The Consumer Welfare Standard in Antitrust: Outdated or a Harbor in a Sea of Doubt?
Questions for the Record
Submitted December 15, 2017

Diana L. Moss, Ph.D.
President, American Antitrust Institute

QUESTIONS FROM SENATOR BLUMENTHAL

1. **From the testimonies of the witnesses at the hearing, it appears that there is agreement that innovation is an important component of antitrust law.**

   a. **Would you agree that if a merger will undermine innovation it can be challenged under the consumer welfare standard?**

   I do agree. The U.S. antitrust agencies and the courts have long applied the consumer welfare standard as the standard for evaluating harms that can result from proposed mergers. Any reduction in consumer welfare is the central focus of an antitrust inquiry into the potential adverse effects of a merger.

   An anticompetitive merger can affect a broad range of parameters that affect consumer welfare, across a wide variety of markets. These include markets for physical and digital (i.e., online) products and services and innovation or research and development (R&D). Under the consumer welfare standard, markets can be identified at any point in a supply chain that is affected by a proposed merger.

   Consumer welfare can be affected by a number of merger-related outcomes. Price increases from the exercise of seller market power, price decreases from the exercise of buyer market power – and corresponding reductions in output from both – directly affect consumer welfare. But consumer welfare is also affected by changes in incentives to compete on dimensions other than price, including: (1) quality, service, or variety and (2) investment in the R&D needed to innovate new technologies, more efficient processes, and new products and services.

   Horizontal mergers that eliminate an innovation rival and diminish important "parallel path" R&D can reduce or eliminate incentives to compete in innovation markets. The larger the presence (i.e., share) of the merging companies in innovation markets and the more concentrated are those markets, the greater should be the concerns over potential reductions in consumer welfare.

   Vertical mergers can also impair innovation competition. For example, enhanced post-merger incentives to restrict rivals' access to R&D inputs such as critical technologies can impair their ability to innovate. Vertical integration of large market players, such as we see in agricultural biotechnology, can also raise entry barriers to smaller innovative rivals operating at only one level. Coming up against large, integrated rivals can make it more difficult for smaller rivals to get their innovative new products and services to market, dampening their incentives to engage in innovation. Consumers suffer from

these effects through a loss of new products and service, less choice, and potentially higher prices than what would otherwise be generated by more competition in R&D markets.

Likewise, defendants in vertical mergers might argue that pairing up innovation assets in complementary markets (e.g., in pharma or agricultural biotechnology mergers) might lead to coordination efficiencies. Failure to deliver on such claims, or difficulty in executing complex integration plans, can reduce innovation capability post-merger.

All of the foregoing examples illustrate how mergers can potentially lead to fewer new technologies, processes, and products and services that are the result of innovation and that would otherwise enhance consumer welfare and benefit consumers.

Perhaps the best indication that the consumer welfare standard reaches to innovation is the body of challenged merger cases where innovation competition has been a central focus. In the past, the U.S. Department of Justice (DOJ) and Federal Trade Commission (FTC) have recognized that some illegal mergers can have adverse effects on innovation, in addition to price and other non-price effects. Increasingly, however, the antitrust agencies are framing "standalone" theories of harm around the elimination of innovation or R&D competition. And they are also addressing some mergers' effects on innovation competition in a more fulsome way.

In 2015, for example, Applied Materials and Tokyo Electron abandoned their proposed merger in the face of opposition by the DOJ. The DOJ noted in its press release that the proposed remedy would not have replaced competition eliminated by the merger, "particularly with respect to the development of equipment for next-generation semiconductors."[1]

In the abandoned 2016 merger of oilfield services and equipment giants Halliburton and Baker Hughes, the DOJ complaint noted that the proposed merger would likely result in "…higher prices, lower service levels and less innovation, as well as greater coordination among the remaining competitors."[2] The DOJ noted that the two companies played "leading roles" in "driving technological innovation."[3] The government's complaint also noted that, as two of the Big 3 companies, the merging companies were "serious participants" because of their capacity to conduct necessary R&D.[4]

On the FTC side, the Commission challenged the 2012 acquisition of PowerReview by Bazaarvoice Inc. involving the market for product ratings and reviews platforms. The FTC noted that the merged company "has significantly reduced incentives to discount

[1] Press Release, U.S. Dep't of Justice, Applied Materials Inc. and Tokyo Electron Ltd. Abandon Merger Plans After Justice Department Rejected Their Proposed Remedy (Apr. 27, 2015), https://www.justice.gov/opa/pr/applied-materials-inc-and-tokyo-electron-ltd-abandon-merger-plans-after-justice-department.
[2] Complaint, *United States v. Halliburton Co.*, No. 1:16-cv-00233-UNA at 30 (D. Del. Apr. 6, 2016), https://www.justice.gov/atr/file/838661/download.
[3] *Id.*
[4] *Id.*

prices, increase the quality of its services, or invest in innovation."[5] In explaining its competitive concerns, the Commission noted the importance of the "pace" and "patterns" of innovation in driving competition between the two companies.

