IN THE MATTER OF

MCWANE, INC.
AND
STAR PIPE PRODUCTS, LTD.

OPINION OF THE COMMISSION AFFIRMING THE INITIAL DECISION AND FINAL ORDER IN REGARD TO ALLEGED VIOLATIONS OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket No. 9351; File No. 101 0080
Complaint, January 4, 2012 – Initial Decision, May 1, 2013
Opinion and Final Order, January 30, 2014

In January 2012, the Commission issued an administrative complaint against respondents McWane, Inc. ("McWane") and Star Pipe Products, Ltd. ("Star Pipe"), 155 F.T.C. 1482 (2013)., alleging that McWane and Star Pipe, along with their competitor Sigma Corporation, conspired in 2008 to raise and stabilize prices for imported ductile iron pipe fittings ("DIPF") and to maintain a monopoly in the market for domestic DIPF. Ductile iron pipe fittings are used in water distribution systems for the installation of valves, water meters, and hydrants, and to change the flow of water. The complaint alleged seven counts of violating Section 5 of the FTC Act, including restraint of trade, unfair methods of competition, conspiracy to monopolize, monopolization, and attempted monopolization. Prior to issuing its complaint, the Commission entered a separate consent agreement settling charges against Sigma Corporation. After the complaint issued, respondent Star Pipe also entered into a consent agreement with the Commission, resolving the Commission's competitive concerns.

Following an administrative trial, Administrative Law Judge D. Michael Chappell issued an Initial Decision, 155 F.T.C. 903 (2013), dismissing the first three counts of the complaint and upholding the remaining four counts. In dismissing the first three counts of the complaint, the court found the Commission failed to establish (1) that McWane illegally conspired with Sigma Corporation and Star Pipe to raise and stabilize prices for imported DIPF; (2) that McWane conspired with its competitors to exchange competitively sensitive sales information; and (3) that McWane invited competitors to collude on prices in the imported DIPF market. However, the court held that the preponderance of the evidence showed that McWane engaged in monopolistic practices, attempted to monopolize, engaged in a conspiracy to monopolize and engaged in an unreasonable restraint of trade with Sigma Corporation in the market for domestic DIPF. The court further found that the evidence supported the existence of a separate product market for domestic DIPF. The court further issued an order requiring McWane to cease and desist from certain conduct within the DIPF market, including allocating or dividing DIPF markets; agreeing with competitors not to compete in the DIPF market; entering into certain types of exclusivity agreements; entering into certain retroactive customer sales incentives; and retaliating or discriminating against customers.

OPINION OF THE COMMISSION

By Chairwoman Edith Ramirez,

I. INTRODUCTION

In this decision we address alleged anticompetitive conduct by respondent McWane, Inc. in the ductile iron pipe fittings industry. Pipe fittings join together pipes and help direct the flow of pressurized water in pipeline systems. They are sold to municipal and regional water authorities and their contractors for waterworks projects, and are distributed mainly through independent wholesalers.

The U.S. market for the sale of small and medium diameter ductile iron pipe fittings (hereafter "fittings") is an oligopoly. Three firms--McWane, Star Pipe Products, Ltd., and Sigma Corporation--account for over 90% of fittings sales in the United States. McWane is the industry leader with a market share of about 45-50%; Sigma and Star are second and third, respectively, with shares of roughly 30% and 20%. IDF 355-56.

Complaint Counsel alleges that McWane engaged in unlawful collusion, information exchange, and exclusionary conduct. The first three counts of the Complaint relate to an alleged McWane-led conspiracy to raise and stabilize fittings prices in 2008. According to Complaint Counsel, McWane, Sigma, and Star conspired to curtail "project pricing," a form of discounting that is the main form of price competition in the industry. Counts 4 through 7 focus on alleged efforts by McWane in 2009 to maintain its monopoly in the market for domestically-manufactured fittings. In particular, Complaint Counsel charges that McWane entered into a Master Distribution Agreement (the "MDA") with Sigma to prevent Sigma from becoming an independent competitor in domestic fittings and imposed an exclusive dealing policy on its distributors to stop Star from becoming a viable rival. The Administrative Law Judge ("ALJ") found that Complaint Counsel failed to establish liability on

Counts 1 through 3 but held McWane liable on Counts 4 through 7. Both McWane and Complaint Counsel have appealed.[1]

On *de novo* review, we affirm the ALJ and find McWane liable on Count 6 for unlawfully maintaining its monopoly in the domestic fittings market. We dismiss all of the remaining counts. Specifically, two Commissioners find that Counts 1 and 2 alleging an unlawful conspiracy and information exchange have been proven and two Commissioners do not. In the absence of a majority decision, we dismiss these counts in the public interest. We reverse the ALJ on Count 4 and conclude that Complaint Counsel failed to establish that the distribution relationship under the MDA between Sigma and McWane was unlawful. In light of our conclusions on Counts 4 and 6, we find it unnecessary to reach Count 5, alleging that McWane and Sigma conspired to monopolize the domestic fittings market through their distribution agreement, and Count 7, alleging that McWane's exclusive dealing policy constituted attempted monopolization of the domestic fittings market.

Having found liability on Count 6, we enter an order remedying McWane's exclusionary conduct and imposing certain fencing-in requirements designed to prevent the unlawful conduct from recurring.[2]

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1 Of the counts dismissed by the ALJ, Complaint Counsel appealed Counts 1 and 2, but not Count 3, which alleged that McWane invited Sigma and Star to collude to fix prices. McWane appealed all four counts on which the ALJ found liability.

2 This opinion uses the following abbreviations for citations to the record:

ID:	Initial Decision of the Administrative Law Judge
IDF:	Numbered Findings of Fact in the ALJ's Initial Decision
CX:	Complaint Counsel's Exhibit
CCAppB:	Complaint Counsel's Appeal Brief
CCAnsB:	Complaint Counsel's Answering Brief to Respondent's Appeal Brief
CCRB:	Complaint Counsel's Reply Brief
RX:	Respondent's Exhibit
Tr.:	Transcript of Trial before the ALJ
JSLF:	Joint Stipulations of Law and Fact
RAppB:	Respondent's Appeal Brief
RAnsB:	Respondent's Answering Brief to Complaint Counsel's Appeal Brief

II. PROCEDURAL HISTORY

A. THE ALLEGATIONS

On January 4, 2012, the Commission issued a seven-count administrative complaint against McWane and Star after Sigma had separately entered into a consent agreement with the Commission. Later, on May 12, 2012, Star also entered into a consent agreement, and McWane remained the only respondent in the case.

Count 1 of the Complaint charges a violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, focusing on two rounds of price increases in the fittings market, the first in January 2008 and the second in June 2008. With respect to the January increase, the Complaint alleges that McWane devised a plan to trade its support for higher list prices in exchange for Sigma's and Star's curtailment of "project pricing"; that McWane communicated the terms of its plan to Sigma and Star; and that "Sigma and Star manifested their understanding and acceptance of McWane's offer by publicly taking steps to limit their discounting from published price levels." Complaint ¶¶ 31-32, 64. The Complaint further alleges, with respect to the June price increase, that McWane traded its support for higher prices in exchange for monthly shipment information from Sigma and Star disseminated through their industry association, the Ductile Iron Fittings Research Association ("DIFRA"). *Id*. ¶¶ 33-34.

Count 2 alleges that McWane's agreement to exchange information through DIFRA facilitated collusion and is therefore an independent violation of Section 5. In particular, the Complaint asserts that the exchange of aggregated data regarding the firms' fittings shipments, including shipment information typically no more than two months old, "enabled each of the Sellers to determine and to monitor its own market share and, indirectly, the output levels of its rivals," and "[i]n this way, . . . facilitated price coordination among the Sellers on the pricing of [fittings]." *Id*. ¶¶ 35-36.

The remaining counts relate to the domestic fittings market. McWane, as the only major supplier with domestic production capability, is alleged to be a monopolist in that market. The

Complaint alleges that the February 2009 enactment of the American Recovery and Reinvestment Act of 2009 ("ARRA"), which conditioned funding on the use of domestically-produced fittings, "significantly altered the competitive dynamics of the [fittings] industry, and upset the terms of coordination" among McWane, Sigma, and Star by spurring Sigma and Star to seek to enter the domestic fittings market. *Id*. ¶¶ 3, 18, 44. Counts 4 through 7 are based on McWane's alleged efforts to exclude competitors from this market.

Count 4 charges that McWane entered into the MDA with Sigma to prevent Sigma from becoming an independent competitor in the domestic fittings market, and therefore that the MDA unreasonably restrains trade. *Id*. ¶¶ 48, 67. Count 5 alleges that McWane and Sigma entered into the MDA to monopolize the domestic fittings market and exclude their rivals. *Id*. ¶ 68. In Counts 6 and 7, the Complaint alleges that McWane adopted a restrictive and exclusive distribution policy to impede or delay the ability of Star and others to enter the domestic fittings market. *Id*. ¶¶ 57, 61. Count 6 charges McWane with monopolization, and Count 7 alleges that McWane engaged in attempted monopolization. *Id.* ¶¶ 69-70.

In its Answer, McWane denied all of the substantive allegations of the Complaint.

B. SUMMARY DECISION MOTIONS AND TRIAL

In August 2012, both parties moved for summary decision. McWane sought summary decision on all counts. Complaint Counsel sought summary decision on one episode of alleged price-fixing involving McWane and Star in the Spring of 2009. The Commission denied both motions, concluding that a trial was necessary to resolve disputed issues of fact. *In re McWane, Inc. & Star Pipe Prods., Ltd.*, Docket No. 9351, Order and Decision Denying Respondent's Motion for Summary Decision and Complaint Counsel's Motion for Partial Summary Decision, August 9, 2012.

The evidentiary hearing before Administrative Law Judge D. Michael Chappell commenced on September 4 and concluded on November 2, 2012. Complaint Counsel called 15 fact witnesses, including executives from McWane, Star, and Sigma, and an economic expert, Dr. Laurence Schumann. McWane called one witness, economic expert Dr. Parker Normann.

C. The Initial Decision

On May 1, 2013, the ALJ issued a 464-page opinion. He dismissed the first three counts relating to the alleged price conspiracy, concluding that Complaint Counsel had failed to establish liability by a preponderance of the evidence. He explained that "Complaint Counsel's conspiracy theory is not implausible; it is indeed 'possible' that there is some truth in the story Complaint Counsel tells." ID at 351. However, he found that, "[w]hen fairly and objectively scrutinized and weighed, the evidence fails to prove that McWane conspired with Sigma and Star to raise and stabilize prices in the Fittings market." *Id.* "At best," he concluded, "the evidence shows interdependent or consciously parallel conduct, unaided by an agreement, which is not illegal." *Id*.

With respect to Count 2, the ALJ found that the agreement by McWane, Star, and Sigma to participate in the DIFRA information exchange was not an unlawful facilitating practice. He reasoned that while Complaint Counsel had shown that the fittings market was an oligopoly susceptible to tacit coordination, the nature of the information exchanged—aggregated, historic shipment volumes—was insufficiently specific and not the type of information, like pricing-related data, that can facilitate price coordination. ID at 352-62.

The ALJ ruled in favor of Complaint Counsel with respect to Counts 4 through 7. On Count 4, the ALJ found that by entering into the MDA with Sigma, McWane had unreasonably restrained trade in the domestic fittings market. The ALJ focused on the provisions of the MDA that barred Sigma from producing its own domestic fittings and required Sigma to charge prices close to those charged by McWane. He concluded that, although the evidence failed to show that Sigma was a potential competitor in the domestic fittings market, the availability of reasonable, less restrictive alternatives and the absence of any valid procompetitive justifications rendered the MDA unlawful under the rule of reason. ID at 433-37. The ALJ also determined that, through the MDA, McWane had conspired with Sigma to monopolize the domestic fittings market, as alleged in Count 5. ID at 445. As to Count 6, he found that sales requiring domestic fittings constituted a separate product market in which McWane held monopoly power. He ruled that McWane's so-called "Full Support Program" was an exclusive dealing arrangement that foreclosed Star from a substantial share of the domestic fittings market and thereby unlawfully maintained McWane's monopoly. The ALJ also found that this conduct amounted to attempted monopolization of the domestic fittings market, as alleged in Count 7. ID at 419.

On May 13, 2013, the parties filed timely notices of appeal. Complaint Counsel appeals the ALJ's ruling with respect to Counts 1 and 2, and McWane appeals his findings on Counts 4 through 7.

III. FACTUAL BACKGROUND[3]

A. THE DUCTILE IRON PIPE FITTINGS INDUSTRY

Fittings are small but essential components of pressurized water distribution and treatment systems. They are used to join pipes, valves and hydrants, and to change, direct or divide the flow of water. IDF 5, 278. Although there are several thousand unique configurations of fittings in different shapes, sizes and coatings, approximately 80% of the demand may be serviced with only about 100 commonly-used fittings. IDF 286, 306.

Fittings are commodity products produced to American Water Works Association ("AWWA") standards and can be made anywhere in the world. Any fitting that meets AWWA specifications is functionally interchangeable with other fittings made to that standard, regardless of the country of origin. IDF 322-23. Despite the commodity nature of these fittings, however, some waterworks projects are closed to bids that include fittings made outside of the United States. IDF 346. A "domestic" or "domestic-only" specification or project requires fittings manufactured in the United States because of either end-user

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3 Because there is no majority position with respect to Counts 1 and 2, the facts described herein are limited to those relevant to Counts 4 through 7.

preferences or legal procurement requirements. IDF 347-48, 519-23. Projects that do not require domestic fittings are referred to as "open specification" projects. IDF 349. Domestic fittings sold for use in projects with domestic-only specifications generally command substantially higher prices than imported fittings or domestic fittings sold for use in projects with open specifications. IDF 547, 1075-76.

A few decades ago, most fittings were manufactured in the United States, and there were a number of full-line domestic fittings manufacturers, including U.S. Pipe and Foundry Co. ("U.S. Pipe"), Griffin Pipe Products Co., and American Cast Iron Pipe Co. ("ACIPCO"), as well as McWane. IDF 462. However, in the mid-1980s, importers, including Star and Sigma, began to make significant inroads, and, by 2005, imported fittings made up the vast majority of sales. IDF 463, 465-67. Faced with competition from lower-cost and lower-priced imports, several domestic manufacturers, including U.S. Pipe, Griffin, and ACIPCO, dramatically reduced or ceased domestic fittings production. IDF 472-76. From April 2006 until Star entered the domestic fittings market in late 2009, McWane was the only significant supplier of domestic fittings. IDF 1040.

B. FITTINGS INDUSTRY SUPPLIERS

1. McWane

McWane manufactures, imports, and sells various products for the waterworks industry, including fittings, which account for about 5% of McWane's business. Its principal place of business is in Birmingham, Alabama. IDF 1-2, 13. Until November 2008 McWane produced fittings at two foundries, one in Anniston, Alabama, and the other in Tyler, Texas. IDF 15. In 2005, it also began producing fittings in China, and in 2007 it consolidated its fittings business into a single division, Tyler/Union. IDF 17. Faced with high levels of inventory and low demand, McWane closed the Tyler, Texas foundry in November 2008. IDF 18.

The key McWane employee for purposes of this case is Mr. Richard Tatman, who joined the company in May 2006 and became Vice President and General Manager in charge of Tyler/Union in 2007. IDF 20-27.

2. Sigma

Based in Cream Ridge, New Jersey, Sigma has imported and sold a range of waterworks products, including fittings, in the United States since roughly 1985. IDF 51. Sigma sells to distributors and original equipment manufacturers, making it both a competitor and supplier to McWane. IDF 59-60. Fittings are Sigma's primary product line, accounting for 40-45% of its revenues in 2008 and 2009. IDF 52. Unlike McWane, Sigma has no production facilities. It uses a "virtual manufacturing" model, providing technical know-how and quality control but relying on foundries in China, Mexico, and India for the manufacture of its fittings. IDF 57.

The Sigma employees most relevant here include Victor Pais, one of Sigma's founders and its CEO and President (IDF 64-69), and Mitchell Rona, Sigma's OEM business manager (IDF 82).

3. Star

Star also imports and sells fittings and a variety of other waterworks products. IDF 108. It was founded in 1981 and has sold fittings since approximately 1985. IDF 109. Like Sigma, fittings are Star's primary product line, accounting for about 50% of Star's total sales. IDF 111. It sources its fittings primarily from foundries in China. IDF 113. However, beginning in 2009, Star contracted with a number of U.S. foundries to produce domestic fittings in competition with McWane. IDF 112.

4. Others

There are also a number of pipe and other companies that manufacture or sell certain types and sizes of fittings as ancillary product lines, but none is a significant supplier. IDF 154-57, 161-62, 164-67, 169-73, 176-81, 186-88, 190-93, 196-99.

C. MARKET STRUCTURE

The fittings market is an oligopoly with three major suppliers: McWane, Star, and Sigma. Together they account for over 90% of all fittings sold in the United States. IDF 354-55, 362. During the relevant time period, McWane was the market leader with approximately [redacted]% of the market in 2008; Sigma had about [redacted]% of the market that year, and Star roughly [redacted]%. IDF 356, *in camera*. As of 2008, Sigma and Star only sold fittings manufactured abroad, primarily in China. IDF 56, 113-15. As discussed further below, in late 2009, Star began selling fittings produced by several U.S. foundries in response to the passage of ARRA. IDF 112, 1094-1113, 1127-29. By 2010, Star accounted for about [redacted]% of domestic fittings sales and by 2011 about [redacted]%. IDF 357, *in camera*.

McWane, Sigma, and Star sell fittings to wholesale waterworks distributors, which then resell them to end users, typically municipalities, regional water authorities, and contractors. IDF 363, 367, 373-74. There are two national distributors: HD Supply and Ferguson, which together account for about 60% of the overall waterworks distribution market. IDF 222, 227, 377-79. There are also a few regional distributors, as well as hundreds of local ones. IDF 236-277, 375. Most distribution business is conducted on a bid-by-bid basis, with distributors competing on the basis of service as well as price. IDF 383-84, 386-87.

D. PRICING

Fittings prices have two main components: (i) a nationwide list price, typically issued by suppliers once a year or even less frequently; and (ii) published "multipliers," which vary by region and are discounts off the list price. IDF 413, 416-19. The "published" or "standard" price for a given fitting is the list price multiplied by the applicable regional multiplier. IDF 414.

Virtually no customer buys fittings at the list price. IDF 418. At the very least, sale prices usually reflect the multiplier discount. IDF 425. Suppliers often also offer a variety of other price concessions, the most important of which are discounts variously referred to as "job prices," "special prices," or "project prices," which are discounts off the published or standard price. IDF 428, 430-33. Project prices are the primary form of price competition among suppliers, but, unlike the published list prices and multipliers, they are not transparent. IDF 435, 442.

E. DOMESTIC FITTINGS, THE FULL SUPPORT PROGRAM, AND THE MASTER DISTRIBUTION AGREEMENT

1. Expected Growth in Sales of Domestic Fittings

In February 2009, Congress passed ARRA, which allocated more than $6 billion to water infrastructure projects. JSLF ¶¶ 19-20; IDF 524. Waterworks projects funded by ARRA were required to use domestically manufactured fittings and to be "under contract or under construction" within 12 months of ARRA's enactment.[4] IDF 525-27.

Given the anticipated increase in domestic fittings demand due to ARRA funding, both Star and Sigma began exploring options to enter the market. IDF 1094, 1421. In June 2009, Star sent a letter to customers and publicly announced at an AWWA industry conference that it would offer domestic fittings starting in September 2009. IDF 1095-96. Sigma initially considered two approaches for entering the domestic fittings market—purchasing Sigma-branded fittings manufactured by McWane or producing domestic fittings by contracting with independent domestic foundries. IDF 1423. In April 2009, Sigma contacted McWane to ask that it supply Sigma with "private label" domestic fittings, advising McWane that Sigma would pursue its own domestic production if McWane did not supply it with domestic fittings. IDF 1425-26.

The possible entry of Star and Sigma into the domestic fittings market created significant concerns for McWane. Not surprisingly, McWane did not want to share domestic sales and worried that entry by Star and Sigma would threaten to undermine its domestic fittings prices. IDF 1148-49, 1151-53.

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4 During the distribution of funds provided by ARRA, the Environmental Protection Agency granted certain waivers of the "Buy American" requirement. IDF 530-46. These included public interest waivers, cost waivers if using domestic materials resulted in an overall cost increase of more than 25%, and waivers when domestic materials were unavailable in adequate quantities. IDF 531-33.

2. Development of McWane's Full Support Program

By May 2009, the Vice President and General Manager in charge of McWane's fittings business, Mr. Tatman, was developing McWane's strategic response to possible domestic entry. He noted in a May 26 "brainstorming" document that any competitor seeking to enter the domestic fittings market could face "significant blocking issues" if they lacked a full line of domestic fittings. IDF 1155. A few weeks later, in a June e-mail exchange with other McWane executives about how to deal with entry, Mr. Tatman laid out his strategic vision for protecting McWane. He wrote:

> [A]t this stage the chance for profitable cohabitation with Star owning a [piece] of the Domestic market is slim. . . . If their claims are ahead of their actual capabilities we need to make sure that they don't reach any critical market mass that will allow them to continue to invest and receive a profitable return. . . . I don't sense that Sigma is yet fully committed and they will be watching our response very closely to assess their strategy and probability of financial success.

IDF 1150.

As of late June, Mr. Tatman had developed three potential options for McWane's response to domestic entry: "Wait and See"; "Handle on a Job by Job basis"; or "Force Distribution to Pick their Horse." CX0076 at 009. He explained the advantages of the third approach: (1) "Avoids the job by job auction scenario within a particular distributor"; (2) "Potentially raises the level of supply concern among contractors"; and (3) "Forces Star/Sigma to absorb the costs associated with having a more full line before they can secure major distribution[.]" *Id.* When considering how to implement such a program, Mr. Tatman outlined a "Soft Approach" in which a "Domestic rebate would require exclusivity," and a "Hard Approach – Full Line or No Line," whereby access to McWane's domestic fittings would "require[] exclusivity for Domestic fitting items we manufacture." *Id.* at 010.

By August, McWane had determined to implement an exclusive dealing requirement for distributors. Mr. Tatman explained the plan: "To protect our domestic brands and market position we are going to adopt a distributor exclusivity program for 2010 wherein we won't provide domestic product to distributors who are not fully supporting our domestic product lines." CX0113 at 001. McWane's management emphasized to its sales staff that the "new policy" meant that "if a customer buys Star domestic . . . the customer will no longer have access to [McWane] domestic [fittings]." IDF 1179.

3. McWane Announces and Implements the "Full Support Program"

McWane announced its exclusive dealing policy, called the "Full Support Program," in a September 22, 2009 letter to distributors. IDF 1173. McWane's executives and sales force proceeded to contact customers to discuss the program, explaining it would be applied to them on a "company-wide basis"—if one branch purchased domestic fittings from Star, "all branches would be cut off." IDF 1180-82. There were only two exceptions permitting the purchase of another company's domestic fittings: where McWane products were not readily available or where the customer bought domestic fittings and accessories along with another manufacturer's ductile iron pipe. IDF 1173.

The message was received, and nearly all customers believed they would lose rebates or be cut off from purchasing McWane's domestic fittings if any branch bought domestic fittings from Star. IDF 1184-85, 1188-89, 1191-92, 1300. As a consequence, unless an exception applied, major distributors purchased only from McWane. *See* IDF 1231-51, 1259-64, 1299-1304, 1334-40, 1313-18, 1353-58, 1364.

McWane's enforcement of the Full Support Program was consistent with what it had described to customers. Distributor Hajoca Corporation provides one example. Because Hajoca's branches operated independently, Hajoca asked McWane to modify the Full Support Program so that not all Hajoca branches would be penalized if one branch bought from Star. McWane refused. IDF 1197-1202. Later, when Hajoca's Tulsa branch purchased Star domestic fittings, McWane cut off sales of its domestic fittings to all Hajoca branches, including branches that had complied with the program. IDF 1206-13. As a result, Hajoca was unable to place any new domestic fittings orders with McWane between December 4, 2009, and April 13, 2010 (IDF 1219), and McWane withheld its rebates for the fourth quarter of 2009 (IDF 1224-27, 1230).[5]

4. Impact of McWane's Exclusive Dealing Policy on Star

Following McWane's announcement of the Full Support Program, Star saw a dramatic reduction in the number of requests for quotes. IDF 1381-82. Numerous distributors pulled their outstanding bid requests from Star. IDF 1382. Conversations with customers led Star to believe that McWane's policy made customers less willing to risk purchasing domestic fittings from Star.[6] IDF 1382-92; Bhargava, Tr. 2960, *in camera*. Star was rebuffed by some distributors even after offering a more generous rebate than McWane. IDF 1391. Star estimated that it would have secured [redacted] in sales of domestic fittings in 2010, and potentially as much as [redacted] in 2011, but for McWane's Full Support Program. IDF 1394, *in camera*. Star's actual sales in 2010 were approximately [redacted], less than half of the sales it estimated it would have garnered in the absence of McWane's program. IDF 1396, *in camera*. Star's revenue from domestic fittings declined to [redacted] in 2011, or roughly one-third of its estimated sales in the absence of McWane's program. IDF 1397, *in camera*. [redacted] IDF 1399, *in camera*.

Despite McWane's program, distributors did make some purchases from Star. Hajoca's Tulsa branch began purchasing

5 Although McWane cut off new orders, McWane allowed Hajoca branches, except Tulsa, to place orders to satisfy known commitments of existing contracts. IDF 1214.

