

HOWREY & SIMON

Attorneys at Law
1299 Pennsylvania Ave., NW
Washington, DC 20004-2402
(202) 783-0800
FAX (202) 383-6610

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OFFICE OF OPERATIONS
ANTI-TRUST DIVISION

Michael P. A. Cohen
202/383-6962
cohenm@howrey.com

BY HAND DELIVERY

The Honorable Joel I. Klein
Assistant Attorney General
United States Department of Justice
Antitrust Division
950 Pennsylvania Ave., N.W., Room 3109
Washington, D.C. 20530

Re: Proposed NSM Joint Purchasing Association

Dear Mr. Klein:

Pursuant to the Antitrust Division's business review procedure, 28 C.F.R. § 50.6 (1998), this request is for a business review letter stating the Division's enforcement intentions regarding the NSM Purchasing Association, a proposed joint buying group for independent, family-owned funeral homes.

The primary and express purpose of the Association will be to achieve buying efficiencies in connection with the purchase of caskets, through volume discounts currently attained by larger, corporate organizations like Service Corporation International or The Loewen Group, who have thousands of funeral locations nationwide. Small, independent, family-owned funeral firms with only one or at most a handful of locations cannot accumulate sufficient buying quantities on their own to reach these discount levels. Through the Association, independent firms hope to aggregate purchases to obtain competitive discounts, reducing both their costs, and corresponding prices to consumers.

The Association will be formed and organized in conformity with the Division's joint purchasing guidelines, and will specifically be structured to contain all requisite safeguards against any possibility of collusion or competitively-sensitive information exchanges among the Association participants. To assist your evaluation of the proposed venture, an overview of the industry, the structure for the Association and an analysis of relevant antitrust issues are set forth below.

I. INDUSTRY BACKGROUND

The face of the funeral industry has changed dramatically over the past decade, and the emerging landscape has resulted in cost competition that independent, family-owned funeral homes must find ways to meet in order to survive. First, and foremost, the family-owned, independent community funeral home is bowing to a trend of corporate consolidation in the

industry. The leaders of the consolidation movement are the conglomerate acquisition companies, Service Corporation International (SCI), The Loewen Group and Stewart Enterprises.¹ Together, these three companies accounted for 36% of all funeral revenues in the United States in 1996.² And of the 22,156 funeral homes in this country, 5,017 -- approximately 22% -- are now owned by the five largest firms -- SCI, Loewen, Stewart, Equity Corporation International, and Carriage Services, Inc.³

Through acquisition campaigns in target regions, the conglomerate funeral corporations have managed to achieve lower cost structures. Typically, a corporation will have a number of funeral homes located around a cemetery, also owned by the corporation. The conglomerate funeral homes will then share resources, such as transportation between all the facilities, in an effort to cut costs, putting price pressure on the family-owned, independent firms, which, for example, must maintain a full fleet for their own services.

Similarly, due to their size, these firms have successfully negotiated volume discounts from a number of their suppliers. SCI, Loewen and Stewart, for example, are reported to be receiving volume discounts "in the range of 40%" off the wholesale price of caskets from Batesville Casket Company, the leading casket manufacturer in the United States.⁴ Such discounts leave independent homes scrambling for ways to cut costs to compete effectively, given their inability to reach purchase levels that trigger these volume discounts on their own.

In addition, independent, family-owned funeral homes confront new competitive pressures from the rapidly rising number of crematoria, which are quickly becoming the alternative of choice to the traditional funeral. Between 1990 and 1995, cremation as a

¹ SCI is the largest funeral services corporation in the world operating primarily in Australia, Canada, France, the UK and the United States. SCI owns about 3,127 funeral homes, 392 cemeteries, and 166 crematoria in 17 countries. See SCI Form 10K Filing with the Securities & Exchange Commission, Mar. 30, 1998. SCI employs over 24,072 individuals and its total revenues exceeded \$2.4 billion last year. *Id.* Loewen is the second largest funeral services company in the world, controlling 1,101 local homes and 497 cemeteries in the US, Canada, and the UK. It currently employs approximately 16,000 individuals and its total revenues exceeded \$1.1 billion dollars last year. See Loewen Group Form 10-K filing with the Securities & Exchange Commission, Mar. 30, 1998. Stewart is the third largest provider of funeral services in North America, operating 419 funeral homes and 131 cemeteries in 25 states and 8 countries. Stewart employs 9,300 people in the industry, and its total revenues last year were \$532 million. See Stewart Form 10-K filing with the Securities & Exchange Commission, Jan. 29, 1998.

