches to the ‘monopoly problem’ had emerged.”⁵² Two of

⁵⁰ On regulatory policy debates in the states, *see generally* Steven L. Piott, *THE ANTI-MONOPOLY PERSUASION: POPULAR RESISTANCE TO THE RISE OF BIG BUSINESS IN THE MIDWEST* (1985); James May, *Antitrust in the Formative Era: Political and Economic Theory in Constitutional and Antitrust Analysis, 1880-1918*, 50 *OHIO STATE L. J.* 257 (1989).

⁵¹ Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 4 (1966).

⁵² *Id.* at 9. *Cf.* Elizabeth Sanders, *ROOTS OF REFORM: FARMERS, WORKERS, AND THE AMERICAN STATE, 1977-1917* 280-82 (1999) (describing three different positions on antitrust policy that had “crystallized” by 1912, and their bases of political support). The three approaches emphasized by Hawley did not exhaust the alternative regulatory frameworks raised in the

these, Woodrow Wilson's New Freedom and Theodore Roosevelt's New Nationalism, can be understood as alternative ways of taming concentrated economic power. Wilson's approach viewed large firms as illegitimate and sought to restore competition – first, by eradicating special privileges benefitting the trusts and, second, by preventing large firms from engaging in unfair competition.⁵³ Roosevelt rejected deconcentration in favor of domesticating large firms through extensive governmental supervision and planning.⁵⁴ Both approaches sought to benefit consumers, workers, farmers, and small business – the sectors of society most concerned with the monopoly problem. When considered in the context of contemporaneous political efforts to reduce tariffs (viewed as taxing the general population for the benefit of private industry) and to enact a progressive income tax,⁵⁵ both approaches can fairly be considered variants of the pro-consumer price controls regime that was set forth as an alternative in the stylized story of regulatory politics.⁵⁶ The third approach to the monopoly problem, more appealing to many

political debate, though they account for those most seriously debated. *Cf.* Robert L. Rabin, *Federal Regulation in Historical Perspective*, 38 *STANFORD L. REV.* 1189, 1216-24 (1986) (describing regulatory reforms in 1914 as emerging out of complex ideological and interest group activity). The other alternatives included relying on common law tort and contract rules to regulate large business, and the socialist alternative of governmental economic management and control.

⁵³ Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 7 (1966).

⁵⁴ *Id.*

⁵⁵ *See generally*, Steven R. Weisman, *THE GREAT TAX WARS* 237-88 (2002) (describing political debates over taxes and tariffs during the 1912 presidential election campaign and after the election of Woodrow Wilson).

⁵⁶ The difference between these broad approaches had deep ideological roots, however, making compromise among their partisans difficult. William E. Kovacic, *The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement*, 17 *TULSA L. J.* 587, 604-05

business leaders with large firm ties, sought to place business regulation in the hands of self-governing trade associations.⁵⁷ This approach is reasonably equated with the market power regulatory regime in the stylized story.

This three-sided argument framed a hotly contested political debate for the next three decades. The question of which regulatory approach to follow took center stage during the presidential election of 1912.⁵⁸ Although that election led to the creation of the Federal Trade Commission and the enactment of the Clayton Act, it did not resolve the fundamental issue. The role of large scale enterprise and the appropriate form of regulation remained contested, and at times the subject of bitter policy debates, throughout the 1930s.⁵⁹

Between 1912 and 1940, national regulatory policy was politicized, and any apparent stability was only temporary. When times were good, the reputation of business was at its peak, making business self-regulation appealing and giving business forces the upper hand in political debates. But hard times, particularly the onset of the Great Depression and the 1938 recession that interrupted the economic recovery, promoted anti-business sentiment. While the Theodore Roosevelt, Taft and Wilson administrations of the early 20th century had brought a number of

(1982).

⁵⁷ Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 8-9 (1966).

⁵⁸ James Chace, 1912 7-8 (2004); William E. Kovacic, *The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement*, 17 *TULSA L. J.* 587, 603-05 (1982) .

⁵⁹ *See generally*, Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* (1966). *But see* Martin Sklar, *THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM, 1980-1916* 324-32 (1988) (concluding the “corporate-liberal solution” had become established as “the national political consensus on the regulation of the market” through the enactment of the Clayton and Federal Trade Commission Acts in 1914).

enforcement actions against trusts,⁶⁰ the Republican administrations of the prosperous 1920s generally accepted interfirm cooperation as benign industrial self-government and encouraged industries to form trade associations.⁶¹ Throughout this period, and especially during the economically-challenging decade of the 1930s, direct regulation had become routine in much of

⁶⁰ Morton Keller, *The Pluralist State: American Economic Regulation in Comparative Perspective, 1900-1930*, in REGULATION IN PERSPECTIVE 68-69 (Thomas K. McCraw, ed. 1981); see Richard A. Posner, A Statistical Study of Antitrust Enforcement, 13 J. L. & ECON. 365, 366 (1970) (table showing that the rate at which the Justice Department instituted antitrust cases rose beginning in 1905 or 1906, during the T. Roosevelt administration). In response to expanded antitrust enforcement during the early 20th century, “business leaders began to agitate for revision of the Sherman Act to render it less threatening.” Elizabeth Sanders, ROOTS OF REFORM: FARMERS, WORKERS, AND THE AMERICAN STATE, 1977-1917 276 (1999); *but cf.* Martin Sklar, THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM, 1980-191 203 (1988) (all organized groups, not just large corporate capitalists, were dissatisfied with the Supreme Court’s interpretation of the Sherman Act).

⁶¹ Thomas K. McCraw, PROPHETS OF REGULATION 144-52 (1984); Ellis Hawley, *Three Facets of Hooverian Associationalism: Lumber, Aviation, and Movies, 1921-1930*, in REGULATION IN PERSPECTIVE: HISTORICAL ESSAYS 95-123 (Thomas K. McCraw, ed., 1981); William E. Kovacic, The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement, 17 TULSA L. J. 587, 606-08 (1982); see generally Morton Keller, *The Pluralist State: American Economic Regulation in Comparative Perspective, 1900-1930*, in REGULATION IN PERSPECTIVE 75-91 (Thomas K. McCraw, ed. 1981). The Commerce Department, particularly when led by Herbert Hoover, took the lead in promoting trade associations during the 1920s, to some extent at odds with the Justice Department’s concern that information exchange among rivals could lessen competition. See *American Column & Lumber Co. v. United States*, 257 U.S. 377 (1921) (upholding Justice Department challenge to information exchange among trade association members); *Maple Flooring Manufacturers Ass’n v. United States*, 268 U.S. 563 (1924) (rejecting Justice Department challenge to information exchange among trade association members). The Justice Department instituted antitrust cases at nearly the rate of prior administrations through the 1920s, though the rate declined at the FTC beginning during the middle of that decade. See Richard A. Posner, A Statistical Study of Antitrust Enforcement, 13 J. L. & ECON. 365, 366, 369 (1970). The Justice Department’s efforts to protect the antitrust laws from being overrun by the rising tide in favor of business self-regulation led the Supreme Court to reaffirm the core antitrust prohibition against price-fixing and reject the possibility of a defense based on the “reasonableness” of prices. *United States v. Trenton Potteries Co.*, 273 U.S. 392 (1927).

the economy, particularly the transportation, financial services, electric power and communications industries, including a number of industry sectors not plausibly characterized as natural monopolies.⁶²

All three regulatory visions of these decades – industry self-regulation, national economic planning, and restoration of traditional competition – were pursued through the enactment of the regulatory centerpiece of the early New Deal, the National Industrial Recovery Act.⁶³ The act, and the National Recovery Administration (NRA) it established, offered the potential for national economic planning to the heirs of Theodore Roosevelt, offered opposition to unfair competition to the heirs of Woodrow Wilson, and offered the potential for industry-self regulation to business groups weaned on the trade association emphasis of the Republican administrations of the previous decade. In implementation, however, the NRA Codes of Fair Competition were rapidly captured by multiple concentrated industry groups, industry by industry, under cover of the self-regulatory ideology promoted by big-business interests. The NRA effectively gave industry

⁶² See generally, Morton Keller, *REGULATING A NEW ECONOMY: PUBLIC POLICY AND ECONOMIC CHANGE IN AMERICA, 1900-1933* (1990). The political coalition originally favoring direct regulation was likely dominated by those opposed to producer interests. *But see* Roger G. Noll, *Economic Perspectives on the Politics of Regulation*, in *II HANDBOOK OF INDUSTRIAL ORGANIZATION* 1269-70 (Richard Schmalensee & Robert D. Willig, eds. 1989) (noting alternative view that the Interstate Commerce Commission was created to help improve enforcement of a railroad cartel). Notwithstanding its source of political support, direct regulation has not invariably been pro-consumer in application, as agencies can become “captured” by the regulated industry and so allow firms to appropriate rents from consumers.

⁶³ See generally, Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* (1966); Robert L. Rabin, *Federal Regulation in Historical Perspective*, 38 *STANFORD L. REV.* 1189, 1244-45 (1986); Donald R. Brand, *CORPORATISM AND THE RULE OF LAW: A STUDY OF THE NATIONAL RECOVERY ADMINISTRATION* (1988). The National Industrial Recovery Act was enacted in June 1933.

license to cartelize,⁶⁴ contemporaneous with a Supreme Court decision adopting a lax attitude toward price-fixing among rivals.⁶⁵ This outcome was at variance from popular sentiment against big business during the Great Depression⁶⁶ – so much so that the agency might have been abolished had the Supreme Court not declared the statute creating it unconstitutional in 1935.⁶⁷ This unhappy experience put both those favoring industrial self-regulation and the advocates of taming the large corporation through governmental planning on the defensive. When the impetus

⁶⁴ Firms in many industries exploited the opportunity to learn ways of coordination that persisted for years after the National Industrial Recovery Act was declared unconstitutional. Barbara Alexander, *The Impact of the National Industrial Recovery Act on Cartel Formation and Maintenance Costs*, 76 *REV. ECON. & STAT.* 245 (1994); Jonathan B. Baker, *Identifying Cartel Policing Under Uncertainty: The U.S. Steel Industry, 1933-1939*, 32 *J. L. & ECON.* S47 (1989); A. M. McGahan, *Cooperation in Prices and Capacities: Trade Associations in Brewing After Repeal*, *J. L & ECON.* 521 (1985); *but cf.* Barbara Alexander, *Failed Cooperation in Heterogeneous Industries Under the National Recovery Administration*, 57 *J. ECON. HISTORY* 322 (1997) (other attempts at coordination were unsuccessful).

⁶⁵ *Appalachian Coals, Inc. v. United States*, 288 U.S. 344 (1933). This decision, allowing a crisis cartel among distressed coal producers, was effectively overruled in 1940. *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940). The federal agencies responded to the National Industrial Recovery Act and *Appalachian Coals* by “virtually halt[ing]” antitrust enforcement activity. William E. Kovacic, *The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement*, 17 *TULSA L. J.* 587, 609-10 (1982).

⁶⁶ Once it became apparent during the code-writing process that “organized business had emerged as the dominant economic group ..., criticism of the NRA began to mount.” Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 477 (1966); *see* Robert H. Jackson, *THAT MAN: AN INSIDER’S PORTRAIT OF FRANKLIN D. ROOSEVELT* 66 (2003) (By mid-1935, “it was doubtful if it was not fostering monopoly,” and those favoring restoration of traditional competition “had come to fear” the NRA.)

⁶⁷ Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 479 (1966). The National Industrial Recovery Act was held unconstitutional on commerce clause and delegation doctrine grounds. *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

to regulate big business became more urgent with the recession of 1938,⁶⁸ the stage was set for a political resolution of the longstanding debate among regulatory visions.

Thurman Arnold, a former law professor appointed to lead the Justice Department's Antitrust Division in 1938, took advantage of this political space by reinvigorating government antitrust enforcement.⁶⁹ In a sense, Arnold's program offered something to all sides. For those who wanted to restore competition, Arnold expanded the government's antitrust enforcement capability, used those new resources to attack large firms in concentrated markets, and justified doing so as removing "bottlenecks" to competition. For those who favored national economic planning, Arnold took on firms in one industry after another, seeking systematically to identify and remove industry-specific bottlenecks with multiple enforcement actions. For those who preferred industry self-regulation, Arnold relied upon case-by-case enforcement, which forced the government to prove a competitive problem to an independent judge, and he emphasized the

⁶⁸ In response to that renewed concern, a blue-ribbon panel, the Temporary National Economic Commission (TNEC) was set up by Congress during 1938 to study the economy and regulatory policy. The Commission held extensive hearings and issued its final report during 1941. TNEC did not resolve the longstanding three-cornered debate over regulatory policy, however. Its final report was "as timid as it was unoriginal." Ellis W. Hawley, *THE NEW DEAL AND THE PROBLEM OF MONOPOLY* 465 (1966). That debate was resolved elsewhere in the political system.

