

**Political Representation in Concentrated Industries:
Revisiting the ‘Olsonian Hypothesis’**

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Abstract

This paper considers whether highly concentrated industries are better represented in the political process, as Olson’s *Logic of Collective Action* suggests, and, if they are, whether this is so for the reasons that the *Logic* claims. It begins with a review and critique of the quantitative literature that has largely tried and failed to substantiate Olson’s view. The bulk of the paper consists of five longitudinal case studies of firms that dominate or have dominated industries: IBM, Intel, Microsoft, America Online, and Cisco. The cases suggest that there is merit to the Olsonian view, but that alone it does not constitute an adequate political theory of the concentrated industry or the dominant firm. Additional variables drawn from organizational and institutional theory need to be incorporated into such a theory, including variables that bear on the allocation of attention, threat perception, and information flow within dominant firms.

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¹ Acknowledgments omitted to preserve anonymity.

Introduction

*The Logic of Collective Action*² has stimulated an extraordinary range of research. In applications as diverse as military alliances, state formation, and environmental policy³ (to name but a few), political scientists have explored the free rider problem and solutions to it. *The Logic* itself focused on interest groups in U.S. politics and, in so doing, fundamentally reshaped that field and, indeed, the study of interest groups the world over.

To be sure, not all of the attention focused on *The Logic* has been adulatory.⁴ Many a career has been built around qualifying or criticizing the book. Yet, in general, the more likely a political actor seems to approximate the assumptions of rationality inherent in Olson's framework, the more likely scholars are to accept his conclusions. Businesses, in particular, seem likely to fit the framework. It is not surprising, then, that studies of business in politics, especially those done by economists and political scientists who have adopted econometric techniques, tend to take *The Logic* for granted.

Yet, to the extent that empirical researchers have attempted to substantiate *The Logic* with respect to business (an effort which has not yet received the effort that it warrants), they have achieved mixed results at best. Mixed results even characterize tests of the

² Mancur Olson, *The Logic of Collective Action* (Cambridge: Harvard University Press, 1965).

³ Mancur Olson, Jr., and Richard Zeckhauser, "An Economic Theory of Alliances," *Review of Economics and Statistics* 48:266-279 (1966); Margaret Levi, *Of Rule and Revenue* (Berkeley: University of California Press, 1988); Elinor Ostrom, *Governing the Commons: Evolution of Institutions for Collective Action* (New York: Cambridge University Press, 1990).

⁴ This literature in the U.S. interest groups area is reviewed in Frank R. Baumgartner and Beth L. Leech, *Basic Interests: The Importance of Groups in Politics and Political Science* (Princeton: Princeton University Press, 1998). Broader reviews can be found in Jan Potters and Randolph Sloof, "Interest Groups: A Survey of Empirical Models that Try to Assess Their Influence," *European Journal of Political Economy* 12:403-442 (1996); and Fran van Winden, "On the Economic Theory of Interest Groups," *Public Choice* 100:1-29 (1999)

archetypal "Olsonian hypothesis"⁵: that highly concentrated industries are more likely to be represented in the policy-making process than less concentrated ones. Unfortunately, results that fail to support this hypothesis are often simply ignored or wished away. Only a few scholars have taken such results seriously enough to begin to modify Olson's formal model in order to try to account for the apparent anomalies.⁶

This paper takes an alternative approach to the challenge of reconciling theory and data. Rather than elaborating Olson's model, I dig into the data more deeply by examining a set of important cases. The ultimate end is the same: a better political theory of concentrated industries and dominant firms. This objective is important, because businesses are the most numerous and among the most powerful interest organizations in the U.S., and American businesses are increasingly exporting their approach to politics to the rest of the world.⁷ Traditional interest group theory in U.S. politics, extending well beyond Olson, simply does not fit business very well.⁸

⁵ I use this term to allude to the "Schumpeterian hypothesis," which is well-known in the field of industrial organization. Joseph A. Schumpeter, *Capitalism, Socialism, and Democracy* (New York: Harper and Row, 1942) argued that more concentrated industries are more technologically innovative than less concentrated ones for reasons that are roughly similar to those that underlie the Olsonian hypothesis.

⁶ Paul Pecorino, "Is There a Free Rider Problem in Lobbying? Endogenous Tariffs, Trigger Strategies, and the Number of Firms," *American Economic Review* 88:652-660 (1998); Devasish Mitra, "Endogenous Lobby Formation and Endogenous Protection: A Long-Run Model of Trade Policy Determination," *American Economic Review* 89:1116-1134 (1999); R. Damania and P.G. Fredriksson, "On the Formation of Industry Lobby Groups," *Journal of Economic Behavior and Organization* 41:315-335 (2000); Wen Mao and Peter Zaleski, "The Effect of Industry Concentration on Free Riding," *Review of Industrial Organization* 19:295-303 (2001); Paul Pecorino, "Market Structure, Tariff Lobbying, and the Free Rider Problem," *Public Choice* 106:203-220 (2001).

⁷ Frank R. Baumgartner and Beth L. Leech, "The Business Advantage in the Washington Lobbying Community: Evidence from the 1996 Lobbying Disclosure Reports," Midwest Political Science Association, 1999; David Coen, "The Impact of US Lobbying Practices on the European Business-Government Relationship," *California Management Review*, Summer, 1999, 27-44.

⁸ The reasons were stated succinctly by Robert H. Salisbury, "Interest Representation: The Dominance of Institutions," *American Political Science Review* 78:64-76 (1984). I develop this point at length in a forthcoming article.

In the next section, I review the literature built around the Olsonian hypothesis and critique the way the hypothesis has been conceived and operationalized. The empirical meat of the paper draws on case studies of five firms that dominate or have dominated their industries. I analyze how these firms first came to be represented in Washington and how the scale and scope of their representation has evolved. I conclude by offering insights from the case studies for future quantitative and qualitative research. I argue in particular for relaxing the assumptions of rational action that underlie the Olsonian approach and seeking to model the attention thresholds and communication patterns that shape the political decisions (and non-decisions) of senior executives in the dominant firms that I studied.

The Olsonian Hypothesis: Theoretical Propositions and Empirical Findings

To restate the Olsonian hypothesis in its baldest form: highly concentrated industries are more likely to be represented in the policy-making process than less concentrated ones. Its logic is straightforward. An industry that has many producers, like agriculture, faces significant barriers to collective action. It is expensive to identify the beneficiaries of a favorable public policy measure and difficult to convince enough of them that a joint effort seeking its enactment will come to fruition in the absence of selective incentives unrelated to public policy. Free riding on the efforts of others, the argument goes, is likely under such conditions. Such an industry, much like other diffuse societal groups, such as consumers, workers, and even "business" as a whole, will tend to be "latent," by which Olson means having a shared political interest but remaining unrepresented.⁹

Concentrated industries like the "Big 3" U.S. auto manufacturers, on the other hand, face relatively low transaction costs in mobilizing to secure collective goods. Each member of such an industry knows all of the others and can estimate with relative ease the costs and benefits associated with efforts to secure government assistance. Incentives to free-ride are minimized, and sanctions against doing so are strong. Such an industry will either be "privileged" or "intermediate," in Olson's terms, but it will not be "latent." Although strategic considerations complicate small group interactions making "outcomes in particular cases...indeterminate," Olson states, "the essence of the relationship between the size of the group...and the extent of collective action is beautifully simple..."¹⁰

⁹ Olson, 1965, *op. cit.*, 49-50.

¹⁰ Mancur Olson, *The Rise and Decline of Nations* (New Haven: Yale University Press, 1982), 30.

Perhaps it is the theoretical beauty of the relationship that leads to the Olsonian hypothesis being “generally accepted,”¹¹ because, as one recent contribution put it, the “empirical work does not bring clarity.”¹² Research that has attempted to link industrial concentration to trade policy outcomes, such as protectionist trade barriers, is at best “subject to interpretation” and more plausibly, “disappointing.”¹³ Efforts to test directly the relationship between industrial concentration and political activity (an intermediating variable in trade policy models that is often omitted¹⁴) also tend to find that it lacks statistical significance.¹⁵

Two papers by Grier, Munger, and Roberts (GMR), however, represent a major exception to this tendency. GMR find support for the Olsonian hypothesis, and the quality of their analysis gives heft to the “generally accepted” view.¹⁶ GMR’s work is therefore worth considering in some detail to substantiate the value of revisiting the Olsonian hypothesis.

