

# **An Economic Defense of Multiple Antitrust Goals: Reversing Income Inequality and Promoting Political Democracy**

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## **ABSTRACT**

Two recent papers by prominent antitrust scholars argue that a revived antitrust movement can help reverse the dramatic rise in economic inequality and the erosion of political democracy in the United States. Both papers rely on the legislative history of the key antitrust statutes to support their case. Not surprisingly, their recommendations have been met with alarm in some quarters and with skepticism in others. Such proposals by antitrust reformers are often contrasted with the Consumer Welfare Standard that pervades antitrust policy today. The Consumer Welfare Standard suffers from several defects: (1) It employs a narrow, unworkable measure of welfare; (2) It excludes important sources of welfare based on the assumption that antitrust seeks only to maximize wealth; (3) It assumes a constant and equal individual marginal utility of money; and (4) It is often combined with extraneous ideological goals. Even with these defects, however, if applied consistent with its theoretical underpinnings, the consideration of the transfer of labor rents resulting from a merger or dominant firm conduct is supported by the Consumer Welfare Standard.

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Moreover, even when only consumers (and not producers) are deemed relevant, the welfare of labor still should consistently be considered part of consumer welfare. In contrast, fostering political democracy—a prominent traditional antitrust goal that was jettisoned by the Chicago School—falls outside the Consumer Welfare Standard in any of its constructs. To undergird such important broader goals requires that the Consumer Welfare Standard be replaced with the General Welfare Standard. The General Welfare Standard consists of modern welfare economics modified to accommodate objective analyses of human welfare and purged of inconsistencies.

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## Introduction

Competition can be a powerful tool to help tackle such important social problems as increased inequality, reduced privacy, rampant misinformation, and erosion of political democracy. For example, in their recent paper, Lina Khan and Sandeep Vaheesan demonstrate how practices that increase market power have facilitated the transfer of income and wealth from the working class, small business, the middle class, and the poor to large corporations and wealthy shareholders.<sup>1</sup> They contend that reenergized antitrust enforcement can help slow this destructive trend toward inequality. Khan and Vaheesan lay blame for this wealth transfer at the feet of the Chicago School, which emphasized limited antitrust enforcement under the banner of the Consumer Welfare Standard. Adoption of the Consumer Welfare Standard resulted in the abandonment of the traditional antitrust goals of protecting “consumers and small suppliers from the market power of large sellers and buyers, [maintaining] the openness of markets, and [dispersion] of economic and political power.”<sup>2</sup> The authors document the large monopoly rents generated by six major economic sectors in the U.S. economy.<sup>3</sup> They contend that the current limited goals of antitrust enforcement stand in stark contrast to the broad concerns expressed by Congress in passing the major antitrust laws.<sup>4</sup>

In a complementary analysis, Robert Lande and Sandeep Vaheesan, argue that the antitrust laws should once again be concerned with firm size as it once did.<sup>5</sup> They argue that excessive firm size must be addressed even when not accompanied by reductions in competition, as in many conglomerate mergers. They advise that excessive firm size inevitably leads to an erosion of political democracy, especially in an environment where limitations on political spending have been eliminated on constitutional grounds.<sup>6</sup> Like Khan and Vaheesan, the authors rely on an extensive review of the statutory history of the antitrust laws that reveals a concern for preservation of political democracy.<sup>7</sup>

Throughout this paper, I endorse these works, but take it one step further—offering up an alternative to the outdated Consumer Welfare Standard, which I term the General Welfare Standard—and demonstrate how that standard is supported both in economics and by recent advances in biology and the social sciences. My argument is straightforward: progressive antitrust reforms are not “populist” or “hipster,” as detractors have maintained, but rather are fully supported by economic theory. Progressive policies of reducing income inequality and

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<sup>1</sup> Lina Khan and Sandeep Vaheesan, “*Market Power and Inequality: The Antitrust Counterrevolution and Its Discontents*,” 11 HARVARD LAW & POL. REV. 235 (2017).

<sup>2</sup> *Id.* at 237.

<sup>3</sup> *Id.* at 246.

<sup>4</sup> *Id.* at 270-271.

<sup>5</sup> Robert Lande & Sandeep Vaheesan, “*Preventing the Curse of Bigness Through Conglomerate Merger Legislation*,” 52 ARIZ. STATE L. J. 75, 82 (2020) (“Since the early 1980s, the federal antitrust agencies have broken with Supreme Court precedent and reinterpreted the anti-merger statute to focus exclusively on mergers’ effect on consumer welfare – an unsettled term.”).

<sup>6</sup> *Id.* at 86-89.

<sup>7</sup> *Id.* at 82-85.

fostering social democracy are entirely compatible with fundamental economic principles, as well as being historically consistent with the purposes of the antitrust statutes.

The first section of this paper validates the contentions of the earlier works by Khan, Lande and Vaheesan (and others) that Congressional intent in passing the antitrust statutes was never limited to correcting only “pure” economic effects such as higher prices, lower output, compromised product quality, or even reduced innovation. It was much broader. In general, Congress saw antitrust law as a tool to curb the practices and influence of dominant firms in the economy. The damage from excessive influence of large firms ran the gamut of limiting the opportunities of small business, undermining political democracy through domination of the political process, creating income inequality, distorting corporate governance, harming innovation and growth, and yes, raising prices and lowering output to consumers. Today, one would have to add concerns about privacy and misinformation to that list.

Part II of this paper critically assesses the Consumer Welfare Standard and its theoretical flaws. As originally articulated by Judge Bork, the Consumer Welfare Standard was simply a restatement of Marshall’s theory of consumer’s surplus. As I have argued elsewhere, Marshall’s approach assumed cardinal utility and interpersonal comparison of utility.<sup>8</sup> This point is addressed at length in the Appendix to this paper, where I discuss aggregation of ordinal utility and its problems. Marshall also assumed that the marginal utility of income was constant and equal among individuals, although he acknowledged this was not a reliable assumption. Marshall measured utility by willingness to pay and did not consider willingness to accept as another measure of utility. These assumptions were ported over by Judge Bork in his Consumer Welfare Standard. Bork, however, did not accept (or was unaware of) Marshall’s views that poverty and inequality were particularly harmful to human welfare based on his reading of the empirical evidence. Quite the opposite, the Consumer Welfare Standard has come to be associated with conservative and/or libertarian values that are unconnected to welfare economics.

Part III of this paper discusses two critical aspects of human well-being ignored by the Consumer Welfare Standard: the deleterious results of transferring labor rents to corporations, their executives and shareholders; and the undermining of political democracy caused by the concentration of political power in large corporations and the wealthy. The Consumer Welfare Standard is not a barrier to a revitalized antitrust concern for income inequality and transfers from labor to shareholders; however, that has been the practical result of its application. Even under the Consumer Welfare Standard, the welfare of all individuals impacted by mergers or dominant firm conduct must be considered. And even if restrictions are imposed, such as limits on cross markets effects, or singular consideration of consumer surplus, the welfare of workers should be considered part of consumer welfare.<sup>9</sup>

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<sup>8</sup> Mark Glick, “*The Unsound Theory Behind the Consumer (and Total) Welfare Goal in Antitrust*,” 63 ANTITRUST BULL. 455 (2018).

<sup>9</sup> *United States v. Philadelphia National Bank*, 374 U.S. 321, 370-371 (1963); *United States v. Topco Assocs.*, 405 U.S. 596, 609-610 (1972). See discussion in Daniel Crane, “*Balancing Effects Across Markets*,” 80 ANTITRUST L. J.

Transfers of labor rents have to date been ignored primarily because the Consumer Welfare Standard assumes that the marginal utility of income is constant and equal for everyone – an assumption that has no economic supporters. Treating transfers of income from the poor to the rich as welfare neutral has no justification. Moreover, in this section I show how lowering wages dilutes incentives to innovate and harms the economic performance of the economy generally.

Part III then turns to another important source of welfare loss—welfare losses from reduced political democracy—that could be ameliorated by antitrust enforcement but is beyond the ability of the Consumer Welfare Standard to address. Indeed, it is particularly ironic that a key concern of Congress in crafting the antitrust laws—protecting political democracy—falls outside of the boundaries of the Consumer Welfare Standard. Judge Bork claimed that antitrust’s pursuit of its traditional goals “would have serious deleterious effects upon national wealth.”<sup>10</sup> Subsequent research, to the contrary, has shown that political democracy is actually a critical element of economic growth, innovation, and efficiency. This is because dominant firms use their influence to raise their own profitability by avoiding competition, rent seeking from the government, shifting costs (such as environmental costs) to the public, outsourcing legal responsibilities for worker safety and medical benefits to smaller firms, and reducing the power of unions. Nonetheless, the Consumer Welfare Standard’s narrow subjective measure of welfare makes it virtually impossible to bring modern social science to bear in the debate about how antitrust policy can advance welfare.

In the last section (Part IV), I contend that the Consumer Welfare Standard should be replaced with a “General Welfare Standard,” informed by advances in modern welfare economics and other disciplines. Modern welfare economics considers every effect of dominant firm conduct on every impacted individual. It treats the welfare of all individuals, whether workers in the firm or hedge fund shareholders, as relevant. Obviously, judicial rules and presumptions would be fashioned, but artificial limitation of antitrust goals would be eliminated. A General Welfare Standard could accommodate Congressional concern for political democracy, because democracy increases welfare by establishing social cohesion and giving citizens greater control over their lives. I argue, however, that to be meaningful, a General Welfare Standard must be capable of incorporating objective evidence of welfare, not simply subjective measures based on willingness to pay.<sup>11</sup> In this way, a General Welfare Standard would necessarily incorporate the

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391 (2015). On labor welfare as part of consumer welfare *see* Ted Tatos and Hal Singer, “The Abuse of Offsets as Procompetitive Justifications: Restoring the Proper Role of Efficiencies After Amex and Alston,” unpublished manuscript (2022); Clayton Masterman, “*The Customer is Not Always Right: Balancing Worker and Customer Welfare in Antitrust Law*,” 69 VANDERBILT L. REV. 1387, 1400 (2016) (“Equity requires that employee surplus is part of consumer welfare” any other result “is absurd as well as inapposite to Supreme Court precedent.”).

<sup>10</sup> Robert Bork, “*The Goals of Antitrust Policy*,” 57 AMER. ECON. REV. 242, 245 (1967).

<sup>11</sup> A similar point is made by Robert Cooter and Peter Rappoport, “*Were the Ordinalists Wrong About Welfare Economics?*” 22 J. OF ECON. LIT. 507, 509 (1984) (“The aim of this paper is to demonstrate that the arguments developed some fifty years ago to criticize the material welfare school do not in fact address the claims of that school, whose scientific integrity remains intact.”). The material welfare school focused on the material needs of individuals such as school meals, health care, and training. *Id.* at 514. My discussion of objective measures of welfare is broader, and follows in the modern work by Sen, Griffin, and others.

contributions of leading welfare economists like A.K. Sen and major moral philosophers like James Griffin and T. M. Scanlon.

## **I. U.S. Antitrust Policy’s Broad, Multi-Goal Tradition**

Reading antitrust’s legislative history from today’s viewpoint, it is surprising how thoroughly the Consumer Welfare Standard and its narrow focus on “legitimate” goals has taken hold in antitrust policy circles. The Consumer Welfare Standard stands in stark contrast to the rich legislative history demonstrating Congressional intent to tackle much broader social goals. Indeed, it is a mystery why the courts, enforcement agencies, and antitrust lawyers have been so willing to sidestep the clearly stated goals of Congress when implementing antitrust policy.

### *A. Antitrust in the Late Nineteenth Century*

The Sherman Act, the first of the antitrust statutes, was a response to the economic and political tensions caused by the industrial revolution in the United States. The industrial revolution gained its full stride after the Civil War, helped by a series of events, including the discovery of new coal deposits in eastern Pennsylvania, the influx of immigrants following the 1848 revolutions in Europe, and the rise of the railroads—a joint effort by local governments and private interests.<sup>12</sup> The railroads opened up mass markets and large corporations arose. These large corporations attempted to shield themselves from the emerging fierce competition by the formation of trusts and cartels.<sup>13</sup> At the same time, the new firms generated enormous wealth for their owners, giving rise to extreme income inequality and political corruption.<sup>14</sup> The legislative debates around the Sherman Act pitted big business against the interests of other economic classes including agriculture, small business, and to a lesser degree labor. At the time, the power of these two sides were roughly comparable in the Senate.<sup>15</sup>

#### 1. Antitrust Goals in the Sherman Act Legislative History

As noted by legal historian James May, the Sherman Act Congressional “debates appear to indicate a widespread congressional commitment to the long-established ideals of economic

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<sup>12</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*,” 64 ANTITRUST BULL. 295, 298 (2019).

<sup>13</sup> The fierce competition was referred to as “ruinous competition” at the time. It was ruinous because it involved price competition among homogeneous products. This point is developed in NAOMI LAMOREAUX, “THE GREAT MERGER MOVEMENT IN AMERICAN BUSINESS, 1895-1904,” Pub. (1985).

<sup>14</sup> BENJAMIN PAGE AND MARTIN GILENS, “DEMOCRACY IN AMERICA?,” Chicago (2020) at 25-26 (“[T]he extreme economic inequality of the Gilded Age brought with it a high degree of political inequality. Democracy declined. ‘Muckraker’ journalists wrote of the ‘treason of the Senate’; they showed that key senators were on the payrolls of wealthy bankers or industrialists and did the bidding of their employers.”).

<sup>15</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*,” 64 ANTITRUST BULL. 295, 300 (2019).

opportunity, security of property, freedom of exchange, and political liberty, and considerable hope that antitrust law might prove to be an effective vehicle for their substantial, simultaneous realization.”<sup>16</sup> The Senate debaters voiced concerns beyond higher prices and lower output resulting from the cartels. Indeed, discussions of “pure” economic effects are hard to locate in the legislative history. The three main protagonists in the Sherman Act Senate debates, Senators Sherman, Hoar, and George all expressed concerns arising from political domination by big business. An obvious example is Senator Sherman’s famous floor speech:

The popular mind is agitated with problems that may disturb social order, and among them all none is more threatening than the inequality of condition, of wealth, and opportunity that has grown within a single generation out of the concentration of capital into vast combinations to control production and trade and break down competition.<sup>17</sup>

Senator Hoar likewise voiced concern about monopolies and described “the great monopolies as a menace to republican institutions themselves.”<sup>18</sup> Senator George hoped the legislation would specifically protect small businesses that were harmed by monopolies:

It is a sad thought to the philanthropist that the present system of production and of exchange is having that tendency which is sure at some not very distant day to crush out all small men, all small capitalists, all small enterprises.<sup>19</sup>

Hence, the major legislator contributors to the text of the Sherman Act expressed concern for two “non-economic” goals of antitrust laws: political democracy and protection of small business.<sup>20</sup> At least there cannot be doubt that these were the stated goals of Congress.<sup>21</sup>

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<sup>16</sup> James May, “*Antitrust in the Formative Era: Political and Economic Theory in Constitutional and Antitrust Analysis, 1880-1918*,” 50 OHIO ST. L. J. 257, 288 (1989). May also commented, “Sherman continued to embrace traditional nineteenth century assumptions treating economic opportunity, efficiency, competition, wealth distribution and political liberty as all of a piece.” *Id.* at 290.

<sup>17</sup>Quoted in David Millon, “*The Sherman Act and the Balance of Power*,” 61 S. CAL. L. REV 1219, 1277-1278 (1988) (quoting 21 Cong Rec. 2457 (1890)).

<sup>18</sup> *Id.* at 1277 (quoting 21 Cong. Rec. 2460 (1890)).

<sup>19</sup> HANS B. THORELLI, “THE FEDERAL ANTITRUST POLICY: ORIGINATION OF AN AMERICAN TRADITION,” The Johns Hopkins Press 1955 at 191 (quoting 21 Cong. Rec. 2597 (1890)).

<sup>20</sup> The Sherman Act was debated in the context of a period of deflation and economic instability, and efforts by big business to avoid the impact of competition and deflation on profits. The U.S. Industrial Commission reported in 1900: “Among the causes which have led to the formation of industrial combinations, most of the witnesses were of the opinion that competition, so vigorous that profits of nearly all competing establishments were destroyed, is to be given first place.” Quoted in MARTIN SKLAR, “THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM 1890-1916,” Cambridge U.P 1988 56 (1988). Rudolph Peritz explores the conflicting ideologies of the Sherman Act debates in “COMPETITION POLICY IN AMERICA 1988-1992: HISTORY, RHETORIC, LAW,” Oxford U.P 1996. On the other hand, Gabriel Kolko shows how the railroad magnates were able to craft a legalized cartel for the railroads, the Interstate Commerce Act of 1887, and garner the requisite political support for its passage. GABRIEL KOLKO, “RAILROADS AND REGULATION 1877-1916,” Princeton (1965).

<sup>21</sup> However, Gabriel Kolko has argued that much of the early antitrust activity was motivated by big business interests and only couched in the interests of the other classes. GABRIEL KOLKO, “THE TRIUMPH OF CONSERVATISM: A REINTERPRETATION OF AMERICAN HISTORY, 1900-1916” Free Press (1963) at 58-59 (“[T]he history of the United

However, it is one thing to pass a federal statute; it is quite another to enforce it. President Harrison signed the Sherman Act into law. But during the remaining thirty-two months of the Harrison Administration, it brought only seven cases. The Cleveland Administration brought eight cases, of which four were against labor. The McKinley Administration brought only three cases. Although the Sherman Act was a criminal statute, in the first few decades of enforcement, only Eugene Debs, a prominent labor leader and self-proclaimed socialist, went to jail.<sup>22</sup>

Early Supreme Court cases also interpreted the goals of the Sherman Act broadly. In *United States v. Trans-Missouri Freight Association*, 166 U.S. 290 (1897), Justice Peckham made clear that his understanding of the goals of the Sherman Act included protection of smaller business:<sup>23</sup>

In business or trading combinations [trusts or similar arrangements] may even temporarily, or perhaps permanently, reduce the price of the article traded in or manufactured, by reducing the expense inseparable from the running of many different companies for the same purpose. Trade or commerce under those circumstances may nevertheless be badly and unfortunately restrained by driving out of business the small dealers and worthy men whose lives have been spent therein, and who might be unable to readjust themselves to their surroundings. Mere reduction in the price of the commodity dealt in might be dearly paid for by the ruin of such a class, and the absorption of control over one commodity by an all-powerful combination of capital.<sup>24</sup>

In later cases, several well-known jurists also recognized that the Sherman Act had broad-ranging goals, including dispersion of economic and political power and support for small business.<sup>25</sup> For example, in his dissent in the *Columbia Steel* case, Justice Douglas noted:

The philosophy of the Sherman Act is that it [economic power] should not exist. For all power tends to develop into a government in itself. Power that controls the economy should be in the hands of elected representatives of the people, not in the hands of an industrial oligarchy. Industrial power should be decentralized. It should

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States from Theodore Roosevelt through Woodrow Wilson is consistently conservative. Nor is the extension of federal regulation over the economy a question of progressive intent thwarted by conservative administration and fulfilment. Important business elements could always be found in the forefront of agitation for such regulation, and the fact that well-intentioned reformers often worked with them—indeed, were often indispensable to them—does not change the reality that federal economic regulation was generally designed by the regulated interests to meet its own end, and not those of the public or the commonweal.”)

<sup>22</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School*,” 64 ANTITRUST BULL. 295, 301 (2019). I

<sup>23</sup> See discussion in Harlan Blake and William Jones, “*Towards a Three-Dimensional Antitrust Policy*,” 65 COL. L. REV. 422, 423-424 (1965).

<sup>24</sup> 166 U.S. at 323-324. See also George Bittlingmayer, “*Did Antitrust Policy Cause the Great Merger Wave*,” 28 J. OF LAW AND ECON. 77, 86-92 (1985) (arguing that the early antitrust cases, including the *Trans-Missouri Freight* case, were important causes of the first great merger wave in the United States).

<sup>25</sup> See Stephen Martin, “*Dispersion of Power as an Economic Goal of Antitrust Policy*,” Institute for Research in the Behavioral, Economic, and Management Sciences, Purdue Univ. Working Paper 1285, December 2016 (collecting relevant quotations).



be scattered into many hands so that the fortunes of the people will not be dependent on the whim or caprice, the political prejudices, the emotional stability of a few self-appointed men.... That is the philosophy and the command of the Sherman Act. It is founded on a theory of hostility to the concentration in private hands of power so great that only a government of the people should have it.<sup>26</sup>

And, in *United States v. Aluminum Co. of America*, Judge Hand expressly acknowledged that:

[Congress in passing the Sherman Act] was not necessarily actuated by economic motives alone. It is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept the direction of a few.<sup>27</sup>

Finally, Chief Justice Warren's construction of the goals of the antitrust laws in *Brown Shoe Co. v. United States* was as follows:

It is competition, not competitors, which the Act protects. But we cannot fail to recognize Congress' desire to promote competition through the protection of viable, small locally owned businesses. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets.<sup>28</sup>

*B. Antitrust During the Progressive Era: The Clayton Act and the Federal Trade Commission Act*

Recognition of the antitrust laws' multi-goal foundations persisted into the twentieth century. The United States entered the twentieth century in the midst of the first great merger movement.<sup>29</sup> As described by Gabriel Kolko, the newly formed large firms were largely organized as corporations with professional managers in control. The financial backers of these mergers took board seats and bankers exercised substantial corporate control.<sup>30</sup> Not surprisingly then, opposition to mergers during this period combined antipathy not only for mergers *per se*, but also for the size and corporate practices of the new enterprises. Resultant reform efforts included legislative proposals that combined regulation of large corporations with limitations on efforts by banks to control corporate boards. Lawrence Mitchell described the efforts as follows:

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<sup>26</sup> *United States v. Columbia Steel Co.*, 334 U.S. 495, 535 (1948) (Douglas, J. dissenting).

<sup>27</sup> *United States v. Aluminum Co. of America*, 148 F. 2d 416, 427 (2d Cir. 1945) (emphasis added). Quoted in Kenneth G. Elzinga, "The Goals of Antitrust: Other than Competition and Efficiency, What Else Counts?" 125 UNIV. OF PENN L. REV. 1191, 1203 (1977).

<sup>28</sup> *Brown Shoe Co. v. United States*, 370 U.S. 294, 344 (1962).

<sup>29</sup> NAOMI LAMOREAUX, "THE GREAT MERGER MOVEMENT IN AMERICAN BUSINESS, 1895-1904," Cambridge U.P., 1985; Anthony O'Brien, "Factory Size, Economies of Scale, and the Great Merger Wave of 1898-1902," 48 J. ECON. HIST. 639 (1988).

<sup>30</sup> GABRIEL KOLKO, "THE TRIUMPH OF CONSERVATISM: A REINTERPRETATION OF AMERICAN HISTORY, 1900-1916," Free Press (1963). For example, the Morgan partners held 167 directorships in eighty-nine corporations with assets over \$20 billion. MICHAEL HILTZIK, "THE NEW DEAL: A MODERN HISTORY," Free Press (2011) at 82.

No fewer than sixty-two unsuccessful bills embraced federal incorporation or federal licensing. An additional eight attacked overcapitalization and seven more tried to create some form of securities regulation.... Antitrust concerns remained central. But the growing congressional understanding that the “corporations” problem was bigger than monopoly alone led federal incorporation or licensing proposals to become the most frequently introduced type of antitrust legislation.<sup>31</sup>

Thus, the antitrust reform debates at the turn of the century were about corporate power and corporate governance, not prices paid by consumers. Many of these legislative reforms were efforts by big business to establish “reasonable” reforms to insulate them from the political dangers posed by the Grangers, Populists, trade unionists, and the socialists.<sup>32</sup> The American Federation of Labor participated in the debates around antitrust policy and fought hard to prevent the erosion of labor’s bargaining power within the new large enterprises, and to eliminate the use of Sherman Act injunctions against union activity.<sup>33</sup>

### 1. Legislative History of the Clayton Act and the Federal Trade Commission Act

The last two major comprehensive antitrust statutes, the Federal Trade Commission Act (the “FTC Act”) and the Clayton Act, passed in 1914 during the Wilson Administration.<sup>34</sup> Once again, the legislative history of those acts evinces broad concerns significantly beyond traditional economic factors. Zephyr Teachout & Lina Khan point out that the Congressional debates around the FTC Act displayed much consternation about the political influence of large corporations, and the resulting lesser opportunities open to other social classes.<sup>35</sup> Robert Lande and Sandeep Vaheesan have collected Congressional statements during the Clayton Act debates expressing disquiet about corporate size, political influence of corporations, and closure of

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<sup>31</sup> LAWRENCE MITCHELL, “THE SPECULATION ECONOMY: HOW FINANCE TRIUMPHED OVER INDUSTRY,” (pub) (date) at 136.

<sup>32</sup> MARTIN SKLAR, “THE CORPORATE RECONSTRUCTION OF AMERICAN CAPITALISM, 1890-1916,” Cambridge (1988) at 77. Many of the reforms were the product of the National Civic Federation, the major organization for big business. JAMES WEINSTEIN, “THE CORPORATE IDEAL IN THE LIBERAL STATE 1900-1918,” Beacon Press, (1968) at 6 (“Before the first World War, the Civic Federation was the most important single organization of the socially conscious big businessmen and their academic and political theorists.”).

<sup>33</sup> Both Roosevelt and Wilson opposed a labor exemption from the antitrust laws. But the AFL had Congressional supporters and the Clayton Act contained a statement that labor was not a commodity (Section 6) and created a qualified limitation to the labor exemption (Section 20). The Supreme Court in a series of cases held that virtually all strike, boycott, picketing, or other union protest activity was not exempted. *Colorado Coal Co. v. United Mine Workers*, 268 U.S. 295 (1925); *Duplex Printing Press Co. v. Deering*, 254 U.S. 443 (1921); *American Foundries v. Tri-City Central Trades Council*, 257 U.S. 184 (1921). See generally WILLIAM FORBATH, “LAW AND THE SHAPING OF THE AMERICAN LABOR MOVEMENT” Harvard (1989).

<sup>34</sup> For an in-depth examination of the original Clayton Act and the 1950 amendments, see DAVID MARTIN, “MERGERS AND THE CLAYTON ACT,” U. of Cal. (1958).

