What Antitrust Attys Need To Know About Labor Monopsony

By **Eric Posner**

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Readers of Law360 may have noticed that in the last several months, numerous news articles and attorney-authored articles have focused on the role of antitrust law in policing labor market abuses.[1] These articles were published in the wake of a series of dramatic developments in policy, litigation and academic research. But while the policy decisions and cases have received most of the attention, the academic research shows that the problem of labor market concentration is deep, pervasive and likely to produce litigation for years to come. This is the cutting edge of antitrust law, and antitrust lawyers need to educate themselves about it.

Two scandals got the ball rolling. In 2010, the U.S. Department of Justice sued Apple Inc., Google Inc. and other Silicon Valley tech firms for engaging in no-poaching agreements — agreements not to hire away each other's software engineers — in violation of the Sherman Antitrust Act. The defendants quickly settled for a small fine, but subsequently paid hundreds of million dollars to settle a class action brought on behalf of workers.[2]

In 2016, Jimmy John's Franchise LLC settled a lawsuit brought by the attorneys general of Illinois and New York who alleged that the sandwich chain imposed noncompete clauses on its low-wage sandwich makers. That case, too, spawned a class action. It also led to a series of cases brought both by governments and private litigants against franchises — including McDonald's and Arby's — for using no-poaching agreements to limit competition for labor among the members of a franchise. The Justice Department has entered the fray by filing statements of interest in many of these cases in which it disagreed with some of the theories of the plaintiffs.[3]

While the two scandals involved very different labor markets — high-skill in the first case, low-skill in the more recent group — they had a great deal in common. The defendants allegedly conspired or (in the case of Jimmy John's) acted unilaterally to cartelize the labor market in violation of the antitrust laws. Economists use the term "labor monopsony" to refer to this type of behavior.

"Monopsony" is the mirror-image of "monopoly": it refers to a market in which there is a single buyer rather than a single seller. A labor monopsony exists when that buyer buys labor rather than supplies. Just like in the more familiar product-market case, a true single buyer of labor is rare, but antitrust problems begin when a few such buyers dominate a market — that is, the labor market is concentrated. Each employer enjoys labor market power, and it can use that labor market power — alone or in collaboration with other employers — to suppress wages.

Economists have long understood that labor monopsony can exist. The classic example was the company town like Pullman, Illinois, where a single employer employed most of the workforce in the area. But company towns no longer exist. Most Americans live in densely populated urban areas, and when we think about cities, we imagine a large number of employers vying to hire workers. Perhaps for this reason, economists for a long time assumed that labor markets are competitive. And if labor markets are competitive, then they do not pose any problems for antitrust law.

But beginning just last year, new research has shown that this assumption is wildly inaccurate. To understand this research, you need to understand a few concepts. A labor market consists of a type of occupation (like accountant) for a particular area (usually defined as a commuting zone). A labor market is concentrated if a small number of employers employ most or all of the people who are qualified (by experience, training or credentials) to work in an occupation in question.

Economists usually measure concentration using the Herfindahl-Hirschman Index, which is equal to the sum of the squares of the market share of each firm in the market. For example, if only two firms employ all the accountants in a commuting zone, and each firm has market share of 50%, then the HHI is 5,000 ($50^2 + 50^2$). If 20 firms have equal shares of the employment market, then the HHI is 500 ($5^2 \times 20$). As the number of firms increase, HHI approaches 0, which is the economist's ideal of perfect competition; if only one firm exists, HHI is 10,000 (100^2). Under Justice Department guidelines, an HHI of 1,500 is a matter of concern; an HHI of 2,500 means a market is "highly concentrated," often justifying government intervention, for example, to block a merger.

The new studies have found that labor market concentration is extremely common. One study found that 60% of labor markets in the Unites States, accounting for about 20 percent of employment, have an HHI over 2,500.[4] Other studies, using different data and methods, also provide strong evidence of pervasive labor market concentration.[5] The studies also show, consistent with economic theory, that wages decline as HHI increases. For example, the study cited above finds that a 10% increase in HHI implies a decline of wages by 0.4% to 1.5%.

The key to understanding this research is to recall that not all Americans live in big cities. Labor market concentration is greatest in rural areas, suburbs, small or medium-size towns, and other lightly populated areas where few employers are located. Putting aside CEOs and other highly compensated employees, labor markets tend to be small: People rarely commute more than an hour, or move across the country in search of higher-paying jobs. This means that employers can pay them less than the value of their contribution to the firm.

