General Counsel Corner

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Why The FTC Is Unlikely Ever To Be Your Friend

The Federal Trade Commission is the federal agency having primary responsibility for the enforcement of federal antitrust legislation with respect to the petroleum industry. It has no responsibilities or duties relating to the implementation or enforcement of state, as opposed to federal, legislation.

Yet the FTC persistently has employed its prestige and purported expertise to attack state legislation intended to promote fair competition in the retail gasoline market.

Why is the FTC so hostile to dealer-sponsored legislation and is there any likelihood that it will change its position?

Recent writings either sponsored or generated by the FTC provide an insight into its rationale for opposing below cost selling, open supply and divorcement legislation, and suggest that it is unlikely that the FTC will change its position in the foreseeable future.

Consider first the academic paper recently submitted under the sponsorship of the FTC by professors Cary Deck and Bart Wilson.

Using undergraduate students, these professors formulated a “game” analysis to explore the effects of zone pricing and divorcement on a hypothetical market. Their study assumes the unavailability of real world data, and relies entirely on the hypothetical price moves made by a limited number of student “refiners” and “dealers”.

The professors’ conclusions are highly theoretical and dependent upon academic economic theory. They conclude, based upon the students’ responses, that zone pricing is “pro-competitive” because it may reduce pump prices, while preserving already fat refiner margins. Vertical integration, i.e. company-operated stations, also appears to the professors to be largely “pro-competitive” based on theoretical grounds.

Two aspects of the professors’ study are typical of the FTC’s overall approach. First is their willingness to jump at conclusions without any real extrinsic evidence. There is no real world economic evidence that zone pricing is “pro-competitive” or that divorcement legislation has an “anti-competitive” effect.

Second, the professors' study is entirely oblivious to dealer welfare. They recognize that the party squeezed by zone pricing is the dealer, but do not consider the long-term consequences of the elimination of independent dealers from an increasingly oligopolistic market.

It is undeniable that under the FTC's watch the petroleum industry has become much more concentrated as a result of the mergers that it has approved. If independent dealers are squeezed from the market, it could be far easier for oligopolistic suppliers controlling the supply of gasoline from the refinery to the pump to do what oligopolists traditionally do – increase their profit margins at everyone else's expense.

Consider next the recent paper, "The Economics of Price Zones and Territorial Restrictions in Gasoline Marketing," authored by David Meyer and Jeffrey Fischer of the FTC who, incidentally, are among the persons acknowledged by professors Deck and Wilson as assisting in the preparation of their paper.

Relying upon purely theoretical analysis, these authors theorize that zone pricing and supplier "redlining" (i.e., prohibitions imposed by refiners on jobbers not to sell to direct supply dealers) are both "pro-competitive". They conclude, for example, that it may be "pro-competitive" to prohibit jobbers from selling to direct supply dealers at prices below dealer tankwagon in order to prevent them from "cherry-picking" the refiner's most profitable stations. That the dealer could pass on those savings to the public appears to be inconsequential under their analysis.

Consider finally the recently-released FTC staff study, "The Petroleum Industry: Mergers, Structural Change, and Antitrust Enforcement." There, the FTC concludes that state laws that restrict refiners' ability to own or operate gasoline retail outlets have resulted in higher retail prices, which may amount to an increase of 3 to 4 cents per gallon. There is, however, no economic evidence to support that canard.

Taken together, these writings suggest that the FTC has bought into a theoretical framework under which practices utilized by major oil companies to swell their margins are "pro-competitive"; anything that would improve the dealer's lot is "anti-competitive"; and dealers themselves are largely inconsequential. And all this with little or no supporting economic analysis.

It is somewhat ironic that the FTC has devoted so much effort to defeating state legislative efforts over which it has no jurisdiction upon purely theoretical grounds, while approving a series of major supplier acquisitions and mergers, which -- according to the recent study of the General Accounting

Office -- have had a materially anti-competitive impact in the real world. Unfortunately, the FTC appears to be more persuaded by its own economic assumptions than by real world events.

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