AN FTC GUIDE TO
THE ANTITRUST LAWS

THE THREE CORE FEDERAL ANTITRUST LAWS

CONGRESS PASSED THE FIRST ANTITRUST LAW, the Sherman Act, in 1890 as a "comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade." In 1914, Congress passed two additional antitrust laws: the Federal Trade Commission Act, which created the FTC, and the Clayton Act. With some revisions, these are the three core federal antitrust laws still in effect today.

The antitrust laws proscribe unlawful mergers and business practices in general terms, leaving courts to decide which ones are illegal based on the facts of each case. Courts have applied the antitrust laws to changing markets, from a time of horse and buggies to the present digital age. Yet for over 100 years, the antitrust laws have had the same basic objective: to protect the process of competition for the benefit of consumers, making sure there are strong incentives for businesses to operate efficiently, keep prices down, and keep quality up.

OVERVIEW OF THE THREE CORE FEDERAL ANTITRUST LAWS

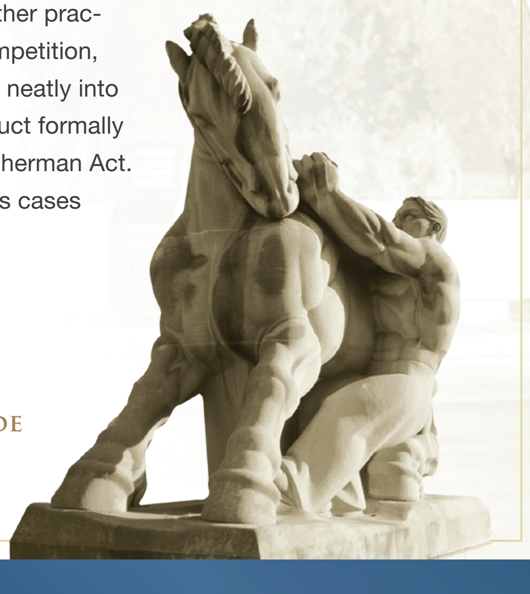
The Sherman Act

The Sherman Act outlaws "every contract, combination, or conspiracy in restraint of trade," and any "monopolization, attempted monopolization, or conspiracy or combination to monopolize." Long ago, the Supreme Court decided that the Sherman Act does not prohibit every restraint of trade, only those that are unreasonable. For instance, in some sense, an agreement between two individuals to form a partnership restrains trade, but may not do so unreasonably, and thus may be lawful under the antitrust laws. On the other hand, certain acts are considered so harmful to competition that they are almost always illegal. These include plain arrangements among competing individuals or businesses to fix prices, divide markets, or rig bids. These acts are "per se" violations of the Sherman Act; in other words, no defense or justification is allowed.

The penalties for violating the Sherman Act can be severe. Although most enforcement actions are civil, the Sherman Act is also a criminal law, and individuals and businesses that violate it may be prosecuted by the Department of Justice. Criminal prosecutions are typically limited to intentional and clear violations such as when competitors fix prices or rig bids. The Sherman Act imposes criminal penalties of up to $100 million for a corporation and $1 million for an individual, along with up to 10 years in prison. Under federal law, the maximum fine may be increased to twice the amount the conspirators gained from the illegal acts or twice the money lost by the victims of the crime, if either of those amounts is over $100 million.

The Federal Trade Commission Act

The Federal Trade Commission Act bans "unfair methods of competition" and "unfair or deceptive acts or practices." The Supreme Court has said that all violations of the Sherman Act also violate the FTC Act. Thus, although the FTC does not technically enforce the Sherman Act, it can bring cases under the FTC Act against the same kinds of activities that violate the Sherman Act. The FTC Act also reaches other practices that harm competition, but that may not fit neatly into categories of conduct formally prohibited by the Sherman Act. Only the FTC brings cases under the FTC Act.



THE ANTITRUST LAWS PROSCRIBE UNLAWFUL MERGERS AND BUSINESS PRACTICES IN GENERAL TERMS, LEAVING COURTS TO DECIDE WHICH ONES ARE ILLEGAL BASED ON THE FACTS OF EACH CASE.

The Clayton Act

The Clayton Act addresses specific practices that the Sherman Act does not clearly prohibit, such as mergers and interlocking directorates (that is, the same person making business decisions for competing companies). Section 7 of the Clayton Act prohibits mergers and acquisitions where the effect "may be substantially to lessen competition, or to tend to create a monopoly." As amended by the Robinson-Patman Act of 1936, the Clayton Act also bans certain discriminatory prices, services, and allowances in dealings between merchants. The Clayton Act was amended again in 1976 by the Hart-Scott-Rodino Antitrust Improvements Act to require companies planning large mergers or acquisitions to notify the government of their plans in advance. The Clayton Act also authorizes private parties to sue for triple damages when they have been harmed by conduct that violates either the Sherman or Clayton Act and to obtain a court order prohibiting the anticompetitive practice in the future.

In addition to these federal statutes, most states have antitrust laws that are enforced by state attorneys general or private plaintiffs. Many of these statutes are based on the federal antitrust laws.

AN FTC GUIDE TO

The Enforcers

The Federal Government, States, and Private Parties

The Federal Government

Both the FTC and the U.S. Department of Justice (DOJ) Antitrust Division enforce the federal antitrust laws. In some respects their authorities overlap, but in practice the two agencies complement each other. Over the years, the agencies have developed expertise in particular industries or markets. For example, the FTC devotes most of its resources to certain segments of the economy, including those where consumer spending is high: health care, pharmaceuticals, professional services, food, energy, and certain high-tech industries like computer technology and Internet services. Before opening an investigation, the agencies consult with one another to avoid duplicating efforts. In this Guide, “the agency” means either the FTC or DOJ, whichever is conducting the antitrust investigation.

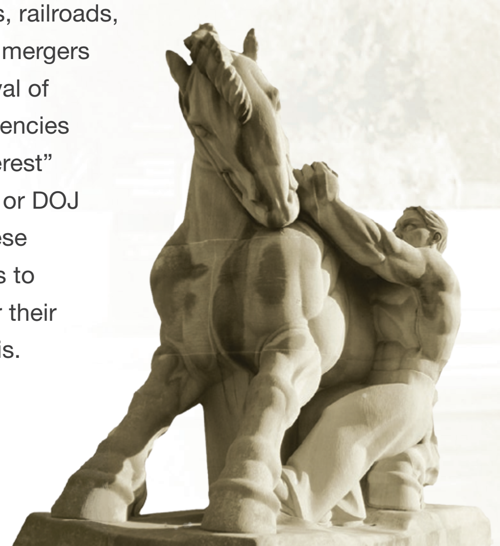
Premerger notification filings, correspondence from consumers or businesses, Congressional inquiries, or articles on consumer or economic subjects may trigger an FTC investigation. Generally, FTC investigations are non-public to protect both the investigation and the individuals and companies involved. If the FTC believes that a person or company has violated the law or that a proposed merger may violate the law, the agency may attempt to obtain voluntary compliance by entering into a consent order with the company. A company that signs a consent order need not admit that it violated the law, but it must agree to stop the disputed practices outlined in an accompanying complaint or take certain steps to resolve the anticompetitive aspects of its proposed merger.

If a consent agreement cannot be reached, the FTC may issue an administrative complaint and/or seek injunctive relief in the federal courts. The FTC’s administrative complaints initiate a formal proceeding that is much like a federal court trial but before an administrative law judge: evidence is submitted, testimony is heard, and witnesses are examined and cross-examined. If a law violation is found, a cease and desist order may be issued. An initial decision by an administrative law judge may be appealed to the Commission.

Final decisions issued by the Commission may be appealed to a U.S. Court of Appeals and, ultimately, to the U.S. Supreme Court. If the Commission’s position is upheld, the FTC, in certain circumstances, may then seek consumer redress in court. If the company violates an FTC order, the Commission also may seek civil penalties or an injunction.

In some circumstances, the FTC can go directly to federal court to obtain an injunction, civil penalties, or consumer redress. For effective merger enforcement, the FTC may seek a preliminary injunction to block a proposed merger pending a full examination of the proposed transaction in an administrative proceeding. The injunction preserves the market’s competitive status quo.

The FTC also may refer evidence of criminal antitrust violations to the DOJ. Only the DOJ can obtain criminal sanctions. The DOJ also has sole antitrust jurisdiction in certain industries, such as telecommunications, banks, railroads, and airlines. Some mergers also require approval of other regulatory agencies using a “public interest” standard. The FTC or DOJ often work with these regulatory agencies to provide support for their competitive analysis.



THE FTC DEVOTES MOST OF ITS RESOURCES TO SEGMENTS OF THE ECONOMY WHERE CONSUMER SPENDING IS HIGH.

States

State attorneys general can play an important role in antitrust enforcement on matters of particular concern to local businesses or consumers. They may bring federal antitrust suits on behalf of individuals residing within their states ("parens patriae" suits), or on behalf of the state as a purchaser. The state attorney general also may bring an action to enforce the state's own antitrust laws. In merger investigations, a state attorney general may cooperate with federal authorities. For more information on joint federal-state investigations, consult the *Protocol for Coordination in Merger Investigations.*

Private Parties

Private parties can also bring suits to enforce the antitrust laws. In fact, most antitrust suits are brought by businesses and individuals seeking damages for violations of the Sherman or Clayton Act. Private parties can also seek court orders preventing anticompetitive conduct (injunctive relief) or bring suits under state antitrust laws. Individuals and businesses cannot sue under the FTC Act.

Issues of International Jurisdiction

U.S. and foreign competition authorities may cooperate in investigating cross-border conduct that has an impact on U.S. consumers. For more information on the application of U.S. antitrust laws to businesses with international operations, consult the 1995 *Antitrust Enforcement Guidelines for International Operations*. In addition, as more U.S. companies and consumers do business overseas, federal antitrust work often involves cooperating with international authorities around the world to promote sound competition policy approaches. There are now more than 100 foreign competition agencies. For more information on the agency's work with these authorities, visit the Office of International Affairs web pages.

An FTC Guide to
Dealings with Competitors

Introduction

IN ORDER TO COMPETE IN MODERN MARKETS, competitors sometimes need to collaborate. Competitive forces are driving firms toward complex collaborations to achieve goals such as expanding into foreign markets, funding expensive innovation efforts, and lowering production and other costs.

In today's marketplace, competitors interact in many ways, through trade associations, professional groups, joint ventures, standard-setting organizations, and other industry groups. Such dealings often are not only competitively benign but procompetitive. But there are antitrust risks when competitors interact to such a degree that they are no longer acting independently, or when collaborating gives competitors the ability to wield market power together.

For the most blatant agreements not to compete, such as price fixing, big rigging, and market division, the rules are clear. The courts decided many years ago that these practices are so inherently harmful to consumers that they are always illegal, so-called per se violations. For other dealings among competitors, the rules are not as clear-cut and often require fact-intensive inquiry into the purpose and effect of the collaboration, including any business justifications. Enforcers must ask: what is the purpose and effect of dealings among competitors? Do they restrict competition or promote efficiency?

These Fact Sheets provide more detail about the types of dealings with competitors that may result in an antitrust investigation. For further guidance, read Antitrust Guidelines for Collaborations Among Competitors.