² *Id.*; United States Census Bureau, Service Annual Survey 1996, Table 3.1.

³ See *supra* note 1 (SEC 10K Filings for SCI, Loewen and Stewart reporting funeral locations); Microsoft Investor <http://investor.msn.com/research/snapshot.asp?Symbol=CSV> (Carriage Services, Inc. rank and number of funeral locations); Microsoft Investor [http://investor.msn.com/research/snapshot.asp? Symbol = EQU](http://investor.msn.com/research/snapshot.asp?Symbol=EQU) (Equity Corporation rank and number of funeral locations).

⁴ Ron Hast, *Loewen, SCI, Stewart Marry Batesville*, Mortuary Management, Apr. 1998, at 4; *Batesville Casket Discounts to SCI: Keeping It Secret Not So Simple*, 7 Funeral Monitor, May 11, 1998, at 1.

percentage of total funeral services rose from 17% to 21%, with Alaska, Nevada and Montana leading the trend with cremation rates of 50% or more.⁵ The most obvious reason for such a shift in preferences is the fact that the average cremation cost is \$500 compared to the average traditional funeral cost of more than \$4,600 (not including burial plot and marker).⁶

As cremations become the most popular choice of final interment, the corporate firms like SCI, Loewen and Stewart are well positioned with the financial resources to diversify into this capital-intensive industry. The independent funeral home, on the other hand, must find ways to be more cost effective to compete with the low costs of cremation.

The independent funeral homes also face new competition from cemeteries, which are now consolidating services in an effort to offer "one-stop shopping" for funeral needs, in reaction to competition from conglomerate-owned cemetery/funeral home combinations. Cemeteries are also engaging in long-term contracts with corporate homes for a percentage of all interments, again increasing cost pressure on independents, whose business is not of sufficient volume for such long-term agreements.

Finally, on top of the crematoriums, cemeteries and the 22,156 funeral homes, discount casket retailers have stepped into the competitive landscape, mass marketing caskets. There are currently at least 169 direct casket retailers in the United States.⁷ Many are equipped to ship caskets on twenty-four hour notice to anywhere in the world.⁸

Not surprisingly, consumer reactions to the current environment are consistent with this new cost competition:

Record evidence indicates...that consumers' selections of individual funeral providers, overall types of funeral service, and individual funeral goods and services are price-sensitive.... "[L]ow-cost" funeral homes, where they exist,

⁵ American Demographics, Inc., *The Information on Cremation*, 4 Forecast, at 7 (Apr. 1997); Cremation Association of North America, <http://www.cremation.org/stats.htm>.

⁶ 4 Forecast, *supra*, at 7.

⁷ See www.consumercasket-usa.com (National Casket Retailers Association Web Page); www.illinoiscasketco.com (Illinois Casket Co. Web Page); www.casketstoreoutlet.com (Thwal/Casket Outlet Page); Colles Stowell, *Hampton Falls Firm Finds a Lively Market for Retail Casket Sales*, *New Hampshire Business Review*, Nov. 21, 1997 at 14; Su-jin-Yim, *Casket Store Challenges Funeral Cost*, *News & Observer*, July 12, 1997 at D1; Steve Everly, *Caskets To Go: Store Is First for KC Area*, *Kansas City Star*, Mar. 18, 1998, at A1; Jim Yardley, *Selling Coffins From a Storefront*, *N.Y. Times*, May 29, 1998, at A19; Linda McNatt, *New North Carolina Store Has Customers Dying to Get In*, *Roanoke Times & World News*, Jan. 27, 1998 at A5.

