Bootleggers and Baptists Go Digital

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Technical change in general and digitalization in particular enhance competition by reducing the cost of transactions (Munger 2015). However, potentially valuable transactions may be prevented by already-existing or newly introduced regulations. Why are such regulations that clearly have a welfare-decreasing effect not promptly removed?

Economists have developed models to understand why regulation exists. They have found that policy makers do not always pursue the general interest (however defined) but rather their own personal interest—as much as anybody else in society. In doing so, they interact with pressure groups that may have an interest (monetary or otherwise) in the proposed regulations.

A useful framework to understand how the regulatory process works comes from the bootleggers-and-Baptists (B&B) theory. The theory was originally proposed and later refined by Bruce Yandle (Yandle 1983, 1999, 2010; Smith and Yandle 2014). As Yandle explains, it gets its name "from a common phenomenon in the United States in regions that restrict the sale of alcoholic beverages on Sunday. Baptists lobby for the associated regulations; they prefer a world where less alcohol is consumed. Bootleggers, the illegal sellers of alcoholic beverages, support the laws as well. Sunday closing laws shut down legitimate sellers, giving an open field in which bootleggers can sell their wares" (2010, 3). Bootleggers and Baptists need not explicitly cooperate with each other, although that may happen: what matters is that their joint interest and their interaction can drive down the political cost of regulations.

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This paper tries to answer the following question: Can B&B help to understand the regulation of emerging digital services? The paper builds both on the existing economic literature and on the author's experience in the Italian Ministry of Economic Development during the Renzi (2014–16) and Gentiloni (2017–18) governments. The next two sections review the relevant literature. Then I put B&B in the context of digital services and present a few case studies from my experience in Italy.

Theories of Economic Regulation

Why does regulation exist? The demand for regulation is affected by changes in the economic environment, which can be either exogenous or endogenous. Yandle (1983) identifies at least four factors that may affect the demand for regulation: (1) technological change; (2) demographic change; (3) significant changes in factor costs; and (4) new information. Whenever any of these changes happens, a case can be made for or against regulation.

Economists have developed several explanations concerning what happens next—that is, how regulatory decisions are made—and which specific regulations are likely to emerge from societal or economic changes. Adam Smith and Bruce Yandle (2014) track five potential theories to explain the emergence of regulation and how collective decisions are made.

To begin with, an argument can be made that regulation is introduced to correct so-called market failures—that is, all the circumstances whereby markets do not spontaneously deliver an efficient resource allocation. This assumption lies at the core of the so-called theory of the public interest. A famous example is Arthur Pigou's (1920) treatise on externalities, which introduced the notion of Pigouvian taxes to align the private and social cost of goods. The theory fell short of explaining how things work in the real world, not least because it assumed complete information (Coase 1960).

More sophisticated explanations emerged over time, starting from the acknowledgment that policy makers may have their own legitimate goals, which they take into account as they perform their jobs (Tullock, Seldon, and Brady 2002). The so-called regulatory-capture theory recognizes that policy makers do not possess all the relevant information. In order to make a meaningful decision, they entertain a relationship with vested interests.

George Stigler (1971) and Sam Peltzman (1976), among others, went further with the special-interest theory: they suggested that the political process should be viewed as a market, where rent seekers demand regulation and policy makers supply it. Rent seekers will be most effective as they (1) offer the highest bid and (2) reduce the cost of the proposed policies to the policy makers.

A fourth theory can be labeled "money for nothing" (McChesney 1991): a policy maker may publicly make an argument for a new regulation that affects a group that has been not regulated so far. The groups affected by the proposed regulation will

organize themselves and lobby for or against it, which will allow the policy maker to extract rents.

Bootleggers and Baptists

The B&B theory (Yandle 1983, 1999, 2010) supplements the previous four theories. It explains how political coalitions can lower the cost of lobbying. The key insight is that different pressure groups that apparently have little in common may join forces to pursue targets that they share, although for different reasons. The theory is named after the archetypical case of bootleggers and Baptists in southern U.S. states: Baptists advocate Sunday closing laws (or wider restrictions) for bars and liquor stores on religious grounds; bootleggers see the same laws as a useful tool to shut down competition from legal agents. Baptists provide the moral high ground for the proposed regulation, hence making it more socially acceptable: in a way, they lower the cost of obtaining consensus, or, to put it in Coasean terms, they reduce the cost of political transactions. Bootleggers lobby policy makers behind closed doors and provide political support (as well as electoral support). One key feature of the kind of regulation that emerges is that while being "morally" acceptable to Baptists, it will create a window of opportunity for the bootleggers: the latter will support Sunday closing laws because they are in the position of directly benefitting from them, but they would not support a ban on *drinking* alcohol on Sunday. Generally speaking, these regulations are not aimed at correcting some potential failure of the market; rather, they are aimed at restricting competition. In other words, Baptists are interested in the *intentions* of regulation, bootleggers in its *outcomes* (I borrow this point from Milton Friedman [1975]).

