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Monopsony and the Business Model of Gig Economy Platforms – Note by Marshall Steinbaum

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Monopsony and the Business Model of Gig Economy Platforms

By Marshall Steinbaum*

1. The Competition Committee's background note for this meeting is an excellent summary of the empirical research done to date on labor market monopsony and the suggestions that have been made regarding its application to competition policy.¹ For that reason, I will not summarize the same material, but rather focus on one part of it: the competition policy implications of the labor market platforms that, in general, rely on labor from workers who are not legally employed by the platform itself.

2. This so-called "gig economy" business model has survived legal challenges related to employment misclassification brought in US jurisdictions. Most recently, the National Labor Relations Board's general counsel issued a letter to the effect that Uber drivers are not employed by Uber and thus do not enjoy federal protections for collective bargaining.² Earlier this year, the Department of Labor found that the service providers on an unnamed digital labor platform are not employees and are thus exempt from the federal Fair Labor Standards Act.³ In both cases, the substance of the regulators' conclusions were that the platform does not exercise sufficient control over service providers to qualify them as employees, and further that the service providers retain exposure to "profit and loss." Thus, they are properly classified as independent contractors without the protections employers owe to employees: social insurance contributions, minimum wage, membership in a company health insurance plan, and the like.

3. The continued deference of labor law enforcement to the independent contractor business model typical of the labor platforms raises competition policy concerns: if gig economy workers are not employed, then why is the platform empowered to set prices and allocate customers to individual, notionally independent service providers, as well as to supervise and evaluate their performance on the job, when these would seem to be analogous to price-fixing, market division, exclusionary practices, and other core antitrust concerns? The theme of this note is that the prevalence of the gig economy business model reflects the eroded jurisprudence of vertical restraints in competition law, thereby creating a large legal gray area where there was once a sharp boundary between the jurisdiction of labor law (regulating the exercise of power within firms) and competition law (regulating

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¹ "Competition Concerns in Labour Markets," Background Note, Directorate for Financial and Enterprise Affairs Competition Committee (Organization for Economic Cooperation and Development, 2019), [https://one.oecd.org/document/DAF/COMP\(2019\)2/en/pdf](https://one.oecd.org/document/DAF/COMP(2019)2/en/pdf).

² Peter Robb, Uber Technologies Inc., No. 13- CA-163062 (National Labor Relations Board April 19, 2019); Noam Scheiber, "Uber Drivers Are Contractors, Not Employees, Labor Board Says," *New York Times*, May 15, 2019, New York edition, <https://www.nytimes.com/2019/05/14/business/economy/nlrb-uber-drivers-contractors.html>.

³ Keith E. Sonderling, "US Department of Labor Wage and Hour Division Opinion Letter on FLSA Employment Classification for Gig Economy Workers," Opinion Letter, April 29, 2019, https://www.dol.gov/whd/opinion/FLSA/2019/2019_04_29_06_FLSA.pdf.

the exercise of power between firms). This gray area permits the gig economy platforms to exercise power and control unhindered by liability from either source.

4. This note first summarizes the evolution from an antitrust system suspicious of vertical restraints and the imbalance of power they represent between related-but-separate entities to one deferential to them. It then analyzes how the practices typical of the gig economy platforms could be approached as anti-competitive vertical restraints. Finally, it proposes a return to the older jurisprudence, better-grounded in new research about how labor markets work. Throughout, the focus will be exclusively on the history and current status of antitrust's treatment of vertical restraints imposed by dominant firms in the United States.

1. A Brief History of the Jurisprudence of Vertical Restraints

5. The district court judge's opinion in the 1951 case *United States v. Richfield Oil Company* concerned the exclusive supply contracts that a dominant oil refiner imposed on its affiliated retailers, which the court held to be independent contractors.⁴

When, in law, we speak of "an independent contractor" or "an independent business man" we deal with a practical concept, not with a philosophical phrase. We mean a person who, in the performance of a particular contract, or in the conduct of his business, acts chiefly for himself and for his own benefit and profit, and not for others and the benefit and profit of others...

And when a corporation like Richfield deals with such an enterprise, it cannot be said to be dealing with itself, as though the estate it created were nothing and the person in charge, to whom possession was turned over, is a mere employee because, under clauses not contained in the contract, they supervise his actions, regulate, to some extent, his personal appearance, and do other things, some distinctly illegal, as will presently appear.

6. The court went on to find liability in the oral restraints of trade that Richfield imposed on retailers, on pain of termination of their lease: that they had to source their gasoline solely from Richfield's refineries, and that they could only sell auto parts sourced from Richfield's supply contracts.