<sup>35</sup> Zephyr Teachout & Lina Khan, “*Market Structure and Political Law: A Taxonomy of Power*,” 9 DUKE J. OF CONST. LAW & PUB. POL. 1, 62 (2014). This is not to say that the FTC Act was not favorable to big business. It was largely the work of the National Civic Federation, a policy organization dominated by big business. JAMES WEINSTEIN, “THE CORPORATE IDEAL IN THE LIBERAL STATE 1900-1918,” Beacon Press, (1968).

economic opportunities for others.<sup>36</sup> For example, they note the remarks of Representative Kelly who stated: “Enterprises with great capital have deliberately sought not only industrial domination but political supremacy as well...”<sup>37</sup> The House Committee Report on Section 8 of the Clayton Act further expressed a concern for political democracy. It noted that “[t]he concentration of wealth, money and property in the United States under the control and in the hands of a few individuals or great corporations has grown to such an enormous extent that unless checked it will ultimately threaten the perpetuity of our institutions.”<sup>38</sup>

## 2. Antitrust After the Passage of the Clayton Act and the Federal Trade Commission Act

The outbreak of World War I cut short much of the potential for economic and social change implicit in the new antitrust statutes. As the United States prepared for the war effort, Wilson established the War Industries Board, which in turn established trade committees to gather market information, coordinate supply, and stabilize prices.<sup>39</sup> The “scientific management” practices of the War Industries Board carried over into the 1920s, and little attention was paid to antitrust enforcement.<sup>40</sup> The antitrust debates still were not primarily about consumer prices, however. The main issues were how to maintain macroeconomic stability through trade commission planning, while limiting the dangers of price fixing and big rigging.<sup>41</sup>

### C. *The Great Depression and the New Deal*

Antitrust policy’s broad goals continued into the New Deal era; indeed, that emphasis both accelerated and expanded. The Great Depression resulted in a loss of confidence in the ability of big business and large banks to achieve economic stability. As Peter Temin has demonstrated, the initial downturn in 1929 was strongest in the industries dominated by big business.<sup>42</sup> In

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<sup>36</sup> Robert Lande & Sandeep Vaheesan, “*Preventing the Curse of Bigness Through Conglomerate Merger Legislation*,” 52 ARIZ. ST. L.J. 75, 82-85 (2020). However, the final Clayton Act bill did not contain the exemption for labor that the American Federation of Labor sought. “The New York Times reported on February 2, 1914 that the president [Wilson] had let it be known that he would veto any antitrust measure that exempted labor from its provisions.” PHILIP FONER, “HISTORY OF THE LABOR MOVEMENT IN THE UNITED STATES,” 131 Vol. 5, Int. Pub. (1980). As a result, there were thousands of labor injunction cases during the 1920s. WILLIAM FORBATH, “LAW AND THE SHAPING OF THE AMERICAN LABOR MOVEMENT,” 118 Harvard U.P. (1989).

<sup>37</sup> *Id.* at 83

<sup>38</sup> *Id.*

<sup>39</sup> ROBERT CUFF, “THE WAR INDUSTRIES BOARD, BUSINESS-GOVERNMENT RELATIONS DURING WORLD WAR I,” Johns Hopkins Press (1973).

<sup>40</sup> The trade association movement in the 1920s is well described by RUDOLPH PERITZ, “COMPETITION POLICY IN AMERICA 1888-1992: HISTORY, RHETORIC, LAW” pub (1996).

<sup>41</sup> Antitrust cases in this period grappled with these issues. See *American Column & Lumber Co. v. United States*, 257 U.S. 377 (1921); *Maple Flooring Manufacturers’ Ass’n v. United States*, 268 U.S. 563 (1925); *Cement Manufacturers’ Protective Ass’n v. United States*, 268 U.S. 688 (1925). The *American Column* case reflects Louis Brandeis’ support for the trade association movement.

<sup>42</sup> PETER TEMIN, “LESSONS FROM THE GREAT DEPRESSION,” pub (1991) at 163 (“More concentrated industries and industries where the largest 50 firms were important appear to have suffered the largest decline in production.”).

addition, the financial sector created massive instability by forcing businesses to dilute retained earnings by paying high dividends.<sup>43</sup> In the early years of the New Deal, the Roosevelt Administration focused on regulation of banks and finance, in part a result of the powerful non-Morgan investment banking firms that backed Roosevelt.<sup>44</sup> Immediately following Roosevelt's inauguration, Congress passed the Banking Acts of 1933 (The Glass Steagall Act) and 1934, and the Securities Acts of 1933 and 1934. At the same time, Roosevelt embraced greater corporate planning through the National Recovery Administration (NRA).<sup>45</sup> The NRA created 546 industrial codes covering 550 industries and issued 11,000 orders interpreting the various code sections.<sup>46</sup>

Even before it was declared unconstitutional, the Roosevelt Administration became disenchanted with the NRA, however. The NRA was racked with conflict between protectionists and free traders, big firms and small firms (especially in the oil industry), while labor grew dissatisfied with enforcement of the NRA's 7A clause guaranteeing employee representation.<sup>47</sup> Clarence Darrow was asked to review the NRA in 1934. The Darrow Report concluded that the NRA was creating greater monopoly power and was not improving the position of labor as Roosevelt had hoped.<sup>48</sup> In 1935, the NRA was declared unconstitutional by the Supreme Court in *A.L.A. Schechter Poultry Corp. v. United States*.<sup>49</sup>

A second major policy shift occurred in what is sometimes called the second New Deal, but which I refer to as the New Deal Consensus. This policy change resulted from the emergence of a new political coalition of capital-intensive firms with internationalist free trade interests.<sup>50</sup> The ideological expression of the new coalition was that income and wealth inequality causes macroeconomic instability. Measures that increase social equality (unfortunately racial equality

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<sup>43</sup> See Apostolos Fasianos, et al., "Have We Been Here Before? Phases of Financialization Within the 20<sup>th</sup> Century in the United States," (Levy Inst. Working Paper 869 (June 2016) n. 102 at 14) (showing that on average retained earnings were negative during the 1920s).

<sup>44</sup> Thomas Ferguson, "From Normalcy to New Deal: Industrial Structure, Party Competition, and American Public Policy in the Great Depression," in "GOLDEN RULE: THE INVESTMENT THEORY OF PARTY COMPETITION AND THE LOGIC OF MONEY-DRIVEN POLITICAL SYSTEMS," Chicago (1995) at 148 ("A few days after Roosevelt was inaugurated, Chase and the investment bankers started their campaign, both in public and in private, for a new banking law. Aldrich made a dramatic public plea for the complete separation of investment and commercial banking.").

<sup>45</sup> Interestingly, the Blue Eagle emblem of the NRA was the origin of the name Philadelphia Eagles.

<sup>46</sup> Mark Glick, "Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust," 64 ANTITRUST BULL. 295, 313 (2019).

<sup>47</sup> Thomas Ferguson, "From Normalcy to New Deal: Industrial Structure, Party Competition, and American Public Policy in the Great Depression," in "GOLDEN RULE: THE INVESTMENT THEORY OF PARTY COMPETITION AND THE LOGIC OF MONEY-DRIVEN POLITICAL SYSTEMS," Chicago (1995) at 151.

<sup>48</sup> National Recovery Review Board: First Report to the President of the United States (1934).

<sup>49</sup> 295 U.S. 495 (1935).

<sup>50</sup> Thomas Ferguson, "From Normalcy to New Deal: Industrial Structure, Party Competition, and American Public Policy in the Great Depression," in "GOLDEN RULE: THE INVESTMENT THEORY OF PARTY COMPETITION AND THE LOGIC OF MONEY-DRIVEN POLITICAL SYSTEMS," Chicago (1995) at 152-153.

was rarely included), it was posited, would create the foundations for both a growing economy and political democracy.<sup>51</sup> The historian Ellis Hawley described the policy as follows:

But if one insisted on a dominant theme, he could probably find it in the concept of counter organization, in the idea of using government to promote the organization of economically weak groups, thus restoring economic balance.<sup>52</sup>

This sentiment provided the foundation for much of the later New Deal legislation: the National Labor Relations Act (the “Wagner Act”) promoted unionization; the first minimum wage was passed as part of the Fair Labor Standards Act; the Social Security Act created unemployment insurance; the Civilian Conservation Corps and other programs increased the income of the unemployed; and the Agricultural Adjustment Act increased farm income.<sup>53</sup>

In 1938, President Roosevelt introduced a new antitrust agenda. His focus was on the use of competition policy to curb the power of big business and the protection of political democracy. He stated that: “The liberty of a democracy is not safe if the people tolerate the growth of private power to a point where it becomes stronger than their democratic state itself. That, in its essence, is fascism—ownership of government by an individual, by a group, or by any other controlling private power.”<sup>54</sup>

The economic strategy of the New Deal Consensus was wildly successful. Among other things, it initiated a trend of more egalitarian income distribution. At the end of the 1920s, the top 1% of the population garnered about 24% of total income.<sup>55</sup> During the 1930s, this percentage declined to 16.6%.<sup>56</sup> Worker productivity soared in the 1930s,<sup>57</sup> as did growth in innovation.<sup>58</sup> On almost every economic measure of performance, increased income equality in the period of

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<sup>51</sup> Even before Keynes, Harold Moulton at the Brookings Institution had developed a theory of inadequate effective demand. HAROLD MOUTON, “INCOME AND ECONOMIC PROGRESS,” Brookings, (1934).

<sup>52</sup> ELLIS HAWLEY, “THE NEW DEAL AND THE PROBLEM OF MONOPOLY: A STUDY IN ECONOMIC AMBIVALENCE,” 187 Princeton (1985).

<sup>53</sup> All of these programs, passed by majority democratic Congresses, required the support of Southern Democrats. This resulted in concessions to Jim Crow policies and exclusion of black Americans from many New Deal programs. See IRA KATZNELSON, “FEAR ITSELF: THE NEW DEAL AND THE ORIGINS OF OUR TIME,” Liveright (2013).

<sup>54</sup> Quoted in Laura Phillips Sawyer, “Jurisdiction Beyond Our Borders: United States v. Alcoa and the Extraterritorial Reach of American Antitrust, 1909-1945” presentation at the University of Utah, Feb. 10, 2022 at 21-22.

<sup>55</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*,” 64 ANTITRUST BULL. 295 (2019), Appendix 1.

<sup>56</sup> *Id.*

<sup>57</sup> ROBERT GORDON, “THE RISE AND FALL OF AMERICAN GROWTH: THE U.S. STANDARD OF LIVING SINCE THE CIVIL WAR,” PRINCETON (2016) at 535 (“The Great Leap Forward of the American level of labor productivity that occurred in the middle decades of the twentieth century is one of the greatest achievements of all of economic history.”).

<sup>58</sup> Alexander Field, “*The Most Technologically Progressive Decade of the Century*,” 93 AMER. ECON. REV. 1399, 1406 (2003) (“[E]mployment of research scientists and engineers grew 72.9 percent between 1929-1933, while employment totals in other occupational categories collapsed. Between 1933 and 1940, R&D employment in U.S. manufacturing almost tripled, from 10,918 to 27,777.”).

the 1930s and continuing into the 1940s through the 1960s, was associated with favorable economic outcomes.<sup>59</sup>

### 1. The New Deal Consensus Antitrust Amendments

In the decades of the New Deal Consensus and the first decade following World War II, Congress twice amended the Clayton Act. The first revision was the Robinson Patman Act that amended section 2 of the Clayton Act. During the 1930s, opposition grew among small retailers to the growth of large chain stores. The FTC opened an investigation and issued its Final Report on the Chain Store Investigation in 1934.<sup>60</sup> The FTC discovered that the chain stores were not monopolists because they competed among themselves. Nevertheless, it found that the chain stores had buyer power that allowed them to obtain lower prices from manufacturers and farmers, resulting in a competitive advantage that harmed smaller retailers. The FTC found that, on average, chain grocery stores were able to underprice independents by 7.31%.<sup>61</sup>

In 1935, Representative Wright Patman of Texas introduced the Patman Bill in the House, which would become the Robinson Patman Act the next year. Patman described the purpose of the bill thusly:

This bill is designed to accomplish what so far the Clayton Act has only weakly attempted, namely to protect the independent merchant, the public whom he serves, and the manufacturers from whom he buys, from exploitation by his chain competitor.<sup>62</sup>

Similarly, in the Senate debate, Senator Joseph Robinson of Arkansas posed the following question revealing the bill's task:

How long does the Senator think the little man, the independent dealer, would last if he were left to the mercy of the larger dealer...?<sup>63</sup>

Accordingly, the explicit purpose of the 1935 revision to the Clayton Act was to protect small business. That protection was not from monopoly power *per se* (indeed, the FTC expressly concluded that the chain stores were not monopolists), but instead from price discrimination benefitting a larger competitor with buyer power. The Robinson Patman Act did not ignore the benefit of the lower costs that a larger competitor might garner as a result of its size, however. Rather, it added a cost justification defense, allowing price differences up to the amount of the

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<sup>59</sup> ROBERT GORDON, "THE RISE AND FALL OF AMERICAN GROWTH: THE U.S. STANDARD OF LIVING SINCE THE CIVIL WAR" Princeton (2016) at 555.

<sup>60</sup> FTC, "Final Report on the Chain Store Investigation" (1934).

<sup>61</sup> *Id.* at 29.

<sup>62</sup> EARL KINTNER & JOSEPH BAUER, "FEDERAL ANTITRUST LAW, A TREATISE ON THE ANTITRUST LAWS OF THE UNITED STATES," Anderson Pub. (1989) at 2933.

<sup>63</sup> *Id.* at 3117.

cost savings, but allocated the burden of proving such savings to the larger competitor.<sup>64</sup> Thus, it is evident that Congress was sufficiently concerned about protecting small business that an entire amendment was devoted to such protection.

Congress also passed the Celler-Kefauver Act in 1950. The Celler-Kefauver Act sought to close a loophole in the Clayton Act by expanding section 7's application to include mergers through stock acquisitions.<sup>65</sup> During the Celler-Kefauver Act debates, Congress made clear that it was concerned with economic concentration because, among other reasons, of its impact on political democracy.<sup>66</sup> Senator Kefauver stated:

I am not an alarmist, but the history of what has taken place in other nations where mergers and concentrations have placed economic control in the hands of very few people is too clear to pass over easily. A point is eventually reached, and we are rapidly reaching that point in this country, where the public steps in to take over when concentration and monopoly gain too much power. The taking over by the public through its government always follows one or two methods and has one or two political results. It either results in a Fascist state or the nationalization of industries and thereafter a Socialist or Communist state.<sup>67</sup>

The legislative history of the antitrust statutes is clear: Congress's concerns went well beyond traditional notions of monopoly power and its impact on consumer prices. Rather, Congress expressed broad concerns that economic and political power not become too concentrated, and that small businesses be protected from their larger competitors.

#### *D. Chicago School Efforts to Rewrite History*

By the end of the 1970s, however, corporate profits fell, the stock market was flat, and there was high inflation, and bond investments were losing value. The combination of these four factors eroded incomes at the high end, creating conditions for a counter-revolution against the New Deal Consensus by large corporations and the wealthy.<sup>68</sup>

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<sup>64</sup> Since the Robinson Patman Act expressly authorizes price differences resulting from efficiencies of scale, its modern critics focus their criticisms on the Act's allocation of the burden of proof on big business to prove such efficiencies. See Mark Glick, et al., "*Toward a More Reasoned Application of the Robinson Patman Act: A Holistic View Incorporating Principles of Law and Economics in Light of Congressional Intent*," 60 ANTITRUST BULL. 279, 284 (2015).

<sup>65</sup> Thus, Congress effectively closed the exception created by the Supreme Court's decision in *Brown Shoe v. United States*, 370 U.S. 294, 313 (1962).

<sup>66</sup> Robert Pitofsky, "*The Political Content of Antitrust*," 127 UNIV. OF PENN. L. REV. 1051, 1064 (1979) ("A striking feature of the legislative history of amended section 7 was the widely-shared perception of danger to the political well-being of the country and its citizens stemming from the merger movement.").

<sup>67</sup> Quoted in Robert Lande and Sandeep Vaheesan, "*Preventing the Curse of Bigness Through Conglomerate Merger Legislation*," 52 ARIZ. STATE L. J. 75, 84-86 (2020). Lande and Vaheesan assemble numerous statements during the 1950 Amendment's Congressional debate with similar import.

<sup>68</sup> Mark Glick, "*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*," 64 ANTITRUST BULL. 295, 324 (2019). During the 1970s corporate profits fell, the stock market was not growing, and

The core themes of this counter-revolution were the elimination of regulations and other impediments to expanding high incomes, reductions in the influence of unions and worker power, shareholder dominance in corporate governance, and a general return to free market laissez faire ideology.<sup>69</sup> This paradigm shift is often referred to as the “rise of neoliberalism.”<sup>70</sup> In antitrust, the Chicago School exemplified the principles of the neoliberal revolution.<sup>71</sup> At the core of the Chicago School approach to antitrust was the Consumer Welfare Standard.

In fairness to other neoliberals, only Judge Bork and a few of his most ardent devotees had the audacity to contend that Congress endorsed anything like the Consumer Welfare Standard when passing the Sherman Act. According to Judge Bork, Congress “was confined by the policy of advancing consumer welfare,” and “[t]he wide variety of other policy goals that have since been attributed to the framers of the Sherman Act is not to be found in the legislative history.”<sup>72</sup> Among antitrust historians, not surprisingly, Judge Bork’s analysis of the legislative history of the Sherman Act is considered thoroughly debunked.<sup>73</sup>

In sum, it is a matter of historical fact that the goals of the antitrust laws prior to the rise of neoliberalism and the Chicago School included dispersion of economic and political power, and protection of small business. From the vantage point of today, looking back on antitrust history, the Consumer Welfare Standard has been only a brief digression in a long history of a multi-goaled antitrust.

## II. Understanding the Consumer Welfare Standard

Contrary to the rich history detailed in Part I above, the Consumer Welfare Standard applied from the late 1970s on, authorized antitrust action directed at only a limited number of economic

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interest rates were zero or negative because of inflation. As a result, the income share of the top 1% of earners hit a Post-World War II low. This created a political backlash, and the founding and growth of conservative think tanks such as the Heritage Foundation (1973), and centers in law and economics at law schools. *See, e.g.*, ALAN NASSAR, “OVERRIPE ECONOMY AMERICAN CAPITALISM AND THE CRISIS OF DEMOCRACY,” pub. (2018) at 155, describing the spectacular increase in corporate lobbyists and corporate PACs in the late 1970s and early 1980s.

<sup>69</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*,” 64 ANTITRUST BULL. 295, 320-324 (2019).

<sup>70</sup> QUINN SLOBODIAN, “GLOBALISTS: THE END OF EMPIRE AND THE BIRTH OF NEOLIBERALISM,” Harvard (2018); PHILIP MIROWSKI AND DIETER PLEHWE, “THE ROAD FROM MONT PELERIN,” Harvard (2009); ANGUS BURGIN, “THE GREAT PERSUASION: REINVENTING FREE MARKETS SINCE THE DEPRESSION,” Harvard (2012); GERARD DUMENIL AND DOMINIQUE LEVY, “THE CRISIS OF NEOLIBERALISM,” Harvard (2011).

<sup>71</sup> PHILIP MIROWSKI AND DIETER PLEHWE, “THE ROAD FROM MONT PELERIN,” Harvard (2009) at 140 (“[T]he rise of the Chicago School must be understood as one component of a specific larger transnational project of innovating doctrines of neoliberalism for the postwar world.”). *See also* Herbert Hovenkamp, “*Antitrust Policy after Chicago*,” 82 MICH. L. REV. 213 (1985); Richard Posner, “*The Chicago School of Antitrust Analysis*,” 127 U. PENN. L. REV. 926 (1979).

<sup>72</sup> ROBERT BORK, “THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF,” 20-21 Basic (1978); Robert Bork, “*Legislative Intent and the Policy of the Sherman Act*,” 9 J. L. & ECON. 7 (1966).

<sup>73</sup> John Flynn, “*The Reagan Administration’s Antitrust Policy, ‘Original Intent’ and the Legislative History of the Sherman Act*,” 33 ANTITRUST BULL. 259 (1988); Robert Lande, “*Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*,” 34 HASTINGS L. J. 65 (1982-83); Herbert Hovenkamp, “*Antitrust’s Protected Classes*,” 88 MICH. L. R. 1 (1989); Thomas Hazlett, “*The Legislative History of the Sherman Act Re-examined*,” 30 ECON. INQUIRY 263 (1992).



consequences from mergers or conduct by dominant firms. Today, a majority of jurisdictions around the world have adopted the Consumer Welfare Standard, and even most of the post-Chicago school economists appear to accept it.<sup>74</sup>

The central text and source behind the Consumer Welfare Standard is Judge Bork's book *The Antitrust Paradox*. Bork's formulation and popularization of the Consumer Welfare Standard suffers from four fundamental problems. First, Bork erroneously understood welfare to be a measurement of wealth, by which he meant GDP. Noneconomic sources of well-being are excluded. As applied to antitrust policy, this translates into a scenario where only "economic effects" count. Second, Bork accepted wholesale Marshall's assumptions of cardinal utility and a constant and equal marginal utility of money, without acknowledging limitations on both that Marshall himself recognized. For example, it is widely acknowledged (including by Marshall) that there is diminishing incremental welfare when income increases. Third, Bork's formulation of the Consumer Welfare Standard is susceptible to, and has suffered from, contamination by political philosophies independent from and largely irrelevant to welfare economics. Indeed, the Consumer Welfare Standard has wrongly come to be viewed as inherently coextensive with conservative or libertarian political values, values that are foreign to welfare economics. Lastly, and the topic of Sections III and IV of this paper, the subjective measure of welfare embodied in the Consumer Welfare Standard is unsupportable and limits its applicability and usefulness.

#### *A. The Neoliberal Banishment of Antitrust's Traditional Goals and its Detrimental Effects*

While antitrust policy's history supports multi-faceted policy goals, the neoliberal construct limits antitrust to a single goal. According to Bork, the goal of antitrust is to maximize wealth. As Bork contended in a Yale Law Journal article prior to the publication of *The Antitrust Paradox*:

The existing scope and nature of the Sherman Act, as well as considerations of effective administration, thus indicate the statute is better suited to implement the policy of wealth maximization than the policies underlying the Brandeis approach.<sup>75</sup>

Unfortunately, Bork consistently confused the concept of wealth maximization and the economic concept of welfare in *The Antitrust Paradox*. He believed, for example, that "Consumer Welfare, in this sense, is merely another term for the wealth of the nation. Antitrust, thus, has a built-in preference for material prosperity, but it has nothing to say about the ways prosperity is distributed or used"<sup>76</sup>

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<sup>74</sup> Marshall Steinbaum & Maurice Stucke, *The Effective Competition Standard: A New Standard for Antitrust*, ROOSEVELT INSTITUTE (2018) at 11 (30 of 33 countries in a 2007 survey by the International Competition Network (ICN) identified consumer welfare as an antitrust objective.)

<sup>75</sup> Robert Bork, *The Rule of Reason and the Per Se Concept: Price fixing and Market Division* (Pt. 1), 74 YALE L. J. 775, 838 (1965).

<sup>76</sup> ROBERT BORK, "THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF," 90 Basic (1978)

But Judge Bork's construct is manifestly false. Wealth, by which Bork means output measured in current prices, or GDP, is not welfare. Normally we would think of wealth as a stock of assets valued at current prices. Bork appeared to use wealth as synonymous with GDP—the annual physical production of goods and services valued at current prices. But welfare is much more; it is the total additional utility individuals receive from that annual economic activity. The two are manifestly not the same: indeed, welfare and GDP can move in different directions.<sup>77</sup> Moreover, the amount of welfare inescapably depends on how economic output is distributed.<sup>78</sup>

Judge Bork further misapplied the term “efficiency.” Greater productive output does not necessarily translate into greater welfare. For example, the resulting increased goods and services achieved may not be useful or, indeed, they could even be harmful. Rather, properly understood, efficiency necessarily means achieving the maximum welfare. Wealth maximization can also not be used to identify efficient policy. The measurement of wealth depends on current prices, but these prices change whenever distribution (which results from a policy shift) changes, thus resulting in an inconsistent measure.<sup>79</sup>

After promoting wealth as the sole goal of antitrust enforcement, Bork then argued that wealth could be increased by ridding antitrust of its misguided traditional goals (labelled value judgments by him) of protecting small business and promoting political democracy:

Because [antitrust] serves the single, unchanging value of wealth maximization it does not require the courts to choose or weigh ultimate values in the decision of individual cases or in the continuing evolution of doctrine.<sup>80</sup>

But Bork seems to miss the fact that limiting antitrust policy solely to wealth maximization is, itself, the result of a value judgment.

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<sup>77</sup> For example, a point on the production possibility frontier can be on a lower social welfare curve than a point within the production possibility frontier.

<sup>78</sup> Economists trained in industrial organization may be forgiven for ignoring the welfare effects of distribution. In his leading graduate textbook in Industrial Organization, Jean Tirole candidly admits: “In this book, I will treat income distribution as irrelevant. In other words, the redistribution of income from one consumer to another is assumed to have no welfare effect. (The marginal social utilities of income are equalized.) I certainly do not feel that actual income distributions are optimal, even with an optimal income-tax structure (because there are limits and costs to income taxation, as is emphasized by the optimal-taxation literature). Market intervention does have desirable or undesirable income-redistribution effects. But I will focus on the efficiency of markets...” JEAN TIROLE, “THE THEORY OF INDUSTRIAL ORGANIZATION,” MIT (1989) at 12.

<sup>79</sup> Wealth Maximization where wealth is defined using current prices is not a consistent measure of efficiency because, as Kaplow and Shavell point out, “one must know the prices of different goods and services, yet there is no natural set of prices to use.” LOUIS KAPLOW AND STEVEN SHAVELL, “FAIRNESS VERSUS WELFARE,” Harvard U. P (2002) at 36. To apply the principle of wealth maximization one must take current prices as a given and then compute the wealth implication of the policy under consideration. However, once the policy impacts legal rules and distribution, relative prices change and wealth changes. Jules Coleman, “*Efficiency, Utility and Wealth Maximization*,” 8 HOFSTRA L. REV. 509, 525-526 (1980).

<sup>80</sup> Robert Bork, “*The Rule of Reason and the Per Se Concept: Price Fixing and Market Division* (Pt. 1), 74 YALE L. J. 775, 838 (1965).

Acceptance of the Chicago School’s own value judgment that antitrust regulation of business should be limited, and its misunderstanding that this result was somehow dictated by welfare economics, has led to at least two important detrimental consequences for antitrust enforcement. First, important Congressional concerns and traditional antitrust goals were banished from “legitimate” discussion among antitrust policy makers. Even today, such discussions are labelled “hipster” antitrust. The second detrimental consequence is more practical in nature: Recognition of the broader, traditional noneconomic antitrust goals was important in preventing courts and agencies from shifting the burden of proof in antitrust inquiries to plaintiffs, *i.e.*, the party challenging the proposed business activity. When the antitrust inquiry is limited to “economic effects,” economists can question the link between structural variables such as increased concentration, introducing the argument that the effects themselves are unlikely and cannot be presumed from structural changes.<sup>81</sup> This is, of course, what happened in merger enforcement when the *Philadelphia Bank* structural presumptions were loosened by the lower courts and by the Department of Justice and Federal Trade Commission 1982 Horizontal Merger Guidelines.<sup>82</sup> It is much harder to shift burdens of proof to regulators and antitrust plaintiffs when the goals of antitrust include a commitment to preserve dispersion of economic and political power. The consequences are readily apparent: The rise to prominence of the Chicago School and the Consumer Welfare Standard has led to ineffective and lax antitrust enforcement.<sup>83</sup>

*B. Alfred Marshall and The Consumer Welfare Standard’s Assumption That Marginal Utility of Money is Constant and Equal*

Judge Bork based his Consumer Welfare Standard on Alfred Marshall’s much earlier work. In 1890, the same year that the Sherman Act passed, Alfred Marshall introduced the concept of

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<sup>81</sup> This point is made by JONATHAN BAKER in his book “THE ANTITRUST PARADIGM: RESTORING A COMPETITIVE ECONOMY,” Harvard (2019) at 76-77 (“While the nature and strength of presumptions usually derives from two considerations related to error costs, deterrence policy and inferred effects, it may also depend on overarching policy goals. (...) Mid-twentieth-century courts justified antitrust rules limiting concentration by merger on political grounds. These courts argued that concentrated economic power produced political problems.”)