Randy Simmons, Ryan Yonk, and Diana Thomas (2011) have contributed to the debate by framing B&B within the framework of "political entrepreneurship"—that is, the activity of maximizing profits by seeking political rents rather than providing valuable products in the market. B&B helps explain real-life regulatory processes. Yandle (1983, 1999, 2010) and Smith and Yandle (2014) provide several examples. Environmental regulation is a fertile ground for the theory because it is where the interaction between vested interests and nongovernmental organizations can best be observed (Zywicki 2002): fuel-economy standards in the United States (Yandle 1999), carbon control (Buck and Yandle 2002), and nuclear-waste management (Darst and Dawson 2008). International trade also provides examples (Desombre 1995; Morris 2003). Other cases include tobacco regulation (Morriss 2008), e-cigarette regulation (Adler et al. 2016), marijuana-related land-use control (Kochan 2015), and timber regulation in the European Union (EU) (Sotirov, Stelter, and Winkel 2017).

To make a long story short, B&B suggests that the probability that a regulation will be adopted is greater when it is endorsed by groups with the characteristics of bootleggers and Baptists. But how do these groups interact with each other? Smith and Yandle (2014) define four potential modes of interaction:

1. *Covert,* when bootleggers dress themselves like Baptists and try to hide their real goals behind the facade of public interest
2. *Noncooperative,* when the two groups act independently from each other without direct forms of cooperation (as was the case with the real bootleggers and Baptists)
3. *Cooperative,* when Baptists and bootleggers develop conscious forms of cooperation by recognizing their mutual interests (see also Shogren 1990)
4. *Coordinated,* when a policy maker kickstarts a debate on a new proposal for regulation, thereby offering de facto an opening to bootleggers and Baptists

The Digital Economy: Some Case Studies

Most of the literature reviewed in the previous section finds evidence of B&B interactions in the "old economy." More specifically, large companies generally play the role of bootleggers (because they have greater resources to invest in lobbying activities, as shown in—among other sources—Stigler 1971 and Philippon 2019). But what about the "new economy"? Digitalization and the development of information and communication technologies (ICTs) are generally credited for improving productivity and reducing transaction costs, which often result in greater competition.

In an extensive review of the literature, Federico Biagi (2013) found that

1. The effect of ICTs on productivity is both direct (ICTs are embedded in goods and services and in technological improvements) and indirect (ICTs contribute to the generation, storage, and dissemination of knowledge).
2. ICTs are responsible in part for the acceleration in productivity growth observed in the United States in 1996–2006 as well as for the widening productivity gap between the United States and the EU.

Bronwyn Hall, Francesca Lotti, and Jacques Mairesse (2013) show the complementarities between ICTs and research-and-development spending, with the former having a greater effect on productivity and the latter being more relevant for innovation.

One way of understanding and rationalizing how the digital economy works is by focusing on transaction costs. Ronald Coase's seminal paper "The Nature of the Firm" (1937) explains that the cost of transactions determines the optimal size of firms and dictates their choices regarding vertical and horizontal integration. As transactions become less costly, markets gain advantage over hierarchy (as defined in Williamson 1973), and integration loses ground vis-à-vis procuring goods and services from third parties. Online platforms perform precisely this function of reducing transaction costs by facilitating the matching of demand and supply either in existing markets or in newly created ones (Rochet and Tirole 2006; Evans et al. 2011; Munger 2015).

These changes deeply affect the functioning of competition. By decreasing the costs of transactions (such as the costs of information, search, and negotiation), they expand the physical size of markets, allow the entry of new competitors into old markets, and create new markets altogether. This process is sometimes hindered by existing regulation; at other times, new regulations are introduced that result in limiting the opportunities that stem from the digitalization of the economy.