The foregoing examples of enforcement actions highlight the growing importance of innovation competition under the existing antitrust laws and consumer welfare standard.

b. More broadly, would you agree that harm to innovation constitutes a harm to consumers under current law?

Yes. Under the existing antitrust laws and the consumer welfare standard, the loss or dampening of innovation competition through anticompetitive mergers and illegal collusive or exclusionary conduct can adversely affect consumer welfare. When consumer welfare is reduced, consumers are harmed.

As discussed in more detail in my response to question 1.A above, mergers can result in such adverse effects on consumers. I would like to note that innovation competition is also important in non-merger settings such as single firm conduct that restricts innovation competition and coordinated conduct that limits competition. In the FTC's recent 2017 case against chipmaker Qualcomm, for example, the Commission explained "Qualcomm's anticompetitive practices have excluded competitors, increased consumer prices, and suppressed innovation."[6] The FTC's complaint goes on to note that "[e]nhanced innovation in mobile technologies would offer substantial consumer benefits, especially as these technologies expand to new applications, including extending mobile connectivity to consumer appliances, vehicles, buildings, and other products. . . . By suppressing innovation, Qualcomm's anticompetitive practices threaten these benefits."[7]

In the context of anticompetitive agreements, enforcers should be aware that agreements to coordinate on non-price dimensions of competition can also adversely affect innovation. In 2014, the American Antitrust Institute (AAI) submitted comments to the U.S. Department of Transportation highlighting the dangers of the International Air Transport Association's (IATA's) collective proposal to create a standard business model for the distribution of airfares.[8] Among other things, such a model could squeeze out more innovative airfare distribution models and alternative (non-airline) distribution channels, to the detriment of consumers.[9]

There should be an increased focus on innovation competition in antitrust cases moving forward, for a number of reasons. First, the loss of innovation competition delivers real harms to U.S. consumers and stifles growth in the U.S. economy. Second, with higher

[5] Complaint, *United States v. Bazaarvoice, Inc.*, No. C13 0133 JSC at 19 (N.D. Cal. Jan. 10, 2013), https://www.justice.gov/atr/case-document/file/488911/download.
[6] Complaint, FTC v. Qualcomm Inc., Case No. 17-MD-02773-LHK at 29 (Jan. 17, 2017), https://www.ftc.gov/system/files/documents/cases/170117qualcomm_redacted_complaint.pdf.
[7] *Id.* at 30 (emphasis added).
[8] Comments of the American Antitrust Institute, Before the Dep't of Transp. Docket No. OST-2014-0056 (Sept. 29, 2014), http://antitrustinstitute.org/sites/default/files/AAI%20Comments_OST-2013-0048.pdf.
[9] *Id.* at 7-8, 11, 13.

levels of market concentration and the rise of dominant firms in some markets, innovation may be the first non-price dimension of competition to fall by the wayside. Indeed, there is a compelling case that supports the notion that dominant firms and oligopolies have weaker economic incentives to innovate and stronger incentives to limit competition. Indeed, competition from more innovative rivals can be a major threat to a protected oligopoly or dominant market position.

As one expert put it, for example, there is "good reason to think that increases in concentration do not persistently lead to greater incentives to innovate; rather, beyond some high level of concentration, further increases could actually reduce the incentive to innovate."[10] There are a number of possible reasons for this, notwithstanding the fact that firms can appropriate returns from innovation more easily with less competition. One, with robust competition, new product development is done with an eye toward stealing sales from rivals. But with fewer rivals and consolidated or reduced numbers of product lines, new product development can increase the risk that the innovator cannibalizes its own sales of existing products.[11]

In sum, the antitrust agencies and the courts should be encouraged to use the full scope of the existing law and consumer welfare standard to look at the effect of potentially anticompetitive mergers and conduct on innovation competition. Consumers are harmed directly through actions that eliminate or stifle innovation competition.

