The Political Forum

A review of social and political trends and events
impacting the world's financial markets

Mark L. Melcher
President
melcher@shentel.net

Friday, August 2, 2002

A REPRINT FROM A PIECE PUBLISHED July 15, 1998

The Man In The Cement Shoes

Mark L. Melcher
Stephen R. Soukup

Once in a while, something happens in Washington that provides persons interested in political science with an opportunity to witness a real-time, unvarnished example of the seamiest side of modern day, big power, big nation Democracy.

The lust for power becomes so overwhelming that politicians drop all pretense of respectability and just "go for it." These are special moments for political junkies like myself. Like a flawless diamond, or a hole-in-one, or an incredibly beautiful day in Virginia's Shenandoah Valley, we look at it and say, "Wow!"

I had that feeling a few weeks ago when the Clinton Justice Department filed an antitrust suit against Microsoft. I didn't write about it at the time, but I have been thinking about it a lot ever since. And the more I think about it, the more I realize that this is . . . . a special moment. Repugnant, yes. But special.

Attorney General Janet Reno doesn't quite see it this way, of course. She portrays the attack on Microsoft as one waged on behalf of the American people. Indeed Miss Reno has gone out of her way to assure all would-be critics that her intentions are good; that the antitrust action is simply designed "to preserve competition and promote innovation," and to protect and benefit "consumers and computer manufacturers."

Others however, many of whom would appear to be far more intimately acquainted with the economic intricacies of the free market than Miss Reno, have suggested that she is misguided. These include Fed Chairman Alan Greenspan and the U.S. Court of Appeals for the D. C. Circuit.

Greenspan didn't attack the Microsoft action directly, but he wondered aloud during recent congressional testimony whether, in the words of the *Wall Street Journal*, "antitrusters could conceivably adopt a humbler pose as they set about reordering a sizable section of the economy." His exact words were as follows.

"I would like to see far more firm roots in our judgments as to whether particular market positions do, in fact, undercut competition or are only presumed on the basis of some generalized judgment of how economic forces are going to evolve."

The D. C. Court of Appeals was much more direct in its criticism. It reversed a lower court injunction against Microsoft, arguing that "antitrust scholars have long recognized the undesirability of having courts oversee product design, and any dampening of technological innovation would be at cross-purposes with antitrust law."

Then what, one might ask, motivated the Justice Department, if not the consumer protection intrinsic in the Sherman Antitrust act? If the action is indeed "at cross-purposes with anti-trust law," why then do it?

The one thing we can assume is that the action does not spring from some newfound antipathy within the Clinton administration toward big business. One would be hard pressed to find any prior administration, whether Republican or Democrat, going back to the founding of the Republic, that is more favorable to the concept of "bigness" in business than this one.

Indeed, big business is a key part of the Clinton administration's underlying industrial policy philosophy. As outlined in numerous books and articles by Robert Reich, former Labor Secretary and long time Clinton friend and advisor, the nation's "New Democrats" are unflinching advocates of "partnerships" between Washington and business. Such partnerships result in huge reservoirs of raw political power, and the bigger the partner the better, despite (or perhaps because of) the propensity of such partnerships to promote corruption and to severely damage competition.

As I argued last August in a piece entitled "The New Political Paradigm," the old saw about the GOP being the party of big business and Democrats being the party of labor no longer has much meaning. Today, the bulk of the Democratic Party's strength stems from an alliance of big business, big bureaucracy, and labor union bosses.

Republican support comes primarily from small businesses, which are the principal victims of the above-mentioned alliance, and blue-collar workers, including a majority of the members of the above-mentioned union bosses. I put it this way.

> Throughout most of the 20th century, the Democratic Party was the preferred political home for blue-collar workers. Today, Republicans get a majority of their votes from these so-called "Joe Sixpacks" and their wives. Conversely, the GOP was, from the time of the so-called "Robber Barons" in the late 19th century until very recently, the home of big business.

> While the GOP still has a huge following in the small business community, the board rooms of most of America's corporate giants are filled with Democrats, who aggressively support the Washington colossus in exchange for huge amounts of business, important tax breaks and direct subsidies, and most importantly, for a steady stream of regulatory initiatives and trade rulings that serve to cripple their smaller competitors both at home and abroad. . . .
>
> Liberal commentators still appear to labor under the misconception that the Democratic Party represents the blue-collar worker in his fight against the "capitalist dogs." Conservative pundits, on the other hand, seem to believe that "we are all capitalists now" and that no significant threat to free enterprise exists anymore. Both assumptions are wrong.
>
> The reality is that a powerful new paradigm has emerged onto the American political scene that has completely changed the nature of the Democratic Party, and is a direct threat to America's traditional brand of free enterprise capitalism.

So, once again, why pick on Microsoft? I think that a reasonable person could be forgiven for concluding that the answer to this question may well be a phenomenon much older even than America's antiquated antitrust laws, namely something called extortion.

I know that this is a serious charge. But I think a serious person, seriously concerned about the government's impact on the marketplace, will consider it seriously. After all, as I have pointed out numerous times the Clinton Justice Department is so "cronied up" with political hacks that it couldn't avoid the "appearance of a conflict of interest" even if it tried, which it seldom does.

In addition, it is worth noting that this administration's track record when it comes to raising money is amazingly sordid, including not only the acceptance of funds from a host of sleazy foreign interests, but what *New York Times* columnist William Safire once described as "Bribes From Tribes," in piece about the relationship between Interior Department actions concerning Native Americans and campaign contributions from the various tribes.

