ABA SECTION OF ANTITRUST LAW
COMMENTS ON FEDERAL TRADE COMMISSION
"MARKET MANIPULATION" RULEMAKING
JUNE 23, 2008

The Section of Antitrust Law (Section) of the American Bar Association (ABA) appreciates the opportunity to present its views in response to the Federal Trade Commission's (FTC's) Advance Notice of Proposed Rulemaking (ANPR) under Section 811 of the Energy Independence and Security Act of 2007 (EISA or the Act). The views expressed in these comments are those of the Section and have been approved by the Section's Council. They have not been approved by the ABA's House of Delegates or Board of Governors and should not be construed as representing the policy of the ABA.

The high price of petroleum products today is a serious problem for economies and consumers in the U.S. and throughout the world. Increased fuel prices in particular are straining budgets and causing consumers to cut back. Fuel suppliers have taken steps to increase output. Governments are exploring how to counter these difficulties. Where shortages or higher prices are the cause of anticompetitive conduct, the FTC has stated its commitment to enforce the antitrust laws vigorously. To the extent prices are affected by "market manipulation," Section 811 may offer a new tool to address these problems.

The Antitrust Section's principal recommendation is that any regulations implementing Section 811 should not be used as a new regulatory tool for policing business activities that may affect market competition, which already is governed by the antitrust laws, but should be focused on deceptive or manipulative conduct that hinders the operation of markets by misleading market participants. These comments focus on distinguishing the role of the antitrust laws from the potential scope of Section 811 and are consistent with prior ABA statements opposing industry-specific antitrust legislation.

I. Energy Independence and Security Act of 2007

Section 811, titled "Prohibition on Market Manipulation," states:

> It is unlawful for any person, directly or indirectly, to use or employ, in connection with the purchase or sale of crude oil, gasoline or petroleum distillates at wholesale, any manipulative or deceptive device or contrivance, in contravention of such rules and regulations as the Federal Trade Commission may prescribe as necessary or appropriate in the public interest or for the protection of United States citizens.[1]

[1] Pub. L. 110-140, 121 Stat. 1723 (Dec. 19, 2007), Title VIII, Subtitle B, to be codified at 42 U.S.C. §§ 17301-17305.

The Act explicitly states that it does not "modify, impair, or supersede the operation of any of the antitrust laws."[2] The Act also provides that Section 811 can be enforced by the FTC in the same manner as it enforces the FTC Act.[3] "Any supplier" who violates Section 811 is subject to a civil penalty of not more than $1 million per violation, and each day of a continuing violation is a separate violation.[4]

II. FTC market manipulation regulations should address only deceptive conduct, rather than anticompetitive conduct now governed by the antitrust laws

The Antitrust Section recommends that any regulations implementing Section 811 should focus on deceptive or manipulative conduct that undercuts the operation of markets, not collusive or exclusionary conduct that may harm competition in markets, which is covered by the antitrust laws. First, the text and legislative history of the Act suggest that Section 811 was not designed to impose new rules governing the types of competitive conduct addressed by antitrust jurisprudence. Second, new antitrust standards specific to the petroleum industry may not benefit consumers.

A. The text and limited legislative history indicate Section 811 was designed to counter deceptive conduct, not to serve as an industry-specific antitrust law

The text of Section 811 authorizes regulations that reach "deceptive or manipulative" conduct of the type addressed by the Act's securities and energy law antecedents, but does not address anticompetitive acts. Likewise, the limited legislative history of Section 811 indicates only a Congressional intent that any Section 811 regulations be modeled on those that now apply to the electricity and natural gas industries, and there is nothing in the legislation or legislative history that would support directing new rules against conduct the antitrust laws now address.