⁶⁹ Spencer Weber Waller, *The Antitrust Legacy of Thurman Arnold*, 78 *ST. JOHN'S L. REV.* 569 (2004); Wyatt Wells, *ANTITRUST & THE FORMATION OF THE POSTWAR WORLD* 82 (2002); William E. Kovacic, *The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement*, 17 *TULSA L. J.* 587, 610 (1982) (Arnold's appointment in 1938 "triggered an unparalleled period of activity" at the Antitrust Division and commenced the "restoration of antitrust as an important national policy"); see Richard Hofstadter, *What Happened to the Antitrust Movement?*, in *THE PARANOID STYLE IN AMERICAN POLITICS, AND OTHER ESSAYS* (1979) (dating a revival of antitrust, and its depoliticization, to 1937).

resolution of such cases by consent decree, which allowed the industry to participate in the development of relief and so avoid costly alterations to market structure. Taken as a whole, however, Arnold's approach, placing antitrust enforcement at center stage, added up to something new: it gave close scrutiny to firm conduct in concentrated markets without engaging in ongoing regulatory supervision or systematically sacrificing the efficiencies generated by large firms. In this way, Arnold moved forward the political debate over regulatory policy, which had for decades seemed incapable of resolution.

Arnold resigned in 1943 to accept an appointment as an appellate judge, after the demands of war mobilization had circumscribed Executive Branch interest in antitrust enforcement. By then he had laid the essential groundwork for a new approach to the problem of monopoly. Over the decade of the 1940s, Arnold's use of antitrust law to regulate large firm conduct was accepted by the other branches of government and became the basis of national regulatory policy. The Supreme Court unequivocally established the *per se* rule against horizontal price-fixing in 1940;⁷⁰ the Sherman Act's concern with monopolization was reaffirmed in litigation involving Alcoa in 1945;⁷¹ and Congress toughened the anti-merger statute in 1950.⁷² With these events, antitrust's structural era – in which legal doctrines and

⁷⁰ *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940).

⁷¹ *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d. Cir. 1945). This decision of a specially-created panel of appellate judges is treated as having the same authority as a Supreme Court decision.

⁷² *See Brown Shoe Co. v. United States*, 370 U.S. 294 (1962) (reviewing 1950 amendments to Clayton Act §7).

enforcement were reorganized around hostility to market concentration – was underway.⁷³ To an important extent, moreover, the antitrust enforcement norms established then – particularly the objection to horizontal price-fixing and to mergers leading to troublesome levels of market concentration – continue to shape competition policy today.⁷⁴

Since the mid-20th century, the political salience of regulatory policy and the monopoly problem has receded.⁷⁵ Historian Richard Hofstadter recognized this as early as 1964, when he wrote that the “antitrust movement is one of the faded passions of American reform.”⁷⁶ Another measure is the quadrennial platforms of the major political parties. Both parties began endorsing antitrust enforcement in 1888, and generally continued to do so for a full century, through 1988.⁷⁷

⁷³ For a brief survey of antitrust’s three historical eras – classical, structural, and Chicago school – see Jonathan B. Baker, *A Preface to Post-Chicago Antitrust*, in *POST CHICAGO DEVELOPMENTS IN ANTITRUST ANALYSIS 60-75* (Roger van den Bergh, Roberto Pardolesi and Antonio Cucinotta, eds. 2002).

⁷⁴ *See generally*, William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 61 *ANTITRUST L.J.* 377 (2003); Thomas B. Leary, *The Essential Stability of Merger Policy in the United States*, 69 *ANTITRUST L.J.* 105 (2002). The major discontinuity in antitrust doctrine and enforcement since the mid-20th century, antitrust’s Chicago school revolution of the late 1970s and 1980s, is addressed in Part III below.

⁷⁵ *Cf.* Eleanor Fox and Robert Pitofsky, *Antitrust Policy*, in *CHANGING AMERICA: BLUEPRINTS FOR THE NEW ADMINISTRATION 319, 322-23* (Mark Green, ed. 1992) (“From the late 1930s through 1980, American antitrust was a largely bipartisan program There were ups and downs in enforcement levels and priorities during those decades, but antitrust was accepted as sound and important policy.”)

⁷⁶ Richard Hofstadter, *What Happened to the Antitrust Movement?*, in *THE PARANOID STYLE IN AMERICAN POLITICS, AND OTHER ESSAYS 188* (1979) (preface to essay notes that it was written in 1964).

⁷⁷ The Republican platform was less consistent than the Democratic platform. The Republicans omitted mention of antitrust in 1932, and their 1980 platform singled out for endorsement only the prevention of predatory pricing and gouging of captive customers. They

But the general absence of antitrust planks in party platforms during the last several presidential elections demonstrates that competition policy has become less prominent over time in political debates.⁷⁸

The stylized story describing the emergence of a competition policy bargain among competing interest groups matches this history in broad outline. If the American polity reached a bargain in favor of competition policy – not in the sense of enacting new statutes but by achieving a long-lasting stability in economic regulatory policy – it did so during the decade of the 1940s.⁷⁹ Regulatory policy was highly politicized before that time, and has become much

did not mention antitrust in 1984, but in 1988 they highlighted the administration's record in criminal antitrust enforcement and called for fostering competition in place of government monopolies. Provisions after that date sought modifications: the 1992 Republican platform called for modification of outdated antitrust rules said to impede beneficial hospital mergers, and the 1996 platform endorsed modification of the antitrust laws to allow health care providers to cooperate in holding down charges.

⁷⁸ The continuing importance of disputes about the appropriate extent of tariffs and other barriers to international trade is not inconsistent with the decreasing importance of disputes about antitrust. Unlike arguments about domestic regulatory policy, the political contests involving international trade are not entirely disputes between large and diffuse interest groups of consumers and producers. The producer interests involved in any political bargain over trade restraints – the specific industries seeking trade protection – are often concentrated, while other producer interests – the foreign producers – are not represented in the political process. Moreover, in this arena, consumers generally have no practical option for appropriating producer rents; the pro-consumer and the aggregate welfare-maximizing policies are likely similar.

⁷⁹ *Cf.* Wyatt Wells, *ANTITRUST & THE FORMATION OF THE POSTWAR WORLD* 82 (2002) (“After 1945, compliance with the antitrust statutes became for the first time a regular concern of most large companies.”). By one view, the seeds of this bargain were planted by the Supreme Court's adoption of a rule of reason standard in 1911, coupled with the 1914 enactment of the Federal Trade Commission Act. Together, though “not without about fifteen years of protracted, sharp, and bitter political conflict,” these developments settled the trust question in the polity, by reaching “a nonstatist accommodation of the law to the corporate reorganization of capitalism,” thereby explaining why the trust question quickly “receded from the center of national politics.”

less so since.⁸⁰ But while the story reasonably captures some of the history, it misses at least six other aspects. First, there were arguably two diffuse and opposing interest groups with a stake in regulatory policy, for example, but political debates during the early 20th century coalesced around three, not two positions. This split makes clear that ideas play an independent role in aggregating interests, promoting collective action and shaping political programs in ways not accounted for in the stylized story's focus on interests.⁸¹ Second, while there was no political consensus on regulatory policy before the mid-20th century, policy did not explicitly cycle

Martin Sklar, *THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM, 1880-1916* 167, 173 (1988).

⁸⁰ The decline in political salience of regulatory policy since the 1940s might be attributed not just to a political bargain in favor of competition policy but also in part to post-World War II prosperity (in parallel with the way that anti-business sentiment, and calls for regulation, receded during periods of relative prosperity during earlier decades). This theory has the virtue of connecting the major interruption in that loss of salience – the Chicago school revolution in antitrust of the late 1970s and 1980s, along with the broader deregulation movement of the 1980s – to the major interruption in the long prosperity, the stagflation of the 1970s. It ignores, however, the likelihood that prosperity derives in part from the ability of the economy to obtain static and dynamic efficiency benefits from competition, through antitrust enforcement. *See generally*, Jonathan B. Baker, *The Case for Antitrust Enforcement*, 17 *J. ECON. PERSPECTIVES* 27 (2003). Another possibility is that U.S. acceptance of antitrust was the product of the Cold War political competition between the U.S. and the U.S.S.R., and that the political salience of regulatory policy in the United States faded as the competing economic system lost legitimacy. But antitrust was becoming less important in U.S. political life long before the late 1980s overthrow of state socialism in Eastern Europe and Russia.

⁸¹ For a discussion of the role of ideas in mediating the competition among interests during debates about regulatory policy around the turn of the 20th century, *see generally*, Martin Sklar, *THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM, 1880-1916* 166-73 (1988) (discussing the evolution of federal law on restraint of trade from 1890 to 1920). The complex relationship between economic ideas and legal doctrine during the second half of the 20th century is sketched in Jonathan B. Baker, *A Preface to Post-Chicago Antitrust*, in *POST CHICAGO DEVELOPMENTS IN ANTITRUST ANALYSIS* 60, 67-71 (Roger van den Bergh, Roberto Pardolesi and Antonio Cucinotta, eds. 2002).

between pro-consumer and pro-producer outcomes; instability would be a better characterization.

Third, the ability of the competing interest groups to overcome collective action problems varied with more than the nature of the current policy regime. Adversity appeared to facilitate political success for consumer interests, but in an indirect manner, requiring both experience with an adverse regulatory regime and hard times generally. Thus, industry self-regulation with minimal governmental involvement, the program of big business, was the most discredited during business cycle downturns (during the early 1930s, when the NIRA was enacted and subsequently abandoned, and during the latter part of the same decade, when the Temporary National Economic Committee was created and Thurman Arnold launched his enforcement effort) and most successful during periods of prosperity (the 1920s).

Fourth, the shifting fortunes of the consumer and producer interest group coalitions during the early 20th century cannot be traced directly to shifts in interest group mobilization, as the stylized story supposes. Rather, changes in the political climate affected the decisions of political leaders, whose fortunes were tied to their ability to garner votes in the future. This dynamic can, however, be interpreted as interest group mobilization of a sort: as decision-making based upon forecasts by politicians as to the likely attitudes of voters and their incentives to participate in the next election. Fifth, the acceptance of Thurman Arnold's antitrust enforcement program by the political system was not tied rhetorically to a recognition that an intermediate antitrust policy could generate efficiency gains that could be shared among interest groups, as the stylized story arguably suggests, but that program did find a way to give something valuable to the advocates of each of the three leading regulatory visions. Finally, the political bargain, if it

indeed was one, was not purely a matter of legislative enactment; it took the form of a broad consensus that had developed among the three branches of government. Notwithstanding these qualifications, it is reasonable to conclude that the stylized political bargain story captures an important dynamic in the historical acceptance of competition policy in the U.S.

III. INTERPRETING THE RISE OF THE CHICAGO SCHOOL

The dramatic shift in antitrust doctrine and enforcement policy during the late 1970s and 1980s poses a challenge to the claim that the U.S. adopted a political bargain in favor of efficiency-enhancing competition policy. Antitrust's Chicago school revolution might seem to belie the claim of substantial continuity in the political acceptance of antitrust policy since the 1940s, and so call into question the relevance of the political bargain perspective to understanding U.S. antitrust history.