<sup>82</sup> In 1963, the Supreme Court, in *United States v. Philadelphia National Bank*, 374 U.S. 321 (1963), explained that the “intense congressional concern” about increasing concentration “warrants dispensing, in certain cases, with elaborate proof of market structure, market behavior, or probable anticompetitive effects.” *Id.* at 363. The Court created a presumption of an anticompetitive effect from a structural increase in concentration, placing the burden on the merging parties to refute the presumption. This is referred to as a “structural approach,” as opposed to an economic “effects approach,” which requires marshalling detailed proof of future competitive effects. In 1982 and 1984, the Department of Justice and Federal Trade Commission drafted merger guidelines in which concentration acts as a screening device to determine if further analysis is required. The DOJ, then, imposed on itself the burden to further demonstrate anticompetitive effects (coordinated or unilateral), essentially shifting the burden of proof from the merging entities. U.S. Dep’t of Just. 1984 Merger Guidelines.

<sup>83</sup> JOHN KWOKA, “MERGERS, MERGER CONTROL, AND REMEDIES: A RETROSPECTIVE ANALYSIS OF U.S. POLICY,” MIT Press, 2015 158-159 (“This project has found that merger enforcement has over time both diminished overall and tilted toward especially problematic mergers.... Simply put, many mergers that result in price increases are cleared.”); JOHN BAKER, “THE ANTITRUST PARADIGM: RESTORING A COMPETITIVE ECONOMY,” Harvard U.P. 2019 15 (“Antitrust Rules today insufficiently deter exclusionary practices that harm competition by raising rivals’ costs or limiting rivals’ access to customers.”); Carl Shapiro, “*Antitrust in a Time of Populism*,” 61 INT. J. OF IND. ORG. 714 (2018) (collecting popular press stories about a competitive decline in the United States).

consumer's surplus or consumer surplus to the English-speaking world.<sup>84</sup> Marshall held the prestigious chair of Political Economy at Cambridge University. His famous work, *Principles of Economics*, became the leading textbook in economics for two generations (until Samuelson's textbook). Marshall defined consumer's surplus as follows:

The excess of price which he (a consumer) would be willing to pay rather than go without the thing, over that which he actually does pay, is the economic measure of this surplus satisfaction. It may be called consumers' surplus.<sup>85</sup>

For Marshall, the amount of money that a consumer is willing to pay expresses the "utility" that the consumer receives from the purchase.<sup>86</sup> Utility is a measure of well-being, and for Marshall well-being derived from the satisfaction of preferences.<sup>87</sup>

Marshall's model is founded on two critical assumptions that also underlie Bork's Consumer Welfare Standard. For Marshall: (1) utility is cardinal (not merely ordinal), and therefore individual utilities can be added;<sup>88</sup> and (2) the marginal utility of money is constant and equal for all individuals, so that a unit of utility can be directly associated with a unit of money.<sup>89</sup>

Marshall assumed that utility could be compared between individuals. In antitrust analysis, individual utilities must be summed among market participants since antitrust is concerned with welfare in markets. However, interpersonal comparability of utility has been a major challenge for welfare economics, a problem that I have addressed elsewhere.<sup>90</sup> In the Appendix to this paper I describe the modern ordinal approach to aggregation of utility and its difficulties.

More fundamental, however, are the problems associated with Marshall's (and Bork's) assumption of an equal and constant marginal utility of money. It is widely acknowledged, and I am unaware of any serious dissenting opinions, that people who lack resources benefit more from additional resources than those with abundant resources.<sup>91</sup> Indeed, there is a growing

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<sup>84</sup> Consumer surplus had been discussed earlier by Jules Dupuit. See R. W. Houghton, "A Note on the Early History of Consumer's Surplus," 25 *ECONOMICA* 49 (1958).

<sup>85</sup> ALFRED MARSHALL, "PRINCIPLES OF ECONOMICS," Macmillan (8<sup>th</sup> ed. 2009) at 103.

<sup>86</sup> Marshall had a single measure of value, willingness to pay. Kaldor and Hicks would later recognize that the measure of value is dual. There is both a willingness to pay, and a willingness to accept. See discussion in Appendix.

<sup>87</sup> See Jacob Viner, "The Utility Concept in Value Theory and its Critics," 33 *J. POL. ECON.* 369 (1925).

<sup>88</sup> Gregory Werden, "Antitrust's Rule of Reason: Only Competition Matters," (DOJ Working Paper 2013) at 2 ("To formalize such ideas, economists struggled in vain to sum utilities of all individuals in the economy [without cardinal utility]. Economists then turned to the concept of Pareto optimality.").

<sup>89</sup> Marshall was a partial equilibrium theorist, meaning that he chose to analyze markets one at a time, a principle compatible with antitrust analysis. Yoon-Ho Alex Lee, "Competition, Consumer Welfare, and the Social Cost of Monopoly," (Yale Law School Working Paper 2006) at 7 ("An economic analysis which focuses on the social surplus of one sector without considering possible implications for other sectors is called partial equilibrium analysis.").

<sup>90</sup> Mark Glick, "The Unsound Theory Behind the Consumer (and Total) Welfare Goal in Antitrust," 63 *ANTITRUST BULL.* 455, 462-463 (2018) (collecting citations to the literature addressing this issue).

<sup>91</sup> Joe Farrell & Michael Katz, "The Economics of Welfare Standards in Antitrust," (Univ. of Cal. Berkeley Working Paper 2006) at 9 ("It is however, a widely held view that a dollar is worth more to society in the hands of a poor

confirmatory empirical literature on this point. Some of this evidence shows that, above a certain initial level of income that brings one out of poverty, additional income brings little increase in utility. For example, Robert Frank summarizes the evidence as follows:

One clear message of this evidence [on happiness and additional income] is that beyond some point across the board increases in spending on many types of material goods do not produce any lasting increment in subjective well-being.<sup>92</sup>

According to Richard Layard, “[t]he fact [is] that, despite massive increases in purchasing power, people in the West are no happier than they were fifty years ago.”<sup>93</sup>

Acceptance of the false assumption of constant marginal utility of money allows some antitrust pundits and policy makers to simply ignore the welfare effects of transfers from labor to corporations altogether.<sup>94</sup> This is because, under an assumption of constant and equal marginal utility of money, transfers have no welfare impact.<sup>95</sup> Worse still, antitrust economists operating under this false assumption often inexplicably treat cost reductions resulting from labor rent transfers as a potentially procompetitive benefit, by simply ignoring the deleterious effects of such transfers on labor surplus.<sup>96</sup>

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person than those of a rich one.”). For citations to the literature in moral philosophy on this point see WILL KYMLICKA, “CONTEMPORARY POLITICAL PHILOSOPHY: AN INTRODUCTION,” Oxford (2002) at 40-41.

<sup>92</sup>Robert Frank, “*Does Money Buy Happiness*,” in FELICIA HUPPERT, ET AL. EDS, “THE SCIENCE OF WELL-BEING,” (2005) 461-474. Macroeconomic data on income growth and growth in aggregate happiness demonstrates a similar result. See Ruben Hernandez-Murillo & Christopher Martinek, “*The Dismal Science Tackles Happiness Data*,” ST. LOUIS FEDERAL RESERVE (Jan. 2010); Daniel Kahneman et al., “*Would You Be Happier if You Were Richer*,” 312 SCIENCE 1908 (2006) (“Most people believe that they would be happier if they were richer, but survey evidence on subjective well-being is largely inconsistent with that belief. . . . Surveys in many countries conducted over decades indicate that, on average, reported global judgments of life satisfaction or happiness have not changed much over the last four decades, in spite of large increases in real income per capita.”).

<sup>93</sup>Richard Layard, “*Happiness and Public Policy: A Challenge to the Profession*,” 166 ECON. J. 510 (2006).

<sup>94</sup>Joseph Farrell and Michael Katz, “*The Economics of Welfare Standards in Antitrust*,” DEPARTMENT OF ECONOMICS, UNIVERSITY OF CALIFORNIA, BERKELEY (July 20, 2006) at 9 (noting that the Canadian Merger Enforcement Guidelines state that “when a dollar is transferred from a buyer to a seller, it cannot be determined a priori who is more deserving, or in whose hands it has a greater value.” Further noting that “If enforcers do not, or cannot, undertake a case-by-case determination of relative deservingness, then it may be best simply to assume that all affected parties are equally deserving.”).

<sup>95</sup>To take one example, there is a voluminous literature showing that when employees are laid off there can be devastating welfare consequences. Peter Van der Meer, “Happiness, Unemployment and Self-Esteem,” Research Report 16016-HRM&OB, University of Groningen, Research Institute SOM (Systems, Organizations and Management) (“Unemployment has a severe effect on the subjective well-being of people. It has been shown over and over again. An obvious reason for this drop in well-being is of course the loss of income. But that is not the major explanation. . . . The psychic costs of unemployment are much bigger than the loss of income. But worse than that: unemployment has lasting, scarring effects. That is, the long term unemployed remain unhappy even if they find a job again. They feel and stay unhappy.”).

<sup>96</sup>The Federal Trade Commission and Department of Justice, Horizontal Merger Guidelines, (2010) Section 10; Hiba Hafiz, “*Interagency Merger Review in Labor Markets*,” 95 CHI-KENT L. REV. 37, 42 (2020) (“In the merger context, until very recently, enforcement agencies almost exclusively regarded merger’s workforce reductions and other adverse labor market effects on workers as procompetitive efficiencies, in part due to the rise of the Chicago School as the dominant intellectual force behind modern antitrust.”). See also C. Scott Hemphill & Nancy Rose, “*Mergers that Harm Sellers*,” 127 YALE L. J. 2078, 2091 (2018) (arguing that lower wages resulting from a merger that increased firm bargaining power is not an efficiency).

Interestingly, Marshall himself did not believe that the constant marginal utility of money was a realistic assumption. Both Marshall and Pigou recognized that the utility gain resulting from additional income declines as income rises.<sup>97</sup> Indeed, Marshall expressly recognized that a more even distribution of income would increase welfare.<sup>98</sup> Moreover, unlike Judge Bork, Marshall favored government action to help the poor, was concerned that capital had too much bargaining power with labor, that children did not receive adequate education, as well as other progressive social concerns.<sup>99</sup> In stark contrast, many of the Chicago School defenders of the Consumer Welfare Standard erroneously graft libertarian values and assumptions on to the theory, as I now explain.

### C. *The Consumer Welfare Standard Does Not Embody Libertarian Values*

Defenders of the Consumer Welfare Standard often contaminate welfare analysis with conservative or libertarian assumptions. To take one example, consider the following statement from Frank Easterbrook in his famous article “The Limits of Antitrust”:

For a number of reasons, errors on the side of excusing questionable practices are preferable. First, because most forms of cooperation are beneficial, excusing a particular practice about which we are ill informed is unlikely to be harmful.... Second, the economic system corrects monopoly more readily than it corrects judicial errors.... Third, in many cases the costs of monopoly wrongly permitted are small, while the costs of competition wrongly condemned are large....<sup>100</sup>

None of the assumptions made by Easterbrook necessarily follow from the Consumer Welfare Standard, however. Moreover, his assumptions have proven factually false. Coordinated practices are more widespread than Easterbrook claims.<sup>101</sup> The average cartel in the studies reviewed by Levenstein and Suslow survived 3.7 to 10 years.<sup>102</sup> Historically, some cartels endured for more than 50 years.<sup>103</sup> OPEC has survived decades, despite Milton Friedman’s predictions to the contrary. Using a more current example, there is no sign of market forces undermining the monopoly power of the tech platforms, to take another example of many. Finally, the economic effects of market power are dramatic. Thomas Philippon estimates the

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<sup>97</sup> DANIEL HAUSMAN, MICHAEL MCPHERSON, AND DEBRA SATZ, “ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY,” Cambridge (2017) at 114 (“Citing the diminishing marginal utility of income, they [Marshall and Pigou] maintained that, for example, an extra thousand dollars contributes less to the well-being of someone with an income of fifty thousand dollars than to the well-being of someone with an income of ten thousand dollars. Other things being equal, then, a more equal distribution of income increases total welfare.”).

<sup>98</sup> Roy Harrod, “*Scope and Method of Economics*,” 48 ECON. J. 383, 395 (1938) (“Marshall says in the Principles that the marginal utility of two pence is greater in the case of a poorer man than in that of a richer. If such comparisons are allowed, recommendations for a more even distribution of income seem to follow logically.”).

<sup>99</sup> See Theodore Levitt, “*Alfred Marshall: Victorian Relevance for Modern Economics*,” 90 QUARTERLY J. OF ECON. 425 (1976); Robert Cooter and Peter Rappoport, “*Were the Ordinalists Wrong About Welfare Economics?*” 22 J. OF ECON. LIT. 507, 514-515 (1984).

<sup>100</sup> Frank Easterbrook, “*The Limits of Antitrust*,” 63 TEX. L. REV. 1, 15-16 (1984).

<sup>101</sup> Margaret Levenstein & Valerie Suslow, “*What Determines Cartel Success?*” 44 J. OF ECON. LIT. 43 (2006).

<sup>102</sup> *Id.* at 50.

<sup>103</sup> *Id.* at 53.

costs of increased market power in the U.S. economy at about \$1 trillion per year, because of lower investment and lower productivity.<sup>104</sup> In contrast, during the New Deal Consensus period, productivity and investment were higher, despite the stronger antitrust regime.<sup>105</sup> Indeed, the post-Chicago school economists have debunked most of the Chicago School claims about specific antitrust enforcement policy.<sup>106</sup> As Tim Wu has summarized:

The Chicago movement, unsurprisingly, began to encounter major resistance during the 1980s through the 2000s. A group of economists and other academics, styled the “post-Chicago school,” emerged to challenge many of its basic premises. What the post-Chicago academics demonstrated was this. Even if you took a strictly economic view of the antitrust laws, you didn’t actually reach Bork’s conclusions.<sup>107</sup>

Accordingly, in evaluating the Consumer Welfare Standard, it is important to separate the actual theory itself from the ideological baggage of the neoliberals and the Chicago School.<sup>108</sup>

### 1. Free Markets Do Not A Priori Increase Welfare

Neoliberals often claim that the goal of the antitrust laws is to protect free markets, and that the Consumer Welfare Standard is somehow connected to this goal. This is patently false. The term “free markets” is ideological not definitional, because no market is truly free of regulation. Nor are markets analytically “free” prior to government or other social organization. Markets cannot

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<sup>104</sup> THOMAS PHILIPPON, “THE GREAT REVERSAL: HOW AMERICA GAVE UP ON FREE MARKETS,” Harvard U.P. (2019) at 293.

<sup>105</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*,” 64 ANTITRUST BULL. 295 (2019), Appendix 1.

<sup>106</sup> See JOHN KWOKA, “MERGERS, MERGER CONTROL, AND REMEDIES: A RETROSPECTIVE ANALYSIS OF U.S. POLICY,” MIT (2015) at 148-149 (showing the average efficiency gain of the reviewed mergers was “near zero”); Bruce A. Blonigen & Justin Pierce, “*Evidence for the Effects of Mergers on Market Power and Efficiency*,” (NBER Working Paper No. 22750 (2016)) (finding mergers had “little evidence for effects on plant level productivity” or other efficiencies); Steven Salop, “*Economic Analysis of Exclusionary Vertical Conduct: Where Chicago Has Overshot the Mark*,” in “HOW THE CHICAGO SCHOOL OVERSHOT THE MARK: THE EFFECT OF CONSERVATIVE ECONOMIC ANALYSIS ON U.S. ANTITRUST,” Robert Pitofsky ed. Oxford (2008) (demonstrating the potential anticompetitive effects of vertical restraints); John Kwoka and Margaret Slade, “*Second Thoughts on Double Marginalization*,” 34 ANTITRUST 51 (2020) (showing the narrow circumstances under which double marginalization efficiencies occur in vertical mergers); Marina Lao, “*Free Riding: An Overstated, and Unconvincing, Explanation for Resale Price Maintenance*,” in “HOW THE CHICAGO SCHOOL OVERSHOT THE MARK: THE EFFECT OF CONSERVATIVE ECONOMIC ANALYSIS ON U.S. ANTITRUST,” Robert Pitofsky ed. Oxford (2008); Jonathan Baker, “*Predatory Pricing After Brooke Group: An Economic Perspective*,” 62 ANTITRUST L.J. 585 (1994) (arguing that predatory pricing is not always irrational).

<sup>107</sup> TIM WU, “THE CURSE OF BIGNESS: ANTITRUST IN THE NEW GILDED AGE,” 76 Columbia Global Reports (2018) at 76.

<sup>108</sup> Values unrelated to welfare often appear as procompetitive justifications for conduct. Antitrust defendants have offered, and antitrust courts have accepted, numerous justifications for their conduct, whether to avoid the per se rule, or as a defense in a rule of reason case. Such non-welfare-based concepts promoting “amateurism,” increased access to Ivy League colleges, and many others have been advanced. See *O’Bannon v. NCAA*, 802 F.3d 1948 (9<sup>th</sup> Cir. 2015); *United States v. Brown Univ.*, 5 F.3d 658 (3<sup>rd</sup> Cir. 1993). For a collection and categorization of procompetitive justifications see John Newman, “*Procompetitive Justifications in Antitrust Law*,” 94 INDIANA LAW J. 501 (2019).

exist without secure property rights, contract rules, and criminal sanctions.<sup>109</sup> Nor can markets exist without social norms for cooperation.<sup>110</sup> However, these are only the most fundamental of regulatory requirements.<sup>111</sup> The existence of corporations, limited liability, financial markets, credit, currency, unions, work rules, and many other prerequisites of modern markets require detailed legal regimes. As Bernard Harcourt describes:

The fundamental problem is that foundational categories of, on the one hand, “market efficiency” or “free markets” and on the other hand “excessive regulation,” “governmental inefficiency,” or “discipline,” are illusory and misleading categories that fail to capture the irreducible individual phenomena of different forms of market organization. In all markets, the state is present.<sup>112</sup>

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<sup>109</sup> JOSEPH STIGLITZ, “THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE,” Norton (2012) at 57-58 (“The most important role of government, however, is setting the basic rules of the game, through laws such as those that encourage or discourage unionization, corporate governance laws that determine the discretion of management, and competition laws that should limit monopoly rents. As we have already noted, almost every law has distributive consequences, with some groups benefiting, typically at the expense of others. And these distributive consequences are often the most important effects of the policy or program.”); JULES COLEMAN, “RISKS AND WRONGS” Cambridge (1992) at 61 (“Competition presupposes a stable, enforceable scheme of property rights. Any such scheme is a collective or public good.”); Betty Mensch, “*Freedom of Contract as Ideology*,” 33 STAN. L. REV. 753, 772 (1981) (“Every market transaction requires contract enforcement, which must be coercive, to protect expectational interests. Voluntary exchange presupposes a world of collective external contract rules and enforcement.”).

<sup>110</sup> JOSEPH STIGLITZ, “THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE,” Norton (2012) at 121 (“Cooperation and trust are important in every sphere of society. We often underestimate the role of trust in making our economy work or the importance of the social contract that binds us together. If every business contract had to be enforced by one party’s taking the other to court, our economy, and not just our politics, would be in gridlock. The legal system enforces certain aspects of “good behavior,” but most good behavior is voluntary. Our system couldn’t function otherwise. If we littered every time we could get away with it, our streets would be filthy, or we would have to spend an inordinate amount on policing to keep them clean. If individuals cheated on every contract—so long as they could get away with it—life would be unpleasant and economic dealings would be fractious.... Throughout history the economies that have flourished are those where a man’s word is his honor, where a handshake is a deal....”); SAMUEL BOWLES, “THE MORAL ECONOMY: WHY GOOD INCENTIVES ARE NO SUBSTITUTE FOR GOOD CITIZENS,” Yale (2016) at 2-3 (“I show that these and other policies advocated as necessary to the functioning of a market economy may also promote self-interest and undermine the means by which a society sustains a robust civic culture of cooperative and generous citizens. They may even compromise the social norms essential to the workings of markets themselves. Included among the cultural casualties of this so-called crowding-out process are such workaday virtues as truthfully reporting one’s assets and liabilities when seeking a loan, keeping one’s word, and working hard even when nobody is looking. Markets and other economic institutions do not work well where these and other norms are absent or compromised.”); FRED BLOCK, “CAPITALISM: THE FUTURE OF AN ILLUSION,” Univ. of Cal. (2018) at 89, 91 (“This dependence of the market system on the rejection of unbridled greed and selfishness has been understood by social theorists back to Adam Smith.... Smith’s recognition that a market economy depends on anti-market values was replicated by such key sociological thinkers as Emile Durkheim and Marx Weber.”).

<sup>111</sup> JACOB HACKER & PAUL PIERSON, “WINNER-TAKE-ALL POLITICS: HOW WASHINGTON MADE THE RICH RICHER AND TURNED ITS BACK ON THE MIDDLE CLASS,” Simon & Schuster (2010) at 55 (“The intertwining of government and markets is nothing new. The frontier was settled because government granted land to the pioneers, killed, drove off, or rounded up Native Americans, created private monopolies to forge a nationwide transportation and industrial network, and linked the land settled with the world’s largest postal system.”).

<sup>112</sup> BERNARD HARCOURT, “THE ILLUSION OF FREE MARKETS,” Harvard (2011) at 47.



Thus, there are not “free markets” and “non free markets.” There are many diverse market organizations depending on how the law and governmental regulatory structures shape these markets. Welfare economics does not advocate *a priori* any particular market organization. Instead, it advocates regulations that improve and ultimately maximize human well-being.

## 2. There is No Road to Serfdom

Welfare economics, likewise, provides no support for the libertarian arguments advanced by Friedrich Hayek in the Road to Serfdom, or in Milton Friedman’s influential book, Capitalism and Freedom.<sup>113</sup> The central point Hayek posits is that increased government involvement in the economy undermines economic prosperity, political liberty, and freedom. Reading Hayek today, one is struck by how any government regulation, including the New Deal, is lumped together with Nazi Germany and Soviet Russia. Keynes, for example, commented to Hayek that:

I should guess that according to my ideas you greatly underestimate the practicability of the middle course. But as soon as you admit that the extreme is not possible, and that a line has to be drawn, you are, on your own argument, done for, since you are trying to persuade us that so soon as one moves an inch in the planned direction you are necessarily launched on the slippery path which will lead you in due course over the precipice.<sup>114</sup>

Hayek famously argued that any interference with a pure laissez-faire economy would thwart the ability of prices to relay the necessary information for the economy to naturally equilibrate.<sup>115</sup> Unfortunately, Hayek offered no theoretical or empirical justification for this argument. And later microeconomists have demonstrated that if the equilibrium is disturbed, market price signals do not guarantee a return to equilibrium and markets under laissez-faire regimes are not stable in any event.<sup>116</sup> Hayek’s famous argument for unregulated markets was pure conjecture.

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<sup>113</sup> F. A. HAYEK, “THE ROAD TO SERFDOM,” Univ. of Chi. (1944); MILTON FRIEDMAN, “CAPITALISM AND FREEDOM,” Univ. of Chi. (1962).

<sup>114</sup> Quoted in RICK TILMAN, “IDEOLOGY AND UTOPIA IN THE SOCIAL PHILOSOPHY OF THE LIBERTARIAN ECONOMISTS,” Greenwood (2001) at 33.

<sup>115</sup> FRED BLOCK, “CAPITALISM: THE FUTURE OF AN ILLUSION,” Univ. of Cal. (2018) at 87 (“Friedman and his allies consistently exaggerate the effectiveness of markets as information processing machines. The reality is that in most market situations, consumers lack key pieces of information for rational decision making. For example, most people don’t know whether the car actually needs a new muffler or a new transmission when they take it to the mechanic. When they buy a pint of strawberries, they don’t know if the ones on the bottom have already gotten moldy. Even in economic theory, price signals will not optimize the use of resources when consumers are being misled about what they are getting for their dollars. This is precisely why in building economic models, economists frequently posit perfect information.”).

<sup>116</sup> S. Bowles, A. Kirman, and R. Sethi, “Friedrich Hayek and the Market Algorithm,” 31 J. OF ECON. PERSP. 215, 230 (2017) (demonstrating no general proof of stability of competitive equilibrium); Michael Mandler, “Sraffian Indeterminacy in General Equilibrium,” 66 REV. ECON. STU. 693, 711 (1999). The literature on this topic is reviewed in Frank Ackerman, “Still Dead After All These Years: Interpreting the Failure of General Equilibrium,” 9 J. ECON METH. 119 (2002).

Both Hayek and Friedman contended that political liberties are undermined by the growth of the government. In retrospect, this also appears to be empirically false. During the New Deal Consensus and the Great Society programs, periods of government growth, the United States passed the Civil Rights Act of 1964, the Voting Rights Act of 1965, the right to vote was lowered from 21 to 18, and the Supreme Court recognized the right to counsel (*Gideon v. Wainwright*, 1963), rights to privacy (*Griswold v. Connecticut*, 1965; *Roe v. Wade*, 1973), and reaffirmed freedom of the press (*N.Y. v. Sullivan*, 1964).<sup>117</sup> These cases expanded citizen rights and liberties, not reduced them. Friedman contrasts the “freedom” of the market economy, where transactions are voluntary, with the “coercion” of government and law.<sup>118</sup> This description is deeply flawed, however. Indeed, it is questionable whether private sector relationships are truly voluntary.<sup>119</sup> Second, coercion also exists in the private sector.<sup>120</sup> Most private production occurs within firms. Employees in large private sector firms work under a system of command and control, supported by substantial coercion.<sup>121</sup> In 2012, for example, “there were 1,906 business enterprises with 5,000 or more employees in the United States averaging 20,366 employees.”<sup>122</sup> These businesses accounted for 34 percent of all business

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<sup>117</sup> RICK TILMAN, “IDEOLOGY AND UTOPIA IN THE SOCIAL PHILOSOPHY OF THE LIBERTARIAN ECONOMISTS,” Greenwood (2001) at 30. (“Hayek and Friedman claim there is a demonstrable causal relation between market freedom and political freedom. It appears, instead, that within as yet undetermined limits, there are many market structures that are quite compatible with political freedom as it exists in the nations of the Atlantic Community and English speaking nations of the Commonwealth.”)

<sup>118</sup> Voluntary transactions do not necessarily increase economic welfare. People could, theoretically, voluntarily accept a life of hardship and unrelenting poverty rather than a worse alternative, while a few lead lives of wealth. Such circumstances, however, are extremely unlikely to maximize human well-being, even if it meets Friedman’s definition of free and voluntary transactions.

<sup>119</sup> JONATHAN WOLFF, “ROBERT NOZICK: PROPERTY, JUSTICE AND THE MINIMAL STATE,” Stanford (1991) at 27-33. A similar debate concerns when unemployment is “voluntary.” Robert Lucas states that “there is always a voluntary element in all unemployment, in the sense that however miserable one’s current work options, one can always choose to accept them,” quoted in DANIEL HAUSMAN, MICHAEL MCPHERSON AND DEBRA SATZ, “ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY,” Cambridge (2017) at 41. Indeed, taxation of property is also voluntary under this logic since the rich could accept jail time rather than pay taxes.

<sup>120</sup> Barbara Ehrenreich, “*Earth to Wal-Mars*,” in JAMES LARDNER AND DAVID SMITH, “INEQUALITY MATTERS: THE GROWING ECONOMIC DIVIDE IN AMERICA AND ITS POISONOUS CONSEQUENCES,” Demos (2005) at 45 (“While it is perfectly legal for an employer to ban employee conversation or assembly, it is also legal to require employees to attend antiunion lectures, where they may be warned that a prounion vote is likely to lead to a company decision to shut down the facility.”); BENJAMIN PAGE & MARTIN GILENS, “DEMOCRACY IN AMERICA?” Chicago (2020) at 133-134 (“[B]ut labor’s decline has been exacerbated by fierce employer offensives and by deliberately antiunion public policies. Business leaders have fired union organizers and obstructed votes to unionize.”).