1. Section 811 is modeled on FERC and SEC authority to challenge deceptive conduct, not on any antitrust law

As the ANPR recognizes, the text of Section 811 is based on existing statutes authorizing rules against intentional misrepresentation, deceit, and fraud. The Energy Policy Act of 2005 gave the Federal Energy Regulatory Commission (FERC) authority to prosecute "market manipulation" in natural gas and electricity markets, mirroring the language that was repeated in Section 811: "any manipulative or deceptive device or contrivance, in contravention of such rules and regulations as [FERC] may prescribe."[5] This language was in turn based on the Securities Exchange Act of 1934. Under the rule developed by FERC, market manipulation is "(1) … any act … that operates or would operate as a fraud or deceit upon any entity; (2) with the requisite scienter; (3) in connection with the purchase or sale of natural gas or electric energy," and it defines fraud as "any action … for the purpose of impairing, obstructing or

[2] *Id.* § 815(b)-(c).

[3] *Id.* § 813.

[4] *Id.* § 814(a).

[5] Natural Gas Act § 4A, 15 U.S.C. 717c-1; Federal Power Act § 222, 16 U.S.C. 824v.

defeating a well-functioning market."[6] The ANPR also mentions enforcement of the Commodities Exchange Act by the Commodities Futures Trading Commission. None of these statutes has been or should be construed to cover the anticompetitive conduct that is the subject of the antitrust laws or in any way to supplement the antitrust laws.

The ANPR asks how any Section 811 rules should relate to the antitrust laws. The Sherman Act prohibits agreements "in restraint of trade" and monopolization. Section 5 of the FTC Act gives the FTC authority to challenge "unfair methods of competition," with which the FTC applies Sherman Act standards."[7] Congress' choice of other models for the text for Section 811, which do not consider the competitive effect of conduct, demonstrates that Section 811 was not designed to overlap with the antitrust laws. Further, EISA Section 815(b) explicitly states that it does not "modify, impair, or supersede the operation of any of the antitrust laws." It would be inconsistent with this explicit savings clause to interpret Section 811 to apply to the same conduct as the antitrust laws apply and to impose different standards than do the antitrust laws.

Finally, it is worth noting that Section 811's prohibition on market manipulation does not authorize rules against price gouging or any effort to enforce or maintain particular pricing or pricing practices. A separate provision prohibiting price gouging was part of versions of the EISA that were considered by Congress, but was removed before passage.

2. The limited legislative history confirms Section 811 is not designed to capture anticompetitive conduct

Section 811 is not discussed in any Senate, House, or Conference Report, nor is there any reported Congressional debate on this provision.[8] However, the floor statements of a leading sponsor of the legislation are consistent with the text of the provision.

During her statement introducing S.1735, Senator Maria Cantwell stated that the market manipulation measures "are based on provisions in the recently enacted bipartisan energy bill [the Energy Policy Act of 2005]." She explained that the market manipulation section provided for "the same kind of anti-manipulation and transparency rules as those with which electricity and natural gas industries must comply."[9]

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[6] *Federal Energy Regulatory Commission, 18 CFR Part 1c: Prohibition of Energy Market Manipulation: Final Rule*, 71 FR 4244, 4254 (Jan. 26, 2006).

[7] 15 U.S.C. §§ 1-2; 15 U.S.C. § 45. Although EISA's Section 813(b) indicates that Section 811 shall be enforced "as an unfair or deceptive act or practice" under the FTC Act, there is nothing to suggest that Section 811 incorporates the antitrust rules the FTC enforces through FTC Act Section 5. These comments do not express any view on the scope of the FTC's authority under Section 5.

[8] The text in Section 811 originally was used by the 109th Congress in S.1735, a bill to Improve the Federal Trade Commission's Ability to Protect Consumers from Price-Gouging During Energy Emergencies, which was reintroduced in the 110th Congress as S.1263. No committee reports were filed on any of these bills in either the 109th or 110th Congress.

[9] 151 Cong. Rec. S10238 (daily ed. Sept. 20, 2005).