A well-studied case is that of the ride-sharing platform Uber. Despite its positive impact on employment, customer satisfaction, and social welfare (Cramer and Krueger 2016; Hall and Krueger 2018), Uber has faced strong regulatory barriers virtually everywhere. These barriers were in many cases already in place when Uber showed up, but in some cases they were created after its arrival and led to the suspension of its operations. Both kinds of barriers are usually advocated by (licensed) taxi drivers, who fear competition from Uber. This kind of regulatory setback can be better understood on the basis of the B&B theory.

In this section, I present a few case studies that I chanced to follow directly during my time at the Italian Ministry of Economic Development between 2014 and 2018.[1] In this capacity, I could closely follow how the requests for new regulations from pressure groups (the bootleggers) translated into law proposals, were endorsed (or rejected) by policy makers, and eventually translated into law or repealed altogether. I could also see to what extent policy makers feel the pressure from public opinion and therefore how important it is for a pressure group to hide its own (monetary) interests behind some sort of broader interest. The cooperation with third parties (the Baptists) that can provide this kind of moral coverage is a key component of a successful lobbying activity. In my time at the ministry, I had a chance to deal directly with lobbyists as well as with members of Parliament and, of course, with the governmental bureaucracy. Among my other tasks, I performed research and prepared notes on the potential economic impacts from the proposed regulations on competition. This work helped me to see directly how common it is for pressure groups to seek reforms that result in restrictions to competition and how often such restrictions entail limits to the business models of online operators. I discuss a few case studies from a much larger sample. These examples come from publicly available information and fit well within the B&B framework. I am aware that they provide only anecdotal evidence, yet I believe they can confirm the power of the B&B model to understand the political process and show how bootleggers and Baptists have adjusted their behavior to the new digital world.

I follow Smith and Yandle's (2014) classification of the four modes of interaction between bootleggers and Baptists.

1. I served as special advisor to the minister on energy and competition in 2014, chief of the minister's technical staff in 2015–16, and economic adviser to the undersecretary for competition policy in 2017 until I left the government in February 2018.

Covert Interaction: The "Anti-Flixbus Amendment"

The most basic mode of interaction between bootleggers and Baptists is when bootleggers dress themselves in Baptists' clothes. An interesting example came in 2017 with the so-called Anti-Flixbus Amendment. Flixbus is a German platform that connects and coordinates bus transit companies. This is how the company describes itself on its website: "FlixBus continues to revolutionize the bus travel industry. Through smart network planning and dynamic price management, we are able to provide our customers with the best offers possible. Our FlixBus network relies on close partnerships with small and medium-sized enterprises and often family-owned businesses—our regional bus partners—who are responsible for the green FlixBus fleet."[2] According to data released by the company, more than 100 million people have traveled on Flixbus-branded buses since 2013.

The Flixbus platform works as a textbook two-sided market: on one hand, there are bus operators (who are required to comply with specific quality standards as well as with the existing national and EU regulations); on the other hand, there are travelers. To be clear, Flixbus is not a bus operator and does not hold a license to run buses: its partners run the buses and simply outsource to Flixbus the tasks of organizing and coordinating the routes, managing ticketing services, and advertising. By optimizing these services, Flixbus can achieve high standards, capture a broad-based demand, and grant its partners high-load factors for their buses and subsequently low prices to their customers. Hence, Flixbus provides an intermediation service between its partners and their customers, thereby reducing transaction, search, and information costs—it does not provide transport services directly. In doing so, Flixbus both *creates* new demand and *attracts* an already-existing demand from traditional operators—that is, nonintegrated, local bus companies.

These local, nonintegrated companies, however, feel the pain from competitive pressures: their business is disrupted by Flixbus's more-efficient, less-expensive bus company partners. Represented by a business association called Anav, these local, nonintegrated companies accused Flixbus of "unfair competition" and claimed it was "disrupting a stagnant market" (Sironi 2016). They waged a legal battle accusing Flixbus of not being licensed as a transport operator (which it is not) and implying that a mere intermediary should not be allowed to provide transport services. The courts and Italy's antitrust body dismissed the case, stating that Flixbus does not directly provide transport services—hence, it needs no license as long as its partners (that operate buses) comply with the regulations. In other words, the courts confirmed that Flixbus's intermediation was legitimate as long as it hooked customers up with licensed bus operators (which, of course, Flixbus does).

At this point, Anav changed strategy: it abandoned litigation and switched to lobbying, effectively taking the bootleggers' stand. It proposed a change in the law

2. See the Flixbus website at https://goo.gl/sJTB8L (accessed June 9, 2020).

under which not just bus operators but also online platforms that provide intermediation (as Flixbus does) would be required to obtain a license. Note that licensees must own buses: the amendment, if accepted, would de facto outlaw Flixbus's business model by making intermediation illegal (Mannheimer 2017).

