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DIRECTORATE FOR FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS
COMMITTEE ON COMPETITION LAW AND POLICY

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ROUNDTABLE ON PRICE TRANSPARENCY

-- Note by the United States --

This note is submitted by the Delegation of the United States to the Committee on Competition Law and Policy FOR DISCUSSION at its forthcoming meeting to be held on 31 May-1 June 2001.

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of price information would likely raise concern, sharing of other information, e.g., information on direct input purchases, might also raise concerns; 4) the speed of the information sharing;[4] 5) whether the information is already available to the participants. These five factors can be used to assess whether a B2B is likely to facilitate collusion among the participants.

9. The first B2B venture reviewed by the Commission, named Covisint, was in the automotive industry supply chain. Covisint would provide assistance in product design, supply chain management, and procurement functions performed by auto manufacturers and their direct and indirect suppliers. The venture was formed by five competing automotive manufacturers and two information technology firms.[5] After analyzing the venture, the Commission closed the investigation in September 2000 but issued a letter to the parties stating:

> Because Covisint is in the early stages of its development and has not yet adopted bylaws, operating rules, or terms for participant access, because it is not yet operational, and in particular because it represents such a large share of the automobile market, we cannot say that

representations about the quality of dental services (such as "special treatment for nervous patients").[9] The case eventually went to the U.S. Supreme Court on the issue of the proper application of the rule of reason; the Court remanded the case to the Ninth Circuit Court of Appeals. The Court of Appeals ultimately ruled against the Commission, finding, from the existing record, that procompetitive benefits of the rules outweighed their anticompetitive harm. In 2001, the Commission decided, for various reasons, not to seek further review in the Supreme Court and dismissed the complaint.[10]

13. The Commission also has brought a number of cases against state boards that maintained various rules against truthful, non-deceptive advertisements about fees and services. The most recent such complaint was against the Texas Board of Chiropractic Examiners in 1992. The Board was the sole licensing authority under Texas law for the approximately 1,600 licensed chiropractors in Texas. The complaint charged the Board with preventing consumers from obtaining information about the chiropractors' fees, services, and products, thereby depriving consumers of the benefits of vigorous competition among chiropractors.[11] The Board agreed to a consent order against the practices.[12] The Commission issued similar complaints against the Massachusetts Board of Registration in Optometry[13] and the Wyoming State Board of Chiropractic Examiners.[14]

Boycotts of organizations publicizing low prices

14. The Commission has brought several cases against trade associations for boycotting organizations that were publishing low prices. In these cases, the Commission has alleged that the restricted advertising and resultant decrease in price transparency were harmful to consumers. In 1995, the Commission issued a complaint against the Santa Clara County Motor Car Dealers Association. The Association had approximately 47 members, constituting about 50 percent of the new automobile and truck dealers in Santa Clara County. In May 1994, the San Jose Mercury News published an article telling consumers how to analyze new car factory invoices so that they could be better negotiators when buying cars. The complaint alleges that after the article was published, Association members agreed to cancel and withhold their advertising from the paper. A consent agreement was reached prohibiting the Association from carrying out, participating in, inducing, or assisting any boycott.[15]

15. In 1998, the Commission issued a complaint against Fair Allocation System, Incorporated (FAS). FAS was an organization of twenty-five automobile dealerships from five Northwest states that was formed to address dealer concerns about an automobile dealership, Dave Smith Motors, which was attracting customers from around the Northwest. Dave Smith Motors offered "no-haggle" pricing, a system that offered new automobiles to all customers at firm, but low, predetermined prices. In addition, Smith was among the first dealers to market automobiles on the Internet. According to the complaint, because of their concerns, the members of FAS collectively threatened to boycott Chrysler to force it to limit sales to car dealers that sell cars at low prices and via a new and innovative channel–the Internet.[16] A consent agreement was reached with FAS prohibiting the alleged practices.[17]

16. In 1998, the Commission accepted a consent agreement from Fastline Publications, Inc. and Mid-America Equipment Retailers Association. Fastline publishes picture buying guides for new and used farm equipment which are mailed free to farmers and ranchers in over 40 states. Mid-America is a trade association whose membership comprises about 90 percent of the farm equipment dealers in Kentucky and Indiana. In early 1991, several Kentucky farm equipment dealers complained to Fastline about dealers advertising prices, including discount prices, for new farm equipment in the Fastline Kentucky Farm Edition. In protest, several dealers withheld their advertising from this guide until Fastline agreed not to publish advertisements that included prices for new farm equipment. In early 1992, Fastline was invited to the annual meeting of the Kentucky Retailers Association, during which several retailers expressed their dislike for renewed price advertising and threatened to withdraw or otherwise cancel their advertisements