Senator Cantwell also could not have been more clear in her April 2008 letter to the FTC, in which she indicated her view that these statutes are not directed against anticompetitive conduct like that addressed by the antitrust laws. Senator Cantwell stated that the statutory language "is not intended to catch sellers who take advantage of the natural market forces of supply and demand, only those who attempt to affect the market or prices 'by artificial means … unrelated to the natural forces of supply and demand.'"[10]

B. Economic regulation can undercut the ability of competitive markets to benefit consumers

Antitrust jurisprudence reflects more than a century of thought on how to limit business conduct to protect the competitive markets that best serve consumer interests. Section 811 regulations that modify or supplement the antitrust laws might actually harm petroleum markets and undercut consumer benefits.

1. The antitrust laws protect consumers and competition

Competitive markets spur businesses to as efficiently as possible develop and sell low cost and high quality products to consumers. After long experience, courts and the antitrust agencies have firmly adopted antitrust standards that focus on guarding competition to promote consumer welfare.[11] As the Supreme Court has put it:

> The Sherman Act … rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conductive to the preservation of our democratic political and social institutions.[12]

The antitrust laws protect these consumer benefits by prohibiting collusion among competitors and the use of market power to exclude competition.

For the FTC to construe Section 811 to authorize new regulation of business activities that may affect competition would be surprising, given the narrow focus of the statute and its antecedents, and would represent a remarkable policy shift away from common law antitrust rules of general application and towards industry-specific economic regulation. However carefully the FTC drafts regulations in 2008, if Section 811 overlaps with antitrust, there remains the risk that those regulations in the future would not keep up with the best ideas on how to

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[10] Letter from Senator Maria Cantwell to FTC Chairman Kovacic and Commissioners Harbour, Leibowitz, and Rosch (April 8, 2008).

[11] To this end, the Sherman Act has been described as a "consumer welfare prescription." Reiter v. Sonotone Corp., 442 U.S. 330, 343 (1979). And there has been a "longstanding congressional commitment to … free markets and open competition." Community Communications Co. v. Boulder, 455 U.S. 40, 56 (1982); *Competition Policy in the European Union and the United States: Convergence or Divergence?* Speech by FTC Chairman William E. Kovacic, at 8, before the Bates White Fifth Annual Antitrust Conference (June 2, 2008) (stating that antitrust has "single-minded focus on 'consumer welfare'").

[12] Northern Pac. Ry. Co. v. United States, 356 U.S. 1, 4 (1958).

protect competitive markets and consumers. The common law approach to defining antitrust rules has allowed antitrust to evolve with improvements in economic thinking. The Section recommends maintaining a common law approach to developing antitrust rules. Even if the FTC were to draft Section 811 regulations that are consistent with "modern" antitrust thinking, over the long run those regulations might fall behind developments in legal and economic theory.[13]

2. New antitrust rules for petroleum could harm consumers

The current federal antitrust laws already bar certain collusive, monopolistic, and anticompetitive conduct by participants in all sectors of the economy, including in the petroleum industry. Monitoring of competition and antitrust enforcement are especially vigorous in petroleum markets, and especially by the FTC, which has indicated it will continue aggressively to enforce the antitrust laws in the petroleum industry.[14]

Section 811 regulations that go beyond deceptive conduct to supplement the antitrust laws or to try to improve the performance of petroleum markets actually may harm these complex markets, as discussed below in the context of the ANPR's "potential practices." Unregulated markets best ensure the availability of products consumers need at competitive prices, and adding new regulation that imposes different standards may result in less output and higher prices. The FTC itself has in the past concluded that new antitrust standards specific to the petroleum industry would not be beneficial. For example, the FTC recommended that Congress not adopt price gouging legislation and that the antitrust laws remain the standard for determining whether unilateral pricing behavior is unlawful: "Enforcing the antitrust laws strictly to prohibit business behavior that has anticompetitive effects will have a major impact in keeping markets free so that prices are set by competitive forces, not by manipulation or 'gouging.'"[15]

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[13] *See* William E. Kovacic & Carl Shapiro, *Antitrust Policy: A Century of Legal and Economic Thinking*, 14 J.L. & Econ. Persp. 43 (2000) ("As economic learning changed, the contours of antitrust doctrine … would shift as well").