From an economic standpoint, the proposal dictated an organizational choice (vertical integration), even though there was clear evidence that disintegration was a more efficient solution. As such, the Ministry of Economic Development (where I was working at the time) opposed the proposal, whereas the Ministry of Transportation took a more nuanced stand (even though it eventually discarded the bill).

What is more interesting, though, is that the proposal was endorsed by several members of Parliament (MPs) from different parties, most of whom were from the Puglia region (including Francesco Boccia, then chairman of the Chamber of Deputies' Budget Committee). Most members of Anav (and Flixbus's largest competitors) were from Puglia, too—the most profitable routes in Italy being north to south. MPs from Puglia were apparently particularly keen to accommodate requests that came from companies located in their same region. In the end, however, the Italian Parliament voted down the amendment, and so Flixbus is still providing its intermediation and allowing the demand for high-quality, low-cost transit to meet its supply.

The story of the Anti-Flixbus Amendment provides an example of what Smith and Yandle (2014) call "covert interaction." Although the amendment's proponents tried to argue that the legislative change was necessary to protect the rights of workers and customers, in fact the proposed law was about protecting the market shares and margins of comparatively less-efficient transit companies. No evidence has ever been provided that workers' conditions under Flixbus partners are worse than workers' conditions under traditional operators; as far as customers are concerned, their actual choices reveal their preferences. One reason why the proponents weren't able to get the amendment passed was that it soon became evident that the ostensible rationale was in reality a fig leaf. Flixbus started a clever campaign to inform passengers that its business model was at risk, and the passengers reacted by petitioning the Parliament against the proposed change (Strade 2017). More than sixty thousand travelers—about one in every thousand Italian residents—signed the petition, which made the contrast crystal clear between the concentrated interests of Flixbus rivals and the diffused interests of consumers. Politicians may be willing to restrict competition in order to favor companies in their district, but not if doing so comes at the cost of losing votes. When the issue became prominent enough in the media to move public opinion, both the government and its parliamentary majority decided that the public interest was better served by a more competitive environment. This outcome is consistent with a major lesson from B&B: lobbying is more effective when the actual interests of rent seekers are hidden behind some broader claim. The competitors of Flixbus weren't successful insofar as they made their case a mere clash of interests, whereas travelers easily understood that their own interest was better served by Flixbus. A take-away from this

experience is that bootleggers may try to play Baptists, but they are more effective when they rely on *real* Baptists—as we shall see in the following examples.

Noncooperative Interaction: Sunday Closing Laws

The example I provide here of a noncooperative interaction follows almost literally the original B&B story—except that in this case we have Roman Catholics instead of Baptists. In fact, it is precisely about Sunday closing laws. Italy deregulated Sunday openings in 2012 (Mitra 2018). According to opinion polls, most Italians support deregulation (Borghese 2018), and more than 24 percent of them now go shopping on Sundays (Italian National Institute of Statistics 2016, 2018). Moreover, there is evidence that deregulation of opening hours results in higher employment, greater social welfare, and—to a lesser extent—increased spending, although not for all retail product categories (Genakos and Danchev 2015).

In 2012, deregulation was strongly opposed by shop owners associations. The welfare effect from deregulation does not come primarily from greater consumption but from the customers' ability to shift their shopping to a time when the opportunity cost of their time is lower (for example, on Sundays rather than on working days). However, longer opening hours cause shops to bear greater costs—wages, energy, heating/air conditioning, and so on. Hence, deregulation results in a competitive advantage for larger outlets vis-à-vis smaller shops because the former can more efficiently spread their increased fixed as well as variable costs over greater revenues. This is why the smaller shops' business associations have consistently opposed deregulation since the beginning. When opening hours were deregulated in 2012, though, Italy was on the edge of bankruptcy. The reform was passed as part of a larger package of recovery measures. Yet retail associations never gave up: they kept lobbying to reintroduce some form of regulation aimed at limiting opening hours (Confersercenti 2018). In doing so, they had a very powerful ally: the Roman Catholic Church.

For religious reasons, Italy's Conference of Bishops stood up for Sunday closing laws, arguing that such laws are not just about Christians attending mass but also about giving individuals and families an opportunity to have rest and spend time together (*AskaNews* 2018). Note that, in contrast to the Flixbus case, in the debate on Sunday closing laws two different groups lobby for the same legislative change—shop owners call for restriction to competition, while the Catholic Church provides the moral high ground.