Fact Sheets for Dealings with Competitors

- **Price Fixing:** an agreement among competitors that raises, lowers, or stabilizes prices or competitive terms
- **Bid Rigging:** competitors agree in advance which firm will win the bid
- **Market Division or Customer Allocation:** an agreement among competitors to assign sales territories or customers
- **Group Boycotts:** an agreement among competitors not to do business with targeted individuals or businesses
- **Other Agreements Among Competitors**
- **Spotlight on Trade Associations**

DEALINGS WITH COMPETITORS THAT ALWAYS RAISE CONCERNS INCLUDE PLAIN PRICE FIXING, BID RIGGING, AND CUSTOMER OR MARKET ALLOCATION. THESE AGREEMENTS ARE ALMOST ALWAYS ILLEGAL, AND MAY BE PROSECUTED AS CRIMINAL VIOLATIONS.

AN FTC GUIDE TO

Dealings with Competitors

Price Fixing

PRICE FIXING IS AN AGREEMENT (written, verbal, or inferred from conduct) among competitors that raises, lowers, or stabilizes price or competitive terms. Generally, the antitrust laws require that each company establish prices and other terms on its own, without agreeing with a competitor. When consumers make choices about what products and services to buy, they expect that the price has been determined freely on the basis of supply and demand, not by an agreement among competitors. When competitors agree to restrict competition, the result is often higher prices. Accordingly, price fixing is a major concern of government antitrust enforcement.

A PLAIN AGREEMENT AMONG competitors to fix prices is almost always illegal, whether prices are fixed at a minimum, maximum, or within some range. Illegal price fixing occurs whenever two or more competitors agree to take actions that have the effect of raising, lowering or stabilizing the price of any product or service without any legitimate justification. Price-fixing schemes are often worked out in secret and can be hard to uncover, but an agreement can be discovered from "circumstantial" evidence. For example, if direct competitors have a pattern of unexplained identical contract terms or price behavior together with other factors (such as the lack of legitimate business explanation), unlawful price fixing may be the reason. Invitations to coordinate prices also can raise concerns, as when one competitor announces publicly that it is willing to end a price war if its rival is willing to do the same, and the terms are so specific that competitors may view this as an offer to set prices jointly.

Not all price similarities, or price changes that occur at the same time, are the result of price fixing. On the contrary, they often result from normal market conditions. For example, prices of commodities such as wheat are often identical because the products are virtually identical, and the prices that farmers charge all rise and fall together without any agreement among them. If a drought causes the supply of wheat to decline, the price to all affected farmers will increase. An increase in consumer demand can also cause uniformly high prices for a product in limited supply.

Price fixing relates not only to prices, but also to other terms that affect prices to consumers, such as shipping fees, warranties, discount programs, or financing rates.

ANTITRUST SCRUTINY may occur when competitors discuss the following topics:

- Present or future prices
- Terms or conditions of sale, including credit terms
- Pricing policies
- Discounts
- Promotions
- Identity of customers
- Bids
- Allocation of customers or sales areas
- Costs
- Production quotas
- Capacity
- R&D plans

A PLAIN AGREEMENT AMONG COMPETITORS TO FIX PRICES IS ALMOST ALWAYS ILLEGAL, WHETHER PRICES ARE FIXED AT A MINIMUM, MAXIMUM, OR WITHIN SOME RANGE.

A defendant is allowed to argue that there was no agreement, but if the government or a private party proves a plain price-fixing agreement, there is no defense to it. Defendants may not justify their behavior by arguing that the prices were reasonable to consumers, were necessary to avoid cut-throat competition, or stimulated competition.

EXAMPLE: A group of competing optometrists agreed not to participate in a vision care network unless the network raised reimbursement rates for patients covered by its plan. The optometrists refused to treat patients covered by the network plan, and, eventually, the company raised reimbursement rates. The FTC said that the optometrists' agreement was illegal price fixing, and that its leaders had organized an effort to make sure other optometrists knew about and complied with the agreement.

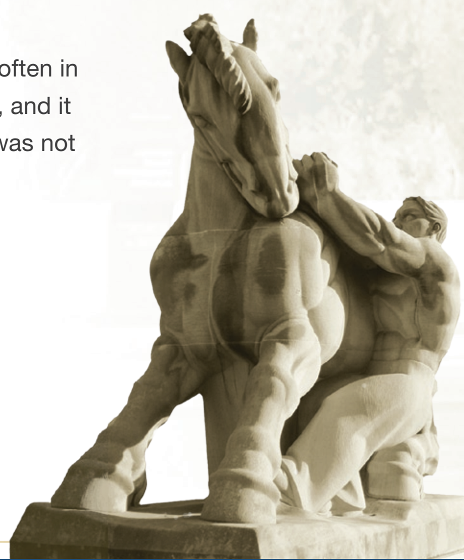
An agreement to restrict production, sales, or output is just as illegal as direct price fixing, because reducing the supply of a product or service drives up its price. For example, the FTC challenged an agreement among competing oil importers to restrict the supply of lubricants by refusing to import or sell those products in Puerto Rico. The competitors were seeking to pressure the legislature to repeal an environmental deposit fee on lubricants, and warned of lubricant shortages and higher prices. The FTC alleged that the conspiracy was an unlawful horizontal agreement to restrict output that was inherently likely to harm competition and that had no countervailing efficiencies that would benefit consumers.

Q: The gasoline stations in my area have increased their prices the same amount and at the same time. Is that price fixing?

A: A uniform, simultaneous price change could be the result of price fixing, but it could also be the result of independent business responses to the same market conditions. For example, if conditions in the international oil market cause an increase in the price of crude oil, this could lead to an increase in the wholesale price of gasoline. Local gasoline stations may respond to higher wholesale gasoline prices by increasing their prices to cover these higher costs. Other market forces, such as publicly posting current prices (as is common with most gasoline stations), encourages suppliers to adjust their own prices quickly in order not to lose sales. If there is evidence that the gasoline station operators talked to each other about increasing prices and agreed on a common pricing plan, however, that may be an antitrust violation.

Q: Our company monitors competitors' ads, and we sometimes offer to match special discounts or sales incentives for consumers. Is this a problem?

A: No. Matching competitors' pricing may be good business, and occurs often in highly competitive markets. Each company is free to set its own prices, and it may charge the same price as its competitors as long as the decision was not based on any agreement or coordination with a competitor.



BID RIGGING

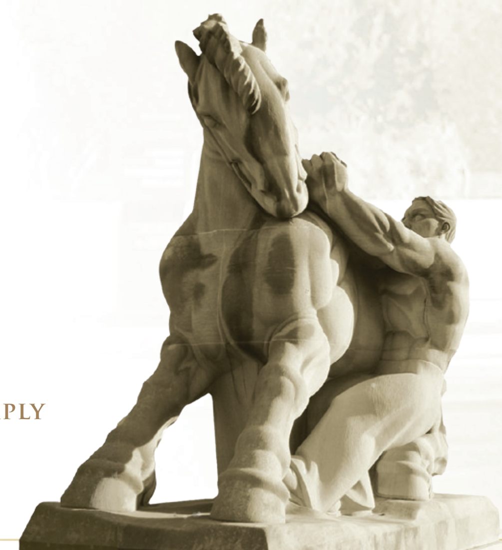
WHENEVER BUSINESS CONTRACTS ARE AWARDED by means of soliciting competitive bids, coordination among bidders undermines the bidding process and can be illegal. Bid rigging can take many forms, but one frequent form is when competitors agree in advance which firm will win the bid. For instance, competitors may agree to take turns being the low bidder, or sit out of a bidding round, or provide unacceptable bids to cover up a bid-rigging scheme. Other bid-rigging agreements involve subcontracting part of the main contract to the losing bidders, or forming a joint venture to submit a single bid.

EXAMPLE: Three school bus companies formed a joint venture to provide transportation services under a single contract with the school district. The joint venture did not involve any beneficial integration of operations that would save money. The FTC found that the joint venture mainly operated to prevent the bus companies from offering competing bids.

ARE YOU A PROCUREMENT OFFICER?

The Department of Justice has developed a tip sheet to help you assess suspicious bidding behavior and determine when to notify the government.

BID RIGGING CAN TAKE MANY FORMS, BUT OFTEN COMPETITORS SIMPLY AGREE IN ADVANCE WHICH FIRM WILL WIN THE BID.



Market Division or Customer Allocation

Plain agreements among competitors to divide sales territories or assign customers are almost always illegal. These arrangements are essentially agreements not to compete: "I won't sell in your market if you don't sell in mine." The FTC uncovered such an agreement when two chemical companies agreed that one would not sell in North America if the other would not sell in Japan. Illegal market sharing may involve allocating a specific percentage of available business to each producer, dividing sales territories on a geographic basis, or assigning certain customers to each seller.

Q: I want to sell my business, and the buyer insists that I sign a non-compete clause? Isn't this illegal?

A: A limited non-compete clause is a common feature of deals in which a business is sold, and courts have generally permitted such agreements when they were ancillary to the main transaction, reasonably necessary to protect the value of the assets being sold, and limited in time and area covered. There are other situations, however, in which non-compete clauses may be anticompetitive. For instance, the FTC stopped the operator of dialysis clinics from buying five clinics and paying its competitor to close three more. The purchase agreement also contained a non-compete clause that prevented the seller from opening a new clinic in the same local area for five years, and required the seller to enforce non-compete clauses in its contracts with the medical directors of the closed facilities. In this situation, the non-compete clause prevented those doctors from serving as medical directors for any new clinic in the area and reduced the chance that a new clinic would open for five years. The FTC said the agreement to close the clinics, reinforced by the agreement not to compete for five years, was an illegal agreement to eliminate competition between rivals.

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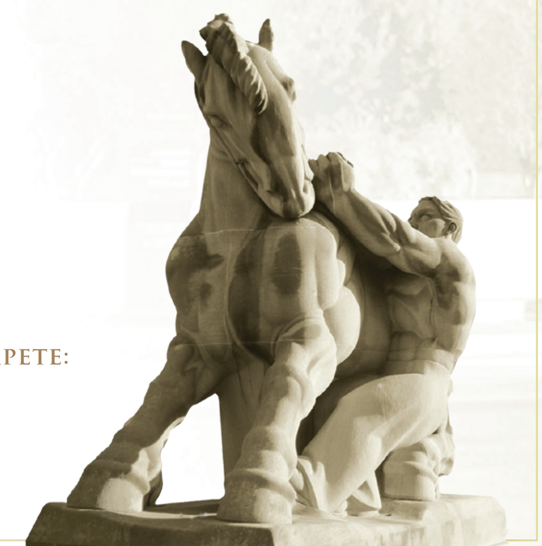


An FTC Guide to

Dealings with Competitors

Group Boycotts

ANY COMPANY MAY, ON ITS OWN, refuse to do business with another firm, but an agreement among competitors not to do business with targeted individuals or businesses may be an illegal boycott, especially if the group of competitors working together has market power. For instance, a group boycott may be used to implement an illegal price-fixing agreement. In this scenario, the competitors agree not to do business with others except on agreed-upon terms, typically with the result of raising prices. An independent decision not to offer services at prevailing prices does not raise antitrust concerns, but an agreement among competitors not to offer services at prevailing prices as a means of achieving an agreed-upon (and typically higher) price does raise antitrust concerns.

EXAMPLE: The FTC has challenged the actions of several groups of competing health care providers, such as doctors, charging that their refusal to deal with insurers or other purchasers on other than jointly-agreed upon terms amounted to an illegal group boycott. For a description of these actions, read the Overview of FTC Antitrust Actions in Health Care Services and Products. The FTC also successfully challenged the group boycott of an association of competing trial lawyers to stop providing legal services to the District of Columbia for indigent criminal defendants until the District increased the fees it paid for those services. The Supreme Court upheld the FTC's ruling in this case. 493 U.S. 411 (1990).

