Why the FTC's McWane Opinions Raise More Questions Than They Answer

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The Federal Trade Commission is meant to be, and is, an expert body on antitrust laws. So, when a case like *McWane*—that raises both collusion and exclusion issues—is in front of the FTC, it seems reasonable to expect to receive guidance that is more helpful than we might get from a jury or generalist judge on two questions important to those of us who counsel clients daily. Unfortunately, the two opinions in this matter raise more questions than they answer.

McWane, Inc. is the only U.S. producer of ductile iron pipe fittings and one of a small number of sellers of the product in the country. McWane was accused by the FTC both of excluding its few rivals from the domestically-produced part of the market through loyalty rebates and colluding with them in the overall market to raise prices. An Administrative Law Judge (ALJ) found illegal exclusion but not collusion. In a February 6, 2014, decision, the four FTC commissioners split 2-2 on the issue of collusion, allowing the ALJ decision to stand and the charges dismissed. On the exclusion charges, Chairwoman Ramirez and Commissioners Brill and Ohlhausen found sufficient evidence to support one of the ALJ's findings of anticompetitive conduct, while Commissioner Wright dissented.

While media reports have focused on inside the Beltway issues like the party-line split and rare loss by FTC staff, I want to focus instead on the substance of the case and three missed opportunities to help antitrust counselors advise their clients.

While the exclusion issue is more interesting to the antitrust thinkers, it is the missed opportunity to provide guidance on the collusion issue, faced by counselors every day, that might be more unfortunate. FTC complaint counsel focused on three categories of evidence that allegedly showed an agreement. Because of the even split among the commissioners, we will never get an opinion from these experts that might have acknowledged some real-world, competition-neutral reasons for such price chatter.

First, counsel showed the large number of unexplained phone calls and other direct contacts among McWane and its two main competitors. Counsel's theory seemed to be Adam Smith's quote: "People of the same trade seldom meet together … but the conversation ends in … some contrivance to raise prices." Yet, the reality is that competitors can use such meetings for many other purposes, like sizing up the competition, making contacts for the next job switch and even, as Smith recognized, "merriment and diversion" with someone with whom you at least have an industry in common.

Second, complaint counsel pointed to alleged indirect communication with the competitors through each company's periodic messages to customers about list prices, normal discounts off those prices and one-off discounts ("project pricing"). The theory was that the competitors read each other's customer messages and used this means to try to arrange an elimination of project pricing. Part of McWane's defense was that its messages to customers on this topic were just a "head fake." Complaint counsel—and, at oral argument, Commissioner Brill—seemed skeptical of such an elaborate ruse. Yet, the reality could be that McWane aimed these customer messages at, strangely enough, customers, in hopes the deke would discourage them from expecting robust project pricing discounts.

Finally, complaint counsel pointed to the numerous internal documents at all the competitors that complained of discounts at the others, often by describing the continued use of "project pricing" as cheating. But the reality is that such internal documents blaming last month's sales shortfall on a competitor's aggressive pricing can be found in any company's emails, especially in industries with a limited number of competitors.

Most importantly, the ALJ found that all these factors were meant to explain why the competitors' common actions on pricing could be explained by an agreement—except the ALJ found that those actions were not common, that net pricing to distributors or indirectly to contractors was "all over the map" and that project pricing continued, despite the documents.

Second, both opinions missed the opportunity to explain when loyalty rebate programs should be considered potentially problematic exclusive dealing arrangements (although Commissioner Wright has stated elsewhere his preference for using exclusive dealing theories to evaluate loyalty pricing programs). The key facts seem to be the extensive internal and external discussion by McWane that the program is meant to be an exclusive dealing program—and that exact perception of the program by several distributors. The order accompanying the opinion, however, forbids McWane from offering "retroactive incentives" to customers. Such programs offer rebates on all units if a certain threshold is passed, as compared to providing the rebate just on the units purchased above the threshold. While there is literature that describes the greater anticompetitive risk of that variety of loyalty pricing, nowhere in either opinion is such a factor discussed. Will all retroactive incentives now raise red flags at the FTC? Only under certain circumstances? If so, only the circumstances identical to those in McWane?

Finally, when the FTC issued two dueling opinions, it missed the opportunity to provide clear guidance for when exclusive dealing arrangements are illegal. Commissioner Wright's dissent, at least, articulates the theory and evidence he would have found sufficient to support the allegation of competitive harm from exclusive dealing. He cites both to recent scholarship and venerable precedent like *Tampa Electric* and the FTC's own *Beltone* decision. His dissent finds the evidence for that plausible claim to be woefully lacking. The majority opinion's support comes from an almost completely different set of cases and scholarly articles, including at least 10 cites alone to the controversial 2-1 opinion by the 3rd Circuit in *ZF Meritor v. Eaton.* The majority opinion finds competitive harm because McWane's program blocked its domestic competitor from "accessing a substantial share of distributors" and "significantly impaired" access to that main channel of distribution, thereby preventing effective competition. Unfortunately, "substantial" and "significant" are not fully explained. The opinion references two distributors who chose to buy only from McWane and whose combined share of distribution is just over 50 percent; however, it does not explain if that figure is an important threshold under all circumstances. The figure does show up, again unexplained, in the accompanying order that would prevent conditioning a price based on a customer agreement to purchase 50 percent or more of its needs from McWane. When the confusion over meaningful foreclosure is combined with Commissioner Wright's numerous attacks on the foreclosure measurement methods, the antitrust counselor receives no helpful guidance that would clarify the advice to clients on these common pricing and distribution schemes.

The FTC does much to explain the intricacies and benefits of antitrust law through speeches by commissioners, testimony to state legislatures and consultations with foreign enforcers. McWane offered opportunities for this expert body to provide further guidance to U.S. antitrust counselors and their business clients on bread and butter antitrust issues, such as sufficient evidence of collusion and easily articulable theories of harm from loyalty pricing. Unfortunately, those opportunities were missed.