¹¹ Douglas A. Schuler, “Corporate Political Action: Rethinking the Economic and Organizational Influences,” *Business and Politics* 1:83-97 (1999), 88.

¹² Damania and Frederiksson, *op. cit.*

¹³ Mao and Zaleski, *op. cit.*; Dani Rodrik, “The Political Economy of Trade Policy,” in Gene Grossman and Kenneth Rogoff, eds., *Handbook of International Economics*, vol. 3 (Amsterdam: Elsevier Science, 1995), 1458-1494. Tax policy is another area in which the Olsonian hypothesis has been tested in one form or another. See Carla Inclan, Dennis P. Quinn, and Robert Y. Shapiro, “Origins and Consequences of Changes in U.S. Corporate Taxation,” *American Journal of Political Science* 45:179-201; John T. Williams and Brian K. Collins, “The Political Economy of Corporate Taxation,” *American Journal of Political Science* 41:208-244; and Dennis P. Quinn and Robert Y. Shapiro, “Business Political Power: The Case of Taxation,” *American Political Science Review* 85:851-874 (1991).

¹⁴ Gene M. Grossman and Elhanan Helpman, “Protection for Sale,” *American Economic Review* 84:833-850 (1994), 835, for instance, state “we do not at this point have a theory of lobby formation.”

¹⁵ A few of these papers are Daniel C. Esty and Richard E. Caves, “Market Structure and Political Influence: New Data on Political Expenditures, Activity, and Success,” *Economic Enquiry* 21:24-38 (1983); Asghar Zardkoohi, “On the Political Participation of the Firm in the Electoral Process,” *Southern Economic Journal* 51:804-817 (1985); Frank R. Lichtenberg, “Contributions to Federal Elections Campaigns by Government Contractors,” *Journal of Industrial Economics* 38:31-48 (1989); and Neil J. Mitchell, Wendy L. Hansen, and Eric M. Jepsen, “The Determinants of Domestic and Foreign Corporate Political Activity,” *Journal of Politics* 59:1096-1113 (1997).

¹⁶ Kevin B. Grier, Michael C. Munger, and Brian E. Roberts, “The Industrial Organization of Corporate Political Participation,” *Southern Economic Journal* 57:727-738 (1991); and Kevin B. Grier, Michael C. Munger, and Brian E. Roberts, “The Determinants of Industrial Political Activity, 1978-1986,” *American*

As befits followers of Olson, GMR's theoretical exposition focuses on the free rider problem. They assume that industries seek to maximize profits and that the government may help them to do so if they can overcome the barriers to collective action in lobbying. Other things being equal, more concentrated industries are more likely to be able to overcome these barriers. However, in an interesting twist on the Olsonian hypothesis, GMR argue that other things are not always equal. In particular, the most concentrated industries, they argue, may be less politically active because the benefits that they would receive from government action are small. Given their low costs of collective action, such industries can accomplish more cheaply through private efforts (such as "self-regulation" and collusion) what might require government intervention to achieve in less concentrated industries. Thus, GMR predict that concentration will have a negative effect on political activity at the high end of the range. And, this is indeed what they find, with the effect neatly peaking just below the mean level of concentration in their subsample of 110 industries and turning negative when the four largest firms control 70% or more of the market.¹⁷

GMR's theoretical approach raises at least two significant concerns. One is the assumption that industries, rather than firms, maximize profits. Firms in an industry may well seek to maximize profits by taking sales from one another; indeed, most business strategies are directed at rivals. Much firm-level political activity may therefore be

Political Science Review 88:911-926 (1994). I will focus in the text on the latter article, since it is more refined and elaborate.

¹⁷ In GMR's 124 industry sample (for which they were able to gather fewer independent variables than the 110 industry subsample), three of four estimates of the effect of concentration on political activity are

oriented to “private goods,” such as government contracts that might otherwise be won by competitors.¹⁸ By making the industry the unit of analysis, GMR are unable to rule out the possibility that representation is motivated by intra-industry rivalry.

The other issue is the privileging of opportunity over threat in GMR's exposition.

Industries (and individual firms within them) may take political action in order to mitigate risks or bolster their legitimacy, rather than to secure tangible gains.

Maintenance of the status quo may well be considered a victory for a threatened industry, yet such motivation would not be captured in their framework.¹⁹

GMR's operationalization has significant weaknesses as well. They pool five election cycles together (1978-86), but use a single estimate of industrial concentration as an independent variable for all of these cycles. The interpretation of the parameter that this approach yields may be doubted if either the true values of industrial concentration do change or the measured levels of political activity do not change during this period.²⁰

Moreover, the cross-sectional approach cannot capture dynamic processes, such as strategic interactions of the sort alluded to by Olson, that might complicate the interpretation of the relationship between the two variables.

insignificant at the .05 level. The four firm concentration ratio is a standard measure for concentration in industrial organization.

¹⁸ R. Kenneth Godwin and Barry J. Seldon, “What Corporations Really Want from Government: The Public Provision of Private Goods,” in Cigler and Loomis (2002), *op. cit.*. See also Lichtenberg (1989), *op. cit.*. Obviously, the assumption of collective action is a general problem with the Olsonian paradigm.

¹⁹ GMR do employ cumulative antitrust indictments and regulation as independent variables that might be construed as proxies for threat, but they do not interpret these variables as such. Two other independent variables, import share and wage rates, are interpreted in something like this fashion.

²⁰ If measured political activity is static, then the five cycles ought to be collapsed to one, which would produce larger confidence intervals. Industrial concentration data are collected by the Census every five years (years that end in 2 and 7) and are released about three years later. GMR might have interpolated,

GMR use a measure of industrial concentration that is notoriously problematic. They aggregate data provided by the U.S. Census at the 4-digit SIC level to create measures of the market share of the largest four firms in each 3-digit SIC industry.²¹ Yet, even 4-digit industries may not be homogeneous enough to share political interests, much less 3-digit industries.²² Semiconductor manufacturing, for instance, is a 4-digit industry.

Microprocessors are one of many products made by semiconductor manufacturers. Intel is estimated by most observers to have maintained a roughly 80% market share in microprocessors for the past decade or more, a level of concentration that has regularly drawn scrutiny from U.S. antitrust enforcement authorities and may therefore be considered relevant for political purposes. Yet, the four-firm concentration ratio in this industry at the 4-digit level was only 41% in 1992. Aggregating semiconductor manufacturing with other industries in its 3-digit classification, which encompasses a wide variety of electronic components, would bring the level down much further.²³

GMR treat average firm size in addition to industrial concentration as an independent variable that bears on the capacity to overcome barriers to collective action. “[I]n Olson’s (1965) framework,” they write, “the key element is the absolute size of benefits

using data from 1977 and 1987 (if these data were available at the time of the research), to get some variation on this independent variable, although this choice, too, has its problems.

²¹ The larger the number of digits in the SIC scheme, the broader the industry definition. Thus, 2-digit industries include a number of 3-digit industries, and 3-digit industries include a number of 4-digit industries. The SIC system has now been superseded by the NAICS system.

²² Russell J. Pittman and Gregory J. Werden, "The Divergence of SIC Industries from Antitrust Markets," *Economic Letters* 33:283-286 (1990).

²³ The Census only produces concentration estimates for manufacturing industries, but estimates from other sources used in the recent Microsoft trial (software is considered to be a service industry, not a manufacturing industry) produced similar measurement debates. GMR make an effort to address this concern by including a dummy variable for the diversity of production. Firms that make a wider range of

to the individual.”²⁴ GMR are mistaken on this point, confusing firm size and market share. The key element in the framework is the ratio of individual-level benefits to individual-level costs. In a very large industry with lots of large but equal-sized firms, barriers to collective action may still be quite high according to the *Logic*, since the benefits of collective goods would be widely diffused. If industrial concentration is properly controlled for, firm size should not matter from Olson’s perspective. There are other reasons to think that firm size might matter, such as the fixed costs of specialization in government affairs within an organization and of political representation in Washington, but we should not interpret the significance of the relationship between firm size and political activity to validate the Olsonian hypothesis.²⁵

GMR take as their dependent variables (1) whether or not any firm in an industry maintains a political action committee (PAC) and (2) how much all of the PACs in an industry combined contributed to House candidates in a given election cycle. The match between these measures and Olson’s theoretical dependent variable, political representation, is not very good, although the effect of the mismatch may lead GMR in this case to underestimate the empirical support for the Olsonian hypothesis. As Virginia Gray and David Lowery have argued, the dichotomous variable of PAC formation should be seen as a tactical choice made by a firm that has already established political

products that are lumped together in the same 3-digit SIC, according to their argument, will likely have fewer common interests than those that make a narrower range.