Boycotts to prevent a firm from entering a market or to disadvantage an existing competitor are also illegal. FTC cases have involved a group of physicians charged with using a boycott to prevent a managed care organization from establishing a competing health care facility, and retailers who used a boycott to force manufacturers to limit sales through a competing catalog vendor.

Boycotts targeting "price cutters" are especially likely to raise antitrust concerns, and may be achieved with the help of a common dealer or supplier. This was the case in the FTC's action against a national toy retailer that obtained parallel agreements from several toy manufacturers not to supply low-priced "club" stores with a full range of toys. As a result of the supplier boycott organized by the large retailer, consumers had a difficult time comparing the value of different toys at different retail outlets, the kind of comparison shopping which could have driven retailers to lower their toy prices.

Boycotts for other reasons may be illegal if the boycott restricts competition and lacks a business justification. The FTC charged a group of California auto dealers with using an illegal boycott to prevent a newspaper from telling consumers how to use wholesale price information when shopping for cars. The FTC proved that the boycott affected price competition and had no reasonable justification.

AN AGREEMENT AMONG COMPETITORS NOT TO OFFER SERVICES AT PREVAILING PRICES AS A MEANS OF ACHIEVING AN AGREED-UPON (AND TYPICALLY HIGHER) PRICE DOES RAISE ANTITRUST CONCERNS.

Q: I am a purchasing manager and I have problems with a supplier who is always late with deliveries and won't return my phone calls. I've heard that other companies have stopped doing business with him. Can I recommend that my company find another supplier, too?

A: A business can always unilaterally choose its business partners. As long as it is not part of an agreement with competitors to stop doing business with a targeted supplier, the decision not to deal with a supplier should not raise antitrust concerns.

Other Agreements Among Competitors

OTHER AGREEMENTS AMONG COMPETITORS that are not inherently harmful to consumers are examined under a flexible "rule of reason" standard that attempts to determine their overall competitive effect. Here the focus is on the nature of the agreement, the harm that could arise, and whether the agreement is reasonably necessary to achieve procompetitive benefits. Below are a few examples of these types of dealings with competitors that may pose competitive problems.

Agreements to restrict advertising

Truthful advertising is important in a free market system because it helps consumers compare the price and quality of products offered by competing suppliers. The FTC Act itself prohibits advertising that is false or deceptive, and the FTC vigorously enforces this standard to empower consumers to make choices in the marketplace. Competitor restrictions on the amount or content of advertising that is truthful and not deceptive may be illegal if evidence shows the restrictions have anticompetitive effects and lack reasonable business justifications.

EXAMPLE: The FTC challenged a professional code adopted by a national association of arbitrators that banned virtually all forms of advertising and soliciting clients. In a consent agreement with that organization, the rules were changed so that individual members were not barred from advertising truthful information about their prices and services.

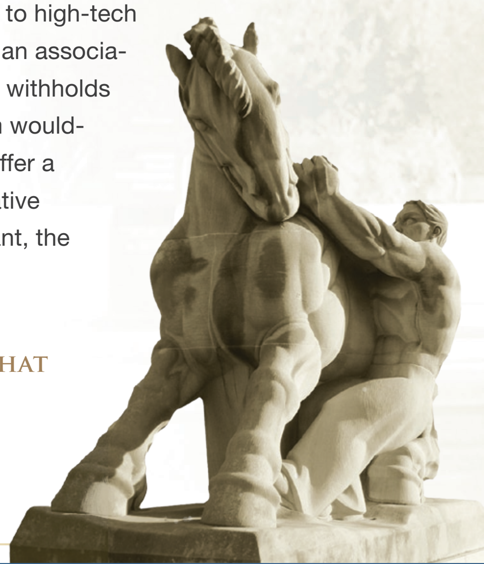
Codes of ethics

The antitrust laws do not prohibit professional associations from adopting reasonable ethical codes designed to protect the public. Such self-regulatory activity serves legitimate purposes, and in most cases can be expected to benefit, rather than to injure, competition or consumers. In some instances, however, ethical rules may be unlawful if they unreasonably restrict the ways professionals may compete. For example, a mandatory code of ethics that prevents members from competing on the basis of price or on terms other than those developed by the trade group can be an unreasonable restraint on competition.

EXAMPLE: The FTC challenged an organization of store planners that sought to prevent its members from offering free or discounted design or planning services. The group's mandatory code of ethics discouraged price competition among the planners to the detriment of consumers.

Exclusive member benefits

Business associations made up of competitors can offer their members important services and benefits that improve efficiency and reduce costs. These services and benefits can range from general industry promotion to high-tech support. But when an association of competitors withholds these benefits from would-be members that offer a competitive alternative that consumers want, the



Here the focus is on the nature of the agreement, the harm that could arise, and whether the agreement is reasonably necessary to achieve procompetitive benefits.

restriction may harm competition and keep prices high. This problem only occurs when members of the association have a significant market presence and it is difficult for non-members to compete without access to association-sponsored benefits.

EXAMPLE: Several antitrust cases have challenged realtor board rules that restricted access to Multiple Listing Services (MLS) for advertising homes for sale. The MLS system of combining the home listings of many brokers has substantial benefits for home buyers and sellers. The initial cases invalidated realtor board membership rules that excluded certain brokers from the MLS because access to the MLS was considered key to marketing homes. More recently, FTC enforcement actions have challenged MLS policies that permit access but more subtly disfavor certain types of brokerage arrangements that offer consumers a low-cost alternative to the more traditional, full-service listing agreement. For instance, some brokers offer a limited service model, listing a home on the local MLS for a fee while handing off other aspects of the sale to the seller. The FTC has challenged the rules of several MLS organizations that excluded these brokers from popular home sale web sites. These rules limited the ways in which brokers could conduct their business and denied home sellers the benefit of having different types of listings.

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Dealings with Competitors

Spotlight on Trade Associations

MOST TRADE ASSOCIATION ACTIVITIES are procompetitive or competitively neutral. For example, a trade association may help establish industry standards that protect the public or allow components from different manufacturers to operate together. The association also may represent its members before legislatures or government agencies, providing valuable information to inform government decisions. When these activities are done with adequate safeguards, they need not pose an antitrust risk.

BUT FORMING A TRADE association does not shield joint activities from antitrust scrutiny: Dealings among competitors that violate the law would still violate the law even if they were done through a trade association. For instance, it is illegal to use a trade association to control or suggest prices of members. It is illegal to use information-sharing programs, or standardized contracts, operating hours, accounting, safety codes, or transportation methods, as a disguised means of fixing prices.

One area for concern is exchanging price or other sensitive business data among competitors, whether within a trade or professional association or other industry group. Any data exchange or statistical reporting that includes current prices, or information that identifies data from individual competitors, can raise antitrust concerns if it encourages more uniform prices than otherwise would exist. In general, information reporting cost or data other than price, and historical data rather than current or future data, is less likely to raise antitrust concerns. Dissemination of aggregated data managed by an independent third party also raises fewer concerns.

The FTC and DOJ have developed guidelines, known as the *Statements of Antitrust Enforcement Policy in Health Care*, for health care providers sharing price and cost data, and the principles in these guidelines are broadly applicable to other industries as well. The DOJ has also issued numerous business review letters relating to proposed information exchanges by various trade associations.

DEALINGS AMONG COMPETITORS THAT VIOLATE THE LAW WOULD STILL VIOLATE THE LAW EVEN IF THEY WERE DONE THROUGH A TRADE ASSOCIATION.

Q: It is my job to collect information on competitors from public sources, such as trade journals, securities filings, and press releases. I circulate my report throughout the company. Is this a problem?

A: No. Your company may collect price or other competitive information from public sources.

Q: I am a regional sales manager and I regularly get calls from an industry consultant. If I share with him our company's plan to raise product prices, does this create a problem for my company?

A: Information about future plans should be closely guarded; disclosing future plans outside the company could alter competitors' decisions and raise antitrust concerns. In addition, employees should be careful when sharing information they could not otherwise share with competitors through intermediaries such as a financial analyst or even a supplier. If the consultant were to share that specific information with the company's competitors, resulting in a change in their pricing strategy, such indirect communications could be seen as facilitating an agreement if other evidence points to a coordinated strategy.

Q: The bylaws of our trade association require my company to provide sales data. What should I do?

A: Many trade associations maintain industry statistics and share the aggregated data with members. Collection of historical data by an independent third party, such as a trade association, that is then shared or reported on an aggregated basis is unlikely to raise competitive issues. Other factors can also reduce the antitrust risk. For instance, the *Statements of Antitrust Enforcement Policy in Health Care* set out a "safety zone" for data exchanges: (1) that are gathered and managed by a third party (like a trade association); (2) involve data more than three months old; and (3) involve at least five participants, when no individual participant accounts for more than 25% on a weighted basis of the statistic reported, and the data is aggregated such that it would not be possible to identify the data of any particular participant.

An FTC Guide to

Dealings in the Supply Chain

Introduction

THE ANTITRUST LAWS ALSO AFFECT a variety of "vertical" relationships—those involving firms at different levels of the supply chain—such as manufacturer-dealer or supplier-manufacturer. Restraints in the supply chain are tested for their reasonableness, by analyzing the market in detail and balancing any harmful competitive effects against offsetting benefits.

IN GENERAL, the law views most vertical arrangements as beneficial overall because they reduce costs and promote efficient distribution of products. A vertical arrangement may violate the antitrust laws, however, if it reduces competition among firms at the same level (say among retailers or among wholesalers) or prevents new firms from entering the market. This is particularly a concern in markets with few sellers or those dominated by one seller. In these markets, manufacturer- or supplier-imposed restraints may make it difficult for newcomers or firms with innovative products to find outlets and reach consumers.

Fact Sheets for Dealings in the Supply Chain

- **Manufacturer-imposed Requirements:** Price, territory, and customer restrictions on dealers.
- **Exclusive Dealing or Requirements Contracts**
- **Refusal to Supply**

An FTC Guide to

Dealings in the Supply Chain

Manufacturer-imposed Requirements

REASONABLE PRICE, TERRITORY, AND CUSTOMER RESTRICTIONS on dealers are legal. Manufacturer-imposed requirements can benefit consumers by increasing competition among different brands (*interbrand competition*) even while reducing competition among dealers in the same brand (*intrabrand competition*). For instance, an agreement between a manufacturer and dealer to set maximum (or "ceiling") prices prevents dealers from charging a non-competitive price. Or an agreement to set minimum (or "floor") prices or to limit territories may encourage dealers to provide a level of service that the manufacturer wants to offer to consumers when they buy the product. These benefits must be weighed against any reduction in competition from the restrictions.

UNTIL RECENTLY, courts treated minimum resale price policies differently from those setting maximum resale prices. But in 2007, the Supreme Court determined that all manufacturer-imposed vertical price programs should be evaluated using a rule of reason approach. According to the Court, "Absent vertical price restraints, the retail services that enhance interbrand competition might be underprovided. This is because discounting retailers can free ride on retailers who furnish services and then capture some of the increased demand those services generate." Note that this change is in federal standards; some state antitrust laws and international authorities view minimum price rules as illegal per se.

If a manufacturer, on its own, adopts a policy regarding a desired level of prices, the law allows the manufacturer to deal only with retailers who agree to that policy. A manufacturer also may stop dealing with a retailer that does not follow its resale price policy. That is, a manufacturer can implement a dealer policy on a "take it or leave it" basis.

Limitations on how or where a dealer may sell a product (that is, customer or territory restrictions) are generally legal–*if they are imposed by a manufacturer acting on its own.* These agreements may result in better sales efforts and service in the dealer's assigned area, and, as a result, more competition with other brands.