Richfield cannot deny to the dealers the right to deal with other suppliers as to their products, or to deny to such suppliers access to the dealers, so that these varied products may reach the public, whose protection the anti-trust laws seek. The law, as the Supreme Court has stated, "does not compel competition". But restrictive contracts are condemned because of their "denial to commerce of the supposed protection of competition."

7. The court thus enjoined the restraints as violations of Section 1 of the Sherman Act and Section 3 of the Clayton Act, and it enjoined the use of Richfield's 24-hour termination clause to enforce any restrictive conditions. The decision reflected antitrust's suspicion of vertical restraints as mechanisms of control extending across the firm boundary, unlike the control within firm boundaries that is the basis for the legal concept of employment.

⁴ *United States v. Richfield Oil Corp.*, 99 F. Supp. 280 (United States District Court S. D. California, Central Division 1951).

8. The 1964 Supreme Court case *Simpson v. Union Oil Company of California* has a similar flavor, if different specifics and a different vertical restraint at issue.⁵ In that case, an independent gasoline dealer protested the termination of an annual lease due to his violation of minimum resale price maintenance, and the defense Union Oil offered was that the dealer did not own the gasoline because it was sold on consignment from Union Oil, so it was lawful for the refiner, its legal owner, to set its price. The court found that what might be a lawful contract when undertaken by two parties bilaterally—a consignment sale—was an antitrust violation when used to control a whole dealer network.

The exclusive requirements contracts struck down in Standard Oil Co. v. United States, 337 U. S. 293, were not saved because dealers need not have agreed to them, but could have gone elsewhere. If that were a defense, a supplier could regiment thousands of otherwise competitive dealers in resale price maintenance programs merely by fear of nonrenewal of short-term leases...

Dealers, like Simpson, are independent businessmen; and they have all or most of the indicia of entrepreneurs, except for price fixing... Practically the only power they have to be wholly independent businessmen, whose service depends on their own initiative and enterprise, is taken from them by the proviso that they must sell their gasoline at prices fixed by Union Oil. By reason of the lease and "consignment" agreement dealers are coercively laced into an arrangement under which their supplier is able to impose noncompetitive prices on thousands of persons whose prices otherwise might be competitive.

9. In these instances, the legal device could not cloak the anti-competitive intent of the business model its use on such a large scale brought into effect. Thus, in these two cases, the court took issue with two different contracts (short term leases and consignment sales) that, analyzed independently, were perfectly legal, because they were used to enforce vertical restraints that had long been recognized as (at least potential) antitrust violations: exclusive dealing and resale price maintenance.

10. With regard to the two specific cases discussed here (taking the facts of the case at face value), consumer welfare was unambiguously harmed by the conduct at issue and thus the two decisions in favor of the plaintiff would have passed muster under the consumer welfare standard. Under a standard in which all that matters for assessing harm to competition is final output, the evaluation of the findings is more ambiguous. The conduct at issue probably reduced output in *Simpson* and had ambiguous effects in *Richfield Oil*. But neither desideratum is true to each court's actual motivation, which was that the dominant firm had used its dominance to reduce competition and expropriate surplus. What distinguishes the whole of mid-20th-century vertical restraints jurisprudence from what followed is the attention of the court to the relative bargaining power between related but separate parties to a transaction, and how this asymmetry could be used by the more powerful refiner to reduce competition in order to shift the surplus generated by the economic relationship in favor of himself. Establishing this was sufficient to adjudicate the antitrust case against the two dominant defendants.

11. That is in contrast with the way the jurisprudence of vertical restraints evolved after the late 1970s, when the federal judiciary became much less worried about inequalities of bargaining power and the anti-competitive effects that could be effectuated through them and more concerned about efficiencies, specifically efficiencies arising from the control of

⁵ *Simpson v. Union Oil Co. of Cal.*, 377 US 13 (Supreme Court 1964).

a distribution network by a single manufacturer. The Supreme Court decision in *Continental Television v. GTE Sylvania* put it as follows: “Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of products.” Evidence regarding said efficiencies was not offered in either *Richfield Oil* or *Simpson*, presumably because it would have been legally irrelevant. But the assumption that efficiencies must have been there in any vertical restraints case colored subsequent economic analysis.