⁸ If none of these options appeal to the purchaser, families can purchase inexpensive home funeral kits that provide all the materials necessary to intern loved one's from the comfort of home.

have increased their business substantially in recent years as a direct result of their competitive pricing practices.⁹

If independent, family-owned funeral homes are to survive in this new, cost-cutting arena, they must establish a means to compete effectively, and the most immediate method to maintain profitability is cost control. The proposed NSM Purchasing Association is intended for just this purpose, to achieve cost controls through volume discounts currently available to the conglomerate funeral consolidators, cemeteries and retail casket outlets, who already have the requisite scale to achieve such purchasing efficiencies.

II. THE ASSOCIATION STRUCTURE

The proposed NSM Purchasing Association will be a separately incorporated, wholly-owned subsidiary of NSM.¹⁰ The directors of the Association will consist of two ex officio positions for the sitting NSM President and active Executive Director, and five at-large NSM members, who will serve staggering two-year terms.

Apart from the directors, no person employed by the Association will be affiliated with any participating member, or any funeral firm generally. The Association plans to hire a full-time, independent buying agent to conduct the business of the Association and negotiate volume discounts with casket suppliers. The buying agent will not be an employee of any member of the Association or any other funeral home. Similarly, none of the Association's other officers or staff will be employees of any participant or any other funeral firm.

Membership in the Association will initially consist of the members of NSM, but the Association will be open to any independent, family or privately-owned funeral home in the United States. Although the Association is expected to grow, it is extremely unlikely that its participation would ever reach levels raising antitrust concerns; nevertheless, to guard against this possibility, the Association's Constitution and By-Laws will contain an express, unalterable cap to ensure membership never exceeds levels that account for more than thirty-five percent of domestic casket purchases, to comply with relevant antitrust guidelines. *See infra* Part III.

Similar to other buying groups the Division has approved in the past, the Association does plan to deny membership to corporate conglomerate organizations such as Service Corporation International, The Loewen Group or Stewart, Inc., whose volume casket purchases

⁹ Funeral Industry Practices Regulatory Ruling Part II, 59 Fed. Reg. 1592, 1598 (1994).

¹⁰ Founded in 1917, NSM (National Selected Morticians) itself is a District of Columbia not-for-profit trade association of 865 independent funeral firms, whose approximately 1400 funeral locations comprise no more than 6.3% of the 22,000 estimated funeral firms in the United States. There are several other funeral firm trade associations in this country, such as the National Funeral Directors Association (NFDA), Order of the Golden Rule (OGR) or National Funeral Directors and Morticians Association (NFDMA).

already result in the volume discounts that the Association is designed to obtain. *See, e.g.*, Nickel Users Purchasing Association Business Review Letter, 1992 DOJBRL LEXIS 29, at *3 (July 13, 1992) (denying membership to “producers [who] do not need a cooperative association to obtain a competitive price”); Independent Drug Wholesalers Group Business Review Letter, 1987 DOJBRL LEXIS 15, at *1 (May 18, 1987) (buying group limited to drug wholesalers with fewer than six distribution centers).

Members will be asked to provide the Association with voluntary commitments for the purpose of negotiating volume discounts, but will remain entirely free to purchase any and all their goods outside the Association. The Association will be funded through annual subscription fees and fees for services provided to participating members.

Finally, the Association will implement a host of measures to safeguard against any possibility of collusion or exchange of competitively-sensitive information among its membership. These safeguards are set forth in greater detail in Part IV, *infra*.

III. THE PROPOSED BUYING GROUP FALLS WITHIN THE JOINT GUIDELINES SAFE HARBOR PROVISIONS

The Department of Justice and Federal Trade Commission Statement of Antitrust Enforcement Policy on Joint Purchasing Arrangements Among Health Care Providers (hereinafter “Guidelines”) sets forth the legal framework for analyzing antitrust implications of joint purchasing arrangements.¹¹ The Guidelines, in the first instance, articulate the procompetitive potential of a joint purchasing group: “the participants frequently can obtain volume discounts, reduce transaction costs, and have access to consulting advice that may not be available to each participant on its own.” Guidelines Introduction. “Where there appear to be significant efficiencies from a joint purchasing arrangement, the Agencies will not challenge the arrangement absent substantial risk of anticompetitive effects.” *Id.* at Part B.