Antitrust issues may arise if a manufacturer agrees with competing manufacturers to impose price or non-price restraints up or down the supply chain (that is, in dealings with suppliers or dealers), or if suppliers or dealers act together to induce a manufacturer to implement such restraints. Again, the critical distinction is between a unilateral decision to impose a restraint (lawful) and a collective agreement among competitors to do the same (unlawful). For example, a group of car dealers threatened not to sell one make of cars unless the manufacturer allocated new cars on the basis of sales made to customers in each dealer's territory. The FTC found the dealers' actions unreasonable and designed primarily to stop one dealer from selling at low "no haggle" prices and via the Internet to customers all over the country.

A manufacturer may suggest prices to dealers, and then deal only with sellers willing to comply with the price demands.

Determining whether a restraint is "vertical" or "horizontal" can be confusing in some markets, particularly where some manufacturers operate at many different levels and may even supply important inputs to their competitors. The label is not as important as the effect: Does the restraint unreasonably reduce competition among competitors at any level? Is the vertical restraint the product of an agreement among competitors? And labeling an agreement a vertical arrangement will not save it from antitrust scrutiny when there is evidence of anticompetitive horizontal effects. For instance, the FTC has stopped exclusive distribution agreements that operated as market allocation schemes between worldwide competitors. In this situation, the competitors agree not to compete by designating one another as an exclusive distributor for different geographic areas

Q: One of my suppliers marks its products with a Manufacturer Suggested Retail Price (MSRP). Do I have to charge this price?

A: The key word is "suggested." A dealer is free to set the retail price of the products it sells. A dealer can set the price at the MSRP or at a different price, as long as the dealer comes to that decision on its own. However, the manufacturer can decide not to use distributors that do not adhere to its MSRP.

Q: I am a manufacturer and I occasionally get complaints from dealers about the retail prices that other dealers are charging for my products. What should I tell them?

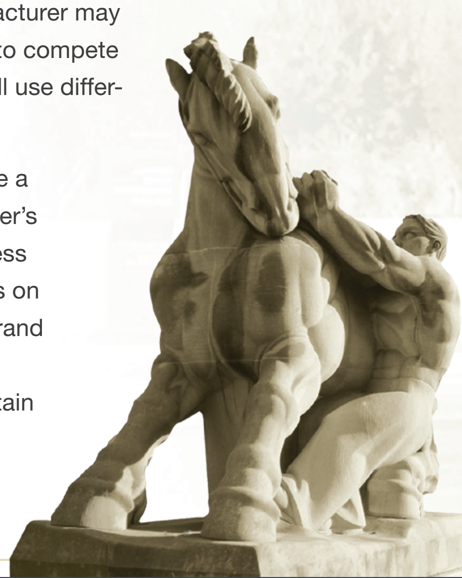
A: Competitors at each level of the supply chain must set prices independently. That means manufacturers cannot agree on wholesale prices, and dealers cannot agree on retail prices. However, a manufacturer can listen to its dealers and take action on its own in response to what it learns from them.

Many private antitrust cases have involved a manufacturer cutting off a discounting dealer. Often there is evidence that the manufacturer received complaints from competing dealers before terminating the discounter. This evidence alone is not enough to show a violation; the manufacturer is entitled to try to keep its dealers happy with their affiliation. Legal issues may arise if it appears that the dealers have agreed to threaten a boycott or collectively pressure the manufacturer to take action.

Q: I would like to carry the products of a certain manufacturer, but the company already has a franchised dealer in my area. Isn't this a restriction on competition?

A: Under federal antitrust law, a manufacturer may decide how many distributors it will have and who they will be. From a competition viewpoint, a manufacturer may decide that it will use only franchised dealers with exclusive territories to compete more successfully with other manufacturers. Or it may decide that it will use different dealers to target specific customer groups.

There are pros and cons to being a franchised dealer. By agreeing to be a franchised dealer, you likely would have to comply with the manufacturer's requirements for selling the product, such as operating hours, cleanliness standards, and the like. These restrictions are seen as reasonable limits on how you run your business in exchange for dealing in an established brand that consumers associate with a certain level of quality or service. For instance, a brewer may require all retail stores to store its beer at a certain



temperature to preserve its quality, because consumers are likely to blame poor quality on the manufacturer–thus reducing sales at all outlets–rather than blaming the retailer's inadequate storage method.

Q: My supplier offers a cooperative advertising program, but I can't participate if I advertise a price that is below the supplier's minimum advertised price. I think that's unfair.

A: The law allows a manufacturer considerable leeway in setting the terms for advertising that it helps to pay for. The manufacturer offers these promotional programs to better compete against the products of the other manufacturers. There are limited situations when these programs can have an unreasonable effect on price levels. For instance, the FTC challenged the Minimum Advertised Price (MAP) policies of five large distributors of pre-recorded music because the policies were unreasonable in their reach: they prohibited ads with discounted prices, even if the retailer paid for the ads with its own money; they applied to in-store advertising; and a single violation required the retailer to forfeit funds for all of its stores for up to 90 days. The FTC found that these policies, in effect for more than 85 percent of market sales, were unreasonable and prevented retailers from telling consumers about discounts on records and CDs. Issues involving advertising allowances may become of less practical concern as manufacturers adjust to new standards that allow more direct influence on retail prices.

Q: I am a health care provider and I want to join a new insurance group to provide services to a large employer in my town. My agreement with another insurance group requires that I give them the lowest price on my services. If I join the new group, do I have to lower my prices for the other insurance group?

A: These provisions, referred to as "most-favored-nations (MFN) clauses," are quite common. Generally, an MFN promises that one party to the agreement will treat the other party at least as well as it treats others. In most circumstances, MFNs are a legitimate way to reduce risks. In some circumstances, however, MFNs can unreasonably limit the offering of targeted discounts and create a de facto industry price. The FTC challenged an MFN clause used by a pharmacy network in individual contracts with its member pharmacies that discouraged them from discounting on reimbursement rates. The network was a group of more than 95 percent of the competing pharmacies in the state. The MFN discouraged any individual pharmacy from offering lower prices to another plan because any discounts would have to be applied to all its other sales through the network.

An FTC Guide to
Dealings in the Supply Chain

Exclusive Dealing or Requirements Contracts

EXCLUSIVE DEALING OR REQUIREMENTS CONTRACTS between manufacturers and retailers are common and are generally lawful. In simple terms, an exclusive dealing contract prevents a distributor from selling the products of a different manufacturer, and a requirements contract prevents a manufacturer from buying inputs from a different supplier. These arrangements are judged under a rule of reason standard, which balances any procompetitive and anticompetitive effects.

MOST EXCLUSIVE DEALING CONTRACTS are beneficial because they encourage marketing support for the manufacturer's brand. By becoming an expert in one manufacturer's products, the dealer is encouraged to specialize in promoting that manufacturer's brand. This may include offering special services or amenities that cost money, such as an attractive store, trained salespeople, long business hours, an inventory of products on hand, or fast warranty service. But the costs of providing some of these amenities—which are offered to consumers before the product is sold and may not be recovered if the consumer leaves without buying anything—may be hard to pass on to customers in the form of a higher retail price. For instance, the consumer may take a "free ride" on the valuable services offered by one retailer, and then buy the same product at a lower price from another retailer that does not offer high-cost amenities, such as a discount warehouse or online store. If the full-service retailer loses enough sales in this way, it may eventually stop offering the services. If those services were genuinely useful, in the sense that the product plus the services together resulted in greater sales for the manufacturer than the product alone would have enjoyed, there is a loss both for the manufacturer and the consumer. As a result, antitrust law generally permits nonprice vertical restraints such as exclusive dealing contracts that are designed to encourage retailers to provide extra services.

On the other hand, a manufacturer with market power may potentially use these types of vertical arrangements to prevent smaller competitors from succeeding in the marketplace. For instance, exclusive contracts may be used to deny a competitor access to retailers without which the competitor cannot make sufficient sales to be viable. Or on the supply side, exclusive contracts may tie up most of the lower-cost sources of supply, forcing competitors to seek higher-priced sources. This was the scenario that led to FTC charges that a large pharmaceutical company violated the antitrust laws by obtaining exclusive licenses for a critical ingredient. The FTC claimed that the licenses had the effect of raising ingredient costs for its competitors, which led to higher retail drug prices.

In some situations, exclusive dealing may be used by manufacturers to reduce competition between them. For example, the FTC challenged exclusive provisions in sales contracts used by two principal manufacturers of pumps for fire trucks. Each company sold pumps to fire truck manufacturers on the condition that any additional pumps would be bought from the manufacturer that was already supplying them. These exclusive supply contracts operated like a customer allocation agreement between the two pump manufacturers, so that they no longer competed for each other's customers.

ANTITRUST LAW GENERALLY PERMITS NONPRICE VERTICAL RESTRAINTS SUCH AS EXCLUSIVE DEALING CONTRACTS THAT ARE DESIGNED TO ENCOURAGE RETAILERS TO PROVIDE EXTRA SERVICES.

For discussion of exclusive licensing arrangements involving intellectual property rights, see *Antitrust Guidelines for the Licensing of Intellectual Property*.

Q: I am a small manufacturer of high-quality flat-panel display monitors. I would like to get my products into a big box retailer, but the company says it has an agreement to sell only flat-panel display monitors made by my competitor. Isn't that illegal?

A: Exclusive distribution arrangements like this usually are permitted. Although the retailer is prevented from selling competing flat-panel display monitors, this may be the type of product that requires a certain level of knowledge and service to sell. For instance, if the manufacturer invests in training the retailer's sales staff in the product's operation and attributes, it may reasonably require that the retailer commit to selling only its brand of monitors. This level of service benefits buyers of sophisticated electronics products. As long as there are sufficient outlets for consumers to buy your products elsewhere, the antitrust laws are unlikely to interfere with this type of exclusive arrangement.

AN FTC GUIDE TO

Dealings in the Supply Chain

Refusal to Supply

IN GENERAL, A SELLER HAS THE RIGHT TO CHOOSE ITS BUSINESS PARTNERS. A firm's refusal to deal with any other person or company is lawful so long as the refusal is not the product of an anticompetitive agreement with other firms or part of a predatory or exclusionary strategy to acquire or maintain a monopoly. This principle was laid out by the Supreme Court more than 85 years ago:

> "The purpose of the Sherman Act is to ... preserve the right of freedom of trade. In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of a trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal."

This remains a fundamental rule of federal antitrust law and draws a line between legal independent decision-making on the one hand and illegal joint or monopolistic activity on the other.

Q: I OWN A SMALL CLOTHING STORE AND THE MAKER OF A POPULAR LINE OF CLOTHING RECENTLY DROPPED ME AS AN OUTLET. I'M SURE IT'S BECAUSE MY COMPETITORS COMPLAINED THAT I SELL BELOW THE SUGGESTED RETAIL PRICE. THE EXPLANATION WAS THE MANUFACTURER'S POLICY: ITS PRODUCTS SHOULD NOT BE SOLD BELOW THE SUGGESTED RETAIL PRICE, AND DEALERS THAT DO NOT COMPLY ARE SUBJECT TO TERMINATION. IS IT LEGAL FOR THE MANUFACTURER TO CUT ME OFF?

A: Yes. The law generally allows a manufacturer to have a policy that its dealers should sell a product above a certain minimum price, and to terminate a dealer that does not honor that policy. Manufacturers may choose to adopt this kind of policy because it encourages dealers to provide full customer service and prevents other dealers, who may not provide full service, from taking away customers and "free riding" on the services provided by other dealers. However, it may be illegal for the manufacturer to drop you if it has an agreement with your competitors to cut you off to help maintain a price they agreed to.