During the late 1970s and 1980s, many if not most antitrust doctrines – including the rules governing vertical intrabrand restraints, predatory pricing, and horizontal agreements – were reconstructed around an economic approach heavily influenced by the ideas of lawyers and economists associated with the University of Chicago (including Robert Bork, Aaron Director, Frank Easterbrook, Richard Posner, and George Stigler).⁸² If these developments are understood

⁸² For a brief survey of the doctrinal shifts, see Jonathan B. Baker, *A Preface to Post-Chicago Antitrust*, in *POST CHICAGO DEVELOPMENTS IN ANTITRUST ANALYSIS* 60, 65-67 (Roger van den Bergh, Roberto Pardolesi and Antonio Cucinotta, eds. 2002). The intellectual roots of the Chicago school approach to antitrust, with an emphasis on a 1956 article published by Aaron Director and Edward Levi, are explored in James May, *Redirecting the Future: Law and the Future and the Seeds of Change in Modern Antitrust Law*, 17 *MISS. COLL. L. REV.* 43 (1996).

as a successful effort by producers to obtain market power that did not trigger a countervailing political effort by consumers to regulate business – that is, if they are understood as producer interests reneging on a political bargain in favor of competition policy – then this dramatic shift in antitrust doctrine would be inconsistent with the view that producer and consumer interests had by mid-century reached a stable long-term political bargain to adopt competition as the nation’s regulatory regime.⁸³

Certain aspects of the transition from antitrust’s structural era to its Chicago school era arguably suggest a radical non-enforcement agenda, and consequently might be thought to show that the Chicago school revolution is inconsistent with the view of antitrust as a political bargain. These features were particularly noticeable at the Antitrust Division of the Justice Department and the Federal Trade Commission during the second term of the Reagan Administration. Budgets at the federal antitrust agencies declined substantially during the 1980s, and staffing fell by nearly half.⁸⁴ Measured by case initiations, the federal agencies exhibited markedly less

⁸³ Anecdotal evidence suggests that producer interests generally supported the doctrinal changes associated with the rise of the Chicago school, while consumer groups often opposed them. This kind of evidence does not distinguish between the possibility that producers induced the legislature to end a political bargain in favor of competition policy and the possibility that producer interests induced reform of the antitrust laws (by highlighting evidence that structural era doctrines were operating to hamstring producers) without reneging on the fundamental competition policy bargain. Accordingly, interest group views on the Chicago school revolution are not systematically evaluated here.

⁸⁴ From 1980 to 1989, FTC staffing fell from 1719 to 894 full time equivalents. (Statistics available at <http://www.ftc.gov/ftc/oed/fmo/fte2.htm>). The staffing reduction was likely split evenly between the agency’s meeting competition and consumer protection missions. See Kirkpatrick Committee Report, 58 ANTITRUST L.J. 43, 139 (1989) (Graph 2, reporting FTC employment by mission from 1981 through 1988). Authorized positions at the Antitrust Division of the Justice Department declined from 939 in 1980 to 549 in 1989, while the number

interest in attacking exclusionary conduct, whether involving vertical agreements, vertical mergers, or monopolization, and they reduced the rate of merger enforcement generally.⁸⁵ These striking declines in enforcement agency activity were part of a broad social and political reaction during the 1970s to the expansion in the role of government that had taken place during the previous half-century, from the New Deal to the Great Society; it is no accident that they occurred at the same time that deregulation and neoconservatism became familiar words.⁸⁶

of attorneys on-board fell from 409 to 237. Report of the American Bar Association Section of Antitrust Law Task Force on the Antitrust Division of the U.S. Department of Justice A3 (July 1989). During the same years, both FTC and Antitrust Division appropriations held constant in nominal dollars, and thus declined by about 31% in real terms (adjusted for inflation using the GDP deflator). (Appropriations statistics are available at <http://www.usdoj.gov/atr/public/10804a.htm> and <http://www.ftc.gov/ftc/oed/fmo/appropriationhistory.htm>).

⁸⁵ Eleanor Fox and Robert Pitofsky, *Antitrust Policy*, in CHANGING AMERICA: BLUEPRINTS FOR THE NEW ADMINISTRATION 319, 324-25 (Mark Green, ed. 1992) (tables showing declining rates of Justice Department investigation and case filing between 1979 and 1991). Federal enforcers during the Reagan administration as a whole initiated vertical restraints cases at an unusually low rate relative to their predecessors and successors. William E. Kovacic, The Modern Evolution of U.S. Competition Policy Enforcement Norms, 61 ANTITRUST L.J. 377, 460 & 462 (2003). Monopolization cases were rarely initiated throughout the Reagan and first Bush administrations. *See id.* at 449 & 449 n. 246. Vertical merger enforcement increased noticeably after the end of the Reagan administration. *See* Thomas B. Leary, The Essential Stability of Merger Policy in the United States, 69 ANTITRUST L.J. 105, 120 & 128-30 (2002). The rate of merger challenges (horizontal and vertical combined) was substantially lower during the second term of the Reagan administration than during any other presidential term between 1982 and 2000. *Id.* at 139. Moreover, during the mid-1980s, when the Department of Transportation was charged with the review of airline mergers, it allowed two large acquisitions involving carriers with overlapping route networks to proceed notwithstanding Justice Department opposition.

⁸⁶ Fluctuations in enforcement activity during the transition between the structural era and the Chicago school era were dominated by the effects of that transition. Vivek Ghosal, Regime Shifts in Antitrust Law (Working Paper, Georgia Institute of Technology, October 2004), available at http://www.encore.nl/documents/RegimeShiftsinAntitrust_Ghosal_001.pdf (mid to

Moreover, the Reagan Administration proposed wide-ranging new antitrust legislation to Congress.⁸⁷ The legislative package could be read as seeking to circumscribe the scope of various antitrust doctrines and remedies. Among other things, the proposals would have exempted from antitrust review mergers in distressed domestic industries harmed by increased imports;⁸⁸ reduced private damages recovery for lost profits (as would apply in cases brought by

late 1970s regime shift associated with antitrust's Chicago school revolution dominates time series data on case filings). Empirical studies of antitrust enforcement activity over that period generally attribute variation in activity more to political factors than economic ones, consistent with the view that the Chicago school revolution was part of a broad, once-in-a-generation shift in social thought and values. *E.g.* Barry R. Weingast and Mark J. Moran, *Bureaucratic Discretion or Congressional Control? Regulatory Policymaking by the Federal Trade Commission*, 91 *J. POL. ECON.* 765 (1983) (explaining a major shift in both antitrust and consumer protection enforcement at the F.T.C. around the late 1970s in terms of a change in the composition of congressional oversight committees) (confirming the qualitative thesis set forth in William E. Kovacic, *The Federal Trade Commission and Congressional Oversight of Antitrust Enforcement*, 17 *TULSA L. J.* 587, 653 (1982)); B. Dan Wood and James E. Anderson, 37 *AM. J. POL. SCIENCE* 1 (1993) (rejecting economic and bureaucratic explanations for the abrupt shift in Justice Department antitrust enforcement inputs and outputs between 1970 and 1989 in favor of a political explanation); Vivek Ghosal and Joseph Gallo, *The Cyclical Behavior of the Department of Justice's Antitrust Enforcement Activity*, 19 *INT'L J. INDUS. ORG.* 27 (2001) (rejecting private interest group explanation of antitrust enforcement between 1955 and 1994 because, contrary to that theory's prediction, enforcement increased during business cycle downturns); John E. Kwoka, Jr., *Commitment to Competition: An Assessment of Antitrust Agency Budgets Since 1970*, 14 *REV. INDUS. ORG.* 295 (1999) (concluding that antitrust enforcement agency budgets between 1970 and 1997 were affected by the scope of economy-wide regulation, the political party in control of Congress and the Executive Branch, and overall economic activity).

⁸⁷ These legislative proposals, along with transmittal letters from the Attorney General and Secretary of Commerce, are reprinted in 50 *ANTITRUST & TRADE REG. REP. (BNA)* 347 (Special Supp. Feb. 20, 1986). They were endorsed by "leaders of the private antitrust bar." Lloyd Constantine, *The Importance of State Antitrust Enforcement* 3 (June 22, 2004), *available at* <http://www.antitrustinstitute.org/recent2/360.pdf>.

⁸⁸ A distressed industry permitted to use this exemption would not have been able to restrain import competition, however.

terminated dealers or excluded rivals) to single damages;⁸⁹ and modified the merger review standard in ways that would have effectively converted it to an unstructured rule of reason review.⁹⁰ The Department of Justice also proposed, through an amicus brief, that the Supreme Court overturn the longstanding rule of *per se* illegality against resale price maintenance (vertical price-fixing).⁹¹

During the transition to antitrust's Chicago school era, the rhetoric of federal enforcement officials often emphasized the benefits of not-intervening, especially during the second term of the Reagan administration,⁹² and were criticized for inaction.⁹³ Commentators associated with the Chicago school approach recommended that the courts toss out entire categories of prior

⁸⁹ This proposal also gave something to antitrust plaintiffs: under it, actual damages could be increased to include prejudgment interest.

⁹⁰ Specifically, the proposals would have replaced the incipency language and lessening of competition test of the existing merger law with a requirement that a court find "a significant probability" that the merger "will substantially increase the ability to exercise market power." Courts would also have been required to consider "all economic factors" relevant to determining the effect of the merger, including market concentration, entry and expansion by rivals, the nature of the product and terms of sale, conduct of firms in the market, and efficiencies.

⁹¹ See *Monsanto v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 n.7 (1984) (declining to reconsider the *per se* rule against resale price maintenance, although urged to do so by the Solicitor General).

⁹² See, e.g., 60 Minutes with Douglas H. Ginsburg, Assistant Attorney General, Antitrust Division, 55 ANTITRUST L.J. 255, 256-59 (benefits of mergers), 263 (problems with attacking non-price predation), 266 (resale price maintenance investigations are unlikely to yield cases) (1986); cf. 60 Minutes with Daniel Oliver, Chairman, Federal Trade Commission, 56 ANTITRUST L.J. 239, 239-40 (1987) (principal source of restrictions on competition is government).

⁹³ Eleanor Fox and Robert Pitofsky, *Antitrust Policy*, in CHANGING AMERICA: BLUEPRINTS FOR THE NEW ADMINISTRATION 319 (Mark Green, ed. 1992).

prohibitions, especially in the area of vertical restraints,⁹⁴ and some commentators called for scrapping the antitrust laws entirely.⁹⁵

These efforts at antitrust reform never added up to replacing a competition regime with a regulatory regime systematically allowing the exercise of market power, however. One reason is that Congress balked: The Justice Department's controversial legislative proposals were not enacted, and Congress prevented the Justice Department from pursuing in oral argument at the Supreme Court its amicus efforts to relax the prohibition against resale price maintenance.⁹⁶

⁹⁴ *E.g.* Richard A. Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6 (1981); *cf.* Frank H. Easterbrook, *The Limits of Antitrust*, 65 TEX. L. REV. 1, 19-23 (1984) (advocating inquiry into defendant(s) market power as initial screen, and suggesting that absence of such power would provide a basis for dismissing antitrust cases without further inquiry).

⁹⁵ *E.g.* D.T. Armentano, *ANTITRUST POLICY: THE CASE FOR REPEAL* (1986); William F. Shugart II, *Don't Revise the Clayton Act, Scrap It!*, 6 CATO J. 925 (1987). Antitrust skeptics most commonly argue that market power is transient and self-correcting (unless protected by government action), while government intervention to protect competition, however well-intentioned, is often ineffectual or counterproductive. *E.g.* Lester C. Thurow, *THE ZERO-SUM SOCIETY: DISTRIBUTION AND THE POSSIBILITIES FOR ECONOMIC CHANGE* 127, 145-50 (1980); Fred L. Smith, Jr., *The Case for Reforming the Antitrust Regulations (If Repeal is Not an Option)*, 23 HARV. J. L. & PUB. POL'Y 23 (1999-2000); Clyde Wayne Crews, Jr., *The Antitrust Terrible 10: Why the Most Reviled 'Anti-Competitive' Business Practices Can Benefit Consumers in the New Economy*, Cato Policy Analysis No. 405, at 16 (June 18, 2001) (describing antitrust as "just another form of inefficient economic regulation"). Other antitrust skeptics advocate displacing competition policy in favor of broader industrial planning. Stuart E. Eizenstat, *Reindustrialization Through Government-Business-Labor Alliance*, 53 ANTITRUST L.J. 105 (1984) (recounting views of senior trade officials during the Reagan administration, and advocating the inclusion of antitrust policy within a coordinated industrial policy process).

