Four Reasons Why Senator Warren's Public Utility Proposal Will Backfire

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Senator Elizabeth Warren recently offered a new proposal to break up tech companies, which she is calling platform utility regulation. If put in place, companies that have annual global revenue of $25 billion or higher and that provide an online marketplace, an exchange, or a platform would be broken up, while all platforms, regardless of size, would be subject to a new series of regulations. Here are four reasons why the proposal will backfire.

Reason One: The Proposal Won't Induce Competition, But Chaos

Under Warren's proposal, the companies would be prohibited from owning both "the platform utility and any participants on that platform." Apple and Google would be prohibited from preloading apps on their mobile operating systems. In its strictest form, this rule would mean a structural separation between the advertising side of the platform and the users. Without both sides of the market, there is no business model. As Michael Moritz, a major investor in Google, said of those early years before the ad side was combined with users, "We really couldn't figure out the business model. There was a period where things were looking pretty bleak." Because these businesses depend on the combination of the two sides, any action meant to break them up would be a death knell.

Moreover, all platforms would be required to engage in "fair, reasonable, and nondiscriminatory dealing with users," swinging open the door to regulation. Because these terms are hard to define, an agency would need to be given wide latitude, much like the amorphous public-interest standard at the Federal Communications Commission (FCC). As former FCC Commissioner Glen Robinson explained, this standard "is vague to the point of vacuousness, providing neither guidance nor constraint on the agency's action." Something similar would be expected for platform regulation under this proposal.

Reason Two: The History of Breakups Isn't Pretty

Warren argues that her separation proposal and regulations "would restore competition to the tech sector," like the United States accomplished in an earlier era of trust busting. But the American Action Forum (AAF) previously tackled this history and came to the opposite conclusion, as have other researchers. The goals of lower consumer prices, more innovation, and higher output don't often happen in the wake of breakups.

It is also a simplification to claim that "in the Gilded Age, waves of mergers led to the creation of some of the biggest companies in American history?—?from Standard Oil and JPMorgan to the railroads and AT&T." Standard Oil was formed in wake of the first antitrust law, the Sherman Act, which caused a merger wave. Yet, the discovery of the Spindletop oil field in Texas is generally credited with toppling the Standard Oil empire. JPMorgan, while often derided, has never been broken up, making it a confusing example. Finally, AT&T got a government-granted monopoly in the Kingsbury Commitment in 1913 that was later pulled apart by the

Department of Justice in the 1980s. If we are to look at the past for guidance, we should recognize just how lackluster the results were when companies were broken up.

Reason Three: The Decline in Entrepreneurism Has Many Causes

Warren blames large platforms for a decline in entrepreneurism, but there are long-term forces at work. For one, a decline in startups was predicted by Nobel winning economist Robert Lucas back in 1978, who first modeled the inverse relationship between productivity and entrepreneurship rates. The model has been adapted extensively, and is supported by research between countries, and historical work in the United States, Canada, Germany, Indonesia, Japan, South Korea, and Thailand, all finding this inverse relationship.

Indeed, productivity goes a long way to explain the shifts in entrepreneurship rates. Nicholas Kozeniauskas, a recently minted economist at New York University, found that the decline in entrepreneurship has been more pronounced for industries with higher education levels, such as tech. Overall, "an increase in fixed costs explains most of the decline in the aggregate entrepreneurship rate." Yet Warren's policy, by making economies of scale more difficult, would raise fixed costs—undercutting this idea's policy goals.

Reason Four: All Combined, The Changes Would Be Radical

Finally, Warren argues that nothing will substantively change: "You'll still be able to go on Google and search like you do today. You'll still be able to go on Amazon and find 30 different coffee machines that you can get delivered to your house in two days. You'll still be able to go on Facebook and see how your old friend from school is doing."

But this couldn't be further from the truth. Breaking up tech companies would be a difficult and technically messy process, as AAF has explained. There wouldn't be more competition or better options for consumers, but the destruction of viable and important businesses. Government agencies would also have to be involved and companies would begin to second guess their decisions. In all, subjecting platforms to utility regulation might seem like a modest proposal, but the idea is actually quite radical.