One of the best ways of understanding what I think is going on here is to consider a thesis advanced in a book my colleague Steve Soukup stumbled across last year while working on a piece we were writing on the 1996 Democratic fund-raising scandal.

This tome, entitled *Money for Nothing: Politicians, Rent Extraction, and Political Extortion,* by Emory University economics Professor Fred McChesney, is far more than a simple diatribe against money in politics. It is a work of academic social science in the true sense of the phrase, a "rational choice/public choice" work replete with econometric models, empirical substantiation of hypotheses, and all the other trappings of positivist social science.

The basic premise of the book is that regulation can be seen as a form of "rent extraction," whereby political actors threaten action against specific entities or industries in order to compel them to take a more active role in the great American pastime of buying influence.

In short, according to McChesney, politicians extract or extort money from producers in return for favorable regulation or, in many cases, for the forbearance of further regulation and the maintenance of the status quo.

Now this would be considered a fairly commonplace observation, except that in an especially prescient section of the book's concluding chapter, McChesney notes that industries and firms that are generally unregulated are often seen as pristine extortion territory, where officials can easily create new rents. In addition, he says, "recent antitrust investigations against firms . . . seeking nothing from government also exemplify this phenomenon."

And then comes the kicker, namely that, in McChesney's opinion, "Silicon Valley, with its sharp competition but rapidly increasing stock of capital, would seem a natural target for extraction soon."

And what better "target" than Microsoft? You see, prior to the start of the Justice Department investigation of Microsoft, Bill Gates, whose business was "generally unregulated," was the quintessential example of someone who was "seeking nothing from government." Indeed, he considered politics to be, in the words of D. Michel Heywood, an editorial writer at *The Columbian* (a newspaper published in Vancouver, Washington, roughly four hours south of Microsoft's Redmond headquarters), "the kind of dirty game that could be safely left to others."

Even as late as last year, Microsoft employed only four employees in its Washington government-affairs office. As *U.S. News and World Report* financial columnist James Glassman once pointed out, this pales in comparison to the 26 lobbyists employed by IBM, the 45 by AT&T, and the 21 by Motorola, all of which have remarkably lower net worth than Gates' firm. Nor did Gates care much about direct political contributions. According to the *Washington Times*, during the 1995-96 election cycle Microsoft gave less than $100,000 to politicians.

All of that has changed now, of course. Heywood notes that "Gates seems to be learning," and is now "plowing [money] into the game about as fast as the law strictly allows." David Boaz, the executive Vice President of the Cato Institute, wrote recently that Microsoft had "hired four former members of Congress, 32 former congressional staffers or government officials, and the former chairman of the Republican Party [Haley Barbour]. It spent $1.9 million on lobbying in 1997, up 67 percent from 1996."

Gates has also upped his contributions to individual politicians. *The Washington Times* reports that in the 1997-98 off-year election cycle, Microsoft has already made nearly a one quarter of a million dollars in campaign contributions, nearly three times its total contributions during the '95-96 cycle.

Now critics of this thesis will point out most of Gates' money (roughly 85%) has gone to Republican candidates, and that this proves that the antitrust action by the Clinton administration couldn't have been politically motivated.

But they, we think, miss the point. Bill Gates, you see, isn't the Democrats' fund raising target. He's the example. He's the guy at the bottom of the lake in the cement shoes; the guy who didn't pay up. The Democratic payoff, if we're right about this, will come from others; those who don't want a similar fate, or who, like Microsoft competitor Novell, benefit from having Gates in the hot seat.

As McChesney points out, none of this is new. Popular folklore holds that the basic concept was developed and refined by Chicago mobsters in the 1920s. They called it the "protection racket." A mobster would say to a businessman, "Would you like to buy some insurance against broken windows." The businessman would say, "Why, I've never had any trouble with broken windows." And the mobster would say, "If you buy this insurance, you won't any trouble in the future either."

In its modern day political form, no political party has an exclusive on the practice. Recently released tapes of Nixon White House conversations concerning the possibility of using antitrust actions against the major television networks unless they treated him better in their news reports reveal, in vivid terms, how the process works. Here's Nixon: "If the threat of screwing them is going to help us more with their programming than doing it, then keep the threat. Don't screw them now [otherwise] they'll figure that we're done."

Nevertheless, it would, in my opinion, be wrong to assume that every administration employs the power of government illegally and unethically to the same degree. As one might expect, some are decidedly more crooked than others, and one of the hallmarks of the most crooked is a propensity toward extortion. In the meantime, it would appear that Microsoft has been drawn into McChesney's world of political rent extraction, and this leaves the financial markets with a whole new set of variables with which to be concerned.

As we said in a recent piece entitled, "Wanted: A Smidgen of Ethics, A Dash of Common Sense, And A Pinch of Patriotism," these variables have nothing to do with traditional securities analysis, but are related to such murky questions as "whether the founder of a company (say . . . just for sake of argument, a large computer software firm) failed to give enough money to the party in control of the White House to avoid some sort of vigorous attack by an executive branch agency (say, again just for sake of argument, the antitrust division of the Department of Justice)."

As we also said in that piece, the value of traditional securities analysis under such circumstances is diminished, and investment risks are increased. It is a nasty situation for investors. But for a student of the American political scene, it is fascinating.

THE POLITICAL FORUM