⁹⁶ After the United States had filed an amicus brief urging that the Supreme Court overrule the *per se* prohibition against resale price maintenance, Congress prohibited the expenditure of funds by the Antitrust Division to pursue that position in oral argument. *See Monsanto v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 n.7 (1984) (Solicitor General's position taken "by brief only"). Congress enacted a joint resolution in 1985 calling on the

After the Reagan administration, moreover, federal enforcement agency budgets and staffing increased⁹⁷ and the longstanding norm protecting individual enforcement decisions from political influence was not undermined.

The states balked as well. During the Reagan administration, they formed a national task force to coordinate their individual efforts,⁹⁸ and issued enforcement guidelines setting out a more interventionist policy than the federal agencies had adopted with respect to vertical agreements and horizontal mergers.⁹⁹ The states then became more active in antitrust

attorney general to withdraw the Antitrust Division's then-new vertical restraints guidelines. 1985 H.R. 2965 (P.L. 99-180). The House and Senate also both passed bills that would have reaffirmed the related rule preventing manufacturers from cutting off discounting dealers by agreement with full service dealers, but legislation was never enacted because of a dispute over whether to exempt firms lacking market power. *See* House Defeats Conference Report on Resale Price Maintenance Measure, 63 ANTITRUST & TRADE REG. REP. (BNA) 3 (July 2, 1992).

⁹⁷ FTC statistics are available at <http://www.ftc.gov/ftc/oed/fmo/fte2.htm> and <http://www.ftc.gov/ftc/oed/fmo/appropriationhistory.htm>; Antitrust Division appropriation statistics are available at <http://www.usdoj.gov/atr/public/10804a.htm>.

⁹⁸ The Multistate Antitrust Task Force of the National Association of Attorneys General was formed in 1983, *see* David W. Lamb, *Avoiding Impotence: Rethinking the Standards for Applying State Antitrust Laws to Interstate Commerce*, 54 VAND. L. REV. 1705, 1715 (2001). At the start of the second term of the Reagan Administration, in March 1985, the states "decided to enter the national enforcement market" and become "de facto a third national antitrust agency." Lloyd Constantine, *The Mission and Agenda for State Antitrust Enforcement*, 36 ANTITRUST BULL. 835, 840 (1991). *See also* Lloyd Constantine, *The Importance of State Antitrust Enforcement* (June 22, 2004), *available at* <http://www.antitrustinstitute.org/recent2/360.pdf>.

⁹⁹ National Association of Attorneys General, *Vertical Restraint Guidelines*, 49 ANTITRUST & TRADE REG. REP. (BNA) 996 (Dec. 5, 1985) (issued Dec. 4, 1985). These Guidelines were revised in 1988 and 1995. National Association of Attorneys General, *Horizontal Merger Guidelines*, 52 ANTITRUST & TRADE REG. REP. (BNA) Special Supplement (March 12, 1987) (issued March 10, 1987). These Guidelines were revised in 1993.

enforcement,¹⁰⁰ emphasizing areas that the federal agencies chose not to pursue.¹⁰¹ In recognition of the more activist role of the states, the Antitrust Section of the American Bar Association began in 1990 routinely inviting a leader of the state task force to join its annual enforcement roundtable, traditionally presented by the Assistant Attorney General for Antitrust and the Chairman of the Federal Trade Commission.

With judicial acceptance of Chicago school views, the regulatory landscape changed dramatically but not fundamentally. Antitrust hostility to cartels has not decreased; the merger waves of the late 1970s and late 1990s were not the product of doctrinal changes in antitrust and

¹⁰⁰ The new antitrust activism of state attorneys general was criticized at that time by the Chairman of the Federal Trade Commission. 60 Minutes with Daniel Oliver, Chairman, Federal Trade Commission, 56 ANTITRUST L.J. 239, 245-47 (1987); 60 Minutes with Daniel Oliver, Chairman, Federal Trade Commission, 57 ANTITRUST L.J. 235, 242-43 (1987) (describing state enforcers as a “group of antitrust counter-revolutionaries”).

¹⁰¹ During the late 1980s, various states attacked resale price maintenance by Minolta and Panasonic; those cases were resolved by settlement. See 50 ANTITRUST & TRADE REG. REP. (BNA) 372 (Feb. 27, 1986) (Minolta case filed); 53 ANTITRUST & TRADE REG. REP. (BNA) 56 (July 9, 1987) (Minolta case settled); 56 ANTITRUST & TRADE REG. REP. (BNA) 89 (Jan. 19, 1989) (Panasonic case filed); 56 ANTITRUST & TRADE REG. REP. (BNA) 428 (March 16, 1989) (Panasonic case settled). The states challenged a debit card joint venture by Master Card and Visa, and settled the case with an agreement that terminated the venture. 57 ANTITRUST & TRADE REG. REP. (BNA) 156 (Aug. 3, 1989) (case filed); 58 ANTITRUST & TRADE REG. REP. (BNA) 709 (May 10, 1990) (case settled). States also brought and later settled a complaint against a number of insurance companies, charging group boycotts that resulted in anticompetitive restrictions on the scope and availability of insurance coverage to municipalities. 54 ANTITRUST & TRADE REG. REP. (BNA) 499 (March 24, 1988) (case filed); 67 ANTITRUST & TRADE REG. REP. (BNA) 434 (Oct. 13, 1994). Federal antitrust enforcers did not join in any of these cases. During this period, the states saw themselves as the primary governmental enforcers of vertical restraints law. Robert Abrams and Lloyd Constantine, *Dual Antitrust Enforcement in the 1990s*, in REVITALIZING ANTITRUST IN ITS SECOND CENTURY 488 (Harry First, Eleanor M. Fox and Robert Pitofsky, eds.) (“In areas such as price and nonprice vertical restraints, the states are the only governmental keepers of the flame.”).

did not concentrate markets in a manner reminiscent of the merger wave around 1900; and there is no reason to think that market power is being exercised more today than during the 1950s and 1960s. Accordingly, if the U.S. political system is understood as having adopted an interest group bargain in favor of competition policy during the 1940s, it is difficult to describe these events four decades later as discarding competition in favor of a regulatory regime that did not police the exercise of market power.

Much of the Chicago school revolution aimed at reform of the antitrust laws rather than repeal.¹⁰² The central economic critique of structural era antitrust was that those earlier doctrines, in their single-minded focus on preventing the harms that could arise from market concentration, systematically deterred procompetitive practices. But the lawyers and economists who provided

¹⁰² To “identify” successful coordination among interest groups (as that term is used by empirical economists), one might ask whether, after the time the competition policy bargain is said to have been reached, antitrust law and enforcement took advantage of opportunities to reform doctrinal rules and enforcement approaches, as they arose, in order to increase the gains to aggregate welfare. *Cf.* Timothy F. Bresnahan, *The Oligopoly Solution is Identified*, 10 *ECON. LETTERS* 87 (1982) (analogous method of identifying coordination among firms playing a repeated prisoners’ dilemma). If the Chicago school revolution is understood as an episode of reform rather than repeal, the answer is surely yes. Antitrust has arguably institutionalized a method of ongoing reform based on incorporating developments in economic theory and empirical economic methodologies for case targeting and evaluation. These developments are incorporated most importantly through the work of economists at the antitrust enforcement agencies and expert witnesses in court proceedings. *See* Jonathan B. Baker, “Continuous” Regulatory Reform at the Federal Trade Commission, 49 *ADMIN. L. REV.* 859 (1997) (agency use of economics); *cf.* Jonathan B. Baker, *A Preface to Post-Chicago Antitrust*, in *POST CHICAGO DEVELOPMENTS IN ANTITRUST ANALYSIS* 60, 68-70 (Roger van den Bergh, Roberto Pardolessi and Antonio Cucinotta, eds. 2002) (describing complex relationship between economic developments and legal change in antitrust). As a result, recent antitrust enforcement exhibits a growing hospitality to econometric evidence and to post-Chicago developments in economic thinking, most notably game theoretic approaches. *See* Jonathan B. Baker and Daniel L. Rubinfeld, *Empirical Methods in Antitrust Litigation: Review and Critique*, 1 *AM. L. & ECON. REV.* 386 (1999) (use of econometrics).

the intellectual support for doctrinal adaptation, the federal enforcers who encouraged that trend, and the courts have consistently and strongly expressed concern about horizontal collusion. Consequently, they have defended an aggressive role for antitrust enforcement in challenging naked horizontal price-fixing and market division, and mergers among rivals creating high concentration.¹⁰³ Arguments about the social costs of structural era antitrust rules gained plausibility in part because they appeared during an economy-wide productivity slowdown,¹⁰⁴ and because the courts adopted Chicago school views about antitrust during an era of more general bipartisan regulatory reform.¹⁰⁵

To a substantial extent, moreover, the shift in antitrust doctrine that took place during the late 1970s and 1980s appears to reflect a bipartisan consensus,¹⁰⁶ consistent with the view that

¹⁰³ *E.g.* Robert H. Bork, *THE ANTITRUST PARADOX* 221 (horizontal mergers), 263 (cartels), (1978); 60 Minutes With Charles F. Rule, Acting Assistant Attorney General, Antitrust Division, 56 *ANTITRUST L.J.* 261 (1987) (highlighting criminal price-fixing and horizontal merger enforcement).

¹⁰⁴ Martin Neil Baily and Alok K. Chakrabarti, *INNOVATION AND THE PRODUCTIVITY CRISIS* (1988).

¹⁰⁵ Part of the regulatory reform movement involved the dismantling of rate regulation schemes in transportation, financial services, energy and communications. Clifford Winston, *Economic Deregulation: Days of Reckoning for Microeconomists*, 31 *J. ECON. LIT.* 1263 (1993). These reforms generally replaced price controls with antitrust enforcement; they did not free deregulated industries from both price controls and antitrust. For example, the 1996 law deregulating telecommunications included rules aimed to assure a transition to a competitive market. With airline deregulation, the authority to challenge mergers was originally given to the Department of Transportation, which allowed some large mergers over the opposition of the Justice Department. After those events, Congress shifted merger review to Justice.

¹⁰⁶ *See generally*, William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 61 *ANTITRUST L.J.* 377, 460 & 462 (2003). Partisan divisions with respect to antitrust have not disappeared entirely in the Chicago school era, however, particularly with respect to allegations of anticompetitive exclusion (which most commonly arise in the review of

they represent efficiency-enhancing reforms.¹⁰⁷ Post-Chicago economic developments generally tend to point antitrust in a more interventionist direction, but without suggesting that the doctrinal changes of the 1970s and 1980s should be overturned in favor of a return to antitrust's structural era.¹⁰⁸ Any suggestion today that the antitrust laws do more harm than good and so

vertical practices, group boycotts and monopolization claims). The number of federal monopolization cases initiated during the eight years covering the most recent Democratic administration was nearly triple the number brought during the twelve years covering the two Republican administrations that preceded it, for example. *Id.* at 449. Federal enforcers during the Clinton administration also filed vertical restraints cases, which often involved an exclusion theory, at more than double the rate as did their predecessors in Reagan and first Bush administrations. *Id.* at 460. The Clinton administration cases included high profile actions against American Airlines, Intel, Microsoft, and Mylan. Notwithstanding these partisan differences over the appropriate scope of enforcement against anticompetitive exclusion in practice, there is little partisan dispute over the principle that exclusion can harm competition and that if that can be proved, and a suitable remedy devised, antitrust enforcement is properly undertaken. The Antitrust Division during the second Bush administration, which takes a distinctly less interventionist view of exclusion than its Clinton administration predecessor, chose to pursue the *American Airlines* predatory pricing case on appeal. See *United States v. AMR Corp.*, 335 F. 3d 1109 (10th Cir. 2003). Similarly, the district court's finding of liability in *Microsoft* was affirmed unanimously by the D.C. Circuit sitting *en banc*. *United States v. Microsoft Corp.*, 253 F.3d 34 (2001) These appellate judges included Douglas Ginsburg, a conservative antitrust expert who headed the Antitrust Division during the second term of the Reagan administration, the least interventionist period for federal enforcement in modern antitrust history. Robert Bork, one of the leading commentators associated with the rise of the Chicago school, has long endorsed the Supreme Court's prohibition of unjustified exclusionary conduct by a monopolist in *Lorain Journal*. Robert H. Bork, THE ANTITRUST PARADOX 344-46 (1978) (discussing *Lorain Journal Co. v. United States*, 342 U.S. 143 (1951)). Bork cited that decision as the basis for his support for the monopolization suit against Microsoft. Robert H. Bork, *The Case Against Microsoft* (1998), available at <http://www.procompetition.org/research/bork.html>.

