Federal Trade Commission

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The views expressed are those of the Chairman and do not necessarily reflect those of the Federal Trade Commission or the other Commissioners.

Good day to you all.

It is a pleasure to be here and to speak about the recent work of the Federal Trade Commission. It is a particular pleasure for me to do this before a group such as this one. I think there is real value in maintaining communication between the antitrust agencies and the trade associations. Associations have an important role in our economy. They represent the interests of their members in various places, including before the antitrust agencies, and they help to spread information and new management techniques through an industry, to name just two of their functions. Many if not most of their activities are procompetitive. At the same time, trade associations are usually groupings of horizontal competitors, and so there is a risk that some of their actions can adversely affect competition. This is one of the areas where a dialogue with the antitrust agencies can be mutually beneficial, to help us learn of industry conditions and to help you avoid legal pitfalls.

In the next few minutes, I would like to bring to your attention three aspects of our recent work. First, the FTC has decided a case directly concerning your industry -- a merger case involving Owens-Illinois and Brockway. Second, the Commission has articulated general analytical frameworks for determining what is permissible conduct for trade associations and other groups of competitors. These principles attempt to ensure that the beneficial and procompetitive work of associations can be

continued without undue concern about antitrust liability, while at the same time defining reasonably clear limits, beyond which such collective activities might be viewed as improper horizontal restraints. Third, we are learning about the increasingly common practice of "benchmarking," or comparing one's performance of certain business functions with the standard set by firms that are especially good at those tasks. I would like to share some of my initial thoughts on how benchmarking and antitrust intersect.

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The Owens-Illinois litigation

As you know, the FTC is not a stranger to your line of business. In 1992 the Commission decided a major case involving Owens-Illinois' acquisition of Brockway.[1] The case is particularly fresh in my mind because I wrote the opinion for the Commission. It's an interesting opinion, both for what it says about our views of the glass packaging industry based on the record in that case, and also for what it shows about our fact-intensive approach to antitrust matters more generally.

In 1987, Owens-Illinois initiated a cash tender offer to acquire Brockway. At the time Owens was one of the nation's two largest producers of glass containers, and Brockway was the third

[1] Owens-Illinois, Inc., Docket No. 9212, 5 CCH Trade Reg. Rep. [1987-93 Transfer Binder] ¶ 23,162 (final order issued Feb. 26, 1992).

largest. The Commission found reason to believe that this increased concentration in the industry might lead to anticompetitive results. It therefore sought a preliminary injunction against the merger, but the district court denied this request.[2] The Commission also issued an administrative complaint. In the administrative litigation that followed, the parties compiled an extensive evidentiary record. The administrative law judge issued an initial decision finding the merger to be unlawful, and Owens-Illinois filed an appeal to the Commission.

After conducting a de novo review of the record, the Commission dismissed the complaint and allowed the acquisition to stand. The Commission's analysis of the full record developed by the administrative proceeding showed that competition was unlikely to be harmed by the acquisition.

The Commission began its analysis by defining the market within which competition was to be measured. To establish the relevant market, we had to determine whether the glass manufacturers competed only with one another, so that we should look only at those firms, or whether they also faced effective competition from other packaging materials, so that we should consider those as well. This wasn't an easy question. Other materials, such as plastic and metal, are also capable of containing many products. On a gross functional basis they might

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[2] See FTC v. Owens-Illinois, Inc., 681 F. Supp. 27 (D.D.C.), vacated as moot, 850 F.2d 694 (D.C. Cir. 1988).

seem to be in the same market with glass. Yet glass containers have special characteristics that other types of packaging materials historically have found difficult to duplicate. Glass containers are clear, impermeable, resealable, retortable, rigid, inert, and recyclable. In contrast, metal cans "are opaque, cannot be readily resealed, and may impart a taste to their contents."[3] Plastic containers, at least until recently, have been more permeable to air and other gasses, have lacked rigidity, have had some recycling disadvantages, and have not combined clarity with retortability.

Despite these differences in characteristics, however, we concluded that there was enough substitutability to preclude a meaningful antitrust market consisting of all glass containers. Even if all the manufacturers of glass containers were to collude together, they could not succeed in imposing a significant, across-the-board price increase. Enough users would switch to other materials to defeat any attempt at a general price increase.