[14] William E. Kovacic, Prepared Statement of the Federal Trade Commission before the Subcommittee on Oversight and Investigations, Committee on Energy and Commerce, U.S. House of Representatives, *Market Forces, Competitive Dynamics, and Gasoline Prices: FTC Initiatives to Protect Competitive Markets* (May 22, 2007) (hereinafter *Kovacic Testimony*) (testifying that "the Commission aggressively polices anticompetitive conduct" in petroleum markets); *Maintaining Our Focus at the FTC: Recent Developments and Future Challenges*, Speech by FTC Chairman Deborah Platt Majoras, at 8, before the ABA Section of Antitrust Law 7th Annual Fall Forum (Nov. 15, 2007) (stating that FTC has for a quarter century maintained a "special vigilance" in petroleum and other energy sectors); Federal Trade Commission, *The Petroleum Industry: Mergers, Structural Change, and Antitrust Enforcement*, at 16-18 (August 2004) ("FTC has devoted substantial resources to investigating alleged anticompetitive conduct, gasoline price differentials, and rapid price increases, and to monitoring gasoline prices.").

[15] Federal Trade Commission, *Investigation of Gasoline Price Manipulation and Post-Katrina Gasoline Price Increases*, at 196 (Spring 2006) (hereinafter *Katrina Report*) ("The Commission cannot say that federal price gouging legislation would produce a net benefit for consumers."); *Kovacic Testimony*, at 17 (noting that price gouging legislation could cause "interference with the market's pricing mechanism that is likely to lead to even worse shortages and more harm to consumers").

The Antitrust Modernization Commission (AMC) also has recommended that Congress limit sectoral economic regulation and avoid industry-specific antitrust rules: "Public policy should favor free-market competition over industry-specific regulation of prices, costs, and entry."[16] The conclusions of the FTC and AMC are consistent with the Section's consistent position that industry-specific antitrust standards are not needed and would not benefit consumers.[17]

C. The ANPR "potential practices" hypotheticals highlight the risks of allowing Section 811 to change antitrust standards

1. Unilateral decisions on supply

Two hypotheticals explore whether it should be unlawful for a supplier to make a unilateral decision to supply or not supply a geographic market, including during a period of price spikes. Outside the context of supply decisions that constitute deceptive conduct, identifying such supply decisions as market manipulation seems well beyond the text of Section 811 and the scope of the statutes on which it is modeled.

Making it a Section 811 violation for a supplier unilaterally to withhold output would be inconsistent with the antitrust laws, as the courts explicitly have recognized that unilateral withholding is not an antitrust violation.[18] It is a premise of the antitrust laws that free markets best can allocate resources and that regulation cannot make better supply decisions to improve consumer welfare. The Section recommends that any Section 811 regulations not cover unilateral decisions on supply and certainly not do so in a way that is inconsistent with antitrust jurisprudence.

"Market manipulation" might incidentally cover some decisions to refrain from supplying, such as when intended to manipulate a published index that relies on data from the market from which supply was "withheld." But beyond such peculiar circumstances, there are reasons to be skeptical that new federal rules governing supply decisions actually could benefit petroleum markets or consumers.

An FTC enforcing "duty to supply" regulation would face difficulty determining whether suppliers are pursuing a desirable business strategy or "withholding" for some ill purpose. A supplier that refrains from supplying an area that is short may have no intention to harm the

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[16] Antitrust Modernization Commission, *Report and Recommendations*, at 334 (April 2007) (emphasizing that "Congress should not displace free-market competition absent extensive, careful analysis and strong evidence that either (1) competition cannot achieve societal goals that outweigh consumer welfare, or (2) a market failure requires the regulation of prices, costs, and entry in place of competition").

[17] The ABA has opposed industry-specific antitrust rules for the petroleum industry since as early as 1992, when it adopted a formal Policy (Report 103B) on then-pending legislation regarding gasoline pricing: "[T]he American Bar Association opposes enactment of legislation regulating gasoline pricing and modifying the antitrust laws by creating industry-specific laws applicable to the sale of gasoline."