6 A number of distributors testified they were reluctant or unwilling to purchase domestic fittings from Star because of McWane's Full Support Program; some also identified other factors that contributed to their decisions not to purchase from Star. *See* IDF 1252-55, 1271-75, 1307, 1341-42, 1359-62.

domestic fittings from Star soon after McWane's announcement of the Full Support Program, and by January 2010, had ordered more than [redacted] worth of Star domestic fittings. IDF 1230, *in camera*. Additionally, many distributors made purchases under the exceptions allowed by the Full Support Program. *See* IDF 1137, 1142, 1242, 1305. For example, HD Supply cancelled pending orders with Star after McWane announced its program, but retained orders for items McWane did not have available or for which a commitment had already been made before the announcement of the Full Support Program. IDF 1242. In all, Star sold to over 100 distributors from the time it entered the market through 2011. IDF 1141. Altogether, however, the sales made by Star were small compared to the overall size of the market. IDF 1396-99, 1042-43.

Star's sales levels had direct implications for its domestic fittings operations. Star had considered three possible manufacturing approaches for entering the market: building a foundry from "ground zero," buying an existing foundry, or contracting with existing domestic foundries to produce the desired fittings. IDF 1097. The cost of sourcing from independent foundries is higher because they are less specialized, which means they have less efficient equipment, run smaller batch sizes, and have higher labor costs, and because they charge a markup on each fitting, sometimes as much as [redacted]%. IDF 1410, 1411, *in camera*, 1412-13. Star believed its sales level was insufficient to justify running its own foundry. IDF 1400-01.

In the end, because it could not expand its sales more quickly, rather than acquiring a foundry, Star contracted with six foundries to produce raw castings, which Star then shipped to its Houston facility for finishing. IDF 1409. Shipping costs alone to Star's Houston finishing facility added [redacted]% to the cost of Star's domestic fittings. IDF 1411, *in camera*. Star estimated that the cost of producing fittings at its own domestic foundry would have been [redacted]% lower than the cost of contracting with independent foundries, and that it could have reduced its domestic fittings prices by [redacted]%. IDF 1419-20, *in camera*.

5. Sigma's Efforts to Enter the Domestic Fittings Market

In April 2009, at the same time as it was developing its exclusive dealing policy, McWane was also responding to a request from Sigma that McWane supply Sigma with "private label" domestic fittings. IDF 1425, 1429. McWane's Mr. Tatman recognized that if McWane did not sell to Sigma, McWane would retain the full margin for its domestic fittings sales, but also realized that by selling to Sigma it could "eliminate the probability" that Sigma would find another domestic fittings source. IDF 1431-39, 1442.

On June 5, McWane made an initial offer to sell domestic fittings to Sigma at 5% off McWane's published prices. IDF 1443. Sigma rejected that offer because it did not allow sufficient margin to cover its operating costs. IDF 1444-45. Sigma then informed McWane that it planned to develop its own domestic fittings capability. IDF 1509-10.

While negotiating with McWane, Sigma tasked a team of executives to investigate the possibility of entering the domestic fittings market using independent foundries. IDF 1446-47. The team held planning meetings that resulted in detailed action plans. IDF 1454. When Sigma rejected McWane's June 5 offer, Sigma's president stated in an update to the Board, "We now need to go all out and implement a [domestic] plan - replicating SIGMA's 'virtual manufacturing' model working with a collection of domestic foundries who have ample idle capacity, to produce the range of Fittings, just as we do thru a collection of facilities overseas." IDF 1455. By June, Sigma's team had begun to take steps to implement a virtual model. They obtained patterns, arranged foundry site visits, placed orders for foam patterns and other equipment, and produced two large sample domestic fittings as trial runs at a foundry in Tennessee. IDF 1457-61. All told, Sigma spent between $50,000 and $75,000 investigating domestic production options. IDF 1449.

As of July 11, Sigma was still pursuing its plan to produce domestic fittings, but it was proceeding more "deliberately and thoughtfully" because it was finding the plan difficult to implement. IDF 1463. Sigma was also in a financially precarious situation and had limited access to capital. IDF 1483, 1487, 1499. At that point, Sigma had no domestic foundries, no contracts with existing domestic foundries, no core boxes, no machining facilities, and no finishing facilities or contracts for coating, painting, and lining, for domestic fittings. IDF 1465.

In September, Sigma still had very few of the patterns it would need to make domestic fittings, did not have any contracts with any pattern shops to build the necessary patterns, and did not have any contracts with any domestic foundries to produce fittings. IDF 1470-73. Ultimately, Sigma decided against producing its own domestic fittings. IDF 1545. Mr. Pais of Sigma informed the Board that "the entire project was found to be too overwhelming and cumbersome" and would have required "a sizeable Capital Expenditure." IDF 1474.

6. McWane and Sigma Enter Into the Master Distribution Agreement

In late June or early July 2009, Mr. Rona of Sigma resumed discussions with McWane. IDF 1522. On July 29, McWane offered to sell McWane-branded domestic fittings to Sigma at a 20% discount off published multipliers, but required that McWane be Sigma's sole source of domestic fittings (other than for fittings that McWane did not produce or could not ship promptly). IDF 1529; CX1805 at 002. The offer also required Sigma to agree to sell the McWane fittings only to distributors that had an exclusive supply relationship with McWane. IDF 1529.

Negotiations continued through August and September. On September 17, McWane and Sigma signed the MDA. IDF 1537. Under the agreement, Sigma agreed to act as an authorized distributor of McWane's domestic fittings on the following key terms: (1) McWane would be Sigma's sole domestic fittings source, unless certain limited exceptions applied; (2) Sigma could resell McWane's fittings at any price, but McWane could cancel the agreement if Sigma's price was less than 98% of McWane's published pricing on a weighted average basis; (3) Sigma could resell only to customers that agreed to purchase McWane domestic fittings exclusively; and (4) there would be an initial term of one year, but either party could terminate the agreement with or without cause by giving 180 days' advance written notice.

CX1194 at 001-002, 007. McWane announced the MDA to customers in the same September 22, 2009 letter that announced the Full Support Program. CX0010.

Sigma's subsequent actions were consistent with the MDA. It ceased efforts to develop its own domestic manufacturing capability. IDF 1543-47. Sigma also priced domestic fittings as prescribed by the MDA and implemented McWane's exclusive dealing program. IDF 1548-53, 1566-74. Additionally, when McWane cut off the supply of domestic fittings to Hajoca, Sigma followed suit. *See* IDF 1568-70.

On February 17, 2010, McWane provided Sigma with 180 days' notice that McWane wished to terminate the MDA. IDF 1595. In all, the MDA was in effect from September 2009 to August 2010. IDF 1596.

IV. STANDARD OF REVIEW

The Commission reviews the ALJ's findings of facts and conclusions of law *de novo*, considering "such parts of the record as are cited or as may be necessary to resolve the issues presented." 16 C.F.R. § 3.54. The Commission may "exercise all the powers which it could have exercised if it had made the initial decision." *Id*. The *de novo* standard of review applies to both findings of fact and inferences drawn from those facts. *See Realcomp II, Ltd.*, No. 9320, 2009 FTC LEXIS 250 at *37 n.11 (Oct. 30, 2009), *aff'd*, *Realcomp II, Ltd. v. FTC*, 635 F.3d 815 (6th Cir. 2011).

V. MCWANE'S EXCLUSIVE DEALING POLICY AS MONOPOLY MAINTENANCE

Complaint Counsel alleges that McWane adopted an exclusionary distribution policy in order to maintain its monopoly in the domestic fittings market in violation of Section 5 of the FTC Act.[7] A claim of monopolization requires proof of "(1) the

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7 Violations of the Sherman Act also constitute "unfair methods of competition" under Section 5 of the FTC Act. *See California Dental Ass'n v. FTC*, 526 U.S. 756, 762 & n.3 (1999); *FTC v. Motion Picture Adver. Serv. Co.*, 344 U.S. 392, 394-95 (1953). Accordingly, we rely on case law and other authority applying the Sherman Act for our analysis of the relevant claims.

possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966). As the Supreme Court underscored in *Spectrum Sports, Inc. v. McQuillan*, "[t]he law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself." 506 U.S. 447, 458 (1993). Accordingly, the Commission must first determine whether McWane has monopoly power in a relevant market, and, if it does, whether McWane acted to maintain its monopoly through anticompetitive conduct. *United States v. Microsoft*, 253 F.3d 34, 79 (D.C. Cir. 2001). As discussed below, we answer both questions in the affirmative and conclude that McWane unlawfully maintained its monopoly of the domestic fittings market.

A. MONOPOLY POWER

A monopolist is defined as a firm that can "profitably raise prices substantially above the competitive level." *Microsoft*, 253 F.3d at 51. Monopoly power can be shown directly, through evidence of the defendant's control over prices or its ability to exclude competition from the market, or indirectly, by examining market structure and a firm's market share. *See Grinnell Corp.*, 384 U.S. at 571. Because direct evidence of monopoly power is often unavailable, courts have traditionally inferred it from "a firm's possession of a dominant share of a relevant market that is protected by entry barriers." *Microsoft*, 253 F.3d at 51. We start by addressing the relevant market and then turn to whether McWane has monopoly power in that market.

1. Domestic Fittings Sold for Use in Projects with Domestic-Only Specifications Are a Relevant Market

A relevant product market consists of "products that have reasonable interchangeability for the purposes for which they are produced." *United States v. E. I. duPont de Nemours & Co.*, 351 U.S. 377, 404 (1956). Courts typically evaluate the reasonable interchangeability of use and the cross elasticity of demand in assessing a potential relevant market, focusing on "the availability of products that are similar in character or use to the product in question and the degree to which buyers are willing to substitute those similar products for the product." *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 157 (D.D.C. 2000).

We agree with the ALJ that there are two relevant product markets in this case. One is comprised of small and medium (*i.e.*, 24 inches and smaller) diameter ductile iron pipe fittings sold in the United States for use in open specification waterworks projects (the "fittings market"). *See* ID at 244, 252-53, 450. There are no reasonable substitutes for ductile iron pipe fittings. The closest substitute is made from polyvinyl chloride ("PVC"), but because PVC fittings lack the strength of ductile iron pipe fittings and thus are not suitable for high pressure applications, the two are not reasonably interchangeable. ID at 246-47. We also find that it is appropriate to group all ductile iron pipe fittings 24 inches and smaller in diameter into a single product market for the purpose of evaluating competitive effects. *See* ID at 244-46 (explaining "cluster" markets); *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 356 (1963) (finding that a cluster of products and services comprising "commercial banking" was a relevant market); *In re ProMedica Health Sys., Inc.*, 2012 FTC LEXIS 58, at *48-55, *62-72 (Mar. 28, 2012) (describing conditions that make it appropriate to delineate cluster markets). Domestically-manufactured and imported fittings are both used in open specification jobs and are therefore both included in the fittings market. This relevant market is not in dispute.

We also find there is a separate relevant market for the supply of domestically-manufactured fittings for use in waterworks projects with domestic-only specifications (the "domestic fittings market"). This is the market that McWane contests.

Product markets are sometimes defined by considering whether a hypothetical monopolist could profitably target a particular subset of customers for price increases. Where existing buyers differ significantly in their likelihood of switching to other products in response to a small but significant and nontransitory increase in price, and a hypothetical monopolist can identify and price differently to targeted buyers that cannot defeat the price increase by substituting other products, there is a "price discrimination" market. In such a case, the hypothetical monopolist would profitably impose a discriminatory price increase on sales to the targeted buyers, and those buyers would define the boundaries of the relevant market. *See* Dep't of Justice and Fed. Trade Comm'n, Horizontal Merger Guidelines § 4.1.4 (2010) ("Horizontal Merger Guidelines"); Phillip E. Areeda, Herbert Hovenkamp & John L. Solow, IIB *Antitrust Law* ¶ 534d.1, at 269 (3d ed. 2007) ("Successful price discrimination means that the disfavored geographic or product class is insulated from the favored class and, if the discrimination is of sufficient magnitude, should be counted as a separate relevant market.").

The supply of domestic fittings constitutes a price discrimination market. Certain waterworks projects require domestic-only fittings because of municipal, state, or federal law, or, sometimes, end-user preferences. IDF 347, 519; JX0001 at 002 (JSLF ¶ 13). For example, Pennsylvania and New Jersey both have "Buy American" laws governing fittings. IDF 348, 520-21. Certain federal government projects, Air Force bases, and municipalities also require domestic fittings. IDF 348, 519-23. Similarly, ARRA contained Buy American provisions requiring domestic fittings in the $6 billion worth of waterworks projects it funded. IDF 524-29. When a project requires domestic fittings, a distributor will not purchase imported fittings even though they have the same form and functionality. IDF 350, 549. Imported fittings therefore are not interchangeable with, or reasonable substitutes for, projects with domestic procurement specifications.

McWane capitalizes on this lack of interchangeability by charging higher prices for domestic fittings used in domestic-only waterworks projects. Answer ¶ 20; IDF 350-51. For instance, McWane's February 2008 price multipliers for domestic fittings sold into domestic-only specifications were substantially higher than its "blended" multipliers for domestically manufactured and imported fittings sold into open specifications, with the price differential ranging from 21.4% to 96%. IDF 1076. Indeed, due to the price differential between fittings sold into open and domestic-only specifications, McWane does not provide quotes for domestic fittings for open specification projects. IDF 548. Importantly, the price difference reflects McWane's ability to target particular customers based on project specifications, not a difference in the cost of production, which is the same for all domestically manufactured fittings.

These targeted price differences confirm that domestic fittings for use in projects with domestic-only specifications are a separate product market. Job specifications readily identify customers susceptible to discriminatory pricing and the persistence of distinct price levels shows that customers cannot use arbitrage to avoid the higher prices. *See Geneva Pharms. v. Barr Labs Inc.*, 386 F.3d 485, 496-98 (2d Cir. 2004) (finding that branded and generic versions of a drug, though "therapeutically equivalent," were in separate antitrust markets when users of the branded drug exhibited inelastic demand that was unresponsive to the lower prices of generic versions). Additionally, because customers can turn only to domestic producers in this relevant product market, the relevant geographic market is the United States. ID at 252-53.

McWane raises several arguments to dispute a domestic fittings market. None is persuasive. As an initial matter, it claims that econometric evidence is necessary to establish a product market and argues that the absence of such evidence here undermines a conclusion that a separate domestic fittings market exists. That is simply incorrect. Econometric analysis can be a valuable tool for defining a market, but it is only one of several that may be used for that purpose. Courts routinely rely on qualitative economic evidence to define relevant markets. *See, e.g.*, *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (recognizing that "practical indicia" such as industry or public recognition and a product's unique attributes can be used to define a relevant market); *Spirit Airlines, Inc. v. Northwest Airlines, Inc.*, 431 F.3d 917, 934-35 (6th Cir. 2005) (relying on party documents and fact and expert testimony to determine the relevant product market); *United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36, 50-71 (D.D.C. 2011) (finding digital do-it-yourself tax preparation software a relevant product market based mainly on defendant's documents, price disparities, and testimony from executives); *In re Polypore Int'l, Inc.*, 2010 FTC LEXIS 97, *31 & n.19 (Dec. 13, 2010) (relying on qualitative evidence to define relevant market), *aff'd*, 686 F.3d 1208, 1217-18 (11th Cir. 2012). As one treatise explains, "[i]n a world of imperfect price and quantity data from which to analyze elasticities, qualitative evidence of buyer's willingness to substitute one good or service for another often provides the principal evidence of the boundaries of a relevant market."[8] ABA Section of Antitrust Law, *Mergers and Acquisitions* 55 (3d ed. 2008). In this case, there is ample economic evidence to support domestic fittings as a relevant market.

McWane also disputes the lack of interchangeability between domestic and imported fittings. It argues that waterworks projects with legally-imposed domestic fittings requirements represent only a small fraction of all specifications, pointing to the increase in sales of imported fittings over time. But observations about the size of the domestic fittings market shed no light on the ability of customers to switch between domestic and imported fittings for domestic-only projects. As the ALJ found, "the evidence overwhelming[ly] showed [Buy American] regulations did in fact limit substitution." ID at 250.

McWane also claims that customers can "flip" specifications from domestic-only to open. The relevant testimony, however, indicates that flipping typically only occurs when domestic fittings are unavailable, rather than as the result of competition between domestic and imported fittings. *See* CX2496 at 006 (Brakefield Dep. at 18-20). In fact, the sole example in the record of flipping was an instance in which domestic fittings were unavailable to complete the job. *Id.* Moreover, while sales of imported fittings may have increased, the share of domestic-only specifications has remained largely unchanged in recent years. *Compare* IDF 1026 (in 2003, Buy American provisions applied to 10%-20% of fittings shipped), *with* IDF 1029 (prior to the passage of ARRA in 2009, projects with domestic-only specifications accounted for 15%-20% of sales). This suggests that any growth in import sales likely came from the greater use of imports in open-specification jobs and not from a decline in domestic-only projects.

8 The Commission's reliance on qualitative economic evidence is also well established. *See* Horizontal Merger Guidelines § 4.1.3 (noting that, in determining relevant markets, the antitrust agencies rely on "reasonably available and reliable evidence," including business documents, customer surveys, and past behavior); U.S. Dep't of Justice and Fed. Trade Comm'n, Commentary on the Horizontal Merger Guidelines 9 (2006) ("In the vast majority of cases, the Agencies largely rely on non-econometric evidence, obtained primarily from customers and from business documents.").

Finally, McWane argues that the Environmental Protection Agency's grant of waivers permitting the use of imported fittings on ARRA-funded projects--and Complaint Counsel's expert's failure to account for such waivers--precludes a finding that a domestic fittings market exists. But EPA-granted waivers were limited, and in any event had no impact on domestic-only requirements imposed by other federal, state, or municipal laws. IDF 531-33, 537. Notably, neither McWane nor Star sold any imported fittings for use in any ARRA-funded projects. IDF 538, 540. McWane even advised distributors that the cost-based exception to ARRA requirements was unlikely to apply to fittings sales. IDF 534. Sigma representatives testified that the quantities of imported fittings used on ARRA-funded waterworks projects were "few." IDF 539. Other suppliers, as well as distributors, also indicated they were unaware of any instances in which imported fittings were used for ARRA-funded projects. IDF 541-43, 544-46. Accordingly, McWane's protest that the potential for waivers offsets ARRA's Buy American requirements is unavailing.

2. McWane Possesses Monopoly Power in the Domestic Fittings Market

Having established that domestic fittings are a relevant market, we now consider whether McWane possessed monopoly power in that market. Both direct and indirect evidence show that it did.

We begin by looking at market structure. From late 2006 until late 2009 when Star entered the domestic fittings market, McWane was the only domestic manufacturer of fittings. IDF 476, 1040. McWane's share continued to be more than [redacted]% in 2010 and [redacted]% in 2011, after Star had entered the market. IDF 1042-43, *in camera*. These market shares far exceed the levels that courts typically require to support a *prima facie* showing of monopoly power. *See United States v. Dentsply Int'l, Inc.*, 399 F.3d 181, 188 (3d Cir. 2005) (holding that market share between 75% and 80% of sales is "more than adequate to establish a *prima facie* case of [monopoly] power"); *Colo. Interstate Gas Co. v. Natural Gas Pipeline Co. of Am.*, 885 F.2d 683, 694 n.18 (10th Cir. 1989) (noting that to establish "monopoly power, lower courts generally require a minimum market share of between 70%

and 80%"). Enduring high market-share figures provide particularly strong evidence of monopoly power, especially in a mature and stable industry such as this one. *See ZF Meritor LLC v. Eaton Corp.*, 696 F.3d 254, 285 (3d Cir. 2012) (recognizing competitors' "paltry penetration" in the market "over the years" as a sign of market power).

Moreover, there are substantial barriers to entry in the domestic fittings market. ID at 375-77; IDF 1050. A *de novo* entrant would need to build its own foundry or develop a supply chain of foundries to produce fittings, develop or purchase hundreds of patterns or moldings necessary to make a full line of fittings, have its products tested and certified to conform to AWWA standards and get on "approved" lists for engineers and municipalities, and develop a sales force and relationships with distributors. IDF 1044-48. As a result, a *de novo* entrant seeking to enter the fittings market would need approximately three to five years to do so. IDF 1049.

Even existing suppliers of imported fittings face significant barriers to enter the domestic fittings market. Although equipped with an existing sales team and relationships with customers, to enter this market a supplier of imported fittings would still need to build its own foundry or arrange for existing foundries to manufacture its fittings, obtain patterns for the 100-200 fittings necessary to enter with at least a partial line, and have its domestically-manufactured products tested and certified. IDF 1044-47, 1051-55, 1119-26, 1130-32. Additionally, as discussed more fully below, McWane's exclusive dealing policy raised a barrier to entry for even current suppliers of imported fittings, particularly those without a full line of fittings. *See Dentsply*, 399 F.3d at 189-90 (recognizing that the defendant's exclusionary conduct was a barrier to entry).

The record reflects the significance of these barriers. Although Star was able to and did enter the market, two other suppliers of imported fittings investigated entry, but were deterred from making the attempt. After considering the availability of domestic foundries, patterns, and other equipment, as well as its weak financial condition, Sigma concluded that it could not overcome the complexity of entering the domestic fittings market. Similarly, although Serampore Industries Private ("SIP"), a small seller of imported fittings, possessed the financial capability of entering, the challenges to entering the market, including the unavailability of a single foundry capable of supplying its full needs, the high cost of developing patterns and drilling and machining capabilities, and McWane's exclusive dealing program, led SIP not to attempt it. IDF 1366, 1368, 1373, 1375-79.

McWane argues Star's entry proves that barriers to entry are low and contradicts a finding of monopoly power. But, as the Ninth Circuit has noted, "[t]he fact that entry has occurred does not necessarily preclude the existence of 'significant' entry barriers." *Rebel Oil Co. v. Atlantic Richfield Co.*, 51 F.3d 1421, 1440 (9th Cir. 1995). "If the output or capacity of the new entrant is insufficient to take significant business away from the predator, they are unlikely to represent a challenge to the predator's market power." *Id.*; *accord Allen-Myland v. Int'l Bus. Mach. Corp.*, 33 F.3d 194, 210 (3d Cir. 1994) (rejecting district court's inference that existence of competitors demonstrated ease of entry that would disprove market power); *Reazin v. Blue Cross & Blue Shield of Kansas, Inc.*, 899 F.2d 951, 971-72 (10th Cir. 1990) (upholding a finding of monopoly power because "no other entrant remotely approached [defendant's] domination of the market").

The evidence here demonstrates that Star's entry did not displace McWane's monopoly position in the domestic fittings market. Star's market share remained below [redacted]% in 2010 and 2011. IDF 1042-43, *in camera*. Moreover, Star's presence in the market failed to constrain McWane's pricing for domestic fittings. CX2199; IDF 1073-74, 1083, 1091-92. McWane's customers testified that, after the 2009 enactment of the ARRA, prices for domestic fittings increased and McWane refused to negotiate prices. IDF 1073. Even after Star's first domestic fittings sales in September 2009, McWane continued to sell its domestic fittings into domestic-only specifications at prices that earned significantly higher gross profits than for non-domestic fittings, which faced greater competition. IDF 1091. McWane also announced a price increase for domestic fittings in December 2009 that it applied in January 2010 (IDF 1083), which allowed McWane to earn even higher gross profits for domestic fittings in 2010 than in the prior year (IDF 1091-92).

Even the testimony of McWane's own expert, Dr. Normann, demonstrates that Star did not have a disciplining effect on McWane. He concluded that Star's presence in the domestic fittings market in several states did not produce lower prices. IDF 1090. Despite McWane's protests to the contrary, these facts establish its ability to control prices in the domestic fittings market and provides direct evidence of McWane's monopoly power.

B. EXCLUSIONARY CONDUCT

The next question is whether the challenged conduct—McWane's Full Support Program—was an unlawful exclusive dealing policy that enabled McWane to maintain its monopoly power in the domestic fittings market. "Unlawful maintenance of a monopoly is demonstrated by proof that a defendant has engaged in anti-competitive conduct that reasonably appears to be a significant contribution to maintaining monopoly power." *Dentsply*, 399 F.3d at 187; *Microsoft*, 253 F.3d at 79.

Distinguishing between exclusionary conduct and vigorous competition is not always easy. *Microsoft*, 253 F.3d at 58. Exclusive dealing arrangements are common and often procompetitive. *See Race Tires Am., Inc. v. Hoosier Racing Tire Corp.*, 614 F.3d 57, 76 (3d Cir. 2010) ("[I]n many circumstances, [exclusive dealing] may be highly efficient--to assure supply, price stability, outlets, investment, best efforts or the like--and pose no competitive threat at all."); *Stop & Shop Supermarket Co. v. Blue Cross & Blue Shield of R.I.*, 373 F.3d 57, 65 (1st Cir. 2004) (exclusive dealing agreements "can achieve legitimate economic benefits (reduced cost, stable long-term supply, predictable prices)"). For instance, exclusive dealing can, among other things, align distributor and manufacturer incentives and thus prevent free-rider problems, or lead a distributor to promote the product of its exclusive supplier more effectively, thereby increasing interbrand competition. *See Ryko Mfg. Co. v. Eden Servs.*, 823 F.2d 1215, 1234 n.17 (8th Cir. 1987); *Roland Mach. Co. v. Dresser Indus., Inc.*, 749 F.2d 380, 395 (7th Cir. 1984); *see also* Jonathan M. Jacobson, *Exclusive Dealing, Foreclosure & Consumer Harm*, 70 Antitrust L.J. 311, 357-58 (2002); Benjamin Klein & Kevin Murphy, *Exclusive Dealing Intensifies Competition for Distribution*, 75 Antitrust L.J. 433, 465-66

(2008). It can also result in lower prices because suppliers may be willing to reduce prices in exchange for higher sales volume. *See Stop & Shop Supermarket*, 373 F.3d at 62. Indeed, "competition to be an exclusive supplier may constitute 'a vital form of rivalry, and often the most powerful one, which the antitrust laws encourage rather than suppress.'" *Race Tires Am.*, 614 F.3d at 76 (quoting *Menasha Corp. v. News Am. Marketing In-Store, Inc.*, 354 F.3d 661, 663 (7th Cir. 2004)).