The Commission then considered whether there might be meaningful narrower markets, consisting of glass containers for specific end uses as to which substitution was not possible. We considered nine such markets, rejected some, and accepted others. We found, for example, that there were no meaningful markets consisting of glass containers intended for shelf-stable juices

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[3] 5 CCH Trade Reg. Rep. [1987-93 Transfer Binder] ¶ 23,162 at 22,811.

or for distilled spirits. Other packaging materials had gained acceptance in both these markets and would constrain attempted price increases by glass producers. Cans were already widely used for juices, for example, and plastics were coming into use for distilled spirits, particularly for the smallest and largest sizes of bottle.[4] On the other hand, there did appear to be well-founded markets for glass containers intended for certain other end uses such as premium wines or jams and jellies. For these uses the unique properties of glass precluded substitutes. Glass was required for premium wines because plastic had problems with oxidation, and metal cans would not have been acceptable to consumers.[5] Jams and jellies similarly required glass for its transparency, resealability, and ability to withstand hot-packing.[6] The Commission found that these inelastic segments, in which substitution away from glass was difficult, constituted relevant product markets for antitrust purposes. The Commission also found that the relevant geographic market was the continental United States.

In short, there did exist some specific markets in which a lessening of competition among glass producers might in theory lead to increased prices. It was therefore these markets that we examined to see if the Owens/Brockway acquisition was likely in fact to produce such price effects.

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[4] Id. at 22,816.

[5] Id. at 22,820-21.

[6] Id. at 22,817-18.

We ultimately concluded that it would not. Increased concentration is a general concern to us because it tends to make express or tacit collusion easier. Here, however, we found factors that would tend to prevent effective collusion. The primary factors are the very small size of the product markets of concern, in comparison with the industry as a whole, and the extraordinary speed with which suppliers of glass containers can convert their facilities to produce containers for different end-use segments. This means that the vulnerable markets could be supplied by virtually any glass manufacturer, and that any collusive arrangement would have to embrace virtually all suppliers in order to be effective. The opinion also identified a variety of supplemental factors making collusion difficult, including the very large size of the customers in the inelastic markets; the presence of long-term contractual protections; and the use of stock containers in some of the end-use segments.

For these reasons we concluded that the glass packaging industry would not be particularly susceptible to supracompetitive pricing, even if it became more concentrated, and we therefore dismissed the complaint challenging the acquisition.

So -- what lesson should you carry away from this particular episode? I think the main point is that antitrust law, as the FTC now practices it, is an intensely practical art. We are willing to put in a great deal of effort to understand the daily workings of an industry. And the outcomes that we seek are

ultimately based, not on some abstract principle, but rather on the question of whether competition will or will not be affected in the real world.

The role of trade associations

We try to bring a similar degree of practicality to our review of trade associations. Trade associations are typically made up of the competitors in a particular industry. Joint conduct can affect competition among those member firms and thus has the potential for restraining trade. At the same time, joint conduct carried out in the context of trade associations also has the potential for enhancing competition and increasing the efficiency of the entire industry. To take but one example, product standards developed by an industry, such as standard dimensions for lumber and building materials, can make it easier for customers to make head-to-head comparisons between products, and can make it easier for customers to mix products of different manufacturers. Such standards may tend to enhance competition, so long as they not unduly restrict the range of consumer choice, unduly limit rivalry based on quality differences, or facilitate oligopolistic pricing.

In our assessment of trade associations we try to be practical at two different levels. First, and most obviously, we try to be fair in our assessments of the costs and benefits of any particular program. We don't automatically condemn an activity just because it involves horizontal competitors, but rather attempt to take account of its benefits as well.

Secondly, and perhaps with greater subtlety, we also try to be aware of the costs that uncertainty poses for the business community. Definite answers are not always possible, but we recognize that it is not ideal to probably permit an activity, or to permit it only at the end of a long investigation. We therefore seek to provide guidance as to what activities are likely to be permissible under current standards. Conversely, we also try to provide guidance as to the thresholds beyond which even a beneficial activity may be seen as going too far. To these ends we produce speeches such as this one, formal policy statements, non-adversarial advisory opinions, and, finally, opinions in litigated cases.

Let me make all of this more concrete by discussing three common association activities: (1) associations sometimes collect and disseminate information relevant to members of an industry; (2) they sometimes inform government of their members' concerns; and (3) they sometimes articulate ethical standards for the industry. In each of these contexts I will try to identify the benefits of the association activity, and also the limits beyond which it may be on more uncertain legal ground.

1. Industry information -- Let's begin with the trade association as a vehicle for collecting and disseminating information useful to the industry. This is a classic association activity, and one long recognized as having the potential to promote competition by generating efficiencies. Associations might, for example, produce appropriate statistics

on industry production and prices. They might provide members with advice on handling business issues. Or they might provide information to the public, in the form of marketing and promotional activities for the industry as a whole, such as ads explaining the generic advantages of glass as opposed to plastic packaging.