<sup>121</sup> WILLIAM LAZONICK, “SUSTAINABLE PROSPERITY IN THE NEW ECONOMY? BUSINESS ORGANIZATION AND HIGH-TECH EMPLOYMENT IN THE UNITED STATES,” Upjohn (2009) at 200 (“In all of the richest economies, business corporations are repositories of large, and in many cases vast, quantities of resources over which corporate managers, rather than markets, exercise allocative control. Indeed, it can be argued that corporate control, as distinct from market control, of resource allocation represented the defining institutional characteristic of twentieth-century capitalist economies.”). Moreover, “it is impossible to explain U.S. dominance in computers, microelectronics, software, and data communications without recognizing the role of government in making seminal investments that developed new knowledge and infrastructural investments that facilitated the diffusion of that knowledge....” *Id.* at 211-212.

<sup>122</sup> WILLIAM LAZONICK AND JANG-SUP SHIN, “PREDATORY VALUE EXTRACTION: HOW THE LOOTING OF THE BUSINESS CORPORATION BECAME THE U.S. NORM AND HOW SUSTAINABLE PROSPERITY CAN BE RESTORED,” Oxford (2020) at 3.

employees.<sup>123</sup> Moreover, the private sector benefits immensely from the support of the government.<sup>124</sup> The U.S. government accounts for 57 percent of basic research, and has infused massive amounts of investment to develop the internet, agriculture, drug development, biotech, communications, and other critical areas.<sup>125</sup> Indeed, dominant firms in the United States do not consistently advocate for “less government”; rather, they seek a regulatory scheme that favors them at the expense of others, including labor organizations and environmental groups, for example. Earlier in this century, Louis Brandeis, persuasively argued in stark contrast to Friedman, that it was the existence of large centers of private power, not government intervention, that threatened the existence of a politically free people.<sup>126</sup>

#### *D. Judge Bork’s Rendition of the Consumer Welfare Standard*

I now turn a critical eye towards Judge Bork’s particular application of the Consumer Welfare Standard. In Chapter 4 of the Antitrust Paradox, Judge Bork introduced Marshall’s consumers’ surplus model with none of the understanding one would obtain from reading Marshall himself. Instead, Bork introduces consumer welfare using a standard economics 101 graph of demand and price in a perfectly competitive market:

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<sup>123</sup> *Id.*

<sup>124</sup> MARIANA MAZZUCATO, “THE ENTREPRENEURIAL STATE: DEBUNKING PUBLIC VS. PRIVATE SECTOR MYTHS,” Anthem (2013) at 60 (American business accounted for 67% of total R&D expenditures in 2008).

<sup>125</sup> *Id.* at Ch. 4; WILLIAM LAZONICK AND JANG-SUP SHIN, “PREDATORY VALUE EXTRACTION: HOW THE LOOTING OF THE BUSINESS CORPORATION BECAME THE U.S. NORM AND HOW SUSTAINABLE PROSPERITY CAN BE RESTORED,” Oxford (2020) at 33-38; WILLIAM LAZONICK, “SUSTAINABLE PROSPERITY IN THE NEW ECONOMY? BUSINESS ORGANIZATION AND HIGH-TECH EMPLOYMENT IN THE UNITED STATES,” Upjohn (2009) at 211-212 (“it is impossible to explain U.S. dominance in computers, microelectronics, software, and data communications without recognizing the role of government in making seminal investments that developed new knowledge and infrastructural investments that facilitated the diffusion of that knowledge”); *See also* FRED BLOCK & MATTHEW KELLER, “STATE OF INNOVATION: THE U.S. GOVERNMENT’S ROLE IN TECHNOLOGY DEVELOPMENT,” Routledge (2016); STEVEN JOHNSON, “WHERE GOOD IDEAS COME FROM: THE NATURAL HISTORY OF INNOVATION,” Riverhead (2010) (showing most of the major inventions arose from non-market decentralized organizations).

<sup>126</sup> JACOB HACKER & PAUL PIERSON, “WINNER-TAKE-ALL POLITICS: HOW WASHINGTON MADE THE RICH RICHER AND TURNED ITS BACK ON THE MIDDLE CLASS,” Simon & Schuster (2010) at 81 (“Brandeis’ argument gained power from an early twentieth-century school of thought known as legal realism. Legal realism challenged the common notion, frequently invoked by those advantaged by the economy, that the structure of the market and the division of its gains was a natural phenomenon, completely separate from politics and government, the result of free choice and unfettered competition that yielded a distribution of property based on merit and hard work. The legal realists countered that property and markets were instead deeply intertwined with politics and government. There are no pre-political markets. Markets are inevitably shaped and channeled by political forces, dependent on the rules that are created and enforced by those who control the coercive power of the state.”).

### A Competitive Market

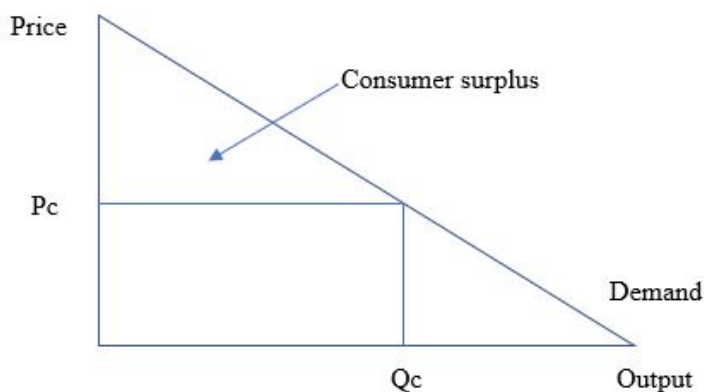


Figure 1: Consumer's Surplus in Perfect Competition

In Marshall's approach, the demand curve represents the amounts that consumers are willing to pay for associated units of output. The willingness to pay represents the dollar amount of utility consumers receive from the purchase. If Judge Bork had been familiar with the broader concepts of welfare economics when he authored his book in the 1970s, he would have been forced to acknowledge that there are two measures of value, not one. There is a measure of willingness to pay, and there is a measure of willingness to accept. These two measures are materially different. The area under the demand curve represents willingness to pay, but only under specific assumptions, *i.e.*, when there are no wealth effects.<sup>127</sup> Willingness to pay is assumed to represent the utility a consumer obtains from consuming each unit of the product in Marshall's model regardless of the wealth of the consumer. While Marshall made this assumption explicit in the Principles and raised doubts about its general applicability, Bork was either unaware of the assumption or was less than transparent about making it. Under these assumptions, the consumers receive utility as read off of the demand curve, but only have to pay the uniform competitive price,  $P_c$ . Thus, the consumer increases his/her utility by the amount of the consumer's surplus equal to the difference between the demand curve and the uniform competitive price.<sup>128</sup>

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<sup>127</sup> If a consumer purchases multiple units of a product, the assumption is made that after each purchase the consumer's income is restored to the amount prior to the first purchase.

<sup>128</sup> Even under this assumption, however, it is not clear that consumers' surplus results in greater welfare. For example, suppose the product at issue is cigarettes. Greater consumption of cigarettes due to lower cigarette prices will not likely result in greater human well-being. This point is made by Barak Orbach, who distinguishes between surplus and welfare. Barak Orbach, "The Antitrust Consumer Welfare Paradox," 7 J. COMP. L. ECON. 133 (2010).

In Chapter 5 of his book, Judge Bork builds on the consumer’s surplus analysis by introducing Oliver Williamson’s model of welfare tradeoffs following a merger.<sup>129</sup> Superimposing a monopolized market on top of the graph of a competitive market renders the following:

In Figure 2, the monopolist maximizes profits by reducing output below the competitive level and raising price above the competitive level. This is because the monopolist realizes that

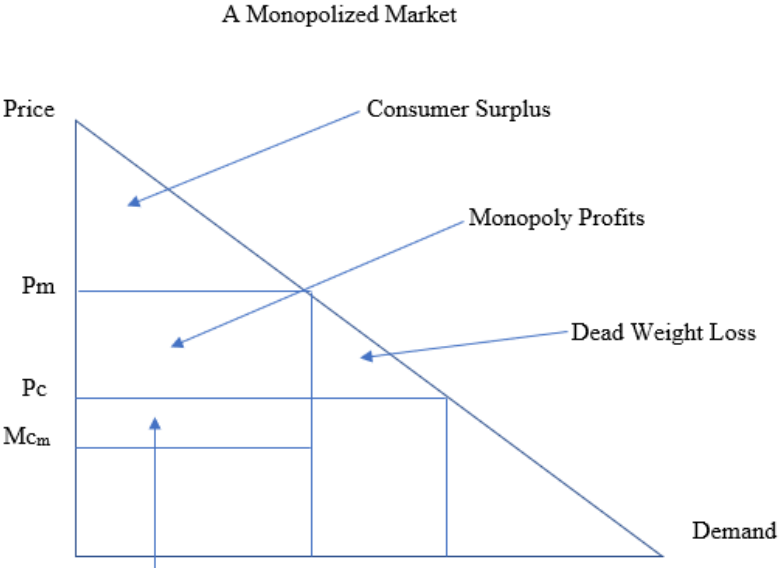


Figure 2: Judge Bork's welfare tradeoffs from mergers

increasing Q can only be sustained by decreasing price. To clear the market at a lower Q, requires a higher price. When a market is monopolized, Pm is above Pc, the competitive price. Qm, the monopolist’s output, is below the competitive output, Q. In practice, when the monopolist raises the price, some consumers switch to a substitute product (perhaps margarine for butter, for example), this results in a lower Q. The firm’s reduction in output creates a “deadweight loss.” The area below the demand curve between Qm and Qc is called deadweight loss because consumers are willing to pay a price higher than the marginal cost of producing these units of the product (Pc = marginal cost), yet these units of the product are not produced. We can call this an allocative inefficiency to the extent that the demand curve measures the utility consumers gain from purchasing the product. The consumers who do not switch away at the higher price pay more, and this increases the profits of the monopolist. This is represented by the square with area (Qm-Qc)Qm. This area also represents a redistribution of income from purchasers to the monopolist. Even under this scenario, however, there is still some consumers’

<sup>129</sup> Oliver Williamson, “Economies as an Antitrust Defense: The Welfare Tradeoffs,” 58 AMER. ECON. REV. 18 (1968).

surplus enjoyed by the non-switching consumers. This is represented by the area under the demand curve up to  $Q_m$ .

Finally, if the merger to monopoly leads to reduced variable costs, as reflected in this example, then there is a resulting efficiency—the reduction from  $P_c$  to  $MC_m$ .<sup>130</sup> Bork’s discussion of this aspect of the model shows that he was actually applying a total welfare approach, not a consumer welfare approach. In a full model of the monopolist’s pricing decision, some of the monopolist’s cost reduction will be passed through to consumers.<sup>131</sup> The economist’s assumption is that this cost reduction will result in additional investment or lower prices, or both, and that these processes will, in turn, increase utility.<sup>132</sup> But these are only assumptions. As we will later see, if instead of reinvesting these cost savings or reducing prices, businesses use those savings to buy-back their own stock, or increase executive pay, or pay increased dividends to hedge fund managers (as appears to be the recent trend), the result can be a reduction in utility.

Moreover, it is important to determine the welfare effect of the reduction in variable costs resulting from the merger, which involves analyzing the input markets in which these variable costs are generated. As discussed later, reductions in variable costs resulting from lower wages and less employment after a merger (*i.e.*, what some may view as efficiencies resulting from the merger), decreases labor surplus, with just as important of an effect on total welfare as any decrease in consumer surplus. Yet, such negative welfare effects are almost uniformly ignored in practice.

Under the Consumer Welfare Standard, business strategies that reduce consumer welfare in a market, or reduce consumer welfare plus profits (total welfare) in a market, are deemed anticompetitive. Labor surplus is inexplicably not considered. The Department of Justice and the Federal Trade Commission 2010 Horizontal Merger Guidelines (the “Merger Guidelines”) include as goals of merger enforcement (under the Consumer Welfare Standard), prevention of price increases, reductions in product quality or variety, reductions in service, and lower innovation. These are all cognizable under the Consumer Welfare Standard because they reduce consumer surplus. But other equally important, welfare-reducing effects are simply ignored, as we shall now see.

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<sup>130</sup> The Chicago School assumed that mergers led to significant efficiencies of this type. The evidence has not supported this assumption, however. JOHN KWOKA, *MERGERS, MERGER CONTROL, AND REMEDIES: A RETROSPECTIVE ANALYSIS OF U.S. POLICY* 149 (2015) (“Overall, these data corroborate the findings of the single-merger studies regarding product prices, such a decrease is found with respect to price but also with respect to quality, R&D, and more often than not, efficiency.”). Most of the many studies of merger efficiencies find few or no such benefits. See Robert Lande and Sandeep Vaheesan, “*Preventing the Curse of Bigness Through Conglomerate Merger Legislation*,” 52 *ARIZ. ST. L. J.* 75, 84-86 (2020).

<sup>131</sup> Paul Yde and Michael Vita, “*Merger Efficiencies: Reconsidering the ‘Passing-On Requirement’*” 64 *ANTITRUST L.J.* 735 (1996).

<sup>132</sup> For a thorough review of merger efficiencies, see Louis Kaplow, “*Efficiencies in Merger Analysis*,” 83 *ANTITRUST L.J.* 557 (2021).

### III. Missing Aspects of Human Welfare Under the Consumer Welfare Standard

In the hands of the Chicago School, the Consumer Welfare Standard result in critical aspects of human welfare being left by the wayside; most notable, the transfer of rents from labor and welfare-reducing impacts from the erosion of political democracy.

#### A. *The Transfer of Labor Rents to Corporations and Shareholders*

##### 1. The Origin of Labor Rents

Just as consumers receive consumer surplus when their reservation price (what they are willing to pay) is above the market price, workers receive rents when the prevailing wage is above the reservation wage (the minimum wage required for a worker to accept the job).<sup>133</sup> Labor rents occur for a variety of reasons.<sup>134</sup> Unions that increase worker bargaining power can cause a transfer of firm rents to employees.<sup>135</sup> In addition, it may be in the interest of firms to share rents with workers in certain circumstances for efficiency wage reasons.<sup>136</sup> Moreover, fairness often

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<sup>133</sup> Theoretically, the competitive wage is the marginal revenue product of labor. Both Marshall and Pareto criticized this theory because in the real world the contributions of the various inputs into the production process cannot be disentangled. An extensive summary of the problems inherent in the marginal productivity theory can be found in JOHN PULLEN, “THE MARGINAL PRODUCTIVITY THEORY OF DISTRIBUTION, A CRITICAL HISTORY,” Routledge (2010). The Cambridge Controversy, a debate between Paul Samuelson and Joan Robinson, also ultimately questioned the logical consistency of this theory. GEOFFREY HARCOURT, “SOME CAMBRIDGE CONTROVERSIES IN THE THEORY OF CAPITAL,” Cambridge (1972).

<sup>134</sup> Anna Stansbury & Lawrence Summers, “*The Declining Worker Power Hypothesis: An Explanation for the Recent Evaluation of the American Economy*,” 2020 Brookings Papers on Economic Activity at 3 (“Worker power—arising from unionization or the threat of union organizing, from firms being run partly in the interests of workers as stakeholders, or from efficiency wage effects—enables workers to increase their pay above the level that would prevail in the absence of such bargaining power. This power gives workers the ability to receive a share of the rents generated by companies operating in imperfectly competitive product markets and can act as countervailing power to firm monopsony power.”).

<sup>135</sup> Henry S. Farber, Daniel Herbst, Ilyana Kuziemko and Suresh Naidu, “*Unions and Inequality Over the Twentieth Century: New Evidence from Survey Data*,” (NBER Working Paper 24587 (2021)) at 39 (“We show that unions were a major force in the Great Compression, above and beyond what can be accounted for by the direct effect of unions on union members.”); Lawrence Mishel, “*Unions, Inequality and Faltering Middle Class Wages*,” EPI (2012) (The union wage premium was 26.7% in 1973 and 13.6% in 2011.). Unions impact more than wages. See RICHARD FREEMAN AND JAMES MEDOFF, “WHAT DO UNIONS DO,” Basic (1984); Mark Stelzner and Kate Bahn, “*Discrimination and Monopsony Power*,” THE REV. OF BLACK POL. ECON. 1, 7-8 (2021) (“An important dynamic which is missing from all of these models is that workers can act as a countervailing force, through collective action, to stymie employer monopsony power. However, workers’ ability to do so is dependent on institutional support for collective action. When institutional support for unions, strikes, and other forms of collective action does not exist, employers are able to wield monopsony power more freely.”).

<sup>136</sup> Janet Yellen, “*Efficiency Wage Models of Unemployment*,” 74 AM. ECON. REV. 200, 201 (1984) (“In most jobs, workers have some discretion concerning their performance. Rarely can employment contracts specify all aspects of a worker’s performance. Piece rates are often impracticable because monitoring is too costly or too inaccurate. Piece rates may also be nonviable because the measurements on which they are based are unverifiable by workers, creating a moral hazard problem. Under these circumstances, the payment of a wage in excess of market clearing may be an effective way for firms to provide workers with the incentive to work rather than shirk.”).

requires that firms keep the relative pay between employee groups within certain proportions.<sup>137</sup> Finally, labor laws have protected working conditions and benefits.<sup>138</sup>

The Sherman Act applies to agreements that restrain labor markets and adversely impact wages.<sup>139</sup> In principle, plaintiffs should also be able to challenge a single firm that monopsonizes a labor market, but successful cases of this type are very rare or non-existent.<sup>140</sup> Mergers can also increase buyer power in labor markets. Yet the Horizontal Merger Guidelines

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<sup>137</sup> Albert Rees, “*The Role of Fairness in Wage Determination*,” 11 J. OF LABOR ECON. 243, 243-244 (1993) (“The factors involved in setting wages and salaries in the real world seemed to be very different from those specified in the neoclassical theory. The one factor that seemed to be of overwhelming importance in all these real world situations was fairness, and fairness seemed to be judged by making some kind of wage comparison; with another union, with another employer, with another person.”); DAVID WEIL, “THE FISSURED WORKPLACE: WHY WORK BECAME SO BAD FOR SO MANY AND WHAT CAN BE DONE TO IMPROVE IT,” Harvard (2014) at 82-83 (“Fairness perceptions affect all kinds of real-world interactions and relationships. Relationships are an intrinsic part of the workplace, and fairness perceptions are therefore basic to how decisions are made within it.... [F]airness considerations about compensation depend not only on how much I think I deserve to be paid on an absolute basis (given my experience, education, skills), but also on what I am paid relative to others.”). JOSEPH STIGLITZ, “THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE,” Norton (2012) at 104 (“Recent experiments in economics have confirmed the importance of fairness. One experiment showed that raising wages of workers who felt they were being treated unfairly had a substantial effect on productivity—and no effect on those who felt they were being treated fairly.”). See also Gerald Davis and J. Adam Cobb, “*Corporations and Economic Inequality Around the World: The Paradox of Hierarchy*,” Wharton Faculty Research (2010) (Finding that the percent of employment in large firms is negatively related to inequality. The authors may be capturing this fairness effect within firms.)

<sup>138</sup> David Weil discusses how firms avoid legal obligations to protect working conditions and benefits. DAVID WEIL, “THE FISSURED WORKPLACE: WHY WORK BECAME SO BAD FOR SO MANY AND WHAT CAN BE DONE,” Harvard (2014) at 78 (“For example, the federal laws regulating employee benefits require that if a benefit like health care is offered to one worker, it must be offered to all workers. By shifting out employment to another business (such as a temporary agency that does not provide its workforce with health benefits) the company can lower the de facto cost of hiring additional workers.... A third incentive for shedding employment arises from the desire to minimize liability. With employment comes responsibility for outcomes like workplace injuries, illnesses, and fatalities as well as for discrimination, harassment, and unjust dismissal. If shedding employment shifts liabilities to other parties, it lowers expected costs to lead businesses.”).

<sup>139</sup> ROGER BLAIR AND JEFFREY HARRISON, “MONOPSONY IN LAW AND ECONOMICS,” Cambridge (2010) at 30-34; ERIC POSNER, “HOW ANTITRUST FAILED WORKERS,” Oxford (2021) at 45-60; Julian Kleinbrodt and Jacqueline Sesia, “*Antitrust Considerations in Labor Market Enforcement*,” 10 PERSPECTIVES IN ANTITRUST 2 (2022). *In re High Tech Emp. Antitrust Litig.*, 985 F. Supp.2d 1167 (N.D. Cal. 2013) (agreement by Apple, Google, and Intel not to recruit each other’s employees); *No More No-Poach: The Antitrust Division Continues to Investigate and Prosecute “No-Poach” and Wage-Fixing Agreements*,” U.S. Dept. of Justice: Antitrust Division (Spring 2018).

<sup>140</sup> ERIC POSNER, “HOW ANTITRUST FAILED WORKERS,” Oxford (2021) at 63 (“A Westlaw search yielded only two cases in the past year and six cases over the past three years. The results of the Westlaw search probably understates the problem. I have not found a single Section 2 labor monopsony case, ever, in which the claim survived a summary judgment motion.”); ROGER BLAIR AND JEFFREY HARRISON, “MONOPSONY IN LAW AND ECONOMICS,” Cambridge (2010) at 38 (“An issue that has emerged as courts have become more acquainted with monopsony is whether the antitrust laws prohibit a firm with monopsony power from using its power to lower prices. This is an odd question in some respects because it is virtually a given that price setting by a seller to take full advantage of any monopoly power it might have is not a violation of the antitrust laws. Courts considering monopsony pricing and seeing the analogy to monopoly price setting have indicated that the use of buying power to obtain a lower price does not violate the antitrust laws.”).



say nothing about wages, and no mergers have been blocked because they adversely impacted workers.<sup>141</sup>

The absence of a concern for the transfer of labor rents by courts and antitrust agencies is unjustifiable. There are two ways in which the Consumer Welfare Standard bears on antitrust protection of labor. First, under any welfare standard, including the Consumer Welfare Standard, the welfare of all individuals impacted by the conduct at issue must be taken into account. There is simply no justification for considering some welfare effects and ignoring others. When mergers or dominant firm conduct causes transfers of labor rents from the work force to corporations, or their executives or shareholders, it harms welfare. This is because, as a general rule, income is transferred from low-income individuals to high income individuals. The losses at the lower end of the income ladder cause serious harm and reduce utility more than the additions to income the wealthy experience from this transfer. This is particularly true when a merger reduces costs by increasing unemployment.<sup>142</sup> Some courts and commentators (contrary to Judge Bork) equate consumer welfare with only the consumer's welfare or consumer surplus, while the welfare of workers should properly be considered as part of the consumer's welfare.<sup>143</sup> Anticompetitive restraints in any output market inevitably impact a firm's internal operations

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<sup>141</sup> Ioana Marinescu and Herbert Hovenkamp, "*Anticompetitive Mergers in Labor Markets*," (Washington Center for Equitable Growth Working Paper (June 2018)) at 1 ("To the best of our knowledge no court has ever condemned a merger because of its anticompetitive effects in labor markets."); ERIC POSNER, "HOW ANTITRUST FAILED WORKERS," Oxford (2021) at 76 ("And, indeed, the FTC and DOJ have never blocked a merger based on labor market effects. This is a serious mistake, for which there is no justification."); Maurice Stucke, "*Looking at the Monopsony in the Mirror*," 62 EMORY LAW J. 1509, 1512 (2013) ("Despite these concerns, the larger jurisdictions, to date, have challenged few mergers or conduct cases that target monopsony or buyer power."). A collection of recent citations on this topic can be found in Hiba Hafiz, "*Interagency Merger Review in Labor Markets*," 95 CHI-KENT L. REV. 37, 38 n. 1 (2020). The impact of monopsony power on minorities and women, who can be even more vulnerable to wage reductions, is discussed in Mark Stelzner and Kate Bahn, "*Discrimination and Monopsony Power*," THE REV. OF BLACK POL. ECON 1, 9 (2021) ("Because of the socially constructed norm which places more household responsibilities on woman compared to men on average, women are more likely to supply their labor to a smaller geographical area. This gives the firms in that area more monopsony power over their female employees. Likewise, Black and Latino workers are less likely to respond to wage differences between jobs because of the potential monetary shocks that can befall a worker in the job transition process and the dramatically lower average and median household wealth of Black and Latino households compared with White counterparts. This allows firms to more intensely exercise their monopsony power over Black and Latino workers."). Oversight of the Enforcement of the Antitrust Laws: Hearing Before the Antitrust Subcomm. of the S. Comm. on the Judiciary, 115<sup>th</sup> Cong. 31 (2018) (Statement by Joseph Simons), quoted in Aryeh Mellman, "*Measuring the Impact of Mergers on Labor Markets*," 53 COL. J. OR L. AND SOC. PROBS 1 (2019) at 21 n. 97.

<sup>142</sup> Gritta Gehrke, Ernst Maug, Stefan Obernberger and Christoph Schneider, "*Post-Merger Restructuring of the Labor Force*," INSTITUTE OF LABOR ECONOMICS, NO. 14409 (May 2021) Appendix A.1 (Collecting 39 studies of the impact of mergers on employment. Most studies, but not all, find a negative average impact of mergers on employment.). There is also anecdotal evidence that mergers result in significant layoffs in many cases. See Sarah Miller, "*Corporate Mergers Hurt Workers – And Drag Down Job Markets*," WASHINGTON POST (Oct. 21, 2021).

<sup>143</sup> Clayton Masterman, "*The Customer Is Not Always Right: Balancing Worker and Customer Welfare in Antitrust Law*," 65 VANDERBILT LAW REV. 1387, 1400 (2016) ("[A]nticompetitive agreements in a labor market affect both the input and output markets sufficiently that a court must analyze welfare changes in the labor market. The issue is whether employees and employers are 'consumers' such that their welfare counts, or whether they are producers who are to be ignored. Equity requires that employee surplus is part of consumer welfare. Otherwise, the rule of reason provides no protection to employees who are the victims of anticompetitive schemes that decrease prices in the output market. Such a result is absurd as well as inapposite to Supreme Court precedent.").

including its buyer power on the input market. Likewise, a restraint imposed on the input market directly impacts consumers of the firm's output. Any restraint of trade automatically will have effects on inputs and outputs of the firm at issue. On the output side, the protected group is consumers measured by consumer surplus. While, on the input side, the analogous group is workers, with their impact measured by labor rents. Thus, under any proper interpretation on the Consumer Welfare Standard, the impact on consumers and workers should be considered together.<sup>144</sup> Yet, this is not what happens in practice: consumer impacts are considered, while worker impacts are ignored.

## 2. Methods by Which Labor Rents are Transferred

Anna Stansbury and Larry Summers show how labor rents have materially declined over the last few decades:

Over recent decades however, a number of forces likely reduced labor rents in the United States, particularly for lower-wage workers. Most obvious have been the decline in unionization and union bargaining power and the erosion of the real value of the minimum wage. In addition, the increase in shareholder activism and the rise of the shareholder value maximization doctrine increased the power of shareholders relative to managers and workers, likely increasing pressure on firms to cut labor costs, and in particular, to redistribute rents from workers to shareholders. The increased fissuring of the workplace, with outsourcing of noncore business functions, may be an outgrowth of this phenomenon.<sup>145</sup>

Stansbury and Summers estimate that labor rents have declined “from 12 percent of net value added in the nonfinancial corporate business sector in the early 1980s to 6 percent in the 2010s.”<sup>146</sup> The main contributing factors to this decline are the inability of workers to achieve wage premia in industries with product market concentration, the decline of unions, and the increased bargaining power of large firms.<sup>147</sup> Mergers and dominant firm conduct can exacerbate all three of these processes.

