U.S. Enforcement Update: McWane Continues to Fight for Vindication on Appeal of Alleged Exclusionary Conduct

Justin P. Hedge, Arnold & Porter LLP

As reported in the spring edition of *Monopoly Matters*,[1] on January 30, 2014, the Federal Trade Commission ("FTC" or "Commission") found that McWane, Inc. unlawfully monopolized the market for domestically manufactured ductile iron pipe fittings ("DIPF") via exclusive dealing conduct in violation of Section 5 of the FTC Act.[2] The original complaint charged McWane with seven counts of violating Section 5. Ultimately, the Commission found McWane was liable only on the monopolization count,[3] with Commissioner Wright issuing a dissent on the basis that there was insufficient evidence of an anticompetitive harm.[4] McWane has now appealed to the 11th Circuit to overturn the Commission's lone finding of liability.

McWane's Alleged Exclusive Dealing Conduct

The conduct at issue in the monopolization claim against McWane arises from what is referred to as McWane's "full support" program for its sales of DIPF. In February 2009, Congress enacted the American Recovery and Reinvestment Act ("ARRA"), which provided low cost stimulus financing for infrastructure projects using domestic products. In June 2009 McWane's competitor, Star Pipe Products, Ltd., announced that it would soon begin to sell some domestically produced products, which it did a few months later, relying on third-party foundries for manufacturing. Then in September 2009, McWane sent a letter to its distributors announcing that if they did not buy McWane's full line of domestic DIPF products, they "may" lose unpaid rebates and experience delivery delays of up to 12 weeks. The Commission found that McWane was the only supplier of a full line of domestic fittings and that its full support program unlawfully maintained McWane's domestic market power by preventing Star from becoming an effective competitor for U.S.-manufactured products.[5]

McWane's Brief Attacks Market Definition and Lack of Competitive Impact

McWane filed its opening appellate brief on June 27, 2014, making three main arguments.[6] First, McWane argued that the record evidence was insufficient as a matter of law to support the Commission's conclusion that a domestic DIPF market is a relevant antitrust market. McWane argues that the evidence was insufficient, in part, because the FTC's expert economist did not perform any economic test—such as calculating a cross-elasticity of demand to measure the extent of domestic and foreign product substitution—to define such a market. The Commission found such a market existed based on testimony and business documents. McWane also pointed to the lack of evidence that *customers* would consider a distinction between domestic and foreign products to exist. To the extent some contracts had buy-American requirements, McWane noted "customers routinely opened their specifications and flipped their purchases from domestic fittings to imports."[7]

Second, McWane argued that Star's concurrent entry and expansion into domestic production further required reversal of the Commission's finding that the full support program was unlawfully exclusionary.[8] According to McWane, the program was in place for only four months and did not contractually obligate customers to any purchases. Indeed, McWane pointed out that Star obtained a 5% share in the first year after entering and nearly 10% in the second year despite McWane's program. In the year following the full support distributor letter, Star added an average of more than two new customers every week. McWane dismissed the Commission's conclusion that Star might have reached a larger, more viable scale and opened its own U.S. production facility as misplaced and speculative, and argued that Star's undisputed entry story is inconsistent with the conclusion that McWane's conduct was unlawfully exclusionary.

Lastly, McWane argued that the Commission's decision merely protects a less efficient competitor, not competition, and ignores the procompetitive benefits of the full support program. To support this argument, McWane relied on evidence that its prices were lower than Star's prices in many states. It also argued that Star's reliance on outsourced production was not an inherent disadvantage as Star had successfully used such outsourcing to grow its import DIPF business. McWane stated that its purpose for the full support program was to ensure it could keep its domestic foundry

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[1] J. Hedge, *The Federal Trade Commission's Split Decision in McWane Serves as Warning on Exclusive Dealing Practices*, 11 A.B.A. Sec. of Antitrust Law Unilateral Conduct Committee Monopoly Matters 34 (Spring 2014), *available at* http://apps.americanbar.org/dch/committee.cfm?com=AT322100.

[2] Opinion of the Commission, *In re McWane*, Dkt. No. 9351 (Jan. 30, 2014) ("Commission Opinion"), *available at* http://www.ftc.gov/enforcement/cases-proceedings/101-0080b/mcwane-inc-star-pipe-products-ltd-matter.

[3] The Commission declined to address the Administrative Law Judge's finding of attempted monopolization, having found actual monopolization, and dismissed a count for conspiracy to monopolize. Two other counts (one alleging a price-fixing conspiracy and another related to an information exchange) resulted in a split Commission vote and were dismissed "in the public interest" given the lack of majority.

[4] At the time the Complaint was voted out by the Commission, there was also a dissent from then-Commissioner Rosch on the basis that the Complaint did not adequately allege exclusive dealing as a matter of law.

[5] Commission Opinion at 16-30.

[6] Brief of Petitioner McWane, Inc., *McWane, Inc. v. FTC*, No. 14-11363 (11th Cir. June 27, 2014).

[7] *Id.* at 35.