The antitrust laws will judge each of these activities in light of its own circumstances. Depending on those circumstances, such activities can often be undertaken free of antitrust risk. The Supreme Court has taught us, in a series of cases,[7] that cost savings through greater productive efficiency are to be counted favorably when joint activities among competitors are weighed under the antitrust laws. Even though a trade association produces abstract things such as industry reports, rather than tangible products such as glassware, efficiency gains in its work should still be relevant. As a recent article put it, "A professional association offers its members economies of scale in the production of information of particular interest to the profession."[8]

The Commission has devised a standard approach for evaluating horizontal agreements, such as those involved in information dissemination by a trade association. This is the

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[7] See, e.g., Northwest Wholesale Stationers v. Pacific Stationery & Printing Co., 472 U.S. 284 (1985); Broadcast Music, Inc. v. Columbia Broadcasting System, 441 U.S. 1 (1979).

[8] Arquit & Kattan, "Efficiency Considerations and Horizontal Restraints," 36 Antitrust Bulletin 717, 723 (1991).

methodology set out in our opinion in Massachusetts Board of Registration in Optometry,[9] and commonly called, for short, the "Mass. Board analysis." This guides a rule of reason inquiry into the procompetitive and anticompetitive effects of agreements among competitors. However, it speeds up the traditional inquiry by condemning certain kinds of agreements that lack efficiency justifications, without requiring a full-blown review of market structure and market power.

The Mass. Board analysis asks a series of questions that focus on the nature and effect of horizontal agreements. The first question is whether an agreement is "inherently suspect" -- that is, whether, absent an efficiency justification, it would tend inevitably to increase price or restrict output.[10] The Commission judges whether a practice is inherently suspect by reference to a mix of factors, including precedent, economic theory, common sense, and evidence of any concrete effect in terms of reduced output or increased prices.

If an agreement is inherently suspect, the analysis then turns to a second question: Is there a plausible efficiency justification for the agreement? If there is not even a plausible efficiency to be claimed, then the agreement has no benefits to be set against its costs, and it is summarily condemned. If there is a plausible efficiency justification, we

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[9] 110 F.T.C. 549 (1988).

[10] 110 F.T.C. at 604. See Broadcast Music, Inc. v. Columbia Broadcasting System, 441 U.S. 1, 19-20 (1979).

then turn to a third question and ask whether the justification is really valid. In other words, does it appear that the theoretically-possible efficiency actually has been achieved, and has it succeeded in actually creating or enhancing competition by reducing costs, creating new products, or the like? If, on examination, the justification is not valid in the particular case, then the agreement is again condemned. Only if the agreement is not inherently suspect to begin with, or if it has a plausible and valid efficiency justification, do we engage in a full-blown rule of reason inquiry, including an assessment of the market power of the parties to the agreement.

Why has the Commission adopted this approach, with its formality and its set series of questions? In brief, to save everyone's time. If cartel-like conduct is inherently suspect, and has no valid offsetting benefits, then we really shouldn't be spending a lot of time assessing the subtleties of its effects. We should be concentrating our efforts instead on understanding the closer and harder cases where a joint activity has both costs and benefits for the public.

Under this analysis, many of a trade association's information-gathering and information-disseminating functions may well pass muster. The information may produce efficiencies, and it may not be likely to harm competition, particularly if it is compiled under appropriate safeguards. For example, information about prices and costs in an industry is likely to be permissible if it is compiled by a third party, is based on historical rather

than current data, and is based on statistics from a sufficiently large number of reporting institutions that recipients could not determine the prices or costs of any one of them.[11] Trouble becomes possible, however, if the information-sharing activities have a strong bearing on price, output, or some other aspect of competitive rivalry, or are likely to facilitate coordinated behavior on those points.

Indeed, there are information-related trade association activities that cross the line into illegal conduct. For example, we recently negotiated consents with two associations of foreign-language conference interpreters.[12] These settled allegations that the associations had published lists of fees that their members were required to charge. The complaints also alleged that the associations had further restrained competition among their members through work rules requiring, among other things, that a specified number of interpreters serve on a team and that all team members be paid the same rate.

The laws will also condemn information-related activities that have an indirect but sufficiently strong effect on price.

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[11] These factors were applied in the Department of Justice and Federal Trade Commission Statements of Enforcement Policy and Analytical Principles Relating to Health Care and Antitrust, at 55 (Sept. 27, 1994) (safety zone requires management of the survey by a third party, historical data more than three months old, and aggregated statistics from at least five institutions, no one of which represents more than 25 percent on a weighted basis of any disseminated statistic).