[18] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004) ("the mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free market system").

public interest. The supplier may have contracts that require shipments be sent elsewhere or a plan to inventory product to respond to greater demand later. The supplier may have determined additional production is unprofitable or even that better returns are available elsewhere. The supplier and purchasers may simply have been unable to reach agreement on price. Today these motivations are not unlawful, and allowing suppliers to pursue any of these courses is necessary in markets where competition decides what is supplied, where, and when. Even if a duty to supply could be unambiguously defined under Section 811, determining what supply allocations and price levels would most benefit consumers over the long run would be impossible for the FTC or any regulator in this complex industry.

The FTC recognized some of these concerns in its evaluation of the BP/ARCO merger. The Commission addressed the concern that BP had engaged in the practice of exporting domestic crude, rather than supplying domestic markets, for the purpose of increasing domestic spot prices. Rejecting a proposal to prevent the combined BP/ARCO from continuing this conduct, the majority of Commissioners observed that BP's unilateral action was not illegal under the antitrust laws and that the "over-regulatory export restriction would be unnecessary, unenforceable, and otherwise inappropriate."[19]

Recent examples of severe shortages, such as followed Hurricanes Katrina and Rita, demonstrate that competitive petroleum markets can respond quickly, which one would not expect in markets subject to pervasive supply and price regulation or where suppliers must pause to evaluate ambiguous legal obligations.[20] This evidence suggests any rules should not be different depending on the proximity of some natural disaster.

The Section believes that the antitrust laws are the best vehicle for determining the circumstances in which unilateral supply decisions should be lawful, to benefit consumers over the long run. The antitrust laws have struck a balance that imposes few restrictions on the freedom of firms to make their own supply decisions. The Section believes that Section 811 does not authorize new rules in this area and that new standards are not desirable.[21]

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[19] Federal Trade Commission, *In the* Matter of BP Amoco plc and Atlantic Richfield Co. (No. C-3938), Statement of Commissioners Anthony, Swindle, and Leary (Aug. 29, 2000) (noting that BP's exporting crude for purpose of increasing domestic prices was lawful and declining to impose restriction on the practice, which would be difficult to enforce and ineffective: "people will be cruelly disappointed if they are led to believe that the export restriction would have a detectable effect on the situation").

[20] The FTC's post-hurricanes study concluded that the "conduct of firms in response to the supply shocks caused by the hurricanes was consistent with competition" and that even "[e]xceptionally high prices on the part of individual retailers generally were very short-lived." *Katrina Report* at ix, x. The FTC also cautioned that the difficulties in defining what price level is acceptable under pricing regulation creates ambiguity, leaving suppliers uncertain how to comply, which may hurt consumer interests. *Id*. at ii n.6, 196.

[21] Existing antitrust laws already contain well-established prohibitions on collusion between competitors that leads to withholding of products from consumers. *E.g.*, FTC v. Indiana Fed. of Dentists, 476 U.S. 447, 459 (1986) (holding that, absent creation of efficiencies or other procompetitive virtue, "an agreement limiting consumer choice by impeding the 'ordinary give and take of the market place'" is unlawful).

2. Denial of access

Another ANPR potential practice hypothetical asks whether market manipulation regulations should impose a duty on terminal owners to provide access to prospective pipeline shippers that lack access to a terminal. As with unilateral supply decisions, this would go beyond the scope of Section 811 and its antecedents.

The question of under what circumstances the owner of terminals or other facilities may be required to provide access to other market participants has received considerable attention in the context of Sherman Act Section 2 jurisprudence, where it remains a controversial topic. However, the Supreme Court has made clear that there are few situations in which the antitrust laws require even a monopolist to share resources with other market participants. Under the antitrust laws, a supplier generally can make the unilateral decision to sell or not sell as it chooses: "In the absence of any purpose to create or maintain a monopoly, the [Sherman] act does not restrict the long recognized right of a trader or manufacturer … freely to exercise his own independent discretion as to parties with whom he will deal."[22] Moreover, courts consistently have rejected unilateral refusal-to-deal claims that do not involve a competitive relationship between a monopolist and the subject of the refusal to deal.[23]