Despite these and other potential benefits, exclusive dealing can harm competition under certain circumstances. *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984) (O'Connor, J., concurring) ("Exclusive dealing can have adverse economic consequences by allowing one supplier of goods or services unreasonably to deprive other suppliers of a market for their goods . . . ."); Jacobson, 70 Antitrust L.J. at 328 (explaining that courts have manifested concern when exclusive dealing has been used to foster market power). Exclusive dealing can be particularly troubling when imposed by a monopolist. *ZF Meritor*, 696 F.3d at 271; *Dentsply*, 399 F.3d at 187 ("Behavior that otherwise might comply with antitrust law may be impermissibly exclusionary when practiced by a monopolist.").

Most pertinent here, exclusive dealing can be harmful when it enables a firm to acquire or maintain monopoly power by impairing the ability of rivals to grow into effective competitors that might erode the firm's dominant position. *See Microsoft*, 253 F.3d at 70-71; *Interface Grp., Inc. v. Mass. Port Auth.*, 816 F.2d 9, 11 (1st Cir. 1987); *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227 (1st Cir. 1983). The dominant firm's exclusive dealing arrangements may prevent new firms from achieving the scale necessary for them to become efficient competitors. *See* Dennis W. Carlton, *A General Analysis of Exclusionary Conduct and Refusal to Deal*, 68 Antitrust L.J. 659, 663, 655 n.15 (2001) (explaining that exclusive dealing may be harmful when it deprives rivals "of the necessary scale to achieve efficiencies, even though, absent the exclusivity," more than one firm "would . . . be large enough to achieve efficiency"). When a monopolist can impede potential rivals from becoming effective competitors, it can maintain monopoly prices and thereby harm consumers. *See* Herbert Hovenkamp, XI *Antitrust Law* ¶ 1802c, at 76-77 (3d ed. 2011); Richard A. Posner, *Antitrust Law* 229 (2d ed. 2001) (noting that exclusive dealing may "increase the scale necessary for new entry, and . . . increase the time required for entry and hence the opportunity for monopoly pricing").

As one leading commentator has summarized, the preconditions for competitive harm are: (i) exclusive dealing or similar arrangements covering a significant portion of distribution; (ii) entry barriers or equivalent impediments making it difficult for rivals or potential rivals to obtain efficient distribution; and (iii) resulting prolongation of the dominant firm's ability to earn monopoly profits in the downstream market. *See* Hovenkamp, XI *Antitrust Law* ¶ 1802b, at 74-76. Exclusive dealing can be anticompetitive, therefore, if it facilitates the exercise of market power by either impairing a rival's ability to achieve the scale necessary to become efficient, or if it makes a rival less efficient by depriving it of "efficient access to the downstream market." *Id.*; Dennis W. Carlton & Ken Heyer, *Appropriate Antitrust Policy Towards Single-Firm Conduct: Extraction vs. Extension*, 22 Antitrust 50, 53 (2008).

We evaluate McWane's Full Support Program using this accepted theory of competitive harm. In assessing McWane's exclusive dealing arrangement, we examine both the anticompetitive and procompetitive effects of the conduct to determine whether, in light of McWane's monopoly power, its use of exclusive dealing prevented rivals from meaningfully competing and had a substantial anticompetitive effect on competition. This approach is consistent with recent court precedent on exclusive dealing. *See ZF Meritor*, 696 F.3d at 271-72; *Dentsply*, 399 F.3d at 187; *Microsoft*, 253 F.3d at 58-59. As discussed below, we conclude that McWane's Full Support Program was an unlawful exclusive dealing policy that contributed significantly to the maintenance of McWane's monopoly power in the domestic fittings market.

1. McWane's "Full Support Program" Is an Exclusive Dealing Policy

"An exclusive dealing arrangement is an agreement in which a buyer agrees to purchase certain goods or services only from a particular seller for a certain period of time." *ZF Meritor*, 696 F.3d at 270. McWane's Full Support Program is an exclusive dealing policy by its terms, operation, and intent. McWane designed and implemented the program to deny Star and other potential competitors access to distributors and thereby impede their effective entry into the domestic fittings market in order to maintain its monopoly.

McWane's strategy and aim is clear from its internal business documents. Despite the fact that about 80% of demand can be met with 100 or fewer commonly used sizes and configurations of fittings, referred to as "A or B" fittings, distributors need access to a full line of domestic fittings to meet all of their customers' needs either through their own supply or with supply from others. IDF 306-08, 1252. As the only full-line supplier of domestic fittings, McWane knew very well that an exclusive dealing requirement would prevent distributors from purchasing from suppliers without full lines and took this into account when designing its Full Support Program. In a June 2009 presentation outlining options for McWane's response to Star's announced entry into the market, Mr. Tatman proposed a strategy to "Force Distribution to Pick their Horse." The proposal included a "Hard Approach – Full Line or No Line" and explained that the advantages of such a strategy included "[p]otentially rais[ing] the level of supply concern among contractors" and "Forc[ing] Star/Sigma to absorb the costs associated with having a more full line before they can secure major distribution." CX0076 at 009-010; *see also* CX0329 at 001 (advocating Full Line or No Line as preferred approach and best option against Star).

Later, while preparing for the rollout of the Full Support Program, McWane's National Sales Manager, Mr. Jansen, led an internal conference call with McWane's sales force during which he explained the new policy: "What are we going to do if a customer buys Star domestic? We are not going to sell them our domestic . . . . Once they use Star, they can't EVER buy domestic from us." IDF 1179. Mr. Tatman similarly noted in an e-mail that "we won't provide domestic product to distributors who are not fully supporting our domestic product lines." CX0113 at 001.

Following Star's first sales of domestic fittings, McWane publicly announced the program on September 22, 2009, in a letter to distributors:

> [E]ffective October 1, 2009, McWane will adopt a program whereby our domestic fittings and accessories will be available to customers who elect to fully support McWane branded products for their domestic fitting and accessory requirements. . . . Customers who elect not to support this program may forgo participation in any unpaid rebates for domestic fittings and accessories or shipment of their domestic fittings and accessory orders of Tyler Union or Clow Water products for up to 12 weeks.

CX0010. Despite the soft language of "may" and "or," McWane made sure distributors received the message that they would no longer be able to buy domestic fittings from McWane if they purchased domestic fittings from Star. *See* IDF 1180 (finding that McWane informed customers that if one branch of a distributor purchased domestic fittings from Star, all branches would be cut off). The only exceptions to this exclusivity policy were in situations where McWane domestic fittings were either unavailable within normal time frames, or purchased from a competitor along with pipe.[9] IDF 1173.

As McWane intended, most distributors interpreted the announced policy as a threat that McWane would terminate their ability to purchase any of McWane's domestic fittings if they purchased any domestic fittings from Star. *See* IDF 1184 (distributor Hajoca believed it would lose its rebates or be cut off from purchasing from McWane), 1187 (Groeniger viewed the policy as a threat that if it purchased domestic fittings from Star, McWane would not sell it any domestic fittings), 1188 (Illinois Meter believed it had been threatened with loss of access to McWane's domestic fittings if it bought from Star), 1190 (E.J. Prescott believed "If you bought one [domestic] fitting [from Star] in one of our 26 places, we're out, simple. . . . [McWane] said it's

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9 To the extent that McWane's rebates were part of the policy, McWane's threat to terminate any rebates previously offered if a distributor purchased from Star served only to further advance the exclusive dealing requirement of the program. As a result, because McWane's program was plainly more than a rebate policy, the arguments McWane raises about above-cost pricing are inapposite. Our principal concern is with McWane's threats to terminate its supply to distributors who purchased rival domestic fittings.

all or nothing."), 1192 (CI Thornburg interpreted the letter as a threat); IDF 1300 (U.S. Pipe was told that if it purchased from Star, "don't come back to McWane"); *but cf.* Thees, Tr. 3109-11 (Ferguson believed there may have been room to negotiate the Full Support Program's requirements and that its status as a large buyer would offer protection; ultimately, however, Ferguson chose not to purchase domestic fittings from Star unless McWane did not have the domestic fittings available (IDF 1262)). McWane acknowledged in an internal presentation that the message had been received by distributors: "Although the words 'may' and 'or' were specifically used, the market has interpreted the communication in the more hard line 'will' sense. . . . Access to McWane or Sigma requires distributors to exclusively support McWane where products are available within normal lead times. Violations will result in: Loss of access, loss of accrued rebates." IDF 1183.

And McWane's threat to terminate distributors who did not comply with its Full Support Program was not hollow. When Hajoca's Tulsa branch purchased Star domestic fittings, McWane cut off domestic fitting sales to all Hajoca branches, including those that had not purchased from Star. IDF 1208-13 (McWane refused to supply Hajoca's Lansdale branch even after Hajoca offered to pay higher prices). In an e-mail to customers of Hajoca's Lansdale, Pennsylvania branch, McWane stated, "We don't like the situation either but feel we can't support someone who is helping our competition build a line against us." IDF 1207. Consistent with McWane's policy, and in fact for a period longer than the 12 weeks specified in McWane's September 2009 letter, Hajoca was unable to place new domestic fittings orders with McWane. IDF 1219. McWane also withheld Hajoca's rebates for the fourth quarter of 2009. IDF 1224-27. It was only in April 2010, after the FTC commenced its investigation, that McWane and Hajoca negotiated an agreement allowing Hajoca to resume buying domestic fittings from McWane. Even under that agreement, however, Hajoca's Tulsa branch continued to be precluded from accessing McWane domestic fittings. IDF 1220-23.

In sum, the Full Support Program effectively required distributors to purchase domestic fittings only from McWane, under a real threat of losing access to McWane's full line of domestic fittings. Accordingly, we find that McWane's Full Support Program was an exclusive dealing policy.

2. McWane's Full Support Program Foreclosed Star's Access to Distributors for Domestic Fittings and Harmed Competition

A finding of exclusive dealing alone is insufficient to establish liability. There must be evidence that competition, not merely a competitor, has been harmed. *Dentsply*, 399 F.3d at 187. The conduct, in other words, "must harm the competitive *process* and thereby harm consumers." *Microsoft*, 253 F.3d at 58. Accordingly, the central question is whether McWane's exclusive dealing policy raised "the cost of obtaining efficient distribution" for its rivals and thereby impaired "the competitive effectiveness" of its rivals with "resulting harm to competition." Carlton, 68 Antitrust L.J. at 665 n.15. Importantly, to be unlawful, the conduct need not have foreclosed all competition from the market; rather, it must have impeded a substantial number of rivals or severely restricted the scope of the market. *Dentsply*, 399 F.3d at 191.

With few exceptions, McWane's program forced its distributors to carry McWane domestic fittings exclusively. McWane thus deprived its rivals, mainly Star, of distribution sufficient to achieve efficient scale, thereby raising costs and slowing or preventing effective entry. The result harmed competition by increasing barriers to entry and allowing McWane to maintain its monopoly position, which prevented meaningful price competition and deprived consumers of the ability to choose among the products, terms of sale, and services of varying suppliers of domestic fittings.

a. Foreclosure of Access to Distributors

A domestic fittings entrant is unable to compete effectively without access to distributors. The benefits that distributors provide to fittings suppliers include offering better sales coverage (IDF 400, 402-03, 408-09); more local influence and knowledge of projects in their market area (IDF 400, 408-09, 412); carrying local inventory (IDF 400, 402-06); aggregating small orders and shipments to capitalize on scale efficiencies (IDF 405); and carrying credit risk (IDF 400, 402, 407, 411). For a fittings supplier to replicate these distributor functions would impose an "astronomical" cost on the supplier that would be prohibitively expensive. IDF 402. The benefits accruing from distributors make them the preferred and most efficient sales channel for domestic fittings manufacturers. Not surprisingly, McWane views distributors as "critical to [its] success," as does Star. IDF 401-02. No evidence supports the existence of viable alternate distribution channels, including direct sales to end users. IDF 381. Indeed, virtually all fittings sales are made through distributors. JSLF ¶ 14, IDF 367 (99% of McWane's sales of fittings are through distributors), IDF 373-74 (similarly, Sigma and Star sell almost all of their fittings to distributors).

McWane's Full Support Program foreclosed Star and other potential entrants from accessing a substantial share of distributors. Following announcement of the program, the country's two largest waterworks distributors, HD Supply, with a roughly 28% to 35% share of distribution (IDF 378), and Ferguson, with about 25% of distribution (IDF 379), prohibited their branches from purchasing domestic fittings from Star unless the purchases fell into one of the exceptions specified in the Full Support Program. One day after learning about the program, HD Supply's management sent a memo to its district, branch, and operations managers describing McWane's policy and stating that "we need to adhere to this mandate and purchase all of our American made fittings through Union-Tyler [McWane] or Sigma . . . [to] ensure that we have a full line of product . . . as well as continued compliance with the Federal [ARRA Buy American] requirements." IDF 1238-41. HD Supply even cancelled pending orders for domestic fittings it had with Star. IDF 1242. Although a Ferguson executive testified that his company "was planning on purchasing all its needs from McWane" regardless of the Full Support Program because Star lacked a complete line of domestic fittings (Thees, Tr. 3109; *see also* IDF 1266, 1272), the record suggests that the Full Support Program nonetheless cost Star some Ferguson business. A Ferguson Vice President called district managers after McWane's policy was announced to ensure that it did not buy from Star, and at least one job Ferguson initially awarded to Star was cancelled. IDF 1260-61, 1263.

Similarly, when WinWholesale, the nation's third-largest waterworks distributor, received notice of the Full Support Program, it listed Star's vendor status internally as "Not Approved," which barred its local companies from buying from Star under any circumstances without board approval. IDF 236, 1331-32, 1334-37. WinWholesale, however, did allow local companies to make purchases from Star that fell within the exceptions allowed by the Full Support Program, and, as a result, some WinWholesale local companies made a handful of purchases from Star. *See* IDF 1338, 1343.

Other large distributors likewise refused to purchase from Star because of the Full Support Program, sometimes even though Star offered lower prices. For instance, despite a commitment from Star to offer lower prices than McWane, U.S. Pipe instructed its purchasing manager not to purchase domestic fittings from Star unless McWane could not provide the needed size. IDF 1295, 1299, 1301-02. As a result, except for minor purchases falling within the exceptions to McWane's exclusive dealing policy, U.S. Pipe did not purchase domestic fittings from Star until September 2010. IDF 1309-11. Similarly, Star offered TDG distributors a more generous rebate program on domestic fittings than McWane, but Star believed they likewise rejected Star's offer because of the Full Support Program. IDF 1391. Groeniger, which had given Star business on two sizeable domestic-only projects prior to McWane's announcement of the Full Support Program, was reluctant to make further purchases of domestic fittings from Star because it needed access to McWane's domestic fittings and feared retaliation. IDF 1313-18; IDF 1329-30 (testifying that, but for McWane's policy, Groeniger would have given Star 50% of its domestic fittings business in 2010). The Full Support Program also deterred Illinois Meter from purchasing domestic fittings from Star because of the need to have access to McWane's full line. Sheley, Tr. 3413, 3417-18; IDF 1357-58, 1362-64.[10]

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10 Complaint Counsel estimates that McWane's policy foreclosed approximately [redacted]% of distribution, emphasizing that this is a far higher percentage than what courts have typically viewed as creating a potential competitive problem. CCAnsB at 17 (citing, *inter alia*, IDF 357, *in camera*); *Microsoft*, 253 F.3d at 70 (noting that a monopolist's use of exclusive contracts may in certain circumstances "give rise to a § 2 violation even though the contracts foreclose less than the roughly 40% to 50% share usually required in order to establish a § 1 violation"); Hovenkamp, XI *Antitrust Law* ¶ 1821c.1, at

In the face of this substantial evidence, McWane argues its program could not have foreclosed access to distributors because it did not require distributors to commit to purchasing McWane's fittings exclusively for a lengthy period of time. McWane's argument ignores the reality of a marketplace where distributors need access to a full line of domestic fittings to service their customers. "An express exclusivity requirement . . . is not necessary, because we look past the terms of the contract to ascertain the relationship between the parties and the effect of the agreement 'in the real world.' Thus, *de facto* exclusive dealing claims are cognizable under the antitrust laws." *ZF Meritor*, 696 F.3d at 270; *Minnesota Mining & Mfg.*, 35 F. Supp. 2d. 1138, 1144 (D. Minn. 1999) (holding that the proper focus of an exclusive dealing arrangement is not its duration, but its "practical effect"). Even arrangements that are terminable at will can be anticompetitive. *Dentsply*, 399 F.3d at 194 (noting that "in spite of the legal ease with which the relationship can be terminated," affected dealers may "have a strong economic incentive to continue carrying [the supplier's product]").

In fact, McWane's Full Support Program required exclusive dealing for as long as McWane desired. The overwhelming evidence shows the practical effect of McWane's program was to make it economically infeasible for distributors to drop McWane's full line of domestic fittings and switch to Star. This reality made McWane's exclusive dealing program as effective and enduring as a long-term contract. *See Lorain Journal Co. v. United States*, 342 U.S. 143, 149-50 (1951) (holding that unilateral conduct of indefinite duration by a monopolist with a "practically indispensable" service "forced numerous [customers] to refrain from" dealing with a rival).

McWane also disputes the connection between its Full Support Program and Star's lagging sales, pointing to other concerns distributors had about Star's supply of domestic fittings. But the Full Support Program need not have been the sole reason for distributors' reluctance to purchase domestic fittings from

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191 (foreclosure above 50% is "routinely condemned"). We need not adopt Complaint Counsel's estimate, however, to conclude that foreclosure here was both substantial and problematic. As the *Dentsply* court concluded, "the reality . . . is that the firm that ties up the key dealers rules the market." 399 F.3d at 190.

Star. The relevant question is whether McWane's policy contributed significantly to that result. *See Microsoft*, 253 F.3d at 78-80; *Conwood Co. v. U.S. Tobacco Co.*, 290 F.3d 768, 791 (6th Cir. 2002) (explaining that defendant's conduct "need not be the sole proximate cause" of lost sales that caused injury). The evidence amply shows that the Full Support Program substantially contributed to distributors' "reluctance to purchase from Star." ID at 410; *see also ZF Meritor*, 696 F.3d at 266, 285-86 (focusing on foreclosure created by exclusive dealing despite acknowledging that plaintiff could have competed more effectively).

b. Adverse Impact on Competition

McWane's exclusive dealing program created a strong economic incentive for distributors to reject Star's products, artificially diminishing Star's competitive prospects in the domestic fittings market. Beginning in Spring 2009, Star considered purchasing its own domestic foundry. IDF 1402. By September or October, it had identified a specific foundry and entered into negotiations to purchase it. IDF 1404. Star estimated it would cost [redacted] to acquire the facility and had the financial ability to make the purchase. IDF 1405-06, *in camera*. However, McWane's announcement of its exclusive dealing policy in September and its impact on Star's sales prompted Star to rethink its strategy of acquiring a domestic foundry. IDF 1407-08.

Before McWane's September announcement, Star had received requests for quotes for domestic fittings worth approximately $10 million. IDF 1395. As discussed above, almost immediately following the announcement, distributors, including HD Supply, Ferguson, and WinWholesale, withdrew their requests for quotes or orders and informed Star they were no longer interested in purchasing domestic fittings from Star. IDF 1381-82. Based in part on the withdrawn quotes, Star estimated it would have had [redacted] in sales of domestic fittings in 2010, rising to [redacted] in 2011, if McWane had not implemented the Full Support Program. IDF 1394-95, *in camera*. At trial, Star testified that more refined estimates showed that it needed between [redacted] of domestic fittings sales to justify purchasing its own foundry. IDF 1400, *in camera*;

Bhargava, Tr. 2962-63, *in camera*. Star's actual sales of domestic fittings, [redacted] in 2010, were insufficient for Star to justify operating a foundry of its own. IDF 1396, *in camera*, 1401.

Consequently, rather than acquiring its own foundry, Star contracted with six foundries to produce raw castings, which Star then shipped to its Houston facility for finishing. This route was more costly and less efficient than a foundry owned and operated by Star would have been because using independent foundries means less specialized and efficient equipment; smaller batch sizes; additional logistical costs associated with inventory, finishing, and freight; less control over inventory levels; less ability to expedite orders; and inefficiencies resulting from dealing with multiple foundries. IDF 1409-10. Independent foundries also have higher labor costs and add their own markup. IDF 1412-13. Shipping costs alone from the foundries to Houston for finishing added an additional [redacted]% to the cost of Star's domestic fittings. IDF 1411, *in camera*. Star estimated that the cost of producing domestic fittings at its own foundry would have been [redacted]% lower than the cost of contracting with independent foundries, and that it could have reduced its domestic fittings prices by [redacted]%. IDF 1419-20, *in camera*. Moreover, because some customers were reluctant to rely on a supplier without its own foundry, IDF 1254, 1272, by denying Star the scale necessary to operate its own foundry, McWane further cemented its monopoly.

McWane anticipated and intended this result.[11] Mr. Tatman could not have been more clear: "We need to make sure that they don't reach any critical mass that will allow them to continue to invest and receive a profitable return." CX0074 at 001; s*ee also* IDF 1155 (quoting CX0067 at 002) (in a "brainstorming document," "Mr. Tatman observed that 'any competitor' seeking to enter the domestic fittings market could face 'significant

11 While our aim is to ascertain the effect of McWane's exclusive dealing policy, evidence of McWane's intent is relevant "to the extent it helps us understand the likely effect of [McWane's] conduct." *Microsoft*, 253 F.3d at 59; *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918) ("knowledge of intent may help the court interpret facts and predict consequences").

blocking issues' if they are not a 'full line' domestic supplier"); CX0076 at 009 (explaining that a "Force Distribution to Pick their Horse" strategic response to entry would "Force[] Star/Sigma to absorb the costs associated with having a more full line before they can secure major distribution"). Impairing its rivals' ability to threaten McWane's monopoly was the Full Support Program's core objective.

And Star was not the only firm affected by McWane's exclusive dealing policy. Fittings importer SIP also evaluated whether to enter the domestic fittings market in 2009. IDF 1365-80. SIP believed that because of McWane's policy, it would have difficulty acquiring distributor customers if it entered with less than a full line. IDF 1377. Although McWane's Full Support Program was not the only reason SIP decided not to enter, it was a significant reason. IDF 1380 ("That was the straw that broke the camel's back.") (quoting CX2522, *in camera* (Agarwal, Dep. at 67-68)).

In his dissent, Commissioner Wright asks us to apply a new, heightened standard of proof for exclusive dealing cases and concludes under that standard that Complaint Counsel failed to prove McWane's exclusive dealing policy harmed competition.[12] Although Commissioner Wright assumes that McWane is a monopolist for his analysis and agrees with the majority decision in various respects, including that "[t]here is ample record evidence demonstrating that the Full Support Program harmed McWane's rival Star," he claims "Complaint Counsel fails totally to establish, as it must under the antitrust laws, that McWane's conduct harmed *competition*."[13] Dissent at 4-5. We respectfully

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12 Although harm to competition is certainly necessary for a claim of monopolization, Commissioner Wright would apply a standard of evidentiary proof for this element that is far beyond that called for by applicable Section 2 law. *See generally ZF Meritor*, 696 F.3d at 286; *Dentsply*, 399 F.3d at 191; *Microsoft*, 253 F.3d at 70-71. For instance, he insists that Complaint Counsel was required to calculate the specific level of sales Star lost as result of the Full Support Program. Tellingly, Commissioner Wright offers no legal support for this heightened standard.

13 We note that while the aim of the antitrust laws is to protect competition, not competitors, there *is* harm to competition when a monopolist's only rival is precluded from becoming an effective competitor. *See Spirit Airlines*, 431 F.3d

disagree. In our view, the evidence that McWane's exclusive dealing policy significantly impaired the access of McWane's only rival, Star, to the main channel of distribution, thereby increasing its costs and keeping it below the critical level necessary to pose a real competitive threat, is plainly sufficient to meet the standard of harm to competition set forth in the prevailing case law.

Moreover, there are significant factual oversights in his analysis even applying his proposed heightened standard. For instance, Commissioner Wright argues there is no evidence supporting Complaint Counsel's contention that Star needed its own foundry to compete effectively in the market. But the evidence shows that costs decline substantially when a market participant is able to operate its own foundry.[14] By preventing Star from securing enough sales volume to support its own foundry, McWane's exclusive dealing program increased Star's costs and denied it the ability to compete effectively. We also disagree with Commissioner Wright's assertion that the notion that Star was operating below "minimum efficient scale" "strains credulity" when one takes into account Star's entry and growth in the market. Dissent at 32. Complaint Counsel argues persuasively that McWane was charging a monopoly price, which means that even a less efficient firm could enter and grow market share. The key question is whether the exclusionary conduct kept rivals from developing into real competitive threats; here we find that it did. *See Dentsply*, 399 F.3d at 190-91 (finding competitive harm when defendant's excluded rivals failed to achieve "the critical level necessary for any rival to pose a real [competitive] threat"); *Microsoft*, 253 F.3d at 70-71 (stating that defendant's exclusionary conduct kept [competitor's product] "below the

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at 951 ("[I]n a concentrated market with very high barriers to entry, competition will not exist without competitors.").

14 Commissioner Wright points to Sigma's virtual manufacturing model as evidence that owning a foundry is not essential to achieving efficiencies. Dissent at 31-32. However, this comparison is inapt. We are concerned with the effect of McWane's conduct on Star's ability to do business in the market for domestically-manufactured fittings. The fact that Sigma uses a virtual manufacturing model for its imported fittings business sheds little light on that question.

critical level necessary for [competitor's product] or any other rival to pose a real threat to Microsoft's monopoly").