20. In 1994, the Commission issued a complaint against the International Association of Conference Interpreters (known by its French acronym, AIIC). AIIC is a voluntary professional association of interpreters with 2,500 members from 68 countries who perform interpretation services at multi-lingual conferences or other high-level meetings. The complaint alleges that AIIC's fee schedules, work rules, and other restrictions violated federal antitrust laws. Administrative Law Judge Timony upheld the charges in a July 1996 decision.[25] Judge Timony noted that members were paid AIIC's minimum daily rate 90 percent of the time from 1988 to 1991. Judge Timony found that the effect of many of the rules was to make price undercutting easier to detect. For example, rules requiring that travel expenses and per diem payments be stated separately on contracts for interpretation would make cheating on them and on the minimum daily price easier to see, as would the requirement that fees be paid on an indivisible daily basis because it makes rates more standardized and comparable.[26] AIIC appealed Judge Timony's decision to the full Commission which upheld most of these charges in 1997 but dismissed certain charges against Association rules governing work-day length, interpreter team size, and other non-price-related factors.[27]

21. The Commission'

24. Recently, however, the Commission required an MFN clause as part of the AOL Time Warner consent agreement. AOL is the nation's largest internet service provider (ISP) and Time Warner controls a cable television system servicing about 20 percent of U.S. cable households. The consent agreement

Bid depositories

29. A bid depository is a mechanism whereby subcontractors all submit bids to a depository from which general contractors then select subcontractors when preparing a bid for a prime contract. Bid depositories reduce search costs for a general contractor and increase price transparency since each subcontractor is quoting a single price for the project. However, bid depositories also can serve to reduce competition among subcontractors. In 1984, the Commission issued a complaint against a bid depository, Electrical Bid Registration Service of Memphis Inc., set up by electrical subcontractors. According to the complaint, the registry had a deadline for electrical subcontractors' registering of bids and prohibited electrical subcontractors from offering a lower price after the deadline both before and after the award of the prime contract. The registry then required general contractors who accepted the delivery of registered bids to agree that they would not award an electrical subcontract to any firm that did not have a bid registered with the Registry, and that all such awards would be at the price contained in the registered bid. An administrative law judge issued an order banning these practices and the Commission accepted the decision on appeal.[43]

Price discovery, and reference prices

30. In industries subject to much price volatility, contracts often refer to some readily observable benchmark price, e.g., a NYMEX futures contract price or a posted gasoline rack price. If these reference prices become subject to manipulation, their transparency is reduced and the markets relying upon them function less efficiently. In 2000, the Commission issued a complaint against two merging oil companies: BP Amoco and the Atlantic Richfield Company (ARCO). According to the complaint, the proposed merger would concentrate control of over 43% of storage capacity, 49% of pipeline delivery capacity, and 95% of the trading services in Cushing, Oklahoma. Since Cushing is the specified delivery point for the NYMEX crude oil futures contract, a firm that controls such substantial assets in Cushing would be able to manipulate the NYMEX crude oil futures market and hence to manipulate this important reference price. This threat of manipulation would have ripple effects throughout the oil industry. The Commission's concern was remedied by a divestiture of assets in Cushing.[44]

Regulatory Evasion

31. Regulators rely upon the transparency of prices to evaluate the prudence of input purchases. When prices are highly volatile and there are no reliable benchmark prices, regulators must rely upon the efforts of the regulated company to ensure that costs are prudently incurred. In 2001, the Commission issued a complaint about a joint venture called Entergy-Koch, LP between Entergy Corporation and Koch Industries, Inc. Entergy is engaged in the generation, transmission, and distribution of electricity, and Koch markets natural gas, natural gas transportation, chemicals, petroleum products, minerals, and financial services. According to the complaint, Entergy is permitted, subject to review, to recover 100 percent of the cost of natural gas transportation purchased for its natural gas and electric utilities by passing on this cost directly to ratepayers. The complaint alleges that once Entergy shares in the profits of Koch's Gulf South natural gas pipeline, it will become willing to pay inflated gas costs to its subsidiary, thereby evading regulation. The consent agreement increased the transparency of the market by requiring Entergy to post on its website every request for proposal (RFP) for gas purchases.[45]

Department of Justice: Illustrative Price Transparency Cases [46]

effect.[50] If the terms of agreement are complex (e.g., specifying prices in numerous markets) but there is a common desire to reach agreement, cheap talk can help firms reach a collusive equilibrium.