Under these principles, the Guidelines state that “[j]oint purchasing arrangements are unlikely to raise antitrust concerns unless (1) the arrangement accounts for so large a portion of the purchases of a product or service that it can effectively exercise market power in the purchase of the product or service, or (2) the products or services being purchased jointly account for so

¹¹ Although initially drafted for the health care industry, the Division has applied the Guidelines to proposed joint buying ventures across all industries. *See, e.g.*, Business Review Letter re: California Large Electric Power Purchasing Ass’n, 1997 DOJBRL LEXIS 20 (Nov. 20, 1997); Business Review Letter re: Utilities Service Alliance, 1996 DOJBRL LEXIS 4 (July 3, 1996); Business Review Letter re: Texas Oil Drilling Proposal to Form Joint Purchasing Agent to Procure Chinese Barite, 1996 DOJBRL LEXIS 10 (May 13, 1996); Business Review Letter re: BTCC Proposal to Form Group to Negotiate Domestic Air Travel Fares, 1995 DOJBRL LEXIS 9 (July 14, 1995); Business Review Letter re: Nickel User Purchasing Ass’n, 1993 DOJBRL LEXIS 17 (June 2, 1993); Business Review Letter re: North Texas Regional Clearinghouse Ass’n; 1987 DOJBRL LEXIS 4 (Sept. 23, 1987); Business Review Letter re: Mid-America National Cable Television Cooperative, 1985 DOJBRL LEXIS 48 (Apr. 25, 1985).

large a proportion of the total cost of the services being sold by the participants that the joint purchasing arrangement may facilitate price fixing or otherwise reduce competition." *Id.* at Introduction. "If neither factor is present, the joint purchasing arrangement will not present competitive concerns." *Id.*

Within this framework, the Guidelines establish an "antitrust safety zone." Absent extraordinary circumstances, the agencies will not challenge a joint buying arrangement so long as: "(1) the purchases account for less than 35 percent of the total sales of the purchased product or service in the relevant market; and (2) the cost of the products and services purchased jointly accounts for less than 20 percent of the total revenues from all products or services sold by each competing participant in the joint purchasing arrangement." *Id.* at Part A.

The proposed NSM Purchasing Association falls well within this safe harbor. First, initial participants would be the current NSM membership, which is approximately 865 firms whose total locations comprise approximately 1400 of the more than 22,000 funeral homes in the United States. The Association's initial membership, in other words, would be no more than 6.3% of the domestic funeral home industry, and *far less* of the total market for casket sales, which would include cemeteries and retail casket outlets.

Also noteworthy in this regard is the expectation and need for the Association to aggregate purchases with a single supplier to achieve the greatest volume discounts available. The two prospective suppliers for the Association – York, the second largest casket company, and Aurora, the largest privately-held casket company – have a 15% and 8% market share respectively.¹² Thus assuming participants in the Association accounted for the entire current output of either prospective supplier, which is hardly likely, there is no possibility or even probability of approaching the safe harbor line at current sales levels.

In short, the probability of membership even approximating levels of antitrust concern is unrealistic. Nevertheless, because the Association membership is expected to grow, to preclude any possibility of antitrust danger, the Association's Constitution and By-Laws will contain an express ceiling, capping membership at levels that will ensure its participants cannot ever account for more than thirty-five percent of domestic casket sales. *See Utilities Services Alliance Business Review Letter, 1996 DOJBRL LEXIS 4, at *6 (July 3, 1996)* ("[w]hile membership may grow, it will not be allowed to result in a greater than 35 percent market share, the safe harbor criterion that the Antitrust Division has employed in reviewing joint purchasing