Commissioner Wright also argues that our foreclosure analysis is "defective" on the ground that "[i]t makes little sense to conclude that Star was foreclosed from McWane's sales to distributors that would have taken place with or without the Full Support Program." Dissent at 38. He insists that to prevail, Complaint Counsel was required to show that but for the Full Support Program, a significant volume of sales would have actually shifted to Star. Commissioner Wright appears to assume, however, that the sales a monopolist like McWane has tied up with its distributors are not contestable and that a second meaningful alternative in the market will have no impact on price or other forms of competition, regardless of which supplier customers may ultimately choose. This assumption overlooks record evidence that McWane's main customers immediately sought an alternative when given the option, placing millions of dollars' worth of requests for proposal with Star in the few months after it announced entry and before McWane imposed the Full Support Program.

In addition, contrary to Commissioner Wright's assertion, there is evidence that McWane's exclusionary conduct had an impact on price. McWane itself recognized that if Star entered, prices in the domestic market would likely fall just like in the imported market. IDF 1148-49, 1151-53. McWane understood it had a choice -- it could try to maintain its dominant market share either by lowering prices to compete against Star (CX0465 at 004 (noting that McWane could maintain its "near 100% share" by dropping prices)), or it could adopt an exclusive dealing policy that would prevent its rival from achieving the scale necessary to become a more significant competitor (CX0067 at 002 (noting that rivals without a full domestic line would be susceptible to "significant blocking issues")). By adopting the program, McWane was able to ensure that prices and gross profits for domestic fittings remained high. In fact, following Star's entry, McWane's financials reveal that, while its production costs for domestic fittings remained flat for 2009 and 2010, McWane raised domestic fittings prices and increased its gross profits during that same time. IDF 1091-93, *in camera*. Moreover, McWane was able to impose those higher prices for domestic fittings in both states where it had a 100% market share and those where it faced direct competition from Star. IDF 1090.

In short, Commissioner Wright fails to adequately consider that foreclosure delaying a rival's effectiveness and growth in the market results in consumer harm and that there is considerable evidence to support a reasonable inference that the Full Support Program had that very result.

By foreclosing Star's access to distributors, McWane's exclusive dealing program increased Star's costs and denied it the ability to compete effectively. Courts have not hesitated to find antitrust liability when exclusive dealing contributes significantly to maintaining a monopoly through such effects. *See Dentsply*, 399 F.3d at 190-91 (finding competitive harm when defendant's excluded rivals failed to achieve "the critical level necessary for any rival to pose a real [competitive] threat"); *Microsoft*, 253 F.3d at 70-71 (stating that defendant's exclusionary conduct kept [competitor's product] "below the critical level necessary for [competitor's product] or any other rival to pose a real threat to Microsoft's monopoly"); *cf. ZF Meritor*, 696 F.3d at 289 (finding antitrust injury when the defendant's conduct denied rivals the market share they needed to "remain viable").

McWane's exclusive dealing policy also had another adverse impact on competition: it denied its customers the ability to make a meaningful choice regarding domestic fittings suppliers that the evidence shows many of them sought. *See ZF Meritor*, 696 F.3d at 285 (noting that a monopolist may cause harm to competition when it "use[s] its power to break the competitive mechanism and deprive customers of the ability to make a meaningful choice"); *Dentsply*, 399 F.3d at 194 (holding that the defendant's exclusive dealing policy had the anticompetitive effect of limiting the choice of products available to end users); *see also Race Tires*, 614 F.3d at 77-78 (recognizing the important role "coercion" plays in the Section 2 context). Although fittings are commodity products, there is evidence of competition among suppliers for service and other terms. *See* IDF 1584 (noting that some distributors preferred Sigma over McWane because of certain servicing benefits, including faster delivery); IDF 1586 (ACIPCO preferred Sigma over McWane because Sigma offered additional specialty services, such as coatings, linings, and tapes); IDF 1588

(Groeniger preferred buying from Sigma because it preferred Sigma's service to that offered by McWane and Star). As the Third Circuit noted in *Dentsply*, "[w]hile the [customers] might prefer to sell the [products] of multiple manufacturers, if faced with an all or nothing choice they may accede to the dominant firm's wish for exclusive dealing." 399 F.3d at 194 (internal quotations omitted).

Distributor decisions to reject Star following implementation of the Full Support Program, sometimes even when Star offered lower prices, show that McWane's policy and position as a supplier of necessary products effectively eliminated distributors' choices regarding their source of domestic fittings supply and prevented them from using Star to extract better prices or services from McWane. IDF 1395 (finding that, after announcement of the Full Support Program, Star lost $10 million in request for quotes from, among others, HD Supply, Ferguson, Mainline, WinWater, and other customers); IDF 1295, 1299, 1301-02 (finding that U.S. Pipe rejected Star despite Star's offer of lower prices than McWane). The absence of exclusivity in the more competitive imported fittings market highlights the coercive element of McWane's policy. *See* IDF 392 (noting that distributors typically purchase imported fittings from at least two different suppliers).

c. McWane's Rebuttal

McWane disagrees that its policy impaired Star's ability to compete in the domestic fittings market. It contends first that Star's sales to 130 distributors enabling Star to obtain [redacted]% market share in 2010 and more than [redacted]% market share in 2011 demonstrate successful entry into the domestic fittings market, thereby precluding a finding of liability as a matter of law. IDF 357, *in camera*. We rejected this same argument when we denied McWane motion for summary decision. Under Section 2, "it is not necessary that all competition be removed from the market. The test is not total foreclosure, but whether the challenged practices bar a substantial number of rivals or severely restrict the market's ambit." *Dentsply*, 399 F.3d at 191; *accord ZF Meritor*, 696 F.3d at 265, 283-84 (exclusive dealing violated Section 2 even though monopolist allowed customers to purchase up to 20% of product from rival). Moreover, growth and market share alone is not the relevant benchmark. The appropriate comparison is growth that would have occurred absent the Full Support Program. Here, as we have discussed, McWane's exclusive dealing policy ensured that Star's sales remained limited and enabled McWane to maintain its monopoly position. As we noted previously, even McWane's expert agreed that Star's entry did not affect McWane's prices for domestic fittings. IDF 1090. Indeed, soon after Star entered the market, McWane announced and implemented price increases for domestic fittings. IDF 1083.

Further, McWane's repeated claim that Star sold to 130 distributors is meaningless without context or a showing as to the size of Star's sales. As the ALJ explained, "[i]n counting the number of customers to whom Star sold domestic fittings, Respondent's expert, Dr. Normann, counted each Distributor that may have purchased only a single Domestic Fitting from Star, or whose purchases fell into one of the limited exceptions to McWane's Full Support Program. IDF 1142. The number of customers, without more information on the nature and extent of their purchases, is not entitled to substantial weight." ID at 409. Here, the record shows that distributors primarily bought domestic fittings from Star under the exceptions to the Full Support Program, *i.e.*, when McWane was unable to offer specific fittings in timely fashion or as part of a bundled order, even when they would not otherwise purchase from Star for fear of losing access to McWane's domestic fittings. *See* IDF 1237, 1242, 1257 (HD Supply); 1299, 1305, 1309 (U.S. Pipe); 1328-29 (Groeniger).

McWane also argues that, even if Star was excluded, there was no harm to competition because "the ALJ found that Star's reliance on jobber foundries made it a less efficient, higher cost supplier, and thus that McWane's domestic fittings prices were lower[.]" RAppB at 29. We disagree. McWane's argument conveniently overlooks the role its exclusive dealing policy played in limiting Star's sales and the resulting impact the policy had on Star's scale of operations and reliance on third-party "jobber" foundries. As discussed at length above, McWane designed its exclusive dealing policy precisely to slow its rivals' growth. *See* CX0076 at 009 (noting that the program "[f]orces Star/Sigma to absorb the costs associated with having a more full line before they can secure major distribution"). And there is ample evidence that McWane's program was effective in denying

Star access to customers and thus impeding its ability to compete effectively.

Moreover, McWane is incorrect to the extent it suggests it is immune from liability merely because Star was a less efficient competitor. The fundamental concern with monopoly maintenance is that dominant firms may adopt policies that prevent the development of effective competition. As the D.C. Circuit held in *Microsoft*, it is "inimical to the purpose of the Sherman Act to allow monopolists free reign to squash" emerging competitors before they have the opportunity to become capable rivals that could effectively challenge the monopolist. *Microsoft*, 253 F.3d at 79; *see also* Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 Antitrust L.J. 3, 59-60 (2004) (while "the exclusion of the less efficient firm might not have harmed competition at that precise moment because the rival had yet to reach its potential, . . . Section 2's horizon should not be so clipped if it is to function as an adequate deterrent to strategic behavior that impairs long-run competition").

3. McWane's Procompetitive Justifications for the Full Support Program

Complaint Counsel has demonstrated harm to competition here, shifting the burden to McWane to show that the challenged conduct "promotes a sufficiently pro-competitive objective." *Dentsply*, 399 F.3d at 196. Cognizable justifications are typically those that reduce cost, increase output or improve product quality, service, or innovation. *See FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 459 (procompetitive justifications include "creation of efficiencies in the operation of a market or the provision of goods and services"); *Broadcast Music, Inc. v. Columbia Broadcasting Sys., Inc.*, 441 U.S. 1, 19-20 (1979) (courts should consider whether the challenged practice is likely to "increase economic efficiency and render markets more, rather than less, competitive") (internal quotations omitted); *Data Gen. Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147-1183 (1st Cir. 1994) ("In general, a business justification is valid if it relates directly or indirectly to consumer welfare.").

McWane offers two justifications for its conduct. It argues first that it engaged in exclusive dealing to preserve sales in order to generate sufficient volume to operate its last domestic foundry. While preserving sales volume to continue to operate a foundry may have been a significant business objective, it is not a cognizable procompetitive justification for antitrust purposes. *See Microsoft Corp.*, 253 F.3d at 71-72 (explaining that the desire to increase sales "is not an unlawful end, but neither is it a procompetitive justification"). As the ALJ recognized, McWane's sales goal provides benefits for McWane, but "Respondent has proffered no explanation as to how its Full Support Program benefits consumers." ID at 415.

Significantly, the measures that McWane took to preserve its sales volume were not the type of steps, such as a price reduction, that typically promote consumer welfare by increasing overall market output. Indeed, McWane considered the impact of lowering its domestic fittings pricing "to defend [its] near 100% share position," but ultimately determined that lowering pricing would hurt margins. CX0465 at 004. Instead, the sales gained for production by McWane's exclusive-dealing arrangement were sales taken from Star by virtue of the increased costs imposed by the Full Support Program. That is, McWane's sales did not result from lower prices, improved service or quality, or other consumer benefits; instead, McWane's sales stemmed from anticompetitive reductions in Star's output. Sales so gained are not cognizable as procompetitive justifications. *See* Horizontal Merger Guidelines § 10 ("Cognizable efficiencies . . . do not arise from anticompetitive reductions in output or service."); c*f. NCAA v. Bd. of Regents*, 468 U.S. 85, 116-17 (1984) (holding that a defendant could not justify curbing access to a more-desired product to induce consumers to purchase larger amounts of a less-desired product); *In re Polygram Holding, Inc.*, 136 F.T.C. 310, 345-46 (2003) ("[C]ognizability . . . allows the deciding tribunal to reject proffered justifications that, as a matter of law, are incompatible with the goal of antitrust law to further competition."), *aff'd*, 416 F.3d 29 (D.C. Cir. 2005).

Furthermore, contemporaneous evidence belies McWane's contention that its exclusive dealing policies were motivated by a desire to gain volume in order to preserve operations at McWane's domestic foundry. Although that justification shows up in testimony from McWane witnesses, McWane's contemporaneous planning documents from 2009 demonstrate that the objectives were almost exclusively to maintain domestic prices and profitability, deny Star critical mass, and prevent Star from becoming an effective competitor. *See* IDF 1149 (quoting CX0074 at 001) ("Whether we end up with Star as a complete or incomplete domestic supplier my chief concern is that the domestic market gets creamed from a pricing standpoint just like the non-domestic market has been driven down in the past."), 1151 (citing CX 0102 at 002 (2010 budget describing "biggest risk factor" as the "[e]rosion of domestic pricing if Star emerges as a legitimate competitor")), 1158 (citing CX0076 at 009) (explaining that a disadvantage of not adopting exclusive dealing was that it would allow Star to "drive profitability out of our business"), 1150 (quoting CX0074 at 001) ("I agree that at this stage the chance for profitable cohabitation with Star owning a [piece] of the Domestic market is slim . . . we need to make sure that they don't reach any critical market mass that will allow them to continue to invest and receive a profitable return.").

McWane also argues that the Full Support Program prevents customers from cherry-picking the highest selling items from Star and persuades them to support McWane's full line of domestic fittings. Here too McWane fails to identify the benefit to consumers.[15]

In support of McWane's claim, its expert, Dr. Normann, explains that a full-line manufacturer incurs the costs of producing all fitting types and is able to bear these costs because it captures the benefit of scale economies arising from production of the most common fittings. According to Dr. Normann, a manufacturer that produces only the common fittings could avoid the cost of producing a full line and consequently could sell the common fittings at lower prices. If distributors were able to source from multiple manufacturers, he reasons, they would buy the common fittings from the limited supplier (at lower prices) and turn to the

15 Although preventing dealer or competitor free riding on manufacturer-supplied investments is commonly proffered as a procompetitive justification for exclusive dealing, there is no showing that is the case here. Indeed, the absence of evidence of exclusive dealing arrangements for sales of imported fittings belies such an argument.

full-line supplier for less common products only, which could lead to the collapse of the full-line seller. *See* RX712A at 056.

This argument is unpersuasive. If a limited supplier undersells a full-line supplier for more common products, there is no reason in principle why the full-line supplier could not compete for that business by lowering its price for those products and increasing its price for the less common products. McWane offers no reason why supply would not be forthcoming to meet demand at a higher price, and we cannot conclude that consumers are necessarily worse off because less common fittings are sold for higher prices, when simultaneously, more common fittings are sold at lower prices. Even if selective entry by the full-line supplier's rivals led to the collapse of the full-line seller, that itself would not constitute a harm to the market (as opposed to harm to a single firm). Courts have long rejected claims that "because of the special characteristics of a particular industry, monopolistic arrangements will better promote trade and commerce than competition," *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 689 (1978), concluding instead that "[t]he Sherman Act reflects a legislative judgment that ultimately competition" will produce the best results. *Id*. at 695-96 (also noting that "the Rule of Reason does not support a defense based on the assumption that competition itself is unreasonable"). McWane's claim is not consonant with this core judgment of the Sherman Act, and it is inconsistent with the basic objectives of Section 2.[16]

VI. THE MASTER DISTRIBUTION AGREEMENT AS A RESTRAINT OF TRADE

We now turn to the charge that McWane and Sigma unreasonably restrained trade in the domestic fittings market in violation of Section 5 of the FTC Act by entering into the MDA. According to Complaint Counsel, McWane saw that Sigma was preparing to enter the domestic fittings market and sought to

16 As noted above, the Commission dismisses Count 7 of the Complaint, alleging attempted monopolization based on McWane's exclusive dealing requirements. In view of our conclusion that McWane unlawfully monopolized the domestic fittings market through the same conduct, it is unnecessary to ask whether McWane attempted to monopolize the market. Accordingly, we do not reach this issue, and do not adopt the ALJ's analysis. *See Spectrum Sports*, 506 U.S. at 451-53, 460-61.

eliminate the risk of competition by inducing Sigma to become an exclusive distributor of McWane's domestic fittings.

Complaint Counsel's claim, based on Section 1 of the Sherman Act, requires that there be a contract, combination, or conspiracy among two or more entities that unreasonably restrains trade. *Realcomp II, Ltd. v. FTC*, 635 F.3d 815, 824 (6th Cir. 2011). Here, there is no question that there was an agreement. The dispute is over the agreement's lawfulness. Complaint Counsel asserts two theories of liability. Their main contention is that, without the MDA, Sigma would have entered the market independently and competed against McWane. In Complaint Counsel's view, the MDA amounted to an agreement that Sigma would cede the domestic fittings market to McWane. Complaint ¶¶ 47-55, 67. Complaint Counsel argues in the alternative that the MDA was an unreasonable vertical restraint of trade. We find there is no violation under either theory.

A. THE MDA WAS NOT A MARKET ALLOCATION AGREEMENT

Under Section 1 of the Sherman Act, an agreement among competitors to allocate markets is *per se* illegal. *See Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46, 49 (1990) (*per curiam*); *United States v. Topco Assocs*., 405 U.S. 596, 608-09 (1972). Likewise, naked agreements "not to compete among potential competitors are also illegal *per se*." *Transource Int'l, Inc. v. Trinity Indus.*, 725 F.2d 274, 280 (5th Cir. 1984); *see also Engine Specialties, Inc. v. Bombardier, Ltd.*, 605 F.2d 1, 9-11 (1st Cir. 1979) (finding a market allocation agreement between potential competitors *per se* unlawful). Complaint Counsel's Section 1 theory is premised on Sigma being a potential competitor in the domestic fittings market. Accordingly, we must first determine if, but for the MDA, Sigma was sufficiently likely to enter the domestic fittings market to be considered a potential competitor of McWane.

In evaluating this question, we look to whether Sigma had "the necessary desire, intent, and capability to enter the market." *Bombardier*, 605 F.2d at 9. The ultimate issue is whether Sigma's entry was reasonably probable in the absence of the MDA. *See* Fed. Trade Comm'n & Dep't of Justice, Antitrust Guidelines for

Collaborations Among Competitors § 1.1 n.6 (2000) ("A firm is treated as a potential competitor if there is evidence that entry by that firm is reasonably probable in the absence of the relevant agreement.") ("Competitor Collaboration Guidelines"); *cf. Yamaha Motor Co. v. FTC*, 657 F.2d 971, 977 (8th Cir. 1981) (evaluating, in a Clayton Act Section 7 case, whether, absent the joint venture, the merging party "probably" would have entered). We agree with the ALJ that Sigma's entry was not reasonably probable.

As explained above, Sigma began investigating two potential avenues for entry into the domestic fittings market following the passage of the ARRA in February 2009: (1) purchasing domestic fittings from McWane; and (2) producing domestic fittings by contracting with independent domestic foundries (a "virtual manufacturing" model). Rona, Tr. 1630; Pais, Tr. 1752; IDF 1423-24. In April, Sigma approached McWane about obtaining private label fittings but was dissatisfied with McWane's initial offer, which was insufficient to cover Sigma's operating costs. IDF 1425, 1443-45. After rejecting McWane's first offer, Sigma President and CEO Mr. Pais wrote: "We now need to go all out and implement a SDP [Sigma Domestic Production] plan – replicating SIGMA's 'virtual manufacturing' model . . . just as we do thru a collection of facilities overseas." IDF 1455. Before long, however, Sigma approached McWane to resume discussions about a possible distribution arrangement. IDF 1522. Ultimately, Sigma decided to forgo independent entry and chose instead to purchase domestic fittings from McWane pursuant to the MDA.

Complaint Counsel points to troubling evidence showing that McWane believed Sigma was likely to enter the domestic fittings market independently, and that McWane entered the MDA in order to eliminate that possibility. For example, an internal McWane memorandum, dated May 26, 2009, concludes that McWane's decision to sell domestic fittings to Sigma "probably comes down to . . . [h]ow legitimate of a risk is there with a competitor successfully introducing a Domestic product line?" CX0067 at 002, 004. In addition, Mr. Tatman and Mr. McCullough referred to the MDA as an "insurance policy" against potential Sigma entry. CX2353 at 004; CX1184 at 001. The evidence also indicates that McWane believed selling domestic fittings to Sigma would "help drive some additional level of price stability." CX 0465 at 002, 010. Yet other evidence shows that McWane harbored doubts as to Sigma's capabilities. For example, McWane's Vice President and General Manager, Mr. Tatman, sent an internal email to both of his bosses, Mr. McCullough and Mr. Walton, on August 18, 2009, explaining that he was "leaning towards not throwing too much [money]" at what he referred to as an "insurance policy" against Sigma's entry, noting that he is "not picking up any strong sense that they have a strong alternate path at this point that they'd be willing to invest significant $ into." CX1184 at 001; Tatman, Tr. 771-72, 783-85.

In fact, Sigma did take various preliminary steps to explore the viability of its virtual manufacturing plan. This included assembling a team of executives responsible for evaluating entry. The team considered domestic foundries' costs and capabilities, as well as the time it would take for Sigma to start production. IDF 1447. They investigated all aspects of the necessary processing steps and concluded that Sigma would need to offer approximately 730 different types of domestic fittings in order to be an effective competitor. IDF 1468.

As described by Mr. Pais, however, the plan never went beyond "the early stages." Pais, Tr. 1761-62. As of mid-2009, Sigma had "[n]o contracts with any foundries," only a couple of patterns borrowed from Sigma's Mexico supplier, no core boxes, no machining facilities, and no contract to complete the coating, painting, or lining. Pais, Tr. 2173-74. All of these are essential prerequisites for the production of fittings. IDF 1046-47. In August, Sigma informed its customer, U.S. Pipe, that Sigma had "not made any concrete plans to either invest in all the required tooling or not invest at all." IDF 1467. By the end of the summer, Sigma had a domestic foundry produce a couple of sample fittings, but the foundry was not prepared to do the machining, painting, or cement lining. Pais, Tr. 1803; IDF 1461, 1465. As of September, Sigma only had a small number of the needed patterns, and it did not have contracts with any pattern shops or domestic foundries. IDF 1470-72; Rona, Tr. 1672, 1674-76.

As a whole, Sigma's actions relating to the virtual manufacturing plan were merely exploratory and preliminary and certainly not those of a "reasonably probable" entrant. It invested no more than $50,000 to $75,000 toward the effort, a nominal sum when compared to Sigma's estimate that it would need $5 to $10 million to enter the domestic fittings market. IDF 1449, 1479-80.

Importantly, Sigma found itself facing significant financial challenges just as it was pursuing the idea of entering the domestic fittings market. Sigma's financial resources had been greatly strained by the economic downturn in 2008. At the end of 2008, Sigma had suffered a loss of [redacted], had only [redacted] in cash, and was over [redacted] in debt. IDF 1482, 1490-91, *in camera*; Pais, Tr. 2190, *in camera*. Sigma began 2009 with a large portion of its debt unsecured and subject to high interest rates, and it remained in a financially "precarious" position throughout the year. IDF 1483, 1489, 1493-94; ID at 426. In May 2009, Sigma's internal midterm review revealed that Sigma's financial situation was "bleak." IDF 1484; CX0214 at 002; Pais, Tr. 2163-64. By June, after the outlook continued to worsen, conditions reached a point where Mr. Pais presented Sigma's Board of Directors with an "SOS" plan to save Sigma. IDF 1496. With sales down [redacted], and despite laying off employees and making substantial cuts, Sigma ended 2009 breaching some of its bank covenants. IDF 1485, *in camera*, 1486-88.

Not surprisingly given Sigma's financial condition, its lenders imposed very low capital spending limits on the company in 2009. IDF 1499. During Sigma's July 2009 Board meeting, the Frontenac Group, a private equity firm with a 60 percent ownership interest in Sigma, opined that Sigma did not have the capability to invest in domestic fittings and declared that Frontenac would not finance Sigma's domestic production plan. IDF 1500-01. Against this backdrop, Sigma's ability to make an investment of $5 to $10 million to enter the domestic fittings market independently seems questionable at best.

Complaint Counsel nonetheless argues that all of this is outweighed by an e-mail from Walter Florence of Frontenac to Mr. Pais and other Sigma executives on July 27, twelve days after the July Board meeting, outlining proposals for various upcoming banking group meetings. In the context of discussing how Sigma could best pitch ideas to potential lenders, the e-mail states:

"Investors and rollover shareholders are prepared to invest up to $7.5m in equity . . . to fund domestic sourcing initiative and to fund the Strategic business additions which will enhance credit quality and help Sigma grow and build equity value." CX0099 at 007. According to Complaint Counsel, this e-mail demonstrates that Sigma would have been able to obtain financial backing to expand into domestic fittings.

We find the cited statement much more ambiguous, particularly when considered in light of the position taken by Frontenac at the Board meeting less than two weeks prior and the other substantial evidence of Sigma's financial struggles. Indeed, Mr. Pais's July 28 response to Mr. Florence is in line with all of the other evidence of Sigma's difficult financial situation. In his reply, Mr. Pais revealed a "setback" that the company had "just unearthed last evening, with a significant *unfavorable* variation in [Sigma's] EBITDA projections – of as much as even $2M – from the CORE business for 09 and possibly 2010, as compared to those projections presented @ the BOD meeting in Boston." CX0099 at 004 (emphasis in the original). As described by Mr. Pais, "heading into this bank meeting, [Sigma was] actually in an even worse position than [initially] believed." Pais, Tr. 2181.

In sum, the evidence shows that Sigma took only the most preliminary acts to enter the market on its own and that it lacked the financial means necessary to get its virtual manufacturing underway. By September 2009, Sigma's President and CEO recognized that it could not overcome the complexity of entering the domestic fittings market. Pais, Tr. 1801-04. Finding "no other option" for serving the domestic fittings market, Sigma turned to McWane. Pais, Tr. 1800-01. Accordingly, we do not find there was a reasonable probability that Sigma would have been McWane's competitor in the domestic fittings market.[17] *See*

17 Citing *Microsoft*, Complaint Counsel contends that, even if Sigma does not qualify as a potential competitor, the actions taken by McWane to eliminate the possibility of competition from a "nascent" entrant should nevertheless serve as *prima facie* evidence of anticompetitive conduct. *See Microsoft*, 253 F.3d at 79. In appropriate cases we will condemn anticompetitive activity, whether in the form of unreasonable restraints of trade or monopolization, that targets potential competition, as set forth in the Competitor Collaboration Guidelines at § 1.1 n.6 (2000), *Transource Int'l*, 725 F.2d at 280, and *Bombardier*, 605 F.2d at 9-11, or nascent competition, as set forth in *Microsoft*, 253 F.3d at 53-

Transource Int'l, 725 F.2d at 280 (finding that Transource lacked the financial ability to enter the market and had previous failures in manufacturing for a similar line of business); *Conergy AG v. MEMC Elec. Materials, Inc.*, 651 F. Supp. 2d 51, 57-58 (S.D.N.Y. 2009) (considering, on a motion to dismiss, plaintiff's background and experience in the industry, its affirmative acts to enter, its financial capabilities, and the contracts in place). It therefore follows that the MDA is not an unlawful horizontal agreement.