37. Cheap talk figured prominently in U.S. v. ATP.[51] ATP, a joint venture owned by the major airlines, collects fare information from the airlines, and distributes it daily to all the airlines and to the major computer reservation systems (CRSs) that serve travel agents. This arrangement is an efficient instrument for cheap talk:

> Airlines are charged a fee for each change, so that changes are not absolutely costless, but the fees for any change are very small relative to the revenues involved. Since ATP updates all CRSs

***Remedies in* U.S. v. ATP**

40. Complex negotiations like this satisfy the courts' test for an illegal agreement to fix prices. The Justice Department obtained consent decrees from all airlines and ATP. The basic provisions in the

> It is, I think, useful to look at the proposed tuition and salary levels in the light of our own tentative decisions.[60]
>
> When I told them that we were considering salary heights of 8%-8½% and tuition increases not far off from that number, there was an audible gasp. The other Presidents felt that it was not possible to increase tuition at a rate that far above the CPI and that some of the pressure on faculty salaries was self-induced to serve the faculty's interest. . . . In view of the above information, we will need to rethink our proposed salary and tuition scheduled increases and to do so rather promptly.[61]

45. Might it be that the only effect of sharing prospective prices is to make prices more uniform and transparent, but not any higher on average? That seems implausible. Our normal, instinctive assumption is that eliminating price competition raises price. The purpose of this discussion is to identify several strands of economic literature that support this assumption. In our view, sharing prospective price does help firms achieve a collusive price level.[62]

Swift Detection Fosters Collusion

46. Illegal cartels cannot enforce their agreements in court. Consequently, the agreements must be self-enforcing: each cartel member, acting in its independent self-interest, must choose to abide by the terms of the agreement. Cheating is deterred by the fear of detection and swift retaliation, since prospective cheaters have to trade off the short-term gains from cheating against the long-term loss of cartel profits:

> This leads us to one of the most important conclusions with genuine policy implications that

[67] Additional support comes from "the many experiments that show that collusion is likely to be sustained in long but finite games."[68]

50. To avoid relying too heavily on relationships, longstanding cartels may develop detailed rules and procedures to prevent misunderstanding, resolve disputes, and ensure rapid detection.[69] In the Ivy

57. These complex arrangements -- the Ivy Methodology, the spring meetings to negotiate uniform offers to individual students, the moral exhortations to nurture compliance from cartel members and even non-cartel members -- illustrate the role that price transparency plays in a complex, longstanding cartel. It is one of an array of strategies that economize on trust, so that cartel members don't act selfishly in their own self-interest. Complex conspiracies impose great demands for price transparency; and legal constraints on price transparency make it more difficult to sustain complex conspiracies.

NOTES

[1] See James L. Langenfeld and Louis Silvia "The Federal Trade Commission's Horizontal Restraint Cases: An Economic Perspective," *Antitrust Law Journal* 61:3 (1993) pp. 653-697, for a complete survey of earlier cases involving horizontal restraints.

[2] Materials from the workshop are available at www.ftc.gov/bc/b2b/index.htm.

[3] "Entering the 21st Century: Competition Policy in the World of B2B Electronic Marketplaces," October 2000.

[4] An additional consideration is whether the shared information is received by competitors before it is received by buyers.

[5]

[20] *Concerning the Market for Prerecorded Music in the United States*, FTC File No. 971 0070 (C-3971 to C-3975) (May 10, 2000) (Analysis to Aid Public Comment).

[21]

[34] The four manufacturers were Ethyl Corporation, E.I. du Pont de Nemours, and Company, PPG Industrices, Inc., and Nalco Chemical Company.

[35] Two other aspects of this case, advance price notices and uniform delivered pricing, also raise important price transparency issues. See Hay (1989) and Vita (2001), *supra* n. 33.

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[51] *United States v. Airline Tariff Publishing*, Civil Action No. 92-2854, (D.D.C. filed Dec. 21, 1992).

[52] William Gillespie, "Cheap Talk, Price Announcement, and Collusive Coordination," EAG 95-3, Discussion Paper, Economic Analysis Group, Antitrust Division, U.S. Department of Justice (9/25/95). See also Severin Borenstein, "Rapid Price Communication and coordination: The Airline Tariff Publishing Case (1994)," chapter 13 in John E. Kwoka, Jr. and Lawrence J. White (eds.), *The Antitrust Revolution: Economics, Competition, and Policy*, 3rd ed. (1999).

[53] U.S. v. ATP, United States' Response to Public Comments, April 8, 1993, p. 17, quoted in Gillespie, *op. cit.*, p. 11.

[54] Gillespie, *op. cit.*, p. 14.

[55] "For example, future fares could be tested out on a few seats. The fares could go into effect immediately, but be limited to only a few seats. The fares would be extended to all seats only if rivals signal that they will go along with such a general fare increase by matching their rival's fare on the few seat basket. Because this alternative is so good a substitute (from a cooperative pricing perspective) for preannouncement, a ban on preannouncement would only be effective if this alternative were also banned. however, a ban on this alternative may be very costly, because fares limited to a few seats are often efficient and the regulatory costs to enforce the ban may be large. Furthermore, there may be other alternatives, which allow the initial equilibrium to be reestablished." Carlton *et al., op. cit.*, 439.

[56] Gillespie, *op. cit.*, p. 16.

[57] The major focus of the Ivy League investigation was on collusive arrangements for the discounted price (tuition minus financial aid). It resulted in consent decrees from the eight Ivy League Universities (U.S. v. Brown University, *et al.*. cum4.1soni1 Tf 637.2669TD 0.0025 Tcc 0.115er7