



# DEPARTMENT OF JUSTICE

---

REMARKS OF

CHARLES F. RULE  
DEPUTY ASSISTANT ATTORNEY GENERAL  
ANTITRUST DIVISION  
U.S. DEPARTMENT OF JUSTICE

BEFORE THE

CHEMICAL MANUFACTURERS ASSOCIATION

CONCERNING

THE ANTITRUST DIVISION'S APPROACH  
TO SHIPPERS' ASSOCIATIONS

WASHINGTON HILTON HOTEL  
WASHINGTON, D.C.  
OCTOBER 21, 1985

I am very pleased to be here with you this afternoon to discuss the topic of shippers' associations. With increasing frequency, shippers are responding to the economic and regulatory changes in transportation markets by forming cooperatives to purchase transportation services -- normally called shippers' associations. As a result, the Department has recently been giving a good deal of attention to the antitrust issues raised by the formation and operation of such associations. Given this Administration's commitment to eliminating unnecessary government intrusion into the marketplace and to clarifying the circumstances that make intervention necessary to eliminate antitrust violations, I welcome this opportunity to share with you the Department's views concerning the appropriate antitrust analysis of shippers' association.

The recent surge of interest in shippers' associations is due largely to the enactment of the Shipping Act of 1984.<sup>1</sup> That Act defines a shippers' association as, "a group of shippers that consolidates or distributes freight on a nonprofit basis for the members of the group in order to secure carload, truckload, or other volume rates or service contracts."<sup>2</sup> The Act specifically authorizes ocean common carriers and conferences to enter into service contracts, which involve volume discount rates, with shippers' associations.<sup>3</sup> Moreover, the Act expressly prohibits any ocean common carrier from refusing to negotiate with a shippers' association.<sup>4</sup> The 1984 Act, however, does not confer antitrust immunity on the individual members of a shippers' association or on the shippers' association itself. Thus, joint activities among members of the shippers' association must be conducted in accordance with the antitrust laws.

The Department of Justice has a procedure, known as the business review procedure, whereby an organization such as a shippers' association can receive guidance in advance as to whether certain proposed conduct would be challenged by the Justice Department as an antitrust violation.<sup>5</sup> Under the business review procedure, a firm or individual may submit a letter to the Antitrust Division describing a proposed business activity and receive a statement of the Justice Department's enforcement intentions with respect to the proposed conduct. It should be stressed that a business review request can only deal with prospective conduct. The Justice Department will not issue a business review letter that deals with conduct already implemented.

Not unexpectedly, over the past year the Antitrust Division has received a number of business review requests from shippers' associations. Within the past two months we have issued three business review letters for shippers' associations, in each of these cases concluding that the proposed activities of these associations would be in conformity with the antitrust laws.

There are currently 10 more requests pending. We are attempting to respond to these requests as expeditiously as possible. We are also seeking to decrease substantially the time needed to complete our review process. To accomplish this, however, we need the full cooperation of those who request business review letters to ensure that all the relevant information is presented to the Antitrust Division as part of the initial request. I hope that by describing the criteria we use to assess the likely competitive risks of a particular shippers' association and to determine when enforcement action is necessary, private efforts to form shippers' associations can proceed with greater certainty and confidence and our processing of business reviews can be completed with less time and at less cost.

At the outset I want to emphasize that the antitrust laws recognize the efficiency-enhancing potential of shippers' associations. For example, through the consolidation of shipments to obtain volume discounts, these associations permit smaller shippers to receive lower freight transportation rates than they otherwise could on their own. This could well prove to be procompetitive and socially beneficial. On the other hand, there are certain concerns that the Justice Department has regarding the possible anticompetitive impact of shippers' associations. Since the Justice Department believes that the majority of shippers' associations are likely to be procompetitive, the criteria we have adopted to identify possible anticompetitive effects are designed to be simple enough to permit quick preparation of business review requests and expeditious processing of these requests.

In analyzing the competitive effects of shippers' associations, we seek answers to two basic questions. First, would the association, as a purchaser of transportation services, possess what we refer to as monopsony power? That is, we ask whether the members of the association would account for so large a portion of the purchases of the relevant good or service that the association could effectively force carriers or conferences to agree to transportation rates below competitive levels. Such an exercise of monopsony power is economically harmful because society's resources are misallocated as inputs are not purchased for their most highly valued use. Second, we ask whether the association would be likely to facilitate price fixing or otherwise to reduce competition among its members in some final product or service market. The exercise of such monopolistic power is also economically harmful because, by reducing demand and

restricting output resources are not put to their most highly valued use. If the answer to both questions is no, the formation of a shippers' association raises no antitrust concern.

To resolve the monopsony power issue, we first need to identify the members of the shippers' association. In those cases where the association is not yet in existence at the time the business review request is submitted, we obviously have to make some assumptions as to the anticipated membership. We then project the total volume of cargo to be shipped by the combined membership of the association over a given period of time and compare that figure to the total transportation capacity available to ship that cargo for that same period. In order to determine the total capacity available, we take into account any special equipment needs of the shippers. In general, if the membership's total projected volume is less than 35 percent of available transportation capacity, it is unlikely that it will be profitable for the association to restrict its usage of transportation services in order to drive down rates. We have chosen 35 percent because, under the Department's Merger Guidelines, that is the point at which we begin to become concerned that a leading firm can unilaterally exercise market power.