[12] See American Society of Interpreters, C-3525 (Aug. 31, 1994); The American Association of Language Specialists, C-3524 (Aug. 31, 1994).

For example, in Association of Engineering Firms Practicing in the Geosciences,[13] the Commission issued a consent order settling charges that an association of engineers had used its insurance and peer review programs to discourage its members from price competition. The association's members had created a company offering professional liability insurance. According to the complaint, however, this insurance was available only on condition of peer review, and the reviewers looked into whether an applicant had offered competitive bidding, discounted fees, or credit terms for customers. The Commission alleged that this inquiry chilled price competition without appearing to offer any offsetting efficiencies. The consent order therefore bars the association from using peer review to consider such pricing matters.

Finally, information-disseminating activities may become improper when they cross a line and become facilitating practices. "Facilitating practices" are activities that tend to promote interdependence by reducing rivals' uncertainty or by diminishing their incentives to deviate from a coordinated strategy. All information-sharing activities will tend to diminish uncertainty to some degree. This does not mean that all such activities are likely to facilitate anticompetitive interdependence, however. The procompetitive or anticompetitive nature of an information exchange depends in part on the nature of the information being exchanged and on the market context in

[13] C-3430 (June 11, 1993).

which it occurs -- such as whether the market itself is susceptible to tacit collusion. Thus, for example, in concentrated markets, information-exchange activities may become improper when the nature of the information being conveyed is such that it is not particularly useful in achieving output-increasing efficiencies, but it is particularly useful in enabling firms to coordinate their actions in anticompetitive ways.

We saw one such practice as part of our recent Infant Formula Cases.[14] The three main infant formula producers were active in a trade association, the Infant Formula Council. The complaints filed against two of the firms -- Abbott Laboratories and Mead Johnson & Co. -- alleged that during trade association meetings they had exchanged information concerning their own marketing practices, and that this exchange reduced uncertainty as to whether any of the companies would begin to engage in consumer advertising. According to the complaint, this information exchange did not help the firms increase production in any significant way, but the assurances that were conveyed did facilitate coordinated avoidance of competitive advertising. The Commission therefore secured consent orders barring the practice.

2. Government relations -- A second function of trade associations is lobbying. Associations can be a very efficient

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[14] FTC v. Mead Johnson & Co., Civ. No. 92-1366 (D.D.C. June 11, 1992) (consent decree); FTC v. American Home Products, Civ. No. 92-1367 (D.D.C. June 11, 1992) (consent decree); Abbott Laboratories, Dkt. No. 9253 (filed June 11, 1992) (administrative complaint), consent issued (Feb. 28, 1994).

means of communicating their members' views to the government. They can report what their members think about certain government policies, and can efficiently support those views by preparing position papers in a central location. This process has benefits to both parties. The association members get efficient representation, and the government gets input that allows it to make more informed decisions.

What the association cannot do is orchestrate the actual commercial conduct of competing members. It cannot, for example, advocate and then coordinate a boycott of a government purchasing program whose reimbursement it thinks is too low. This is the teaching of our litigation a few years ago in Superior Court Trial Lawyers Ass'n.[15] This group was made up of lawyers who represented indigent criminal defendants in the District of Columbia Superior Court. The group lobbied, as was their right, for an increase in the fees paid to those lawyers. When this effort failed to win an increase, however, the association announced a "strike" and most of its members jointly agreed to cease accepting new cases. The Commission found, and the Supreme Court ultimately agreed, that this was a per se violation of the antitrust laws.

3. Ethical standards -- A final function of trade associations has been to develop and articulate ethical standards for their industries. This too is a classic function, and one

[15] 107 F.T.C. 510 (1986), order vacated, 856 F.2d 226 (D.C. Cir. 1988), rev'd, 493 U.S. 411 (1990).

with which we have no problems in principle. Quite the contrary: the ethical conduct of business tends to prevent the abuse of uninformed consumers, and to protect smaller competitors from unfair practices, and both these things are conducive to beneficial competition on the merits.

Where we would grow concerned would be if it appeared that nominally "ethical" standards were in fact being used to suppress competition. The Commission continues to bring a variety of cases challenging such conduct. In Connecticut Chiropractic Association[16] we entered into a consent order with an association whose ethical code allegedly prohibited members from offering free or discounted services. In Structural Engineers Association[17] we entered into a consent with an association whose ethical standards allegedly prohibited its members from advertising their work or merit in a self-laudatory manner. In Community Associations Institute[18] we entered into a consent with an association that had allegedly applied its ethical code in such a way as to prohibit members from soliciting other members' clients. Even if such ethical rules have worthy goals in mind, such as preventing tortious interference with contracts, in some cases they appear to have been written more broadly than those goals actually require.