12. In their discussion of *Simpson*, Blair and Kaserman (1983) asserted that there were three possible motivations for RPM: to enforce a manufacturer’s cartel, to enforce a dealer’s cartel, and to provide an incentive for dealers to enhance the brand with ancillary services.⁶ Since the former two reduce output and the latter ostensibly increases it, they proposed that minimum RPM be adjudicated under the Rule of Reason, and specifically that the effect of the restraint on output be the desideratum for an antitrust violation. Notably, the actual motivation for RPM discussed in the case—the appropriation of surplus in favor of the dominant firm—was assumed away by Blair and Kaserman. The operative assumption is that dealers subjected to the restraint could easily disaffiliate from Union Oil of California and find a different supplier under circumstances where its only effect would be to transfer surplus. That assumption is analogous to the assumption discussed in this meeting: that labor markets are competitive, and therefore that exploitation of labor is impossible, or at the very least, that it is of no import for antitrust analysis.

13. In fact, in discussing exclusionary practices such as those at issue in *Richfield Oil*, Blair and Kaserman went so far as to praise them as a positive good, rising to the level of an “efficiency” that could form a defense in its own right to anti-competitive vertical conduct, and certainly as part of a larger case that antitrust scrutiny of such conduct be reduced or eliminated. They write “The supplier may get improved product promotions from those with exclusive contracts. There will be added incentive to promote the seller’s product vigorously if that is all the buyer has to sell to the final consumer. Thus, the supplier can be sure that each of the distributors will work very hard on the seller’s behalf.” While it is indeed likely that the ability to coerce dealers would cause them to work harder on behalf of their supplier, the authors provide no empirical basis for this assertion, nor do they question its significance for the dealers’ welfare or for aggregate welfare. It is in statements like this that we can observe the inconsistency between the consumer welfare standard, which would supposedly be indifferent to negative welfare effects to mere “competitors” such as gasoline retailers (and notwithstanding the actual negative impact of the restraints on consumer welfare, as discussed above) with more intuitive notions of aggregate economic welfare, such as Mark Glick discusses in a more generalized welfare-theoretic context.⁷

14. The received history of antitrust treats *GTE Sylvania* as a turning point, the first appearance of the Chicago School or even of “economics” in antitrust caselaw, and thus the beginning of the modern era. But a recent paper by Brian Callaci paints a different historical picture. He shows that the case was in fact the culmination of a long campaign

⁶ Roger D. Blair and David L. Kaserman, *Law and Economics of Vertical Integration and Control* (New York: Academic Press, 1983).

⁷ Mark Glick, “The Unsound Theory Behind the Consumer (and Total) Welfare Goal in Antitrust,” *The Antitrust Bulletin* 63, no. 4 (December 1, 2018): 455–93, <https://doi.org/10.1177/0003603X18807802>.

by franchisors to retroactively legalize their business model of semi-controlled but legally independent distributors after the 1967 case *United States v. Arnold, Schwinn & Co.* subjected non-price vertical restraints to per se illegality.⁸ The net effect of the post-*Sylvania* vertical restraints jurisprudence was to create a wedge between the legal and the economic definitions of the firm: suppliers can legally outsource their distribution while retaining economic control over it, without running afoul of antitrust. If we're looking for the antecedents to the current labor platform business models, it is to be found there. And notably, throughout both the court opinions bringing into effect the weakening of antitrust vertical restraints jurisprudence and the scholarly literature that provided justification for them, the assumption of free entry and perfect competition among dealers is maintained as part of the apparatus that treats antitrust claims they might bring (or that might be brought on their behalf) as efforts to protect competitors rather than competition. It is this maintained assumption that the contemporary evidence about the pervasiveness of labor market power calls into question.

2. Restrictive Practices by Gig Economy Labor Platforms

15. When gig economy platforms first appeared on the scene, enabled by near-universal penetration of GPS-enabled mobile devices, the economic research tended to treat them as facilitating bilateral matching between atomistic service providers and customers, reducing or eliminating search frictions and thus bringing markets closer to an ideal of competitive equilibrium.⁹ More recently, the platforms have started to present themselves instead as dominating the market and causing it to operate more efficiently through their direct supervision and control over market participants.¹⁰ The latter interpretation places them in the role of either dominant supplier (in the event that service providers on the platform are understood to transact directly with customers) or as two-sided platform transacting in both upstream and downstream markets. The distinction between the two of course has legal significance: the former tends to be preferred when the platforms face potential sectoral regulation in whatever sector they happen to operate in, as well as when resisting employment classification, while the latter makes the better case for antitrust immunity, especially following the Supreme Court's decision in *Ohio v. American Express* carved out special, more lenient treatment for two-sided platforms.¹¹

16. For the analysis here, it does not really matter whether the platform sits between service providers and customers or whether it supplies its service providers, only that it is dominant. The former is more directly implicated by the question of monopsony power,

⁸ Brian Callaci, "Vertical Dis-Integration and the Creation of a New Business Form: Franchising 1960-1980" (Working Paper, 2018).

