



1015 15<sup>th</sup> Street, NW, 6<sup>th</sup> Floor, Washington, DC 20005  
Telephone: 202-777-3000 – Fax: 202-777-3010

Irwin Stelzer  
29 June 2012  
Economic Update

## **Economy-Watchers Should Keep An Eye On The Courts**

If you want to get some sense of where the economy is heading, don't ignore what the courts are doing. No need to repeat much of what you have heard -- some of it may be true -- about the Supreme Court's decision to uphold the constitutionality of the Patient Protection and Affordable Care Act, aka Obamacare. That decision will have major impacts both on the economy and on the health care sector. Its macroeconomic impact will be similar to any massive tax increase, which is what the Court has said Obamacare is all about: it will reduce the competitiveness of those firms that operate in global

markets, hurt small businesses, and transfer income from millions of Americans to insurers and to the government.

As for the health care sector, insurance companies think they will eventually get as many as 30 million more generally healthy customers who will have to maintain a "minimum essential" level of coverage or pay a penalty, oops, tax, one that will rise steadily until it is punitive enough to force the currently uninsured to prefer coverage to paying the fine. This huge new market comes at a cost: insurers' profits are to be limited by regulators, and they can't turn away people with pre-existing

conditions, among other measures that will inevitably drive up the cost of insurance.

Hospitals will see the bad debts imposed on them by uninsured patients drop. Manufacturers of medical devices will face a 2.3% tax on their gross sales, which will come to as much as 40% of the net profits of smaller "med tech" companies, an example of how tax policy is often crafted by a government-big business coalition to the disadvantage of smaller competitors. Small businesses will see their health care costs rise and two-thirds of affected small businesses are finding the system that is supposed to provide them with some tax-credit relief so confusing as to be unusable. Pharmaceutical companies cut a deal that protects them from some of the competition they face from generic drugs and the re-importation of drugs that can be bought and imported more cheaply from Canada and other countries, another example of crony capitalism; the administration bought Big Pharma's support by allowing those companies to maintain higher drug prices than would otherwise prevail. And some trends will continue, among them hospital mergers, digitalization of records, and increases in health

care costs that Obamacare does not address.

Nor is the important energy sector free from judicial impact. The use and prices of the various fuels are determined in markets importantly influenced by what judges think of the regulations pouring out of the Obama administration. Last week the District Court for the District of Columbia ruled that the Environmental Protection agency was "unambiguously correct" to tighten rules limiting greenhouse gas emissions. Fred Upton, chairman of the House Energy and Commerce Committee says -- allow something for politicians' hyperbole -- the regulation that the court upheld "threatens to drive energy prices higher, destroy jobs and hamstring economic recovery."

Coal-fired generation of electricity is at an all-time low as the industry mothballs dozens of coal plants. Many electric utilities are substituting natural gas for coal because it produces about half as much carbon dioxide as does coal, and a glut has driven prices so low that many in the oil industry say they are losing money on their natural gas operations. Barring reversal on appeal -- not likely -- the court has driven another nail into the coffin of the coal industry, a coffin the Obama administration has been eager to

nail shut, and a few companies are trying to keep open at least a crack by investing in clean coal technology. So anyone who invests in the energy sector has to worry as much about the courts' preferences as about consumers' preferences.

And followers of the auto industry's fortunes should know that the court's decision favors fuel efficient and electric vehicles over greenhouse-gas emitting vehicles, seen as a plus for Ford's line-up of new models. Given the much higher cost of electric vehicles, anything the courts can do to narrow the price gap between electric and gasoline vehicles is much appreciated by advocates of these alternatives to the increasingly efficient gasoline engines.

Then there is the high-tech sector, on which the economy depends for its long-term growth. A steady flow of innovations is needed if productivity in the manufacturing and other sectors of the economy is to advance. And a steady flow of new consumer products is needed if consumers are to be persuaded to part with their increasingly hard-earned and scarce dollars -- doubt that and look at the pictures of consumers queuing in pouring rain so as to be the first to cross the thresholds of Apple stores around the world

when a new product is announced.

That sector has been the scene of patent wars, with all of the players suing each other for violating patent rights in an attempt to gain advantage, not by innovating, but by preventing rivals from bringing competing products to market. All of the participants in these legal battles profess distaste for that other guy's decision to move rivalry from the market place to the court room, and profess disgust at the fees they have to pay the lawyers for whom patent litigation is providing a substitute for the decline in fees from big merger deals.

Along comes one of America's most distinguished and brilliant jurists and scholars (also a senior lecturer at the prestigious University of Chicago Law School and author of some 40 books and countless articles), Judge Richard Posner, sitting as a trial court judge in a patent infringement suit between Apple and Motorola Mobility, the latter owned by Google. The competition between those companies has heated up: sales of smart phones using Google's Android operating system overwhelm sales of iPhones around the world, and Apple plans to kick Google Maps off its iPhones in favor of its own product.

Instead of allowing the case to proceed to a jury trial, Posner called halt. Even if Apple's patents were infringed, said Posner, it is "wild conjecture" that Motorola can damage Apple, and he declined to allow Apple's lawyers to "turn the case into an Apple versus Motorola popularity contest." So why bother having a long trial to determine whether there is infringement, when no money will change hands if there is?

There are other cases wending their way through the courts, so Judge Posner's decision might not end the patent wars. But because of the esteem in which Posner is held, this decision might, only might, persuade other courts to follow, and the combatants to settle their differences and transfer funds from their lawyers to their labs.

These are only some of the examples of the way in which the courts play an important part in shaping the American economy. These courts, of course, deal with the laws handed to them for interpretation. But because laws are often vague -- designedly so in order to forge a compromise in a fractious legislature -- courts have considerable discretion. In past weeks alone they have transferred billions of dollars of income from younger, healthier people to older, less healthy people. They have transferred income from owners of

small businesses to executives in larger ones by forcing entrepreneurs to increase payments to large insurers, and saddling small competitors with costs and regulations that larger companies can more easily accommodate. They have pushed the coal industry closer to distinction, transferring income from hard-working coal miners to more affluent environmentalists and their friends. And they might have hastened the end of the patent wars, for which income transfer -- lawyers to entrepreneurs and inventors -- we can be provisionally thankful.

But don't put all of the blame on the judges. It is not their fault if the law they are asked to apply is, as Dickens' Mr. Brumble put it, "a ass". The bucks in their billions stop with the legislators.

[ET