[1] Federal Trade Commission Act, 15 U.S.C. § 45.

[2] *See*

[4] *FTC Closes Western States Gasoline Investigation*, FTC Press Release (May 7, 2001), at http://www.ftc.gov/opa/2001/05/westerngas.htm.

[5] *FTC to Hold Public Conference/Opportunity for Comment on U.S. Gasoline Industry*, FTC Press Release (July 12, 2001), at http://www.ftc.gov/opa/2001/07/gasconf.htm; *FTC to Hold Second Public Conference on the U.S. Oil and Gasoline Industry in May 2002*, FTC Press Release (Dec. 21, 2001), at http://www.ftc.gov/opa/2001/12/gasconf.htm.

[6] FTC Staff comments, *Study of Unique Gasoline Fuel Blends, Effects on Fuel Supply and Distribution and Potential Improvements*, EPA 420-P-01-004, Public Docket No. A-2001-20 (Jan. 30, 2002), at http://www.ftc.gov/be/v020004.pdf.

[7] *See* Letter from Susan Creighton, Director, FTC Bureau of Competition, et al., to Demetrius Newton, Speaker Pro Tempore of the Alabama House of Representatives (Jan. 29, 2004), at http://www.ftc.gov/be/v040005.htm; Letter from Susan Creighton, Director, FTC Bureau of Competition, et al., to Wisconsin State Rep. Shirley Krug (Oct. 15, 2003), at http://www.ftc.gov/be/v030015.htm; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, et al., to Eliot Spitzer, Attorney General of New York (July 24, 2003), at http://www.ftc.gov/be/nymfmpa.pdf; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, et al., to Roy Cooper, Attorney General of North Carolina (May 19, 2003), at http://www.ftc.gov/os/2003/05/ncclattorneygeneralcooper.pdf; *Competition and the Effects of Price Controls in Hawaii's Gasoline Market: Before the State of Hawaii, J. Hearing House Comm. On Energy and Environmental Protection et al.* (Jan. 28, 2003) (testimony of Jerry Ellig, Deputy Director, FTC Office of Policy Planning), at http://www.ftc.gov/be/v030005.htm; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, et al., to Gov. George E. Pataki of New York (Aug. 8, 2002), at http://www.ftc.gov/be/v020019.pdf; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, and R. Ted Cruz to Hon. Robert F. McDonnell, Commonwealth of Virginia House of Delegates (Feb. 15, 2002), at http://www.ftc.gov/be/V020011.htm. *See also* Letter from Ronald B. Rowe, Director for Litigation, FTC Bureau of Competition, to Hon. David Knowles, California State Assembly (May 5, 1992); Prepared Statement of Claude C. Wild III, Director, FTC Denver Regional Office, before the State, Veterans, and Military Affairs Committee of the Colorado State Senate (Apr. 22, 1992); Letter from Claude C. Wild III, Director, FTC Denver Regional Office, to Hon. Bill Morris, Kansas State Senate (Feb. 26, 1992); Letter from Claude C. Wild III, Director, FTC Denver Regional Office, to David Buhler, Executive Director, Utah Department of Commerce (Jan. 29, 1992); Letter from Thomas B. Carter, Director, FTC Dallas Regional Office, to Hon. W.D. Moore, Jr., Arkansas State Senate (Mar. 22, 1991); Letter from Jeffrey I. Zuckerman, Director, FTC Bureau of

> "[C]ost" means product cost and actual freight or transportation costs plus applicable taxes and fees pursuant to federal, state and local law or if such costs are unavailable then "cost" means the average of the three lowest terminal prices posted by a supplier on the day at the terminal from which the most recent supply of motor fuel delivered to the retail location was acquired as published by a nationally recognized petroleum price reporting service and actual freight offered from a common carrier for hire designated for the terminal from which the most recent supply of motor fuel delivered to the retail location, plus applicable taxes and fees pursuant to federal, state and local law.[9]

If the Division of Weights and Measures of the Department of Agriculture "receives a complaint and has reason to believe that a marketer or retailer has violated the provisions of this act," the Bill would have the Division demand that the offending marketer or retailer "raise [its] price . . . to comply with the provisions of this act."[10] Within 10 business days following this demand, the Division "shall investigate and determine whether the allegations contained in the complaint are still true."[11] If the allegations are "still true," the marketer or retailer "shall provide the [D]ivision with all records and documentation requested in order . . . to determine if a violation of the act has occurred."[12] If the Division determines that a violation has occurred, it will provide the Attorney General "with all records, documentation and findings of the [D]ivision related to such violation."[13]

In turn, the Attorney General may seek a declaratory judgment, injunctive relief, monetary penalties, and "reasonable expenses and investigation fees" incurred by both the Division and the Attorney General.[14] On the first violation, "the [A]ttorney [G]eneral shall send to the violator by certified mail, return receipt requested, an order that the violator cease and desist from the violation within 24 hours of receipt of such order."[15] A second violation "shall render the violator liable for the payment of a civil penalty in a sum of $1,000 for each day the violation occurs."[16]

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[9] *Id.* at § 1(c).