David Weil documents how labor rents have been eliminated by many firms through a process called fissuring, by which firms outsource labor activities such as janitorial, logistics, IT,

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<sup>144</sup> Moreover, this analysis is not impacted by the judicial market specificity rule. When, for example, the Supreme Court stated in *Topco* emphasized its “inability to weigh, in any meaningful sense, destruction of competition in one sector of the economy against promotion of competition in another sector” it could not have been referred to the dual effects of a restraint on a firm's output prices and its input prices which are inextricable intertwined. *United States v. Topco Assocs.*, 405 U.S. 596, 609 (1972). Rebecca Allensworth demonstrates convincingly how antitrust courts routinely deal with tradeoffs between consumer groups impacted by a restraint. Rebecca Allensworth, “*The Commensurability Myth in Antitrust*,” 69 *VANDERBILT LAW REV.* 1 (2016). On cross market balancing generally, see Daniel Crane, “*Balancing Effects Across Markets*,” 80 *ANTITRUST LAW J.* 391 (2015).

<sup>145</sup> Anna Stansbury & Lawrence Summers, “*The Declining Worker Power Hypothesis: An Explanation for the Recent Evolution of the American Economy*,” 2020 *Brookings Papers on Economic Activity* at 10.

<sup>146</sup> *Id.* at 5.

<sup>147</sup> *Id.* at 23.

manufacturing, accounting, H.R., and other jobs to smaller, less stable firms. By so doing, large corporations can reduce their internal wages and avoid other labor related costs such as benefits and legal liability. As Weil describes:

By shifting employment to smaller organizations external to the enterprise that operates in competitive markets, the lead firm creates a mechanism whereby workers will receive a wage close to the additional value they create. At the same time, this avoids the problem of having workers with very different wages operating under one roof. The lead firm captures the difference between the individual additional productivity of each worker and what would be the prevailing single wage rate if it set one.<sup>148</sup>

As labor rents are being decimated, hedge funds and wealthy shareholders are gaining control of boards and siphoning cash through high dividends and share buyback programs.<sup>149</sup> This trend results from several factors, including SEC rule changes and shareholder activism by hedge firms, and the emergence of the ideology of maximizing shareholder value.<sup>150</sup> In addition, executive compensation that is tied to company stock through performance or derivatives aligns executive incentives with shareholder interests to the exclusion of worker interests, productivity growth, or firm health in general.<sup>151</sup> As a result, firms have increased the cash paid out to shareholders in the form of dividends and have significantly increased their stock buybacks in order to keep their share prices high.

These practices have dramatic, adverse consequences on economic performance and worker welfare as we shall now see.

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<sup>148</sup> DAVID WEIL, “THE FISSURED WORKPLACE: WHY WORK BECAME SO BAD FOR SO MANY AND WHAT CAN BE DONE,” Harvard (2014) at 88.

<sup>149</sup> NEIL FLIGSTEIN AND TAKE-JIN SHIN, “THE SHAREHOLDER VALUE SOCIETY: A REVIEW OF THE CHANGES IN WORKING CONDITIONS AND INEQUALITY IN THE UNITED STATES, 1976 TO 2000,” in KATHRYN NECKERMAN ed., “SOCIAL INEQUALITY,” Russell Sage (2004) at 402-403 (“During the 1980s changes in the market for corporate control promoted ‘shareholder value’ over stakeholder rights. It was thought that management was not focused enough on profits and too focused on growth and size. With this change in perspective, management culture began to view employees not so much as partners as costs to be minimized. Plants were closed, some economic activities were moved offshore, others were outsourced to lower cost operations.... The beneficiaries of the ‘shareholder value’ solution to the economic crisis of the 1970s were shareholders and the managers and professionals who controlled the restructuring of firms.”).

<sup>150</sup> Jang-Sup Shin, “*The Subversion of Shareholder Democracy and Rise of Hedge Fund Activism*,” (INET Working Paper No. 77 (2018)) (explaining how SEC rule changes have led to greater shareholder power and cash extraction from firms).

<sup>151</sup> Harvard Law Forum on Corporate Governance (April 16, 2019) (“In fiscal year pay 2018, stock based compensation comprises the majority of CEO pay at S&P 500 and S&P 400 companies for the first time.”); WILLIAM LAZONICK & JANG-SUP SHIN, “PREDATORY VALUE EXTRACTION: HOW THE LOOTING OF THE BUSINESS CORPORATION BECAME THE U.S. NORM AND HOW SUSTAINABLE PROSPERITY CAN BE RESTORED,” Oxford (2020) at 70 (“Also since the 1980s, the most important components of senior executives’ total compensation have been modes of stock based pay in the form of stock options and stock awards. This stock-based pay is structured to incentivize executives to make corporate allocation decisions that will boost the stock prices of the companies that employ them and reward them for achieving this objective.”).

### 3. Transferring Labor Rents Reduces Investment, Innovation, and Productivity

Transferring labor rents to shareholders, corporate executives, and hedge fund managers reduces firm investment, including investment in retaining employees with deep human capital as well as in-house research and technological innovation. This process supplants the prior firm “retain and reinvest” regime that was so successful in the United States up until the 1980s, with a “downsize and distribute” approach through which short run cash is extracted from the firm to increase executive and shareholder incomes, as described by Lazonick and Shin:

Under the retain-and reinvest regime, senior executives made corporate resource-allocation decisions that, by retaining people and profits within the company, permitted reinvestment in productive capabilities that could generate competitive (high-quality, low-cost) products. The social foundation of retain and reinvest was employment relations that offered decades long job security, in-house promotion opportunities, rising real earnings, and health insurance coverage, with a defined benefit pension at the end of a long career.... In sharp contrast, under downsize and distribute a company is prone to downsize its labor force and to distribute to shareholders, in the form of cash dividends and stock buybacks, corporate cash that it might previously have retained.<sup>152</sup>

The impact of this transfer of labor rents to shareholders can be seen in U.S. investment data. There has been a steady decline in the proportion of profits dedicated to investment since the 1990s.<sup>153</sup> As Thomas Philippon describes:

In recent years firms have been plowing back into investment only a bit more than 10 cents for each dollar of profit.... [W]e see that the growth rate of the capital stock of corporate businesses was 3.7 percent on average between 1962 and 2001, but only 1.9 percent on average between 2002 and 2012.<sup>154</sup>

Philippon directly attributes the low investment rate in the U.S. to the rise of market power among large corporations.<sup>155</sup> Others, such as Dumenil and Levy, attribute the low investment to the drain of corporate internal cash to dividends and share buybacks.<sup>156</sup>

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<sup>152</sup> WILLIAM LAZONICK & JANG-SUP SHIN, “PREDATORY VALUE EXTRACTION: HOW THE LOOTING OF THE BUSINESS CORPORATION BECAME THE U.S. NORM AND HOW SUSTAINABLE PROSPERITY CAN BE RESTORED,” Oxford (2020) at 3.

<sup>153</sup> G. Gutierrez & T. Philippon, “*Declining Competition and Investment in the U.S.*,” (NBER Working Paper No. 23583 (2017)).

<sup>154</sup> THOMAS PHILIPPON, “THE GREAT REVERSAL: HOW AMERICA GAVE UP ON FREE MARKETS,” Harvard (2019) at 65.

<sup>155</sup> *Id.* at 70-71.

<sup>156</sup> GERARD DUMENIL & DOMINIQUE LEVY, “THE CRISIS OF NEOLIBERALISM,” Harvard (2011) at 152 (contending that high cash payouts to shareholders have reduced funds for investment); Jonathan Lewellen & Katharina Lewellen, “*Investment and Cash Flow: New Evidence*,” 51 J. FIN. & QANT. ANALYSIS 1135, 1161 (“Our results suggest that investment and cash flow are strongly linked after controlling for a firm’s investment

In any event, low investment should be a major antitrust concern because it means a reduction in spending on product improvements, innovations, and other standard antitrust goals.<sup>157</sup> Yet, all of these concerns are simply swept under the rug by the Consumer Welfare Standard as dollars in shareholder, hedge fund manager, and corporate executive pockets are given equal weight to those paid out to employees or reinvested in improvements to technology and productivity.

Historical evidence establishes the benefits of eliminating or reducing the transfer of labor rents to corporations. Periods of ascendancy of worker rights correlate with increased growth and productivity.<sup>158</sup> A comparison of the period 1947 to 1973 at the height of the welfare state, with the period of neoliberalism and free market ideology, 1980 to 2015, reveals a deterioration of economic performance across numerous metrics during the neoliberal period:

| Year                      | Real GDP Growth Rate | Profit Rate | Labor Productivity Growth Rate | Real Wage Growth Rate | Unemployment Rate | Investment Growth Rate | Top 1% Share of Income |
|---------------------------|----------------------|-------------|--------------------------------|-----------------------|-------------------|------------------------|------------------------|
| Golden Age (1947-1973)    | 3.88                 | 19.95       | 2.36                           | 2.28                  | 4.77              | 8.95                   | 10.61                  |
| Neoliberalism (1980-2015) | 2.51                 | 16.86       | 1.18                           | 1.12                  | 6.42              | 5.25                   | 17.01                  |

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opportunities....”). See also Laurent Cordonnier & Franck Van de Velde, “*The Demands of Finance and the Glass Ceiling of Profit Without Investment*,” 39 *CAMB. J. OF ECON.* 871 (2014).

<sup>157</sup> There is also a direct adverse impact on innovation from inequality. See H.J. HABAKKUK, “AMERICAN AND BRITISH TECHNOLOGY IN THE NINETEENTH CENTURY: SEARCH FOR LABOR SAVING INVENTIONS,” Cambridge (1962); ROBERT ALLEN, “GLOBAL ECONOMIC HISTORY: A VERY SHORT INTRODUCTION,” Oxford (2011) at 33; Gerard Dumenil & Dominique Levy, “*A Stochastic Model of Technical Change, Applications to the U.S. Economy (1869-1985)*,” 46 *METROECONOMICA* 213 (1995); ROBERT GORDON, “THE RISE AND FALL OF AMERICAN GROWTH: THE U.S. STANDARD OF LIVING SINCE THE CIVIL WAR” cite (2016) at 563; Lance Taylor & Oxlem Omer, “*Race to the Bottom: Low Productivity, Market Power, and Lagging Wages*,” (INET Working Paper, Aug. 8, 2018) at 5.

<sup>158</sup> See JOSEPH STIGLITZ, “THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE,” Norton (2012) at 107 (“The large gaps between private rewards and social returns that characterize a rent-seeking economy mean that incentives that individuals face often misdirect their actions, and that those who receive high rewards are not necessarily those who have made the largest contributions. In those instances where private rewards of those at the top exceed by a considerable amount their marginal social contribution, redistribution could both reduce inequality and increase efficiency.”); JAMES GALBRAITH, “INEQUALITY: WHAT EVERYONE NEEDS TO KNOW,” Oxford (2016) at 124 (“...greater equality is associated with stronger growth, mainly because a more egalitarian society creates stronger incentives to develop education, training, and job skills...and indeed if one looks at a selection of Asian countries in the 1990s, it does appear that the more egalitarian ones had stronger rates of growth”); Fred Block, “*The Ruling Class Does Not Rule: Notes on the Marxist Theory of the State*,” in THOMAS FERGUSON AND JOEL ROGERS, “THE POLITICAL ECONOMY: READINGS IN THE POLITICS AND ECONOMICS OF AMERICAN PUBLIC POLICY,” Sharpe (1984) at 41 (“When workers are able to win wage gains, they increase the pressure on the capitalist to find ways to substitute machines for people.”) There is also a robust economic literature on inequality and growth, possibly beginning with Simon Kuznets, “*Economic Growth and Income Inequality*” 45 *AM. ECON. REV.* 1 (1955). Studies differ by time period, countries, data sets, econometric approaches and control variable. Most, but not all, such studies, however, show a negative impact of inequality on growth. A recent literature review can be found in Francesco Grigoli, Evelio Paredes, and Gabriel Bella, “*Inequality and Growth: A Heterogeneous Approach*,” (IMF Working Paper WP/16/244 (2016)).

Growth, productivity, investment, and wage growth were all higher under the New Deal Consensus.<sup>159</sup> This pattern holds not only in the United States, but also in Europe.<sup>160</sup> One explanation for waning economic performance when income inequality worsens is that firm motivation for innovation is diluted.<sup>161</sup>

#### 4. Transferring Labor Rents Leads to Greater Income Inequality

Finally, the cumulative effects of transfers between labor and wealthy shareholders results in greater income inequality and concomitant reductions in well-being. Richard Wilkinson and Kate Pickett document how high levels of income inequality undermine human well-being through numerous social mechanisms. Income inequality creates social barriers, undermines common understanding and discourse, undermines the sense of community, and creates status anxiety.<sup>162</sup> Communities and friends engender “trust” or “social capital” and make us feel “safe,” which activates the parasympathetic nervous system that reduces the cortisol levels in the blood.<sup>163</sup> Reduced social connections lead to greater anxiety, greater insecurity, and increased feelings of shame (all of which are related to violence). Indeed, Wilkinson and Pickett find a strong statistical relationship between income inequality (across countries and U.S. states) and

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<sup>159</sup> Mark Glick, “*Antitrust and Economic History: The Historic Failure of the Chicago School of Antitrust*,” 64 ANTITRUST BULL. 295, 335 (2019).

<sup>160</sup> SAM BOWLES & HERB GINTIS, “RECASTING EGALITARIANISM: NEW RULES FOR COMMUNITIES, STATES AND MARKETS,” Verso (1998) at 13 (“Thus a better indicator of a positive relationship between egalitarian institutions and policies on the one hand and economic performance on the other is the fact that the advanced capitalist countries, taken as a whole, have grown faster under the aegis of the post-Second World War welfare state than in any other period for which the relevant data exist.”). See also SAMUEL BOWLES, “THE NEW ECONOMICS OF INEQUALITY AND REDISTRIBUTION,” Cambridge (2012) at 20 (“[C]ountries experiencing rapid productivity growth between the 1960s and 1980s, including China, Singapore, Taiwan and South Korea, exhibited a degree of economic equality and a level of state involvement in economic decision-making considerably greater than in the relatively laissez-faire industrialized countries which, in the same period, experienced weak productivity growth and increases in economic inequality.”). On the role of planning in Asian development, see JOE STUDWELL, “HOW ASIA WORKS: SUCCESS AND FAILURE IN THE WORLD’S MOST DYNAMIC REGION,” Grove (2013) (stressing the role of agricultural reform, protectionism, government planning and support for manufacturing, and financial controls on successful development.).

<sup>161</sup> See JAMES GALBRAITH, “INEQUALITY: WHAT EVERYONE NEEDS TO KNOW,” Oxford (2016) at 130-131 (“In the early 1950s two Swedish trade union economists, Rudolf Meidner and Gosta Rehn, formulated a theory of egalitarian wage structures that had been guiding Swedish social democratic policy since the mid-1930s and that would continue to do so for another thirty years...[W]age policy should prohibit the payment of low wages, on the ground that this will force backward firms to upgrade, and will give progressive firms a strong competitive advantage.... It may be argued that this ‘Scandinavian’ or ‘LO’ model played a powerful role in transforming Sweden from a country with roughly average income for Europe, strongly dependent on timber, iron, and other natural resources, into the engineering, aviation, and automotive powerhouse that it eventually became.”). Another explanation is the traditional Keynesian argument that redistribution favoring the rich lowers the average marginal propensity to consume.

<sup>162</sup> RICHARD WILKINSON & KATE PICKETT, “THE SPIRIT LEVEL: WHY GREATER EQUALITY MAKES SOCIETIES STRONGER,” Bloomsbury (2010) at 38-39; Shigehiro Oishi, Selin Kesebir and Ed Diener, “*Income Inequality and Happiness*,” 22 PSCH. SCI. 1095 (2012) (showing that U.S. happiness levels are negatively related to inequality, and suggesting perceived unfairness and lack of trust as the mediating factors).

<sup>163</sup> There are other mechanisms by which inequality increases anxiety. For example, Dirk Krueger and Fabrizio Perri show that inequality increases debt levels. Dirk Krueger and Fabrizio Perri, “*Does Income Inequality Lead to Consumption Inequality? Evidence and Theory*,” (NBER Working Paper 9201 (2002)).

lower trust,<sup>164</sup> increased mental illness,<sup>165</sup> greater illegal drug use,<sup>166</sup> lower life expectancy,<sup>167</sup> greater violence,<sup>168</sup> and lower social mobility.<sup>169</sup> Yet, supporters of the Consumer Welfare Standard, paradoxically purport to place “consumer welfare” front and center in antitrust policy debates while ignoring the obvious welfare-reducing impact of dominant firm conduct on income inequality.<sup>170</sup>

### B. *Welfare Losses from Reduced Political Democracy*

Current application of the Consumer Welfare Standard also ignores the detrimental welfare effects from reduced political democracy. Louis Brandeis argued in the early twentieth century that “we have to make a choice. We may have democracy, or we may have wealth concentrated in the hands of a few, but we can’t have both.”<sup>171</sup>

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<sup>164</sup> RICHARD WILKINSON & KATE PICKETT, “THE SPIRIT LEVEL: WHY GREATER EQUALITY MAKES SOCIETIES STRONGER,” Bloomsbury (2010) at 52-53. *See also* Jan Delhey and Georgi Dragolov, “*Why Inequality Makes Europeans Less Happy: The Role of Distrust, Status Anxiety and Perceived Conflict*,” 30 EUR. SOC. REV. 151 (2013) (finding inequality erodes trust in developed countries causing lower welfare).

<sup>165</sup> RICHARD WILKINSON & KATE PICKETT, “THE SPIRIT LEVEL: WHY GREATER EQUALITY MAKES SOCIETIES STRONGER,” Bloomsbury (2010) at 67. *See* Christine Eibner and William Evans, “*The Income-Health Relationship and the Role of Relative Deprivation*,” in KATHRYN NECKERMAN, “SOCIAL INEQUALITY,” Russell Sage (2004) at 545 (“While there is a strong, positive relationship between individual income and individual health, there is less evidence of a relationship between aggregate income and aggregate health. Several recent papers argue that increases in individual income affect health and well-being not just through increases in absolute material standards but also through a relative deprivation effect.”); Richard Layte, “*The Association Between Income Inequality and Mental Health: Testing Status Anxiety, Social Capital, and Neo-Materialist Explanations*,” 28 EUR. SOC. REV. 498 (“mental health is worse in more unequal European Societies”).

<sup>166</sup> RICHARD WILKINSON & KATE PICKETT, “THE SPIRIT LEVEL: WHY GREATER EQUALITY MAKES SOCIETIES STRONGER,” Bloomsbury (2010) at 71.

<sup>167</sup> *Id.* at 82-83.

<sup>168</sup> *Id.* at 134-35.

<sup>169</sup> *Id.* at 160. *See also* JAMES LARDNER & DAVID SMITH, “INEQUALITY MATTERS: THE GROWING ECONOMIC DIVIDE IN AMERICA AND ITS POISONOUS CONSEQUENCES,” Demos (2005) at 34 (“The sons of fathers from the bottom three-quarters of the socioeconomic scale (defined by income, education, and occupation) were less likely to move up in the 1990s than in the 1960s. By 1998, only 10 percent of sons of fathers in the bottom quarter had moved into the top quarter; in 1973, by comparison, 23 percent of lower-class sons had moved up to the top. The evidence shows that there is today a smaller chance than in the past that someone from a low-income family will move up the income ladder.”); Emily Beller and Michael Hout, “*Intergenerational Social Mobility: The United States in Comparative Perspective*,” 16 FUTURE OF CHILDREN 19 (2006) (reviewing occupational, income and wealth mobility and concluding “that slower economic growth since 1975 and the concentration of that growth among the wealthy have slowed the pace of U.S. social mobility”); Miles Corak, “*Do Poor Children Become Poor Adults? Lessons from a Cross-Country Comparison of Generational Earnings Mobility*,” 13 RESEARCH ON ECON. INEQUALITY 143 (2006) (finding the U.S. has relatively low-income mobility).

<sup>170</sup> For an exception to this all-too-common phenomenon, *see* C. Scott Hemphill & Nancy Rose, “*Mergers that Harm Sellers*,” 127 YALE L. J. 2078, 2091 (2018).

<sup>171</sup> Quoted in JACOB HACKER & PAUL PIERSON, “LET THEM EAT TWEETS: HOW THE RIGHT RULES IN AN AGE OF EXTREME INEQUALITY,” Liveright (2020) at 19. As Paul Krugman put it: “Extreme concentration of income is incompatible with real democracy. Can anyone seriously deny that our political system is being warped by the influence of big money, and that the warping is getting worse as the wealth of a few grows ever larger?,” quoted in JOSEPH STIGLITZ, “THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE,” Norton (2012) at 137.

As detailed in Part I, protection of political democracy has been a traditional antitrust goal since the Congressional debates surrounding passage of the Sherman Act. Yet the Consumer Welfare Standard cannot effectively theoretically underpin this goal. Accordingly, a more general conception of welfare (as I advocate in Part IV below) is required to support the use of competition policy to defend political democracy. But first, one must appreciate why promoting political democracy is such an important economic objective.

### 1. Political Democracy Improves Economic Performance

Judge Bork and the Chicago School were able to jettison traditional antitrust values such as improved income equality and protection of political democracy on the grounds that those values purportedly did not contribute to economic growth (wealth maximization). More recent research defies this premise. For example, in their comprehensive study of why some nations fail, Daron Acemoglu and James Robinson identify inclusive economic and political institutions as the one common element of successful economies:

Central to our theory is the link between inclusive economic and political institutions and prosperity. Inclusive economic institutions that enforce property rights, create a level playing field, and encourage investments in new technologies and skills are more conducive to economic growth than extractive economic institutions.... Inclusive economic institutions are in turn supported by, and support, inclusive political institutions, that is, those that distribute political power widely in a pluralistic manner....<sup>172</sup>

For Acemoglu and Robinson, an inclusive economy is one that is not dominated by a few large firms, and an inclusive political system is one in which political power is similarly dispersed. They argue that inclusive political institutions create successful economies by allowing creative destruction of old technologies and the encouragement of new and better innovations (think replacement of fossil fuels by more efficient climate friendly technologies). Only when dominant firms unduly wield political power, can rent seeking and extraction of value be sustained.<sup>173</sup>

But how is this accomplished? Excessive political influence allows dominant firms to externalize costs. Wages and benefits can be outsourced to smaller firms, and the public can be forced to bear the costs of environmental damage and any necessary social safety protections. Fred Block describes the process as follows:

The more successful firms gradually get larger and larger, either through mergers and acquisitions or simply by driving their competitors out of the marketplace. As their size increases, they see the advantages of locking in profits by finding paths to profits

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<sup>172</sup> DARON ACEMOGLU & JAMES ROBINSON, "WHY NATIONS FAIL: THE ORIGINS OF POWER, PROSPERITY, AND POVERTY," Currency (2012) at 430.

<sup>173</sup> *Id.* at 430-32.



that are protected from any kind of competition and by shifting costs onto others through sweating workers or contributing to environmental degradation. Since their size generates profits and political influence, they have both the incentive and the capacity to get political rulings that support these shortcuts to continuing profitability. Without strong democracy, this degenerative process saps the economy of its dynamism.<sup>174</sup>

Block points out that “oligarchies will have slower rates of economic growth than egalitarian democracies”<sup>175</sup> because, once dominant firms capture political power, they can blunt competitive challenges resulting in “little incentive to invest much in upgrading their production facilities.”<sup>176</sup> As Block describes, “members of the existing elite might occasionally invest in something new, but this still means a much slower rate of change than occurs in more open [political] systems.”<sup>177</sup> Block continues:

[I]t is almost always easier for firms to make profits by shifting costs onto others than by increasing efficiency. Under oligarchy, the dominant firms and families often shift costs onto employees by paying low wages and maintaining dirty and dangerous work conditions, or they shift costs onto the environment through dumping their waste into water, air, or landfills.<sup>178</sup>

Democracy, in contrast, allows the other classes in society (*e.g.*, smaller firms, workers, smaller agricultural interests, emerging firms) to penalize government officials that subsidize dominant firms, aid in large firm rent seeking, and facilitate the imposition of unreasonable costs on the public.<sup>179</sup> But representative democracy is further imperiled by another phenomenon.

## 2. The Destructive Influence of Money in Politics

Mark Hanna, William McKinley’s campaign manager, was famously asked what matters in politics; he answered: “There are two things that matter in politics. The first is money. I can’t remember the second.”<sup>180</sup> Several studies by political scientists have concluded that the rich have already captured almost complete political power.<sup>181</sup> This power is exercised through

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<sup>174</sup> FRED BLOCK, “CAPITALISM: THE FUTURE OF AN ILLUSION,” Univ. of Cal. (2018) at 75.

<sup>175</sup> *Id.* at 70.

<sup>176</sup> *Id.*

<sup>177</sup> *Id.*

<sup>178</sup> *Id.*

<sup>179</sup> Antitrust is concerned that higher prices reduce the consumption of preferred commodities by consumers. Concentrated political power has a similar impact. Large firms that capture undue political power will use that power to lower taxes and other costs, and increase their share of public goods. The classes and groups that are disempowered are left to consume a diminishing share of public goods.

<sup>180</sup> Quoted in JACOB HACKER & PAUL PIERSON, “WINNER-TAKE-ALL POLITICS: HOW WASHINGTON MADE THE RICH RICHER AND TURNED ITS BACK ON THE MIDDLE CLASS,” Simon & Schuster (2010) at 170.

<sup>181</sup> BENJAMIN PAGE & MARTIN GILENS, “DEMOCRACY IN AMERICA?” Chicago (2020) at 96 (“In the 1980s, about 10 percent of all campaign spending came from one-tenth of 1 percent (.01 percent) of the voting population. By 2012, more than 40 percent of the spending came from this tiny sliver of wealthy Americans.”); LARRY BARTELS,

numerous mechanisms including direct political contributions,<sup>182</sup> lobbying,<sup>183</sup> dissemination of misleading or misinformation,<sup>184</sup> choice of candidates, sponsorship of think tanks, and co-opting academics.<sup>185</sup>

The investment theory of politics provides a coherent explanation of how large firms can control political decisions even when their interests differ from the vast majority of the voting public. A key tenet of the theory is that the relevant information voters need is prohibitively expensive to access. Voters must instead rely on advertising and political party affiliation to guide their voting decisions.<sup>186</sup> Voters vote for candidates that represent a bundle of positions. Dominant firms, in contrast, are the only entities with sufficient resources to make the required investments to make their preferences attractive, and political parties compete for investment (in the form of campaign contributions) by these dominant firms and rich individuals. As Peter Temin describes:

Elections become contests between several oligarchic parties whose major public policy proposals reflect the interests of large investors. The Investment Theory of Politics focuses attention on investors' interests, rather than those of candidates or voters. The expectation is that investors will not be responsive to public desires, particularly if they conflict with their interests, and they will be responsive to their own concerns. They will try to adjust the public to their views, rather than altering their views to accommodate voters.<sup>187</sup>

Kathleen Kemp describes how dominant firms can assemble in groups to support a particular candidate even though they may have conflicting interests with other firms and businesses.<sup>188</sup>

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“UNEQUAL DEMOCRACY: THE POLITICAL ECONOMY OF THE NEW GILDED AGE,” Russell Sage (2008); Matthias Lalisie, “*Measuring the Impact of Campaign Finance on Congressional Voting: A Machine Learning Approach*,” (INET working paper, February 22, 2022).