²⁴ GMR (1994), *op. cit.*, 915.

²⁵ GMR actually allude to the fixed costs of representation, but only to justify using a probit model. Olson (1965, 143-144) states “When a large firm is interested in legislative or administrative regulations of unique importance to itself, there is little doubt it will act in its interest.” Olson seems to be referring to a private good, rather than a collective good. Interestingly, the confusion between firm share and market size in the literature about the Olsonian hypothesis is paralleled by a similar confusion in the literature on the

representation in some form.²⁶ Some firms with government affairs departments or senior executives active in public policy choose not to form PACs. On the other hand, GMR equate the existence of a single PAC in an industry with the overcoming of collective action barriers, an interpretation that is doubtful if many firms create PACs in order to pursue private goods.

The continuous variable PAC size (available, of course, only for that subset of industries in which at least one firm maintains an active PAC in the first place) is determined by a wide range of factors in addition to the firm's desired level of representation, which GMR presume it measures. These factors include the Congressional districts within which the firm's facilities happen to lie, the committees with jurisdiction over its key issues, and the views of the managers within the firm from whom the PAC must raise funds. GMR's focus on PACs is widely shared in the literature and provides an excellent example of what Godwin and Seldon call the "streetlamp problem" – looking only where the data are most easily available.²⁷

I want to reiterate that GMR's work is among the best available on this subject. Their efforts to overcome empirical difficulties and find a relationship between industrial

Schumpeterian hypothesis. A significant relationship between firm size and political representation has been validated in many studies.

²⁶ Virginia Gray and David Lowery, "Reconceptualizing PAC Formation: It's Not a Collective Action Problem and It May Be an Arms Race," *American Politics Quarterly* 25:319-346 (1997). See also Wendy L. Hansen and Neil J. Mitchell, "Disaggregating and Explaining Corporate Political Activity: Domestic and Foreign Corporations in National Politics," *American Political Science Review* 94:891-903 (2000).

²⁷ Godwin and Seldon (2002), *op. cit.*, 206. To the extent that the trade and tax policy literatures measure political representation, they rely almost exclusively on campaign contributions. Collins and Williams, *op. cit.*, for instance, state (223) mistakenly that "almost all corporate and noncorporate interests do organize PACs." Data from lobbying reports have begun to ease this problem. Schuler, *op. cit.*, among others, has taken the important step of measuring representation using multiple indicators, as discussed in the conclusion to this paper, but this approach is not yet standard.

concentration and political behavior are impressive. Others do worse, often much worse. That such good work should nonetheless leave so many doubts justifies, as Kathleen Rehbein and Douglas Schuler put it, a “[return] full circle to the richness of historical information, such as that recorded by Epstein (1969) in his classic analysis...”²⁸

Five Cases

This section explores the political development of five firms -- America Online (AOL, now AOL Time Warner), Cisco Systems, Intel, International Business Machines (IBM), and Microsoft -- from their foundings through the end of 2000. I have used public documents, archival materials, and interviews to create capsule corporate political histories. These case studies are "heuristic," according to Harry Eckstein's typology. They serve to generate hypotheses and to provide feedback to scholars, like Grier, Munger, and Roberts, who are conducting large *n* research.

Eckstein maintains that case study research is particularly appropriate when the research subject is a "complex collective individual."²⁹ Eckstein had nations in mind, but it is not inappropriate to conceive of large firms in this way as well. Wal-Mart, which ranked first in *Fortune's* annual list of the 500 largest U.S. companies for 2001, had revenues of \$220 billion (larger than the gross domestic product of all but twenty nations) and employed 1.4 million people in 2001. The simplifications required by large *n* studies, such as depicting nations and firms as unitary actors, can obscure important causal processes.

²⁸ Kathleen A. Rehbein and Douglas A. Schuler, "Testing the Firm as a Filter of Corporate Political Action," *Business and Society* 38:144-166 (1999), 160. The reference in the quote is to Edwin M. Epstein, *The Corporation in American Politics* (Englewood Cliffs, NJ: Prentice-Hall, 1969).

Like the unitary actor conception of the nation in international relations, the unitary actor conception of the firm has an important place in the study of business and politics, but it deserves to be complemented by richer, more textured, small *n* research.³⁰

No five firms could be a representative sample, and this group certainly is not. Some of this group's peculiarities, however, are virtues with reference to the task set by Eckstein. All five firms dominate or have dominated in the past the main markets in which they compete; indeed, all have drawn attention from the antitrust enforcement authorities at some point as a result of their market positions. Compared in their periods of maximum market power, the cases allow one to explore the reasons that dominant firms seek political representation, rather than simply imputing the Olsonian interpretation. Just as Cathie Martin has explored "how size matters,"³¹ this study comments on "how concentration matters."

Yet, with the exception of IBM,³² the cases trace the firms from start-up to dominance. Their political capabilities can therefore be compared when their market shares were small as well as when they approached or attained monopoly power. This longitudinal variation in the level of concentration yields insights into the development of political

²⁹ Harry Eckstein, "Case Study and Theory in Political Science," in Fred I. Greenstein and Nelson W. Polsby, eds., *Handbook of Political Science, Volume 7: Strategies of Inquiry* (Reading, MA: Addison-Wesley, 1975), 79-137, esp. 104-108. Quote from 121.

³⁰ Richard M. Cyert and James G. March, *The Behavioral Theory of the Firm* (Englewood Cliffs, NJ: Prentice-Hall, 1963); David J. Vogel, "The Study of Business and Politics," *California Management Review* 38:146-165 (1996).

³¹ Cathie J. Martin, *Stuck in Neutral: Business and the Politics of Human Capital Investment Policy* (Princeton: Princeton University Press, 2000), 125.

³² IBM was founded more than a half-century before the other four firms, and it entered the IT industry from a related field, in which it was well-established. The early years of IBM are covered only briefly in the capsule history.

capabilities that the cross-sectional approach misses. In some cases, for instance, representation predates concentration, and it may be that there is some simultaneous causation of the two by another factor, such as leadership.³³ The longitudinal dimension also allows me to explore the notion of representation in ways that are much more subtle than the dichotomous variable used, for example, in probit models.

Another interesting feature of this set of cases is that these firms interact over time. Microsoft, for instance, was first the partner of and then supplanted IBM as the dominant firm in the operating systems software market. These interactions permit some insights into the "indeterminate" small group dynamics that Olson alludes to. Not all of these interactions are mediated by the market, however. In some cases, one or more of the five firms serve as the reference group for another of the five, even though the firms are not head-to-head competitors. They think of themselves and are thought of by outside observers as being in the same "industry," and therefore they may respond to similar environmental signals or learn from one another.³⁴

The "industry" that these firms belong to, of course, is information technology (IT). IT has at least two features worth noting. One is that the malleability of IT leads to abrupt shifts in competition and in the boundaries of markets. Indeed, it may call into question the concept of industrial concentration, as Microsoft's advocates in its antitrust travails

³³ Reverse causation, in which political representation leads to greater concentration, is also a possibility, as in the case of the early AT&T. However, my cases do not illustrate it.

³⁴ Paul J. DiMaggio and Walter W. Powell, "The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields," *American Sociological Review* 48(2):147-160 (1983); Neil H. Fligstein, *The Transformation of Corporate Control* (Cambridge: Harvard University Press, 1990).

have argued.³⁵ IT firms are often simultaneously competitors and collaborators, and that may make it difficult for them to identify collective goods. The other feature is the sector's rapid growth. Processes that take longer to occur and might be more difficult to observe elsewhere in business and politics are easier to observe in this one. There is a parallel to the molecular biologist's fruitfly, which is a popular research subject because it reproduces and mutates rapidly.

