The Limits of Rivalry

Kelly Fayne — 2 November 2020

[***TOTM**: The following is part of a symposium by TOTM guests and authors marking the release of Nicolas Petit's "Big Tech and the Digital Economy: The Moligopoly Scenario." The entire series of posts is available here.*

This post is authored by Kelly Fayne (Antitrust Associate, Latham & Watkins).]

Nicholas Petit, with *Big Tech and the Digital Economy: The Moligopoly Scenario*, enters the fray at this moment of peak consternation about big tech platforms to reexamine antitrust's role as referee. Amongst calls on the one hand like those in the Majority Staff Report and Recommendation from the Subcommittee on Antitrust ("these firms have too much power, and that power must be reined in and subject to appropriate oversight and enforcement") and, on the other hand, understandably strong disagreement

from the firms targeted, Petit offers a diagnosis. A focus on the protection of rivalry for rivalry's sake is insufficiently adaptive to the "distinctive features of digital industries, firms, and markets."

I am left wondering, however, if he's misdiagnosed the problem – or at least whether the cure he offers would be seen as sufficient by those most vocally asserting that antitrust is failing. And, of course, I recognize that his objective in writing this book is not to bring harmony to a deeply divided debate, but to offer an improved antitrust framework for navigating big tech.

Petit, in Chapter 5 ("Antitrust in Moligopoly Markets"), says: "So the real question is this: should we abandon, or at least radically alter traditional antitrust principals modeled on rivalry in digital markets? The answer is yes." He argues that "protecting rivalry is not perforce socially beneficial in industries with increasing returns to adoption." But it is his tethering to the notion of what is "socially beneficial" that creates a challenge.

Petit argues that the function of the current antitrust legal regimes – most significantly the US and EU – is to protect rivalry. He observes several issues with rivalry when applied as both a test and a remedy for market power. One of the most valuable insights Petit offers in his impressive work in this book, is that tipped markets may not be all that bad. In fact, when markets exhibit increasing returns to adoption, allowing the winner to take it all (or most) may be more welfare enhancing than trying to do the antitrust equivalent of forcing two magnets to remain apart. And, assuming all the Schumpeterian dynamics align, he's right. Or rather, he's right ***if*** you agree that welfare is the standard by which what is socially beneficial should be measured.

Spoiler alert: My own view is that antitrust requires an underlying system of measurement, and the best available system is welfare-based. More on this below.

When it comes to evaluating horizontal mergers, Petit suggests an alternative regime calibrated to handle the unique circumstances that arise in tech deals. But his new framework remains largely tethered to (or at least based in the intuitions of) a variation of the welfare standard that, for the most part, still underlies modern applications of antitrust laws. So the question becomes, if you alter the means, but leave the ends unchanged, do you get different results? At least in the merger context, I'm not so sure. And if the results are for the most part the same, do we really need an alternative path to achieving them? Probably not.

The Petit horizontal merger test (1) applies a non-rebuttable (OMG!) presumption of prohibition on mergers to monopoly by the dominant platform in "tipped markets," and (2) permits some acquisitions in untipped markets without undue regard to whether the acquiring firm is dominant in another market. A non-rebuttable presumption, admittedly, elicited heavy-pressure red pen in the margins upon my first read. Upon further reflection … I still don't like it. I am, however, somewhat comforted because I suspect that its practical application would land us largely in the same place as current applications of antitrust for at least the vast majority of tech transactions. And that is because Petit's presumptive prohibition on mergers in tipped markets doesn't cancel the fight, it changes the venue.

The exercise of determining whether or not the market is tipped in effect replicates the exercise of assessing whether the dominant firm has a significant degree of market power, and concludes in the affirmative. Enforcers around the world already look skeptically at firms with perceived market power when they make horizontal acquisitions (among an already rare group of cases in which such deals are attempted). I recognize that there is theoretical daylight between Petit's proposed test and one in which the merging parties are permitted an efficiencies defense, but in practice, the number of deals cleared solely on the basis of countervailing procompetitive efficiencies has historically been small. Thus, the universe of deals swept up in the per se prohibition could easily end up a null set. (Or at least, I think it should be a null set given how quickly the tech industry evolves and transforms).