B. THE MDA WAS NOT AN UNREASONABLE VERTICAL RESTRAINT OF TRADE

Having concluded that Sigma was not a potential competitor of McWane, we now consider whether certain provisions in the MDA amounted to an unreasonable vertical restraint under the rule of reason. *See Leegin Creative Leather Prods. v. PSKS, Inc.*, 551 U.S. 877, 898 (2007) (holding that vertical restraints are analyzed under the rule of reason); *Transource Int'l*, 725 F.2d at 280 (analyzing the alleged restraint under the rule of reason after concluding that the relationship between the two firms was vertical rather than horizontal). Courts typically accord less scrutiny to vertical restraints than to horizontal restraints. *See Leegin*, 551 U.S. at 888 (noting that recent precedent recognizes the difference in economic effect between horizontal and vertical agreements); *Arizona v. Maricopa County Med. Soc'y*, 457 U.S. 332, 348 n.18 (1982) (noting that "horizontal restraints are generally less defensible than vertical restraints"). In assessing the lawfulness of a vertical restraint, we look to the "the restraint's history, nature, and effect," recognizing that a manufacturer with market power might use the restraint to facilitate collusion with its competitors or exclude new entrants or smaller rivals. *See Leegin*, 551 U.S. at 885-86, 893-94.

Complaint Counsel challenges three aspects of the MDA: (1) the fact that the MDA anointed McWane as Sigma's sole source of domestic supply and precluded Sigma from producing its own domestic fittings; (2) that it prescribed the minimum price at which Sigma could sell domestic fittings in competition with

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54, 79. We find the facts here to be distinguishable from the nascent competition at issue in *Microsoft.*

McWane; and (3) that it required Sigma to adhere to McWane's Full Support Program.

The ALJ centered his rule of reason analysis and finding of liability on the MDA's sole source and pricing provisions. He found that these terms were unnecessary for McWane to sell domestic fittings to Sigma and concluded that the availability of reasonable, less restrictive alternatives and the absence of procompetitive justifications rendered the MDA an unreasonable restraint of trade. ID at 433. We disagree with the ALJ's reasoning.

To the extent that the Initial Decision purports to find a violation because the terms were unnecessary or because McWane could have structured the MDA less restrictively, the analysis is flawed. The rule of reason first requires a basis for finding conduct anticompetitive. Only after there has been such a finding do courts consider whether there are less restrictive alternatives. *See Care Heating & Cooling, Inc. v. Am. Standard, Inc.*, 427 F.3d 1008, 1012 (6th Cir. 2005) (explaining that, under Section 1 rule of reason burden-shifting analysis, plaintiff bears the initial burden of showing the challenged restraint caused anticompetitive harm; the burden then shifts back to defendant to provide procompetitive justifications for the conduct, which, if met, allows plaintiff to provide evidence that any legitimate objectives can be achieved in a less restrictive manner); *Tanaka v. Univ. of S. Cal.*, 252 F.3d 1059, 1063 (9th Cir. 2001) (same); *see also* Hovenkamp, XI *Antitrust Law* ¶ 1913c, at 376 ("[A] showing of possible less restrictive alternatives is part of the 'burden shifting' procedure that goes on in a rule of reason case and is required only if the preceding inquiries warrant it . . . . That is, the availability of a purported less restrictive alternative does not make a challenged practice effectively illegal per se.").

The initial question, therefore, is whether the MDA, in place less than a year, caused anticompetitive harm. We begin with the sole source requirement, which prohibited Sigma from producing its own domestic fittings and barred Sigma from purchasing from Star. In light of our finding that Sigma was not a probable entrant in the domestic fittings market, we conclude that the prohibition against Sigma producing domestic fittings was unlikely to have had an anticompetitive effect.

We reach the same conclusion with respect to the MDA's pricing provisions. Although McWane had monopoly power in the domestic fittings market, Sigma was only one of many McWane distributors and it had a limited market presence in that market. IDF 1597. Indeed, there is no evidence in the record that the price restraint placed on Sigma had or was likely to have market-wide effects.

Finally, the MDA also prohibited Sigma from selling McWane's domestic fittings to any customers who bought from Star. To the extent there was any anticompetitive consequence resulting from this provision, we have already condemned McWane's conduct in connection with the Full Support Program in our discussion of Count 6, and there is no evidence that this provision materially added to the adverse competitive effects of the Full Support Program.

We therefore conclude that Complaint Counsel failed to establish that the MDA had or was likely to have anticompetitive effects in the domestic fittings market, apart from those already condemned. Accordingly, we reverse the ALJ's holding of liability on Count 4.[18]

VII. THE ALLEGED AGREEMENT TO CURTAIL PROJECT PRICING

Complaint Counsel alleges a conspiracy, initiated by McWane, to stabilize and raise fittings prices through two allegedly unlawful agreements. According to Complaint Counsel, in early 2008 McWane agreed with Star and Sigma to curtail project pricing, the major form of discounting in the industry, and

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18 We also dismiss Count 5, which alleges that by enlisting the assistance of Sigma in enforcing McWane's exclusive dealing program against Star, McWane and Sigma conspired to monopolize the domestic fittings market. We find this count subsumed by our resolution of Counts 4 and 6. *See* Phillip E. Areeda & Herbert Hovenkamp, IIIB *Antitrust Law* ¶ 809, at 463-67 (3d ed. 2008) (noting the redundancy between a claim of conspiracy to monopolize and Section 1 claim); s*ee also Int'l Distrib. Centers v. Walsh Trucking Co.*, 812 F.2d 786, 795-96 (2d Cir. 1987) (holding that establishing a conspiracy to monopolize claim requires largely the same proof as an unreasonable restraint of trade claim under Section 1).

later to raise its list prices in return for participation by Star and Sigma in the DIFRA information exchange.

On appeal, Complaint Counsel focuses on the first of the claimed agreements—the agreement to curtail project pricing. They point to a variety of circumstantial evidence from which they infer a price conspiracy, orchestrated by McWane through price signaling and other communications with Sigma and Star, designed to curtail project pricing and stabilize prices. Complaint Counsel contends the ALJ erred in a number of important respects, including that he: "failed to make reasonable inferences . . . and instead demanded direct proof of an agreement before any inference could be made," CCRB at 2; "improperly ignored evidence that Sigma and Star participated in the price-fixing conspiracy," CCAppB at 9; and failed to evaluate the evidence as a whole," instead "dissect[ing] each piece of the evidentiary puzzle, asking whether it alone made collusion more likely than not." *Id*. at 11.

McWane defends the ALJ's conclusion that "'[t]he totality of the evidence, given due weight and viewed as a whole, fails to demonstrate that [it], together with Sigma and Star, had an agreement'" or "'engaged in parallel conduct by curtailing Project Pricing'" and thus was "not consistent with the alleged conspiracy.'" RAnsB at 3 (quoting ID at 317-18, 350). In particular, McWane argues there were numerous project pricing episodes in 2008. Distinguishing between an unlawful agreement and independent action or conscious parallelism is often difficult, especially in contexts involving oligopolists. *See, e.g.*, *In re Flat Glass Antitrust Litig.*, 385 F.3d 350, 356-61 (3d Cir. 2009).

The Commission has not reached a majority as to liability on Count 1. Chairwoman Ramirez and Commissioner Brill find, by a preponderance of the evidence, that McWane, Sigma, and Star engaged in concerted action in violation of the law. Commissioners Ohlhausen and Wright, on the other hand, find the evidence insufficient to establish a conspiracy. In the absence of a majority decision, we dismiss Count 1 in the public interest.[19]

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19 Where no majority decision is reached on a claim or cause of action, the Commission may exercise its discretion to dismiss it. *See In re Ticor Title Ins.*

VIII. THE DIFRA INFORMATION EXCHANGE

Finally, Complaint Counsel also alleges that McWane conspired with Star and Sigma to exchange competitively sensitive sales information through DIFRA. They argue that this information enabled each of them "to determine and to monitor its own market share and, indirectly, the output levels of its rivals," thereby facilitating price collusion in a market already susceptible to pricing coordination, with no countervailing procompetitive justification. Complaint ¶¶ 35-36.

On appeal, Complaint Counsel points to evidence indicating that McWane, Sigma, and Star expected the DIFRA information exchange to allow them to better detect cheating and to stabilize prices and argues that the ALJ erred by "requiring direct evidence of actual price effects and ignoring evidence that the principal tendency of DIFRA was to facilitate collusion." CCAppB at 44. Specifically, Complaint Counsel argues that "the DIFRA exchange allowed each participant to monitor its own market share, and to deduce from monthly changes in that share, its rivals' relative price levels." *Id*. at 45. Emphasizing that the information exchanged was historical, aggregated data, McWane defends the ALJ's determination that "the evidence fails to prove that the DIFRA tons-shipped data reporting system has the nature and tendency to facilitate price coordination." ID at 362.

The Commission has not reached a majority as to liability on Count 2. Chairwoman Ramirez and Commissioner Brill find, by a preponderance of the evidence, that the DIFRA information exchange constituted an unlawful facilitating practice under a rule of reason analysis. Commissioners Ohlhausen and Wright, on the other hand, find the evidence insufficient to establish a violation of the rule of reason. Lacking a majority position, we dismiss Count 2 in the public interest.

IX. REMEDY

The Commission has considerable discretion in fashioning an appropriate remedial order, so long as the relief bears a reasonable

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Co., 112 F.T.C. 344, 442 n.13 (1989); *In re Am. Cyanamid*, 72 F.T.C. 623, 690 (1967).

relationship to the act or practice found unlawful. *See FTC v. Ruberoid Co*, 343 U.S. 470, 473 (1952); *Rubbermaid, Inc. v. FTC*, 575 F.2d 1169, 1174 (6th Cir. 1978). Having determined that McWane sought to maintain its monopoly power in the domestic fittings market through an unlawful exclusive dealing policy, we issue the attached order, which prohibits McWane from requiring exclusivity from its customers.

McWane objects to the remedy as moot, arguing that its exclusive dealing policy ended over two years ago and that the ALJ did not find any ongoing impact or threat of recurrence. In particular, McWane asserts that it modified its Full Support Program by January 2010, eliminating the provision stating that distributors risked losing shipments for up to 12 weeks if they did not support the program. It also notes that ARRA, which provided the initial impetus for the policy, is no longer in force. Under these circumstances, McWane argues, injunctive relief is unwarranted. We disagree.

First, it is well-established that the Commission may issue a cease and desist order even when a respondent no longer engages in the illegal conduct if there is sufficient danger of recurrence. *See W.M.R. Watch Case Corp. v. FTC*, 343 F.2d 302, 304 (D.C. Cir. 1965); *see also In re The Coca-Cola Co.*, 117 F.T.C. 795, 1994 FTC LEXIS 327, at *199 (1994) ("Voluntary cessation of unlawful activity is not a basis for halting a law enforcement action."). Thus, even assuming that McWane's Full Support Program ended over two years ago, that in itself does not bar a remedial order in this case.

More importantly, we are not persuaded that McWane has in fact ended its exclusive dealing policy. McWane has not publicly withdrawn the policy or notified distributors of any changes. *See* Tatman, Tr. 707-09 (asserting that the program was modified in January 2010, but that he never sent a letter to his customers to that effect). Whatever McWane may have decided internally, it failed to communicate a withdrawal of its policy to its distributors, and there is testimony from distributors who regard the exclusive dealing requirement as still in effect. *See* Thees, Tr. 3118 (Ferguson) (testifying that as far as he is aware, McWane never rescinded the policy or indicated that it was no longer in force); Morton, Tr. 2908-09, 2911 (U.S. Pipe) (testifying that no one from McWane communicated that the policy had been withdrawn or revised); Pitts, Tr. 3364-65 (Hajoca) (testifying that as far as he is aware, McWane never withdrew its policy); Sheley, Tr. 3419 (Illinois Meter) (stating that, as a result of McWane's policy, Illinois Meter still does not purchase domestic fittings from Star); Webb, Tr. 2770 (HD Supply) (testifying that an exclusive dealing policy remains in place). As the court explained in *Rubbermaid*, "The crucial question . . . is to what degree one can be certain that the same or related practices will not recur." 575 F.2d at 1172. Here, the record contains no public communication of a withdrawal and reflects distributor concern that the exclusive dealing policy has continued, which poses an even greater danger than a risk of recurrence.

Third, the fact that ARRA is no longer in effect is irrelevant. *See Rubbermaid*, 575 F.2d at 1171-73 (rejecting defendant's mootness claim based on repeal of legislation and discontinuance of the practice at issue). While ARRA may have provided the initial impetus for Star's entry into the domestic fittings market, other "Buy American" laws and buyer preferences remain, and McWane continues to have monopoly power in that market. Executives at the highest level of McWane's organization developed and implemented an exclusive dealing policy to maintain monopoly prices, and all but one of those executives remain at McWane. *See* IDF 20-38, 1145-92. Without an order, there is no reason to believe that McWane would not again attempt to protect its monopoly power in the domestic fittings market with exclusive dealing or other arrangements that have similar effects. *See Rubbermaid*, 575 F.2d at 1172 ("The Commission may be properly concerned not only with the open and formal implementation of agreements exactly like those entered into in the past, but also with the possibility that past unlawful conduct will be perpetuated in some more subtle form in the future.")

Finally, McWane argues that injunctive relief is only appropriate where the plaintiff shows there is an imminent threat of injury that is concrete and specific. The authority McWane relies on for this proposition, however, is inapposite. It speaks to Article III standing requirements and standards for injunctive relief in cases brought by private plaintiffs, rather than to the

Commission's remedial authority in exercise of its statutory law enforcement responsibilities.[20]

It is McWane that has the "formidable burden of showing that it is absolutely clear [its] allegedly wrongful behavior could not reasonably be expected to recur." *Friends of the Earth v. Laidlaw Envtl. Servs., Inc.*, 528 U.S. 167, 190 (1999); *accord Rubbermaid*, 575 F.2d at 1173 ("A company bears a heavy burden in showing that past conduct will not be repeated."). As the ALJ correctly concluded, "Respondent has not met that burden here." ID at 447.

Accordingly, we issue the attached cease and desist order to address McWane's exclusionary conduct. The order prohibits McWane from: (1) implementing or enforcing any condition, policy, or practice requiring exclusivity with a customer; (2) implementing or enforcing any retroactive rebate program that would effectively demand exclusivity; (3) "[d]iscriminating against, penalizing or otherwise retaliating" against any customer that purchases a competitor's domestic fittings or that "otherwise refuses to enter into or continue any condition [or] agreement" requiring exclusivity; and (4) "enforcing any condition, requirement, policy, agreement, contract or understanding that is inconsistent with the terms of [the] Order." Order, ¶¶ II.A.-D. The order is designed to bring an end to McWane's unlawful conduct, rectify its past violation, and ensure it does not recur. It is necessary and appropriate to remedy McWane's past and continuing competitive harm.

X. CONCLUSION

For the foregoing reasons, the Commission concludes that McWane violated Section 5 of the FTC Act, 15 U.S.C. § 45, by adopting an unlawful exclusive dealing policy to maintain its monopoly power in the domestic fittings market. Consequently,

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20 In *Winter v. NRDC*, 555 U.S. 7, 22 (2008), for instance, the Court clarified that a private party seeking a preliminary injunction must show the likelihood of irreparable injury rather than just the possibility. Similarly, in *Summers v. Earth Island Inst*., 555 U.S. 488, 493 (2009), and *Los Angeles v. Lyons*, 461 U.S. 95, 101-10 (1983), the Court addressed the requirements for Article III standing and equitable relief applicable to private plaintiffs. These cases do not apply to the Commission.

we issue a Final Order to remedy McWane's violation and prevent its recurrence.

FINAL ORDER

The Commission has heard this matter upon the appeals of Respondent and Complaint Counsel from the Initial Decision, and upon briefs and oral argument in support thereof and in opposition thereto. For the reasons stated in the accompanying Opinion of the Commission, the Commission has determined to dismiss Counts 1, 2, 4, 5, and 7 of the Complaint in this proceeding and issue an order to cease and desist in disposition of Count 6. The Initial Decision dismissed Count 3; that ruling was neither appealed nor placed on the Commission's docket for review, and the dismissal of Count 3 consequently became the Commission's final decision. 16 C.F.R. § 3.51(a). Accordingly,

IT IS ORDERED that Counts 1, 2, 4, 5, and 7 of the Complaint issued in this proceeding be, and hereby are, dismissed.

IT IS FURTHER ORDERED that the following Order to cease and desist be, and it hereby is, entered:

ORDER

I.

IT IS ORDERED that, as used in this Order, the following definitions shall apply:

A. "Commission" means the Federal Trade Commission.

B. "Respondent" means McWane, Inc., its officers, directors, employees, agents, representatives, successors, and assigns; and the United States based subsidiaries, divisions, groups, and affiliates controlled by it, and the respective officers, directors, employees, agents, representatives, successors, and assigns of each.

C. “Competitor” means Respondent and any person that, for the purpose of sale, or resale within the United States: (1) manufactures DIPF or Domestic DIPF; (2) causes DIPF or Domestic DIPF to be manufactured; or (3) imports DIPF.

D. “Customer” means any person that purchases any DIPF from Respondent.

E. “Designated Manager” means the Executive Vice President, General Manager, National Sales Manager, Pricing Coordinator, Regional Manager, or the OEM Manager for sales of DIPF in and into the United States, and any employee performing any job function relating to the setting of Prices (including offering any discounts) for DIPF sold in or into the United States.

F. “Domestic DIPF” means DIPF that is manufactured in the United States of America.

G. “Ductile Iron Pipe Fittings” or “DIPF” means any iron casting produced in conformity with the C153/A21 or C110/A21 standards promulgated by the American Water Works Association, including all revisions and amendments to those standards and any successor standards incorporating the C153/A21 or C110/A21 standards by reference.

H. “Exclusivity” or “Exclusive” means any requirement, whether formal or informal, or direct or indirect, by the Respondent that a Customer purchase all of their Domestic DIPF from Respondent, or any other requirement that a Customer restrain, refrain from, or limit its future purchases of Domestic DIPF from any Competitor.

Provided, however, that the terms “Exclusivity” or “Exclusive” do not:

1. apply to Respondent's sales of non-Domestic DIPF or any product other than Domestic DIPF; and

2. apply to individual bids of Domestic DIPF for specific jobs or refer to the sale by Respondent to a Customer of any specified number of units during any term, without more. For the avoidance of doubt, the fact that a Customer purchases its full requirements of Domestic DIPF from Respondent does not establish that Respondent has engaged in Exclusivity and is not prohibited by this Order unless the Customer does so because Respondent imposes a requirement of Exclusivity.

I. "Person" means any natural person or artificial person, including, but not limited to, any corporation, unincorporated entity, or government. For the purpose of this Order, any corporation includes the subsidiaries, divisions, groups, and affiliates controlled by it.

J. "Price" means the retail or wholesale price, resale price, purchase price, list price, multiplier price, job price, credit term, freight term, delivery term, service term, or any other monetary term defining, setting forth, or relating to the money, compensation, or service paid by a Customer to Respondent, or received by a Customer in connection with the purchase or sale of DIPF or Domestic DIPF.

K. "Retroactive Incentive" means any flat or lump-sum payment of monies or any other item(s) of pecuniary value to a customer based upon the Customer's sales or purchases of Respondent's Domestic DIPF reaching a specified threshold (in units, revenues, or any other measure), or otherwise reducing the Price of one unit of Respondent's Domestic DIPF because of the purchase or sale of an additional unit of that product. This definition excludes discounts or providing other item of pecuniary value to a customer based upon sales or purchases of Domestic DIPF beyond a specified threshold.

1. By way of example, Respondent may offer or provide a discount of X% on all sales of Domestic DIPF in excess of Y units, but it may not offer or provide a discount of X% on all units of Domestic DIPF if sales exceed Y units.

L. "Service" means any service, assistance or other support provided by Respondent to a Customer, including without limitation, responsiveness to requests for bids, responsiveness in filling purchase orders, product availability, handling of warranty claims, and handling of returns.

II.

IT IS FURTHER ORDERED that in connection with the business of manufacturing, marketing or selling Domestic DIPF in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, Respondent shall cease and desist from, either directly or indirectly, or through any corporate or other device:

A. Inviting, entering into, adhering to, maintaining, implementing, enforcing, or attempting thereto any condition, policy, practice, agreement, contract, or understanding that requires Exclusivity with a Customer, including but not limited to:

1. Conditioning the sale or purchase of any product, including Respondent's Domestic DIPF, on a Customer's Exclusivity;

2. Conditioning any term of Price or Service offered or provided by Respondent to a Customer relating to any product, including Respondent's Domestic DIPF, on a Customer's Exclusivity;

3. Conditioning any term of Price or Service offered or provided to a Customer based upon a requirement that the Customer purchase 50% or more of its purchases (in units, revenues, or any

other measure) of Domestic DIPF from Respondent over any period of time; and

4. Conditioning any term of Price or Service offered or provided to a Customer relating to any product marketed by Respondent upon that Customer's purchases or sales of Respondent's Domestic DIPF.

B. For ten (10) years from the date this Order becomes final, inviting, entering into, adhering to, maintaining, implementing, enforcing, or attempting thereto any condition, policy, practice, agreement, contract, or understanding that offers or provides any Retroactive Incentive.

C. Discriminating against, penalizing, or otherwise retaliating against any Customer, for the reason, in whole or in part, that the Customer engaged in, or intends to engage in, the distribution, purchase or sale of a Competitor's Domestic DIPF, or otherwise refuses to enter into or continue any condition, agreement, contract, or understanding that requires Exclusivity. Examples of prohibited discrimination or retaliation against a Customer shall include, but not be limited to:

1. Terminating, suspending, or threatening or proposing thereto, sales of any product marketed by the Respondent to the Customer;

2. Auditing the Customer's purchases or sales of Domestic DIPF to determine the extent of purchases or sales of competing Domestic DIPF;

3. Withdrawing or modifying, or threatening or proposing thereto, any terms of Price or Service offered or provided by Respondent to a Customer relating to any product marketed by Respondent; and

4. Refusing to deal with a Customer on terms and conditions generally available to other Customers.

D. After ninety (90) days from the date this Order becomes final, from enforcing any condition, requirement, policy, agreement, contract or understanding that is inconsistent with the terms of this Order.

Provided, however, that nothing in Paragraphs II A-D of this Order prohibits Respondent from providing discounts, rebates, or other Price or non-Price incentives to purchase Domestic DIPF that are (i) volume-based, above average variable cost, and not Retroactive Incentives as defined herein; or (ii) designed to meet competition, if Respondent determines in good faith that one or more Competitors are offering terms of sale for their Domestic DIPF that Respondent needs to match in order to win contested business.

Provided, further, that nothing in Paragraph II.D of this Order prohibits Respondent from honoring or providing discounts, rebates, or other Price or non-Price incentives to purchase its Domestic DIPF that a Customer contracted for prior to the date this Order becomes final even if paid or provided by Respondent subsequent to that date.

III.

IT IS FURTHER ORDERED that Respondent shall:

A. Within sixty (60) days from the date this Order becomes final distribute by first-class mail, return receipt requested, or by electronic mail with return confirmation, a copy of this Order with the Complaint, to each of its officers, directors, and Designated Managers;

B. Within sixty (60) days from the date this Order becomes final, distribute by first-class mail, return receipt requested, or by electronic mail with return confirmation, a copy of this Order with the Complaint, to each Customer of Respondent that has purchased DIPF or Domestic DIPF at any time since September 1, 2012;

C. For ten (10) years from the date this Order becomes final, distribute by first-class mail, return receipt requested, or by electronic mail with return confirmation, a copy of this Order with the Complaint, within sixty (60) days, to each Person who becomes its officer, director, or Designated Manager and who did not previously receive a copy of this Order and Complaint; and

D. Require each person to whom a copy of this Order is furnished pursuant to Paragraphs III.A and III.C of this Order to sign and submit to Respondent within sixty (60) days of the receipt thereof a statement that: (1) represents that the undersigned has read and understand the Order; and (2) acknowledges that the undersigned has been advised and understands that non-compliance with the Order may subject Respondent to penalties for violation of the Order.

IV.

IT IS FURTHER ORDERED that Respondent shall file verified written reports within ninety (90) days from the date this Order becomes final, annually thereafter for ten (10) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice require. Each report shall include, among other information that may be necessary:

A. Copies of the signed return receipts or electronic mail with return confirmations required by Paragraphs III.A-D of this Order;

B. A detailed description of the manner and form in which Respondent has complied and is complying with this Order.

V.

IT IS FURTHER ORDERED that Respondent shall notify the Commission:

A. Of any change in its principal address within twenty (20) days of such change in address; and

B. At least thirty (30) days prior to any proposed: (1) dissolution of Respondent; (2) acquisition, merger, or consolidation of Respondent; or (3) any other change in Respondent including, but not limited to, assignment and the creation or dissolution of subsidiaries, if such change might affect compliance obligations arising out of this Order.

VI.

IT IS FURTHER ORDERED that, for the purpose of determining or securing compliance with this Order, Respondent shall permit any duly authorized representative of the Commission:

A. Access, during office hours of Respondent, and in the presence of counsel, to all facilities and access to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and all other records and documents in the possession, or under the control, of Respondent relating to compliance with this Order, which copying services shall be provided by Respondent at its expense; and

B. Upon fifteen (15) days notice, and in the presence of counsel, and without restraint or interference from it, to interview officers, directors, or employees of Respondent.

VII.

IT IS FURTHER ORDERED that this Order shall terminate twenty (20) years from the date it becomes final.

By the Commission.