2. **New research has shown that more concentrated labor markets are generally correlated with lower wages.**

   a. **Would you agree that a more effective antitrust enforcement regime could help combat labor market monopsony, and in turn help fight stagnant wages and inequality? Why or why not?**

Yes. There is a lot that more vigorous antitrust enforcement can do to address the welfare of workers under the current regime and consumer welfare standard. Harm to workers can enter the antitrust calculus in a number of ways. First, and most generally, seller market power is exercised by cutting back on output, which reduces demand for workers. Second, a focus on squeezing out cost efficiencies through merger means streamlining the workforce and laying off workers. Third, large firms now wield significant market power in buying labor, reducing the bargaining power of workers – even those in collective bargaining units and organizations. Fourth, "non-compete" (i.e., no-poach) and wage-rigging agreements among firms harm workers.

Antitrust is an important policy tool for addressing labor and inequality problems that arise from potential violations of the antitrust laws. The consumer welfare standard facilitates this assessment. At the broadest level, for example, the consumer welfare standard accounts for the distribution of wealth between consumers and firms – a big

[10] James. M. MacDonald, *Mergers and Competition in Seed and Agricultural Chemical Markets*, AMBER WAVES (Apr. 3, 2017), https://www.ers.usda.gov/amber-waves/2017/april/mergers-and-competition-in-seed-and-agriculturalchemical-markets/.
[11] *Id.*

part of what is driving inequality gaps. The standard also allows for evaluating buyer market power issues by defining a relevant market around input markets (of which labor can be one) at any point along a supply chain.

As I noted above, past antitrust enforcement actions illustrate the ability of the existing regime to help workers. For example, antitrust investigations have focused on the effects of mergers and abusive conduct on labor markets. Enforcers have taken on monopsony issues in mergers of beef and pork packers and health insurance companies.[12] In forcing the abandonment of a merger of broadband distributors, enforcers flagged the negative effects of greater bargaining power on content writers and producers.[13]

In a merger of acute care cardiac facilities, enforcers required hospitals to release doctors from their non-compete clauses to restore competition.[14] And in the merger of health insurers Anthem and Cigna, the DOJ's case revolved around how the larger insurer could drive down reimbursement rates paid to hospitals and physician practices, making it more difficult to attract labor to the medical professions and early retirement of physicians.[15]

The government and private plaintiffs have challenged anticompetitive bid rigging, wage fixing, no-poach, and information-sharing agreements that hurt workers. These workers include nurses, tech professionals, and others.[16] And the agencies have made it clear through their guidance that such agreements will not be tolerated. Moreover, occupational licensing cases in North Carolina and Texas demonstrate how state licensing boards may not be immunized under the antitrust laws for actions that exclude non-typical or innovative market entrants.[17]

The foregoing demonstrates that antitrust has the tools to address labor and inequality problems. But it can and should do more. Enforcers should challenge deals that create powerful buyers that can depress wage rates and force down prices paid to suppliers. Public and private enforcers can pursue alleged bid rigging in auction markets, such as those for cattle, which drives down prices paid for cattle. They can scrutinize conduct that raises entry barriers for smaller innovators in markets like medical devices and online retailing.

---

[12] Complaint, *United States v. JBS S.A.*, Case No. 08CV5992, 2008 WL 5560009 (N.D. Ill. Oct. 20, 2008); Complaint, *United States v. Tyson Foods, Inc.*, Case No. 1:14-cv-01474, 2014 WL 4249929 (D.D.C. Aug. 27, 2014); Complaint, *United States v. Anthem, Inc.*, Case No. 1:16-cv-01493, 2017 WL 242848 (D.D.C. July 21, 2016).

[13] Press Release, U.S. Dep't of Justice, Comcast Corporation Abandons Proposed Acquisition of Time Warner Cable After Justice Department and the Federal Communications Commission Informed Parties of Concerns (Apr. 25, 2015), https://www.justice.gov/opa/pr/comcast-corporation-abandons-proposed-acquisition-time-warner-cable-after-justice-department.

[14] Final Order, *In the Matter of ProMedica Health System, Inc.*, F.T.C. Docket No. 9346 (Mar. 22, 2012), https://www.ftc.gov/sites/default/files/documents/cases/2012/06/120625promedicaorder.pdf.

[15] Complaint, *United States v. Anthem, Inc.*, Case No. 1:16-cv-01493, 2017 WL 242848 (D.D.C. July 21, 2016).

[16] Complaint, *United States v. Adobe Sys., Inc.*, No. 10-cv-01629, 2010 WL 11417874 (D.D.C. Sept. 24, 2010); Complaint, *United States v. Lucasfilm Ltd.*, No. 10-cv-02220, 2010 WL 5344347 (D.D.C. Dec. 21, 2010); Complaint, *United States v. eBay, Inc.*, No. 12-cv-5869, 2012 WL 5727488 (N.D. Cal. Nov. 16, 2012).