As for the untipped markets, Petit argues that it is "unwarranted to treat firms with monopoly positions in tipped markets more strictly than others when they make indirect entry in untipped markets." He further argues that there is "no economic basis to prefer indirect entry by an incumbent firm from a tipped market over entry from (i) a new firm or (ii) an established firm from an untipped market. Firm type is not determinative of the weight of social welfare brought by a unit of innovation." His position is closely aligned with the existing guidance on vertical and conglomerate mergers, including in the recently issued FTC and DOJ Vertical Merger Guidelines, although his discussion contains a far more nuanced perspective on how network effects and the leveraging of market power from one market to another overlay into the vertical merger math. In the end, however, whether one applies the existing vertical merger approach or the Petit proposal, I hypothesize little divergence in outcomes.

All of the above notwithstanding, Petit's endeavor to devise a framework more closely calibrated to the unique features of tech platforms is admirable, as is the care and thoughtfulness he's taken to the task. If the audience for this book takes the view that the core principals of economic welfare should underlie antitrust laws and their application, Petit is likely to find it receptive. While many (me included) may not think a new regime is necessary, the way that he articulates the challenges presented by platforms and evolving technologies is enlightening even for those who think an old approach can learn new tricks. And, of course, the existing approach, but has the added benefit of being adaptable to applications outside of tech platforms.

Still, the purpose of antitrust law is where the far more difficult debate is taking place. And this is where, as I mentioned above, I think Petit may have misdiagnosed the shortcomings of neo-structuralism (or the neo-Brandeisian school, or Antitrust 2.0, or Hipster Antitrust, and so on). In short, these are frameworks that focus first on the number and size of players in an industry and guard against concentration, even in the absence of a causal link between these structural elements and adverse impact on consumer, and/or total welfare. Petit describes neo-structuralism as focusing on rivalry without having an "an evaluative premise" (i.e., an explanation for why big = bad). I'm less sure that it lacks an evaluative premise, rather, I think it might have several (potentially competing) evaluative premises.

Rivalry indeed has no inherent value, it is good – or perceived as good – as a means to an end. If that end is consumer welfare, then the limiting principle on when rivalry is achieving its end is whether welfare is enhanced or not. But many have argued that rivalry could have other potential benefits. For instance, the Antitrust Subcommittee House Report, identifies several potential objectives for competition law: driving innovation and entrepreneurship, privacy, the protection of political and economic liberties, and controlling influence of private firms over the policymaking process. Even if we grant that competition could be a means to achieving these ends, the measure of success for competition laws would have to be the degree to which the ends are achieved. For example, if one argues that competition law should be used to promote privacy, we would measure the success of those laws by whether they do in fact promote privacy, not whether they maintain a certain number of players in an industry. Although, we should also consider whether competition law really is the most efficient and effective means to those ends.

Returning again to merger control, in the existing US regime, and under the Petit proposal, a dominant tech platform might be permitted to acquire a large player in an unrelated market assuming there is no augmentation of market power as a result of the interplay between the two and if the deal is, on net, efficiency enhancing. In simpler terms, if consumers are made better off through lower prices, better services, increased innovation etc. the deal is permitted to proceed. Yet, if antitrust were calibrated, e.g., for a primary purpose of disaggregating corporate control over capital to minimize political influence by large firms, you could see the same transition failing to achieve approval. If privacy were the primary goal, perhaps certain deals would be blocked if the merging parties are both in possession of detailed consumer data without regard to their size or existence of other players in the same space.

The failure of neo-structuralism (etc.) is, in my view, also likely the basis for its growing popularity. Petit argues that the flaw is that it promotes rivalry as an end in itself. I posit instead that neo-structuralism is

flawed because it promotes rivalry as a means and is agnostic to the ends. As a result, people with strongly differing views on the optimal ends of competition law can appear to agree with one another by agreeing on the means and in doing so, promote a competition law framework that risks being untethered and undisciplined. In the absence of a clearly articulated policy goal – whether it is privacy, or economic equality, or diluting political influence, or even consumer welfare – there is no basis on which to evaluate whether any given competition law is structured or applied optimally. If rivalry is to be the means by which we implement our policy goals, how do we know when we have enough rivalry, or too little? We can't.

It is on this point that I think there is more work to undertake in a complete critique of the failings of neo-structuralism (and any other neo-isms to come). In addition to other merits, welfare maximization gives us a framework to hold the construct and application of competition law accountable. It is irresponsible to replace a system that has, as Petit puts it, an "evaluative premise" with one possesses no ends-based framework for evaluation, leaving the law rudderless and susceptible to arbitrary or even selective enforcement.