A FIRM'S REFUSAL TO DEAL IS LAWFUL SO LONG AS THE REFUSAL IS NOT THE PRODUCT OF AN ANTICOMPETITIVE AGREEMENT WITH OTHER FIRMS OR PART OF A PREDATORY OR EXCLUSIONARY STRATEGY TO ACQUIRE OR MAINTAIN A MONOPOLY.

An FTC Guide to Single Firm Conduct

Introduction

SOME COMPANIES SUCCEED IN THE MARKETPLACE to the point where their behavior may not be subject to common competitive pressures. This is not a concern for most businesses, as most markets in the U.S. support many competing firms, and the competitive give-and-take prevents any single firm from having undue influence on the workings of the market.

SECTION 2 OF THE SHERMAN ACT makes it unlawful for a company to "monopolize, or attempt to monopolize," trade or commerce. As that law has been interpreted, it is not illegal for a company to have a monopoly, to charge "high prices," or to try to achieve a monopoly position by what might be viewed by some as particularly aggressive methods. The law is violated only if the company tries to maintain or acquire a monopoly through unreasonable methods. For the courts, a key factor in determining what is unreasonable is whether the practice has a legitimate business justification.

These Fact Sheets discuss antitrust rules that courts have developed to deal with the actions of a single firm that has market power.

Fact Sheets for Single Firm Conduct

- **Monopolization Defined:** Market power plus exclusionary or predatory acts without business justification
- **Exclusionary or Predatory Acts**
  - Exclusive Supply or Purchase Agreements
  - Tying the Sale of Two Products
  - Predatory or Below-Cost Pricing
  - Refusal to Deal

AN FTC GUIDE TO

Single Firm Conduct

Monopolization Defined

THE ANTITRUST LAWS prohibit conduct by a single firm that unreasonably restrains competition by creating or maintaining monopoly power. Most Section 2 claims involve the conduct of a firm with a leading market position, although Section 2 of the Sherman Act also bans attempts to monopolize and conspiracies to monopolize. As a first step, courts ask if the firm has "monopoly power" in any market. This requires in-depth study of the products sold by the leading firm, and any alternative products consumers may turn to if the firm attempted to raise prices. Then courts ask if that leading position was gained or maintained through improper conduct—that is, something other than merely having a better product, superior management or historic accident. Here courts evaluate the anticompetitive effects of the conduct and its procompetitive justifications.

MARKET POWER. Courts do not require a literal monopoly before applying rules for single firm conduct; that term is used as shorthand for a firm with significant and durable market power–that is, the long term ability to raise price or exclude competitors. That is how that term is used here: a "monopolist" is a firm with significant and durable market power. Courts look at the firm's market share, but typically do not find monopoly power if the firm (or a group of firms acting in concert) has less than 50 percent of the sales of a particular product or service within a certain geographic area. Some courts have required much higher percentages. In addition, that leading position must be sustainable over time: if competitive forces or the entry of new firms could discipline the conduct of the leading firm, courts are unlikely to find that the firm has lasting market power.

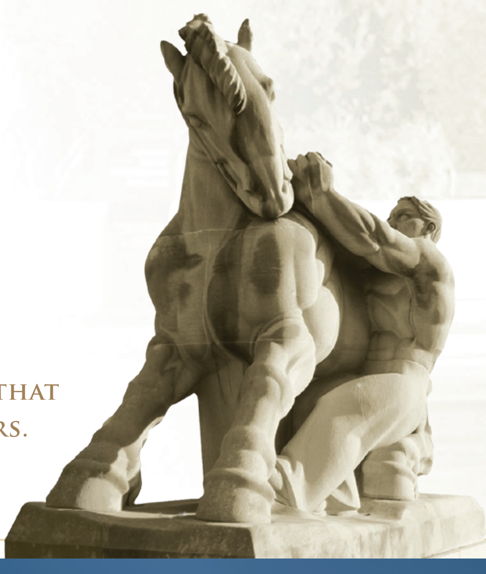
EXCLUSIONARY CONDUCT

Judging the conduct of an alleged monopolist requires an in-depth analysis of the market and the means used to achieve or maintain the monopoly. Obtaining a monopoly by superior products, innovation, or business acumen is legal; however, the same result achieved by exclusionary or predatory acts may raise antitrust concerns. Exclusionary or predatory acts may include such things as exclusive supply or purchase agreements; tying; predatory pricing; or refusal to deal. These topics are discussed in separate Fact Sheets for Single Firm Conduct.

BUSINESS JUSTIFICATION

Finally, the monopolist may have a legitimate business justification for behaving in a way that prevents other firms from succeeding in the marketplace. For instance, the monopolist may be competing on the merits in a way that benefits consumers through greater efficiency or a unique set of products or services. In the end, courts will decide whether the monopolist's success is due to "the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."

MONOPOLY: A FIRM WITH SIGNIFICANT AND DURABLE MARKET POWER–THAT IS, THE LONG TERM ABILITY TO RAISE PRICE OR EXCLUDE COMPETITORS.



EXAMPLE–THE MICROSOFT CASE: Microsoft was found to have a monopoly over operating systems software for IBM-compatible personal computers. Microsoft was able to use its dominant position in the operating systems market to exclude other software developers and prevent computer makers from installing non-Microsoft browser software to run with Microsoft's operating system software. Specifically, Microsoft illegally maintained its operating systems monopoly by including Internet Explorer, the Microsoft Internet browser, with every copy of its Windows operating system software sold to computer makers, and making it technically difficult not to use its browser or to use a non-Microsoft browser. Microsoft also granted free licenses or rebates to use its software, which discouraged other software developers from promoting a non-Microsoft browser or developing other software based on that browser. These actions hampered efforts by computer makers to use or promote competing browsers, and discouraged the development of add-on software that was compatible with non-Microsoft browsers. The court found that, although Microsoft did not tie up all ways of competing, its actions did prevent rivals from using the lowest-cost means of taking market share away from Microsoft. To settle the case, Microsoft agreed to end certain conduct that was preventing the development of competing browser software.

AN FTC GUIDE TO

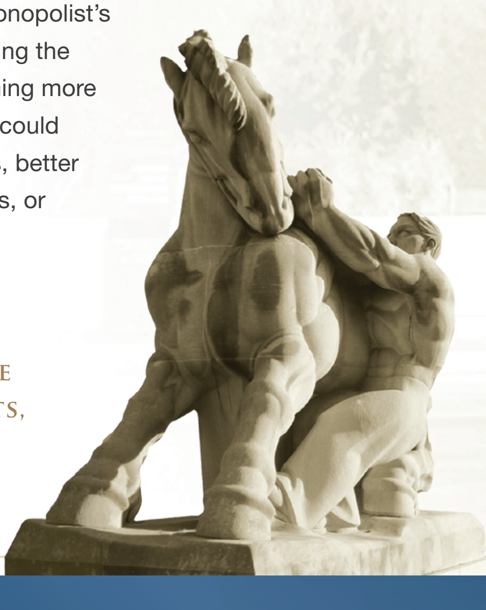
Single Firm Conduct

Exclusive Supply or Purchase Agreements

EXCLUSIVE CONTRACTS CAN BENEFIT COMPETITION in the market by ensuring supply sources or sales outlets, reducing contracting costs, or creating dealer loyalty. As discussed in the Fact Sheets on Dealings in the Supply Chain, exclusive contracts between manufacturers and suppliers, or between manufacturers and dealers, are generally lawful because they improve competition among the brands of different manufacturers *(interbrand competition)*. However, when the firm using exclusive contracts is a monopolist, the focus shifts to whether those contracts impede efforts of new firms to break into the market or of smaller existing firms to expand their presence. The monopolist might try to impede the entry or expansion of new competitors because that competition would erode its market position. The antitrust laws condemn certain actions of a monopolist that keep rivals out of the market or prevent new products from reaching consumers. The potential for harm to competition from exclusive contracts increases with: 1) the length of the contract term; 2) the more outlets or sources covered; and 3) the fewer alternative outlets or sources not covered.

EXCLUSIVE SUPPLY CONTRACTS prevent a supplier from selling inputs to another buyer. If one buyer has a monopoly position and obtains exclusive supply contracts so that a newcomer may not be able to gain the inputs it needs to compete with the monopolist, the contracts can be seen as an exclusionary tactic in violation of Section 2 of the Sherman Act. For example, the FTC stopped a large drug maker from enforcing 10-year exclusive supply agreements for an essential ingredient to make its medicines in return for which the suppliers would have received a percentage of profits from the drug. The FTC found that the drug maker used the exclusive supply agreements to keep other drug makers from the market by controlling access to the essential ingredient. The drug maker was then able to raise prices for its medicine by more than 3000 percent.

EXCLUSIVE PURCHASE AGREEMENTS, requiring a dealer to sell the products of only one manufacturer, can have similar effects on a new manufacturer, preventing it from getting its products into enough outlets so that consumers can compare its new products to those of the leading manufacturer. For instance, the DOJ challenged exclusive dealing contracts used by a manufacturer of artificial teeth with a market share of at least 75 percent. These exclusive contracts with key dealers effectively blocked the smaller rivals from getting their teeth sold to dental labs, and ultimately, used by dental patients. In similar situations, newcomers may face significant additional costs and time to induce dealers to give up the exclusive agreements with the leading firm, or to establish a different means of getting its product before consumers. The harm to consumers in these cases is that the monopolist's actions are preventing the market from becoming more competitive, which could lead to lower prices, better products or services, or new choices.



ILLEGAL MONOPOLIZATION MAY INCLUDE SUCH THINGS AS EXCLUSIVE SUPPLY OR PURCHASE AGREEMENTS, TYING THE SALE OF TWO PRODUCTS, PREDATORY PRICING, AND REFUSAL TO DEAL.

Tying the Sale of Two Products

OFFERING PRODUCTS TOGETHER AS PART OF A PACKAGE can benefit consumers who like the convenience of buying several items at the same time. Offering products together can also reduce the manufacturer's costs for packaging, shipping, and promoting the products. Of course, some consumers might prefer to buy products separately, and when they are offered only as part of a package, it can be more difficult for consumers to buy only what they want.

FOR COMPETITIVE PURPOSES, a monopolist may use forced buying, or "tie-in" sales, to gain sales in other markets where it is not dominant and to make it more difficult for rivals in those markets to obtain sales. This may limit consumer choice for buyers wanting to purchase one ("tying") product by forcing them to also buy a second ("tied") product as well. Typically, the "tied" product may be a less desirable one that the buyer might not purchase unless required to do so, or may prefer to get from a different seller. If the seller offering the tied products has sufficient market power in the "tying" product, these arrangements can violate the antitrust laws.

The law on tying is changing. Although the Supreme Court has treated some tie-ins as per se illegal in the past, lower courts have started to apply the more flexible "rule of reason" to assess the competitive effects of tied sales. Cases turn on particular factual settings, but the general rule is that tying products raises antitrust questions when it restricts competition without providing benefits to consumers.

EXAMPLE: The FTC challenged a drug maker that required patients to purchase its blood-monitoring services along with its medicine to treat schizophrenia. The drug maker was the only producer of the medicine, but there were many companies capable of providing blood-monitoring services to patients using the drug. The FTC claimed that tying the drug and the monitoring services together raised the price of that medical treatment and prevented independent providers from monitoring patients taking the drug. The drug maker settled the charges by agreeing not to prevent other companies from providing blood-monitoring services.