While not typical, then, these five cases should enrich the political theory of the firm, especially the dominant firm. These cases may also serve as harbingers of the future. The knowledge-based economy seems to be characterized by "winner-take-all" markets,³⁶ in part because it is increasingly infused with IT. Dominant firms in general would become more important if this prediction is borne out, and these future firms would be more likely to resemble the five firms considered here than the behemoths of the "old economy." The capsule histories are presented in the order, roughly speaking, in which the five firms attained dominance: IBM, Intel, Microsoft, AOL, and, finally, Cisco.³⁷

³⁵ The apparent paradox here is explained by the fact that a firm that is dominant in one market may choose to enter a market which is dominated by another firm. Microsoft, for instance, is the dominant firm in the personal computer software industry, but with the introduction of Microsoft Network (MSN), it challenged AOL in the internet service provision (ISP) market, which AOL dominates.

³⁶ Carl Shapiro and Hal R. Varian, *Information Rules* (Boston: Harvard Business School Press, 1999), 173-226.

³⁷ A note on sources for the case studies: I have conducted interviews with a range of individuals knowledgeable about the government affairs activities of the five firms, including in most cases, employees of the firms themselves. As often as possible, I have asked for on-the-record interviews and where this request has been agreed to, the footnotes reflect that. Where the subject has asked to be interviewed off the record, I have acceded if there is no alternative; some facts in the text are therefore unsourced. Lobbying expenditure and campaign contribution data are drawn from the database of the Center for Responsive Politics <www.opensecrets.org>.

IBM

IBM was founded in 1911; by the 1930s it had become the dominant firm in the punchcard tabulating industry. The Federal government was one of the firm's largest customers. Thomas Watson, Sr., the firm's founder and CEO, befriended and supported President Franklin D. Roosevelt. Thomas Watson, Jr., who succeeded his father at IBM's helm in 1956, struck up an even closer relationship with President John F. Kennedy. Tom's brother Dick, also a high-ranking IBM executive, personally handled relationships with the Republican side of the aisle during most of the decade and a half that his brother ran IBM. By the 1960s, IBM had made the transition to computers, dominating the new industry to the point that observers dubbed it "IBM and the seven dwarves."³⁸ The firm had extensive political capabilities, but they would not have been measurable using the indicators employed by most contemporary scholars.

Watson, Jr., was deeply committed to the one-on-one approach to government affairs. Not until the firm came under severe threat did he consent to hire a consultant to advise IBM management on public policy strategy, and even then the consent was contingent on assurances that the consultant was not a "lobbyist."³⁹ The threat was mounted by the so-called "dwarves," who lobbied the Justice Department to sue IBM for antitrust violations, which it did in January, 1969. Even then, IBM remained surprisingly complacent, the consultant's advice notwithstanding, initially viewing the suit as "less an

³⁸Norman Gelman, interview by author, February 11, 1999; *Governmental Programs at IBM*, Harvard Business School case 8-389-109 (1988), 1; Leslie D. Simon, interview by author, May 14, 1999; Thomas J. Watson, Jr., and Peter Petre, *Father, Son, and Company* (New York, 1990).

³⁹ James Newmyer, interview, February 12, 1999.

investigation...than an exploration..."⁴⁰ Other threats to IBM, all from interests less concentrated in the Olsonian sense than IBM, such as unions, civil rights groups, and antiwar activists, followed in quick succession. Not long after Watson's departure from his leadership position in 1971, his successors began to institutionalize the firm's government affairs function, first at headquarters, and then, in 1975, by opening a Washington office.⁴¹

Once IBM had planted its flag in the capital, its political capabilities grew steadily, even as its dominance of the computer industry ebbed away. By the late 1980s, IBM employed nearly one hundred public policy professionals, enough to throw a person at nearly any issue. The firm exerted significant control over key industry associations, which provided it with an alternative "delivery system" for its messages and a mechanism for blocking the emergence of opposition from rivals, customers, and suppliers. Indeed, IBM's investment in Washington was so big that competitors like Digital Equipment Corporation (DEC) and Hewlett-Packard (HP) consciously (but somewhat uncomfortably) free rode on it.⁴²

In the early 1990s, IBM's business had eroded to the point of "total entropic meltdown."⁴³ It lost \$5 billion in 1992 and took the extraordinary steps of firing its CEO and hiring a new one from outside the computer industry. The Washington office

⁴⁰ Frank Cary, speech, June 5, 1969, Cary papers, IBM Archives. Cary became CEO in 1973.

⁴¹ Charles E. McKittrick, Jr., interview, February 10, 1999; Simon interview, *op. cit.*; Transcript, IBM Annual Meeting, April 30, 1973, IBM Archives; Barry Newman, "Churches Mount First Joint Campaign Against U.S. Firms in Southern Africa," *Wall Street Journal*, February 15, 1972, 11.

⁴² Douglas Worth, interview, June 4, 1999; Bob Kirkwood, interview, May 21, 1999; Bruce Holbein, interview, April 21, 1999.

⁴³ Doug Garr, *IBM Redux* (New York: Harper Business, 1999), 20.

suffered a cut of about 25-30%, bringing the firm's political capabilities into closer line with its market position. These reductions and the humbling of IBM produced more of a "level playing field" in trade associations in the view of at least one competitor.⁴⁴ One major association, for instance, underwent an image makeover in 1994 in part to dispel perceptions that it was a cat's paw of IBM. Yet, even after the crisis, IBM looms disproportionately large on computer industry policy issues. It continues to be able to cover more issues in more depth than any other firm in the sector.

Interestingly, IBM has never maintained a PAC or contributed soft money. Tarrred ever so slightly by scandal, the firm adopted a code of conduct that prohibited all political contributions in 1976. While executives loyal to the Watsons ran the firm, this decision was never seriously revisited. In the words one CEO, the possibility that IBM employees would feel pressured to support candidates was "counter to all the things that Tom and his father had promised."⁴⁵ The crisis of 1992 offered an opportunity to break from this tradition, but the benefits of preserving the firm's reputation as a source of relatively unbiased expertise ("a statesman," as one Congressional aide put it⁴⁶) have been judged to outweigh the benefits of making campaign contributions.

IBM's political development displays a pattern that younger high-tech firms echo. The firm had a rather casual involvement in politics until its competitors and societal opponents broadened the scope of conflict by engaging supporters in government. E.E. Schattschneider, rather than Olson, provides the most valuable analytic lens for

⁴⁴ Worth interview, *op. cit.*; Kirkwood interview, *op. cit.*.

⁴⁵ John Opel, interview, December 13, 1999.

interpreting this case.⁴⁷ Once IBM had been brought into the fight (to use Schattschneider's metaphor), it rapidly became a heavyweight. Indeed, a mismatch emerged between the firm's market position and its political capabilities, with the curious exception of campaign finance. In that realm, choices made early in the firm's political development seem to have constrained later choices.

Intel

Intel was founded in 1968 to produce semiconductor memory chips. Although it was a technological pioneer, the company struggled with production and market challenges; in the early 1980s, only an infusion of cash from its biggest customer, IBM, saved it from going under. Intel separated itself from its competitors in the late 1980s by concentrating on the microprocessor chips that became standard components in personal computers. Its representation in Washington, however, long predated its rise to dominant status.⁴⁸ The firm first had an employee testify before a Congressional committee in 1973, was a founding member of the Semiconductor Industry Association (SIA) in 1977, formed a PAC in 1980, hired a Washington consultant in 1982, and opened its own office there in 1986.

The motivating factor in Intel's political mobilization was Japanese competition. The company and many of its U.S. competitors believed that Japanese semiconductor

⁴⁶ Personal communication from Patrick Windham, September 27, 1999.

⁴⁷ E.E. Schattschneider, *The Semi-Sovereign People* (New York: Holt, Rinehart and Winston, 1960).

⁴⁸ Alfred D. Chandler, *Inventing the Electronic Century* (New York: Free Press), 155-157; Intel Corporation, "Defining Intel: 25 Years/25 Events," 1993. The founder of Intel's Washington office director notes that he originally borrowed space in the office of a competitor and fellow member of the SIA in late 1985 before establishing the Intel office proper the following year. Michael C. Maibach, letter to the editor, *Harvard Business Review*, September-October, 1988.

companies engaged in illegal anti-competitive practices. Despite the U.S. industry's fragmentation, it easily surmounted its collective action problems. The industry's leaders formed a tight-knit community (intense antagonism among some of the principals notwithstanding) and worked within a few miles of one another in Silicon Valley. They feared for the survival of their firms: "we're toast," as one Intel executive put it.⁴⁹ The SIA was said to have been formed over lunch at a Palo Alto Chinese restaurant by the CEOs of the leading firms, including Intel's Robert Noyce.

