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The State of Labor Market Competition: The Treasury's View and Potential Impact and Regulation on Employers

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On March 7th, the Treasury Department released a draft report entitled "The State of Labor Market Competition" (herein "the report" or "the Treasury"), which addressed the level of concentration and anti-competitive labor practices in the U.S. economy.[1] The report claimed to reaffirm the current administration's executive orders regarding promoting competition in labor markets and examines possible implications.

The stated purpose of the Treasury's report is to summarize the "prevalence and impact of uncompetitive firm behavior in labor markets". The Treasury provides a summary of economic theory regarding labor markets before analyzing a selection of academic literature and discussing examples of firm behavior in select industries. The report concludes by addressing current policies being enacted by the Biden administration and government agencies which relate to labor market competition. As discussed in more detail below, the report describes the government as "committing to the vigorous enforcement of antitrust laws in labor markets". As a result, the federal government is scrutinizing firms which, it argues, exhibit characteristics of a "monopsony" – i.e., firms that supposedly have, to some degree, control over the labor market and the wages paid to its employees.

I. WHAT IS MONOPSONY?

To understand the issues raised by the Treasury report, it is useful to first understand how economists think about "monopsony power". As a reference point, the more commonly known theory of "monopoly power" can be described as a single product market, with a single seller, and is often associated with competition law due to the monopolist's potential ability to raise the prices paid by consumers. A "pure" monopsony on the other hand can be described as a labor market with a single buyer (i.e., a firm that "buys" labor). A classic example of this would be a "company town"—a small town in which the largest (or only) employer is a coal mine, and nearly all residents work for the mine, with little (or zero) outside options for employment.

In this theoretical market structure, a firm can choose to pay its employees a *lower* wage, at the cost of certain employees being unwilling to work at this lower wage. This causes an inefficiency in the labor market in which the firm can raise its profits by lowering the wages paid to all workers, to a level below that of an equivalent

[1] U.S. Department of the Treasury, "The State of Labor Market Competition", March 7th, 2022, ("Treasury Report"), available at, https://home.treasury.gov/system/files/136/State-of-Labor-Market-Competition-2022.pdf

job in a hypothetical perfectly competitive market.[2] In practice, economic realities will dictate if the potential monopsonist can successfully implement this strategy. For example, if the firm's employees have the ability to easily move to another occupation, industry, or city, the firm would not be able to reasonably mark down the employee's wages without losing its workforce. A theoretical monopsonist will be less effective in profitably reducing wages if the "elasticity of labor supply" is high — meaning that for large decreases in wages, many workers would be unwilling to accept that decreased wage. Similarly, outside firms may be able to move into the area to take advantage of the relatively cheap labor, thereby raising firm wages.

As the report correctly explains, a "pure" monopsony example is "an inappropriate descriptor for labor markets" in the United States. However, the Treasury points to the theory that "all employers, to varying degrees, possess market power", and in particular through "frictions" or imperfect information in the hiring and employment process. This is described as a "search and matching" framework, through which job searching is analyzed from the individual viewpoint of both the employee and the employer. The report states that employers are "aware of these frictions" and may be able to "discount wages while retaining their workforce."[3]

II. Labor Practices that Agencies Intend to Focus On

The Treasury's view is that individual firms can hold monopsony power not only if they are a single dominant employer in a given labor market, but more generally if a firm holds some degree of monopsony power through labor market frictions. The report highlights several examples of labor market practices which can lead to monopsony power, and as a result, may attract the attention of regulatory agencies and policymakers. One example relied on by the Treasury is a study of mergers amongst large firms and the occupational-specific impact of the merger, particularly for skilled workers. Another example identified by the Treasury is low-wage or low-skilled employees who may face job search frictions due to a lack of skills that would give them bargaining power to negotiate the terms of their employment.[4] While the former may be thought of more broadly in the environment of a "pure monopsony" post-merger, the latter may be more representative of the search and matching framework discussed above.

Using hospital mergers to analyze the effect of monopsony power, the report discusses how "consolidation in [a] product market […] can negatively impact workers." The report points to studies that show that the hospital industry has consolidated over the last 45 years and that the supply of labor to individual hospitals is "inelastic", meaning that a decrease in wages would be less likely to deter employees from working there. In the various theoretical monopsony frameworks discussed in the Treasury Report, a single hospital may be able to exert monopsony power over its employees if it can reduce wages without fear of employees switching to other firms or occupations. However, the study did not find a consistent wage effect in all hospital mergers, noting that there was "no detectable wage effects of mergers that only mildly increase employer concentration".[5] Additionally, this study finds that the negative effect of mergers is limited to skilled workers

[2] This is simultaneous with the effect of reducing the total quantity of individuals employed relative to the hypothetical perfectly competitive market.

[3] For example, a firm knows the wage it has offered to all of its employees, whereas a jobseeker may have no information beyond their expectation of a reasonable wage.

[4] Specifically, this is discussed here through the framework of restrictive agreements such as "non-competes" and "no-poaching" agreements.