Dissenting Statement of Commissioner Joshua D. Wright

Introduction[1]

I dissent from the Commission's holding that McWane unlawfully monopolized the Domestic Fittings market.[2] In my view, Complaint Counsel has not met its burden to show by a preponderance of the evidence that McWane's Full Support Program harmed competition in the Domestic Fittings market.[3]

Antitrust law has evolved dramatically over the past several decades to incorporate established economic learning.[4] One of the most important developments at the Supreme Court was the Court's recognition that "Congress designed the Sherman Act as a 'consumer welfare prescription.'"[5] The federal antitrust laws,

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1 References to the record are made using the following citation forms and abbreviations:

CC Answering Brief – Complaint Counsel's Answering Brief filed July 2, 2013
Commission Opinion
Complaint – Complaint filed January 4, 2012
CX# – Complaint Counsel Exhibit
IDF – Numbered Findings of Fact in ALJ's Initial Decision
McWane Brief – Respondent McWane, Inc.'s Appeal Brief filed May 31, 2013
Name of Witness, Tr. – Transcript of Trial before the ALJ
Oral Argument Tr. – Transcript of Oral Argument before the Commission August 22, 2013
RX# – Respondent Exhibits
[redacted] **– In Camera Material**

2 I concur with the Commission's decision to reverse the Initial Decision on Counts 4 and 5 and join the Commission's Opinion with respect to those Counts. I also concur with the Commission's decision to dismiss Counts 1 and 2 in the public interest and join the Commission's Opinion with respect to those Counts. I concur with the Commission's decision to dismiss Count 7 but I do so for separate reasons explained below.

3 Though I do not discuss whether Complaint Counsel established that there is a separate relevant market for domestic fittings, I do not join that portion of the Commission's Opinion.

4 Leah Brannon & Douglas H. Ginsburg, *Antitrust Decisions of the U.S. Supreme Court 1967 to 2007*, 3 COMPETITION POL'Y INT'L 1 (2007).

5 Reiter v. Sonotone Corp., 442 U.S. 330, 343 (1979) (quoting R. BORK, THE ANTITRUST PARADOX 66 (1978)).

including the Sherman Act, the Clayton Act, and the Federal Trade Commission Act, have proved enormously flexible in this regard. Perhaps the greatest shift in antitrust jurisprudence since the bad old days has occurred in the area of vertical restraints, the subject of the Supreme Court's decision in *GTE Sylvania* in 1977, which changed the focus of antitrust from achieving a hodgepodge of economic, social, and political goals, to a legal regime concerned entirely with the "market impact" of business conduct.[6] With regard to vertical restraints, it is well-accepted that the economic learning accumulated since *GTE Sylvania* has taught that such restraints, a category that includes vertical territorial restrictions, resale price maintenance, exclusive dealing, loyalty discounts, tying, and other related business practices, rarely harm competition and often benefit consumers by increasing demand and/or creating a more efficient distribution channel.[7]

Complaint Counsel has asked the Commission to conclude that McWane's Full Support Program – a vertical restraint – violates Section 2 of the Sherman Act, and the Commission has

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6 Cont'l TV, Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 51-52 (1977); *see also* William E. Kovacic & Carl Shapiro, *Antitrust Policy: A Century of Economic and Legal Thinking*, 14 J. ECON. PERSP. 43, 53 (2000) (describing *GTE Sylvania* as the "pivotal event" in the evolution of antitrust doctrine because the Court "emphasized that the analysis of economic effects provided the proper basis for evaluating conduct under the antitrust laws"). In *GTE Sylvania*, the Court also declared interbrand competition "the primary concern of antitrust law." 433 U.S. at 52 n.19.

7 James C. Cooper et al., *Vertical Antitrust Policy as a Problem of Inference*, 23 INT'L J. INDUS. ORG. 639, 658 (2005) (stating that although "some studies find evidence consistent with both pro- and anticompetitive effects . . . virtually no studies claim to have identified instances where vertical practices were likely to have harmed competition"); Francine Lafontaine & Margaret Slade, *Exclusive Contracts and Vertical Restraints: Empirical Evidence and Public Policy in* HANDBOOK OF ANTITRUST ECONOMICS 391 (Paolo Buccirossi ed., 2008) ("[I]t appears that when manufacturers choose to impose restraints, not only do they make themselves better off but they also typically allow consumers to benefit from higher quality products and better service provision"); Daniel O'Brien, *The Antitrust Treatment of Vertical Restraints: Beyond the Possibility Theorems in* THE PROS AND CONS OF VERTICAL RESTRAINTS 40, 72-73 (2008) ("[W]ith few exceptions, the literature does not support the view that [vertical restraints] are used for anticompetitive reasons" and vertical restraints "are unlikely to be anticompetitive in most cases").

acquiesced by so holding. This appeal comes to the Commission after a full trial on the merits, which yielded a 464-page opinion from the Administrative Law Judge. The posture of this case is not a motion to dismiss or a motion for summary judgment. The standard of review the Commission is to apply is *de novo*.[8] Accordingly, the Commission's task on appeal is not to determine whether Complaint Counsel asserts a plausible theory of competitive harm or whether there is *some* evidence in the record that tends to show the Respondent was seeking impermissibly to maintain a monopoly position. Rather, the Commission's task is to look at all the evidence in the record and to decide whether Complaint Counsel has carried its burden to prove that McWane's conduct harmed competition. That is, whether the evidence in the record matches and is sufficient to support Complaint Counsel's theory of harm.

At the most basic level, Complaint Counsel's task is to prove that McWane's conduct caused harm to competition.[9] This is a simpler task than typical merger analysis, which requires Complaint Counsel to offer and the Commission to evaluate a *prediction* about *future consequences*. That forward-looking exercise requires a prediction and subsequent comparison of two different futures: one with and one without the allegedly unlawful merger. Here, the Commission is faced with evaluating allegedly anticompetitive conduct that has already taken place. Indeed, the Commission's task is to assess whether the Full Support Program – conduct that first began in 2009 – harmed competition. Precisely because the market has already experienced McWane's allegedly anticompetitive conduct, the Commission has access to a source of critical evidence not usually available in the typical scenario. Specifically, the Commission is able to test Complaint Counsel's theory of competitive harm against evidence of actual market impact.

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8 16 C.F.R. § 3.54 (2013).

9 Rambus v. FTC, 522 F.3d 456, 466-67 (D.C. Cir. 2008) (conduct cannot cause an anticompetitive outcome unless plaintiff can show that outcome would not have occurred but for the challenged conduct); United States v. Microsoft, 253 F.3d 34, 79 (D.C. Cir. 2001) (en banc) (per curiam) (plaintiff must show that defendant's conduct made a "significant contribution" to an anticompetitive outcome).

There is ample record evidence demonstrating that the Full Support Program harmed McWane's rival Star. But, in my view, Complaint Counsel fails totally to establish, as it must under the antitrust laws, that McWane's conduct harmed *competition*. Complaint Counsel could have taken either or both of two general approaches to demonstrate McWane's conduct harmed competition: direct or indirect evidence of anticompetitive effect. Complaint Counsel makes no effort to establish harm to competition directly, such as by demonstrating that McWane's conduct had a deleterious effect upon price or output in the Domestic Fittings market.[10] Instead, Complaint Counsel and the Commission rely upon indirect evidence including market share estimates and imprecise estimates regarding how much the Full Support Program "foreclosed" Star from access to distributors. This evidence is only indirectly relevant to establishing the Full Support Program harmed competition in the Domestic Fittings market because it requires a number of inferences to be drawn and assumptions to be made to establish such a connection. Indeed, the most probative indirect evidence in the record – evidence of Star's successful entry in the Domestic Fittings market and its growing market share – undermines Complaint Counsel's theory of harm. If the challenged conduct that occurred in 2009 and 2010 harmed competition, Complaint Counsel ought to be able to prove it with evidence that *consumers of domestic pipe fittings are worse off as a result of McWane's conduct*. The record is clear that there is no such proof.

The well-established economic learning setting forth the limited theoretical conditions under which a firm can use vertical restraints to monopolize a market, and the state of empirical economic literature demonstrating that such restraints rarely harm competition make clear that although vertical restraints such as the Full Support Program certainly can harm competition under

10 Such direct evidence of an impact upon price or output might be, for example, a comparison of actual prices and industry output during the relevant time period against an estimate of the prices and output that would have occurred during the relevant time period had McWane not engaged in the challenged conduct. If price was higher or output was lower and the difference could be properly attributed to McWane's conduct rather than to other contemporaneous changes in the market, then this evidence would constitute direct evidence that McWane's conduct harmed competition.

some circumstances, those circumstances are the exception to the general rule that vertical restraints are a normal part of the competitive process and benefit consumers. The Commission should be skeptical of attempts to establish competitive harm in vertical cases solely through the use of indirect evidence and inferences of competitive injury.[11] That skepticism should be heightened in cases, such as this one, involving allegations of anticompetitive conduct that has been occurring in the marketplace for some time, which ought to enable the Commission to ascertain its competitive footprint. Given the dearth of record evidence demonstrating that McWane's conduct has had an adverse effect on competition, I do not believe Complaint Counsel has carried its substantial burden.[12] Accordingly, I respectfully dissent from the Commission's holding that McWane unlawfully monopolized the Domestic Fittings market.

I. Count 6: Unlawful Monopolization

Section 2 of the Sherman Act prohibits acts to "monopolize."[13] The Supreme Court has explained that "[t]he offense of monopoly under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *United States v. Grinnell*, 384 U.S. 563, 570-71 (1966). I dissent from the Commission's decision because in my view Complaint Counsel has failed to establish the second

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11 *See* Timothy J. Muris, *The FTC and the Law of Monopolization*, 67 ANTITRUST L.J. 693, 723 (2000) (emphasizing that allowing evidence of harm to a competitor to suffice in monopolization cases "would make it too easy to infer injury to competition from the fact of injury to competitors").

12 Because Complaint Counsel has not carried its *prima facie* burden of establishing anticompetitive effect, I do not consider whether Respondent has asserted a non-pretextual procompetitive justification for the Full Support Program.

13 15 U.S.C. § 2 (2012).

element of a monopolization claim: that McWane's conduct was exclusionary.[14]

A. **The Law of Exclusionary Conduct**

To reach the conclusion that unilateral conduct is exclusionary and therefore a potential violation of Section 2 of the Sherman Act, a trier of fact must undertake the difficult task of separating *bona fide* anticompetitive conduct from competition on the merits. In the words of the D.C. Circuit, "[w]hether any particular act of a monopolist is exclusionary, rather than merely a form of vigorous competition, can be difficult to discern: the means of illicit exclusion, like the means of legitimate competition, are myriad." *Microsoft*, 253 F.3d at 58. Though this exercise is often fact-intensive, courts have laid out some helpful guidelines. Judge Bork observed that exclusionary or predatory conduct "involves aggression against business rivals through the use of business practices that would not be considered profit maximizing except for the expectation that (1) actual rivals will be driven from the market, or the entry of potential rivals blocked or delayed, so that the predator will gain or retain a market share sufficient to command monopoly profits, or (2) rivals will be chastened sufficiently to abandon competitive behavior the predator finds threatening to its realization of monopoly profits." *Neumann v. Reinforced Earth Co.*, 786 F.2d 424, 427 (D.C. Cir. 1986).

The D.C. Circuit in *Microsoft* set forth the general burden-shifting procedure a court should undertake in deciding whether conduct is exclusionary under the meaning of Section 2:

> First, to be condemned as exclusionary, a monopolist's act must have an 'anticompetitive effect.' That is, it must

14 The Commission has also decided that Complaint Counsel established the first element of the offense: that McWane has monopoly power in the Domestic Fittings market. Because both elements must be established for Complaint Counsel to succeed on appeal and it has not, in my view, established the second element, I need not decide whether Complaint Counsel has proven that McWane has monopoly power in a relevant market. For purposes of my Dissenting Statement, I assume but do not decide that McWane has monopoly power in the Domestic Fittings market. Nevertheless, I decline to join the Commission's decision that McWane has monopoly power in the Domestic Fittings market.

> harm the competitive *process* and thereby harm consumers. In contrast, harm to one or more *competitors* will not suffice. The Sherman Act directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself . . .
>
> Second, the plaintiff, on whom the burden of proof of course rests must demonstrate that the monopolist's conduct indeed has the requisite anticompetitive effect. In a case brought by . . . the Government, it must demonstrate that the monopolist's conduct harmed competition, not just a competitor.
>
> Third, if a plaintiff successfully establishes a *prima facie* case under § 2 by demonstrating anticompetitive effect, then the monopolist may proffer a 'procompetitive justification' for its conduct. If the monopolist asserts a procompetitive justification — a nonpretextual claim that its conduct is indeed a form of competition on the merits because it involves, for example, greater efficiency or enhanced consumer appeal — then the burden shifts back to the plaintiff to rebut that claim.
>
> Fourth, if the monopolist's pro-competitive justification stands unrebutted, then the plaintiff must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit . . .
>
> Finally, in considering whether the monopolist's conduct on balance harms competition and is therefore condemned as exclusionary for purposes of § 2, our focus is upon the effect of that conduct, not upon the intent behind it. Evidence of the intent behind the conduct of a monopolist is relevant only to the extent it helps us understand the likely effect of the monopolist's conduct.

Microsoft, 253 F.3d at 58-59. The point of contention between my position and that of the Commission is whether Complaint Counsel can proceed beyond the second step, that is whether, assuming McWane is a monopolist, the Full Support Program has anticompetitive effect. In my view, Complaint Counsel has failed to carry its burden to show that the Full Support Program has had anticompetitive effect.

B. **Exclusive Dealing as a Form of Exclusionary Conduct**

Economic theory shows that exclusive dealing, like most vertical restraints, can harm competition under certain circumstances but can also result in procompetitive efficiencies that benefit consumers. Modern economic theory teaches that exclusive contracts can harm competition when a monopolist uses exclusivity provisions in contracts with suppliers or distributors to raise the cost its rival faces in buying supply or contracting with distributors. Absent these contracts, the rival (or entrant) could cover its fixed costs by attracting a large enough mass of suppliers or distributors.

Economists have developed theories under the moniker of "raising rivals' costs" to articulate the conditions under which it is theoretically possible for a monopolist to use exclusive dealing to harm competition. *See* Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price*, 96 YALE L.J. 209 (1986); Steven C. Salop & David T. Scheffman, *Raising Rivals' Costs*, 73 AM. ECON. REV. 267 (1983). The critical issue is "[w]hether the exclusionary rights arrangement will so limit remaining supply available to rivals that it will lead them to bid up the price of that supply, thereby increasing their costs to the point that the purchaser obtains power over price." Krattenmaker & Salop, 96 YALE L.J. at 259. These economic models make clear that exclusive dealing cannot result in the acquisition or maintenance of market power and harm competition unless the contracts foreclose a rival from access to a critical input necessary to achieve minimum efficient scale (MES).[15] In other words, a

15 Minimum efficient scale is "the size plant that can produce the smallest amount of output such that long-run costs are minimized." DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 783 (4th ed., 2004). The concept of "raising rivals' costs" underlying modern anticompetitive theories of exclusion generally requires input foreclosure sufficient to deprive a rival from achieving minimum efficient scale. *See* Krattenmaker & Salop, 96 YALE L.J. at 247 ("[E]xcluded rivals no longer produce at minimum cost if the exclusionary rights agreement compels them to substitute less efficient inputs."); Benjamin Klein, *Exclusive Dealing as*

coherent theory of exclusion involving exclusive dealing contracts requires an analytical link between the contracts and the MES of production.[16]

The "foreclosure rate" contemplated by the economic paradigm of raising rivals' costs can provide this analytical link in the absence of direct evidence that the exclusive dealing contracts have caused the maintenance or acquisition of market power and have resulted in higher prices and reduced output. Whereas earlier and now discredited formulations of foreclosure raised the concern that exclusive dealing contracts between an input supplier and a buyer foreclosed rival buyers from access to that input seller, Krattenmaker & Salop, 96 Yale L.J. at 231-32, the modern economics of raising rivals' costs recognizes that determining a rate of foreclosure is not the end of the economic analysis, but rather is a starting point for a broader inquiry into whether the contracts raise a rival supplier's costs sufficiently to impact the competitive process.[17]

C. Exclusive Dealing and the Antitrust Statutes

Complaint Counsel has alleged and the Commission has concluded that McWane's Full Support Program is illegal exclusionary conduct because it is a form of exclusive dealing. Complaint ¶ 57; CC Answering Brief at 14-15; Commission Opinion at 22-29. Though the Full Support Program is not part of an agreement between McWane and any of its distributors, Complaint Counsel argued and the Commission concluded that the Full Support Program operated like an exclusive dealing

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Competition for Distribution "On the Merits," 12 GEO. MASON L. REV. 119, 122-28 (2003) ("[I]f exclusive contracts foreclose a sufficient share of distribution to rivals for a significant time so that what remains to serve competitors cannot support a manufacturer of minimum efficient scale, the exclusive will force existing competitors and potential new entrants to operate at a cost disadvantage. The exclusives then may have the effect of driving out and/or preventing entry of manufacturing competitors until sufficient distribution becomes available.").

16 Klein, *supra* note 15, at 126 ("Th[is] economic analysis . . . implies that the critical market share foreclosure rate should depend upon the [MES] of production.").

17 Krattenmaker & Salop, *supra* note 15, at 275.

arrangement. CC Answering Brief at 14-15; Commission Opinion at 20-22. Though I agree with Complaint Counsel and the Commission that the Full Support Program presents the same antitrust issues as would a case involving an explicit exclusivity arrangement, I disagree with their conclusion that the Full Support Program caused harm to competition. To understand why I disagree, it is worthwhile first to consider the evolution of the legal treatment of exclusive dealing claims under the antitrust laws.

Historically, exclusive dealing arrangements have been attacked under multiple provisions of the antitrust laws: Section 1 of the Sherman Act, which prohibits contracts, combinations, and conspiracies in restraint of trade, [18] Section 2 of the Sherman Act, which prohibits unlawful monopolization,[19] and Section 3 of the Clayton Act, which prohibits exclusive sales arrangements where the effect may be to substantially lessen competition or tend to create a monopoly.[20] Prior to the passage of the Clayton Act in 1914, exclusive dealing arrangements were typically upheld both under the common law and in cases brought under the Sherman Act, which was passed in 1890.[21] After the Clayton Act was passed, however, plaintiffs began to use Section 3 of that statute to prosecute exclusive dealing arrangements, and courts began to interpret the Sherman Act more broadly to prohibit certain exclusive dealing arrangements.[22] The three statutory provisions

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18 15 U.S.C. § 1 (2012).

19 15 U.S.C. § 2 (2012).

20 15 U.S.C. § 14 (2012). Exclusive dealing arrangements can also be prosecuted by the Commission as an unfair method of competition under Section 5 of the FTC Act. 15 U.S.C. § 45(a).

21 PHILLIP E. AREEDA & HERBERT H. HOVENKAMP, ANTITRUST LAW ¶ 1800c (3d ed. 2011) (citing Mogul Steamship Co. v. McGregor, Gow & Co., [1892] A.C. 25, 66 Law Times 1 (1892); Whitwell v. Continental Tobacco Co., 125 F. 454 (8th Cir. 1903) (approving tobacco company's granting of rebates to dealers who did not sell competing brands)) [hereinafter *AREEDA*].

22 Jonathan M. Jacobson, *Exclusive Dealing, "Foreclosure," and Consumer Harm*, 70 ANTITRUST L.J. 311, 317 (2002) ("Passage of the Clayton Act did in fact result, almost immediately, in more and successful challenges to exclusive dealing arrangements."); United States v. Am. Can Co., 230 F. 859, 875 (D.

have different requirements, which led courts to apply different standards depending upon the statutory provision under which the plaintiff pursued its claim. For example, Section 1 requires concerted action between two separate entities, whereas Section 2 does not. Section 2, on the other hand, requires some analysis of monopoly and monopoly power, whereas Section 1 and Section 3 focus instead on "market power." Finally, Section 3 requires a "sales" arrangement whereas neither of the other two statutory provisions includes such a requirement.[23]

Today, though the statutory provision under which the claim is pursued makes some difference depending upon the circumstances, the law of exclusive dealing under the three provisions has largely converged in recent years. One commentator has opined that "[t]he focus today is whether exclusive dealing is unreasonably anticompetitive. Which statute is used as the basis for challenge no longer really matters."[24]

In any event, though the statute under which a plaintiff pursues its claim can have some effect on whether its claim is successful, a plaintiff must *always* establish that the exclusive dealing arrangement harms competition as understood under the familiar antitrust rule of reason.[25]

Md. 1916) (holding an exclusive dealing arrangement unlawful under the Sherman Act).

23 *See* A*REEDA*, *supra* note 21, ¶ 1800c.

24 Jacobson, *supra* note 22, at 327 (describing the collapse of any distinction between jurisprudence under Section 1 of the Sherman Act and Section 3 of the Clayton Act); *see also* Microsoft, 253 F.3d at 70 ("The basic prudential concerns relevant to §§ 1 and 2 are admittedly the same: exclusive contracts are commonplace—particularly in the field of distribution—in our competitive, market economy, and imposing upon a firm with market power the risk of an antitrust suit every time it enters into such a contract, no matter how small the effect, would create an unacceptable and unjustified burden upon any such firm. At the same time, however, we agree with plaintiffs that a monopolist's use of exclusive contracts, in certain circumstances, may give rise to a § 2 violation even though the contracts foreclose less than the roughly 40% or 50% share usually required in order to establish a § 1 violation.").

25 Jacobson, *supra* note 22, at 323 (more recent exclusive dealing cases have "reduced the focus on foreclosure and placed greater emphasis on the need to prove market power and actual consumer harm."); *cf.* Brooke Group Ltd. v.

D. The Law of Exclusive Dealing and Anticompetitive Effect

As with many business practices once routinely condemned by courts, antitrust law has become more hospitable toward exclusive dealing arrangements – less likely to hold them to be anticompetitive – as time has passed.[26] The Supreme Court first held certain exclusive dealing arrangements to be unlawful under Section 3 of the Clayton Act in 1922 in *Standard Fashion Co. v. Magrane-Houston Co.*, 258 U.S. 346 (1922) and *United Shoe Machinery Corp. v. United States*, 258 U.S. 451 (1922). In the 1949 *Standard Stations* case, the Supreme Court introduced quantitative "foreclosure" analysis into the law of exclusive dealing. *Standard Oil Co. (Cal) v. United States*, 337 U.S. 293 (1949). A rival is said to be "foreclosed" from access to a distributor if the distributor has committed to deal with a specific supplier exclusively. The Court held that all that was necessary for there to be a violation of Section 3 of the Clayton Act was "proof that competition has been foreclosed in a substantial share of the line of commerce affected." *Id.* at 314. What constitutes a "substantial share" of the line of commerce occupied courts' attention for much of the last half of the twentieth century.

The last time the Court squarely considered an exclusive dealing claim was in 1961 in *Tampa Electric* in which it upheld a 20-year exclusive arrangement that the Court determined foreclosed only a very small percentage of the market. There the Court essentially repeated the same standard, announcing that "the competition foreclosed by the contract must be found to constitute a substantial share of the relevant market." *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320, 328 (1961). Providing some guidance to lower courts, the Court stated that "[t]o determine substantiality in a given case, it is necessary to weigh the probable effect of the contract on the relevant area of effective competition, taking into account the relative strength of the parties, the proportionate volume of commerce involved in relation to the

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Brown & Williamson Tobacco Corp., 509 U.S. 209, 224-25 (1993) (injury to a competitor is "of no moment to the antitrust laws if competition is not injured . . . . Even an act of pure malice by one business competitor against another does not, without more, state a claim under the federal antitrust laws.").

26 Jacobson, *supra* note 22, at 323-325.

total volume of commerce in the relevant market area, and the probable immediate and future effects which pre-emption of that share of the market might have on effective competition therein. It follows that a mere showing that the contract itself involves a substantial number of dollars is ordinarily of little consequence." *Id.* at 329. In *Tampa Electric* the Court therefore made clear that some "measure" of foreclosure is not the "be all end all" of exclusive dealing jurisprudence and that the probative value of any foreclosure measurement must be interpreted in the context of its relationship to the likely market impact of the restraint at issue.

The Commission itself ushered in the modern era of exclusive dealing analysis in 1982 by holding explicitly that exclusive dealing arrangements are governed by the rule of reason and not subject to a special rule that weighs some measure of foreclosure above all other factors. In *Beltone*, recognizing a trend that courts had been "employ[ing] a fuller rule-of-reason analysis" in exclusive dealing cases, we held that that exclusive dealing ought to be governed by the same legal standard – the rule of reason – the Supreme Court had applied to all nonprice vertical restraints five years earlier in *GTE Sylvania*: "A proper analysis of exclusive dealing arrangements should take into account market definition, the amount of foreclosure in the relevant markets, the duration of the contracts, the extent to which entry is deterred, and the reasonable justifications, if any for the exclusivity." *In re Beltone Electronics Corp.,* 100 F.T.C. 68, 204 (1982).

We went on to observe that, "in weighing the potentially diverse effects of a distributional restriction, it should be recognized that the process is not conducive to fine line drawing. Given the limited state of knowledge (especially empirical information) we now have about the actual effects of these practices on competition, *it seems desirable to require reasonably clear evidence of probable overall competitive harm before condemning their use in a particular case*." *Id*. at 209 (emphasis supplied). We observed explicitly that foreclosure is "only one of several variables to be weighed in the rule-of-reason analysis applied to all nonprice vertical restraints." *Id.* at 204. The empirical knowledge accumulated about the competitive impact of exclusive dealing and related practices in the thirty-two years since *Beltone* suggests the practices can but generally do not harm competition,[27] a development that underscores the appropriateness of the Commission's conclusion that clear evidence of anticompetitive effect should be required before condemning any particular business arrangement.