¹⁰⁷ Producers and consumers would be expected to share efficiency gains available through regulatory reform, limiting the extent of partisan debate as to those reforms relative to the debate over policies that would benefit one group at the expense of another.

¹⁰⁸ Post-Chicago criticisms of current antitrust doctrine largely accept the economic approach, and call for modifications to existing rules based upon the application of game

should be repealed entirely remains outside the mainstream consensus,¹⁰⁹ and for good reason.¹¹⁰

In short, even if the Chicago school revolution is understood as an effort by some producer interests to renege on a political bargain in favor of competition policy, rather than an effort to reform the antitrust laws, any attempt to hollow out the antitrust laws ended far short of success.¹¹¹ Many aspects of the competition policy bargain were modified, but the basic

theoretic tools and new empirical economic methods. The doctrinal adjustments that have resulted – unilateral effects in merger analysis, raising rivals’ costs analysis of exclusion, and the like – are better understood as further reforms that improve the targeting of antitrust enforcement efforts than as doctrinal changes conferring monopsony power on consumers. For a brief survey of post-Chicago possibilities for the evolution of antitrust doctrine that have been explored by the federal antitrust agencies and the courts, or suggested in commentary, see Jonathan B. Baker, *A Preface to Post-Chicago Antitrust*, in *POST CHICAGO DEVELOPMENTS IN ANTITRUST ANALYSIS* 60, 70 (Roger van den Bergh, Roberto Pardolesi and Antonio Cucinotta, eds. 2002). *See also*, Jonathan B. Baker, *Recent Developments in Economics that Challenge Chicago School Views*, 58 *ANTITRUST L. J.* 645 (1989).

¹⁰⁹ *See* Robert W. Crandall and Clifford Winston, *Does Antitrust Policy Improve Consumer Welfare? Assessing the Evidence*, 17 *J. ECON. PERSPECTIVES* 1 (2003) (questioning the empirical basis for antitrust policy without calling for repeal).

¹¹⁰ Jonathan B. Baker, *The Case for Antitrust Enforcement*, 17 *J. ECON. PERSPECTIVES* 27, 45 (2003).

¹¹¹ In terms of the political bargain perspective, this outcome could be described as resulting from the mobilization of governmental actors – including state attorneys general, Congress and the courts – on behalf of consumer interests to prevent doctrinal change from going so far as to overturn the political bargain in favor of competition policy. The rise of the Chicago school could have an analogous interpretation: as a reaction by producer interests to a fear that consumer interests during the 1970s were attempting to renege on the competition policy bargain in favor of a pro-consumer regulatory regime that would seek to deconcentrate major industries. *See* William E. Kovacic, *Failed Expectations: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration*, 74 *IOWA L. REV.* 1105 (1989); *cf.* Thomas B. Leary, *The Essential Stability of Merger Policy in the United States*, 69 *ANTITRUST L.J.* 105, 109-110 (2002) (recounting the reaction to a 1977 speech by a new FTC Chairman that ascribed broad social and political objectives to antitrust policy: it “alarmed those opposed to big government generally” as well as “many mainstream antitrust supporters”).

agreement on competition policy as the appropriate regulatory regime has continued.¹¹²

It is possible that this interpretation of the Chicago school revolution – as reform of counterproductive doctrines but not as a successful pro-producer rejection of competition as the fundamental domestic regulatory regime – focuses on the largely intact antitrust edifice without regard for its crumbling foundations. If so, the most important long term political effect of antitrust’s shift to an economic approach, and the concomitant rejection of social and political goals that were important in antitrust’s past, has yet to become apparent in Congress and the courts. That effect would be in lessening the advantages of competition policy to small business interests, and so making it more difficult for consumers to organize politically to oppose any efforts by producer groups to repeal the antitrust laws. The resulting reduction in political support, in this possible interpretation, could set the stage for political acceptance of the anti-antitrust views of some conservative political activists.¹¹³

¹¹² In the present political environment, the most plausible route for producers to renege on the competition policy bargain may involve an expansion of intellectual property rights in order to constrict the application of the antitrust laws. Antitrust officials from both parties have spoken out against this possibility. Robert Pitofsky, *Challenges of the New Economy: Issues at the Intersection of Antitrust and Intellectual Property*, 68 *ANTITRUST L.J.* 913 (2001) (views of FTC Chairman during the Clinton Administration); *To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy* (Federal Trade Commission, October 2003), *available at* <http://www.ftc.gov/opa/2003/10/cpreport.htm> (report issued during George W. Bush administration); *but cf.* R. Hewitt Pate, Acting Assistant Attorney General, Antitrust Division, DOJ, *Antitrust and Intellectual Property*, Speech before the AIPLA, January 24, 2003, *available at* <http://www.usdoj.gov/atr/public/speeches/200701.pdf> (defending Federal Circuit jurisprudence on the antitrust treatment of refusals to license as not representing an expansion of intellectual property rights at the expense of competition, contrary to the claim of former FTC Chairman Pitofsky).

¹¹³ *E.g.* Americans for Tax Reform, *Comments Regarding Commission Issues for Study* (filed before the Antitrust Modernization Commission, Sept. 9, 2004) (letter signed by Grover G. Norquist), *available at* http://www.amc.gov/commission_study_issues.htm (“... it seems clear

This theory is hard to credit, however, given the limited degree of lobbying by producer interests for antitrust repeal a quarter-century after the Chicago school revolution. It also does not account for the extent to which consumer groups have organized political institutions since 1940, amplifying the political influence of consumer interests.¹¹⁴ In particular, this theory does not account for the increasing role of state attorneys general in antitrust enforcement over the past two decades. The states strengthen consumer interests to the extent they use their enforcement authority and political position to help consumers overcome collective action problems. In addition, business consultants, at least those with broad, cross-industry perspective such as Michael Porter and those associated with the McKinsey Global Institute, may also be emerging as advocates of competition policy as an institutional mechanism for achieving productivity growth.¹¹⁵ Accordingly, even from a long run perspective, the Chicago school revolution appears better described as an episode of reform rather than repeal, and thus consistent with the

that the antitrust laws, if they ever served a useful purpose, now only exist to stifle productivity growth and development of new products and services); Robert Levy, *Antitrust*, in CATO HANDBOOK FOR CONGRESS: POLICY RECOMMENDATIONS FOR THE 108TH CONGRESS §38 (2002), available at <http://www.cato.org/pubs/handbook/handbook108.html> (calling for repeal of the antitrust laws).

¹¹⁴ Cf. Samuel P. Hays, *Political Choice in Regulatory Administration*, in REGULATION IN PERSPECTIVE: HISTORICAL ESSAYS 153 (Thomas K. McCraw, ed., 1981) (Before 1940, “competition among producers” was the primary source of regulatory action, while after World War II, the “role of consumers began to change from one of passive choosers in the marketplace to collective action in the political arena”).

¹¹⁵ See Jonathan B. Baker and Steven C. Salop, *Should Concentration be Dropped from the Merger Guidelines?*, in ABA Antitrust Section Task Force Report, PERSPECTIVES ON FUNDAMENTAL ANTITRUST THEORY 339-54, July 2001 (recounting comments by Michael Porter); William W. Lewis, *THE POWER OF PRODUCTIVITY: WEALTH, POVERTY, AND THE THREAT TO GLOBAL STABILITY* (2004) (reporting on research by McKinsey Global Institute).

perspective of a continuing competition policy bargain between diffuse consumer and producer interests.

In sum, it is tempting but ultimately unconvincing to describe antitrust's Chicago school revolution as a successful attempt by producers to walk away from a political bargain in favor of competition policy, replacing antitrust with a regulatory regime permitting the exercise of market power. Rather, the rise of the Chicago school can better be understood either as reform of the antitrust laws to increase the efficiency gains from competition and avoid the possibility that the political bargain for competition would become disadvantageous for producers, or else as a thwarted attempt by producers to renege on that political bargain. Under either of these interpretations, these events are consistent with the political bargain view of competition policy.

IV. THE WELFARE STANDARD DEBATE

The political bargaining interpretation of competition policy offers a new perspective on the longstanding debate over what welfare function antitrust enforcers and courts should maximize.¹¹⁶ Today, the welfare standard question is commonly posed as a choice between two

¹¹⁶ Welfare issues are discussed using a partial equilibrium framework, consistent with the convention in commentary. Intermediate buyers are treated as honorary consumers, as benefits to intermediate buyers are commonly presumed to be passed-through at least in part to consumers (although the question could be susceptible to analysis). Hence buyer welfare is routinely identified with consumer welfare. The choice of welfare standard, the question emphasized here, is independent of another contested issue involving the comparison of benefits and harms not addressed here: whether the victims and beneficiaries of the conduct under review should be treated as an aggregate. The latter issue most commonly arises when out-of-market benefits are proffered as justification for within-market harm, regardless of whether a consumer welfare standard or an aggregate welfare standard is applied. In theory, disputes over the choice of welfare standard and the permissibility of cross-market tradeoffs could be resolved by

alternatives suggested by the partial equilibrium framework for evaluating welfare effects in individual markets.¹¹⁷ Some contend that conduct should be evaluated by its harm to aggregate welfare, measured by lost total surplus (consumers' plus producers' surplus),¹¹⁸ while others argue that it should be tested by its harm to consumers alone, measured by lost consumers' surplus.¹¹⁹ On policy grounds, an aggregate surplus standard is defended primarily as increasing

identifying the consumption streams for all individuals resulting alternative policies and applying a social welfare function to make the comparison, but this kind of analysis is not practical.

¹¹⁷ In the wake of antitrust's Chicago school revolution, the antitrust laws are now most commonly understood as advancing economic goals, largely excluding social and political goals that were important in the past. See Jonathan B. Baker, *A Preface to Post-Chicago Antitrust*, in POST CHICAGO DEVELOPMENTS IN ANTITRUST ANALYSIS (Roger van den Bergh, Roberto Pardolesi and Antonio Cucinotta, eds., 2002), pp. 60-75. For examples of modern commentary advocating greater attention to a broader range of goals, see Eleanor M. Fox and Lawrence Sullivan, *Antitrust – Retrospective and Prospective: Where Are We Coming From? Where Are We Going?* 62 N.Y.U. L. REV., 936 (1987) (rivalry); Robert H. Lande, *Resurrecting Incipiency: From Von's Grocery to Consumer Choice*, 68 ANTITRUST L. J. 875 (2001) (consumer choice); Stephen F. Ross, *Network Economic Effects and the Limits of GTE Sylvania's Efficiency Analysis*, 68 ANTITRUST L. J. 875 (2001) (equal economic opportunity); Maurice E. Stucke and Allen P. Grunes, *Antitrust and the Marketplace of Ideas*, 69 ANTITRUST L. J. 249 (2001) (diversity of voices); Richard Brunell, *Delocalization as a Factor in Merger Analysis* (unpublished manuscript 2004) (local community ties). Some of these articles can be understood within an economic approach as calling attention to certain external costs of promoting competition not accounted for within the traditional partial equilibrium framework.

¹¹⁸ E.g. Robert H. Bork, *THE ANTITRUST PARADOX* (1978). Bork uses the confusing terminology of "consumer welfare" to refer to an aggregate surplus standard.

¹¹⁹ Steven C. Salop, *Question: What is the Real and Proper Antitrust Welfare Standard? Answer: The True Consumer Welfare Standard* (November 2005), available at http://www.amc.gov/public_studies_fr28902/exclus_conduct_pdf/051104_Salop_Mergers.pdf; Robert H. Lande, *Chicago's False Foundation: Wealth Transfers (Not Just Efficiency) Should Guide Antitrust*, 58 ANTITRUST L.J. 631 (1989); see Joseph Kattan, *Efficiencies and Merger Analysis*, 62 ANTITRUST L.J. 513, 528 (1994) (consumer welfare standard is congressionally mandated).

social wealth.¹²⁰ A consumers' surplus standard is defended primarily on grounds of distributional fairness to consumers, although the adoption of a consumer welfare standard in merger enforcement has also been justified on instrumental grounds, as a way of maximizing aggregate welfare for reasons unconnected with the political economy considerations highlighted in this article.¹²¹

¹²⁰ Cf. Louis Kaplow and Steven Shavell, FAIRNESS AND EFFICIENCY 29-38 (2002) (arguing that the policy analysis of legal rules outside those governing the tax and transfer system should generally focus on efficiency considerations rather than distributional ones); *but cf.* Thomas W. Ross and Ralph A. Winter, The Efficiency Defense in Merger Law: Economic Foundations and Recent Canadian Developments, 72 ANTITRUST L.J. 471, 472-73 (2005) (advocating a merger standard expressed as a weighted sum of producer surplus and consumer surplus, with the weights chosen to harmonize the degree of redistribution under the antitrust laws with what a polity has chosen in implementing tax policy). Aggregate surplus is at best only a rough approximation to Pareto efficiency, the welfare concept most commonly employed by economists.