<sup>182</sup> Thomas Ferguson, Paul Jorgensen and Jie Chen, “*How Money Drives US Congressional Elections: Linear Models of Money and Outcomes*,” 30 STRUCTURAL CHANGE AND ECON. DYN. 1 (2019) (demonstrating the enormous influence of money on election outcomes for the Senate and House from 1980 to 2018).

<sup>183</sup> Lee Drutman, “*The Business of America is Lobbying: Explaining the Growth of Corporate Political Activity in Washington D.C.*,” Congress (2005).

<sup>184</sup> BENJAMIN PAGE & MARTIN GILENS, “DEMOCRACY IN AMERICA?” Chicago (2020) at 64 (“big money can produce a lot of misinformation, which can sometimes overwhelm the truth”).

<sup>185</sup> THOMAS FERGUSON, “GOLDEN RULE: THE INVESTMENT THEORY OF PARTY COMPETITION AND THE LOGIC OF MONEY-DRIVEN POLITICAL SYSTEMS,” Chicago (1995) at 41 (“The beginning of real wisdom in these matters, however, occurs when one reflects that direct cash contributions are probably not the most important way in which truly top business figures ... act politically. Both during elections and between election campaigns, their more broadly defined ‘organizational’ intervention is probably more critical. As the earlier discussion of free-riders suggested, such elite figures function powerfully as sources of contacts, as fundraisers (rather than mere contributors) and, especially, as sources of legitimization for candidates and positions.”).

<sup>186</sup> EZRA KLEIN, “WHY WE’RE POLARIZED,” Avid Reader (2020) at 97 (“You can think of Washington as a machine for making identity protective cognition easier. Each party has its allied think tanks, go-to-experts, favored magazines, friendly blogs, sympathetic pundits, determined activists, and ideological moneymen.”).

<sup>187</sup> PETER TEMIN, “THE VANISHING MIDDLE CLASS: PREJUDICE AND POWER IN A DUAL ECONOMY,” MIT (2017) at 72.

<sup>188</sup> Kathleen Kemp, “*Industrial Structure, Party Competition, and the Sources of Regulation*,” in THOMAS FERGUSON AND JOEL ROGERS EDs., “THE POLITICAL ECONOMY: READINGS IN THE POLITICS AND ECONOMICS OF AMERICAN PUBLIC POLICY,” Sharpe (1984) at 104.

While differences exist between the interests of dominant firms, legislation, at best, results in a compromise between these interests. But the interests of the nondominant classes are typically ignored. Larry Bartels finds that, in general, Senators give no weight at all to the preferences of lower income groups:

Using both summary measures of senators' voting patterns and specific roll call votes on the minimum wage, civil rights, government spending, and abortion, I find that senators in this period [1980s and 1990s] were vastly more responsive to affluent constituents than to constituents of modest means. Indeed, my analyses indicate that the views of constituents in the upper third of the income distribution received about 50% more weight than those in the middle third, with even larger disparities on specific salient roll call votes. Meanwhile, the views of constituents in the bottom third of the income distribution received no weight at all in the voting decisions of their senators.<sup>189</sup>

Similar research by Page & Gilens reached the same conclusion:

The most important result of this research is rather alarming. After interest groups and affluent citizens are taken into account, it becomes clear that average citizens exert little or no influence on federal government policy.<sup>190</sup>

This is particularly worrisome because surveys show that the political preferences of dominant firms and wealthy individuals often conflict with the general public. This divergence of interests between socioeconomic classes is documented by surveys of the political views of Americans over many decades. As Page & Gilens summarize:

[O]n many important issues, affluent and wealthy Americans seriously disagree with average citizens. Most Americans want the wealthy to pay more taxes, but the wealthy do not. Most Americans want tighter regulation of big corporations and financial institutions, but the wealthy disagree. Wealthy Americans also tend to oppose government help with jobs, wages, health care, education, retirement pensions, and other matters of great concern to average Americans. So the political

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<sup>189</sup> LARRY BARTELS, "UNEQUAL DEMOCRACY: THE POLITICAL ECONOMY OF THE NEW GILDED AGE," Russell Sage (2008) at 253-254.

<sup>190</sup> BENJAMIN PAGE & MARTIN GILENS, "DEMOCRACY IN AMERICA?" Chicago (2020) at 68. Shawn McGuire and Charles Delahunt apply machine learning techniques to Gilens and Page's data set. They find that "the high predictability of policy outcomes using models based on a few actors reinforces Gilens and Page's findings about the plutocratic tendencies of U.S. government," Shawn McGuire and Charles Delahunt, "*Predicting United States Policy Outcomes with Random Forests*," (INET Working Paper, October 27, 2020) at 10. See review by Thomas Ferguson, "*Affluent Authoritarianism: McGuire and Delahunt's New Evidence on Public Opinion and Policy*," (INET Website, November 2, 2020); <https://www.ineteconomics.org/perspectives/blog/affluent-authoritarianism-mcguire-and-delahunts-new-evidence-on-public-opinion-and-policy>

clout of affluent and wealthy Americans does not automatically translate into popular policies.<sup>191</sup>

Indeed, as demonstrated in an early study by Martin Gilens, when the preferences between the wealthy and the less affluent are not aligned, the less affluent have little or no political influence:

These results indicate that when preferences between the well-off and the poor diverge, government policy bears absolutely no relationship to the degree of support or opposition among the poor.<sup>192</sup>

Unlike wealthy individual donors who are often concerned with broad ideological goals, dominant firms typically, but not always, seek specific regulatory exemptions, tax cuts, and other policies that shift or reduce their costs. These firms employ strategies such as lobbying, and employ large government policy staff that work year-round and offer writing assistance to legislators. Most corporate lobbying has low visibility and is directed toward revising specific legislation at the congressional or state committee level. Such efforts can hold up or water down progressive legislation and create special provisions designed to benefit only a few corporations in other legislation.

### 3. The Conservative Dilemma: How to Maintain Unpopular Policies in a Democracy

This divergence between the interests of the dominant firms and all other classes in society, especially in a period of high income inequality, creates what Jacob Hacker and Paul Pierson call the “Conservative Dilemma.”<sup>193</sup>

We use “Conservative Dilemma” more specifically to describe the tension facing conservative parties. A century ago, in all countries with expanding franchises, conservative parties struggled to maintain their historical defense of elite privilege in the face of electoral challenges from the masses. When suffrage was restricted, conservative parties could ignore the massive gap between the rich and the rest. But this became a losing game once the working class gained the vote. Relatively quickly, conservative parties found themselves caught between a commitment to economic elites and an expanding electorate. How, they were forced to ask

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<sup>191</sup> *Id.* at 69-70. See also PETER TEMIN, “THE VANISHING MIDDLE CLASS: PREJUDICE AND POWER IN A DUAL ECONOMY,” MIT (2017) at 79 (“This study provides a window into attitudes and preferences of the one-percent group, which wants to reduce government activities in order to reduce government deficits. They do not want their taxes raised to lower government deficits, and they favor tax cuts when they can get them.”).

<sup>192</sup> MARTIN GILENS, “AFFLUENCE & INFLUENCE: ECONOMIC INEQUALITY AND POLITICAL POWER IN AMERICA,” Russell Sage (2012) at 81.

<sup>193</sup> JACOB HACKER AND PAUL PIERSON, “LET THEM EAT TWEETS: HOW THE RIGHT RULES IN AN AGE OF EXTREME INEQUALITY,” Liveright (2021). Ezra Klein also addresses large corporations’ need to mobilize voters to support economic policies favoring them in EZRA KLEIN, “WHY WE’RE POLARIZED,” Avid Reader (2020).

themselves, do we reconcile the needs of our core constituency with the need to win elections?<sup>194</sup>

Hacker and Pierson argue that one strategy employed to solve the conservative dilemma is to encourage social divisions within the non-rich population. If such divisions become strong enough, then voters may bypass their economic interests when voting and focus instead on issues related to their group identities, as defined by these divisions.<sup>195</sup> In the United States these divisions historically have been racial, ethnic, and religious. Exacerbating these toxic divisions may be necessary in a highly unequal society for dominant firms to solve the conservative dilemma, but the solution obviously has serious social welfare reducing ramifications—consequences that are not recognized by the Consumer Welfare Standard.<sup>196</sup>

#### **IV. The Consumer Welfare Standard Should be Replaced with the General Welfare Standard**

From all this, I conclude that the Consumer Welfare Standard is simply too narrow and must be replaced. Even the most important traditional antitrust goals and those that motivated Congress to pass the antitrust statutes in the first place are now firmly located outside the Consumer Welfare Standard's narrow bounds. While the Consumer Welfare Standard has served the goals of the Chicago School and its political adherents well, it has done so only at a great social and economic price, and only by embracing unreliable assumptions.

But there is an alternative. This paper proposes that the Consumer Welfare Standard be replaced by a General Welfare Standard, based on modern welfare economics, modified by an ability to incorporate an objective measure of welfare based on evidence from biology and the social sciences.

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<sup>194</sup> JACOB HACKER AND PAUL PIERSON, "LET THEM EAT TWEETS: HOW THE RIGHT RULES IN AN AGE OF EXTREME INEQUALITY," *Livelihood* (2021) at 22.

<sup>195</sup> BENJAMIN PAGE & MARTIN GILENS, "DEMOCRACY IN AMERICA?" Chicago (2020) at 19, 25 ("Economic inequality—the concentration of wealth and income in a few hands, with a big gap between rich and poor—has risen and fallen at various times. And democracy-popular control of government has tended to move in the opposite direction. When citizens are relatively equal, politics has tended to be fairly democratic. When a few individuals hold enormous amounts of wealth, democracy suffers.").

<sup>196</sup> There is obvious harm to the welfare of the portion of the population that has no effective political power. It may also be the case, however, that a working democracy increases welfare generally through a greater sense of social fairness. David Dorn and his co-authors found "a significant positive relationship between democracy and happiness even when controlling for income and culture measured by language and religion." David Dorn, Justina Fischer, Gerhard Kirchgassner and Alfonso Sousa-Poza, "*Is it Culture or Democracy? The Impact of Democracy and Culture on Happiness*," 82 SOC. INDIC. RES. 505, 512 (2007). See also Reinet Loubser & Cindy Steenekamp, "*Democracy, Well-Being and Happiness: A 10-Nation Study*," 17 J. PUB. AFFAIRS 1646 (2017) (finding a strong relationship between life satisfaction and democracy but only a weak or nonexistent correlation between happiness and democracy). Bruno Frey summarized the results from several studies of the impact of democracy on welfare as follows: "Overall, these results suggest that individuals living in countries with more extensive democratic institutions feel happier with their lives according to their own evaluation than individuals in more authoritarian countries." BRUNO FREY, "HAPPINESS: A REVOLUTION IN ECONOMICS," (2010) at 64.

I make this proposal to open, not conclude, debate. How trade-offs between the benefits and costs of mergers and dominant firm policies are resolved remains an open question. Moreover, judicial resources are limited and rules and presumption must be fashioned. Resolving these questions will require deep thinking and probably the kind of knowledge that only comes from years of experience under an antitrust regime comprehensive enough to address such concerns. However, important consequences of dominant firm policy would no longer be ruled out by assumption, and other important goals of antitrust would no longer be declared off limits simply because the measuring standard can't accommodate them.

In an effort to provide an analytical framework for my proposed General Welfare Standard, I identify the currently dominate method of measuring welfare and point out its deficiencies. I then propose an alternative measure, combining both subjective and objective indicia.

#### *A. The Dominant Approach to Measurement of Welfare and its Problems*

Economists evaluate policy by measuring its aggregate impact on the well-being of individuals. By well-being, economists mean whatever it is that makes an individual's life better, or whatever it takes for an individual's life to go well.<sup>197</sup> Well-being includes everything that can influence an individual's quality of life, whether positively or negatively, and it must include all individuals that are affected by the policy change, be they consumers, CEOs, competitors, or workers.<sup>198</sup> Utility is another name for well-being, and the term social welfare refers to the measurement of the sum of individuals' well-being.<sup>199</sup>

If welfare is to be used to analyze policy, there must be a means to measure individual welfare and then aggregate those individual measurements over the broader population.<sup>200</sup> The prevailing economic approach (described in more detail in the appendix) is to assume that individuals' preferences, as reflected in the choices they make, determine their well-being. These preferences are the primitive data in economic theory. Economists rely on observations of individual choice to discern preference. When a choice is made, economists assume that preferences are satisfied and that this leads to a welfare gain. Economists defend this approach as non-paternalistic; however, its purely subjective nature detracts from its usefulness. But surely there must be some connection between well-being and choice. Choice and well being can't be assumed to be coextensive by assumption otherwise utility would be meaningless.<sup>201</sup>

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<sup>197</sup> T.M. SCANLON, "WHAT WE OWE TO EACH OTHER," Belknap (2000) at 109 ("to come up with a theory of well-being: a systematic account of 'what makes someone's life go better' [is needed]"); WILL KYMLICKA, "CONTEMPORARY POLITICAL PHILOSOPHY: AN INTRODUCTION," Oxford (2002) at 11 (same).

<sup>198</sup> Welfare economics faces a boundary issue, like utilitarianism, because well-being could be extended to animals and the future born. In general, the analysis is restricted to impacted individuals today. In climate policy we may want to make an adjustment to the humans only approach.

<sup>199</sup> Or one could refer to an individual's welfare.

<sup>200</sup> Much of the difficulty in welfare economics to date has focused on the problem of aggregation and the use of such principles as Pareto Optimality and Kaldor and/or Hicks' compensation principles. I describe these issues in more detail in the Appendix for those interested.

<sup>201</sup> MICHAEL MANDLER, "DILEMMAS IN ECONOMIC THEORY: PERSISTING FOUNDATIONAL PROBLEMS OF MICROECONOMICS," Oxford (1999) at 79 ("Aware that depriving preference of all connection to an agent's well-

It is useful to distinguish between two senses of preference. In the first use of preference, it can be inferred that I prefer x to y from the fact that I chose x when y was also available. This approach links choice with preference and can be true by definition. This sense of preference tells us very little of value, however. But there is a second sense in which it can be inferred that my choice of x over y (*i.e.*, my preference for x) improved my well-being. This is the sense in which welfare economics uses preference. It links preference to well-being. This sense of preference is not true by definition, however, and requires justification. Unfortunately, so much about what we now understand about human biology and psychology renders untenable the economist's assumption that observation of choice is enough to infer improvement in well-being. As many economists and other social scientists are now understanding, our preferences are influenced by our genes, by social norms, and by life within our current social institutions.

### 1. De-Coupling Choice and Well-Being

At the most basic level, we are now learning that it cannot be reliably postulated that human choices are always motivated by a clear-headed search for greater well-being. Human motivation and cognitive abilities reside in the brain. The human brain is a product of evolution over the last two plus million years during the Pleistocene epoch, where humans primarily lived in small egalitarian hunter-gatherer groups.<sup>202</sup> This evolution resulted in human cognition and emotions that furthered the reproductive fitness of our genes in the original evolutionary environment. But, it did not necessarily result in the faculties necessary to improve our own well-being. For example, we are hard wired with emotions such as envy, guilt, rage, pride, anxiety, love, and jealousy. The role of the emotions is not necessarily to advance well-being, but rather to guarantee the survival of our genes. The two goals are not completely coextensive. Robert Frank, an economist who has written extensively on this topic, observes that:

But people who feel envious will accept different jobs, earn different salaries, spend them in different ways, save different amounts, and vote for different laws than predicted by self-interest [alone].<sup>203</sup>

If cognitive distortions result in greater gene reproductive fitness, then we should expect human cognition to often misread reality.<sup>204</sup> Indeed, the leading school of psychological therapy,

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being would endanger even the simplest welfare conclusions, an agent's preference of x over y is usually taken to imply that the agent believes his or her goals are better served by x than by y.")

<sup>202</sup> The new Darwinian synthesis in biology and psychology is a true science of the motivations behind human motivations. See ROBERT WRIGHT, "THE MORAL ANIMAL: WHY WE ARE THE WAY WE ARE: THE SCIENCE OF EVOLUTIONARY PSYCHOLOGY," Abacus (1994); RICHARD DAWKINS, "THE SELFISH GENE," Oxford (1989); ROBERT FRANK, "THE DARWIN ECONOMY: LIBERTY, COMPETITION, AND THE COMMON GOOD," Princeton (2011).

<sup>203</sup> ROBERT FRANK, "PASSIONS WITHIN REASON: THE STRATEGIC ROLE OF THE EMOTIONS," Norton (1988) at 15.

<sup>204</sup> DANIEL KAHNEMAN, "THINKING, FAST AND SLOW," FSG (2011) (discussing cognitive distortions); ROBERT WRIGHT, "WHY BUDDHISM IS TRUE," Simon & Schuster (2017) at 40 ("Feelings were designed to get the genes of our hunter-gatherer ancestors into the next generation. If that meant deluding our ancestors – making them so fearful that they "see" a snake that isn't actually there, say, so be it.").

cognitive behavioral therapy, focuses on improving well-being by correcting cognitively distorted thinking and redirecting emotions.<sup>205</sup>

Economists and other social scientists interested in understanding human well-being take our genetically based instincts as only a starting point.<sup>206</sup> Natural selection also gave humans the capacity to internalize learned norms and social patterns.<sup>207</sup> Axelrod, for example, theorized that “a norm exists in a given social setting to the extent that individuals usually act in a certain way and are often punished when seen not to be acting in this way.”<sup>208</sup> The operation of social norms is described by Marc Hauser as follows:

Their [Norms’] effectiveness lies in their unconscious operation. And their power to create conformity. On the other hand, although social norms often exert an unconscious hand of control, we do sometimes violate them. When we do, or observe someone else in violation, our brains respond with a cascade of emotions, designed both to register the violation and to redress the imbalance caused. When we break a promise, we feel guilty. Guilt may cause us to reinstate the relationship, repairing the damage done. When we see someone else break a promise, we feel angry, perhaps envious if they have made out with resources that we desire. When a brother and sister have intercourse and are caught, their incestuous consummation represents a violation of a social norm. It can trigger shame in the siblings, sometimes suicide, and often moralistic outrage in both genetically related family members and interested but unrelated third parties. Again, these processes operate outside of our conscious systems of control. An emotion’s effectiveness relies upon two design features: automaticity and shielding from the meddling influences of our conscious, reflective and contemplative thoughts about what ought to be.<sup>209</sup>

The internalization of norms occurs in early childhood through parents, peers, and non-parental adults.<sup>210</sup> Economists recognize that prevailing social norms influence our purchase choices, what we are willing to pay, and what we judge to be acceptable alternatives.<sup>211</sup> As discussed by

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<sup>205</sup> DAVID BURNS, “FEELING GOOD: THE NEW MOOD THERAPY,” William Morrow (1980).

<sup>206</sup> SAMUEL BOWLES AND HERBERT GINTIS, “A COOPERATIVE SPECIES: HUMAN RECIPROCITY AND ITS EVOLUTION,” Princeton (2011) at 14 (“efficient information transmission is likely to ensure that the genome encode information relevant not to ephemeral aspects of the organism’s environment but rather those that are constant, or that change only very slowly through time and space.”)

<sup>207</sup> *Id.*

<sup>208</sup> Robert Axelrod, “*An Evolutionary Approach to Norms*,” 80 AM. POL. SCI. REV. 1095, 1096-1097 (1986) (“Economists are becoming interested in the origin and operation of norms as they have come to realize that markets involve a great deal of behavior that no one individual can determine alone.”); Juliet Kostritsky, “*The Law and Economics of Norms*,” 48 TX. INT. L. J. 465 (2013).

<sup>209</sup> MARC HAUSER, “MORAL MINDS: HOW NATURE DESIGNED OUR UNIVERSAL SENSE OF RIGHT AND WRONG,” CCCO (2006) at 97-98.

<sup>210</sup> SAMUEL BOWLES & HERBERT GINTIS, “A COOPERATIVE SPECIES: HUMAN RECIPROCITY AND ITS EVOLUTION,” Princeton (2011) at 15.

<sup>211</sup> *Id.*; see also Dennis Rook and Robert Fisher, “*Normative Influences on Impulsive Buying Behavior*,” 22 J. OF CON. RESEARCH 305 (1995).



Elster, however, social norms often are not consistent with the individual's self-interest, and are, therefore, anathema to the notion that we can infer individual utility from one's choices.<sup>212</sup>

Preferences are also influenced by institutions such as the mass media.<sup>213</sup> Some forms of advertising influence preferences by causing products and services to be identified with deeper evolved emotions like status or ability to obtain mates.<sup>214</sup> Educational institutions also impact our preferences.<sup>215</sup> When institutions are influenced by the interests of dominant firms, these firms impact preferences, not just consumer choices.

## 2. Debunking Assumptions Equating Choice with Well-Being

So, what do economists specifically assume in order to make preference a usable measure of well-being and how reliable are those assumptions? Economists assume that the decisionmaker is self-interested (*i.e.*, they seek to improve their own well-being), is a competent evaluator, and has sufficient information. But there is no reason to believe that humans inherently possess these qualities, nor have economists presented a forceful argument for their presence.

### a. Preferences Are Not Always Based on Self-Interest

The standard view in economics is that preferences align with self-interest in one's own well-being. F.Y. Edgeworth, a founder of neoclassical economics stated the assumption this way: "The first principle of economics is that every agent is actuated only by self-interest."<sup>216</sup> This is an important assumption because, if preferences are not necessarily self-interested, then it cannot be assumed that preferences reflect well-being. For example, as John Broome puts the concern:

To be more exact, the choice needs to be based on good, self-interested reasons. They must be self-interested, because if a person were to make a choice for a reason which was not self-interested, then by considering the choice alone we should not get a proper indication of this person's interest, as opposed to the interests of other people.<sup>217</sup>

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<sup>212</sup> Jon Elster, "Social Norms and Economic Theory," 3 J. OF ECON. PERSP. 99, 103 (1989) ("[T]he norm of vengeance, obviously override[s] self-interest.").

<sup>213</sup> Amartya Sen & Bernard Williams, "Introduction: Utilitarianism and Beyond," in "UTILITARIANISM AND BEYOND," edited by Amartya Sen & Bernard Williams, Cambridge (1982) at 14-15 ("Any institutionalized or concretely realized processes of social distribution and policy will modify preferences.").

<sup>214</sup> STEPHEN MARTIN, "INDUSTRIAL ORGANIZATION IN CONTEXT," Oxford (2010) at 437 ("[S]ome advertising may inform. But it is difficult to accept that the producers of Wheaties or Cheerios pay for large amounts of advertising with the intent to inform potential consumers about their products' characteristics.").

<sup>215</sup> Tyler Cowen, "The Scope and Limits of Preference Sovereignty," 9 ECON. & PHIL. 253, 256 (1993) (Explaining that the influence of institutions on preferences creates an endogeneity problem: "In the education example, we can imagine that subsidies to a liberal education create individuals who value liberality highly, and subsidies to the authoritarian education create individuals who value strictness and discipline. We might even imagine that each policy change, ex post, is approved of unanimously.").

<sup>216</sup> Quoted in SAMUEL BOWLES & HERBERT GINTIS, "A COOPERATIVE SPECIES: HUMAN RECIPROCITY AND ITS EVOLUTION," Princeton (2011) at 9.

<sup>217</sup> John Broome, "Choice and Value in Economics," 30 OXFORD ECON. PAPERS 313, 333 (1978).

But experience tells us that preferences are often not self-interested. While self-interest is a powerful motivation, it is not the only human motivation for choice.<sup>218</sup> People vote when their vote is unlikely to have any impact. They return lost property, giving rise to lost and found centers. They donate blood, they give money to charity, they tip people they are unlikely to encounter again, they pay taxes when an audit is unlikely, they forego littering in pristine nature areas when no one is around, and they engage in many other practices that violate the self-interest assumption. Soldiers volunteer for dangerous missions. Mothers sacrifice themselves for their children. People will take serious risks to help strangers. It is obvious from causal observation, then, that people make many choices that reduce their own well-being to benefit the well-being of others.<sup>219</sup> Robert Frank summarizes the state of the evidence as follows:

On the strength of the evidence, we must say that the self-interest model provides a woefully inadequate description of the way people actually behave. Yet the model continues to flourish.<sup>220</sup>

Experimental economics also finds that people do not behave in accordance with the self-interest model. To take one example, in the ultimatum game, two players are given a sum of money. The first player, called the proposer, offers a portion of the money to the second player, the responder. If the responder accepts, she gets what was offered and the proposer gets what's left. The simple self-interest model predicts that the proposer should offer a penny and the responder should accept. But this is rarely what happens. Colin Camerer and Richard Thaler report that in ultimatum games, "offers typically average 30-40 percent, with a 50-50 split often the mode. Offers of less than 20 percent are frequently rejected."<sup>221</sup> Similarly, in most experiments using a prisoner's dilemma, participants cooperate, counter to the expectation of defection predicted by the self-interest assumption.<sup>222</sup> Commenting on the totality of the experimental literature, Earnst Fehr and Urs Fischbacher state:

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<sup>218</sup> The public choice literature contends that the acts of legislators are motivated purely by the self-interest of the legislators themselves. However, the evidence appears not to support this thesis. DANIEL FARBER & PHILIP FRICKEY, "LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION," Chicago (1991) at 33 ("Our best picture of the political process, then, is a mixed model in which constituent interest, special interest groups, and ideology all help determine legislative conduct."). Interestingly, if legislators and consumers are governed purely by self-interest, so should economists. However, the founder of the Public Choice school, James Buchanan, commented that his own motivation was never monetary: "To the extent that conscious motivation has entered these [research-publication] efforts, it has always been the sheer enjoyment of working out ideas, of creating the reality that is reflected finally in the finished manuscript. My own proof of normative disinterest lies in my failure to be interested in what happens once a manuscript is a finished draft, a failure that accounts for my sometimes inattention to choice of publisher, promotional details, and the potentials for either earnings or influence." JAMES BUCHANAN, "BETTER THAN PLOWING AND OTHER PERSONAL ESSAYS," Chicago (1992), quoted in RICK TILMAN, "IDEOLOGY AND UTOPIA IN THE SOCIAL PHILOSOPHY OF THE LIBERTARIAN ECONOMISTS," Greenwood (2001) at 114.

<sup>219</sup> Amartya Sen and Bernard Williams, "Introduction: *Utilitarianism and Beyond*," in "UTILITARIANISM AND BEYOND," edited by Amartya Sen & Bernard Williams, Cambridge (1982) at 12 (stating that the self-interest assumption is "an assumption for which the empirical evidence is, to say the least, inconclusive").

<sup>220</sup> ROBERT FRANK, "PASSIONS WITHIN REASON: THE STRATEGIC ROLE OF THE EMOTIONS," Norton (1988) at 256.

<sup>221</sup> Colin Camerer and Richard Thaler, "Ultimatums, Dictators and Manners," 9 J. OF ECON PERSP. 209, 210 (1995).

<sup>222</sup> See, e.g., ROBERT FRANK, "PASSIONS WITHIN REASON: THE STRATEGIC ROLE OF THE EMOTIONS," Norton (1988) at 137-145.