ILLEGAL MONOPOLIZATION MAY INCLUDE SUCH THINGS AS EXCLUSIVE SUPPLY OR PURCHASE AGREEMENTS, TYING THE SALE OF TWO PRODUCTS, PREDATORY PRICING, REFUSAL TO DEAL.

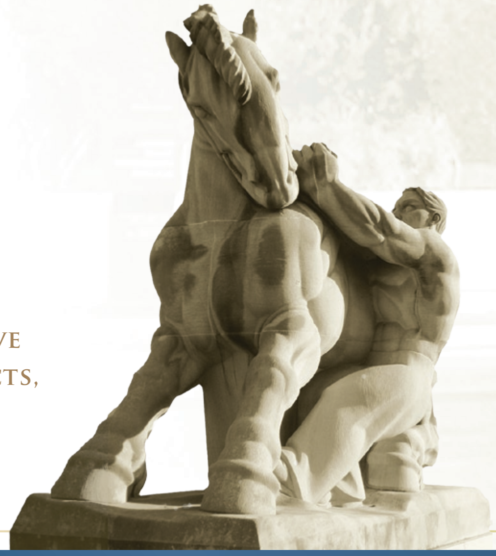
Predatory Pricing

CAN PRICES EVER BE "TOO LOW?" The short answer is yes, but not very often. Generally, low prices benefit consumers. Consumers are harmed only if below-cost pricing allows a dominant competitor to knock its rivals out of the market and then raise prices to above-market levels for a substantial time. A firm's independent decision to reduce prices to a level below its own costs does not necessarily injure competition, and, in fact, may simply reflect particularly vigorous competition. Instances of a large firm using low prices to drive smaller competitors out of the market in hopes of raising prices after they leave are rare. This strategy can only be successful if the short-run losses from pricing below cost will be made up for by much higher prices over a longer period of time after competitors leave the market. Although the FTC examines claims of predatory pricing carefully, courts, including the Supreme Court, have been skeptical of such claims.

Q: The gas station down the street offers a discount program that gives members cents off every gallon purchased. I can't match those prices because they are below my costs. If I try to compete at those prices, I will go out of business. Isn't this illegal?

A: Pricing below a competitor's costs occurs in many competitive markets and generally does not violate the antitrust laws. Sometimes the low-pricing firm is simply more efficient. Pricing below your own costs is also not a violation of the law unless it is part of a strategy to eliminate competitors, and when that strategy has a dangerous probability of creating a monopoly for the discounting firm so that it can raise prices far into the future and recoup its losses. In markets with a large number of sellers, such as gasoline retailing, it is unlikely that one company could price below cost long enough to drive out a significant number of rivals and attain a dominant position.

ILLEGAL MONOPOLIZATION MAY INCLUDE SUCH THINGS AS EXCLUSIVE SUPPLY OR PURCHASE AGREEMENTS, TYING THE SALE OF TWO PRODUCTS, PREDATORY PRICING, AND REFUSAL TO DEAL.



AN FTC GUIDE TO

Single Firm Conduct

Refusal To Deal

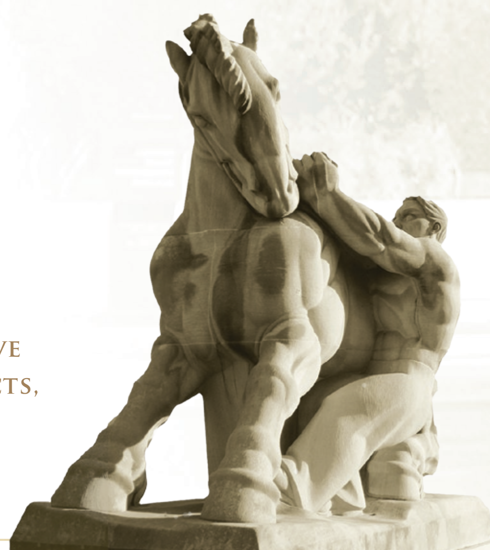
IN GENERAL, ANY BUSINESS–EVEN A MONOPOLIST–may choose its business partners. However, under certain circumstances, there may be limits on this freedom for a firm with market power. As courts attempt to define those limited situations when a firm with market power may violate antitrust law by refusing to do business with other firms, the focus is on how the refusal to deal helps the monopolist maintain its monopoly, or allows the monopolist to use its monopoly in one market to attempt to monopolize another market.

SOMETIMES THE REFUSAL to deal is with customers or suppliers, with the effect of preventing them from dealing with a rival: "I refuse to deal with you if you deal with my competitor." For example, in a case from the 1950's, the only newspaper in a town refused to carry advertisements from companies that were also running ads on a local radio station. The newspaper monitored the radio ads and terminated its ad contracts with any business that ran ads on the radio. The Supreme Court found that the newspaper's refusal to deal with businesses using the radio station strengthened its dominant position in the local advertising market and threatened to eliminate the radio station as a competitor.

One of the most unsettled areas of antitrust law has to do with the duty of a monopolist to deal with its competitors. In general, a firm has no duty to deal with its competitors. In fact, imposing obligations on a firm to do business with its rivals is at odds with other antitrust rules that discourage agreements among competitors that may unreasonably restrict competition. But courts have, in some circumstances, found antitrust liability when a firm with market power refused to do business with a competitor. For instance, if the monopolist refuses to sell a product or service to a competitor that it makes available to others, or if the monopolist has done business with the competitor and then stops, the monopolist needs a legitimate business reason for its policies. Courts will continue to develop the law in this area.

For industries that are regulated, companies may be required by other laws to deal on non-discriminatory terms with other businesses, including competitors and potential competitors. Here, the obligations of a regulated firm to cooperate may be spelled out in a statute or regulations that are enforced by a local, state, or federal agency. The Supreme Court recently found that, for firms that are obliged to share assets with competitors under a regulatory scheme at regulated rates, the antitrust laws do not impose additional duties. That case involved a local telephone company that was required by federal law to provide access to its system, including support services, in a reasonable manner to firms wanting to enter the business of providing local phone service. The Supreme Court dismissed an entrant's antitrust claims, finding that the antitrust laws do not impose additional duties to share assets beyond those required by a comprehensive set of regulations.

ILLEGAL MONOPOLIZATION MAY INCLUDE SUCH THINGS AS EXCLUSIVE SUPPLY OR PURCHASE AGREEMENTS, TYING THE SALE OF TWO PRODUCTS, PREDATORY PRICING, AND REFUSAL TO DEAL.



An FTC Guide to

Price Discrimination Among Buyers

ROBINSON-PATMAN VIOLATIONS

A SELLER CHARGING COMPETING BUYERS DIFFERENT PRICES for the same "commodity" or discriminating in the provision of "allowances"—compensation for advertising and other services—may be violating the Robinson-Patman Act. This kind of price discrimination may give favored customers an edge in the market that has nothing to do with their superior efficiency. Price discriminations are generally lawful, particularly if they reflect the different costs of dealing with different buyers or are the result of a seller's attempts to meet a competitor's offering.

The Supreme Court has ruled that price discrimination claims under the Robinson-Patman Act should be evaluated consistent with broader antitrust policies. In practice, Robinson-Patman claims must meet several specific legal tests:

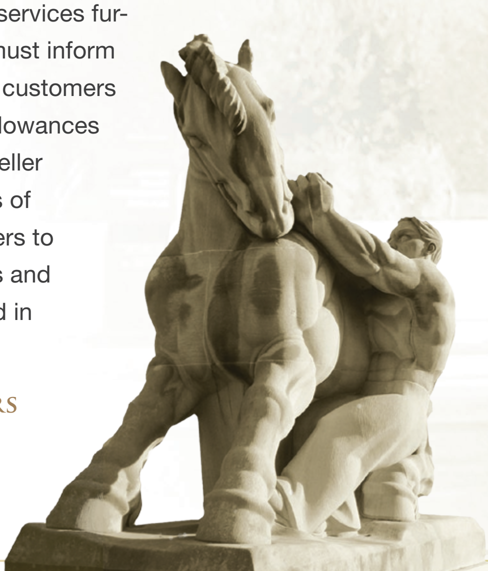
1. The Act applies to commodities, but not to services, and to purchases, but not to leases.
2. The goods must be of "like grade and quality."
3. There must be likely injury to competition (that is, a private plaintiff must also show actual harm to his or her business).
4. Normally, the sales must be "in" interstate commerce (that is, the sale must be across a state line).

Competitive injury may occur in one of two ways. "Primary line" injury occurs when one manufacturer reduces its prices in a specific geographic market and causes injury to its competitors in the same market. For example, it may be illegal for a manufacturer to sell below cost in a local market over a sustained period. Businesses may also be concerned about "secondary line" violations, which occur when favored customers of a supplier are given a price advantage over competing customers. Here, the injury is at the buyer's level.

The necessary harm to competition at the buyer level can be inferred from the existence of significant price discrimination over time. Courts may be starting to limit this inference to situations in which either the buyer or the seller has market power, on the theory that, for example, lasting competitive harm is unlikely if alternative sources of supply are available.

There are two legal defenses to these types of alleged Robinson-Patman violations: (1) the price difference is justified by different costs in manufacture, sale, or delivery (e.g., volume discounts), or (2) the price concession was given in good faith to meet a competitor's price.

The Robinson-Patman Act also forbids certain discriminatory allowances or services furnished or paid to customers. In general, it requires that a seller treat all competing customers in a proportionately equal manner. Services or facilities covered include payment for or furnishing advertising or promotional allowances, handbills, catalogues, signs, demonstrations, display and storage cabinets, special packaging, warehousing facilities, credit returns, and prizes or free merchandise for promotional contests. The cost justification does not apply if the discrimination is in allowances or services furnished. The seller must inform all of its competing customers if any services or allowances are available. The seller must allow all types of competing customers to receive the services and allowances involved in



This kind of price discrimination may give favored customers an edge in the market that has nothing to do with their superior efficiency.

a particular plan or provide some other reasonable means of participation for those who cannot use the basic plan. A more detailed discussion of these promotional issues can be found in the FTC's *Fred Meyer Guides.*

Under certain circumstances, a buyer who benefits from the discrimination may also be found to have violated the Act, along with the seller who grants the discrimination, if the buyer forced, or "induced," the seller to grant a discriminatory price.

Although proof of a violation of the Robinson-Patman Act often involves complex legal questions, businesses should keep in mind some of the basic practices that may be illegal under the Act. These include:

- Below-cost sales by a firm that charges higher prices in different localities, and that has a plan of recoupment;
- Price differences in the sale of identical goods that cannot be justified on the basis of cost savings or meeting a competitor's prices; or
- Promotional allowances or services that are not practically available to all customers on proportionately equal terms.

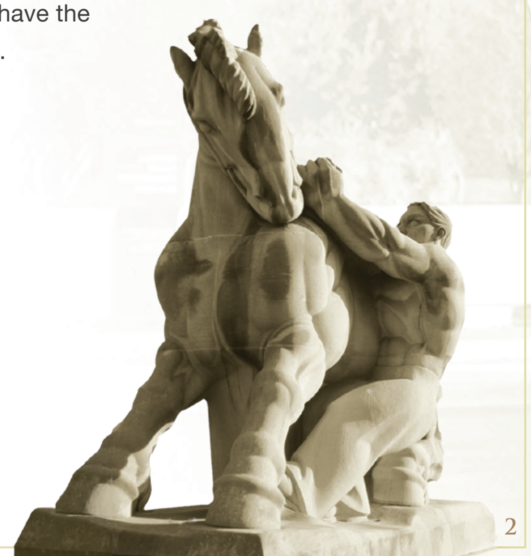
Under the Nonprofit Institutions Act, eligible nonprofit entities may purchase—and vendors may sell to them—supplies at reduced prices for the nonprofit's own use, without violating the Robinson-Patman Act. The Health Care Services & Products Division issued a recent advisory opinion discussing the application of this exemption to pharmaceutical purchases by a nonprofit health maintenance organization.