After *Beltone*, the modern approach is to analyze exclusive dealing under the rule of reason, considering a host of factors, of which foreclosure is only one. A modern statement of the general rule is offered by Judge Posner:

> First [the plaintiff] must prove that [the challenged restraint] is likely to keep at least one significant competitor of the defendant from doing business in a relevant market. If there is no exclusion of a significant competitor, the agreement cannot possibly harm competition. Second, [the plaintiff] must prove that the probable (not certain) effect of the exclusion will be to raise prices above (and therefore reduce output below) the competitive level, or otherwise injure competition; he must show in other words that the anticompetitive effects (if any) of the exclusion outweigh any benefits to competition from it.

Roland Machinery Co. v. Dresser Indus., 749 F.2d 380, 394 (7th Cir. 1984). This statement of the law illustrates that exclusion of a competitor is necessary but not sufficient for liability: an exclusive dealing plaintiff must also establish harm to competition. In this sense, modern antitrust law has merged with modern economic theory: substantial foreclosure is necessary but not sufficient for plausible successful exclusion and is also required by the law.[28] The fundamental question as to whether a particular example of exclusive dealing is lawful has merged with the fundamental economic inquiry: does the arrangement harm competition?

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27 *See supra* note 7.

28 Klein, *supra* note 15, at 125 ("[a]ntitrust law is consistent with economic analysis, in that an exclusive must cover a substantial share of the market for liability").

The best and most straightforward way to establish harm to competition is, of course, direct evidence that the exclusive dealing arrangement caused prices to rise and output to fall relative to a but-for world in which the defendant did not employ exclusive dealing contracts. The procedural posture and the facts unique to a given case are undoubtedly relevant to whether such direct evidence will exist. A plaintiff is given much more leeway on a motion to dismiss or a motion for summary judgment.[29] For example, at the motion to dismiss phase, the plaintiff cannot be expected to have evidence that price rose or output fell as a result of the defendant's exclusive dealing arrangements. The plaintiff need only allege a set of facts that would allow a court to conclude that anticompetitive effects are the plausible result of the defendant's exclusive dealing arrangements.[30] Indeed, the procedural posture in *Roland Machinery* was a motion for a preliminary injunction against the defendant's exclusive dealing arrangements, which presumably is why Judge Posner was concerned about the "probable (not certain) effect of the exclusion." *Roland Machinery*, 749 F.2d at 394. When considering an exclusive dealing arrangement that occurred in the past and examining a record developed after lengthy discovery and a trial on the merits, a plaintiff has had ample opportunities to develop direct evidence of anticompetitive effects. Similarly, the Commission and the Department of Justice recognize the value of direct evidence when it is available, such as when examining mergers that have already taken place, as opposed to the normal merger review process that requires predictions about the future, "[e]vidence of observed post-merger price increases or other changes adverse to customers is given *substantial weight*." U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 2.1.1 (2010), *available at* http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf (emphasis supplied).

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29 *See* Bennett v. Spear, 520 U.S 154, 167-68 (1997) ("[W]hile a plaintiff must set forth by affidavit or other evidence specific facts to survive a motion for summary judgment, and must ultimately support any contested facts with evidence adduced at trial, at the pleading stage, general factual allegations of injury resulting from the defendant's conduct may suffice, for on a motion to dismiss we presume that general allegations embrace those specific facts that are necessary to support the claim") (internal citations omitted).

30 Bell Atl. Corp. v. Twombly, 550 U.S. 544, 556 (2007).

Though direct evidence of anticompetitive effects is the most persuasive type of evidence in an antitrust case,[31] courts in exclusive dealing cases have held that a plaintiff may prove its case indirectly by considering various observable market factors that allow a court to infer whether anticompetitive effect is likely to have occurred in the market at issue. One of these factors is an estimate of the significance of market foreclosure caused by the exclusive dealing arrangement, but the law is clear that market foreclosure is but one of several factors.[32] *See e.g., Ryko Mfg. Co. v. Eden Services*, 823 F.2d 1215 (8th Cir. 1987) ("[W]here, as here, the foreclosure rate is neither substantial nor even apparent, the plaintiff must demonstrate that other factors in the market exacerbate the detrimental effect of the challenged restraints"); *Beltone*, 100 F.T.C. at 204 (foreclosure is "only one of several variables to be weighed in the rule-of-reason analysis now applied to all nonprice vertical restraints."); *cf. Microsoft*, 253 F.3d at 69 ("the requirement of a significant degree of foreclosure serves a useful screening function").

Other factors are the duration and terminability of the exclusive dealing arrangement. As one court explained, "the short duration and easy terminability of [certain] agreements negate substantially their potential to foreclose competition." *Omega Envtl., Inc. v. Gilbarco, Inc.*, 127 F.3d 1157, 1163 (9th Cir. 1997); *see also W. Parcel Express v. United Parcel Serv. Of Am., Inc.*, 190 F.3d 974, 976 (9th Cir. 1999) (holding that "termination provisions that allowed a customer to terminate the contract for any reason with very little notice" were relevant to upholding agreements). Many courts have held that exclusive dealing

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31 *See* FTC v. Indiana Fed'n of Dentists, 476 U.S 447, 460-61 (1987) ("Since the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, proof of actual detrimental effect, such as a reduction of output, can obviate the need for an inquiry into market power, which is but a surrogate for detrimental effects.") (internal citations omitted).

32 This is because it can be difficult to separate foreclosure that is caused by the exclusive dealing arrangement – the foreclosure the antitrust laws are concerned with – from the consequences of actual competition. *See* Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 236 (1st Cir. 1983) (Breyer, J.) ("[V]irtually every contract to buy 'forecloses' or 'excludes' alternative sellers from some portion of the market, namely the portion consisting of what was bought").

contracts of one year or less are presumptively legal. *See e.g.*, *Roland Machinery*; *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039, 1059 (8th Cir. 2000); *Omega*; *U.S. Healthcare, Inc. v. Healthsource, Inc.*, 986 F.2d 589, 596 (1st Cir. 1993); *CDC Techs., Inc. v. IDEXX Lab., Inc.*, 186 F.3d 74 (2d Cir. 1999); *Thompson Everett, Inc. v. Nat'l Cable Adver.*, 57 F.3d 1317, 1325 (4th Cir. 1995). Still, just as the inquiry does not begin and end once a court has adopted some measure of market foreclosure, some courts have observed that short duration and easy terminability do not preclude liability for exclusive dealing in all cases. *See United States v. Dentsply Int'l*, 399 F.3d 181, 193 (3rd Cir. 2005) ("Although the parties to the sales transactions consider the exclusionary arrangements to be agreements, they are technically only a series of independent sales. Dentsply sells teeth to the dealers on an individual transaction basis and essentially the arrangement is 'at-will.' Nevertheless, the economic elements involved—the large share of the market held by Dentsply and its conduct excluding competing manufacturers—realistically make the arrangements here as effective as those in written contracts").

Some courts have emphasized that exclusive dealing arrangements are less concerning to antitrust courts when the exclusivity is required of end-users rather than of distributor intermediaries. *See Omega*, 127 F.3d at 1162-63 ("[E]xclusive dealing arrangements imposed on distributors rather than end-users are generally less cause for anticompetitive concern. If competitors can reach the ultimate consumers of the product by employing existing or potential alternative channels of distribution, it is unclear whether such restrictions foreclose from competition *any* part of the relevant market."); *Ryko*, 823 F.2d at 1235 (plaintiff faces higher burden of proving harm to competition "[w]here the exclusive dealing restraint operates at the distributor level, rather than at the consumer level"). Still, other courts have correctly observed that the relevant question is whether the exclusive dealing arrangement prevents a rival from competing for distribution sufficient to reach MES, which can occur through exclusivity commitments made by distributors if distributors are a significant gateway to end-users. *See ZF Meritor LLC v. Eaton Corp.*, 696 F.3d 254, 287 (3d Cir. 2012) ("[T]he mere existence of potential alternative avenues of distribution, without an assessment of their overall significance to the market, is insufficient to demonstrate that Plaintiffs' opportunities to compete were not foreclosed") (internal citations omitted).

A final category of indirect evidence is evidence regarding the ease of entry into the industry purporting to be monopolized through exclusive dealing arrangements. Courts are clear that when entry is easy or when there is evidence of actual entry while the exclusive dealing is in force, anticompetitive effect is unlikely to occur. *See Omega*, 127 F.3d at 1164; *AREEDA*, *supra* note 21, ¶ 422e3 ("Entry while alleged exclusionary conduct is underway may suggest both that entry is easy and that the defendant's conduct is not really predatory at all"); *cf. Allen-Myland, Inc. v. IBM Corp.*, 33 F.3d 194, 209 (3d Cir. 1994) ("[T]he ease or difficulty with which competitors enter the market is an important factor in determining whether the defendant has true market power – the power to raise prices").

E. McWane's Full Support Program

What separates the pre-*GTE Sylvania* law and economics of the antitrust analysis of exclusive dealing arrangements from the modern era is that to succeed on a claim that exclusive dealing violates the antitrust laws, a plaintiff *must* demonstrate that the conduct harmed competition and not just disadvantaged a competitor.[33] Accordingly, to present a cognizable theory of harm, Complaint Counsel has the burden of showing that McWane's Full Support Program actually harmed the competitive process, not just that the program made it more difficult for Star to gain distribution.

Complaint Counsel's theory of harm is that "McWane's Exclusive Dealing Policy harmed competition by foreclosing a substantial share of the 'critical' distribution channel, thereby impeding entry. More specifically, McWane's Policy *prevented rivals from gaining a sufficient scale to constrain McWane's exercise of monopoly power*." CC Answering Brief at 14

33 *See* Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962) (antitrust laws concerned with the "protection of *competition,* not *competitors*"); Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477 (1977) (holding plaintiff competitor lacked standing to pursue antitrust claim that harmed it as a competitor but did not harm competition).

(emphasis supplied). This theory of harm tracks the modern economic understanding of how exclusive dealing might harm competition. Accordingly, Complaint Counsel has articulated a coherent theory of economic harm: McWane's exclusive dealing policy raised Star's distribution costs, which prevented Star from achieving MES, which enabled McWane to maintain power over price, preventing consumers from enjoying the benefit of unfettered competition between McWane and Star.

To match this theory of harm to the facts in the record, Complaint Counsel must show that (1) McWane engaged in an exclusive dealing policy; (2) the policy raised Star's distribution costs and prevented it from achieving MES; and (3) the policy enabled McWane to maintain its power over price resulting in consumer harm. Complaint Counsel views its burden differently: "[i]n exclusive dealing cases, a *prima facie* case of competitive harm is established by demonstrating: (1) a significant degree of market foreclosure; and (2) the impairment of one or more significant rivals' ability to compete." CC Answering Brief at 16 (citing *ZF Meritor* 696 F.3d at 271; *Dentsply* at 399 F.3d at 188-90, 194-96; *Microsoft*, 253 F.3d at 69). For additional support, Complaint Counsel also cites our prior decision in this case: "[T]he question here is whether McWane's conduct foreclosed a substantial portion of the effective channels of distribution, and whether the conduct had a significant effect in preserving McWane's monopoly." *In re McWane, Inc.*, 2012 FTC Lexis 155, at *63 (Sept. 14, 2012).[34] The Commission articulates a similar though more economically coherent standard: "we examine both the anticompetitive and procompetitive effects of the conduct to determine whether, in light of McWane's monopoly power, its use of exclusive dealing prevented rivals from meaningfully competing and had a substantial anticompetitive effect on competition." Commission Opinion at 20.

Complaint Counsel's statement of the law is, at best, question begging, and, at worst, misleading. As explained, foreclosure is an imprecise tool used by a court to assess whether harm to

34 I did not participate in the earlier decision as it predated my term as Commissioner.

competition can occur or is likely to occur in a given case; it is but one of several factors relevant to the same question.[35] Like market definition, the purpose of which is to screen for whether a business arrangement can plausibly result in "genuine adverse effects on competition," *Indiana Fed'n of Dentists*, 476 U.S. at 460-61, foreclosure is but a proxy for the real question of whether the arrangement harms competition.[36] How to calculate a foreclosure percentage and what that foreclosure percentage means will invariably depend upon the facts peculiar to each case. And in calculating a foreclosure percentage a tribunal must always be cognizant of the fact that foreclosure is valuable only insofar as it helps the tribunal understand whether the exclusive dealing policy is one that harms the competitive process and causes the firm implementing the policy to acquire or maintain monopoly power. Simply calculating a foreclosure percentage and declaring the percentage significant is insufficient to establish anticompetitive effect, both under existing antitrust jurisprudence and under Complaint Counsel's theory of the case.[37]

1. The Full Support Program as Exclusive Dealing

In September 2009, McWane sent a letter to its distributors stating that "McWane will adopt a program whereby our domestic

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35 *See e.g.*, Ryko, 823 F.2d at 1233; Barry Wright, 724 F.2d at 236; Beltone, 100 F.T.C. 68.

36 The Supreme Court recognized this fact when it first adopted foreclosure analysis as part of exclusive dealing jurisprudence in *Standard Stations*: "The issue before us, therefore, is whether the requirement of showing that the effect of the agreements 'may be substantially to lessen competition' may be met simply by proof that a substantial portion of commerce is affected or whether it must also be demonstrated that competitive activity has actually diminished or probably will diminish." *Standard Stations*, 337 U.S. at 299.

37 The Commission's assertion that I "would apply a standard of evidentiary proof . . . that is far beyond that called for by applicable Section 2 law . . . [and that I] offer[] no legal support for this heightened standard" is simply incorrect. Commission Opinion at n.12. The case law is clear that an antitrust plaintiff must show harm to competition in an exclusive dealing case and that "significant foreclosure" is only a proxy for harm to competition, and only one factor a tribunal is to consider in assessing harm to competition. Indeed, this point is made clear by the Commission's own precedent in *Beltone*, a case the Commission does not cite a single time in its opinion. *Beltone*, 100 F.T.C. at 204, 209.

fittings and accessories will be available to customers who elect to fully support McWane branded products . . . Customers who elect not to support this program may forgo participation in any unpaid rebates for domestic fittings and accessories." CX0010. In discussions with distributors, McWane explained that "if a customer buys Star domestic . . . the customer will no longer have access to" McWane's domestic fittings. IDF 1179; *see also* IDF 1183 (quoting CX0119 at 002, 004) ("Access to McWane or Sigma requires distributors to exclusively support McWane where products are available within normal lead times. Violations will result in: Loss of access, loss of accrued rebates."). McWane's letter on its face allows distributors to buy from non-McWane sources under certain circumstances: "Exceptions are where [McWane] products are not readily available within normal lead times or where domestic fittings and accessories are purchased from another domestic pipe and fitting manufacturer along with that manufacture[r]'s ductile iron pipe." CX0010.

Refusing to deal with a distributor if it also distributes the products of your competitor is a tell-tale sign of an exclusive dealing arrangement. And whether the Full Support Program is a "complete" exclusive dealing arrangement is beside the point. The relevant question from an analytical standpoint is whether the Full Support Program has exclusionary potential, which, in my view, it undoubtedly does. *ZF Meritor*, 696 F.3d at 283 ("[J]ust as 'total foreclosure is not required for an exclusive dealing arrangement to be unlawful, nor is complete exclusivity required with each customer.").[38] Of course, the relevant question on appeal after trial is whether the exclusionary potential resulted in actual exclusion and anticompetitive effects.

2. Minimum Efficient Scale

The second component of Complaint Counsel's theory of harm is that the Full Support Program raised Star's distribution costs and prevented it from achieving MES. If the Full Support Program did not prevent Star from achieving MES, then its

38 McWane argues that the Full Support Program was not an exclusive dealing arrangement because some distributors dealt with Star and distributors that did deal with McWane were not contractually obligated to do so. McWane Brief at 29. The Commission, in my view, correctly rejects McWane's argument. Commission Opinion at 20-22.

distribution costs could not have increased sufficiently to harm competition in the domestic fittings industry. Thus, a necessary predicate for evaluating whether the Full Support Program raised Star's distribution costs and prevented it from achieving MES is establishing what MES is in the domestic fittings industry.

The primary finding of fact that relates to MES is Star's own estimate that it would need between [redacted] in annual fittings sales to justify purchasing its own foundry. IDF 1400, *in camera*. Complaint Counsel claims that "[b]ut for the [Full Support Program], the deterred distributors would have offered Star sufficient sales opportunities for it to achieve economies of scale" and that "[s]imple arithmetic confirms the anticompetitive exclusion." CC Answering Brief at 19. Here, Complaint Counsel points to the amount of sales Star made in 2010 and 2011, [redacted], and to the additional amount of sales, [redacted], Star would need to justify purchasing a domestic foundry. CC Answering Brief at 19 (citing IDF 1143, *in camera*). The Commission accepts Complaint Counsel's argument wholesale. Commission Opinion at 25 ("Star testified . . . that it needed between [redacted] of domestic fittings sales to justify purchasing its own foundry. IDF 1400, *in camera*; Bhargava, Tr. 2962-63, *in camera*. Star's actual sales of domestic fittings, [redacted] in 2010, were insufficient for Star to justify operating a foundry of its own. IDF 1396, *in camera*, 1401.").

The unstated but implicit assertion in the argument made by Complaint Counsel and accepted by the Commission is that MES in the domestic fittings industry is achieved only when a supplier is able to operate its own foundry. And the basis for that assertion is *Star's own estimate about what a foundry would cost and nothing else*. *See* Oral Argument Tr. 82:2-83:2 ("COMPLAINT COUNSEL: In this case, the minimum efficient scale would be Star having its own foundry, which would allow Star -- Star was using jobber foundries instead, and that was less efficient. If it could have had its own foundries, it could have brought its costs down, and it could have -- and, again, there are numbers in the record. COMMISSIONER WRIGHT: Is there evidence in the record to establish that minimum efficient scale is equivalent to a foundry? COMPLAINT COUNSEL: No, I don't think -- I think that was Star's view of what minimum efficient scale was. I don't think they phrased it that way, but I think that's the closest thing in the record. COMMISSIONER WRIGHT: And there is a difference between saying they would be more efficient if they had a foundry and deprivation from achieving minimum efficient scale, which is the underlying basis of [the Commission's] theory. I'm wondering if there is anything you can point me to in the record that would help me distinguish between the two. COMPLAINT COUNSEL: I can't think of anything. I mean, Star's testimony was this is what we thought we needed, but no, I can't -- there is not, for example, any comments that spoke to what minimum efficient scale would be."). Such evidence is, as Complaint Counsel recognized, insufficient to establish MES. It is also inadequate, even accepting *arguendo* Complaint Counsel's assertion that Star's own estimate of the cost of a foundry is probative of its efficiency relative to other available sourcing options, to establish that any increase in Star's distribution costs was of sufficient magnitude to impact competitive conditions in the domestic fittings industry.

Complaint Counsel's expert, Dr. Laurence Schumann, explained the economics of exclusive dealing arrangements and how a firm with market power can use exclusive dealing to harm competition by preventing a rival from achieving MES. CX2260-A, ¶120-132. Dr. Schumann's testimony does not endeavor to define MES in the domestic fittings industry, however. He points to evidence that there are economies of scale in producing fittings, ¶163-164, and argues that economies of scale matter in the fittings industry, n.177 ("Greater production levels make the use of the most efficient equipment more economical; accordingly, as the scale of production grows, costs decline through the adoption of more efficient production equipment (Interview with Charles Frazier, May 25, 2012)."). Nor is there any evidence in the record from an industry expert regarding whether MES – as the term is understood in modern economics – is scale sufficient to justify the purchase of a foundry and whether Star's estimate of the amount of sales sufficient to justify the purchase of a foundry is indeed accurate.

In fact, evidence in the record supports the conclusion that owning and operating an independent foundry is not necessary to achieving MES in the fittings industry. Sigma's entire business model is based upon *not* owning production facilities. Sigma's "virtual manufacturing" model is to purchase fittings produced by independent foundries in China, Mexico, and India and to rely on its own employees for technical know-how and quality control. IDF 56-57. Sigma's business model of sourcing production to independent foundries has enabled it to become the second-leading supplier of fittings sold in the United States with a share of [redacted], almost twice as large a share as Star, which owns and operates foundries abroad. IDF 356, *in camera*, 111. Complaint Counsel has made no effort to reconcile the fact that Sigma was able to enter and achieve scale in the fittings industry without owning a foundry with its argument that MES in the *domestic* fittings industry requires owning a foundry.

Not surprisingly given Sigma's success with its virtual manufacturing model, there is evidence in the record that Star was able to enter, compete, and *grow its business* without operating its own foundry. IDF 1041, 1042, *in camera*, 1143, *in camera*, 1144 (noting that Star's share grew from [redacted] in its first year as a domestic supplier to more than [redacted] in its second year, and was on pace to continue its growth into its third year). In other words, for Complaint Counsel's view of MES to make sense on the facts that exist in the record, Star would have to be operating below MES, becoming less efficient over time as McWane's Full Support Program further raised the costs of distribution, and yet remaining in the market and growing its business. Such a position strains credulity.

In my view, Complaint Counsel has simply failed to introduce sufficient evidence to compel the conclusion that MES in the domestic fittings industry is the scale necessary to justify the purchase of a foundry.[39] As preventing a rival from achieving MES is a key element in the case – both articulated by the economic theory of using exclusive dealing to raise rivals' costs and by Complaint Counsel itself – failing to prove this point is fatal to Complaint Counsel's case. Without putting forth some credible evidence regarding MES in the domestic fittings industry, Complaint Counsel cannot logically establish the harm to

39 Nor, as explained below, has Complaint Counsel made any other attempt to establish through evidence or analysis the level of foreclosure that would be sufficient to create an impact on prices and output in the relevant market.

competition that the antitrust laws require a plaintiff to establish. This is because one thing that is necessary but not sufficient to distinguish mere harm to a competitor from harm to a competitor that also results in harm to competition is that the harm to a competitor prevents that competitor from achieving MES.

3. Harm to Competition

a. Foreclosure Analysis

Complaint Counsel argues that the Full Support Program harmed competition because the program "foreclosed a substantial share of the domestic fittings market," which prevented Star from being able to compete effectively, *i.e.*, achieve MES. CC Answering Brief at 16-23. The Commission largely accepts Complaint Counsel's argument, deciding that Star and other competitors were foreclosed from access to distributors and that this foreclosure impacted their ability to compete. Commission Opinion at 22-25.[40] As discussed, foreclosure in modern exclusive dealing analysis is not itself the end of any complete analysis but rather a starting point for understanding whether the exclusive arrangements at issue are capable of harming competition. What is strikingly absent from Complaint Counsel's argument, and the Commission's Opinion, is any evidence establishing the requisite analytical link between what the Commission describes as "foreclosure" and harm to competition. A measure of foreclosure caused by McWane's Full Support Program is relevant to the inquiry under Section 2 only insofar as there is evidence linking the identified foreclosure percentage to McWane's maintenance of its monopoly power.[41]

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40 In accepting this argument, the Commission finds that "[a] domestic fittings entrant is unable to compete effectively without access to distributors." Commission Opinion at 22 (citing IDF 400-09, 411-12, JSLF ¶ 14, IDF 367, IDF 373-74, IDF 381). I agree with the Commission's conclusion that in the domestic fittings industry, distributors are a key distribution channel and that a supplier cannot compete effectively without having some access to distributors.

41 *See* Krattenmaker & Salop *supra* note 15, at 259 (the key issue is "[w]hether the exclusionary rights arrangement will so limit remaining supply available to rivals that it will lead them to bid up the price of that supply, thereby increasing their costs to the point that the purchaser obtains power over price.").

Complaint Counsel argues that foreclosure is "calculated by determining the percentage of the downstream market subject to the challenged policy." CC Answering Brief at 16. Using this measure, Complaint Counsel says that because "McWane sold [redacted] of all Domestic Fittings in 2010, [and] roughly 99% of those sales were through Distributors, and all Distributors were subject to McWane's Exclusive Dealing Policy . . . [the] foreclosure percentage [is] [redacted]." CC Answering Brief at 17 (citing IDF357, *in camera*; CCPF475).

The Commission does not settle on a specific foreclosure percentage, preferring instead to point to the market shares of all the distributors that could potentially have been foreclosed by the Full Support Program, adding them up, and intimating that such a percentage is significant. "McWane's Full Support Program foreclosed Star and other potential entrants from accessing a substantial share of distributors. Following announcement of the program, the country's two largest waterworks distributors, HD Supply, with a roughly 28% to 35% share of distribution (IDF 378), and Ferguson, with about 25% of distribution (IDF 379), prohibited their branches from purchasing domestic fittings from Star unless the purchases fell into one of the exceptions specified in the Full Support Program." Commission Opinion at 23. In addition to HD Supply and Ferguson, the Commission points to other distributors such as U.S. Pipe, Groeninger, and WinWholesale and finds that they would have made more purchases from Star had McWane not started the Full Support Program. Commission Opinion at 23-24.

