



UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Bureau of Competition
Bureau of Economics
Office of Policy Planning

June 17, 2004

The Honorable Gene DeRossett
Michigan House of Representatives
District Fifty-Two
The State Capitol
Lansing, MI 48913

Re: The Michigan Petroleum Marketing Stabilization Act

Dear Representative DeRossett:

The staffs of the Federal Trade Commission's Office of Policy Planning, Bureau of Competition, and Bureau of Economics are pleased to respond to your letter of May 19, 2004, asking us to comment on Michigan H.B. 4757, also known as the "Petroleum Marketing Stabilization Act."¹ Specifically, in your capacity as Chairperson of the Michigan House of Representatives standing committee on Transportation, you asked us the following:

- What is the likely competitive impact of this legislation?
- What impact would this legislation have on consumers if it were signed into law? Would it significantly raise prices?
- Are there existing protections against "predatory pricing" found in the federal antitrust laws, and to that end would this legislation be duplicative in nature?
- Are there any scholarly studies or court decisions in recent years that address the effect of "below-cost" pricing in relation to the creation of monopolies?

The FTC is charged by statute with preventing unfair methods of competition and unfair

¹This letter expresses the views of the FTC's Office of Policy Planning, Bureau of Competition, and Bureau of Economics. The letter does not necessarily represent the views of the Commission or of any individual Commissioner. The Commission has, however, voted to authorize us to submit these comments.

or deceptive acts or practices in or affecting commerce.² Under this statutory mandate, the Commission seeks to identify business practices and regulations that impede competition or increase costs without offering countervailing benefits to consumers. In particular, the Commission and its staff have investigated, conducted workshops, and commented on proposed regulations regarding motor fuel pricing. In 2001, the Commission completed investigations of spikes in reformulated gasoline prices in several Midwest states,³ and of gasoline price increases in West Coast markets.⁴ In the last two years, the Commission held two public conferences to examine factors that affect prices of refined petroleum products in the United States.⁵ Commission staff have also filed public comments with the Environmental Protection Agency that discussed how “boutique fuels” regulations may increase average costs to produce gasoline and may give rise to conditions that make short-term price spikes more prevalent.⁶

On many occasions, Commission staff has commented on state bills that would regulate the price at which retailers could sell gasoline to consumers.⁷ In the past two years, for example,

²Federal Trade Commission Act, 15 U.S.C. § 45.

³FTC, Final Report, *Midwestern Gasoline Price Investigation* (Mar. 29, 2001), at <http://www.ftc.gov/os/2001/03/mwgasrpt.htm>.

⁴*FTC Closes Western States Gasoline Investigation*, FTC Press Release (May 7, 2001), at <http://www.ftc.gov/opa/2001/05/westerngas.htm>.

⁵*FTC to Hold Public Conference/Opportunity for Comment on U.S. Gasoline Industry*, FTC Press Release (Jul. 12, 2001), at <http://www.ftc.gov/opa/2001/07/gasconf.htm>.

⁶FTC staff comments, *Study of Unique Gasoline Fuel Blends, Effects on Fuel Supply and Distribution and Potential Improvements*, EPA 420-P-01-004, Public Docket No. A-2001-20 (Jan. 30, 2002), at <http://www.ftc.gov/be/v020004.pdf>.

⁷See Letter from Susan Creighton, Director, FTC Bureau of Competition, et al., to Kansas State Senator Les Donovan (Mar. 12, 2004), at <http://www.ftc.gov/be/v040009.pdf>; Letter from Susan Creighton, Director, FTC Bureau of Competition, et al., to Wisconsin State Rep. Shirley Krug (Oct. 15, 2003), at <http://www.ftc.gov/be/v030015.htm>; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, et al., to Eliot Spitzer, Attorney General of New York (July 24, 2003), at <http://www.ftc.gov/be/nymfmpa.pdf>; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, et al., to Roy Cooper, Attorney General of North Carolina (May 19, 2003), at <http://www.ftc.gov/os/2003/05/nclattorneygeneralcooper.pdf>; *Competition and the Effects of Price Controls in Hawaii's Gasoline Market: Before the State of Hawaii, J. Hearing House Comm. On Energy and Environmental Protection et al.*, (Jan. 28, 2003) (testimony of Jerry Ellig, Deputy Director, FTC Office of Policy Planning), at <http://www.ftc.gov/be/v030005.htm>; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, et al., to Gov. George E. Pataki of New York (Aug. 8, 2002), at <http://www.ftc.gov/be/v020019.pdf>; Letter from Joseph J. Simons, Director, FTC Bureau of Competition, and R. Ted Cruz to Hon. Robert F. McDonnell, Commonwealth of Virginia House of Delegates (Feb. 15, 2002), at <http://www.ftc.gov/be/V020011.htm>. See also Letter from Ronald B. Rowe, Director for Litigation, FTC Bureau of Competition, to Hon. David Knowles, California State Assembly (May 5, 1992); Prepared Statement of Claude C. Wild III, Director, FTC Denver Regional Office, before the State, Veterans, and Military Affairs Committee of the Colorado State Senate (Apr. 22, 1992); Letter from Claude C. Wild III, Director, FTC Denver Regional Office, to Hon. Bill Morris, Kansas State Senate (Feb. 26, 1992); Letter from Claude C. Wild III, Director, FTC Denver Regional Office, to David Buhler, Executive Director, Utah Department of Commerce (Jan. 29, 1992); Letter from Thomas B. Carter, Director, FTC Dallas Regional Office, to Hon. W.D. Moore, Jr., Arkansas State Senate (Mar. 22, 1991); Letter from Jeffrey I. Zuckerman, Director, FTC Bureau of Competition, to Hon. Jennings G. McAbee, Chairman, Other Taxes and Revenues