During the 2013–18 term, the Italian Parliament debated several law proposals concerning Sunday closings. A compromise was found at the Chamber of Deputies in a piece of legislation that would mandate at least six closing days per year out of twelve days identified by the proposed law itself. The proposal, which the Ministry of Economic Development opposed on the basis that it would reduce competition while not pursuing any countervailing general interest, was passed by the Chamber of

Deputies in 2014 with a striking majority: 283 voted in favor, 15 abstained from voting, and none voted against (about half of the MPs were not attending, though). However, the bill never went to a vote in the Senate, and therefore it never entered into effect.

In March 2018, Italy held national elections, and a majority coalition was formed by the Movimento 5 Stelle (M5S, Five Star Movement) and the Lega (League), both parties having previously supported Sunday closing laws (the bill mentioned in the previous paragraph was based on a draft from an M5S MP). In the summer of 2019, the majority broke up, and the government fell. A new government was formed with a different supporting coalition: M5S and the Democratic Party (DP). The issue of Sunday closings reemerged several times, both under the Lega–M5S government and under the M5S–DP government (Bartoloni 2019).

Several bills were proposed. Interestingly enough, as the debate developed, it became clear that small shops do not face competition from larger outlets alone but also—and increasingly—from online platforms such as Amazon and the like. Mandatory Sunday closings might create an advantage for online retailers and provide little or no benefit for small retailers: under the proposed legislation, small and large retailers would be forced to stay closed, but the internet never sleeps. In order to prevent e-commerce operators from gaining a competitive edge from the stricter regulations, some proposed to extend the Sunday closing obligation to online platforms as far as order processing is concerned. In other words, if you make an order on Sunday, the online platform would receive it on Monday.

As of June 2020, no bill has yet been passed. According to the media, the M5S is pushing hard to get one passed, the Democratic Party would prefer a watered-down version, and a smaller component of the parliamentary majority—former prime minister Matteo Renzi's own party, Italia Viva (Italy Alive)—is against any kind of re-regulation whatsoever. Temporary regulations that limit opening hours on Sunday or ban Sunday openings were introduced at the regional or local level during the Covid-19 outbreak, and some would like to postpone the phasing out of these regulations as long as possible. Still, widespread economic evidence shows that re-regulation would decrease economic welfare; moreover, most voters oppose it, although they are unlikely to switch their electoral preferences *because* of their favorite party's position on Sunday closings. In this complicated context, the Catholic Church's support has proved to be an invaluable asset for those lobbying for regulation. In fact, it has increased public support for the proposed laws and shifted the debate from an economic one (under which a case for closing laws can hardly be made) to a broader, social one.

We don't know how this story will end. However, for the purposes of this paper, it provides an example of how the interaction between vested interests and moral authorities may give momentum to reforms that would otherwise enjoy small or no support from the public. The debate on the regulation of online retailers also provides a twist from the digital world.

Cooperative Interaction: Food Delivery

A more sophisticated mode of interaction occurs when bootleggers and Baptists work together directly. An illustrative story is that of food-delivery regulation. Food delivery has historically been provided in several Italian cities by riders directly employed by restaurants or pizzerias—quite often in the underground economy. Online delivery platforms radically changed the landscape by connecting the three sides of the market: riders, restaurants, and customers. Most food-delivery platforms do not hire riders: self-employed persons instead freely make themselves available (Del Prato and Stagnaro 2018b). Flexibility is a feature of peer-to-peer jobs that workers seem to appreciate, as emerged from surveys in environments as diverse as Uber drivers in the United States (Hall and Krueger 2018) and Deliveroo riders in Italy (Del Prato and Stagnaro 2018a). Given the nature of the online food delivery business, little sectoral regulation exists, if any. As self-employed workers, riders are entitled to no specific protection (such as severance pay, mandatory insurance against accidents at work, sick leave, or holiday leave), although most platforms voluntarily provide various kinds of insurance or other benefits.

Some riders self-organized themselves in associations, aiming to unionize their peers. Their take is that riders are typically low-skill, low-salary workers who are exploited by platforms, so they deserve greater protection, and their status as employed workers should be recognized, no matter if that recognition may undermine the platforms' business model entirely.