Imposing liability under the facts of the ANPR hypothetical could cause some of the same problems that have led the courts to narrowly construe Section 2. First, it may be difficult to discern whether a denial of access has been motivated by an improper purpose on the part of the supplier or merely represents the failure of two reasonable parties to agree on the terms of access. Second, even if regulation only requires access on reasonable terms, if those could be determined, the obligation discourages investment by the party seeking access and by firms that might build additional facilities in the future.[24] Third, some government authority, here the FTC, must take on the task of regulating the terms of the mandated access, and there is no reason think a government regulator can do this in a way that promotes long term consumer benefits better than unregulated market forces. Finally, depending on how the authority imposing terms seems inclined to regulate, the obligation may promote gaming by either owners or users of the facilities in question.[25]

The Section believes that, in petroleum and other markets, the antitrust laws should be the guide for when firms may be required to provide competitors with access to facilities. The Section believes that Section 811 does not authorize new rules in this area and that new standards are not desirable.

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[22] United States v. Colgate & Co., 250 U.S. 300, 307 (1919).

[23] Mr. Furniture Warehouse, Inc. v. Barclays Commercial Inc., 919 F.2d 1517, 1523 (11th Cir. 1990) ("It requires a long stretch to call an individual refusal to deal 'monopolizing' when it does nothing to increase the refuser's monopoly power and nothing to increase his position in any market."; citing P. Areeda, Antitrust Law § 736, at 274 (1978)).

[24] Herbert Hovenkamp, Federal Antitrust Policy, § 7.5b (3d ed. 2005) (forced sharing "undermines the competitive market process of forcing firms to develop their own sources of supply" that will benefit consumers over the long run).

[25] *See Trinko*, 540 U.S. at 408.

3. Public announcements of capacity changes

The last potential practices on which the Section will comment relate to market participants publicly announcing information relating to capacity, such as pipelines reaching full capacity or refineries scheduling downtime.

The antitrust laws recognize that publishing information relating to capacity or other data relevant to future competitive potential is not always beneficial. The exchange among competitors of detailed, current information may lessen competition among them or allow them to police some other anticompetitive agreement they have made. Jurisprudence under Sherman Act Section 1 has a well-developed approach for distinguishing between information exchanges that are procompetitive and those that can restrain trade.[26] Similarly, the *Socony-Vacuum* case, which condemned a conspiracy in the 1930s among gasoline purchasers to purchase at agreed prices from independent refiners illustrates how the antitrust laws can address efforts to affect prices that results from an agreement among petroleum market competitors.[27] The conduct there violated Section 1 of the Sherman Act and would still under modern cases. Beyond the context of the release of deceptive information into a market, there seems no reason for new market manipulation regulations also to cover anticompetitive information exchanges or collusion among competitors.

Of course, it is advisable that any general or specific rules relating to publishing competitive information should take into account the potential legitimate reasons and benefits for such disclosures. For example, refinery downtime plans may be pre-announced as part of scheduling maintenance contractors or advising employees and local communities of significant events. Preannouncement of either refinery downtime or pipeline capacity constrictions may give other market participants the chance to plan around the upcoming changes.

The Section believes that the FTC can rely on the Section 1 rules on advance information disclosures to determine when publishing competitive information may have anticompetitive effects on the market. The Section believes that new standards are not desirable would not be beneficial to consumers.

III. Conclusion

The Section recommends that any regulations implementing Section 811 be narrowly focused on deceptive or manipulative conduct that undercuts the operation of markets and should not impose new regulations that cover conduct today addressed by the antitrust laws.

Respectfully submitted,

SECTION OF ANTITRUST LAW
AMERICAN BAR ASSOCIATION

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[26] *See* Todd v. Exxon Corp., 275 F.3d 191, 196 (2d Cir. 2001) (reversing dismissal of antitrust challenge to exchange of salary information); In re Petroleum Prods. Antitrust Litig., 906 F.2d 432, 445-48 (9th Cir. 1990) (holding that advance announcements of price increases could support inference of price fixing).

[27] United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).