⁹ For example, see Nicholas Buchholz, "Spatial Equilibrium, Search Frictions, and Dynamic Efficiency in the Taxi Industry" (Working Paper, 2019), https://scholar.princeton.edu/sites/default/files/nbuchholz/files/buchholz_taxi_2018.pdf; Peter Cohen et al., "Using Big Data to Estimate Consumer Surplus: The Case of Uber," *NBER Working Papers*, no. 22627 (2016); Jonathan V. Hall, John J. Horton, and Daniel T. Knoepfle, "Labor Market Equilibration: Evidence from Uber" (Working Paper, 2017).

¹⁰ For an example of the latter: Meng Liu, Eric Brynjolfsson, and Jason Dowlatabadi, "Do Digital Platforms Reduce Moral Hazard?," *NBER Working Papers*, no. 25015 (2018).

¹¹ *Ohio vs. American Express*, 838 F. 3d 179 (Supreme Court of the United States 2018).

while the latter looks more like the restraints at issue in *Richfield Oil* and *Simpson*. And the question of whether the platforms buy from service providers or sell to them would affect the interpretation of price-fixing in the final output market, for example: is it RPM, or is it managing a cartel? Nonetheless, the core issue of the exercise of power in an affiliated network of service providers does not turn on the question of whether the platform is up or downstream of them. Whichever way we choose to represent them, their practices appear analogous to vertical restraints, as do their motives: to use market power to appropriate surplus.

17. First of all, many, though not all, of the gig economy platforms fix the prices that their independent contractor service providers charge to consumers, whether we interpret this as RPM or as cartelization.¹² This was the issue in the private class action *Meyer v. Kalanick*, but since that case was sent to arbitration, there has been no action by public enforcers to target such price fixing as an antitrust problem.¹³ The platforms that do set prices for the customer-service provider transactions have also moved toward individualized pricing as the platforms have amassed data on each individual user's demand elasticity, so it's not obvious whether the price-fixing reduces or increases prices on average.¹⁴ What is clear, however, is that the platforms that do price-fix use their control over prices to widen the wedge between what consumers pay and what service providers earn.

18. The platforms also utilize non-linear bonus-based pay policies to induce service providers to work in areas and at times that are most favorable to the platform, on threat of termination. The mechanism is to pay workers less than their reservation wage on a minute-by-minute basis, only making a shift worthwhile if it is completed on the schedule and in the location the platform determines.¹⁵ This algorithmic management at a distance is useful for evading labor laws that hinge on direct control and can be gamed with the simulacrum of choice on the part of workers. It is also analogous to market division or territorial restrictions in the antitrust context.

19. In some cases, workers are also penalized for "multi-homing," that is, activating more than one platform concurrently and selecting the gig with the best terms.¹⁶ In the past, when Uber utilized surge pricing, it would penalize drivers for foregoing non-surge fares in expectation that a surge might make their time more valuable imminently.¹⁷ These practices are akin to exclusive dealing and exclusive supply contracts respectively, forcing dealers to forego more economic opportunities in favor of those that take place on the dominant firm's terms. In its SEC filings in preparation for its recent Initial Public Offering,

¹² Julian Nowag, "When Sharing Platforms Fix Sellers' Prices," *Journal of Antitrust Enforcement* 6, no. 3 (2018): 382–408, <https://doi.org/10.1093/jaenfo/jny007>.

¹³ Marshall Steinbaum, "Antitrust Implications of Labor Platforms," *CPI Antitrust Chronicle*, 2018.

¹⁴ Alex Rosenblat, *Uberland: How Algorithms Are Rewriting the Rules of Work* (Oakland, California: University of California Press, 2018), 121–25.

¹⁵ Rosenblat, 138–67.

¹⁶ Ignacio Herrera Anchustegui and Julian Nowag, "Buyer Power In The Big Data And Algorithm Driven World: The Uber & Lyft Example," September 15, 2017, <https://www.competitionpolicyinternational.com/buyer-power-in-the-big-data-and-algorithm-driven-world-the-uber-lyft-example/>.

¹⁷ Rosenblat, *Uberland*, 137.