[10] *Id*. at § 1(d).

[11] *Id*.

[12] *Id.* If a retailer or marketer fails to comply with the request for documents, the Division "shall take [its pumps] out of service." *Id*.

[13] *Id*.

[14] *Id*. at § 1(e)(1)-(4).

[15] *Id*. at § 1(f). It appears that a violation is defined either with respect to a specific transaction with a specific customer or, if a specific transaction cannot be identified, with respect to each day. *Id.*

[16] *Id*.

[17] *Id*.

injunctive relief to prevent current and future violations, and to "recover court costs and reasonable attorney fees."[18]

We believe that, if followed by retailers and marketers, the Bill likely would restrict competition and may lead to higher prices for consumers. Unlike federal antitrust law, the Bill would have the effect of protecting individual retailers and marketers of motor fuel from lower-priced competitors. In doing so, the Bill likely would harm consumers by discouraging procompetitive price-cutting. We also believe that the Bill is unnecessary, both because scholarly studies and court decisions indicate that anticompetitive below-cost pricing happens infrequently, and because the federal antitrust laws already prohibit anticompetitive below-cost pricing.

I. Legal and scholarly analysis of predatory pricing

A. Federal antitrust law condemns below-cost pricing that harms competition

i. Antitrust law protects consumers, not competitors

[18] *Id.* at § 1(g)(1)-(3).

[19] Predatory pricing claims generally are brought either as violations of Sherman Act § 2 (15 U.S.C. § 2) or as "primary-line" violations of the Robinson-Patman Act (15 U.S.C. § 13(a)).

[20] One notable example is *United States v. Microsoft*, 253 F.3d 34 (D.C. Cir.), *cert. denied*, 534 U.S. 952 (2001).

[21] 15 U.S.C. § 15.

[22] Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 488 (1977) (quoting Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962)).

matter, low prices are "a boon to consumers."[23] As the Supreme Court observed in *Spectrum Sports, Inc. v. McQuillan*:

> The purpose of the [Sherman] Act is not to protect businesses from the working of the market; it is to protect the public from the failure of the market. The law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself.[24]

Thus, unless conduct threatens to lead to lower output, higher prices, lower quality, or less variety, it is of no concern to the antitrust laws.[25]

ii. Only below-cost prices can be predatory

The Supreme Court has directly addressed low-pricing strategies. In *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, the leading case in this area, the Court expressly held that a defendant does not violate the federal antitrust laws by cutting prices merely because the low prices decrease a competitor's profits. "Low prices benefit consumers regardless of how those prices are set. . . . To hold that the antitrust laws protect competitors from the loss of profits due to such price competition would, in effect, render illegal any decision by a firm to cut prices in order to increase market share."[26] To be unlawful, the low prices must, at a minimum, be predatory. "[S]o long as they are above predatory levels, [low prices] do not threaten competition . . . . We have adhered to this principle regardless of the type of antitrust claim involved."[27]

The Court has defined predatory pricing, in turn, as "pricing below an appropriate measure of [the defendant's] cost for the purpose of eliminating competitors in the short run and reducing competition in the long run."[28] Although the Court has not stated what the appropriate measure of cost should be, prominent antitrust scholars and several federal circuit courts have concluded that the price-cutter's marginal costs, or a close proxy such as average variable costs, should be the yardstick.[29]

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[23] Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224 (1993). *See also* Atlantic Richfield Co. v. USA Petroleum Co., 495 U.S. 328 (1990); Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574 (1986). After *Brooke Group*, it is clear that a plaintiff must show injury to competition in a primary-line case under the Robinson-Patman Act. *See Brooke Group*, 509 U.S. at 222-23.

[24] 506 U.S. 447, 458 (1993).

[25] *Cf. Brooke Group*, 509 U.S. at 224 ("That below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured: It is axiomatic that the antitrust laws were passed for the protection of *competition*, not *competitors*.") (internal quotations and citations omitted) (emphasis in original).

[26] *Id.* at 223 (internal quotations and citations omitted).

[27] *Id.* (quoting *Atlantic Richfield*, 495 U.S. at 340).

[28] Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 117 (1986).

[29] Marginal costs are those costs associated with producing an additional unit of output. *See* United States v. AMR Corp., 335 F.3d 1109, 1116 (10th Cir. 2003) (marginal cost and average variable cost are relevant in determining whether prices are predatory); Kelco Disposal, Inc. v. Browning-Ferris Indus., 845 F.2d 404, 407 (2d Cir. 1988), *aff'd on other grounds*, 492 U.S. 257 (1989) (finding that "[p]rices that are below reasonably anticipated marginal cost, and its surrogate, reasonably anticipated average variable cost . . . are presumed predatory"); MCI

Communications Corp. v. AT&T, 708 F.2d 1081, 1122-23 (7th Cir. 1983) (holding that no predatory intent can be presumed from prices at or above long-run incremental cost); Int'l Air Indus. v. American Excelsior Co., 517 F.2d 714, 724 (5th Cir. 1975) (holding that plaintiff must show that "either (1) a competitor is charging a price below his average variable cost . . . or (2) the competitor is charging a price below its short-run, profit-maximizing price and barriers to entry are great enough to enable the discriminator to reap the benefits of predation before new entry is possible"); P. AREEDA & H. HOVENKAMP, ANTITRUST LAW ¶ 724; P. Areeda & D. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975). In *Brooke Group*, the parties both agreed that average variable cost should be the appropriate measure.