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[16] No. C-3351 (Nov. 19, 1991).

[17] Structural Engineers Ass'n of Northern California, 112 F.T.C. 530, 531 (1989).

[18] C-3498 (June 15, 1994).

Benchmarking

Not all interesting joint business activity is conducted through trade associations, of course. Another type of joint activity has recently been coming into prominence. This is benchmarking. This term denotes the process of studying the business practices of companies that are among the best in their class, from whatever industry, and comparing those practices to one's own. Companies are selected as models on the basis of their performance of the particular task under examination, and not necessarily on their overall performance.

Benchmarking is a relatively new topic. We have not yet opened any cases or investigations involving it, and my views are therefore still subject to change.

That said, it appears that many kinds of legitimate benchmarking may not raise antitrust concerns. This is so for at least three reasons. First, benchmarking often is not directed at the dimensions of rivalry with which antitrust is most concerned -- namely, price and output. Benchmarking is more commonly used to look for possible improvements in more technical areas such as billing and collection, inventory control, order processing, quality control, maintenance procedures, or waste management. An exchange of information on these topics does not seem likely to lead to agreements on an anticompetitive increase in price or a decrease in output.

Second, benchmarking often appears to be benign because it can have obvious procompetitive consequences. By diffusing

knowledge of the most efficient business techniques, it may raise the productive efficiency of an entire industry.

Third, benchmarking is particularly unlikely to be harmful to the extent that it is carried out among companies that are not in the same line of business. And indeed, most benchmarking exercises seem to involve this situation. If you are studying, say, statistical techniques of quality control, there is no absolute need to limit your models to firms in your own industry. Firms in the glass packaging business and in some other line of manufacturing may still be able to learn from one another at the level of managerial technique. In such cases the likelihood of competitive harm is very small.

If a particular instance of benchmarking <u>does</u> raise competitive concerns, it is most likely to do so where the three factors that I just mentioned are reversed. Alarm bells should go off if you find yourself engaged in benchmarking with rivals in your own industry, when the upside benefits to efficiency may be questionable, and when you are studying an aspect of the business that has a fairly direct effect on price or output.

Effect on price or output will often be a critical part of the inquiry. The concept of benchmarking is not intended to include explicit or tacit agreements on these topics. Effects on price and output may nonetheless come about as "spill-overs" from even a legitimate benchmarking discussion. Improper spill-over

effects may be particularly likely to occur under two circumstances.[19]

First, harmful spillovers are possible when the market is otherwise conducive to tacit collusion. The factors that tend to increase the likelihood of this include such elements as high concentration, high barriers to entry and homogeneous products.

Second, improper spill-over effects on price or output become more likely as the subjects under discussion themselves become more closely related to price and output. This is most likely to be a problem if the parties to the benchmarking exercise are rivals in the same industry. For example, consider benchmarking on the strategies used for negotiating the purchase of a critical input. Learning better cost-containment techniques is a social benefit. Yet if the companies exchanging this information are purchasing the same input, the discussions on the topic might facilitate parallel conduct on the prices they are willing to pay. If the companies are in the same industry, and if the input is a large component of the final price, then the benchmarking may facilitate parallel conduct on output price as well. This example shows the desirability of finding benchmarking partners outside your own line of business if the issue is at all doubtful.

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[19] For further exploration of some of the issues involved see Henry, "Benchmarking and Antitrust," 62 Antitrust L.J. 463 (1994); Slowey, "Benchmarking: Boon or Buzz Word?," Antitrust, Summer issue, at 30 (1993).

In short, benchmarking is an exciting and useful new development, but still one where some limits need to be observed. When in doubt, it would be wise to seek antitrust counsel.

Conclusion

This brings me almost to the end of my remarks. Let me leave you with two final thoughts. First, you can all be very proud of the good work that trade associations have done. They play a crucial role in transmitting information and new management techniques to firms that can use them. They are one of the vehicles for making American industry more competitive.

Second, you should also keep in mind that agreements reached under the auspices of a trade association are usually horizontal agreements, as to which antitrust scrutiny is required. Thus, again, the prudent thing for you to do is to consult with antitrust counsel before embarking on any course of action that has the potential to affect price, output, or any other element of competitive rivalry.

Thank you all very much.