Q: I operate two stores that sell compact discs. My business is being ruined by giant discount chains that sell their products for less than my wholesale cost. What can I do?

A: Discount chains may be able to buy compact discs at a lower wholesale price because it costs the manufacturer less, on a per-unit basis, to deal with large-volume customers. If so, the manufacturer may have a "cost justification" defense to the differential pricing and the policy would not violate the Robinson-Patman Act.

Q: One of my suppliers is selling parts at its company-owned store at retail prices that are below the wholesale price that it charges me for the parts. Isn't this illegal?

A: The transfer of parts from a parent to its subsidiary generally is not considered a "sale" under the Robinson-Patman Act. Thus, this situation would not have the required element of sales to two or more purchasers at different prices.



An FTC Guide to

Mergers

Introduction

MANY MERGERS BENEFIT COMPETITION AND CONSUMERS by allowing firms to operate more efficiently. But some mergers change market dynamics in ways that can lead to higher prices, fewer or lower-quality goods or services, or less innovation.

Section 7 of the Clayton Act prohibits mergers and acquisitions when the effect "may be substantially to lessen competition, or to tend to create a monopoly." The key question the agency asks is whether the proposed merger is likely to create or enhance market power or facilitate its exercise. The greatest antitrust concern arises with proposed mergers between direct competitors (horizontal mergers). The FTC and the DOJ have developed Horizontal Merger Guidelines that set out the agencies' analytical framework for answering that key question, and have provided a Commentary on the Horizontal Merger Guidelines that provides many specific examples of how those principles have been applied in actual mergers reviewed by the agencies.

Merger law is generally forward-looking: it bars mergers that may lead to harmful effects. The premerger notification requirements of the Hart-Scott-Rodino Act allow the antitrust agencies to examine the likely effects of some proposed mergers before they take place. This advance notice avoids the difficult and potentially ineffective "unscrambling of the eggs" once an anticompetitive merger has been completed. The agencies also investigate some completed mergers that subsequently appear to have harmed customers.

Each year, the FTC and Department of Justice review many merger filings. Fully 95 percent of merger filings present no competitive issues. For those deals requiring more in-depth investigation, the FTC has developed Merger Best Practices to help streamline the merger review process and more quickly identify deals that present competitive problems. For those, it is often possible to resolve competitive concerns by consent agreement with the parties, which allows the beneficial aspects of the deal to go forward while eliminating the competitive threat. In a few cases, the agency and the parties cannot agree on a way to fix the competitive problems, and the agency may go to federal court to prevent the merger pending an administrative trial on the merits of the deal.

By law, all information provided to, or obtained by, the agencies in a merger investigation is confidential, and the agencies have very strict rules against disclosing it. These rules prevent the agencies from even disclosing the existence of an investigation. In some situations, however, the parties themselves may announce their merger plans, and the FTC may then confirm the existence of an investigation.

Fact Sheets for Mergers

- » Premerger Notification and the Merger Review Process: Steps in the Merger Review Process
- » Markets: Similar products or services sold in the same locale
- » Competitive Effects:
  Horizontal Mergers,
  Vertical Mergers, or
  Potential Competition Mergers
- » Entry and Efficiencies

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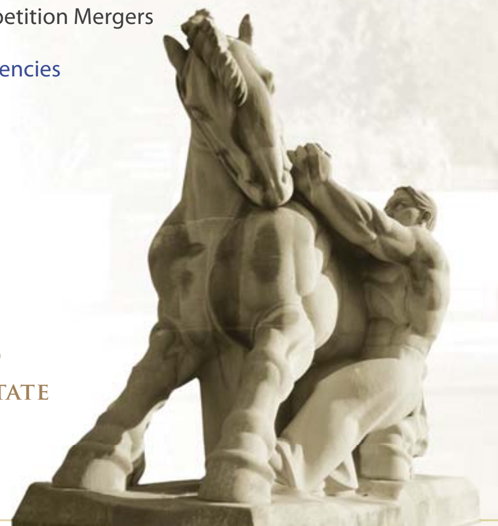


AN FTC GUIDE TO
MERGERS

Premerger Notification and The Merger Review Process

UNDER THE HART-SCOTT-RODINO (HSR) ACT, parties to certain large mergers and acquisitions must file premerger notification and wait for government review. The parties may not close their deal until the waiting period outlined in the HSR Act has passed, or the government has granted early termination of the waiting period. The FTC administers the premerger notification program, and its staff members answer questions and maintain a website with helpful information about how and when to file. The FTC also provides daily updates of deals that receive early termination.

Steps in the Merger Review Process

Step One: Filing Notice of a Proposed Deal

Not all mergers or acquisitions require a premerger filing. Generally, the deal must first have a minimum value and the parties must be a minimum size. These filing thresholds are updated annually. In addition, some stock or asset purchases are exempt, as are purchases of some types of real property. For further help with filing requirements, see the FTC's Guides to the Premerger Notification Program. There is a filing fee for premerger filings.

For most transactions requiring a filing, both buyer and seller must file forms and provide data about the industry and their own businesses. Once the filing is complete, the parties must wait 30 days (15 days in the case of a cash tender offer or a bankruptcy) or until the agencies grant early termination of the waiting period before they can consummate the deal.

Step Two: Clearance to One Antitrust Agency

Parties proposing a deal file with both the FTC and DOJ, but only one antitrust agency will review the proposed merger. Staff from the FTC and DOJ consult and the matter is "cleared" to one agency or the other for review (this is known as the "clearance process"). Once clearance is granted, the investigating agency can obtain non-public information from various sources, including the parties to the deal or other industry participants.

Step Three: Waiting Period Expires or Agency Issues Second Request

After a preliminary review of the premerger filing, the agency can:

1. Terminate the waiting period prior to the end of the waiting period (grant Early Termination or "ET");
2. Allow the initial waiting period to expire; or
3. Issue a request for additional information ("Second Request") to each party, asking for more information.

If the waiting period expires or is terminated, the parties are free to close their deal. If the agency has determined that it needs more information to assess the proposed deal, it sends both parties a Second Request. This extends the waiting period and prevents the companies from completing their deal until they have "substantially complied" with the Second Request and observed a second waiting period. A Second Request typically asks for business documents and data that will inform the agency about the company's products or services, market conditions where the company does business, and the likely competitive effects of the merger. The agency may conduct

THE FTC ADMINISTERS THE PREMERGER NOTIFICATION PROGRAM, ANSWERS QUESTIONS, AND MAINTAINS A WEBSITE WITH HELPFUL INFORMATION ABOUT HOW AND WHEN TO FILE.

interviews (either informally or by sworn testimony) of company personnel or others with knowledge about the industry.

Step Four: Parties Substantially Comply with the Second Requests

Typically, once both companies have substantially complied with the Second Request, the agency has an additional 30 days to review the materials and take action, if necessary. (In the case of a cash tender offer or bankruptcy, the agency has 10 days to complete its review and the time begins to run as soon as the buyer has substantially complied.) The length of time for this phase of review may be extended by agreement between the parties and the government in an effort to resolve any remaining issues without litigation.

Step Five: Waiting Period Expires or the Agency Challenges the Deal

The potential outcomes at this stage are:

1. Close the investigation and let the deal go forward unchallenged;
2. Enter into a negotiated consent agreement with the companies that includes provisions that will restore competition; or
3. Seek to stop the entire transaction by filing for a preliminary injunction in federal court pending an administrative trial on the merits.

Unless the agency takes some action that results in a court order stopping the merger, the parties can close their deal at the end of the waiting period. Sometimes, the parties will abandon their plans once they learn that the agency is likely to challenge the proposed merger.

In many merger investigations, the potential for competitive harm is not a result of the transaction as a whole, but rather occurs only in certain lines of business. One example would be when a buyer competes in a limited line of products with the company it seeks to buy. In this situation the parties may resolve the concerns about the merger by agreeing to sell off the particular overlapping business unit or assets of one of the merging parties, but then complete the remainder of the merger as proposed. This allows the procompetitive benefits of the merger to be realized without creating the potential for anticompetitive harm. Many merger challenges are resolved with a consent agreement between the agency and the merging parties.

Markets

THE LAW BARS MERGERS THAT HAVE POTENTIAL HARMFUL EFFECTS in a “line of commerce” in a “section of the country.” In practical terms, this means the agency will examine the businesses of the merging parties both in terms of what they sell (a product dimension) and where they sell it (a geographic dimension).

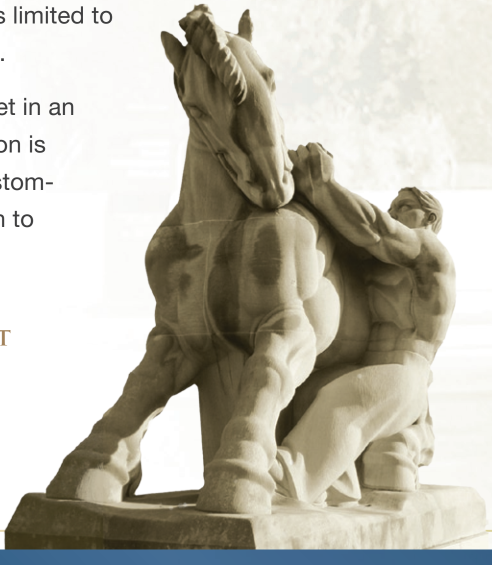
MARKET ANALYSIS STARTS with the products or services of the two merging companies. In the case of a horizontal merger, the companies have products or services that customers see as close substitutes. Before the merger, the two companies may have offered customers lower prices or better service to gain sales from one another. After the merger, that beneficial competition will be gone as the merged firm will make business decisions regarding the products or services of both companies. The loss of competition may not matter if a sufficient number of customers are likely to switch to products or services sold by other companies if the merged company tried to increase its prices. In that case, customers view the products of other rivals to be good substitutes for the products of the merging firms and the merger may not affect adversely the competitive process with higher prices, lower quality, or reduced innovation if there is a sufficient number of competitive choices after the deal.

In the most general terms, a product market in an antitrust investigation consists of all goods or services that buyers view as close substitutes. That means if the price of one product goes up, and in response consumers switch to buying a different product so that the price increase is not profitable, those two products may be in the same product market because consumers will substitute those products based on changes in relative prices. But if the price goes up and consumers do not switch to different products, then other products may not be in the product market for purposes of assessing a merger’s effect on competition.

In some investigations, the agencies are able to explore customers’ product preferences using actual prices and sales data. For instance, when the FTC challenged the merger of Staples and Office Depot, the court relied on pricing data to conclude that consumers preferred to shop at an office superstore to buy a wide variety of supplies, even though those same products could be purchased at a combination of different retailers. The product market in that case was the retail sale of office supplies by office supply superstores. In the majority of cases, however, the agency relies on other types of evidence, obtained primarily from customers and from business documents. For instance, evidence that customers highly value certain product attributes may limit their willingness to substitute other products in the event of a price increase. In the FTC’s review of a merger between two ready-mix concrete suppliers, customers believed that asphalt and other building materials were not good substitutes for ready-mix concrete, which is pliable when freshly mixed and has superior strength and permanence after it hardens. Based on this and other evidence, the product market was limited to ready-mix concrete.