Noyce had particular value as a spokesman for the group; he was a brilliant inventor, a serial entrepreneur, and well-spoken and good-looking to boot. "He is a symbol," said one industry lawyer, "what people think of when they think of this industry."⁵⁰ In 1983, Intel hired its first full-time government affairs professional, Michael Maibach, whose main job was "to put Noyce on stage effectively." At first, Maibach was based at Intel's California headquarters. Like SIA as a whole, the firm preferred – for strategic, ideological, and operational reasons – to keep its distance from Washington. As the industry's campaign intensified and the circumstances of its members grew more dire, however, Maibach found himself spending the majority of his time there, to the point that he established a virtual Washington office on his own volition. Once open, it never shut.⁵¹

⁴⁹ Ted Jenkins, interview, November 29, 2001. Philip A Mundo, *Semiconductor Industry Association, in Interest Groups: Cases and Characteristics* (Chicago, 1992), 41-66.

⁵⁰ Bruce Stokes, "Sematech Chief's Personal Magnetism," *National Journal*, May 26, 1990, 1301, quoting Michael Gadbaw of Dewey Ballantine.

⁵¹ Michael Maibach, interview, June 15, 2000.

The semiconductor industry's campaign for assistance from the U.S. government in the mid-1980s produced significant results. The U.S.-Japan Semiconductor Trade Arrangement "managed" imports in both countries for the better part of a decade; the Sematech consortium received matching government funding to support R&D of value to the industry. Ironically, even though Intel played a leading role in this campaign (Robert Noyce became the first CEO of Sematech in 1988), the company changed its business strategy in the midst of it to focus on microprocessors and withdrew from the memory chip market, which was at the center of the debate.⁵² Nonetheless, having made an investment in Washington, Intel found that that it continued to reap a return on that investment even after the threat that prompted the investment in the first place was no longer relevant. Having just one person in Washington, senior management found, was "incredibly useful."⁵³

By 1988, a second person had been moved from the tax department at Intel's Silicon Valley headquarters to the Washington office, and the office continued to grow at a pace roughly proportional to the firm's growth after that. Intel has not faced a crisis since shifting its emphasis from memory chips to microprocessors. Interestingly, it seems to have taken on something like the "statesman" role that IBM played before its crisis. Intel Chairman Andrew Grove, for instance, broke from the conventional wisdom among high-tech executives on Internet privacy and taxation in 2000, arguing that a longer-term view of the sector's interests than was normally taken would lead to the conclusion that a

⁵² Andrew S. Grove, *Only the Paranoid Survive* (New York: Currency, 1996).

⁵³ Jenkins interview, *op. cit.*

larger role for government was inevitable and perhaps sensible in these areas.⁵⁴ Its statesmanship is also evident in its hiring of a former chief of staff of the Federal Communications Commission (FCC) to work on broadband policy, even though Intel neither provides broadband service itself nor supplies equipment directly to the providers.⁵⁵

The early phases of the Intel story echo not IBM, but IBM's competitors. Intel entered politics (however one chooses to measure entry) as one member (and not the largest) of an industry with unusually low transaction costs that sought to broaden the scope of conflict in the face of a grave threat from its Japanese rivals. Noyce represented the industry as much as the firm. Like IBM, however, once Intel was mobilized by threat, it soon found political opportunities in pursuit of which its capabilities could be deployed. Intel assumed command of its key markets in parallel with this political development. These processes are not causally related, but rather are both results of its leaders' choices. Unlike its early history, Intel's recent ascension to industrial statesmanship would not have surprised Olson. Secure in its position, it has the slack (or "bandwidth," as Intel executives like to say) to adopt a long-term and broad perspective of its interests.

⁵⁴ Ted Bridis, "Intel Chairman Says He Favors Sales Tax on Internet Purchases," *Wall Street Journal*, June 7, 2000, B6.

⁵⁵ Les Vadasz, interview, December 21, 2001. Broadband is a generic term for high-speed internet connections to homes and small businesses. Broadband service can be supplied through both telephone and cable television lines. Intel executives are quick to point out that their interest in broadband is not altruistic; broadband users typically own personal computers. But the policy is one step removed from the narrowest definition of the firm's self-interest.

Microsoft

Virtually every personal computer (PC) that uses Intel chips uses Microsoft software, too. Founded in 1975, Microsoft grew in parallel with (but even faster than) Intel as the PC market boomed in the 1980s. As early as 1985, Microsoft CEO Bill Gates was considered to be “the most powerful man in the personal-computer industry,”⁵⁶ and by the end of the decade, the firm had achieved a near-monopoly in PC operating systems. It had also begun to express its views in Washington, hiring a consultant there in 1988 and presenting Congressional testimony the following year. More important, Microsoft became active in industry associations, joining the Software Publishers Association (SPA) and helping to found the Business Software Association (BSA) in 1988.⁵⁷

These organizations focused on software piracy. Microsoft viewed illegal copying of its programs as a potential threat to its entry into new markets and estimated substantial revenue losses as a result. Concern about piracy also prompted the firm to hire a full-time government affairs professional at its Redmond, Washington headquarters at the end of 1991. Over the next few years, the resources devoted to this function slowly accreted and Microsoft’s policy agenda grew. After what the company’s director of government affairs later termed “a hard sell” to her superiors, Microsoft took “the next step” in 1995, hiring a full-time Washington representative.⁵⁸ His office, though, was not in the capital

⁵⁶Brenton R. Schlender, “Software Hardball: Microsoft’s Gates Uses Products and Pressure To Gain Power in PCs,” *Wall Street Journal*, September 25, 1987.

⁵⁷ Mitch Betts, “Software Firms Unite, Aim to Keelhaul Pirates,” *Computerworld*, October 17, 1988.

⁵⁸ Kimberley Ellwanger, interview, August 12, 2002.

district itself, but was co-located with a Microsoft sales unit in suburban Chevy Chase, Maryland, a very long drive, by lobbyists' standards, from Pennsylvania Avenue.⁵⁹

While Microsoft's political capabilities grew incrementally, the external threats to it multiplied. The most important of these was a series of antitrust cases, supported by the firm's competitors and spearheaded by executive branch officials. In May, 1998, the U.S. Department of Justice filed a suit that had the potential to break the company into two or more pieces. The mismatch between threat and capability was palpable to observers, who characterized Microsoft as a "Washington wimp" and its CEO as "virtually invisible."⁶⁰ Although Gates visited Washington on occasion beginning in 1993, he told *Fortune* in June, 1998 that "Until this year, dealing with this [antitrust suit] hasn't taken up a measurable amount of my time."⁶¹

Around the time the 1998 suit was filed, the situation changed completely. Microsoft moved its Washington office downtown and expanded it from two lobbyists to ten. Its contributions to Congressional candidates and to the national political parties rose by an order of magnitude to about \$1 million between the 1996 and 1998 campaigns, and climbed to over \$2.5 million between 1998 and 2000.⁶² Reported annual lobbying expenses rose from roughly \$2 million to over \$6 million. A subtler indicator of the firm's enhanced political reach and savvy was its rise to the top of the list of companies

⁵⁹ Jack Krumholtz, interview, January 25, 2002.

⁶⁰ W. John Moore, "Ganging Up on Microsoft," *National Journal*, February 7, 1998, 301; Juliet Eilperin, "High-Tech Lobbying: Microsoft Steps Up Effort," *Roll Call*, October 27, 1997.

⁶¹ Brent Schlender, "An Interview with Gates," *Fortune*, June 8, 1998, 152.