[34] F. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263, 313-14 (1981) (citations omitted).

[35] DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 342 (3d ed. 2000).

[36] *See* J. CHURCH &

[41] 124 S. Ct. 872, 882 (2004) (quoting *Matsushita*, 475 U.S. at 594).

[42] USDOE, DEREGULATED GASOLINE MARKETING: CONSEQUENCES FOR COMPETITION, COMPETITORS, AND CONSUMERS (Mar. 1984); DR. JAMES B. DELANEY & DR. ROBERT N. FENILI, U.S. DEP'T OF ENERGY, FINAL REPORT: THE STATE OF COMPETITION IN GASOLINE MARKETING (Jan. 1981).

[43] STAFF OF ARIZ. JOINT LEGISLATIVE STUDY COMMITTEE, FINAL REPORT ON PETROLEUM PRICING AND MARKETING PRACTICES AND PRODC( )]7C( )]TJ

anticompetitive below-cost pricing, and it warned that a "sales below cost" law could harm consumers:

> Unfortunately, such laws may serve to deter, rather than enhance, competition. The reason for such deterrence is that it may open up firms who engage in low, but non-predatory, pricing to litigation. Seeing the threat of litigation, such firms may change strategy and charge consumers higher prices.[45]

Of course, competitors often will complain that the competition charges prices that are "too low." Competitors have an incentive to do so if they believe such complaints will lead to legislation that will allow them to charge higher prices. To date, however, no systematic study has produced evidence that predatory pricing is a significant problem in retail gasoline markets.

II. The Bill likely would restrict competition and harm consumers

To the extent that motor fuel sellers would adjust their behavior to comply with the proposed Bill, it would most likely have a detrimental effect on competition and consumer welfare. By allowing liability to be predicated on a single act of below-cost pricing, regardless of any effect on competition, the Bill would shield vendors of motor fuel from competition by deterring competitive price-cutting. This result would harm consumers. Additionally, the Bill's definition of "cost" does not reflect the true marginal cost of motor fuel in a vendor's inventory. Finally, we believe that the Bill is unnecessary, both because scholarly studies and court decisions indicate that anticompetitive below-cost pricing happens infrequently, and because the federal antitrust laws already prohibit anticompetitive instances of below-cost pricing.

A. The Bill likely would deter price-cutting and thus harm competition

A marketer or retailer found to have violated the Bill would face penalties that include a fine of up to $10,000 per violation, as well as private litigation that could result in injunctive relief and legal fees. Given the possibility of mistakenly being found liable and facing these substantial penalties, the Bill likely would deter vendors from cutting prices. Indeed, the Supreme Court has cautioned that because of the risk of false condemnation, rules that too easily condemn behavior consistent with competition (*e.g.*, price-cutting), will have the effect of deterring firms from competing.[46] Thus, unlike federal antitrust law, which protects competition, the Bill likely would lead marketers and retailers to compete less vigorously, thus having the effect of protecting marketers and retailers of motor fuel *from* competition.

The Bill, moreover, would condemn below-cost sales, even if those sales result in lower prices for consumers, and even where there is no danger that the price-cutter subsequently will

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[45] STAFF OF BUDGET AND FINANCE COMM., COMMONWEALTH OF PA. LEGISLATURE , FACTORS AFFECTING MOTOR FUEL PRICES AND THE COMPETITIVENESS OF PA.'S MOTOR FUELS MARKET, A REPORT IN RESPONSE TO H.R. 451, at 35 (Oct. 2000).

[46] *See* notes 40 & 41, *supra*, and accompanying text.

[47] As the staff of the FTC has noted in prior comments concerning below-cost sales laws, provisions that allow a violation to be premised on harm to a single competitor (as opposed to harm to competition as a whole) are likely to have adverse effects on competition and consumer welfare. *See* Letter to Demetrius Newton, *supra* note 7.

B. The Bill's definition of "cost" does not reflect the true marginal cost of motor fuel in a vendor's inventory

By focusing on historic cost rather than replacement cost, the Bill ignores a vendor's opportunity cost, and thus does not accurately reflect the true marginal cost of motor fuel in inventory.[50] For instance, a marketer or retailer that lowers its prices in response to a decline in wholesale motor fuel prices would be subject to liability if its new lower prices were below its actual acquisition cost or "the average of the three lowest terminal prices posted by a supplier" on the day the vendor purchased its most recent supply of motor fuel.[51] Further, the use of an

[50]Opportunity cost is "the value of the best forgone use of the resources employed in that action." CARLTON & PERLOFF, *supra* note 35, at 33.

[51]*See* House Bill No. 2330 at § 1(c).

Respectfully submitted,

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