¹²¹ The consumer surplus standard operates as a commitment device employed by antitrust enforcers and courts in order to promote aggregate welfare when merging firms are better able to lobby enforcers than are consumers. Damien J. Neven and Lars-Hendrik Röller, Consumer Surplus vs. Welfare Standard in a Political Economy Model of Merger Control (Working Paper, December 2003); Joseph Farrell, *Negotiation and Merger Remedies: Some Problems*, in Francois Lévêque and Howard Shelanski, eds. MERGER REMEDIES IN AMERICAN AND EUROPEAN COMPETITION LAW (2004). It also induces firms on average to propose mergers that generate efficiencies rather than harm competition, given that firms know more about likely costs savings than do enforcers. David Besanko and Daniel F. Spulber, Contested Mergers and Antitrust Policy, 9 J. L. ECON. & ORG. 1 (1993); *see* Joseph Farrell, *Negotiation and Merger Remedies: Some Problems*, in Francois Lévêque and Howard Shelanski, eds. MERGER REMEDIES IN AMERICAN AND EUROPEAN COMPETITION LAW (2004) (some enforcer hostility to efficiency claims can discourage merging firms from seeking out deals that would confer both efficiencies and market power), and given that enforcers have difficulty in obtaining the information necessary to prove the availability of practical less restrictive alternatives while the merging firms can commonly restructure contracts easily to obtain efficiencies at less threat of harm to competition. Steven C. Salop, Question: What is the Real and Proper Antitrust Welfare Standard? Answer: The True Consumer Welfare Standard (November 2005), available at http://www.amc.gov/public_studies_fr28902/exclus_conduct_pdf/051104_Salop_Mergers.pdf; Sven-Olof Fridolfsson, A Consumer Surplus Defense in Merger Control (February 2002), available at http://congrega.fund.uc3m.es/earie2002/papers/paper_309_20020326.pdf.

The two welfare standards commonly lead to the same conclusion as to whether competition has been harmed by the conduct under review.¹²² Hard core cartel conduct, for example, raises prices to consumers, reducing consumers' surplus while simultaneously reducing aggregate surplus.

But in at least five settings, application of the two standards could yield different conclusions. The first involves an agreement among rivals (a horizontal merger or joint venture) that reduces competition, resulting in higher prices or other consumer harm, such as reduced quality or lessened likelihood of new product introduction. If, in addition, the ensuing allocative efficiency loss is less than the production efficiency benefit that arises from fixed cost savings or from variable cost savings not passed through to buyers, then the antitrust evaluation of the agreement turns on the welfare standard. Such an agreement would be considered harmful under a consumer welfare standard, because prices rose, but not under an aggregate welfare standard, as aggregate surplus increased (the production cost savings exceeded the allocative efficiency loss).

Second, suppose that the merger of two inefficient firms would allow them to lower costs and prices, and so to divert sales from the low cost producer. (A high cost producer can survive because products are differentiated.) If market demand is relatively inelastic, the allocative efficiency consequences of the transaction will likely be dominated by the increase in overall production costs arising from the shift in production away from the low cost firm. Then the

¹²² Terry Calvani, *Rectangles & Triangles: A Response to Mr. Lande*, 58 ANTITRUST L.J. 657 (1989); *cf.* Gary L. Roberts and Steven C. Salop, *Efficiencies in Dynamic Merger Analysis*, 19 WORLD COMP. 5 (1996) (part of the tension between consumer welfare and aggregate welfare standards is resolved by recognizing that efficiencies may be emulated by rivals and so passed through to consumers).

merger would be harmful under an aggregate welfare standard but beneficial under a consumer welfare standard.¹²³

Third, the exclusionary conduct of a dominant firm or a group of firms acting collectively that harms rivals could under some circumstances lead to lower consumer prices, perhaps by preventing free-riding or ending double marginalization. This conduct would be beneficial if tested under a consumer welfare standard, because price declines. But under an aggregate welfare standard, the practice could either be beneficial or harmful on balance. The welfare benefit would include production efficiency gains from any reduction in marginal cost, and an allocative efficiency gain generated by the expansion of output associated with lower prices. That benefit would be compared with the welfare loss to the excluded rivals (their lost producers' surplus). If the welfare loss dominates,¹²⁴ the conduct would be found harmful under an aggregate welfare standard.¹²⁵

The fourth setting involves an agreement among end-use consumers to exercise monopsony power in an input market. Consumer prices decline, so the agreement is not harmful if tested under a consumer welfare standard. But the agreement also creates an allocative

¹²³ This example was suggested by Steven C. Salop. It shows that the aggregate welfare standard is not necessarily more generous to merging firms than the consumer welfare standard.

¹²⁴ This could happen, for example, if market demand is relatively inelastic, so any allocative efficiency gain is small, and the production cost savings are small, while the exclusionary impact of the conduct is substantial.

¹²⁵ This example was suggested by Steven C. Salop. As the example implies, the aggregate welfare test calls for a more interventionist approach to exclusion than the consumer welfare test. However, conservative antitrust commentators who claim to accept the aggregate welfare standard over the consumer welfare standard have not embraced this implication of their position.

efficiency loss, both because output is reduced and because sellers may be led to invest less in the future than they would have invested in a competitive market. Hence the agreement would be considered harmful under an aggregate welfare standard.

Finally, consider practices that facilitate price discrimination, as by making it easier for firms to target buyers with different willingness to pay or by preventing buyer arbitrage.¹²⁶ The result could be an allocative efficiency gain along with a reduction in consumers' surplus.¹²⁷ If so, the practices would be considered unreasonable if reviewed under a consumer welfare standard but reasonable under an aggregate welfare standard.

The political bargain view of antitrust suggests a role for aggregate surplus, consumers' surplus and producers' surplus – a role for all three welfare concepts – in testing proposed antitrust enforcement actions. In particular, it suggests that antitrust enforcers and courts should seek to maximize aggregate surplus, so long as consumers and producers sufficiently share the efficiency gains, at least on average, in order to ensure that neither group can do better by renegeing on the political bargain. This condition does not mandate any particular split of the efficiency gains, so long as consumers on average do at least as well as they would absent a

¹²⁶ In the airline industry, for example, advance purchase and Saturday night stay requirements might be a way of targeting business travelers (who often would not be willing or able to accept such restrictions) for higher prices, and a requirement that passengers show identification before boarding may help the airlines prevent leisure travelers from reselling their tickets to business travelers with higher willingness to pay. The antitrust treatment of such practices might depend in part on whether they are adopted unilaterally or by agreement among firms.

¹²⁷ For example, a shift from uniform pricing at a price in excess of marginal cost to perfect price discrimination would increase aggregate surplus while reducing consumers' surplus. But it is possible to construct other examples in which instituting price discrimination increases both consumer and aggregate welfare.

competition regime, and producers on average also do at least as well as they would absent a competition regime.

Aggregate surplus matters in the stylized story because the efficiency gains from competition relative to the alternative – regulatory regime cycles between market power and price controls – help make it possible for producers and consumers to bargain to a competition regime in repeated play. But consumers’ surplus also matters, as consumers would organize politically to seek price control regulation unless they are confident that they will do better under a competition regime.¹²⁸ Similarly, producers’ surplus matters. If competition enforcement does not systematically protect producers from overly-stringent antitrust rules and relief (and the rules are not reformed when that possibility is threatened), producers would come to see the political bargain as disadvantageous, and would organize politically to seek repeal of the antitrust laws.¹²⁹

Of these two constraints, the protection of consumers is by far the more important one in practice today. Antitrust’s Chicago school revolution was so successful at reorienting antitrust doctrine to protect producers from enforcement practices and doctrinal rules that might

¹²⁸ *Cf.* Oliver E. Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoffs*, 58 *AM. ECON. REV.* 18, 28 (1968) (transfers from consumers to producers may be regarded unfavorably because they produce social discontent, with serious efficiency implications).

¹²⁹ *Cf.* Daron Acemoglu, Simon Johnson, and James Robinson, *Institutions as the Fundamental Cause of Long-Run Growth* 59 (NBER Working Paper 10481, May 2004) (examples in which interest groups, some large and diffuse, have employed their political power to prevent distortionary policies that would harm their interests); Gene M. Grossman and Elhanan Helpman, *Protection for Sale*, 84 *AM. ECON. REV.* 833, 848 (1994) (“When competition between interest groups is intense (because their interests are in direct opposition), the availability of an efficient income-transfer tool makes credible an implicit governmental threat to join forces with the opposing lobbies. Individual interest groups have little political power under these conditions, and they prefer to tie the hands of the government.”).

discourage pro-competitive business conduct that it is hard to see how antitrust could now be used systematically to redistribute wealth away from firms.¹³⁰ Moreover, when firms complain about antitrust enforcement these days, they typically argue that aggregate surplus will decline, not that the antitrust laws are being used improperly to transfer surplus from producers to consumers.¹³¹

In contrast, present-day enforcers and courts should be concerned more about the possibility that antitrust rules might systematically transfer rents from consumers to firms, by allowing firms to adopt practices that generate allocative efficiency benefits while reducing consumers' surplus.¹³² Any policy that threatens to undermine consumer confidence that competition is the superior regulatory option would tend to undermine consumer political support for the political bargain in favor of antitrust.

The 1997 efficiency revisions to the Federal Trade Commission and Justice Department Horizontal Merger Guidelines strike the right balance in the wake of antitrust's Chicago school

¹³⁰ Such a dramatic change would probably require the active participation of more than one branch of the government. For example, if the Justice Department were now to pursue an antitrust enforcement program that aimed to benefit consumers in one industry after another without regard to the loss of efficiencies and cost to producers, its efforts would likely be rebuffed in the courts unless either Congress or the judicial branch were persuaded to change the rules.

¹³¹ For example, Microsoft's argument that antitrust enforcement against it would discourage innovation and penalize it for success had this character.

¹³² Cf. Joseph F. Brodley, *The Economic Goals of Antitrust: Efficiency, Consumer Welfare, and Technological Progress*, 62 N.Y.U. L. REV. 1020 (advocating similar standard).

revolution.¹³³ The Guidelines emphasize agency concern with protecting consumers against mergers that would lead to higher prices.¹³⁴ But the emphasis on consumers is qualified. The agencies note that under some circumstances, they would count cost savings “with no short-term, direct effect on prices” as a reason not to challenge the acquisition,¹³⁵ thus preserving leeway not to challenge the rare merger that raises prices while increasing aggregate surplus. The placement of the qualifying language in the margin sends the message that the agencies expect to use that discretion only in unusual cases where the production cost savings or other efficiency gains are substantial while the loss to consumers appears small.¹³⁶

¹³³ U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines §4 (1992, revised 1997). Although I participated in drafting these agency guidelines, my interpretation is not necessarily that of either federal enforcement agency.

¹³⁴ This consumer-oriented posture also tends to promote aggregate welfare, because mergers that harm consumers also typically reduce aggregate surplus.

¹³⁵ U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines §4 n.37 (1992, revised 1997).