Some readers may be tempted by the thought that if lower wages may be a hardship for workers, at least those lower wages will be passed on to consumers in the form of lower prices for goods and services. But that is a mistake. The reduction in wages must result in less employment (as some workers exit the market rather than accept low wages), which in turn means lower production. Lower production means higher prices for consumers. Just like monopoly, monopsony leads to waste — less economic activity as well as lower wages.

For lawyers, the new research has important consequences for practice. If most labor markets are highly concentrated, then many otherwise innocent business decisions of employers may give rise to antitrust liability.

Consider, for example, mergers and acquisitions. A firm that operates one of two chicken processing plants in a rural area might consider buying the other plant. From the usual product-market standpoint, the acquisition rings no antitrust warning bells because the product market — processed chickens — is national in scope. The acquisition will not affect chicken prices because multiple producers, scattered throughout the country, will continue to compete. But the labor market is local. And if the labor market is concentrated, then the acquisition will increase labor market concentration and hence reduce wages. That's likely an antitrust violation. One of the recent studies on labor monopsony looks at mergers and indeed finds that those mergers that significantly raised labor market HHIs also reduced wages.[6]

Similarly, a firm that requires its employees to sign noncompete agreements will not normally face antitrust liability. But that could change if the labor market in which the firm operates is concentrated. When the labor market is concentrated, the employee has fewer alternative employment options, and the noncompete can also prevent other firms from entering the market because they cannot hire away qualified workers. The no-poaching agreements used within franchises are also more vulnerable to antitrust challenge where labor markets are concentrated than where they are competitive.

The Obama administration expressed concern about labor monopsony back in 2016,[7] and while the Trump administration has not officially expressed a view on the topic, both the Justice Department and the Federal Trade Commission appear to be taking the problem seriously.[8] As empirical research continues to document and clarify the scope of the problem, expect government agencies and private litigants alike to bring more antitrust cases that target antitrust abuses in labor markets. As well they should.

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[1] See, e.g., Bryan Koenig, DOJ's No-Poach Stance Called 'Wasteful And Inappropriate.' Law360, May 2, 2019, https://www.law360.com/articles/1155854/doj-s-no-poach-stance-called-wasteful-and-inappropriate-; Jee-Yeon Lehmann, Federico Mantovanelli, Rebecca Scott and Samuel Weglein, Assessing The Effect Of Mergers On Labor Markets, Law360, January 3, 2019, https://www.law360.com/articles/1112541/assessing-the-effect-of-mergers-on-labor-markets; Carolina Bolado, Fla. Oncologists Try To Save Antitrust Suit Over Noncompetes, Law360, April 23, 2019, https://www.law360.com/articles/1152536/fla-oncologists-try-to-save-antitrust-suit-over-noncompetes.

[2] Robin van der Meulen and Brian Morrison, An Update On Anti-Poach Enforcement And Class Actions, Law360, July 11, 2018, https://www.law360.com/articles/1062322/an-update-on-anti-poach-enforcement-and-class-actions.

[3] Boris Bershteyn, Karen Hoffman Lent, Tara Reinhart and Zachary Siegler, DOJ Is Trying To Rein In Franchise No-Poach Suits, Law360, February 19, 2019, https://www.law360.com/articles/1130056/doj-is-trying-to-rein-in-franchise-no-poach-suits.

[4] José A. Azar, Ioana Marinescu, Marshall I. Steinbaum and Bledi Taska, Concentration in US Labor Markets: Evidence From Online Vacancy Data (Nat. Bureau of Econ. Res. Working Paper No. 24395, 2019), https://www.nber.org/papers/w24395.

[5] See, e.g., Efraim Benmelech, Nittai Bergman, and Hyunseob Kim, Strong Employers and Weak Employers: How Does Employer Concentration Affect Wages?, (NBER Working Paper No. 24307, 2018), https://irs.princeton.edu/sites/irs/files/w24307.pdf;, Kevin Rinz, Labor Market Concentration, Earnings Inequality, and Earnings Mobility (Center for Economic

Studies, U.S. Census Bureau Working Paper No. 2018-10,
2018), https://kevinrinz.github.io/concentration.pdf.

[6] Benmelech, et al., supra.

[7] Council of Economic Advisors, Labor Market Monopsony: Trends, Consequences, and Policy Responses, October 2016, https://obamawhitehouse.archives.gov/sites/default/files/page/files/20161025_monopsony_labor_mrkt_cea.pdf.

[8] See U.S. Department of Justice, Antitrust Division Update Spring 2019, https://www.justice.gov/atr/division-operations/division-update-spring-2019/no-poach-approach; "FTC Considers Workers in Deal Reviews," Global Competition Review, October 4, 2018, https://globalcompetitionreview.com/article/usa/1175255/ftc-considers-workers-in-deal-reviews.