Complaint Counsel and the Commission's foreclosure analysis is incomplete and offers little illumination regarding the competitive effect of the Full Support Program. Most fundamentally, neither Complaint Counsel nor the Commission provides an analytical link between Complaint Counsel's foreclosure analysis and competitive harm.[42] As discussed, one

42 The Commission is correct that "[t]he test is not total foreclosure, but whether the challenged practices bar a substantial number of rivals or severely restrict the market's ambit." Commission Opinion at 29 (citing Dentsply, 399 F.3d at 191; *accord* ZF Meritor, 696 F.3d at 265, 283-84). But the mere fact that the foreclosure rate need not be 100% to violate the law does not obviate the need to connect the identified foreclosure rate with the defendant's ability to maintain monopoly power.

obvious such link entirely absent in the record is direct evidence that the Full Support Program actually increased prices and reduced output relative to what they would have been had Star entered and McWane not implemented the Full Support Program – that is, evidence consistent with Complaint Counsel's theory and Complaint Counsel and the Commission's assertion that the level of foreclosure was sufficient to cause competitive harm over the time it was in effect. Neither Complaint Counsel nor the Commission makes any attempt to reconcile the absence of actual evidence of anticompetitive effects with the high foreclosure rates they claim are at issue.[43] Because foreclosure rates are relevant

43 The Commission points to certain categories of evidence it considers direct. First, the Commission points out that "McWane itself recognized that if Star entered, prices in the domestic market would likely fall just like in the imported market." Commission Opinion at 27 (citing IDF 1148-49, 1151-53). McWane's own prediction about a "likely" price effect in the future is simply not evidence of what actually happened to prices once Star did enter, evidence the Commission could have acquired and introduced into the record in this case. Second, the Commission points to the fact that "soon after Star entered the market, McWane announced and implemented price increases for domestic fittings." Commission Opinion at 29 (citing IDF 1083). Notwithstanding that there is no evidence suggesting that McWane's announced price increase led to an actual increase in prices, the Commission again misunderstands Complaint Counsel's task in this case. Showing a change in prices or output that corresponds with the timing of some event, say, a firm's entry into a market, is necessary but not sufficient to show that challenged conduct was exclusionary. Complaint Counsel's burden is to show that McWane's conduct *caused* any price effect. That McWane announced a price increase after Star's entry does not satisfy Complaint Counsel's burden. Indeed, Complaint Counsel has made no effort to show that the price increase announced by McWane occurred as a result of the Full Support Program. This is likely because there is ample evidence in the record to suggest that the price increase announced by McWane in 2010 was caused by a host of other factors. There is evidence that McWane's costs were increasing at the time it announced the price increase, which would also explain the fact that it announced a price increase for *all* McWane fittings at the same time it announced a price increase for domestic fittings. IDF 1083-85. Further, the price increase was announced in December 2010, likely within the timeframe for ARRA-funded projects during which demand for domestic fittings increased. It is basic economics that an increase in demand increases prices as well, holding all else constant. Further, there is additional evidence in the record to suggest demand was high in 2010. As the Commission has pointed out, Star's revenue in 2011 was lower than in 2010 despite Star having twice as high a market share in 2011. IDF 1397. One plausible explanation for such facts would be a decrease in demand for domestic fittings in 2011 relative to 2010. This would also be consistent with the fact that ARRA-funded projects were to be under contract or under

only as a proxy for better understanding competitive effects, this failure undermines the Commission's heavy reliance upon inferences drawn from foreclosure rates. By concluding that Complaint Counsel need only demonstrate that Star was foreclosed from some unspecified amount of distributors as a result of the Full Support Program, without linking that foreclosure to the preservation of McWane's monopoly power, the Commission in effect holds that harm to a competitor without more is sufficient to establish a violation of Section 2.[44]

construction by February 2010. IDF 525-27. Of course, a host of other factors could explain McWane's announcement to increase prices in 2010. The record, including the expert reports, simply does not provide enough evidence to make a reliable conclusion about the cause of the announcement. Accordingly, the simple fact that McWane announced a price increase after Star's entry sheds almost no light on whether the Full Support Program was exclusionary.

44 The Commission's argument that there is harm to competition because McWane's conduct reduced "choice" fares no better. Commission Opinion at 28 ("McWane's exclusive dealing policy also had another adverse impact on competition: it denied its customers the ability to make a meaningful choice"). There are two problems with the Commission's reliance on a loss of consumer choice as evidence of harm to competition. First, the Commission cites no precedent to support the proposition that a loss of consumer choice, without any *other* evidence of harm to competition, such as an adverse effect upon price or output, is sufficient to establish the harm to competition required under the antitrust laws. *Cf.* Brantley v. NBC Universal, Inc., 675 F.3d 1192, 1202 (9th Cir. 2012) ("[A]llegations that an agreement has the effect of reducing consumers' choices or increasing prices to consumers does not sufficiently allege an injury to competition."); *AREEDA*, *supra* note 21, ¶1703 f5 ("To the extent that [a defendant's interference with customers' free will] is relevant to antitrust law, interference has already been covered by diminished product variety resulting from substantial foreclosure or by elevated prices depressing production and use"). Second, the Commission's analysis of consumer choice ignores the fact that pipe fittings are commodity products. The two cases the Commission cites to support its position, *Dentsply* and *ZF Meritor*, both involve markets with differentiated products (artificial teeth and heavy duty truck transmissions). Here, there is no evidence that end-users placed different values on pipe fittings made by different suppliers. To the extent choice is valuable to consumers in a commodity industry, it is because choice begets price competition between suppliers. And if a reduction in consumer choice also results in a reduction in price competition, then one would expect to see some price effect accompanying the loss of choice, and no such price effect can be gleaned from the record.

In addition, there are numerous reasons to doubt that the foreclosure claimed by Complaint Counsel and observed by the Commission is measured accurately, or is probative of anticompetitive effects. In other words, the measure is defective for the purpose asserted by Complaint Counsel and the Commission. Under Complaint Counsel's theory of harm – that but for the Full Support Program, distributors would have made enough purchases from Star for Star to achieve MES and threaten McWane's monopoly position – the appropriate measure of foreclosure is not the sum of the market shares of distributors that are "subject" in some way to the Full Support Program, but the dollar value of purchases distributors would have made from Star *but for* the Full Support Program.[45] It makes little sense to conclude that Star was foreclosed from McWane's sales to distributors that would have taken place with or without the Full Support Program, or that McWane's restricting a rival's access to such sales in any way disadvantages the rival by reducing the rival's access to distribution.

Indeed, there is evidence in the record that certain distributors would not have made any purchases from Star even if McWane had not introduced the Full Support Program. A Ferguson executive testified that Ferguson "was planning on purchasing all its needs from [McWane]" regardless of the Full Support Program because Star would not be able to provide Ferguson with a full line of fittings. Thees, Tr. 3108-09; *see also* IDF 1266, 1272. The Commission recognizes this evidence, but concludes "the record suggests that the Full Support Program nonetheless cost Star *some* Ferguson business." Commission Opinion at 23 (emphasis supplied) ("A Ferguson Vice President called district managers after McWane's policy was announced to ensure that it did not buy from Star, and at least one job Ferguson initially awarded to Star was cancelled (IDF 1260-61, 1263)."). Of course, the record does not answer the most relevant question: how much Ferguson business did the Full Support Program cost Star?

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45 *See* Krattenmaker & Salop, *supra* note 15, at 259 (defining the net foreclosure rate as "the percentage of the suppliers' capacity that was available to rivals before the exclusionary rights agreement was adopted but that is no longer available as a result of the agreement").

There is also evidence in the record that WinWholesale's decision not to purchase from Star was unrelated to the Full Support Program. IDF 1342 (Star is not on WinWholesale's approved list of vendors because "because WinWholesale had no background on where Star was making its product, because Star had not produced any test data or anything that would lead WinWholesale to believe that Star was as credible a vendor on Domestic Fittings as it was on imported Fittings, or that they could do a good, consistent job making Domestic Fittings using seven foundries. (RX 705 (Gibbs, Dep. at 85-88)"). There is evidence that another distributor, Illinois Meter, "would have purchased 90-plus percent of its Domestic Fittings from McWane, whether the Full Support Program existed or not. (RX 674 (Sheley, IHT at 90) ("Q: Had McWane not implemented this policy, would you have purchased domestic Fittings from Star? A: Probably not. I'd probably still be buying 90-plus percent of all my stuff from [McWane].")).'' IDF 1359. Further, there is evidence in the record that some distributors' decisions not to purchase from Star were a result of their perceptions of the quality of Star's products and services, not because of the Full Support Program. *See* IDF 1132 ("Star recognized that some Distributors were cautious about purchasing Domestic Fittings from Star in 2009 and early 2010 because of delays in filling orders. (Bhargava, Tr. 3003, *in camera*; McCutcheon, Tr. 2634)"); IDF 1275 ("Ferguson has had past business dealings with Star that put a strain on the relationship between the two companies. This strain was a leading component in Ferguson's decision to not purchase Domestic Fittings from Star (Thees, Tr. 3105-3107)").[46]

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46 The Commission asserts that my argument is based upon the assumptions that "the sales a monopolist like McWane has tied up with its distributors are not contestable and that a second meaningful alternative in the market will have no impact on price or other forms of competition, regardless of which supplier customers may ultimately choose." Commission Opinion at 27. I make no such assumptions. The relevant question for purposes of exclusive dealing law is whether the Full Support Program harmed consumers of domestic pipe fittings. The evidence shows that McWane would have won many contests to make deals with distributors *even without the Full Support Program*. If, absent the Full Support Program, Star would have competed for sales to certain distributors and have lost those sales to McWane, then the Full Support Program could not have foreclosed those lost sales. This conclusion is not based on any assumption regarding the impact a second supplier would have on price, output, or quality in the Domestic Fittings market. Star's entry may well have had a positive impact on these economic factors, though there is no direct

Complaint Counsel and the Commission's foreclosure analysis is also defective for another reason: they fail even to attempt to quantify the percentage of domestic fittings that were not subject to the Full Support Program. There is no dispute that the Full Support Program itself contained two exceptions: "where [McWane] products are not readily available within normal lead times or where domestic fittings and accessories are purchased from another domestic pipe and fitting manufacturer along with that manufacture[r]'s ductile iron pipe." CX0010. Complaint Counsel concedes that there is no credible argument that Star's fittings that fall into these categories are foreclosed from access to distributors through the Full Support Program. Oral Argument Tr. 84:2-84:4 ("COMPLAINT COUNSEL: If fittings were sold under an exception to the policy, no, I don't think they should be counted as foreclose[ed]."). Even though fittings that qualify as exceptions do not belong in the foreclosure analysis, Complaint Counsel failed to quantify the percentage of excepted fittings. The Commission also recognized that the exceptions existed, but asserted with minimal support in the record that the effect of the exceptions was "minor." Commission Opinion at 23.[47] There is no dispute that Star made at least some sales pursuant to the exceptions to the Full Support Program. IDF 1137; 1242; 1309. Of course, the relevant question, which cannot be gleaned from the record is: how much?

The Commission recognizes these issues but brushes them to the side in holding that the foreclosure is substantial in this case.[48]

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evidence the record demonstrating such an impact. Regardless, the key inquiry is whether McWane unlawfully excluded Star, not whether two suppliers are better than one, an issue that is of limited relevance to the underlying inquiry.

47 For support the Commission points to the testimony of a single distributor that claimed its purchases from Star through the exceptions to the Full Support Program were "minor." IDF 1309-11 (citing Morton, Tr. 2915-2916). The testimony of one distributor (U.S. Pipe) (out of more than 100) is not enough to establish that the sum total of purchases from distributors through the exceptions to the Full Support Program is indeed minor as it relates to assessing foreclosure.

48 The Commission argues that I "insist[] that Complaint Counsel was required to calculate the specific level of sales Star lost as a result of the Full Support Program." Commission Opinion at n.12. This is a mischaracterization of my position. I discuss the factual defects with Complaint Counsel and the Commission's foreclosure analysis to illustrate that the foreclosure percentage

In so holding, the Commission ignores the fact that it is Complaint Counsel's burden to establish that the Full Support Program harms competition. Complaint Counsel has chosen to establish harm to competition solely by relying upon foreclosure percentages and indirect evidence. But the evidence in the record demonstrates that the percentages put forward by Complaint Counsel are simply inaccurate. There are exceptions to the Full Support Program – McWane allows distributors to buy from Star if certain conditions are met – but there is no evidence in the record regarding whether the exceptions comprise a significant amount of the Domestic Fittings Market. Further, there is evidence in the record that some distributors that chose to buy from McWane (or chose not to buy from Star) would have done so even without the Full Support Program. Star cannot possibly have been foreclosed from these distributors. The Commission's conclusion that foreclosure was significant enough to impact competitive conditions in the domestic fittings industry relies primarily upon inferences from sales McWane's Full Support Program allegedly foreclosed from Star. Complaint Counsel's failure to quantify sales Star made under the Full Support Program's exceptions and to deduct distributor purchases from McWane that would have occurred with or without the Full Support Program make it impossible accurately to assess the foreclosure rate, much less to determine whether the foreclosure was significant enough to compel the conclusion that the Full Support Program harmed competition.

b. Other Indirect Evidence

Of course, as explained above, the foreclosure rate is not the only type of indirect evidence relevant to assessing whether an exclusive dealing arrangement has anticompetitive effects. However, the other forms of indirect evidence do not overcome the absence of direct evidence or the deficiencies that plague Complaint Counsel's evidence of foreclosure and the Commission's conclusions derived therefrom.

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put forward by each is unreliably high, and, most importantly, we have *no idea how large the error is*. It is Complaint Counsel's burden to establish that the foreclosure at issue is significant, and in my view, there is substantial evidence showing that Complaint Counsel has vastly overestimated its claimed foreclosure percentages.

One relevant consideration is the length and terminability of the exclusive dealing arrangements. *Omega*, 127 F.3d at 394 (short duration and easy terminability limit the possibility of anticompetitive effects). Here, the Full Support Program was not an agreement between McWane and its distributors. Distributors were never contractually obligated to make *any* purchases from McWane; they could choose to purchase from Star or another supplier at any time. Though not dispositive – it is possible for a dominant firm to exclude competitors through non-contractual mechanisms that result in distributor exclusivity – this point certainly counsels against a holding that the Full Support Program resulted in anticompetitive effect.

Another issue is whether exclusivity is imposed upon an intermediary or a final consumer. Though some courts have held that exclusivity requirements are more concerning when imposed on the end user rather than on an intermediary, *see Omega*, 127 F.3d at 1162-63, other courts have held that exclusivity requirements imposed on intermediaries can have anticompetitive effects when the intermediary is a significant channel of distribution. *ZF Meritor*, 696 F.3d at 287. Here, in my view, Complaint Counsel has satisfied its burden to establish that in the domestic pipe fittings industry, distributors are a significant channel of distribution. *See* Commission Opinion at 22. Accordingly, I give little weight to the fact that the Full Support Program applied to distributors and not to end users.

A final but important category of indirect evidence is evidence relating to entry.[49] As explained, the case law demonstrates that evidence of entry and expansion by a purportedly excluded rival counsels against a decision that an exclusive dealing arrangement harmed competition. *See Omega*, 127 F.3d at 1164 ("Nor did plaintiffs produce credible evidence to support their contention that Gilbarco's policy actually deterred entry into this market.

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49 Statement of Commissioner J. Thomas Rosch, Concurring in Part and Dissenting in Part In the Matter of McWane, Inc. and Star Pipe Products, Ltd., and the Matter of Sigma Corporation, FTC File No. 1010080 (Jan. 4, 2012), *available at* http://www.ftc.gov/sites/default/files/documents/public_statements /statement-commissioner-rosch-concurring-part-and-dissenting-part-matter-mc wane-inc.and-star-pipe-products-ltd.matter-sigma-corporation/120104sigma statement.pdf.

The actual entry and expansion of Schlumberger in 1991, through the purchase of a small dispenser manufacturer, Southwest, demonstrate the contrary. The record shows that . . . by trial Schlumberger had 'something over ... 100 distributors' . . . . And, although the parties contest the extent of the increase, it is undisputed that Schlumberger's market share has increased since its entry by at least one third (from approximately 6% to 8%), while industry output in the retail dispenser market has expanded substantially. This undisputed evidence precludes a finding that exclusive dealing is an entry barrier of any significance."). Here there is undisputed evidence that Star was able successfully to enter the domestic fittings industry and to succeed in expanding its business once it did enter. IDF 1042, *in camera* (Star's market share in its first full year in the Domestic Fittings market was [redacted]); IDF 1043, *in camera* (Star's market share in its second full year in the domestic fittings market doubled to [redacted]. The record shows that Star made sales to more than 100 distributors. IDF 1141 (citing Normann Tr. 5042-43, *in camera*).[50]

Further, the fact that McWane did not enforce the Full Support Program after Star's first year in the domestic market[51] provides an opportunity to examine the impact of the Program. The evidence shows that Star's growth rate was *identical* before and after McWane stopped enforcing the Full Support Program. Neither Complaint Counsel nor the Commission attempts to explain how growth that is equal with and without the Full Support Program is consistent with Complaint Counsel's theory of harm that the Program raised Star's costs of distribution and

50 I agree with the ALJ's finding that simply counting the number of distributors Star was able to contract with can be misleading because such a count could include distributors that made only a small number of purchases from Star. IDF 1142. Indeed, the measure of Star's market share over the relevant period is a more relevant piece of information. However, the number of distributors Star was able to deal with is not irrelevant. It illustrates that Star was able to find a significant number of trading partners notwithstanding the Full Support Program. Nevertheless, the key issue is whether Star was able to compete with McWane for enough distributors that, if they agreed to distribute Star's fittings, would enable Star to operate at MES.

51 IDF 1219 (McWane did not enforce the Full Support Program against any distributor after April 13, 2010).

impaired competition.[52] The most plausible inference to draw from these particular facts is that the Full Support Program had almost no impact on Star's ability to enter and grow its business, which, under the case law, strongly counsels against holding that McWane's conduct was exclusionary. Further, evidence of Star's successful entry is especially probative because it requires minimal interpretation. Unlike foreclosure, which can be measured in different ways and is subject to different interpretations, a firm's entry is an observable fact that contravenes the precise point – exclusion – Complaint Counsel is seeking to establish.

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In my view, Complaint Counsel has failed to carry its burden to demonstrate that the Full Support Program resulted in cognizable harm to competition and this would doom its case even if it had established that MES in the domestic fittings industry was operating a foundry. Harm to competition can be shown with direct evidence that market prices were impacted by the alleged exclusionary conduct. Such evidence is favored both by courts in evaluating restraints of trade[53] and by the agencies in deciding whether to challenge a consummated merger.[54] The record is devoid of direct evidence of competitive harm.

Harm to competition can also be established by indirect evidence, which is the route Complaint Counsel chose to go in this case and the evidence the Commission relied upon in affirming the ALJ's decision that McWane's conduct was exclusionary. My view of the indirect evidence of harm to competition is that it is very weak and does not and cannot satisfy

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52 Complaint Counsel argues that the Full Support Program is still in effect because McWane has not "withdrawn" it and that "it continues to prevent [distributors] from purchasing from Star today." CC Answering Brief at 14. This fails to consider evidence that distributors began to ignore the Full Support Program after they learned of the FTC's investigation into McWane's conduct. IDF 1311 (US Pipe not concerned in September 2010 about McWane enforcing the Full Support Program because of FTC investigation).

53 *See* Indiana Fed'n of Dentists, 476 U.S. at 460-61.

54 U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 2.1.1 (2010), *available at* http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf.

Complaint Counsel's burden. As I have explained, the foreclosure analysis put forward by Complaint Counsel and accepted by the Commission is unpersuasive because the analysis does not properly account for the fact that some distributors would have bought from McWane regardless of the Full Support Program, and that Star could not possibly have been foreclosed from selling fittings that were excepted from the Full Support Program.

The other indirect evidence of competitive harm points in multiple directions. On the one hand, distributors are a key distribution channel, which counsels against following the case law that says exclusive dealing requirements applied to intermediaries are less concerning than exclusive dealing requirements applied to end users. On the other hand, no distributor *agreed* to distribute McWane's fittings exclusively and for a lengthy period of time. Distributors were not contractually forbidden from dealing with Star, which is how Star was able to enter and acquire more than [redacted] of the market by its second full year in the domestic business. IDF 357, *in camera*.

In my view, the indirect evidence in the record does not point to the conclusion that the Full Support Program resulted in harm to competition. With such a record, Complaint Counsel would need to proffer some direct evidence that McWane's conduct raised price and reduced output in the domestic fittings industry relative to the price and output levels that would have occurred with Star's entry and without the Full Support Program. The Commission has stated in the past that it must tread lightly when condemning an exclusive dealing arrangement, requiring "reasonably clear evidence of probable overall competitive harm." *Beltone*, 100 F.T.C. at 209. Unfortunately for Complaint Counsel and the Commission, there is no such clear evidence in the record.[55]

55 Because I conclude Complaint Counsel has not shown the requisite anticompetitive effect, the burden should not shift to McWane to proffer a procompetitive justification for the Full Support Program. *See* Microsoft, 253 F.3d at 59. The Commission rejects McWane's proffered justifications that the Full Support Program was necessary to ensure sales volume and to prevent Star from "cherry picking" sales of the most popular fittings by forcing distributors to accept McWane's full line. Commission Opinion at 29-30. Though I make no decision or conclusion regarding McWane's proffered justifications, I must

II. Count 7 – Attempted Monopolization

Count 7 of the Complaint charges McWane with attempted monopolization of the Domestic Fittings market and relies on the same conduct – the Full Support Program – as part of its claim. The Commission deemed it unnecessary to make a decision on Count 7 in light of its decision to hold McWane liable for actual monopolization under Count 6. Commission Opinion at n.16 ("In view of our conclusion that McWane unlawfully monopolized the domestic fittings market through the same conduct, it is unnecessary to ask whether McWane attempted to monopolize the market. Accordingly, we do not reach this issue and do not adopt the ALJ's analysis."). Though I agree with the Commission's conclusion that a decision on Count 7 is unnecessary in light of its decision on Count 6, because I dissent from the Commission's decision that McWane monopolized the Domestic Fittings market, I must write separately to explain why I agree with the Commission's conclusion that Count 7 ought to be dismissed.

Attempted monopolization, like ordinary monopolization, sounds under Section 2 of the Sherman Act. 15 U.S.C. § 2. "[T]o

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dispute the Commission's apparent rejection that full-line forcing or block-booking contracts can result in cognizable efficiencies, even if the contracts reduce the full-line supplier's costs or prevent its exit from the marketplace altogether. Commission Opinion at 32 ("If a limited supplier undersells a full-line supplier for more common products, there is no reason in principle why the full-line supplier could not compete for that business by lowering its price for those products and increasing its price for the less common products . . . . Even if selective entry by the full-line supplier's rivals led to the collapse of the full-line seller, that itself would not constitute a harm to the market (as opposed to harm to a single firm)."). Economists have shown that a multi-product monopolist can use full-line forcing or block-booking contracts to prevent buyers from engaging in precisely the sort of "cream-skimming" the Commission describes and thus facilitate efficient distribution. *See* Roy W. Kenney & Benjamin Klein, *The Economics of Block Booking*, 26 J. L. & ECON. 497 (1983); Bruce H. Kobayashi, *Does Economics Provide a Reliable Guide to Regulating Commodity Bundling by Firms? A Survey of the Economic Literature*, 1 J. COMP. L. & ECON. 707 (2005). Consistent with the economics literature exploring the competitive implications of full-line forcing contracts, recent empirical tests confirm the practice can result in increased efficiency and consumer welfare. *See, e.g.*, Katherine Ho, Justin Ho, & Julie Holland Mortimer, *The Use of Full-Line Forcing Contracts in the Video Rental Industry*, 102 AM. ECON. REV. 686 (2012); Katherine Ho, Justin Ho, & Julie Holland Mortimer, *Analyzing the Welfare Impacts of Full-line Forcing Contracts,* 60 J. INDUS. ECON. 468 (2012).

demonstrate attempted monopolization a plaintiff must prove (1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power." *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456 (1993). The ability to prosecute attempted monopolization "provides . . . a mechanism for the control of unilateral behavior by firms *not guilty of monopolization itself*." PHILLIP E. AREEDA & HERBERT HOVENKAMP, FUNDAMENTALS OF ANTITRUST LAW § 8.02 (4th ed. 2013) (emphasis supplied).

Both completed monopolization and attempted monopolization require that the defendant engage in exclusionary conduct. *See, e.g.*, *Am. Tobacco Co. v. United States*, 328 U.S. 781, 785 (1946) ("The phrase 'attempt to monopolize' means the employment of methods, means and practices which would, if successful, accomplish monopolization, and which, though falling short, nevertheless approach so close as to create a dangerous probability of it"). Because I have concluded that Complaint Counsel failed to satisfy its burden of proving that McWane engaged in exclusionary conduct required for a finding of completed monopolization, it follows that McWane cannot be found liable for attempted monopolization by engaging in the same conduct.

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Though Complaint Counsel's failure to establish that the Full Support Program was exclusionary precludes it from succeeding on its attempted monopolization claim, the claim itself is somewhat unusual and worthy of additional reflection. Typically, a plaintiff pursues an attempt claim because the defendant lacks the monopoly power required to prove ordinary monopolization under Section 2. Because my view is that Complaint Counsel has failed to prove McWane's conduct was exclusionary, this case presents the rare circumstance of an attempt claim involving a firm that already has monopoly power – a conclusion I assume but do not decide – engaging in conduct that *could have* but did not result in unlawful monopoly maintenance. Such a claim might be called "failed monopoly maintenance."

As a logical matter, such a claim is conceivable. However, there is little settled law on whether a firm with monopoly power can be held liable for attempting to maintain a monopoly position in the same market. At least one court has determined such liability is consistent with the text of Section 2. *See, e.g.*, *In re Mushroom Direct Purchaser Litigation*, 514 F. Supp. 2d 683, 701 (E.D. Pa. 2007) (concluding that "[b]ecause plaintiffs allege[d] that defendants tried to reduce opportunities for new entry into the market, . . . defendants [could] be liable for attempted monopolization even if defendants possessed a monopoly in [the relevant market]"). A better approach in my view, however, is to force a plaintiff to choose between a monopoly maintenance claim and an attempted monopolization claim. I see no benefit in using the offense of attempted monopolization to prosecute conduct that might be viewed as exclusionary *ex ante* but turned out not to be *ex post* once the evidence has been examined. *See* AREEDA, *supra* note 21, ¶806a ("exclusionary conduct by a monopolist within its own market, whether successful or not, is best treated as an aspect of the full monopolization offense."). One decision, since vacated, shares this view: "Section 2 of the Sherman Act does not create a cause of action for an attempt to maintain a monopoly." *LePage's Inc. v. 3M*, 277 F.3d 365, 385 (3d Cir. 2002), *vacated on other grounds*, 324 F.3d 121 (3d Cir. 2003) (en banc). In doing so, the court stated any such "claim would be covered by the 'willful maintenance' part of the monopolization offense and would have been encompassed adequately by the monopolization count." *Id.*