¹³⁶ The Merger Guidelines do not purport to allocate burdens of proof: they merely provide guidance as to the prosecutorial intentions of the federal enforcement agencies. One way to deal with burdens consistent with the approach of the Guidelines would be to treat proof of efficiencies as a “defense” under some circumstances (shifting a burden of production, not persuasion) and as an “affirmative defense” (shifting both burdens) under others. In particular, if efficiencies are put forward as evidence tending to disprove that price would rise (that is, if they are offered to disprove plaintiff theories of coordinated or unilateral competitive effects), they would play the role of a “defense.” By proffering evidence that the merger would generate efficiencies for this purpose in response to plaintiff’s prima facie case based on market concentration and plaintiff’s explanation of the economic logic by which it believes competition would be harmed, defendant would shift a burden of production back to plaintiff to demonstrate harm to competition, while the burden of persuasion would always remain with plaintiff. (This is consistent with the way that the courts generally treat evidence of ease of entry.) Proof that efficiencies would be passed-on to buyers would be relevant if proof of efficiencies is a “defense” (although pass-through from intermediate buyers to end use consumers could be presumed). But if efficiencies are instead proffered as evidence that would excuse higher prices,

The studied ambiguity of the Merger Guidelines in resolving the welfare standard issue as it might apply in the review of challenges to horizontal mergers could be adopted generally in settings in which aggregate welfare and consumer welfare might also be at odds. In these contexts too, a qualified emphasis on consumers would be unlikely to threaten the political bargain in favor of competition. Consumers are unlikely to organize political opposition to the antitrust laws if enforcers occasionally challenge an exclusionary practice that reduces prices slightly but generates so much loss of producers surplus for excluded rivals as to reduce aggregate welfare, if enforcers occasionally challenge the collective exercise of monopsony power when the price reduction is small and the allocative efficiency loss is great, if enforcers decline to challenge horizontal mergers that would likely raise price slightly when the aggregate surplus seems likely to increase substantially, or if enforcers decline to challenge practices facilitating price discrimination when the price increase to disfavored buyers is small and the

for example through demonstration of cost savings not passed-through to buyers or a showing of lower prices in other markets, defendant would have both a burden of production and the burden of persuasion. This approach effectively raises defendant's burden when it seeks to defend its merger under an aggregate welfare standard rather than a consumer welfare standard. This outcome would be consistent with the implication of the political bargain perspective in the context of the doctrinal rules adopted in the wake of antitrust's Chicago school revolution for antitrust's welfare standard: that antitrust should seek to protect consumers except when the aggregate efficiency costs of doing so would be large. For elaboration of these points, see Testimony of Jonathan B. Baker before the Antitrust Modernization Commission (Nov. 17, 2005), *available at* http://www.amc.gov/commission_hearings/merger_enforcement.htm. For discussions of the relationship between the rationale for crediting efficiencies and the allocation of burdens of proof, *see generally* Andrew I. Gavil, Secondary Line Price Discrimination and the Fate of Morton Salt: To Save It Let It Go, 48 EMORY L. J. 1057, 1119-20 (1999); Andrew I. Gavil, Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance, 72 ANTITRUST L.J. 3, 69-74 (2004).

allocative efficiency gains are great.¹³⁷ But if the political constraints are disregarded through an overbearing enforcement effort or an ostentatious non-enforcement policy, that choice could ultimately threaten the political bargain that underlies a competition regime.

The welfare standard dispute has limited practical importance because harm to consumers and harm to aggregate welfare tend to go hand-in-hand. Moreover, the lines between consumers and producers are not distinct – most of us are to some extent both, though we may have a primary stake in one or the other camp in any individual case. When controversy arises, however, the political bargain perspective suggests that enforcers and courts have substantial leeway to maximize aggregate surplus, within the political constraint that consumers and producers share the efficiency gains on average across cases.

In recognition of the extensive modifications to antitrust doctrine implemented during antitrust's Chicago school revolution, which collectively address any serious concern that antitrust rules might be exploited by consumers to transfer rents systematically from producers, antitrust rules could reasonably be enforced today with a qualified emphasis on consumers: protecting consumers (and other buyers) except when the aggregate efficiency costs of doing so would be large. This approach would be expected to protect consumer support of the political

¹³⁷ Similarly, producers are unlikely to organize political opposition to the antitrust laws if enforcers do not challenge exclusionary practices that increase prices slightly but also raise aggregate welfare substantially, if enforcers decline to challenge the collective exercise of monopsony power when the price reduction is substantial but the allocative efficiency loss is not large, if enforcers occasionally challenge horizontal mergers that would likely raise price substantially even though aggregate surplus seems likely to increase slightly, or if enforcers occasionally challenge practices facilitating price discrimination when the price increase to disfavored buyers is great even when the conduct results in small allocative efficiency gains.

bargain in favor of competition policy without undermining the political support of producers, while securing most of the economy-wide efficiency gains available from antitrust enforcement. To those who seek a welfare standard specified with mathematical precision, this conclusion will seem unsatisfactory. But that lack of clarity arises because the controversy is one of politics not economics.

V. CONCLUSION

The main features of the historical evolution of competition policy in the U.S. are consistent with the view that the U.S. political system adopted a competition policy around the middle of the 20th century. Before that time, regulatory regimes fluctuated unstably between pro-producer policies of industry self-regulation hospitable to the exercise of market power and pro-consumer policies emphasizing either national economic planning or the restoration of traditional competition from the era preceding the rise of the large corporation. This politicized contest over regulatory policy ended mid-century when consumers and producers reached a political bargain to adopt a regime that protects competition through antitrust enforcement. The antitrust enforcement regime enhanced aggregate economic welfare relative to the regulatory instability it displaced.

Once securely adopted, the competition regime has been largely self-enforcing, with an assist from institutions established to implement the bargain, including federal and state enforcement agencies and the courts. Passionate political debates over the economic regulation of large firms have faded in salience, with the notable exception of the major change in antitrust

policy since the mid-20th century: the rise of the Chicago school, during the late 1970s and 1980s. Those events are better understood either as reform of the antitrust laws to increase the efficiency gains from competition and avoid the possibility that the political bargain for competition would become disadvantageous for producers, or else as a thwarted attempt by producers to renege on that political bargain, rather than as a successful effort by producers to induce the political system to discard competition policy in favor of a pro-producer regime permitting the exercise of market power. Accordingly, antitrust's Chicago school revolution reaffirms rather than undermines the view that the U.S. had by 1950 adopted competition policy as a political bargain.

The extensive modifications to antitrust doctrine implemented during antitrust's Chicago school revolution have collectively addressed any serious concern that antitrust rules might be exploited by consumers to transfer surplus systematically from producers, without undermining the effectiveness and independence of the enforcement agencies. Accordingly, antitrust rules could reasonably be enforced today with a qualified emphasis on consumers: protecting consumers except when the aggregate efficiency costs of doing so would be large. This approach would help protect consumer support of the political bargain in favor of competition policy without undermining the political support of producers, while securing most of the economy-wide efficiency gains available from antitrust enforcement.

Appendix

This appendix sets forth a mathematical example demonstrating how competition policy can emerge politically as a self-enforcing bargain between competing interest groups. Voters are viewed as adopting a primary loyalty to one of two interest groups: producers or consumers. The fraction β of voters are consumers, while the fraction $1-\beta$ are producers. Consumers are in the majority: $\beta > 1/2$. Differences among types of consumers or producers (such as small business vs. large business) are ignored.¹³⁸ These two interest group actors interact repeatedly in the legislature. An interest group's collective political influence in the legislature is taken to turn both on its nominal size as a voting bloc and on its ability to mobilize votes by overcoming free riding problems.¹³⁹ A period lasts from one meeting of the legislature to the next.

All political decision-making takes place in the legislature, which selects a regulatory regime from among three options: competition (generated by antitrust enforcement), market power, and price controls. The market power and price controls regimes can be understood as special interest legislation by which producers or consumers, respectively, exploit a legislative majority to appropriate rents from the other interest group. The competition regime permits the

¹³⁸ The possibility that some consumers or firms would care more about long-term consequences than others is also ignored; a single, common discount rate will be assumed.

¹³⁹ A similar perspective is reflected in the "political influence functions" postulated by Gary Becker. Gary S. Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 Q. J. ECON. 371 (1983); Gary S. Becker, *Public Policies, Pressure Groups, and Dead Weight Costs*, 28 J. PUB. ECON. 329 (1985). Becker specifies a general equilibrium model of political interaction, in which interest groups compete to produce redistribution in their favor. By contrast, the example in this Appendix illustrates the consequences of interest group interactions when adverse past policies promote current political mobilization.

economy to obtain efficiency gains unavailable under the market power or price controls regimes.

Single-period payoffs to interest group members depend on the regulatory regime.

Payoffs are expressed as per capita (per voter) consumption, normalized so that the single period payoffs under competition to both producers and consumers are set at unity. Single period payoffs to producers and consumers are represented by Π and K , respectively, with superscripts for the possible regulatory regimes of market power (MP) and price controls (PC). In any period, producers prefer market power to competition, and competition to price controls: $\Pi^{mp} > 1 > \Pi^{pc}$. Consumers prefer the reverse: $K^{pc} > 1 > K^{mp}$. Both price controls and market power result in an efficiency loss, so $\Pi^{mp} + K^{mp} < 2$ and $\Pi^{pc} + K^{pc} < 2$. The distribution of the efficiency loss between interest groups is, by assumption, not wildly asymmetric. In particular, producers and consumers would each prefer a stable competitive regime to alternating between market power and price control regimes: $\Pi^{mp} + \Pi^{pc} < 2$ and $K^{pc} + K^{mp} < 2$. The disparity between single period per capita payoffs in the most and least attractive regulatory regimes for producers is assumed to exceed the disparity in the number of actors in each interest group: $[\Pi^{mp}/\Pi^{pc}] > [\beta/(1-\beta)]$.

Each interest group can marshal votes in the legislature for its favored proposal,¹⁴⁰ but interest group size in the electorate does not translate proportionally to votes in the legislature because of differences in the success of each group in overcoming collective action problems. Consumers and producers are both viewed as large and diffuse interest groups, for which

¹⁴⁰ The extensive empirical literature on the extent to which legislators act as agents of their constituents and contributors is surveyed in Dennis C. Mueller, *PUBLIC CHOICE III* §20.3 (2003).

collective action problems may be particularly severe.¹⁴¹ Each interest group's ability to overcome its collective action difficulties is by assumption related to the per capita stakes in the vote for that group.

These ideas are formalized by introducing V^i , an index number summarizing the strength of the voting coalition that interest group i (either consumers or producers) can assemble in the legislature in favor of a particular legislative proposal for a regulatory regime. V^i is conditional on the prior regulatory regime and is written: $V^i(\text{proposed regulatory regime}; \text{prior regulatory regime})$. The two interest groups, producers and consumers, are denoted P and C , respectively. The three possible regulatory regimes, of market power, competition, and price controls, are denoted MP , CM , and PC , respectively. For example, the index number related to the legislature votes assembled by consumers in favor of switching the regulatory regime to price controls from market power is represented as $V^C(PC; MP)$.

Votes in the legislature take the form of a choice between the regulatory regime proposed by one interest group and the regime favored by another. In any such head to head comparison, the legislative victory goes to the proposal with the highest index number.¹⁴² (The possibility of a

¹⁴¹ Mancur Olson, *THE LOGIC OF COLLECTIVE ACTION* (1965). Were it not for such difficulties, consumers, with a majority in the polity, would invariably enact the proposals they favor in the legislature.

¹⁴² To specify legislative behavior fully, this decision rule may be understood as derived from a prior assumption that the legislative votes each proposal achieves depends on the relative index number. Thus, if consumers favor price controls while producers favor market power, and the market power regime was in force during the previous period, then a proposal by consumers to switch to price controls would receive the fraction $V^C(PC; MP) / [V^C(PC; MP) + V^P(MP; MP)]$ of legislative votes. Under a majoritarian voting rule the outcome of legislative contests between a pair of alternatives is then determined directly by a comparison of index numbers, without need to compute the fraction of the vote each proposal receives.

tie is ignored.) Thus, a proposal that the regulatory regime switch to price controls (favored by consumers) from market power (favored by producers) will be victorious in the legislature if $V^C(PC; MP) > V^P(MP; MP)$.