Where are the bootleggers in this debate? They are where one wouldn't expect: within traditional trade unions. Union membership has been declining steadily for several years—the largest unions in Italy lost almost half a million members in 2012–17 (Demoskopika 2018). That shrinkage is due in part to the shift in value added and employment from the manufacturing to the service sector, where firms are on average smaller and less unionized (Autor and Dorn 2013). Unions have an incentive to try and enter markets and industries where they have not been able to gain members. Hence, the alleged problems of a relatively small number of riders (about ten thousand [Boeri et al. 2018]) became a top issue in Italy's politics for a while. The national leaders of the largest trade unions jumped in and called for regulating riders as employees instead of allowing them to be treated as independent workers (Cottone 2018). They also tried to attract or form riders' associations within unions in order to gain legitimacy and start negotiating a national contract for riders (under Italy's labor laws, national contracts are negotiated between unions and employers' association and become binding for all businesses within the same industry).

One nontrivial question is what industry riders belong to. Ironically, although most riders were in favor of greater protections in principle, when faced with a trade-off between protection and flexibility, on the one hand, and protection and higher salaries, on the other, they chose the latter (Del Prato and Stagnaro 2018a). Almost nine hundred riders signed a petition *against* any reform that, by regulating their labor

relationship with platform, might result in lower employment and lower wages (Ichino 2019).

Large unions have a vested interest in regulating riders under at least two different dimensions. On one hand, they would gain a role in negotiating the riders' contracts and would attract new memberships from professions that until now have had no incentive whatsoever to join unions. On the other hand, and more crucially, structural transformations and (partial) labor deregulation have progressively reduced the attractiveness of being part of a union as well as the unions' ability to play a socially meaningful role in labor. One driver of this development is the employment shift from large manufacturing firms to smaller firms operating in the services industry. These smaller firms are less unionized and, on top of that, quite often rely on outsourcing labor to self-employed people (who are in many professions, such as lawyers, engineers, architects) or to workers who are somewhere in a gray zone between traditional employment and self-employment. Laws that restrict this gray zone by shifting larger shares of workers toward traditional employment and regulation would increase the role, influence, and power of trade unions. In this respect, regulating riders has a political meaning that goes well beyond the numbers of those involved. In waging the battle for labor regulation, large unions were actually fighting for their own survival rather than for the rights of riders. This is why they are the bootleggers in this case.

Large unions were so vocal on the rider issue that it made the headlines for a relatively long period. At the beginning of the summer of 2018,[3] then minister of economic development Luigi Di Maio chose riders for his first official meeting with an external stakeholder in the debate, a highly symbolic decision (*HuffPost* 2018). After several attempts to regulate riders, the government passed a decree in the summer of 2019 that introduced several obligations on online platforms. In particular, they are now required to

1. Provide riders with insurance against accidents at work, following the current regulation for regular employment, under which such insurance must be supplied by Inail, a state-owned company that is also the legal monopolist for insurance against accident at work for employed people;
2. Pay a minimum hourly wage to riders, which can be split into a fixed as well as a variable component, provided that the former accounts for the larger part.

Incidentally, it can be easily shown that under minimum-wage regulation, more efficient riders (i.e., those who make at least two to three deliveries per hour) would earn a lower wage (Cancelliere and Stagnaro 2019). Despite the vocal opposition from online platforms as well as from many riders, the legislative proposal was eventually passed, notwithstanding the large evidence that riders would not benefit from the new

3. I was no longer working at the ministry when all this happened.

regulation, insofar as (1) most online platforms already provided insurance supplied by private insurers, and (2) while the less-efficient riders would gain from the minimum wage, the most efficient ones would lose (unless they put in practice offsetting behaviors, such as working with several platforms simultaneously). At the same time, platforms will need to adjust their business models by relying on a larger number of less-efficient riders. Moreover, the cost of complying with the new regulation is likely to work as a barrier to entry in the market. As a consequence, existing online platforms—which are harmed by the regulation in the short run—may benefit from lower competition in the long run. The interests of customers and third parties (such as restaurants) have not been considered at all and are likely to be harmed, too, if lower competition drives prices of intermediation services upward.

The outcome from this political process is clearly such that social welfare has been decreased. Baptists (i.e., the small groups of riders calling for greater "protection" and "worker's rights") and bootleggers (i.e., the large trade unions struggling to play a role even within those industries that do not rely on traditional labor relations) openly cooperated to achieve the outcome of this affair: each group had its own distinct agenda in the sense that the "unionized riders" wanted to take the leadership of a larger group of workers, whereas unions were looking for a sort of Trojan Horse to get into an industry they had not been able to penetrate until then. The awareness that the two agendas were broadly consistent with each other led both groups to reach out and cooperate, to the point that some rider associations became openly affiliated with the unions. Without this effective, conscious cooperation between bootleggers and Baptists, the support for industry regulation and the public attention on the issue would have not been as high, and the probability of the new regulation passing would have been accordingly lower.