⁶² A brief filed by a trade association antagonistic to Microsoft found that the growth in the firm's campaign contributions was the most rapid in the history of corporation contributions. Edward Roeder, "Declaration," *U.S. v. Microsoft*, civil action 98-1232, U.S. District Court for the District of Columbia.

financing trips for Congressional aides in 1999. As one traveler to Redmond put it, “They are engaged in the traditional lobbying process now...that they didn’t seem to be engaged in in the past.”⁶³

Although Microsoft continued to cooperate with its competitors and other firms to seek collective goods, these efforts were overshadowed by the intra-industry political arms race. Microsoft’s antagonists, led by Netscape, Sun, and Oracle, hired high-profile conservative figures not previously associated with the high-tech industry, like Supreme Court nominee Robert Bork and former Senate minority leader Robert Dole. “Allowing Microsoft to be badly outflanked on the right side of the political spectrum,” wrote the *Wall Street Journal*’s David Bank, “was arguably Gates’s biggest tactical mistake.”⁶⁴

Some of the ways that Microsoft flexed its muscles proved to be counterproductive. Its effort to cut the Justice Department’s appropriation, for instance, reaped criticism even from its allies. “That might have been the dumbest political move of the year,” said a senior [Congressional] leadership aide in late 1999.⁶⁵

By the following year, however, the tenor of the discussion had begun to shift. “We readily admit that we came to D.C. late,” said a Microsoft spokesman in March, 2000, evincing a newfound humility.⁶⁶ Gates, in particular, softened the edges of his public persona and took more care in how he presented himself and his company’s positions to

⁶³ Amy Keller, “Microsoft Takes D.C. to Washington,” *Roll Call*, November 15, 1999.

⁶⁴ David Bank, *Breaking Windows: How Bill Gates Fumbled the Future of Microsoft* (New York: Free Press, 2001), 137. Some details of Microsoft’s opposition’s campaign are described in John Heilemann, “The Truth, the Whole Truth, and Nothing But the Truth: The Untold Story of the Microsoft Case,” *Wired*, November, 2000, 260-311; and Wendy Goldman Rohm, *The Microsoft File: The Secret Case Against Bill Gates* (New York: Times Books, 1998).

⁶⁵ Jim Vandehei, “Microsoft Plans to Boost Lobbying Presence on Hill,” *Roll Call*, November 11, 1999.

public officials and the media. In April, 2000, for instance, the *New York Times* reported that he was "treated...as a national treasure" in meetings with the leadership of both parties in both houses of Congress and the President.⁶⁷ Microsoft's massive investment and subsequent learning paid its richest dividend in November, 2001 with a tentative settlement on relatively lenient terms with the Department of Justice of the George W. Bush Administration.

Microsoft's political development bears important similarities to IBM's. Both firms were represented in Washington early in their history, but neither recognized a potentially devastating Schattschneiderian threat in time to head it off. Once the threat finally breached the attention threshold of senior management, the firms responded massively, perhaps even overcompensating. The irony in this parallel stems from the fact that Gates saw IBM as a negative model and was determined not to repeat the mistake, as he perceived it, of becoming distracted from the business by external threats.⁶⁸ Although he has now stepped aside as CEO, Gates's imprint is likely to remain on Microsoft, just as Watson's did on IBM. Nonetheless, it seems likely that, having adapted to the norms of Washington and moved far toward putting its antitrust problems behind it, Microsoft will begin to play the "statesman" role that IBM played in its heyday and Intel still plays.

AOL

⁶⁶ Judy Sarasohn, "Microsoft's Image Operators," *Washington Post*, March 23, 2000, A27.

⁶⁷ Marc Lacey and Eric Schmitt, "Gates Keeps Washington Dates," *New York Times*, April 6, 2000, D1.

⁶⁸ John Heilemann, "The Truth, the Whole Truth, and Nothing But the Truth: The Untold Story of the Microsoft Case," *Wired*, November, 2000, 260-311, esp. 273-274.

America Online took its current name⁶⁹ in 1991 after six years of existence as Quantum Computer Services. Even after its initial public offering of stock in 1992, AOL remained a distant third in the online service industry⁷⁰ to Prodigy and CompuServe, both of which were subsidiaries of much larger firms. AOL gained momentum rapidly, though, signing up its one millionth subscriber in August, 1994. Although it was beginning to leave its old rivals behind, the “underdog mentality”⁷¹ that suffused AOL in its early years did not disappear, and for good reason: Microsoft wanted its business. Bill Gates famously promised to buy or “bury” AOL. Gates’ threat prompted what *Wall Street Journal* reporter Kara Swisher called an “aggressive public policy campaign” by AOL to convince antitrust investigators that Microsoft’s prospective bundling of its Microsoft Network (MSN) internet service with the Windows operating system was worthy of their attention.⁷²

AOL’s campaign against MSN was mounted largely behind the scenes. The company’s battle against the Communications Decency Act (CDA), which sought to make Internet service providers (ISPs) liable for offensive content flowing through their networks, on the other hand, was highly public. The CDA, which was first proposed in 1994, crystallized complaints about the ease with which pornography could be accessed over the Internet. It placed AOL in jeopardy, since the company derived a substantial portion

⁶⁹ In 2000, AOL merged with Time Warner to form AOL Time Warner, of which the old AOL is now a subsidiary. This paper deals with AOL before the merger and therefore will use that name.

⁷⁰ Online service allowed computer users to communicate with one another and to gain access to content arranged by the service provider. These proprietary networks were opened up to the Internet in the mid-1990s after the commercialization of the Internet and invention of the browser, at which time the term “Internet service provider” (ISP) came into use.

⁷¹ David Phillips, interview, May 17, 2002.

⁷² Kara Swisher, *AOL.com* (New York: Random House, 1998), xv, 121-124.

of its revenue from “chat rooms” in which sex was frequently discussed.⁷³ AOL’s first government affairs manager, who was hired in early 1995 primarily to deal with the issue, viewed it as a “stress test,” not only of the firm, but of the Internet as a communications medium.⁷⁴

The CDA passed Congress as part of the Telecommunications Act of 1996, but it was held to be in violation of the first amendment of the U.S. Constitution by the Supreme Court in June, 1997. AOL’s closest allies in opposing the measure were public interest groups, like People for the American Way (whose lobbyist on the issue AOL ultimately brought onto its own staff), rather than other ISPs. While AOL’s “purity”⁷⁵ on first amendment questions in this period genuinely reflected CEO Steve Case’s “vision” for the new medium,⁷⁶ which he shared with these allies, it also made good business sense. Case’s firm gained more than its rivals from the ultimate victory, because Internet service was AOL’s only business and because it held such a large share of the market. (MSN fizzled at its inception.)

Although AOL made no campaign contributions to Congressional candidates or the national political parties until the 1999-2000 election cycle, its political capabilities were well-established by the time the CDA was overruled. Case personally hired a senior executive, George Vradenburg, to manage public policy for the firm in March, 1997. Vradenburg had previously served as executive vice-president at Fox and senior vice-

⁷³ Swisher, *op. cit.*, 226.

⁷⁴ Bill Burrington, interview, January 8, 2002.

⁷⁵ Jill Lesser, interview, December 4, 2001.

⁷⁶ Burrington, interview, January 8, 2002, *op. cit.*

president at CBS; he was, in short, a “heavyweight” (in the words of the head of AOL’s Washington office, who now reported to him).⁷⁷ AOL’s policy agenda mushroomed in 1997 along with Washington’s interest in the Internet. Copyright, privacy, taxation, and a raft of other issues followed on the heels of the CDA. AOL’s dominant position in the new medium ensured that its views would be sought on these matters. But its leadership was not simply reacting to events. AOL was particularly attuned to public policy because its headquarters was in northern Virginia. “Our hometown paper,” one AOL government affairs representative quipped, “is The Washington Post.”⁷⁸

⁷⁷ Burrington, interview, January 8, 2002, *op. cit.*

⁷⁸ Jill Lesser, interview, August 8, 2002.

Vradenburg's influence was felt immediately. Rather than "making it up as we went along,"⁷⁹ AOL's government affairs unit became more careful and more strategic in its choice of issues, positions, and tactics. AOL took the lead in trying to organize collective action on behalf of the new industry, separating out issues unique to the firm from those for which costs might be shared. AOL's efforts to create an entity that could "speak for the Internet," however, never bore fruit. Even though AOL spent "serious money" and some of Case's time on the effort, key potential member firms proved unable to agree on a set of policy priorities and positions. The chaotic nature of the medium and confusion over its commercial potential contributed to the stalemate, but mistrust of the dominant firm in the industry seems to have played an important role as well.⁸⁰

AOL's political development through January, 2000, when it purchased Time Warner (thereby transforming its corporate identity and structure),⁸¹ shares some features with the other cases. Like Intel, AOL's political mobilization occurred before the firm had clearly established its dominance, in the face of perceived threats to its existence. One of these threats, interestingly, lay in Microsoft's competing product, and it was AOL that sought to expand the scope of conflict by attracting government interest in Microsoft's behavior. Soon thereafter, though, AOL began to operate as Mancur Olson might have expected it to. It climbed the political learning curve more quickly than IBM and Microsoft, in part because of the unique furor surrounding the Internet, but also because of its headquarters

⁷⁹ Lesser, interview, December 4, 2001, *op. cit.*

⁸⁰ Jeff Richards, interview, December 21, 2001; George Vradenburg, interview, December 11, 2001; Bill Burrington, interview, January 28, 2002.

location and the views of its CEO. AOL bore a disproportionate burden in seeking collective goods on behalf of the industry and the medium as well as representing itself on issues of unique interest. Intra-industry conflict, though, remains a theme in this case, as in the others; tension between dominant firms and their rivals, particularly under conditions of high uncertainty, impeded the building of a united industry front in Washington.