A geographic market in an antitrust investigation is that area where customers would likely turn to

In the most general terms, a product market in an antitrust investigation consists of all goods or services that buyers view as close substitutes.



buy the goods or services in the product market. Competition may be limited to a small area because of the time or expense involved in buying a lower-cost product elsewhere. For instance, in a merger between two companies providing outpatient dialysis services, the FTC found that most patients were willing to travel no more than 30 miles or 30 minutes to receive kidney dialysis treatment. The FTC identified 35 local geographic markets in which to examine the effects of that merger. The FTC often examines local geographic markets when reviewing mergers in retail markets, such as supermarkets, pharmacies, or funeral homes, or in service markets, such as health care.

Shipping patterns are often a primary factor in determining the scope of a geographic market for intermediate or finished goods. In some industries, companies can ship products worldwide from a single manufacturing facility. For other products where service is an important element of competition or transportation costs are high compared with the value of the product, markets are more localized, perhaps a country or region of the country. For example, when examining the market for industrial gases, the FTC found that the cost of transporting liquid oxygen and liquid nitrogen limited customers to sources within 150 to 200 miles of their business.

AN FTC GUIDE TO

MERGERS

Competitive Effects

THE LAW BARS MERGERS WHEN THE EFFECT "may be substantially to lessen competition or to tend to create a monopoly." Three basic kinds of mergers may have this effect: horizontal mergers, which involve two competitors; vertical mergers, which involve firms in a buyer-seller relationship; and potential competition mergers, in which the buyer is likely to enter the market and become a potential competitor of the seller, or vice versa

Horizontal Mergers

There are two ways that a merger between competitors can lessen competition and harm consumers: (1) by creating or enhancing the ability of the remaining firms to act in a coordinated way on some competitive dimension (coordinated interaction), or (2) by permitting the merged firm to raise prices profitably on its own (unilateral effect). In either case, consumers may face higher prices, lower quality, reduced service, or fewer choices as a result of the merger.

Coordinated Interaction

A horizontal merger eliminates a competitor, and may change the competitive environment so that the remaining firms could or could more easily coordinate on price, output, capacity, or other dimension of competition. As a starting point, the agencies look to market concentration as a measure of the number of competitors and their relative size. Mergers occurring in industries with high shares in at least one market usually require additional analysis.

Market shares may be based on dollar sales, units sold, capacity, or other measures that reflect the competitive impact of each firm in the market. The overall level of concentration in a market is measured by the Herfindahl-Hirschman Index (HHI), which is the sum of the squares of the market shares of all participants. For instance, a market with four equal-sized firms has an HHI of 2500 ($25^2 + 25^2 + 25^2 + 25^2$). Markets with many sellers have low HHIs; markets with fewer players or those dominated by few large companies have HHIs approaching 10,000, a level indicating one firm with 100% market share. The larger the market shares of the merging firms, and the higher the market concentration after the merger, the more disposed are the agencies to require additional analysis into the likely effects of the proposed merger.

During a merger investigation, the agency seeks to identify those mergers that are likely either to increase the likelihood of coordination among firms in the relevant market when no coordination existed prior to the merger, or to increase the likelihood that any existing coordinated interaction among the remaining firms would be more successful, complete, or sustainable. Successful coordination typically requires competitors to: (1) reach an agreement that is profitable for each participant; (2) have the means to detect cheating (that is, deviations from the plan); and (3) have the ability to punish cheaters and reinstate the agreement. The coordination may take the form of an explicit agreement, such as agreeing to raise prices or reduce output, or the coordination may be achieved by subtle means–known as tacit coordination. Firms may prefer to cooperate tacitly rather than explicitly because tacit agreements are more difficult to detect, and some explicit agreements may be subject to criminal prosecution. The question is: does the merger create or enhance the ability of remaining firms to coordinate on some element of competition that matters to consumers?

THE LAW BARS MERGERS WHEN THE EFFECT "MAY BE SUBSTANTIALLY TO LESSEN COMPETITION OR TO TEND TO CREATE A MONOPOLY."

EXAMPLE: The FTC challenged a merger between the makers of premium rum. The maker of Malibu Rum, accounting for 8 percent of market sales, sought to buy the maker of Captain Morgan's rums, with a 33 percent market share. The leading premium rum supplier controlled 54 percent of sales. Post-merger, two firms would control about 95 percent of sales. The Commission challenged the merger, claiming that the combination would increase the likelihood that the two remaining firms could coordinate to raise prices. Although a small competitor, the buyer had imposed a significant competitive constraint on the two larger firms and would no longer play that role after the merger. To settle claims that the merger was illegal, the buyer agreed to divest its rum business.

Unilateral Effects

A merger may also create the opportunity for a unilateral anticompetitive effect. This type of harm is most obvious in the case of a merger to monopoly–when the merging firms are the only competitors in a market. But a merger may also allow a unilateral price increase in markets where the merging firms sell products that customers believe are particularly close substitutes. After the merger, the merged firm may be able to raise prices profitably without losing many sales. Such a price increase will be profitable for the merged firm if a sufficient portion of customers would switch between its products rather than switch to products of other firms, and other firms cannot reposition their products to entice customers away.

EXAMPLE: The FTC challenged the merger of two makers of ultrasonic non-destructive testing (NDT) equipment used for quality control and safety purposes in many industries. For many customers, the products of the merging firms were their first and second choice, and evidence showed that the two firms were frequently head-to-head rivals. The merger would have eliminated this beneficial competition on pricing and innovation. To settle the FTC's claim that the proposed merger was illegal, the companies agreed to divest the buyer's NDT business.

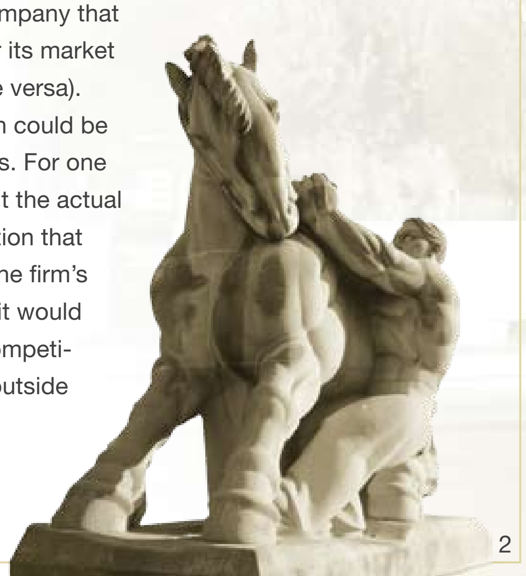
Vertical Mergers

Vertical mergers involve firms in a buyer-seller relationship–for example, a manufacturer merging with a supplier of an input product, or a manufacturer merging with a distributor of its finished products. Vertical mergers can generate significant cost savings and improve coordination of manufacturing or distribution. But some vertical mergers present competitive problems. For instance, a vertical merger can make it difficult for competitors to gain access to an important component product or to an important channel of distribution. This problem occurs when the merged firm gains the ability and incentive to limit its rivals' access to key inputs or outlets.

EXAMPLE: The FTC challenged the combination of an ethanol terminal operator and a gasoline refiner. Refiners need ethanol to create specially blended gasoline, and before the merger, an independent firm with no gasoline sales controlled access to the ethanol supply terminal. After the merger, the acquiring refiner could disadvantage its competitors in the gasoline market by restricting access to the ethanol terminal or raising the price of ethanol sold to them, which would reduce competition for sales of gasoline containing ethanol and raise prices to consumers. As part of a consent agreement, the FTC required the merged firm to create an informational firewall so there could be no preferential access or pricing for its refining affiliate.

Potential Competition Mergers

A potential competition merger involves one competitor buying a company that is planning to enter its market to compete (or vice versa). Such an acquisition could be harmful in two ways. For one thing, it can prevent the actual increased competition that would result from the firm's entry. For another, it would eliminate the procompetitive effect that an outside



firm can have on a market simply by being recognized as a possible entrant. What accounts for that effect? The firms already in the market may avoid raising prices to levels that would make the outside firm's entry more likely. Eliminating the potential entrant through a merger would remove the threat of entry and possibly lead to higher prices.

EXAMPLE: The FTC has challenged a number of mergers between pharmaceutical companies where one firm is already in the market with an-FDA approved drug and the second company has a drug that is in the approval process and could compete once it is approved. Mergers of this type eliminate a future competitor and further delay price competition for certain drugs.

Entry and Efficiencies

ENTRY

IF A MERGER CREATES opportunities for the merged firm to raise price, other firms may be enticed to enter the market after the merger. This entry—if it is timely, likely and sufficient—may counteract the harmful effects of the merger and make enforcement action unnecessary. Under certain conditions, even the possibility of new firms entering the market will keep prices in check.

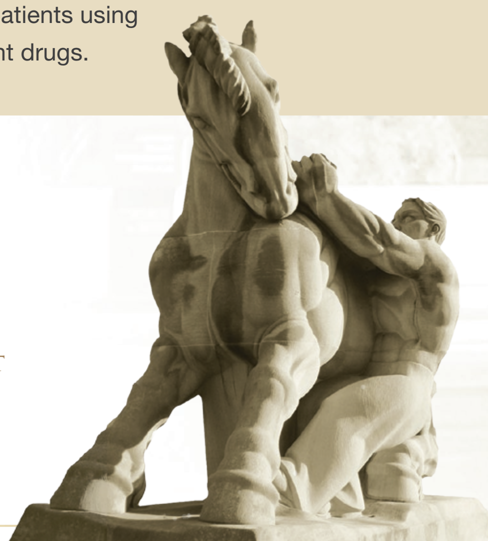
On the other hand, many factors can impede entry: licensing restrictions, zoning regulations, patent rights, inadequate supply sources, and cost of capital, among others. Entry may also take a long time, and consumers would be paying higher prices all that time. And, finally, the new firm may fail to attract customers away from existing firms, particularly in markets where existing firms have a proven track record. Assessing entry conditions calls for intensive fact-finding and is unique to each industry.

EXAMPLE: The FTC challenged a merger between two leading U.S. makers of field-erected industrial and water storage tanks. The Commission found that although new firms had attempted to compete for customers, they lacked the reputation and experience that most customers demand and were not capable of replacing the competition lost due to the merger. The Commission ordered the company to create two separate, stand-alone divisions that would restore competition to the market.

EFFICIENCIES

MANY MERGERS PRODUCE SAVINGS by allowing the merged firms to reduce costs, eliminate duplicate functions, or achieve scale economies. Firms will often pass merger-specific benefits on to consumers in the form of lower prices, better products, or more choices. The agencies are unlikely to challenge mergers when the efficiencies of the merger prevent any potential harm that might otherwise arise from the proposed merger. Theoretical cost savings would not be enough, however; they must be demonstrated. And the efficiencies must involve a genuine increase in productivity. It is not enough for cost savings to result merely from a reduction in output, or from the assertion of newfound market power against suppliers. The price reductions should result from real efficiencies in the merger and not from reducing output or service.

EXAMPLE: The FTC reviewed a proposed merger between two pharmaceutical companies that sold competing drugs used with solid organ transplants to reduce the patient's risk of rejection. The Commission found that the merger would reduce competition in the market for these life-saving drugs, and tailored a remedy to preserve competition in that market. The companies then merged to realize potential benefits in the related field of oncology treatment, where use of certain diagnostic tests could lead to more patients using these important drugs.



ENTRY—IF IT IS TIMELY, LIKELY AND SUFFICIENT—MAY COUNTERACT THE HARMFUL EFFECTS OF THE MERGER AND MAKE ENFORCEMENT ACTION UNNECESSARY.