First, during the last decade experimental economists have gathered overwhelming evidence that systematically refutes the self-interest hypothesis.... Second, there is also strong evidence indicating that the deviations from self-interest have a fundamental impact on core issues in economics.<sup>223</sup>

b. Preferences Can be Other Regarding and Be Perverse

Preferences can also be other regarding, meaning that choices are motivated by their effects on others, thereby further compromising the link between choice and human welfare. Some choices are altruistic: someone reduces their own well-being to benefit the well-being of others.<sup>224</sup> Altruism by parents and within families is common and explained by the fact that family members carry the altruist's genes.<sup>225</sup> And economists, such as Bowles and Gintis, have compiled significant evidence of non-kin-based altruism.<sup>226</sup>

But other regarding preferences can also be negative. Humans can harbor racial or ethnic bias, can be revengeful, and can at times be sadistic. Adler and Posner offer the following example:

Frank has dedicated his life to leading the Ku Klux Klan and working for the oppression of blacks. Frank prefers that they be subordinated. The traditional welfare economist is committed to saying, in this case, that a race-based caste system might be worse for the oppressed but is better for Frank—better quite apart from any change in Frank's material welfare or any other tangible benefit that racial oppression might produce.<sup>227</sup>

Modern welfare economists consider negative other regarding preferences as a serious problem. If we simply include the welfare gained by satisfying all subjective preferences, then the preferences of the racists and the sadists potentially could have considerable influence. For example, John Harsanyi, a Nobel Prize winning welfare economist believes that “we must exclude all clearly antisocial preferences, such as sadism, envy, resentment, and malice.”<sup>228</sup> But

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<sup>223</sup> Earnst Fehr and Urs Fischbacher, “*Why Social Preferences Matter: The Impact of Non-Selfish Motives on Competition, Cooperation and Incentives*,” 112 *ECON. J.* C1 (2002). Bowles and Gintis summarize the results of the literature on eight types of experimental games, including the prisoner's dilemma, the dictator game, the ultimatum game and various public goods games. See Chapter 3 of SAMUEL BOWLES AND HERBERT GINTIS, “A COOPERATIVE SPECIES: HUMAN RECIPROCITY AND ITS EVOLUTION,” Princeton (2011).

<sup>224</sup> The material welfare economists, such as Pigou and Marshall, focused only on measurable outcomes like number of calories, not freezing, not being a social outcast. Using this approach, it is easy to identify altruism. What is more difficult is identifying altruism when motives are subjective.

<sup>225</sup> *Id.* at Chapter 6. See also William Hamilton, “*The Genetical Evolution of Social Behavior, I & II*,” 7 *J. OF THEORETICAL BIO.* 1 (1964).

<sup>226</sup> SAMUEL BOWLES AND HERBERT GINTIS, “A COOPERATIVE SPECIES: HUMAN RECIPROCITY AND ITS EVOLUTION,” Princeton (2011) at 53.

<sup>227</sup> MATTHEW ADLER & ERIC POSNER, “NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS,” Harvard U.P. (2006) at 33-34.

<sup>228</sup> John Harsanyi, “*Morality and the Theory of Rational Behavior*,” in “UTILITARIANISM AND BEYOND,” edited by Amartya Sen & Bernard Williams, Cambridge (1977) at 56.

once we move away from crediting all actual preferences, the process becomes more complicated because we need a theory to guide what preferences are excluded.<sup>229</sup>

### c. Economists Assume that Choices are Competent

Another necessary assumption to equating preference with improved well-being involves the cognitive competence of human decisionmakers. The connection between choice and well-being requires that agents are “rational” in the nontechnical sense that their “beliefs are [not] grossly out of kilter with available evidence.”<sup>230</sup> Researchers have identified at least three separate phenomena impacting the competency assumption: (1) negativity bias, (2) the endowment effect, and (3) reference bias.

Evolution has left humans with a “negativity bias.” Our brains react more strongly to negative news than positive news.<sup>231</sup> This bias helped our ancestors avoid life threatening dangers. A central tenet of the Buddhist practice for more than two thousand years has been to neutralize the negativity bias (that Buddhists believe causes “suffering” through fear and anxiety) through mindful meditation.<sup>232</sup> The point is that rules of thumb, self-deception, and other processing errors may have resulted from evolution’s goal of greater reproductive fitness of our genes, not from any sense of welfare-enhancing preferences.

More than forty years of behavioral economic research has shown that humans are more averse to losing something that they own, than they are to value the benefit from obtaining something new, even if the object lost and gained is of the same value. This cognitive feature is called the “endowment effect.” For example, Knetsch and Sinden found that individuals demand four times more money to give up a lottery ticket than they were willing to pay to acquire the same ticket.<sup>233</sup> In the classic endowment effect study, students were divided into two groups. One group was given a coffee mug, and a second group was given a candy bar of similar value. Students in the two groups were given a chance to trade the mug for candy or vice versa. Ninety percent of the students in each group opted not to trade. But a control group that received neither candy nor a mug split nearly 50/50 between preference for the mug or preference for the candy. According to Knetsch who conducted the study, “contrary to the expectation of an equal

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<sup>229</sup> In *Taking Rights Seriously*, Ronald Dworkin argues that it is impossible to avoid counting other regarding preferences. But the crediting of negative other regarding preferences poses a challenge to democracy. A majority with negative other regarding preferences can subordinate a minority. Dworkin makes the interesting proposal that the foundation of legitimate inherent rights involves the protection of liberties that are threatened by large external preferences in a community. RONALD DWORKIN, “TAKING RIGHTS SERIOUSLY,” Harvard (1977), Chapter 12.

<sup>230</sup> Paul Rozin and Edward Royzman, “*Negativity Bias, Negative Dominance, and Contagion*,” 5 PERSONALITY AND SOC. PSYCH. REV. 269 (2001).

<sup>231</sup> Hara Estroff Marono, “*Our Brains’ Negativity Bias: Why Our Brains are More Highly Attuned to Negative News*,” PSYCHOLOGY TODAY, June 20, 2003.

<sup>232</sup> Alice Walton, “*Mindfulness Meditation Helps Quell Negative Thoughts, Monkey Mind*” FORBES, Feb. 13, 2017.

<sup>233</sup> J. Knetsch & J. Sinden, “*Willingness to Pay and Compensation Demanded: Experimental Evidence of an Unexpected Disparity in Measures of Value*,” 99 Q.J. ECON. 507 (1984). See also D. Coursey, J. Hovis, 7 W. Schulze, “*The Disparity Between Willingness to Accept and Willingness to Pay Measures of Value*,” 102 Q. J. ECON 679 (1987).

proportion favoring one good over the other in each group, based on conventional assertion of economic theory and practice, the different initial entitlements and subsequent direction of potential trades heavily influenced the participants' valuation of the two goods."<sup>234</sup> The endowment effect demonstrates how perceptions of value are influenced by reference points, in this case initial endowment. Herbert Hovenkamp has argued that the endowment effect also runs counter to the assumptions required for the existence of a utility function—something critical to the use of welfare economics to evaluate competing policy proposals.<sup>235</sup>

Points of reference influence people's valuations and choices through a concept known as "framing effects." One such framing effect, "anchoring," occurs when choices are influenced by exposure to information that is not relevant to the decision. Exposure to large but irrelevant numbers can influence willingness to pay.<sup>236</sup> Choices are also influenced by the context of the choice or how the choice is framed. Kahneman, Knetsch, and Thaler provide several examples of experiments that demonstrate this effect. For example, consumers seem to consistently judge a list price increase differently from a refusal to give a price discount, even if the resulting sales price is the same.<sup>237</sup> Similarly, workers experience a reduction in money wages when prices are falling differently from the impact of constant money wages during an inflationary period, even if the resulting real wage is the same.<sup>238</sup>

The point is that preferences are merely a prediction of the benefit one expects to receive from the choice made. There is often a gap, however, between formation of the preference and the actual experience of preference satisfaction. In particular, people are notoriously bad at predicting the degree of adaptation to post-choice situations. For example, people's predictions of the satisfaction from a windfall in income do not take account of the immense ability humans have to adapt to higher income levels. Studies have found that recent lottery winners are no happier than those in a control group, for instance.<sup>239</sup> Bruno Frey, summarizing the experimental literature on forecasting utility, concludes that:

Individuals are not good at foreseeing how much utility they will derive from their future consumption. Research on affective forecasting shows, for instance, that people underestimate their ability to cope with negative effects. Usually, therefore, people have biased expectations about the intensity and duration of emotions. People fail to foresee that they will adapt more in the future than they predict at present.<sup>240</sup>

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<sup>234</sup> Jack Knetsch, "The Endowment Effect and Evidence of Nonreversible Indifference Curves" 79 AM. ECON. REV. 1277 (1989).

<sup>235</sup> Herbert Hovenkamp, "Legal Policy and the Endowment Effect," 20 J. LEGAL STUD. 225 (1991).

<sup>236</sup> DANIEL KAHNEMAN, "THINKING, FAST AND SLOW," FSG (2011), Chapter 11.

<sup>237</sup> Daniel Kahneman, Jack Knetsch and Richard Thaler, "The Endowment Effect, Loss Aversion, and Status Quo Bias," 5 J. ECON. PERSP. 193, 194 (1991).

<sup>238</sup> *Id.* at 204.

<sup>239</sup> Daniel Kahneman & Carol Varey, "Notes on the Psychology of Utility," in "INTERPERSONAL COMPARISONS OF WELL-BEING," (Jon Elster and John Roemer ed.) at 131 (1991).

<sup>240</sup> BRUNO FREY & ALOIS STUTZER, "HAPPINESS & ECONOMICS," Princeton (2002) at 130, n. 62.

Moreover, humans are programmed to care about status and relative social position.<sup>241</sup> They can seek higher and higher income at the expense of other uses of time in order to secure or retain a relative position with peers.<sup>242</sup> Concern for relative position can lead to lower overall well-being. For example, Robert Frank believes that:

Despite their higher incomes, then, the rich now appear to be worse off on balance. Their higher spending on cars and houses has simply raised the bar that defines adequate in those categories, while the corresponding decline in the quality of public goods has had a significant negative impact.<sup>243</sup>

Behavioral economists and cognitive psychologists have uncovered numerous examples of misperception and cognitive errors. These errors open a gap between preference, choice, and well-being. These gaps do not entirely undermine the utility of welfare economics as a device for evaluating competing policy proposals, however. The imperfect is not necessarily the enemy of the good.

#### d. Competent Choices Require Adequate Information

Another necessary assumption for equating choice with improved well-being is that decision makers have adequate and accurate information on which to base their choices. If individuals hold beliefs based on inaccurate information, their decisions will not necessarily accord with their well-being.<sup>244</sup> Economists are well aware that people can make mistakes because of information deficiencies.<sup>245</sup> Because welfare economics is concerned with aligning preferences

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<sup>241</sup> ROBERT WRIGHT, "THE MORAL ANIMAL: WHY WE ARE THE WAY WE ARE," Abacus (1994) at 245 ("Once this status ladder exists, and the higher rungs bring reproductive payoffs, genes that help a chimp climb it at acceptable cost will spread. The genes may work by instilling drives that, in humans, get labeled ambition or competitiveness...."); Daniel Kahneman and Carol Varey, "Notes on the Psychology of Utility," in "INTERPERSONAL COMPARISONS OF WELL-BEING," (Jon Elster and John Roemer ed.) at 142 (1991) ("sociological studies of soldiers' morale in World War II identified relative deprivation as a more important factor than objective circumstances").

<sup>242</sup> Robert Frank, "How the Middle Class is Injured by Gains at the Top," in JAMES LARDNER AND DAVID SMITH, "INEQUALITY MATTERS: THE GROWING ECONOMIC DIVIDE IN AMERICAN AND ITS POISONOUS CONSEQUENCES," Demos (2005) at 138 ("Suppose you had to choose between two worlds: World A, where you earn \$110,000 a year and everyone else earns \$200,000, and world B, where you earn \$100,000 and everyone else earns \$85,000. Most neoclassical economists would have an easy time deciding. Neoclassical economics, long the dominant wing of the profession, tends to equate personal well-being with absolute income, or purchasing power.... And yet, when the choice is put to American survey respondents, many seem torn, and most actually end up opting for World B.").

<sup>243</sup> ROBERT FRANK, "SUCCESS AND LUCK: GOOD FORTUNE AND THE MYTH OF MERITOCRACY," Princeton (2016) at 120. Frank argues that an across-the-board consumption tax would lower everyone's consumption and therefore have little impact on well-being.

<sup>244</sup> DANIEL HAUSMAN, MICHAEL MCPHERSON, AND DEBRA SATZ, "ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY," Cambridge (2017) at 130 ("The second objection arises from the fact that people are ignorant of many things. Consequentially, people may prefer something that is bad for them because they mistakenly believe it is beneficial. It is not true that x is better for A than y if and only if A prefers x to y. Indeed, many people live in circumstances in which their governments, their poverty, or their lack of education makes it almost impossible for them to make informed choices.").

<sup>245</sup> MATTHEW ADLER AND ERIC POSNER, "NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS," Harvard U.P. (2006) at 38 ("One general approach to idealization, popular among many philosophers of welfare and some welfare economists, too, is to invoke fully informed preferences."); John Harsanyi, "Morality and the Theory of Rational

with well-being, an individual needs to understand completely what makes a life go well for the theory to function optimally.<sup>246</sup>

Information relevant for aligning choice and well-being must concern what is most valuable for someone's well-being. Choice must be based on what achieves the most such value. But once value is determined by the theory used to assemble the information, that nexus is severed and value is no longer derived from individual preference.<sup>247</sup> Elizabeth Anderson has argued that information is a woefully inadequate remedy because choice is often driven by "appetites and whims," "actions prompted by habits," and "blind emotions." For Anderson, no amount of information can ensure that such motivations result in greater well-being.<sup>248</sup>

## B. *Reconsidering the Measurement of Well-Being*

### 1. Laundered Preferences

Welfare economists are well aware of the many issues that have been raised about the viability of measuring well-being based solely on subjective choice. One response has been to switch from actual preferences to "laundered"<sup>249</sup> or "ideal" preferences.<sup>250</sup> For example, as Harsanyi explains:

All we have to do is to distinguish between a person's manifest preferences and his true preferences. His manifest preferences are his actual preferences as manifested by his observed behavior, including preferences possibly based on erroneous factual

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*Behavior*," in "UTILITARIANISM AND BEYOND," Amartya Sen & Bernard Williams ed., Cambridge (1977) at 55 (preferences can be "based on erroneous factual beliefs").

<sup>246</sup> JAMES GRIFFIN, "WELL-BEING: ITS MEANING, MEASUREMENT AND MORAL IMPORTANCE," Clarendon (2002) at 13 ("[I]nformation is full when more, even when there is more, will not advance them [life plans] further. So there is only one way to avoid all the faults that matter to 'utility': namely, by understanding completely what makes life go well.").

<sup>247</sup> Amartya Sen, "Introduction: *Utilitarianism and Beyond*," in "UTILITARIANISM AND BEYOND," Amartya Sen and Bernard Williams, Ed. Cambridge (1977) at 13 ("But to respond to the question, 'What is most valuable?', or even 'What is most valuable to me?', by answering, 'whatever I would choose', would seem to remove the content from the notion of valuing, even when qualifications are added to the supposed choice in the form of 'under ideal conditions' or 'with full understanding'").

<sup>248</sup> ELIZABETH ANDERSON, "VALUE IN ETHICS AND ECONOMICS" Harvard U.P. (1993) at 131-132.

<sup>249</sup> Robert Gordon, "*Laundering Preferences*," in "FOUNDATIONS OF SOCIAL CHOICE THEORY," Jon Elster and Aanund Hylland ed., Cambridge (1989)

<sup>250</sup> John Harsanyi, "*Morality and the Theory of Rational Behavior*," in "UTILITARIANISM AND BEYOND," Amartya Sen & Bernard Williams ed., Cambridge (1977) at 55; J. A. Mirrless, "*The Economic Uses of Utilitarianism*," in "UTILITARIANISM AND BEYOND," Amartya Sen & Bernard Williams ed., Cambridge (1977) at 64 ("People sometimes have mistaken conceptions of their well-being. At least the conception must somehow be purified of obvious errors of foresight or memory."); Peter Hammond, "*Book Review: The Economics of Justice by Richard Posner*," 91 YALE L. J. 1493, 1501 (1982) ("This in turn suggests defining the utility of a particular individual as that which the individual would wish a utilitarian moral agent to maximize on his or her behalf."); MATTHEW ADLER & ERIC POSNER, "NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS," Harvard U.P. (2006) at 36 ("Call our view a restricted preference-based view of well-being. This account shall undergird our defense and elaboration of CBA. The account stipulates that an outcome benefits a person if she has an appropriately restricted preference for that outcome—a preference that survives idealization and concerns her own interests.").

beliefs, or on careless logical analysis, or on strong emotions that at the moment greatly hinder rational choice. In contrast, a person's true preferences are the preferences he would have if he had all the relevant factual information, always reasoned with the greatest possible care, and were in a state of mind most conducive to rational choice.<sup>251</sup>

Laundering or adjusting preferences is not an adequate answer to the many problems of subjective welfare measurement, however. In order to adjust preferences, one needs a theory about what preferences align with human well-being and what preferences do not. But if we had such a theory, we wouldn't need to try to divine "true" preferences from individual choices in any event. Welfare economists could simply rely on the objective evidence of what advances human well-being and promote these goals and processes, and ignore preferences based on choice altogether. Harvard philosophy professor T.M. Scanlon makes the same observation:

I mentioned above, as a problem for an informed-desire theory of well-being, that on such a view the value of desire fulfillment seems in the end to play no real role in explaining why some things contribute to a person's well-being. It may be true that something contributes to one's well-being only if one has reason to desire it. But even when this is so, what makes this thing good will not be the fact that it would satisfy that hypothetical desire but rather those considerations whatever they may be, that provide reasons for desiring it. The fact of desire itself seems to play no role.<sup>252</sup>

Because of this recognition, many mainstream economists have resisted the call to adjust or launder preferences.<sup>253</sup>

## 2. Objective Measures of Well-Being

So, what are we to do when neither actual choice, nor an adjustment of those choices provides a reliable basis for measuring human welfare? This paper advocates that welfare economics take an objective approach to measuring well-being. Objective measures of well-being take the

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<sup>251</sup> John Harsanyi, "Morality and the Theory of Rational Behavior," in "UTILITARIANISM AND BEYOND," Amartya Sen & Bernard Williams ed., Cambridge (1977) at 55.

<sup>252</sup> T. M. SCANLON, "WHAT WE OWE TO EACH OTHER," Harvard U.P. (1998) at 119. See also DANIEL HAUSMAN, MICHAEL MCPHERSON, AND DEBRA SATZ, "ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY," Cambridge (2017) at 136 ("Others have no reason to satisfy Hausman's preferences unless they can make sense of why what he wants is worth wanting, or why his life will be better in some substantive way if he gets what he wants. On the constitutive view, there is nothing to be said about whether what people prefer is worth preferring, because to maintain that some things are not worth pursuing assumes that there is some source of value other than the satisfaction of preferences.").

<sup>253</sup> Kaplow and Shavell are consistent in resisting any revision to actual preferences because, as they state, the revision undermines welfare economics' entire approach to measuring utility: "But such an approach [revising preferences] is troubling from the perspective of welfare economics because the moral force and appeal of welfare economics lies in promoting the actual well-being of people, not in advancing some hypothetical notion of satisfaction that is distinct from that of the individuals who are the object of our concern." LOUIS KAPLOW AND STEVEN SHAVELL, "FAIRNESS VERSUS WELFARE," Harvard U.P. (2002) at 420.



position that humans have a common ancestral heritage and cultural similarities that allow us to identify at least some things that, for the most part, universally advance human well-being.<sup>254</sup> The types of items that are typically listed as objectively beneficial to well-being include basic needs, human relationships, knowledge, freedom, dignity, and true beauty.<sup>255</sup>

Amartya Sen, a Nobel Prize winning economist, has advanced a particularly promising objective theory. According to Sen, people are entitled to equal respect and concern, but it makes little sense to equalize welfare based on subjective actual preferences. This is because the poor and oppressed of the world often adjust their desires and expectations to what little they see feasible, while the rich may have developed expensive tastes.<sup>256</sup> The equalization of subjective welfare in such a situation results in gross unfairness.<sup>257</sup> What Sen proposes is that we seek to achieve equality of real opportunity. This means that people have equal access to what is necessary to function in their choice of work and private life. For Sen, people are free to make the choice to work hard or seek a life of leisure. The first will likely be rewarded with more resources and status than the latter.

However, for everyone to have the opportunity to choose requires equal access to public goods such as education and medical care, as well as supportive relationships and monetary resources. According to Sen:

The functionings relevant for well-being vary from such elementary ones as escaping morbidity and mortality, being adequately nourished, having mobility, etc., to complex ones such as being happy, achieving self-respect, taking part in the life of the community, appearing in public without shame (the last a functioning that was illuminatingly discussed by Adam Smith). The claim is that the functionings make up a person's being, and the evaluation of a person's well-being has to take the form of an assessment of these constituent elements.<sup>258</sup>

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<sup>254</sup> DEREK PARFIT, "REASONS AND PERSONS," Oxford (1984) at 499 ("According to this theory [objective list theory] certain things are good or bad for people. Whether or not these people would want to have the good things, or to avoid the bad things."). See also JAMES GRIFFIN, "WELL-BEING: ITS MEANING, MEASUREMENT AND MORAL IMPLICATIONS," Clarendon (1986) Chapter III.

<sup>255</sup> T.M. SCANLON, "WHAT WE OWE EACH OTHER," Harvard U.P. (1998) at 125 ("These include such things as friendship, other valuable personal relations, and the achievement of various forms of excellence, such as art or science. These intuitive fixed points provide the basis for rough judgments of comparative well-being: a person's well-being is certainly increased if her life is improved in one of the respects just mentioned while the others are held constant."). Marshall and Pigou also identified important items that impact welfare. See MARSHALL'S PRINCIPLES, Book IV, Chapter V.

<sup>256</sup> STUART WHITE, "EQUALITY," Polity (2007) at 85 ("If people choose to develop expensive tastes, then it is certainly not fair for them to expect others to subsidize them.").

<sup>257</sup> AMARTYA SEN, "THE IDEA OF JUSTICE," Harvard U.P. (2009) at 282-283. For an explanation of this type of adaptation, see Jon Elster, "Sour Grapes: Utilitarianism and the Genesis of Wants," in "UTILITARIANISM AND BEYOND," Amartya Sen & Bernard Williams eds., Cambridge (1977).

<sup>258</sup> Amartya Sen, "Capability and Well-Being," in "THE QUALITY OF LIFE," Martha Nussbaum and Amartya Sen eds., Clarendon (1993) at 36-37.

Sen's approach is compelling because he has identified an objective element of human well-being that is difficult to dispute. That is, one's ability to marshal resources to choose the path of one's life for herself, to have equal access and opportunity to these choices, and the freedom to make such choices.<sup>259</sup> This approach is particularly credible when combined with a reimagining of how one looks at and measures welfare in general—replacing the Consumer Welfare Standard with a General Welfare Standard.

### *C. Advantages of Adopting a General Welfare Standard*

While much of the work in this area remains in the future, adopting Sen's approach opens the door to an evidence-based method for evaluating impacts on human well-being. Allowing objective measures of well-being based on social science research would materially increase the usefulness and effectiveness of welfare measurement. It would also enhance the potential role of economists in the social policy debate.

Replacing the Consumer Welfare Standard with a General Welfare Standard incorporating evidence-based, objective research on human welfare will allow economists to make important policy-based interventions in the debates about the future of antitrust. They will no longer be forced to make policy arguments untethered to economic theory simply because the Consumer Welfare Standard is too narrow to consider many beneficial goals; nor will they be forced to make unrealistic assumptions such as constant marginal utility of money or the many assumptions necessary to sustain a purely subjective measurement of welfare. Rather, economics and economists will be freed up to contribute to the healthy and important debate over antitrust policy and its impact on business decisions, and important welfare-inducing factors like reduced income inequality and increased political democracy.

## **Conclusion**

Properly understood, welfare economics endorses any policy that increases human well-being or welfare. The welfare of all affected individuals must be considered, and the mere fact that measuring individual well-being or aggregating welfare is complicated, is not adequate justification for ignoring significant groups impacted by market power or dominant firm conduct. Measured against this standard, current antitrust policy under the Consumer Welfare Standard is woefully inadequate.

Because of Chicago School influence, courts and antitrust agencies blindly ignore the impact of mergers and dominant firm action on income distribution and our democratic institutions. This

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<sup>259</sup> L. W. SUMNER, "WELFARE, HAPPINESS & ETHICS," Oxford (1996) at 61 ("The ground floor of Sen's account treats an individual's well-being as a matter of his functionings. But Sen then adds a second level to the analysis. A capability is a freedom or opportunity to achieve a certain functioning—the ability to eat well if one chooses, say, rather than actually doing so. Although capabilities may be prudentially valuable chiefly for the functionings which they make available, Sen argues that they also have certain value in their own right: we are better off for having avenues open to us which we never actually choose to pursue. Our level of well-being is therefore determined both by our set of functionings and by our set of capabilities.").

is not an oversight. It results directly from the standard applied. But, as established in Part I here and elsewhere, in doing so, the Consumer Welfare Standard inappropriately ignores Congressional intent, which envisioned a multi-goal role for antitrust that sought competitive remedies for broad social issues such as the preservation of democracy.

As developed in Parts II and III, the Consumer Welfare Standard, influenced by political motivations rather than the dictates of economics, improperly truncates “legitimate” antitrust inquiry to “purely-economic” effects, and specifically effects on consumers. This latter limitation is simply a misunderstanding of the Consumer Welfare Standard and its theoretical undergirding. The Consumer Welfare Standard is capable of including within its gambit remedies for the noxious impact that dominant firms have had on labor; it simply has largely chosen not to consider those effects, often even categorizing them as efficiencies rather than detrimental effects. But being sensitive to the needs of large corporations, while putting on blinders when it comes to labor, does not follow logically from the Consumer Welfare Standard. Rather, it results from super-imposing a conservative or libertarian political ideology on that standard. The Consumer Welfare Standard’s ignorance to the beneficial economic effects resulting from more robust political democracy is equally troubling as also addressed in Part III.

Replacing the Consumer Welfare Standard with a General Welfare Standard offers some hope for the future, as proposed in Part IV. Those who advocate a broader agenda in antitrust are often referred to in antitrust circles as “populists” or “hipsters.” In truth, I maintain that they are simply rejecting unsupportable limitations imposed by an outdated economic approach to welfare, or an indefensible interpretation of that approach. In fact, a strong case can be made that the “hipsters” are merely harkening back to a conception of economic welfare originally held by Marshall and Pigou, the originators of the economics that Judge Bork appropriated and renamed the Consumer Welfare Standard.

In sum, New Brandeis School scholars invite a return to a more traditional role for antitrust policy. One that not only guards against monopolies, but also fosters more equal and fair treatment of disadvantaged groups, and yes, even promotes more democratic institutions. As this article proves, economic theory—and, more precisely, basic principles of welfare economics—are allied with such efforts.

The process of measuring and aggregating utility or welfare remains complicated, and much more thought and work are needed to develop a workable General Welfare Standard to replace the clearly deficient Consumer Welfare Standard. Amartya Sen’s revolutionary work on objective measures of welfare provides a good starting point, however, and the basic human needs and wants he identifies are undeniably consistent with the broad, historic, and Congressionally-authorized purposes of the antitrust laws.