[17] *North Carolina Bd. Dental Exam'r v. Fed. Trade Comm'n*, 135 S.Ct. 1101 (2015); *Teladoc, Inc. v. Texas Med. Bd.*, 112 F. Supp. 3d 529 (W.D. Tex. 2015).

Enforcers can also block mergers that eliminate important head-to head competition between R&D pipelines that employ scientists and researchers. Finally, enforcers can look even more skeptically at claims that mergers will lower costs (by among other things, reducing employment). By protecting the competitive process, enforcement also promotes market conditions that are conducive to retaining and attracting labor.

Of course, lax antitrust enforcement is not the only source of concern as it pertains to labor and inequality problems. Advances in manufacturing and information technology, further shifts from a manufacturing to a service economy, expanding globalization of trade, and rising levels of education and income in other countries contribute as well. Moreover, there are a host of other statutory and regulatory constraints that affect labor through restrictions on worker mobility and occupational licensing requirements. While more vigorous antitrust enforcement is needed, antitrust needs support from other policy instruments. Trade, labor, education, tax, and small business policies all bear importantly on promoting competition.

3. **The pending merger between Sinclair Broadcast Group, the largest owner of local TV stations in America, and Tribune Media would create a broadcasting colossus, reaching 223 stations in 108 markets, covering 72% of households.**

   a. **Given the Justice Department's recent action to block the AT&T-Time Warner merger, wouldn't it raise serious concerns if the Department allowed the Sinclair-Tribune merger to proceed?**

The DOJ has recently moved to block large horizontal mergers and, more specifically, mergers that could adversely affect important markets for content such as news, entertainment and sports, and for the distribution of content to subscribers. The former category includes deals such as Comcast-NBCU and AT&T-Time Warner. While those are vertical combinations, the competitive issues raised by the horizontal combination of Sinclair-Tribute are equally compelling, for a number of reasons.

One is that consolidation in regional broadcasting markets eliminates important competition in the production and delivery of content. As we know, competition between independently controlled rivals is the best way to ensure benefits to consumers. In media, this includes the quality, diversity, and the independence of content. A free and diverse media is a critical foundation of a democratic society. The Sinclair-Tribune merger, which eliminates important competition in broadcasting markets, thus deserves significant scrutiny by antitrust enforcers.

Two, vigorous antitrust enforcement is particularly important in media and distribution because, under the Trump administration, the Federal Communications Commission (FCC) has loosened basic rules that protect diversity and consumers. This includes rules pertaining to national TV audience caps and the rollback of net neutrality. The loosening of FCC rules, abolishment of important policies, and associated abandonment of its public interest mandate disrupts a fundamental and important partnership between antitrust and regulation to promote competition and consumer benefits. Antitrust enforcement is therefore now more important in media and distribution than ever before.

Finally, the proposed deal would create the largest-single group of local TV stations,[18] in which the merged company would have a "commanding presence."[19] A merger in a highly concentrated market should be considered presumptively anticompetitive and illegal under Section 7 of the Clayton Act.[20] As a result, it should be blocked. The DOJ and FTC came to the same decision in recent large horizontal mergers, including Staples/Office Depot, Sysco-US Foods, Halliburton and Baker-Hughes, to name a few.

b. Recent media reports indicate that the Justice Department may be proposing a deal in which Sinclair would be required to sell off 12 to 13 Tribune stations. Do you think the remedies proposed by the Justice Department can adequately mitigate the effects of this merger?

I do not. Precedent is vitally important in this case. The antitrust agencies' inability to come to settlements in recent large horizontal mergers highlights the difficulty of fashioning a remedy(ies) in markets where there are only a few large rivals and strong incentives to coordinate, rather than compete. In highly concentrated markets, viable buyers for critical assets are difficult, if not impossible to find, the remedy often must include the merger firms in some way (e.g., supply agreements), and the chances of finding a remedy that will fully restore competition lost by the merger are slim to none. In short, some deals are too anticompetitive to fix.

---

[18] Todd C. Frankel, *Sinclair Broadcast to buy Tribune Media for $3.9 billion, giving it control over 215 local TV stations*, WASH. POST. (May 8, 2017), https://www.washingtonpost.com/news/business/wp/2017/05/08/sinclair-broadcast-to-buy-tribune-media-for-3-9-billion-creating-nations-largest-tv-station-group/?utm_term=.992d2ebec4b9.
[19] Brent Kendall & John D. McKinnon, *Sinclair's Purchase of a Tribune Likely to Win Approval of Justice Department*, WALL ST. J. (Dec. 14, 2017), https://www.wsj.com/articles/sinclairs-purchase-of-tribune-likely-to-win-approval-of-justice-department-1513252800.
[20] *See* United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 364 (1963).