Coordinated Interaction: The Airbnb Tax

In 2017, Italy introduced two taxes on digital products: a webtax applicable to every business-to-business online transaction above a certain threshold, and the so-called Airbnb tax on short-term rentals. Both taxes make the consumption of digital products relatively more expensive than that of traditional products. A tax increase on online rentals, for example, would make hotel accommodation through offline channels relatively less expensive, all else being equal. To understand where these taxes come from, a digression is required.

Taxation of digital products is a very large and complex issue (Cockfield 2014). Taxes are traditionally due where value is created (for example, a manufacturer would pay its corporate income taxes in the jurisdictions where its facilities are located, not where its products are sold, even though complex architectures can be created for the sake of tax avoidance). It is relatively easy to tell where the manufacturing of a physical product takes place and how high the underlying costs—whether fixed or variable—are. In contrast, the cost of a digital product may depend to a large extent on intellectual

property, which in turn can be shifted to a different jurisdiction than where the research was performed in the first place. Moreover, variable costs are very low or even nil, which makes issues of within-firm transfer prices even trickier. As a consequence, online operators can and often do organize themselves in order to artificially shift revenue and profit streams to minimize their tax burden. To what extent this is a legitimate behavior rather than an abuse is far from obvious. The Organization for Economic Cooperation and Development (2019) is leading a multilateral effort to achieve a shared approach to taxation of multinational companies in general and of digital profits in particular. A report prepared for the EU Parliament estimated that corporate tax avoidance all over the EU may amount to somewhere between 50–70 billion euro and 160–190 billion euro annually and that the location of intangible assets is partly responsible for this alleged tax gap (Dover et al. 2015). These estimates may or may not reflect reality. What matters, though, is that (1) there is a serious debate on corporate tax avoidance, of which digitalization may be a driver, and (2) this issue should be (and is being) addressed at the international level because the problem itself stems from multinational companies' ability to shift their tax base to low-tax jurisdictions.

In the Italian public debate, this complex reasoning was translated into the commonsensical but wrong belief that (digital) multinationals evade taxes, so they should be forced to pay what is due. This idea is so deeply rooted in the Italian culture that even the head of the Italian Competition Authority, the country's antitrust body, Roberto Rustichelli, devoted much of his first annual report to international tax issues, arguing that corporate tax avoidance is a major blow to competition (Rustichelli 2019). Although that may or may not be true, it should be emphasized that international tax policy is well outside the Competition Authority's mandate and that lack of competition is a major driver of Italy's stagnant economy (Lanau and Topalova 2016).

How is it possible that complex tax issues are popularized in such a skewed way? One possible answer is that the debate on tax avoidance provides a useful foil to hide other issues—that is, rent seekers' hopes to restrict competition from innovative digital companies through tax policy. Richard Posner's (1971) intuition that regulation can be designed to act the same way as a tax can be turned upside down: taxes can be designed that result in the same outcome as a regulation. Therefore, digital taxation offers a fertile ground for rent seekers who feel competitive pressure from digital companies. Italy introduced two ad hoc taxes on digital companies in 2017: the so-called Airbnb tax on short-term rentals (in force since June 2017) and the so-called webtax on online transactions (which I do not deal with in this paper).[4] The former provides that both online and offline intermediaries, such as the home-sharing platform Airbnb, should pay rental taxes of 21 percent on behalf of hosts. However, if hosts have a right to a lower rate (which is the case for low-income individuals), a tax credit will be issued to the intermediary equal to the difference between the

4. For a more detailed appraisal of the webtax, see Falasca and Del Prato 2018 and Trovato and Zuluaga 2018.

amount paid to Italy's tax authorities and the correct amount. This tax has at least two consequences that are relevant from a competition perspective: (1) the intermediary pays taxes in advance that it will only recover later, resulting in a liquidity cost that traditional operators (hotels) are not required to bear; (2) if the intermediary collects tax credits exceeding the amount of taxes that it should pay, its tax rate is effectively raised. Enforcement is also somewhat problematic and generates extra costs for intermediaries (Sbroiavacca 2018).