[5] Treasury Report, p. 23; Prager, Elena, and Matt Schmitt. 2021. "Employer Consolidation and Wages: Evidence from Hospitals." American Economic Review 111 (2): 397–427.

such as doctors, suggesting that monopsony power is specific only to certain occupations which may have been consolidated under the merger.[6] For example, the study finds no effect on jobs that require less training, such as cafeteria workers, or those with more employment options outside of the hospital industry.

With respect to labor market frictions, the Treasury report discusses many nuanced examples, such as "restrictive employment agreements" including "non-compete" and "no-poaching" agreements.[7] For example, hourly workers at restaurant chains may be subject to "no-poach" agreements which the Treasury states "are common in […] the franchise context". The report also states that a low wage worker may "lack sufficient bargaining power to refuse a non-compete agreement". Within the Treasury's "search and matching" framework that argues "all employers, to varying degrees, possess market power", a low-skilled worker at a restaurant chain may face reduced wages (from the employer acting as a monopsonist) in addition to reduced employment mobility (from the "restrictive employment agreements").[8]

In practice, these types of agreements will vary in many of their characteristics across industries and among occupations. For example, as the report states, C-suite executives can be subject to non-compete agreements in order to decrease the chance that they leave the firm and share trade-secrets.[9] However, the effect of this type of restriction is, at best, ambiguous on highly skilled workers, who may have sufficient bargaining power to negotiate a pay increase in exchange for signing a non-compete agreement. The Treasury again discusses a recent study from 2021 which finds that "initial CEO compensation is higher when enforceability of non-competes is higher, suggesting CEOs demand a compensating differential".[10]

This highlights the need to examine the industry- and occupation-specific economic factors, and the extent of their effects on a given employee's wages and opportunities, when studying these labor-market topics. As the Treasury acknowledges, these agreements may also have pro-competitive benefits, such as encouraging employers to invest in and train their employees.

III. Regulatory Changes Related to Monopsony

Importantly, the Treasury report draws attention to the recent civil enforcement and competition advocacy from the Federal Trade Commission ("FTC") and the Department of Justice ("DOJ"). In January 2022, the FTC and the DOJ announced a request for input to update the horizontal merger guidelines.[11] As part of this request, the agencies explicitly state their "particular[] interest[] in aspects of competition [that] the guidelines may underemphasize or neglect, such as labor market effects and non-price elements of competition". The Treasury notes that public commentators have suggested that labor

[6] It is important to note that concentration alone may not be a useful indicator. The Treasury also points out that labor market concentration is a "flawed proxy for labor market power" (Treasury Report, p. 27).

[7] The Treasury defines these terms as:

- No-poach agreement: "Two or more employers agree to not solicit or hire each other's current or former employees".
- Non-compete agreement: "Former employee cannot work for a competitor following separation. Typically applies for a certain amount of time, over a certain geographic area, and within a specific industry".

[8] The report identifies that restrictive covenants are more common amongst skilled workers but can also apply to "workers with minimal employer-specific training" (Treasury Report, p. 28).

[9] The Treasury finds that "twenty-one percent of workers in the top income quintile are covered by a non-compete agreement" (Treasury Report, p. 28).

[10] Treasury Report, p. 28; Kini, Omesh, Ryan Williams, and Sirui Yin. 2021. "CEO noncompete agreements, job risk, and compensation." The Review of Financial Studies 34 (10): 4701–4744.

[11] See, "Request for Information on Merger Enforcement", January 18, 2022, available at https://www.regulations.gov/document/FTC-2022-0003-0001

market enforcement should be more directly addressed by the merger guidelines. During the FTC's "Enforcers Summit" in early April 2022, commissioner Rebecca Slaughter stated that recent cases "mark[] a real turning point in how [the agencies are] thinking about mergers […] from labor specifically".[12]

IV. POTENTIAL IMPLICATIONS

As illustrated by the Treasury report, the current administration is heavily focused on antitrust regulation in labor markets. This is also reflected in the enforcement activities of the regulatory agencies, which have noted that investigations into potential anticompetitive conduct in labor markets are a "high priority".[13] However, the DOJ has also experienced setbacks in its attempted enforcement of competition law in labor markets—including recent not guilty verdicts in the first criminal wage-fixing and no-poach cases, respectively.[14] As described above, the potential effects of mergers or "frictions" are not uniform across industries or even occupations, and any investigation or analysis of labor market competition must properly account for the economic facts of each specific scenario.[15]

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[12] *See*, "FTC Enforcers Summit Transcript", April 4, 2022, available at https://www.ftc.gov/news-events/events/2022/04/enforcers-summit

[13] See https://www.justice.gov/jmd/page/file/1491651/download (p. 7)

[14] See, *USA v. Jindal (4:20-cr-00358)* and *USA v. DaVita Inc. et al (1:21-cr-00229)*.

[15] Beyond the issues discussed here, the report points out a variety of other labor market characteristics, for which this economic assessment is also relevant. For example, there is discussion on licensing reform and union organization which are similarly tied to labor market frictions, such as lack of mobility due to state licensing differences. Again, economic realities must dictate the analysis of the situation.