The second issue, that is, the association's ability to facilitate price fixing or reduce competition in some final product or service market, may be a concern where some or all of the association's members are direct competitors in at least one such output market. For example, an association comprised of widget manufacturers might, under certain circumstances, be able to use the association in order to coordinate the prices and output of widgets. If the cost of shipping widgets constituted a large fraction of their delivered price and all other costs were uniform among producers, the ability to establish uniform transportation costs could significantly increase the ease with which the members could tacitly coordinate their price and output decisions. Similarly, if the members of the association exchange sensitive price, output or cost information and operate in a highly concentrated market, the members could use the information to coordinate price and output levels.

To resolve the issue of the potential for collusion, we examine two primary areas. First, we need to know the percentage of final product or service price represented by the transportation cost component in question. As this percentage increases, the collective purchase of transportation at identical rates may enhance the ability of member firms collectively to reach and maintain prices above the competitive level. As the transportation component of cost rises,

member firms become “more alike,” are better able to determine their rival members’ costs, and can better interpret the meaning of their rival members’ price changes. All this makes collusion more likely. Ordinarily, if the transportation cost represents less than 20 percent of final product price, a shippers’ association’s setting of transportation rates would not significantly enhance the likelihood that this form of anticompetitive pricing would result.

Our second concern is that the association may function as a device that facilitates, coordinates and/or polices collusion among its members by means other than manipulating the transportation cost variable of delivered price. For example, under certain circumstances, a requirement that all shipments be made through the association allows the members to observe the shipments (and thus the output) of their rivals and to prevent cheating by members that takes the form of increased output shipped outside the association. Agreement by the shippers’ association to a number of procedural and operational safeguards will ordinarily eliminate our concern in this area. First, members cannot be required to tender all their shipments through the association. Members must be free to use rates negotiated by any other shippers’ associations, as well as rates the member negotiates independently with a carrier or conference. Associations can, however, prior to negotiating with a carrier or conference, require each member that intends to use a volume rate to commit to tendering a voluntarily specified amount through the association. This amount must not, however, be so large as to represent a total or near total commitment by the shippers. Second, negotiations between the association and a carrier or conference must be conducted by an officer or employee of the association who is not also an employee of a member. These negotiations must be conducted on a confidential basis, and individual members cannot be permitted to participate directly in the negotiations. Third, all communications between the association and individual members must be kept confidential. In particular, the association cannot disclose which members are purchasing transportation services under a particular rate or contract, or the quantities any member intends to or actually purchases. The second and third prohibitions will eliminate the risk that members may use the association as an opportunity for discussing and coordinating the price and output of the delivered good.

With respect to the issues involving price fixing and other reductions in competition among members, I stated that our concerns would ordinarily be satisfied if transportation cost is less than 20 percent of final product price, and if the association agrees to adopt the previously-

discussed procedural and operational safeguards. In some exceptional circumstances, however, these two elements may not be sufficient to guarantee a favorable business review letter. In analyzing business review requests we always consider the particular characteristics of the industry or industries involved. In this regard, special concerns would be raised, for example, in industries that have had a recent history of price fixing, or where transportation cost is the only significant variable in setting price. In such cases a number of other factors would have to be evaluated before a favorable letter could be issued.

I want to stress, however, that a shippers' association that does not satisfy these "rules of thumb" (i.e., less than 35 percent of shipping capacity, less than 20 percent transportation cost, and the three safeguards) would by no means necessarily run afoul of the antitrust laws and would not necessarily receive an unfavorable business review letter. In a case where any of these tests is not satisfied, we will proceed to examine other structural and performance characteristics of the industry involved to determine whether other factors eliminate any competitive concerns from the formation and operation of the association. For example, in an unconcentrated market, in a market characterized by easy entry, or in a shippers' association accounting for only a small portion of the sales in the market, the likelihood of collusion may be sufficiently remote or easily detected to alleviate the need for some or all these safeguards. Such a conclusion, of course, would generally require a more extensive investigation in which we would make use of market shares for firms in the properly defined output markets that are affected by the shippers' association.

In any event, it is important to stress that a favorable business review letter covers only that conduct that comes squarely within the four corners of the letter itself. A business review letter obviously states our enforcement intentions only for conduct explicitly disclosed. Thus, for example, if members of an association actually fix prices despite a commitment to adopt specified safeguards designed to ensure against collusion, the Justice Department would vigorously and criminally prosecute the anticompetitive conduct.

Finally, as I alluded to earlier, it is the obligation of anyone seeking a business review letter to ensure that the Justice Department is provided with all the information necessary to analyze the request. Putting all relevant information in the initial request is the only way to avoid time consuming follow-up letters between the association and the Justice Department. A

complete and accurate initial request will substantially streamline the review process and shorten the time between the initial request and the Department's final response.

That concludes my remarks; I hope you will find them helpful in forming and operating shippers' associations in the future. We in the Antitrust Division recognize that associations can increase economic efficiencies and benefit consumers and generally do not represent a threat to competition. I can assure you that we are, and will continue to be, mindful of the need to carry out our enforcement obligations in a way that avoids creating unnecessary obstacles to the formation of shippers' associations that do not threaten competition. If, however, shippers' associations are not at least competitively innocuous or are used as a cover for cartel or monopsonistic activity, we will not hesitate to take vigorous enforcement action as required by law.

#### Footnotes

1. Shipping Act of 1984 (the Act), 46 U.S.C. app. §§ 1701-1720.
2. Act § 3(24), 46 U.S.C. app. § 1702(24).
3. Act § 8(c), 46 U.S.C. app. § 1707(c).
4. Act § 10(b)(13), 46 U.S.C. app. § 1709(b)(13).
5. Business Review Procedure, 28 C.F.R. § 50.6.