Uber wrote that in more competitive markets, it is under pressure to provide more generous bonuses to drivers to keep them on Uber's platform, an inducement that might well be understood as a pro-competitive effect.¹⁸ On the other hand, if bonus policies serve to tie drivers more closely to a single platform and prevent them from multi-homing, then their use in competitive markets is analogous to the use of noncompete clauses where they are of greater benefit to employers, i.e., where they face the more imminent likelihood of poaching. If that is the case, then the harm to competition is greater the more the restraints are used.

20. GPS enables both Uber and its customers to track drivers' route-finding in real time and ensure drivers follow the shortest-distance routes, rather than the ones that earn them the most.¹⁹ This too could be analogized to exclusive supply, in that it enforces Uber's interest as to routes taken over those of drivers and potentially of customers. Finally, deactivation from a labor platform is akin to the lease termination through which dominant firms like Richfield Oil enforced its exclusionary contractual terms.

3. Labor Market Monopsony and the Gig Economy Business Model

21. As previously mentioned, all of the vertical restraints imposed by dominant gig economy platforms are enabled by the pervasiveness of employer monopsony power. The idea that service providers might switch to a different platform, or even a different job, as a result of the restrictions placed on them or the reductions in pay associated with those restrictions, depends on the actual availability of outside employment options. The empirical literature cited in the Competition Committee's background note pertains to the availability of such alternatives, and the clear implication is that employers (economically if not legally) have substantial leeway with which to dictate wages and terms of employment. The innovation in the empirical literature is that labor markets are surprisingly monopsonized relative a perfectly competitive baseline, but given actual estimates of firm-specific labor supply elasticities,²⁰ the real anomaly is that employers do not use more of the considerable monopsony power that they do possess. In other words, wages are surprisingly high, not surprisingly low. In that case, the innovation of the gig economy labor platforms is that they in fact make use of monopsony power that more traditional employers have not yet figured out how to deploy in their own favor.

22. The implication of the analogy of labor platforms to supplier-distributor networks discussed in the first section of this note is the potential for antitrust liability in the current business models of those platforms, given that they continue to avoid employing their service providers. The response might well be that service providers of this kind are mere "competitors," not consumers, and hence their welfare is not of concern to antitrust

¹⁸ "Uber Technologies, Inc. S-1 Registration Statement" (United States Securities and Exchange Commission, April 11, 2019), <https://www.sec.gov/Archives/edgar/data/1543151/000119312519103850/d647752ds1.htm>.

¹⁹ Liu, Brynjolfsson, and Dowlatabadi, "Do Digital Platforms Reduce Moral Hazard?"

²⁰ José Azar, Ioana Marinescu, and Marshall Steinbaum, "Measuring Labor Market Power Two Ways," *American Economic Association Papers & Proceedings*, 2019; Douglas A. Webber, "Firm Market Power and the Earnings Distribution," *Labour Economics* 35 (2015): 123–34; Arindrajit Dube et al., "Monopsony in Online Labor Markets," *American Economic Review: Insights* 1, no. 1 (2019).

enforcers. But that is not consistent with the response among antitrust officials and former officials to the empirical literature on labor monopsony. The claim there is rather that antitrust protects competition in labor markets just as much as it protects competition in final output markets notwithstanding the consumer welfare standard, that powerful buyers or cartels of buyers are just as liable as powerful sellers or cartels of sellers, and that consumer price effects are not necessary to establish harm to competition.²¹ On that reasoning, if labor market monopsony is indeed pervasive and if it is caused by anti-competitive conduct or market structures, then the antitrust laws can be properly aimed in that direction. Insofar as there has been relatively little historical enforcement in this area, that may represent a fault in enforcement priorities, but not of underlying antitrust principles.

23. As we have seen, the conduct at issue in vertical restraints cases was very likely to have harmed consumers and thus to be cognizable by antitrust operating under a consumer welfare standard. But the precedents in this area are highly deferential to the possibility of pro-competitive efficiencies arising directly from the exercise of vertical control, even where those ostensible efficiencies have never been verified in empirical fact, either on a case-by-case or economy-wide basis. And consumer welfare was never the motivation for antitrust to concern itself with the exercise of power in supply chains and the resulting expropriation of surplus on the part of dominant firms from their counterparties, when antitrust did so concern itself. So in the event enforcers choose to prioritize the gig economy labor platforms for competitive scrutiny, abandoning the preoccupation with consumer welfare is probably a necessary component of doing so.

²¹ Maureen Ohlhausen, “Letter to Senator Cory Booker,” December 1, 2017; C. Scott Hemphill and Nancy L. Rose, “Mergers That Harm Sellers,” *Yale Law Journal* 127, no. 7 (2018): 2078–2109.