Commission staff have analyzed bills in Alabama, Kansas, New York, Virginia, and Wisconsin. Many of these bills contain provisions similar to those in Michigan H.B. 4757, particularly provisions that would prohibit sales below cost. Because our analysis of H.B. 4757 parallels our analysis of bills in other states, we are attaching to this letter a copy of our letter to Kansas State Senator Les Donovan regarding a similar below-cost gasoline bill. A summary of our analysis is below:

- If signed into law and followed by retailers, H.B. 4757 would likely discourage competitive pricing. Unlike the federal antitrust laws, which condemn only below-cost pricing that has a “reasonable prospect” or “dangerous probability” of allowing the price-cutter to recoup its investment in below-cost prices,⁸ the Bill subjects vendors to civil liability – including treble damages – for cutting prices even if there is no likelihood of harm to competition.
- By focusing on “retailer cost” rather than economically relevant marginal costs, the Bill subjects a greater range of prices to liability in comparison to federal antitrust law.⁹ As a result, many vendors likely would avoid procompetitive pricing.
- Economic studies, legal studies, and court decisions indicate that below-cost pricing that leads to monopoly occurs infrequently. Below-cost sales of motor fuel that lead to monopoly are especially unlikely.
- The Bill is duplicative. The FTC, the Department of Justice’s Antitrust Division, state attorneys general, and private parties can bring suit under the federal antitrust laws against anticompetitive below-cost pricing. Given the strong stance of the Supreme Court in favor of low prices and the care the Court has devoted to explaining the types of price-cutting that are illegal under the antitrust laws, the Michigan Petroleum Marketing Stabilization Act is not necessary to protect consumers.

Further, the Bill appears to protect certain competitors, rather than consumers or competition itself. The text of the Bill singles out retailers with motor fuel membership clubs for scrutiny under the below-cost provisions. Specifically, the Bill applies only to a “retailer” that “[m]aintains a storage facility for motor fuel” and “[s]ells motor fuel at a retail location that sells only to members” who are the “end user of the motor fuel.”¹⁰ In addition, the Bill appears to ban below-cost sales that take business away from only a single competitor, even if there is no danger that a membership club retailer could damage market-wide competition by cutting prices,

Subcomm., Ways and Means Comm., South Carolina House of Representatives (May 12, 1989). All of these letters are on file at the FTC.

⁸*Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222-224 (1993).

⁹H.B. 4757 § (3)(h)(i)(A)-(B); (3)(h)(ii)(A)-(B).

¹⁰*Id.* at § (3)(g)(i)-(iii).

driving out competition, and then recouping losses by later charging higher prices.¹¹ Retailers without such membership clubs are exempt from scrutiny under the Bill.

Finally, in one respect H.B. 4757 has an even greater potential to harm competition than some of the other bills. H.B. 4757 contains a maximum sale price provision that could create fuel shortages.¹² Most economists and antitrust experts doubt that price controls are a viable mechanism to increase consumer welfare in markets where competition is possible. Historical experience demonstrates that price controls tend to create shortages, reduce quality, and generate other inefficiencies.¹³ This is especially true in the sale of gasoline.¹⁴

¹¹“Any person threatened with injury or injured directly or indirectly in his or her business or property by a violation of this act may bring an action for appropriate injunctive or other equitable relief, 3 times the amount of actual damages . . . , interest on the damages . . . , taxable costs, and actual attorney fees.” *Id.* at § 14. There is no requirement that market-wide competition also be injured.

¹²Under H.B. 4757 § 6, “[a] retailer engaged in commerce in this state shall not sell or offer to sell motor fuel for a price above the maximum sale price at a retail location or unattended location.” The “maximum sales price” is defined as “the retail sales price measured as the retailer cost, applying the maximum cost of doing business component.” *Id.* at § (2)(l). The “maximum cost of doing business component” means “3 times the cost of doing business component.” *Id.* at § (2)(k). The cost of doing business component is defined as “all costs incurred in the conduct of business. . .” *Id.* at § (2)(e).

¹³*See Competition and the Effects of Price Controls in Hawaii's Gasoline Market, supra* note 7.

¹⁴*Id.* The U.S. experience with gasoline price controls in the 1970s is illustrative:

A report by the Federal Trade Commission’s Bureau of Economics concluded that the federal price controls led to the adoption of higher-cost production methods and sporadic shortages manifested in gasoline lines.

Customers queued up at gasoline stations are perhaps the most visible example of the inefficiencies resulting from the shortages created by gasoline price controls, but myriad other examples actually occurred during this period: limited station hours, Sunday station closures, “odd-even” purchasing restrictions based on license plate numbers, and restrictions on the number of gallons the customer could purchase in a single trip to the gasoline station. Also noteworthy are the secondary effects of such inconveniences, which included efforts to hoard gasoline and, in some instances, an increased hazard of car fires because people began storing additional gasoline in containers in their trunks.

Id. (citations omitted).

Respectfully submitted,

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