## Appendix: Aggregating Individual Welfare

In this appendix I attempt to sketch how ordinal utilities are aggregated for use in welfare economics. I try to do so in a nontechnical manner for antitrust attorneys. I include the problems and criticisms that are typically raised by economists to various aspects of the theory, but are excised from popular summaries. Obviously, this is just a primer, and many issues in welfare economics are not covered.

### A. *Utility in Economics*

Almost every microeconomics textbook begins with the concept of individual preferences. Preferences are the pre-existing, “given” primitive element in economic theory.<sup>260</sup> Individuals are assumed to know their own preferences for things and are assumed to be able to rank or order those preferences from best to worst.<sup>261</sup>

The term “utility” is often used in policy circles, but rarely is it defined. In fact, the meaning of utility has changed over the history of the economics profession. Early neoclassical economists used utility as a measure of subjective happiness.<sup>262</sup> This was consistent with the view of the utilitarian philosophers.<sup>263</sup> For example, the early neoclassical economists (e.g., Jevons, Walras, Edgeworth) believed that utility was theoretically measurable.<sup>264</sup> They assumed that both the direction of individual preference and the intensity of preferences were knowable, and many thought that interpersonal comparisons of utility were unproblematic.<sup>265</sup>

However, by the time of Jacob Viner’s classical 1925 article on the topic, the economics profession had come around to view utility as a measure of the ability of individuals to satisfy

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<sup>260</sup> JOHN ROEMER, “THEORIES OF DISTRIBUTIVE JUSTICE,” Harvard U.P. (1996) at 15 (acknowledging the “modern viewpoint, that the preference orderings of persons over alternative states are the primitives of economic theory and that utility functions are merely convenient representations of those orderings”).

<sup>261</sup> MICHAEL MANDLER, “DILEMMAS IN ECONOMIC THEORY: PERSISTING FOUNDATIONAL PROBLEMS OF MICROECONOMICS,” Oxford (1999) at 79.

<sup>262</sup> Daniel Kahneman and Carol Varey, “Notes on the Psychology of Utility,” in JON ELSTER AND JOHN ROEMER, “INTERPERSONAL COMPARISONS OF WELL-BEING,” Cambridge (1993) at 126-127 (“Jeremy Bentham and John Stuart Mill also used the term utility to refer to the hedonic quality of experience. Bentham spoke of the two sovereign masters that govern mankind – pleasure and pain – and developed the notion of a ‘hedonic calculus.’”)

<sup>263</sup> JEREMY BENTHAM, “AN INTRODUCTION TO THE PRINCIPLES OF MORALS AND LEGISLATION,” Oxford (1907); JOHN STUART MILL, “UTILITARIANISM,” Parker, Son & Bourn (2015); HENRY SIDGWICK, “THE METHOD OF ETHICS,” Palgrave (1962). For a discussion of the many philosophical issues raised by utilitarianism, see “UTILITARIANISM AND BEYOND” Ed. by Amartya Sen and Bernard Williams, Cambridge (1982).

<sup>264</sup> George Stigler, “The Development of Utility Theory,” 58 J. OF POL. ECON. 307, 316 (1950) (“Without exception, the founders accepted the existence of utility as a fact of common experience, congruent with the most casual introspection.”)

<sup>265</sup> MARC BLAUG, “ECONOMIC THEORY IN RETROSPECT,” Cambridge (1978) at 343-347; J.R. Hicks and R.G.D. Allen, “A Reconsideration of the Theory of Value. Part I,” 1 ECONOMICA 52 (1934). Jevons doubted utility was interpersonally comparable. George Stigler, “The Development of Utility Theory,” 58 J. OF POL. ECON. 307, 318 (1950) (“Unlike Walras and Menger, Jevons considered the question of interpersonal comparison of utilities. He expressly argued that this was impossible, but made several such comparisons...”).

(i.e., achieve) their preferences.<sup>266</sup> By “satisfy” economists do not mean achieve a feeling of satisfaction. The word “satisfy” is used only in the sense that the object of the preference was obtained. The notion being that what counts is the satisfaction of preferences, not the satisfaction of human beings.<sup>267</sup> As discussed by Armen Alchian in his classic clarifying article on utility:

Can we assign a set of numbers (measures) to the various entities and predict that the entity with the largest assigned number (measure) will be chosen? If so, we could christen this measure “utility” and then assert that choices are made so as to maximize utility. It is an easy step to the statement that ‘you are maximizing your utility,’ which says no more than that your choice is predictable according to the size of some assigned numbers.... Whether or not utility is some kind of glow or warmth, or happiness, is here irrelevant; all that counts is that we can assign numbers to entities or conditions which a person can strive to realize.... [I]t is difficult to realize that for present purposes utility has no more meaning than this.<sup>268</sup>

Pareto was the first economist to develop the modern view that only the order of preferences, not their intensity, is knowable. For Pareto, measuring utility really just involves the assignment of numbers to an individual’s preferences.<sup>269</sup> For example, a particular consumer may prefer butter to margarine, and margarine to jam. It is not hard to assign numbers to represent this order of preference, butter = 3, margarine = 2, and jam = 1. The numbers themselves are arbitrary and any set of numbers will suffice so long as the order of choice is preserved.<sup>270</sup> Numbers of this type are called “ordinal” numbers. If two sets of such numbers result in preservation of the ranking or order, they are called monotonic transformations of each other. So, for example, the numbers butter = 9, margarine = 4, and jam = 1 (which result from squaring the original numbers) preserve the order and thus are a monotonic transformation. Intensity of preference

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<sup>266</sup> Jacob Viner, “*The Utility Concept in Value Theory and Its Critics*,” 33 J. POL. ECON. 369 (1925); DANIEL HAUSMAN, MICHAEL MCPHERSON, AND DEBRA SATZ, “ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY,” Cambridge (2017) at 131 (“The satisfaction of preferences is like the satisfaction of degree requirements. It has no necessary connection to any feelings of satisfaction. To satisfy a preference for a state of affairs x for y is for x to obtain rather than y.”); MICHAEL MANDLER, “DILEMMAS IN ECONOMIC THEORY: PERSISTING FOUNDATIONAL PROBLEMS OF MICROECONOMICS,” Oxford (1999) at 78 (“Preference itself is now the primitive element of consumer theory; there is no need to peer into agents’ psyches.”).

<sup>267</sup> MICHAEL MCPHERSON AND DEBRA SATZ, “ECONOMIC ANALYSIS, MORAL PHILOSOPHY, AND PUBLIC POLICY,” Cambridge (2017) at 128 (“Measuring well-being by how well satisfied an agent’s preferences are also appeals to the anti-paternalistic view that individuals are the best judges of their own well well-being.”)

<sup>268</sup> Armen Alchian, “*The Meaning of Utility Measurement*,” 43 AMER. ECON. REV. 26, 31 (1953).

<sup>269</sup> ANDREU MAS-COLELL, MICHAEL WHINSTON, AND JERRY GREEN, “MICROECONOMIC THEORY,” Oxford (1995) at 8-9 (“In economics we often describe preference relations by means of a utility function. A utility function  $u(x)$  assigns a numerical value to each element in X, ranking the elements of X in accordance with the individual’s preferences.”) AJIT DASGUPTA AND D. W. PEARCE, “COST-BENEFIT ANALYSIS: THEORY AND PRACTICE,” Macmillan (1972) at 24 (“With these definitions in mind it is possible to define a utility function as a scale which will reflect the preference relationships of the individual.”)

<sup>270</sup> Armen Alchian, “*The Meaning of Utility Measurement*,” 43 AMER. ECON. REV. 26, 30 (1953) (“We may summarize by saying that, given a method for validly ordering entities, any monotone transformation of the particular numerical values assigned in the ordering process will be equally satisfactory.”)

cannot be discerned from these numbers, nor can we know to what degree butter is preferred to margarine. We also cannot add two individual's utilities together or compare them (other than by their order) because the numbers convey order but are otherwise arbitrary. The inability to directly compare individual utilities, referred to as interpersonal comparability, has been a major problem for welfare economics.<sup>271</sup>

But if we cannot add individual utilities, and utility represents welfare, then how do we obtain social welfare, or consumer's surplus which are aggregates of individual utilities? That procedure is explained in the next section. For intermediate economics students it can appear as a result of magic.

### B. Aggregating Welfare

Once we have a measure of utility, we need to be able to aggregate individual welfare. One can see how this would be necessary in an antitrust analysis because the focus is on the welfare implications of business practices within markets.<sup>272</sup> Markets are aggregations of individuals. Thus, it is important to be able to aggregate individual welfares to at least the market level.<sup>273</sup>

#### 1. Utility Functions

To grasp how aggregation is performed and the assumptions required, we need additional structure. We can express utility in functional form as:

$$\text{Utility} = f(X \text{ butter, } Y \text{ jam})$$

with the *ceteris paribus* assumption of holding all other goods, services, and other factors constant. The existence of a utility function requires that preferences satisfy a few assumptions. Preferences must be rational and continuous.

Preferences are rational when they are both transitive and complete.<sup>274</sup> Preferences are transitive if A (*e.g.*, a quantity of a good) is preferred to B, and B is preferred to C, then A must be

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<sup>271</sup> E MISHAN, "INTRODUCTION TO NORMATIVE ECONOMICS," Oxford (1981) at 308 ("It is a fact that there is no acceptable way of measuring utility or comparing one person's utility with another"); MICHAEL MANDLER, "DILEMMAS IN ECONOMY THEORY, PERSISTING FOUNDATIONAL PROBLEMS OF MICROECONOMICS" Oxford (1999) 114 ("The inability to go beyond non-controversial interpersonal comparisons of welfare has remained a constant of neoclassical welfare economics."); Ruth Weinstein, "Do Utility Comparisons Pose a Problem?" 92 PHIL. STUD. 307, 318 (1998) ("the structure that preferences have does not lend itself to non-arbitrary comparisons between individuals.")

<sup>272</sup> Gregory Werden, "Antitrust's Rule of Reason: Only Competition Matters," (DOJ Working Paper (2013)) at 2 ("To formalize such ideas, economists struggled in vain to sum utilities of all individuals in the economy.")

<sup>273</sup> A market or industry is simply the sum of the producers and consumers for a particular product, such as all of the producers of branded soda, like Coke and Pepsi. I leave aside the technical nature of what is included in a relevant market and for now simply rely on intuitive markets: steel, cars, social media, canned tuna, etc.

<sup>274</sup> ANDREU MAS-COLELL, MICHAEL WHINSTON, AND JERRY GREEN, "MICROECONOMIC THEORY," Oxford (1995) at 6 ("In much of microeconomic theory, individual preferences are assumed to be rational. The hypothesis of rationality is embodied in two basic assumptions about the preference relation: completeness and transitivity.") Proposition 3.C.1 shows that continuity is also required for a utility function.

preferred to C. Transitivity is a reasonable assumption if choices are not too complex, and if the other assumptions concerning measurement of utility are true.<sup>275</sup> If choices are made by whim, emotion, or habit, or are changing, for example, transitivity might not hold.<sup>276</sup>

Completeness is more problematic, however, because it requires that individuals always be able to state which of any two options they prefer.<sup>277</sup> It is not hard to think of situations where completeness may be a problem. For example, behavioral economists have noticed that individuals often value a good more when they own it than when they don't. This is called the endowment effect (discussed in the body of this paper). When the endowment effect holds one does not have a dependable, objective utility function because one's preference will depend on their endowment (whether they own the good or don't own the good). Thus, the presence of the good in the utility function gives rise to two different utility numbers.<sup>278</sup> Alternatively, which is the same thing as Herbert Hovenkamp shows, the endowment effect makes it impossible to have indifference curves.<sup>279</sup>

## 2. Indifference Curves

Assuming away the endowment effect, we now proceed to define an indifference curve. We need the indifference curve to obtain values for willingness to pay and willingness to accept that are denominated in money, and which will allow us to perform the welfare aggregation. We can define an indifference curve as all the combinations of goods and services that give rise to the same level of utility. In our example, an indifference curve might consist of all the combinations of butter and jam that give rise to 20 units of utility. We then may have another indifference curve consisting of all the units of butter and jam that give rise to 30 units of utility. Once we have income and prices, we can also define a budget constraint, which reflects all the combinations of butter and jam that one could purchase with a given income, and prices for butter and jam.

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<sup>275</sup> *Id.* n. 2; Transitivity implies that if I prefer x to y and y to z, I will prefer x to z. This may not always be the case when choice is influenced by framing. See Amos Tversky and Richard Thaler, "The Framing of Decisions and the Psychology of Choice," 211 *SCIENCE* 453 (1981).

<sup>276</sup> ELIZABETH ANDERSON, "VALUE IN ETHICS AND ECONOMICS," Harvard U.P. (1993) at 132 ("Appetites and whims can without contradiction express themselves in intransitive preference orderings.").

<sup>277</sup> Completeness often fails when information about an option is incomplete.

<sup>278</sup> The endowment effect is distinct from the wealth effect. As discussed in the body of this paper, the endowment effect is a result of significant research that shows that whether one owns something influences one's valuation and thus one's preference ranking. This means that, depending on the circumstances, one cannot state which of two options is preferred. See Daniel Kahneman, Jack Knetsch and Richard Thaler, "Experimental Tests of the Endowment Effect and the Coase Theorem," 98 *J. OF POL. ECON.* 1325 (1990); Jack Knetsch, "The Endowment Effect and Evidence of Nonreversible Indifferent Curves," 79 *AM. ECON. REV.* 1277 (1989). MICHAEL MANDLER, "DILEMMAS IN ECONOMIC THEORY: PERSISTING FOUNDATIONAL PROBLEMS OF MICROECONOMICS," Oxford (1999) at 103-104 ("Consequently, if preference is defined as choice, the completeness axiom is justified but the rationale for transitivity is undermined. On the other hand, if preference is defined psychologically as an agent's judgment of his or her well-being, transitivity can be argued for convincingly, but completeness cannot be justified. Under either framework, therefore, ordinalism cannot provide an adequate foundation for the entirety of its account of rational action.").

<sup>279</sup> Herbert Hovenkamp, "Legal Policy and the Endowment Effect," 20 *J. LEGAL STUD.* 225 (1991).

Thus, in the figure below:

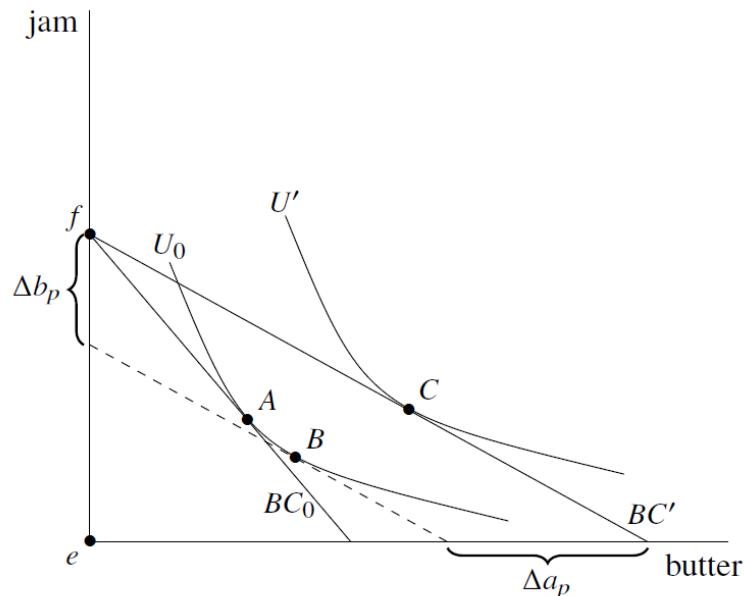


Figure 3: Willingness and Ability to Pay

The original budget constraint in figure 1 is  $BC_0$ . Assume that the price of butter declines, so the amount of butter one can acquire with a given income increases. This causes the intercept where only butter is purchased to shift out and transition to a new budget constraint  $BC'$ . Before the price decline, the consumer was on the  $U_0$  indifference curve and the most utility was achieved at point A. With the shift, the consumer moves to indifference curve  $U'$  and point C. The question then becomes: How much would the consumer be willing to pay to move from A to C? The answer is the additional income represented by the shift of the dotted budget constraint to the new budget constraint  $BC'$ . If the consumer were at B and was given this amount of income, he/she would move to C. This income amount is how much a consumer would be willing to pay to get from B to C.<sup>280</sup> It is labelled  $\Delta b_p$ , which can be an amount of jam or can be expressed in money by multiplying this amount of jam by the price of jam. Again, the policy is a fall in the price of butter. The amount that a consumer is willing and able to pay (“WATP”) in exchange for this policy is this income amount.

One could also ask, what would a consumer accept for being denied a lower price of butter? This is illustrated by the following graph:

<sup>280</sup> Equivalently, if the prices had already changed and the consumer was at C, this is the maximum income amount the consumer would be willing to give up in return for continuing to face the new, lower price of butter.



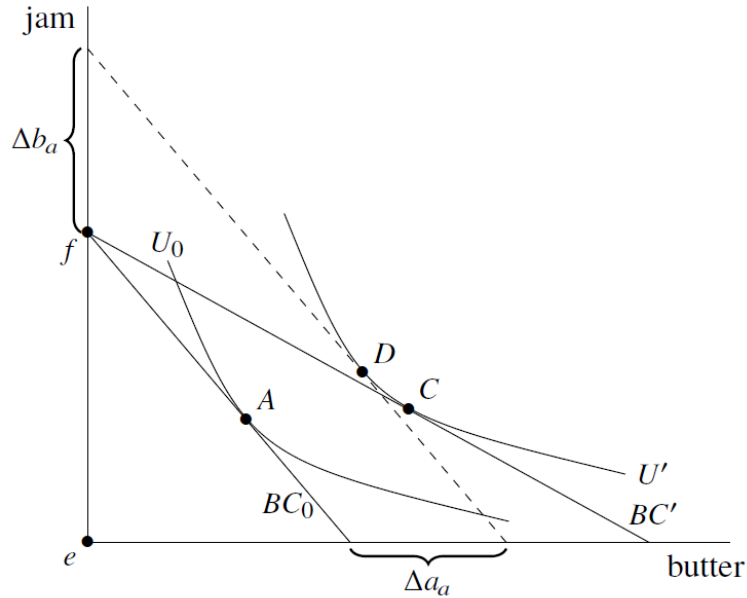


Figure 4: Willingness to Accept

Starting at point C, what would a consumer be willing to accept to forego the price decline of butter prices? We call this willingness to accept (“WTA”). The consumer would be willing to stay with the higher price of butter if they were given enough income to move to the dashed budget constraint, at point D. So, WTA is the income difference between the dashed line and  $BC_0$ . The two measures, willingness to pay (“WATP”) and willingness to accept, are typically different. There is no reason for WATP and WTA to be equal except under highly restrictive assumptions.<sup>281</sup>

### 3. Deriving the Demand Curve

To obtain the demand curve, we simply continue to vary prices, of say butter, and find the optimal quantities of butter the consumer would purchase. It is important to note that this approach assumes that the consumer doesn’t actually purchase any butter. If there were an actual purchase, the consumer’s income would decline. This, in turn, would change demand. For an individual consumer then, if we adjusted income after each purchase, we could ascertain what the consumer would be willing to pay for each subsequent purchase. For welfare purposes, this would be a more accurate measure of the value of the purchase than using a value measure based on the demand curve.

In the body of the paper, we learned that Judge Bork, following Marshall, used the demand curve in defining consumer’s surplus (called consumer welfare by Bork). He should have used “WATP” and “WTA.” Had he done so, however, he would have been forced to acknowledge

<sup>281</sup> See Mark Glick & Gabriel Lozada, “The Erroneous Foundations of Law and Economics,” (INET Working Paper 149 (2021)) at 45.

that value has a dual (or “binary”) definition. WATP and WTA are both equally viable measures of value. The problem is that the two measures can diverge, making the measure of utility ambiguous.

The fact that WATP and WTA are monetary amounts of utility substantially advances the analysis and provides a starting point for aggregation. Because WATP and WTA are expressed in units of money, they are cardinal (not ordinal) and can be aggregated between individuals. Almost by magic, then, we have found a way to aggregate measures of utility that would otherwise be ordinal only. To do this, however, requires that we know the shape of each individual’s indifference curves because that is how we graphically observed the change in utility level in response to price changes in Figures 1 and 2. But do we really know the shape of individual indifference curves? It may be theoretically possible to obtain the shape of the indifference curve from detailed individual level data on purchase responses to price changes, but in practice, this type of household level data is not typically available. The historian of economic thought Mark Blaug concluded his investigation of this issue with the following:

The notion of ‘indifference’ itself is not subject to direct measurement. Although choices between what we might call ‘unambiguously separate’ bundles of goods – bundles that differ only by having more of at least one of the goods – can be rationalized by an ordinal utility scale, no operational method for deriving the exact shape of indifference curves has ever been devised.<sup>282</sup>

Measuring utility by WATP (and WTA) poses a problem, however. WATP and WTA depend on income. A high-income individual is generally willing to pay more for any given item than is a low-income individual. Therefore, it would be improper and unreliable to sum WATP or WTA for various income groups. (This, of course, is part and parcel of the concept of diminishing marginal utility discussed in the body of this paper in relation to Marshall’s model that uses cardinal utility.) But even in the ordinal context, the psychological assumption that the rich will usually be willing to pay more (and able to pay more) is obvious and widely acknowledged by most economists.<sup>283</sup> Unfortunately, there is no reliable way to fix this problem. The remedy

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<sup>282</sup> MARK BLAUG, “ECONOMIC THEORY IN RETROSPECT,” Cambridge (1978) at 364. Gabriel Lozada shows that current econometric practices in the antitrust field do not solve the aggregation problem. Instead, market level data is employed and assumptions are made in order to be able to think of the market demand curve as being derived from a representative or average consumer. These assumptions include unrealistic constraints on consumers’ Engel curves, the relationship between income and expenditures on particular goods and services. See Gabriel Lozada, “A Critique of Antitrust Econometrics: Aggregation, the Representative Consumption, and the Broader Concerns of the New Brandeis School,” THE ANTITRUST BULL. (Forthcoming) at 13-14.

<sup>283</sup> Joe Farrell & Michael Katz, “The Economics of Welfare Standards in Antitrust,” Berkeley (2006) at 9 (“It is however, a widely held view that a dollar is worth more to society in the hands of a poor person than those of a rich one.”); Peter Hammond, “Welfare Economics,” in “ISSUES IN CONTEMPORARY MICROECONOMICS & WELFARE,” Ed by George Feiwel, Palgrave (1985) at 408 (“Yet it hardly requires a very strong sense of moral compassion to regard the dollar a destitute mother needs for medicine to save her dying child as definitely more valuable than the extra dollar an opulent man wants to spend on a better quality cigar.”). In addition, risk adversity requires a declining marginal utility of income. Mark Glick, “The Unsound Theory Behind the Consumer (and Total) Welfare Goal in Antitrust,” 63 ANTITRUST BULL. 455, 463 (2019).

usually suggested is to multiply the willingness to pay by a factor that reflects differences in wealth. But no one has developed a practical procedure for weighting. As Adler and Posner state:

Welfare economists have not proposed a practical way of determining the appropriate method of weighting. The problem is that there does not seem to be a reliable way of determining people's marginal utility of money.<sup>284</sup>

Even if there were a weighting system, such as inferring what individuals would prefer if they had higher incomes, it would not be reliable. This is because preferences themselves are impacted by an individual's life experience, which is strongly influenced by income.<sup>285</sup>

#### 4. Pareto Optimality and the Contribution of Kaldor and Hicks

The inability to reliably weight utilities, is a well-recognized problem and explains why economists would rather use normative concepts such as Pareto Optimality and Kaldor and Hicks compensation principles rather than gross aggregations of WATP or WTA. Pareto Optimality offers economists a way to make policy judgments based on actual preference. Pareto's approach obviates the concern raised above, but at the expense of applicability. Under the Pareto approach, a situation x, is judged to be a Pareto improvement over situation y, if at least one person prefers x to y, and no one prefers y to x. A situation is then considered Pareto efficient if there are no further Pareto improving moves. Pareto efficiency has the advantage that it is based on actual preferences and presumably could be defended by unanimous consent. However, it is difficult to imagine many situations that could be resolved using Pareto efficiency. In particular, the concept is not helpful for antitrust analysis because typically there are both winners and losers in antitrust cases.<sup>286</sup>

Kaldor and Hicks attempted to develop a different policy criterion when there are winners and losers involved. Cost-Benefit Analysis is a version of Kaldor and Hick's approach using money as the metric for utility.<sup>287</sup> A policy is an improvement under Kaldor if, after adoption of the policy, the winners can compensate the losers and still have some of the winnings left over. The logic is that there is an improvement because the "pie" has enlarged, allowing for a greater capacity to satisfy preferences. A policy is an improvement under Hicks if after refusal to adopt the policy, the winners would not compensate the losers and still have some of the winnings left

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<sup>284</sup> MATTHEW ADLER & ERIC POSNER, "NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS," Harvard U.P. (2006) at 24.

<sup>285</sup> AMARTYA SEN, "THE IDEA OF JUSTICE," Harvard U.P. (2009) at 282-284 ("The utilitarian calculus based on happiness or desire-fulfilment can be deeply unfair to those who are persistently deprived, since our mental make-up and desires tend to adjust to circumstances, particularly to make life bearable in adverse situations.").

<sup>286</sup> However, there could be some cases where Pareto Optimality could be applied. In the area of trade, for example, if compensation were provided for the losers, a Pareto Optimal outcome might be possible.

<sup>287</sup> MATTHEW ADLER AND ERIC POSNER, "NEW FOUNDATIONS OF COST-BENEFIT ANALYSIS," Harvard (2006) at 21 ("The difference between CBA and Kaldor-Hicks is that the former uses money as the numeraire, whereas the latter, a more general criterion, does not.").

over. The Kaldor and Hicks criteria are referred to as a “potential Pareto improvement” because, if the losers were actually compensated, there would be a Pareto improvement.<sup>288</sup>

Unfortunately, the Kaldor-Hicks efficiency approach has been shown to be seriously deficient.<sup>289</sup> Measuring the size of the economic “pie” is fraught with so many difficulties that the concept is best abandoned. Furthermore, since Kaldor’s approach and Hicks’ approach are based on two different measures of value (WATP and WTA), the Kaldor-Hicks approach can result in inconsistencies, reversals of policy, and, because there is no actual compensation made to the losers, it results in morally indefensible results.<sup>290</sup>

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<sup>288</sup> Sometimes compensation does not appear to be morally justified. In the Consumer Welfare Standard, competition is Kaldor and Hick efficient compared to monopoly because consumers can compensate the monopolist its monopoly rents and still have consumer’s surplus left over. But should the monopolist be compensated for lost monopoly rents?

<sup>289</sup> Use of tax policy cannot rescue Kaldor and Hicks. Tax policy has never been used to compensate losers from policy decisions in other areas such as legal precedent. There are also problems of measuring the compensation required and targeting taxes to the right individuals. Moreover, when the losers are from the groups with the least political influence (as, unfortunately, is often the case), the likelihood of a change in tax policy in their favor is virtually nil. Indeed, only when big business is the loser is it practical to rely on tax policy for redistribution.

<sup>290</sup> Many of these failures of the Kaldor and Hicks criteria have been well documented by specialists in welfare economics but ignored by the law and economics literature. A catalogue of problems is set forth in Mark Glick & Gabriel Lozada, “*The Erroneous Foundations of Law and Economics*,” (INET Working Paper 149 (2021)). Of course, this appendix is not comprehensive and does not address many of the other problems of modelling competitive equilibrium.