What is interesting from this paper's perspective, though, is not whether the tax will prove effective but how the political consensus was created to get it passed by the Parliament. Identifying who the bootleggers are in this case goes without saying: Italy's hotel owners association, the Federalberghi, had been lobbying for a long time for a special tax on online rentals. It may be surprising that prominent politicians saw an opportunity to please their constituencies while presenting themselves as immaculate defenders of the national interest—or, within our framework, as Baptists.

Federalberghi's argument was that traditional hotels cannot match Airbnb offers because of Airbnb's unfair competition. Airbnb is an intermediation platform that allows apartment owners to rent them for a short period of time. To some extent, Airbnb does compete with traditional hotels: after all, its customers seek an accommodation that might be provided by hotels, too. However, the product being sold is different: an hotel provides a bundle of services that go well beyond the mere availability of a room (including but not limited to room cleaning, breakfast, a restaurant, etc.). A further point is that Airbnb is not the owner of the apartments: it just makes the matching between demand for accommodation and supply of locations easier and less costly. Hence, Airbnb is not and should not be held responsible for apartment owners' tax compliance. According to Federalberghi (2018), most apartment owners do not pay their taxes on the income they receive from rentals, which makes Airbnb their "partner in crime." No hard evidence has ever been provided for this claim, yet it made the headlines and became common wisdom. To offset the alleged tax avoidance by apartment owners, Federalberghi called for Airbnb to be required to pay taxes on the apartment owners' behalf—effectively raising both the fiscal burden and the cost of compliance for the online platform.

Federalberghi became particularly aggressive in its campaign against Airbnb in 2017. There had previously been little chance that its proposals would be passed. The government itself was skeptical about the proposals' effectiveness as well as about their legitimacy within the EU rules on digital markets. In 2017, though, two prominent politicians took the lead, also calling on Federalberghi to increase their political firepower. In the Chamber of Deputies, then chairman of the Budget Committee Francesco Boccia (DP) started a campaign to tax digital services, with particular regard to short-term rentals (the reader may recall that Boccia was a main character in the Flixbus case, too). In the Senate, Bernabò Bocca echoed Boccia's requests, making them even more pressing. Incidentally, Bocca—who was a member of the opposition party Forza Italia (Forward Italy)—was also serving as the president of Federalberghi

because no Italian law forbids a member of the Parliament from chairing a business association.[5]

Increasing pressures from Boccia in the Chamber and Bocca in the Senate made the Airbnb tax a major issue in Italian politics and gained large coverage in the media. As chairman of the Budget Committee, Boccia could push the proposed tax to a position very high on the legislative agenda. The reform was successfully presented as a way to force online platforms (such as Airbnb) to pay the "right" amount of taxes, even though it actually introduced disproportionate obligations insofar as intermediaries such as Airbnb were required to file tax communications and pay taxes on behalf of third parties (i.e., apartment owners).

The story of the Airbnb tax (which Airbnb is currently challenging in court) provides a useful example of coordinated interaction: politicians themselves provided a moral justification for a new regulation (or a tax, as in this case). The political climate they created mobilized a large amount of lobbying, both from the beneficiaries (hotel owners) and from the targeted victims (Airbnb and other online intermediaries). The convergence between political Baptists and entrepreneurial bootleggers resulted in the Airbnb tax being introduced into the tax code despite the concerns from tax experts regarding its effects and the warnings that it would distort competition and harm consumers rather than raise additional tax revenues. When politicians turn into Baptists, being a bootlegger may be a profitable occupation.

Conclusion

The bootleggers-and-Baptists model, originally introduced in the early 1980s, continues to be useful in explaining and predicting the outcomes of the political process by focusing on how rent-seeking agents can maximize their effectiveness by increasing the awareness of the beneficiaries of regulation and lowering the political cost of consensus from those who may be harmed by regulation itself. The model focuses on explicit or implicit cooperation between pressure groups who have a direct benefit from the regulation (either in terms of money or in terms of a reduction in potential and actual competition) and others who have an ideological return from or identification in regulation.

In this paper, I have shown that B&B theory can explain the emergence of regulation in the digital world. To illustrate, I have provided three cases that I observed directly during my time at the Italian Ministry of Economic Development and one immediately after. In all these cases, Baptists—who had an ideological or (in one case) religious interest in regulation—joined forces with vested interests (the bootleggers) that resisted competition from online platforms. A defining feature of the issue is that digital competition does not necessarily entail lower *production* costs or greater

5. See the Federalberghi website at https://bit.ly/2x2XwYE (accessed July 1, 2019).

economies of scale but rather lower *transaction* costs. Even though bootleggers and Baptists come from the distant past, they are still among us.

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