[8] *Id.* at 38-47.

open, as competition from imports had caused many others, including another domestic McWane foundry, to close. Given that McWane's U.S. foundry was underutilized and that McWane sold at lower prices than Star, McWane argued that the full-support program was procompetitive by allowing for an increased output of lower-priced products.

FTC Opposition Defends Absence of Econometric Evidence on Market Definition and Argues McWane's Conduct Made Only Domestic Competitor Less Efficient

The FTC's brief defended a domestic-manufactured market definition based on the existence of projects with domestic-only specifications—largely those subject to "buy-American" legal requirements, such as ARRA-funded projects.[9] The FTC continued to assert, as the Commission found in its decision, that econometric evidence is not necessary to establish a relevant market in light of the "overwhelming record evidence" such as McWane's internal documents distinguishing a domestic market.[10]

With respect to establishing anticompetitive harm, the FTC argued that the intent and effect of the full support program was to keep Star from winning a critical amount of business for domestically produced products that would allow it to continue to invest in its domestic business.[11] The FTC responded to McWane's argument about the non-binding nature of the program by asserting that McWane never publicly withdrew the program nor notified distributors of a change in policy and, with one exception, all major distributors complied with the terms of the full-support program and diverted business from Star. The FTC acknowledged that customers did buy from Star, but argued that those sales were the result of an exception to McWane's full support program for situations when McWane was out of stock. Also, the FTC questioned the significance of the market share that Star was able to obtain on the basis that McWane "tempered its enforcement efforts" after becoming aware of the FTC investigation in early 2010.[12] According to the FTC, Star was giving "serious" consideration to acquiring its own U.S. foundry that would have reduced its cost for supplying domestic product. The FTC argued that Star's ultimate decision against the acquisition when sales projections fell off in the wake of McWane's full support distributor letter sufficiently supports the Commission's finding of competitive harm.[13]

[9] Brief of the Federal Trade Commission at 24-26, *McWane, Inc. v. FTC*, Case No. 14-11363 (11th Cir. August 29, 2014).
[10] *Id*. at 27.
[11] *Id.* at 32-34.
[12] *Id.* at 36.
[13] *Id*. at 37.

Amici Offer Mixed Views

As of the date of the writing of this article, three Amicus briefs have been filed: two in support of McWane and one in support of the FTC. Various law and economics professors called for reversal, suggesting that the Commission's decision will have a chilling effect on the often procompetitive benefits associated with exclusive dealing practices.[14] In particular, the professors criticized the lack of empirical evidence to support the decision, particularly given the Commission was ruling in a conduct case where data on actual market effects are available (as opposed to a merger case where enforcement is typically prospective). The United Steelworkers Union also filed a brief in support of McWane.[15] Its argument focused on the procompetitive benefit that the program had in maintaining the last domestic foundry owned by a DIPF manufacturer and in turn, preserving a skilled domestic workforce. The American Antitrust Institute ("AAI") filed a brief in support of the Commission.[16] AAI rejected the standard suggested by McWane that only "equally efficient competitors" need to be protected from abuse of monopoly power. Furthermore, AAI contended that evidence concerning the extent of foreclosure is not necessary, because as long as monopoly power is preserved by the alleged conduct, there is a direct harm from continued monopoly pricing.

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The *McWane* appeal presents interesting questions about market definition and the evidentiary burden in exclusive dealing cases. Oral argument had not occurred at the time this article was written, so there is no indication yet as to which way the panel will rule, but the court's decision certainly has the potential to provide additional guidance on the boundaries of permissible exclusive dealing. At a minimum, the case establishes a benchmark for the type of exclusive dealing harms that the current Commission will be concerned with in exercising its enforcement mandate via Section 5 of the FTC Act.

[14] Brief for Amicus Curiae Professors of Antitrust Law and Economics in Support of Defendant-Appellant Urging Reversal, *McWane, Inc. v. FTC*, No. 14-11363 (11th Cir. July 7, 2014) (Amicus Curiae: T. Arthur, Emory Univ.; R. Blair, Univ. Fl.; D. Boudreaux, George Mason Univ.; D. Crane, Univ. Mich.; R. Epstein, N.Y. Univ.; K. Elzinga, Univ. Va.; D. Geradin, George Mason Univ.; G. Hurwitz, Univ. Neb.; K. Hylton, Boston Univ.; T. Lambert, Univ. Mo.; G. Manne, Int'l Ctr. for Law & Economics; F. McChesney, Univ. Of Miami; T. Morgan, George Washington Univ.; B. Orbach, Univ. Az.; W. Page, Univ. Fl.; P. Rubin, Emory Univ.; M. Sykuta, Univ. Mo.; T. Zywicki, George Mason Univ.).
[15] Brief for Amicus Curiae United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union in Support of Defendant-Appellant Urging Reversal, *McWane, Inc. v. FTC*, No. 14-11363 (11th Cir. July 7, 2014).
[16] Brief of the American Antitrust Institute as Amicus Curiae in Support of Respondent, *McWane, Inc. v. FTC*, No. 14-11363 (11th Cir. Sept. 5, 2014).