The index number $V^i(\text{proposed regulatory regime; prior regulatory regime})$ is assumed to be computed in a specific way. Its magnitude depends in part on the fraction of voters in interest group i , a measure of the size of the interest group. That fraction is adjusted multiplicatively to account for a measure of the per capita stakes for group members in switching to the proposed regulatory regime from the prior one. The stakes are measured by the present discounted value of the future stream of payoffs resulting from permanent legislative adoption of a regulatory regime, normalized by the present value of the payoffs that would result were the prior regulatory regime to continue permanently. Consumers and producers are each assumed to discount the future at the identical rate δ (that is, they value 1 next period at δ today), for $0 < \delta < 1$. Accordingly, for example, the index reflecting consumer votes in favor of switching from a market power regime to a price control regime takes the following form:

$$V^C(PC; MP) = \beta \left[\frac{\sum_{i=1}^{\infty} \delta^i K^{pc}}{\sum_{i=1}^{\infty} \delta^i K^{mp}} \right] = \beta [\Delta K^{pc} / \Delta K^{mp}] = \beta [K^{pc} / K^{mp}],$$

where $\Delta \equiv 1 + \delta + \delta^2 + \delta^3 + \dots + \delta^j + \dots$.

Because per-period payoffs are constant over time, the terms related to discounting drop out.

Mathematically, the index V^i will be greater than the interest group's fraction of the voting population (*e.g.* greater than β for consumers) if the group does better under the legislative proposal than with a continuation of the prior regime. The index will be smaller than the group's fraction of voting population if the group does less well under the proposal than with a

continuation of the prior regime. This functional form incorporates the assumption that a diffuse interest group's success in solving its collective action problems in order to mobilize politically is greater when the existing regulatory regime is adverse than when it is neutral or favorable. For example, $V^C(PC; MP) = \beta[K^{pc}/K^{mp}] > V^C(PC; PC) = V^C(MP; MP) = \beta > V^C(MP; PC) = \beta[K^{mp}/K^{pc}]$.

Within this framework, the legislature chooses a regulatory regime. The first set of results, set forth in Propositions 1 through 3, assume that the legislature can achieve only the outcomes available through one-shot play. Proposition 4 allows for repeated play, from which the possibility of committing to a future regulatory regime could emerge as an outcome.

If the legislature is unable to commit to a future regulatory regime, the legislative decision as to regulation during any period is driven by political reaction. In particular, the outcome of the stage game, the one-shot interaction in any period, is controlled by the increased organizing ability of the group that lost in the previous period. There are three cases, each corresponding to a different regulatory regime that could have been adopted in the previous period. Propositions 1 through 3 set forth the stage game results.

Proposition 1

In a one-shot interaction, if the prior period regulatory regime permitted the exercise of market power, then a price controls regime would be adopted.

Proof

In any single period contest, consumers will prefer a price controls regime while producers will prefer to exercise market power, so the legislative contest will involve these alternatives. Proposition 1 thus requires that $V^C(PC; MP) > V^P(MP; MP)$, or, equivalently that $\beta[K^{pc}/K^{mp}] > (1-\beta)[\Pi^{mp}/\Pi^{mp}] = (1-\beta)$. The latter inequality, $\beta[K^{pc}/K^{mp}] > (1-\beta)$, follows directly from the assumptions that $\beta > 1/2$ and $K^{pc} > K^{mp}$. \square

Proposition 2

In a one-shot interaction, if the prior period regulatory regime involved price controls, then a regime permitting the exercise of market power would be adopted.

Proof

In any single period, consumers will prefer a price controls regime while producers will prefer to exercise market power, so the legislative contest will involve these alternatives. Proposition 2 thus requires that $V^P(MP; PC) > V^C(PC; PC)$, or equivalently, that $(1-\beta)[\Pi^{mp}/\Pi^{pc}] > \beta[K^{pc}/K^{pc}] = \beta$. The latter inequality, $(1-\beta)[\Pi^{mp}/\Pi^{pc}] > \beta$, follows directly from the assumption that $[\Pi^{mp}/\Pi^{pc}] > [\beta/(1-\beta)]$. \square

Proposition 3

In a one-shot interaction, if the prior period regulatory regime involved

competition, then either a regime permitting the exercise of market power or a price controls regime would be adopted.

Proof

In any single period, consumers will prefer a price controls regime while producers will prefer to exercise market power, so the legislative contest will take the form of a battle between these groups to see which can assemble a voting majority for its preferred outcome. The possibility of a tie is ignored: procedural rules are assumed to break a tie in favor of one or the other interest group's proposal. Hence, either $V^p(\text{MP}; \text{CM}) > V^c(\text{PC}; \text{CM})$ or $V^p(\text{MP}; \text{CM}) < V^c(\text{PC}; \text{CM})$, and one of these alternatives will be adopted. \square

These propositions concerning the outcome of one-shot interactions imply that if the legislature is unable to commit to a future regulatory regime, the regulatory regime will cycle between price controls and market power. Regulatory cycles occur from the start, or after one period if competition were the initial condition. The cycles are driven by the assumption that the losers in the past are better able to organize today. The order will depend on the regime that characterized the past, as set forth in the following table:

<u>Past Period Regime</u>	<u>Present Period Regime</u>	<u>Next Future Period Regime</u>
market power	price controls	market power
price controls	market power	price controls

competition	either A) price controls or B) market power	either A) market power (if present regime was price controls) or B) price controls (if present regime was market power)
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The cycle continues through later future periods. Competition would never be adopted, so the last line of the table applies only if the initial period, presented by history, was competitive.

Even when a competition regime is preferable to cycling for both groups, it cannot be achieved in a one-shot interaction because the interest group that can enact its most preferred policy in any period will do so.

The result that competition cannot be obtained through one-shot play, even though it maximizes aggregate payoffs, is at variance with the literature suggesting that competing interest groups will tend to bargain to achieve (and split) efficiency gains.¹⁴³ That outcome does not occur here for two reasons. First, neither interest group can credibly commit to seeking a

¹⁴³ *E.g.* Gary S. Becker, A Theory of Competition Among Pressure Groups for Political Influence, 98 Q. J. ECON. 371 (1983); Gary S. Becker, Public Policies, Pressure Groups, and Dead Weight Costs, 28 J. PUB. ECON. 329 (1985). As a general theory of regulation, however, this view hard to reconcile with the many studies that identify regulatory inefficiencies. *See* Roger G. Noll, *Economic Perspectives on the Politics of Regulation*, in II HANDBOOK OF INDUSTRIAL ORGANIZATION (Richard Schmalensee & Robert D. Willig, eds. 1989) at 1273-74 (surveying studies finding inefficient regulatory outcomes). *Cf.* Daron Acemoglu, Why Not a Political Coase Theorem? Social Conflict, Commitment and Politics, 31 J. COMPARATIVE ECON. 620 (2003) (explaining why politically powerful groups do not maximize social wealth before appropriating rents).

competitive regulatory regime rather than one in which it would exploit market power.¹⁴⁴

Second, the losing interest group cannot solve its collective action problems as well as can the winner, making it impossible for the two groups to negotiate the side payments that would be necessary to obtain the foregone gains from trade.¹⁴⁵

By contrast, repeated play may permit the legislature to adopt a competition regime and avoid these cycles.¹⁴⁶ Proposition 4 below demonstrates that with infinitely repeated play, competition is enforceable for a sufficiently high discount rate. By assumption, if the legislature deviates from a policy of protecting competition, whether at the behest of either producers or consumers, a competition regime cannot be renegotiated; regulatory instability (a cycle between market power and price controls) follows forever. Deviation from the coordinated outcome is

¹⁴⁴ This point is similar to recognizing that competition is the dominant strategy for two actors in a one-shot “prisoner’s dilemma” interaction, even though both would benefit were they to cooperate, because neither can commit not to cheat.

¹⁴⁵ See Daron Acemoglu, Simon Johnson, and James Robinson, *Institutions as the Fundamental Cause of Long-Run Growth* 42 (NBER Working Paper 10481, May 2004) (“If those who gained political power from institutional change could promise to compensate those who lost power then there would be no incentive to block better institutions.”) This point is similar to the observation that consumers do not routinely bargain with cartels to obtain and share the additional gains from trade that would arise from increasing output to the competitive level.

¹⁴⁶ Infinitely repeated competition between political parties can similarly make possible a welfare-enhancing self-enforcing bargain between them. Alberto Alesina, *Credibility and Policy Convergence in a Two-Party System with Rational Voters*, 78 *AM. ECON. REV.* 796 (1988) (parties competing for votes converge in their policies when repeated play permits them to make credible post-election promises); Avinash Dixit, Gene M. Grossman, and Faruk Gul, *The Dynamics of Political Compromise*, 108 *J. POL. ECON.* 531 (2000) (generalizing Alesina’s result to a case in which parties’ political strength changes according to a Markov process); cf. Daron Acemoglu, *Why Not a Political Coase Theorem? Social Conflict, Commitment and Politics*, 31 *J. COMPARATIVE ECON.* 620, 643 (2004) (Proposition 4) (similar result in repeated interaction between citizens and rulers).

deterred because it would be punished by reversion to less attractive regulatory instability.

As before, the voting index (for an interest group with respect to a regulatory proposal) multiplies the fraction of voters in the group by a measure of the per capita stakes in switching to that proposal for the group. Again, the stakes are measured in terms of the discounted present value of the payoffs resulting from permanent legislative adoption of a regulatory regime, normalized by the discounted present value of the payoffs that would result were the prior regulatory regime to continue permanently.¹⁴⁷

Proposition 4

Competition is supported by the threat of reversion to regulatory cycles in an infinitely repeated legislative interaction, for a sufficiently high discount rate.

Proof

The proposition is demonstrated by showing that if the prior regulatory regime is competitive, the voting index for both consumers and producers is higher for a continuation of the competitive regime relative to the alternative of regulatory cycles (beginning with the regime most advantageous for that interest group).

Producers and consumers are symmetric, so only producers will be considered. A

¹⁴⁷ The results would not change if, when the prior regulatory regime was price controls or market power, the present value of the payoff to the new regime were normalized by the present value of the payoffs that would result were the regulatory regime to cycle infinitely between market power and price controls (as would occur in successive outcomes of one-shot play).

sufficient condition to guarantee this result is that the present value of continued competition exceeds the present value of the payoff from cyclical regime change beginning with market power. This condition requires that

$$\Delta = 1 + \delta + \delta^2 + \delta^3 + \dots + \delta^j + \dots >$$

$$\Pi^{\text{mp}} + \delta\Pi^{\text{pc}} + \delta^2\Pi^{\text{mp}} + \delta^3\Pi^{\text{pc}} + \dots + \delta^j\Pi^{\text{mp}} + \delta^{j+1}\Pi^{\text{pc}} + \dots .$$

After algebraic simplification of the infinite series, the condition takes the form

$$1/(1-\delta) > \Pi^{\text{mp}}/(1-\delta^2) + \delta\Pi^{\text{pc}}/(1-\delta^2).$$

Multiplying all terms by $(1-\delta^2)$, a positive number, and simplifying yields

$$(1+\delta) > \Pi^{\text{mp}} + \delta\Pi^{\text{pc}}. \text{ Recall that the market power and price control regimes}$$

create efficiency losses relative to competition, so $\Pi^{\text{mp}} + \Pi^{\text{pc}} < 2$. Hence, there

exists some $\delta < 1$ such that $(1+\delta) > \Pi^{\text{mp}} + \Pi^{\text{pc}} > \Pi^{\text{mp}} + \delta\Pi^{\text{pc}}$. Thus, at some

discount rate sufficiently high (close to 1), producers would not seek to deviate

legislatively from a competition regime. \square

Proposition 4 is an application of the Folk Theorem for infinitely repeated games.¹⁴⁸ The Folk Theorem demonstrates that any payoff that dominates the best payoffs actors can receive if they are being punished by rivals can be sustained in infinitely repeated play if the actors care sufficiently about the future. In the example, the competition regime offers the only Pareto

¹⁴⁸ See, e.g., Drew Fudenberg and Jean Tirole, *GAME THEORY* 152 (1991) (Theorem 5.1). The notion of infinitely repeated games for which the Folk Theorem applies includes finitely repeated games with an uncertain termination date. See Eric Rasmusen, *GAMES AND INFORMATION: AN INTRODUCTION TO GAME THEORY* 124-26 (2d ed. 1989) (Theorem 5.1).

superior payoff option available to the two interest groups. Accordingly, Proposition 4 has the interpretation that competition is sustainable through repeated interaction if it can be negotiated.¹⁴⁹

¹⁴⁹ As with similar Folk Theorem results, the proposition does not show that the competitive regime will be adopted; it merely shows if competition is adopted, neither interest group would have an incentive to seek an alternative regulatory regime.