Cisco

Cisco Systems was founded in 1984, a year before AOL. It produces switching equipment for the Internet, such as routers. Cisco pioneered this technology and grew explosively as the Internet expanded. Its revenues multiplied more than a hundred-fold between 1990 (\$70 million) and 1998 (\$8.5 billion). Neither traditional telecommunications equipment vendors nor more recent start-ups have been able to dent Cisco's 60-80% market share in its core product lines. By virtually every measure, the company plunged into national politics in the short space of a year, beginning in July, 1997. Cisco CEO John Chambers was one of the founders of TechNet, a Silicon Valley interest organization formed that month; the firm hired Greg Simon, a former senior staff member to Vice-President Al Gore, as a consultant in the capital a couple of months later; its employees testified before Congressional committees for the first time that fall as well; and Cisco opened a Washington office the following spring, in May, 1998.

⁸¹ On the initial impact of the merger on the two companies' government affairs units, see Susan Crabtree, "Culture Clash Affects Merger," *Roll Call*, March 9, 2000.

Although the firm itself makes no campaign contributions,⁸² Chambers first became a major donor during the 1997-1998 election cycle.

Cisco's interest in public policy was triggered by President Clinton's veto of securities litigation reform legislation in late 1995.⁸³ Early the following year, Cisco joined other Silicon Valley firms in rallying against Proposition 211, a California state ballot initiative that would have made it easier for firms with volatile stock prices to be sued. Such suits represented little more than a nuisance to Cisco itself, but they made life difficult for the high-tech start-ups that the company acquired at a prodigious rate to help fuel its growth. Chambers later said that the episode shattered his naivete. "Not only did we realize with Proposition 211 that government could hurt you, but I have changed my philosophy dramatically since then. Business and government should work closely together."⁸⁴ Prop 211 was defeated handily by a coalition that moved onto the national scene the following year as TechNet.⁸⁵

Even though the immediate threat that prompted it was mild, local, and quickly eliminated, Chambers' change of heart precipitated a systematic and rapid entry into Washington on the part of his company. The trial lawyers who had fought Silicon Valley over Prop 211 were a permanent presence in national as well as state politics, and Cisco's leadership felt a need to match them. More generally, Cisco viewed participating in the

⁸² Cisco recently announced (2002) that it is establishing a PAC.

⁸³ Daniel Scheinman, interview, May 13, 2002.

⁸⁴ Neil Munro, "Cisco Puts Money, Effort in Lobbying, Working with DC Trade Groups," *National Journal*, October 3, 1998, 2325.

⁸⁵ Chris Watts, "Proposition 211," Stanford University, Graduate School of Business case S-P-23, October, 1997; Sara Miles, *How To Hack a Party Line: The Democrats and Silicon Valley* (New York: Farrar, Straus, & Giroux, 2001).

policy process as an aspect of becoming “institutional” (as then-general counsel Dan Scheinman put it), being perceived as a fixture not a “flyby,” in spite of the firm’s relative youth. Before setting up the government affairs function, Scheinman conducted what he called a “stupid tour,” meeting with other companies and industry associations to divine best practices and dispel what he perceived to be his own stupidity.⁸⁶ The firm explicitly used Microsoft as a negative model for some aspects of its relationship with Washington, notably dealing with antitrust enforcement authorities.⁸⁷

By the end of 1998, Cisco had built its political relationships sufficiently well that Chambers, despite being “openly Republican,” was invited to keynote what the *National Journal* termed a “White House group hug with the information-technology industry.”⁸⁸ Since then, Cisco has focused its attention on shaping policies that will “drive more bits over the network.”⁸⁹ Some of those bits may flow over Cisco products introduced into the regulated telephone and cable television networks. More will probably flow through the as-yet unregulated Internet as it replaces the older networks in providing such services as voice communication and video-on-demand. Cisco’s dominance of the Internet equipment industry means that the company grows along with the Internet; the more bits, the better. Having achieved this position in an unregulated market, the firm advocates deregulation of the older networks as they converge with the Internet. It was a major supplier to the competitors to the Baby Bells that sprang up in the wake of the Telecommunications Act of 1996, many of which have now gone under.

⁸⁶ Scheinman, interview, *op. cit.*; David Segal, “FTC Cancels Probe of Cisco’s Talks With Rivals,” *Washington Post*, June 2, 1999, E2.

⁸⁷ Thurm Scott, “Safe Conduct: Microsoft’s Behavior Is Helping Cisco Avoid Antitrust Trouble” *Wall Street Journal*, June 1, 2000, A1.

Cisco's government affairs managers are insistent that their operation run "lean." The company's reported lobbying expenditures in 1999-2000 were less than 1/5 of those of AOL and Intel, 1/20 of Microsoft's and IBM's.⁹⁰ On the other hand, Cisco's "senior executive buy-in"⁹¹ (to use the phrase of its Washington office director) stands out in this comparison. Chambers' "passion for politics and policy"⁹² sets the standard among high-tech CEOs, according to a Democratic Senate aide quoted in the summer of 1999.⁹³ Chambers and his wife Constance contributed nearly \$600,000 to candidates for Federal offices and the national political parties during the 1999-2000 election cycle.⁹⁴ A fundraiser at the Chambers's home in Los Altos Hills, California, in June, 2000, brought in an estimated \$4 million for Republican presidential nominee George W. Bush.⁹⁵ Chambers' warm relationship with the President and his affinity with Bush's policies earned him a featured role at the President's August, 2002, economic "summit" in Waco, Texas.

The Cisco case is unique in that the firm entered politics before it faced a threat to its existence. The close-knit geographical and professional network of Silicon Valley heightened its leaders' attention to what they viewed as legal harassment. TechNet, like SIA before it, was easy to organize in this social milieu. Cisco's executives then sought

⁸⁸ "Inside Washington," *National Journal*, December 19, 1998, 2967.

⁸⁹ Scheinman, interview, *op. cit.*; Laura Ipsen, interview, June 20, 2002.

⁹⁰ The five firms' total revenues for 2000 were approximately \$8 billion for AOL; \$19 billion for Cisco; \$34 billion for Intel; \$88 billion for IBM; and \$23 billion for Microsoft.

⁹¹ Michael Timmeny, interview, July 12, 2002.

⁹² Laura Ipsen, interview, June 20, 2002.

⁹³ Neil Munro, "Building a Case," *National Journal*, July 31, 1999, 2218.

⁹⁴ This figure placed the Chambers's 31st among all individual donors in that cycle, according to figures compiled by the Center for Responsive Politics. 82% of these contributions went to Republicans.

⁹⁵ Mary Ann Ostrom, "Gore Maintains Lead with California Voters," *San Jose Mercury-News*, June 20, 2000.

to learn from the political experiences of their rivals and peers, including some of the other companies considered here. Yet, in one important respect, Cisco may well wind up recapitulating the painful learning experiences of IBM and Microsoft at comparable points in their political development. Cisco to date has taken a personalistic approach to government affairs, relying heavily on its CEO and other senior executives, rather than staff. Indeed, its adamantness that it will not build a big staff echoes the earlier cases. In the wake of the bursting of the technology stock bubble and the ensuing corporate scandals, however, Cisco appears vulnerable to a Schattschneiderian expansion of the scope of conflict by its critics and competitors on such hot-button issues as accounting for mergers and stock options.⁹⁶

Conclusions

This scenario for Cisco may prove fanciful; I would not claim that these case studies yield a theory with predictive power, particularly in a single case. What they show is that the logic of collective action is only one element in the explanation of the political behavior of dominant firms, and not necessarily the most important one. The Olsonian hypothesis should be complemented with other hypotheses, particularly those drawing on organizational and institutional theory. Some of these alternatives are testable through quantitative research; others require qualitative methods.

