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Oliver Williamson and the Antitrust Enterprise: Some Perspective and Unfinished Business

To answer the question, "What is institutional and organizational economics (IOE)?" would be to go some way toward illuminating the influence of Oliver Williamson on economics and on the social sciences more generally. There was a time, however, when there effectively was no IOE. The way parties to (possibly complex) exchange organized their collaborations was simply not something that was even cognizable from the perspective of the orthodox, textbook economic theory. It gets worse. From the perspective of the orthodox theory, it was not obvious that anyone should have to concern themselves with organization. Implicit in the established theory was an ambitious and optimistic proposition: Organization is all well and good, but one can analyze the efficiency and design of economic systems without reference to organization – that is, to the messy processes parties to exchange might use to manage their relationships. Organization was just a distraction from the real action. Researchers could ignore those distractions and adopt the ultimate "as if" proposition: the neoclassical theory of decentralized market processes could encompass and digest any relevant inquiry. And, yet, almost anyone else, whether a social scientist or not, might agree that "Organization matters!" But how? Why? What does that mean? Does it matter?

I am not situated to fully unravel the mysteries of the how and why in the space of a short essay. Suffice to say, the optimistic "as if" proposition has left a lot of enduring puzzles about economic organization on the table. For example, it left it to a 21-year old Englishman to observe something so obvious that it was profound. In his 1937, "The Nature of the Firm", a young Ronald Coase could observe that the established theory of his time could not even recognize a role for firms, and yet anyone could look out on the world and see that economies were populated with these pockets of administrative, nonmarket activity (firms). Did this really not matter?

It turns out it does matter, but only after one admits a role for organization. And wherever there is scope for organization, there are tradeoffs. And where there are tradeoffs, there is the question of managing those tradeoffs. That is, there is scope for economic analysis. Hence, "institutional and organizational economics" in all its unavoidably messy glory.

My homework assignment here is to suggest something about the contributions of "Olly" and, by extension, of IOE to the practice of antitrust. One might wonder how it is that a body of theory that still struggles to characterize "the firm" would be situated to illuminate anything about the antitrust enterprise, but there are discrete contributions. I start, however, with the observation that contributions are *right now* being made – and the IOE should participate. Specifically, the Antitrust Division of the US Department of Justice has resurrected efforts to craft *Vertical Merger Guidelines* to complement its well established editions of *Horizontal Merger Guidelines*. How is it that a merger that is "vertical" in that it enables merging parties to join complementary assets and capabilities can harm competition? Do the efficiencies that obtain from combining such assets and capabilities outweigh prospective harm to competition? Finally, can't parties to a prospective merger achieve such efficiencies by contract rather than full-on merger?

These remain difficult questions, but there was a time when the antitrust enterprise admitted little scope for asking such questions much less for admitting efficiencies to the evaluation of mergers. Enter Williamson (1968a). Oliver had just finished an assignment as a Special Economic Advisor to the chief of the Antitrust Division, and he found himself compelled to observe what might have seemed obvious: a merger transaction may make the merged firm a more efficient competitor in a given market; concerns about the merged firm's increase in market power (if any) should be balanced against greater efficiency. Net gains in social welfare might obtain.

Williamson's point mattered, because the prevailing case law as of 1968 would not necessarily credit efficiencies as a rationale for approving mergers. Indeed, Oliver explained that some case law maintained the proposition that efficiencies could comprise a rationale for barring a merger. Indeed, even a generation later, in 2001, the European Commission appealed to a similar rationale when it argued that the proposed merger of General Electric and Honeywell would invest the merged firm with the capacity to compete more effectively and thereby "dominate" certain markets. The "dominance" of the one firm might even discourage other firms from competing vigorously going forward.[1] In contrast, Williamson (1968a) had argued that efficiencies should not be counted against merging parties but could inform an affirmative merger defense.

In recent correspondence a former colleague of mine from the Antitrust Division observed that she had not had reason to give Williamson (1968a) much attention until she found herself early on in her career at the Division advancing the argument that efficiencies should be folded in to merger analysis in an organic way. Having Uncle Oliver to lean on, it turned out, helped to make the case.

My colleague's experience hints at another important aspect of Oliver's contributions to the practice of antitrust: To outside observers, they would have been almost entirely *unseen*. They would have been unseen, because outside observers would not, and do not, have the privilege of observing the important competition for ideas that may obtain with respect to any one antitrust investigation. A more important reason is that Oliver's body of work broadly supports propositions about how vertical integration (and vertical relationships more generally) can be efficiency-enhancing. That is the last thing an enterprising, ambitious young attorney, assigned for the first time to lead an investigation, may want to hear. T'is easier to make one's name pressing matters to litigation and winning glorious battles in court. Closing investigations affords no glory. But to a wily veteran, assembling good reasons to close amount to just that: reasons to close and to move on to matters that would merit more serious (and costly) attentions.

That said, I must credit one wily veteran, Dando Cellini, for volunteering a beautiful interpretation of one of Oliver's general propositions about mergers. We were examining an elaborate financial relationship between two erstwhile competitors. Might a court extend to the

[1] I refer the reader to Schmitz (2002) for useful discussion of some of the unfortunate nuance regarding "dominance" in general and in the GE/Honeywell matter in particular.

financial arrangement, unusual as it was, the status of "passive investment", in which case the court would judge the relationship exempt from antitrust scrutiny? Dando then posed the proposition that the welfare consequences of the existing relationship might be worse than those that would obtain from full on merger, because, presumably, merger would enable the parties to do a better job of deploying their collective assets and capabilities. I can't help but think that Oliver would have smiled at such a clever redeployment of his own ideas.

Dando's sly gambit notwithstanding, Oliver's contributions do actually extend to affirmative rationales for actionable antitrust enforcement. For example, in "Wage Rates as a Barrier to Entry: The Pennington Case in Perspective" (Williamson 1968b), Oliver advanced what antitrust insiders would immediately recognize as a "Raising Rivals' Costs" rationale for opposing certain conduct.

In assembling this short essay, I assembled notes running many pages and spanning many topics. I will have to put those topics aside and will tie things up with just one more observation: Going back to at least the 1930's, just as Ronald Coase was getting his start, the antitrust case law started to develop its own theory of the firm. The theory made contact with questions of delegation and authority in hierarchical structures; with demands for efficient adaptation over the course of long-term exchange; with the assignment of control rights. (One of the better statements of the state of the art might be *Freeman v. San Diego Association of Realtors* 322 F.3d 1133, 9th Circuit 2003. I elaborate on the issues in "The Single Entity Defense in Antitrust", Williamson 2009.) The antitrust enterprise did this without any input from economics and social science more generally. One might, however, expect that the antitrust enterprise to be open to inputs from IOE going forward. The *Vertical Merger Guidelines* provide an immediate opportunity.

In a recent working paper Louis Kaplow observed that contributors to the IOE seem curiously absent from discussion of efficiencies and vertical integration in practical applications such as antitrust. (Kaplow 2020) Kaplow also recognizes, of course, that the issues defy ready formalization in economic models. That is line with George Akerlof's own observations that it may be individually rational for economists to eschew research on important topics that are difficult to (yet) formalize in favor of trendier topics – trendier because they are more amenable to modeling. (Akerlof 2020) The collectively irrational result, as Akerlof indicates in the title of his paper, are "sins of omission". The classic questions of economic organization are classic, because they are hard. But there are demands in the antitrust sphere for new and fresh contributions.

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