¹² *See Encyclopedia of American Industries*, at 1442-43 (2d ed. 1998) (York market share); *US Private Companies* at 98 (1998) (Aurora sales). The market leader is Batesville Casket, a wholly owned subsidiary of Hillenbrand Industries, with around 60% market share. *See 2 Manufacturing USA*, at 2190 (Ward's 5th ed. 1996) (casket shipments valued at \$1.324 billion); Hillenbrand Industries Form 10-K Filing with Securities & Exchange Commission for Fiscal Year Ended Nov. 29, 1997 (casket revenues of \$810 million.) In addition to Batesville, York and Aurora, there are 192 other casket companies in the United States. United States Dep't of Commerce, 1992 Census of Manufacturers, Table 3a.

ventures"); *see also* Business Travel Contractors Corporation Business Review Letter, 1995 DOJBRL LEXIS 9, *2 (July 14, 1995).

Second, the 1997 percentage of casket cost to the selling price for an adult funeral was approximately 16.91%, below the Guidelines 20% threshold.¹³ This percentage cost, moreover, is expected to decrease, as has been the trend over the past two decades. (The percentage casket cost to funeral revenues decreased from 18.11% in 1977 to 17.18% in 1987, and to 16.91% over the past decade.)¹⁴

IV. THE BUYING GROUP WILL BE ESTABLISHED WITH ANTITRUST SAFEGUARDS IN PLACE

To address any potential concerns of member collusion or improper competitive information exchanges by members, the Association will further incorporate the following additional "safeguards:"

- The proposed buying agent will be independent, and not be employed by or affiliated with any funeral firm, let alone any member firm. No member will be allowed to negotiate on behalf of the Association;
- Competitively sensitive information, such as member-specific costs and pricing, will be kept strictly confidential by the independent agent, and not disseminated or exchanged between participating firms. This safeguard will be expressly set forth in the Association's By-Laws. Confidentiality agreements will also be required for this purpose, and only aggregate information necessary to allow members to decide whether to participate in a group purchase will be shared, if at all;
- Members will remain entirely free to purchase any goods on their own behalf outside the Association, but members will be asked to voluntarily commit to minimum purchases in order to negotiate volume discounts;
- Legal counsel will be present at any meetings of the members of the Association or its Directors, and minutes of any such meeting will be maintained; and

¹³ Federated Funeral Directors of Am., Management Analysis Dep't, *Trends in the Last Twenty Years*. "Federated Funeral Directors of America processes records from 1,500 funeral home clients in 30 states that conduct about 181,000 funerals a year, representing just under 10% of all deaths. FFDA is the largest company of its type in the country." Funeral Industry Practices Regulatory Ruling Part II, 59 Fed. Reg. 1592, 1599 n.78 (1994).

¹⁴ Federated Funeral Directors of Am., Management Analysis Dep't, *Trends in the Last Twenty Years*.

- An antitrust compliance policy will be distributed to members, and an undertaking acknowledging receipt of the compliance policy will be executed by each funeral firm as a condition of membership.

These measures should sufficiently safeguard against any potential for improper information exchange or collusion under the antitrust laws. *See generally* Guidelines Part B.

CONCLUSION

In sum, the proposed NSM Purchasing Association is well within the "safe harbor" established by the Division for joint buying groups. With initial membership totaling less than 6.3% of all funeral homes in the United States, and the cost of the casket projected to be no more than 16.9% (and decreasing) of the total revenue for a funeral service, there can be no risk of monopsony purchasing power. The Association will simply provide independent, family-owned, community funeral firms with equal footing to cost-compete with the conglomerate firms, cemeteries and direct casket retailers, enhancing competition and further fueling the current competitive environment, which has resulted in lowering the price of funeral goods and services to consumers. The proposed venture is therefore pro-competitive, and indeed essential for the survival of the independents.

I would be pleased to provide you with any further information you deem necessary, or answer any questions or comments you may have regarding this business review request. Thank you in advance for your attention and consideration of this matter.

Sincerely,



Michael P. A. Cohen
HOWREY & SIMON