Multiple measures for representation. My first conclusion is methodological.

Representation is a complex phenomenon that ought to be assessed with information that

⁹⁶ Paul Krugman, "Clueless in Crawford," *New York Times*, August 13, 2002, A19. Cisco's response appeared in the *Times* on August 20, 2002, A18.

goes well beyond campaign contributions. Forms of representation change over time, as the institutional and strategic environment evolves. What Tom Watson, Jr. could achieve in Washington in the early 1960s for IBM with a single discreet phone call would likely take a squadron of lobbyists, lawyers, and analysts today. Moreover, at any one time, firms make very different judgments about the value created by various modes of representation. Cisco sees itself to be better represented with its combination of a small lobbying office and energetic CEO involvement than Microsoft is with the opposite combination. IBM's management believes that its lobbyists are more effective if the firm refuses to make campaign contributions. Some quantitative researchers have already taken this lesson to heart, creating indices that employ multiple measures of representation, but it merits reinforcement.⁹⁷

Schattschneider often trumps Olson. Even if such improvements are made in the measurement of representation, the “disappointing” results of quantitative tests of the Olsonian hypothesis may not disappear. One important reason suggested by the case studies is that political activity in highly concentrated industries is often initiated by subordinate firms against dominant firms. The competitors of IBM in the 1960s and Microsoft in the 1990s took their complaints to Washington first; the market leaders were political followers. The competitors sought to expand the scope of conflict from the market to the polity, as Schattschneider envisions; the leaders did not seek collective goods, but rather to preserve their leading market positions. Concentration matters in these cases, but not in the way that Olson predicts it should. Quantitative researchers

⁹⁷ Hansen and Mitchell, *op. cit.*; Schuler, *op. cit.*; Stephen Ansolabehere, James M. Snyder, and Micky Tripathi, “Are PAC Contributions and Lobbying Linked? New Evidence from the 1995 Lobbying

might be able to disentangle the two interpretations by adding a variable that measures intra-industry conflict, such as the number of industry associations.

Organizational and institutional variables: leadership attention. To understand why dominant firms more often follow their competitors in entering the Washington interest organization universe than lead them, one must go beyond the rational actor model of the firm.⁹⁸ The decision to enter politics requires approval from senior managers, including the CEO, people whose attention to non-market issues is usually very limited. The case studies point to variations in the threshold that non-market threats and opportunities must breach before senior executives pay attention to them. Some portion of that variation may simply be accounted for by differences in managerial “taste” for politics. John Chambers’ passion contrasts sharply with Bill Gates’ disdain. Although such differences could reasonably be considered noise in a large n study, it might be worthwhile experimenting with variables that measure some personal characteristic of the CEO, perhaps something as simple as whether he or she is the founder of the firm on the premise that CEOs hired externally are more likely to have been exposed to significant non-market issues in previous positions.

Organizational and institutional variables: threat perception. While variations in “taste” might be equally relevant to managerial responses to threats or opportunities, this set of cases suggest that threats are more likely to attract attention than opportunities. Threat perception, in turn, may depend on the reference groups to whom senior managers

Disclosure Act,” *Business and Politics* 4:131-156 (2002).

paid attention and the lessons they drew from them.⁹⁹ Gates viewed IBM's reaction to its antitrust case, which included a large investment in political capabilities, as helping to render it vulnerable to later competitors, including his own firm. He sought to avoid making the same mistake by keeping Microsoft relatively aloof from Washington. Chambers may have taken Microsoft's trouble with the antitrust authorities as a signal that his firm should avoid *that* mistake and be certain to build strong relationships with public officials. Steve Case seems to have switched his reference group from the high-technology industry to the media industry while AOL headed off liability for content flowing through its network. The new reference group was a regulated industry with a long tradition of activism in Washington, and the switch may have contributed to the hiring of a high-level manager for public policy from outside the firm. Such differences in threat perception do not seem easily amenable to quantitative research.

Organizational and institutional variables: information flows. Attention and perception at the top of an organization should not be conceived of as purely individual phenomena, of course. The information that flows to the holders of senior positions is significantly influenced by structural factors. In the case studies, the establishment of a government affairs staff at headquarters and a Washington office tended to make executive decision-makers more sensitive to political threats and much more aware of political opportunities. Formal reporting channels for these entities and decision-making processes may also shape political representation, especially within dominant firms. The engagement of a

⁹⁸ Cyert and March, *op. cit.*; Raymond Bauer, Ithiel de Sola Pool, and Lewis Anthony Dexter, *American Business, Public Policy, and the Politics of Foreign Trade*, second ed. (Chicago: Aldine-Atherton, 1972).

⁹⁹ Paul Slovic, Baruch Fischhoff, and Sarah Lichtenstein, "Rating the Risks," *Environment* 21(3):14-20, 36-39 (1979).

senior technical executive like Intel's Noyce in government affairs virtually ensures that policy-related information will make it through the filters that surround such a firm's leadership team. Policy-relevant information may also be received by senior executives through networks that transcend the firm's boundaries. AOL's location in Washington, D.C., to take a variable that would be easy to incorporate into quantitative analyses, seems to have given its executives different kinds of contacts than those developed by Microsoft's in Washington state. Cathie Martin has shown how these kinds of variables might be incorporated into quantitative research.¹⁰⁰

Don't throw out the baby. None of the foregoing should be taken to mean that we should discard the Olsonian hypothesis. The case studies provide some evidence in support of it. When IBM was at the peak of its power, for instance, some of its competitors let it do the talking for them in Washington. Similarly, after AOL achieved a dominant position in the ISP market, it defined its main policy objective to be building confidence in the Internet as a medium and made significant investments to try to secure that elusive collective good. Intel, too, once it had secured its commanding position in the market, sought collective goods, such as large-scale deployment of broadband service, that would benefit many other firms as well as itself. Moreover, the Olsonian framework, conceived of more broadly, helps to make sense of other elements of some of these cases that do not conform to the narrow hypothesis. Intel's entry into politics when it was far from dominant, for instance, was eased by the low transaction costs that faced the Silicon Valley community in organizing collectively; the same was true for Cisco a couple of decades later. My argument is intended to foster theoretical and methodological

¹⁰⁰ Martin, *op. cit.*

pluralism in the study of business and politics, not to substitute one monopoly for another.

Path dependence. The case studies suggest that early choices may leave a long-lasting imprint on a firm's political development. IBM and Intel, for instance, have not participated fully in the campaign finance system. IBM's entry into politics coincided with the Watergate backlash of the mid-1970s, and the company sought to establish beyond a doubt that it was clean. This commitment, which was strongly endorsed by CEO Watson, Jr., put IBM on a path that emphasized in-house expertise deployed through lobbyists as the firm's key political asset. Had it entered in the 1990s, as Microsoft, AOL, and Cisco did, it seems likely that IBM's path would have been different. Intel's entry came in between these two generations, and it fits in between in terms of campaign contributions, too, maintaining a PAC, but not contributing soft money to the national parties. Each firm's organizational culture and the perceptions of it in the Washington environment help to reduce the chances it will switch paths in this aspect of its behavior.

The question of path dependence leads to two final questions that might be asked about the politics of dominant firms: does their investment in political capabilities contribute to the maintenance of their market position? For those firms that entered politics before they achieved dominance, the question is even more pointed: did they achieve that position in part because of this investment? AOL and Intel fall into the latter category, and the evidence in these cases suggests that the answer to the second question is

negative. However, their relatively early entrance into politics may be correlated with subsequent success in a non-trivial way; political and market success may be products of strategically broad-minded management teams.

My hunch is that the answer to the first question is “yes,” and that provisional answer brings me back once again to Olson. Dominant firms are natural targets for non-market threats, whether from competitors or from societal forces. Political capabilities help these firms to blunt or even avoid such threats. Although dominant firms may not be first movers in the way that Olson thought they should be, they seem often to be fast second movers. Even if they overcompensate for a late start, the expense of building political capabilities is modest enough that paying extra is of little concern in the long run (as long as the firm’s interlocutors in Washington perceive it as a credible actor). Although the IBM case shows that such capabilities are not sufficient to maintain dominance indefinitely, they may well be necessary, as Microsoft seems to have found out. Watching Cisco over the next few years may provide a test of this theory.