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ROUNDTABLE ON ELECTRONIC COMMERCE

-- Note by the United States --

The attached note is submitted by the Delegation of the United States to the Committee on Competition Law and Policy FOR DISCUSSION at its forthcoming meeting on 24-25 October 2000.

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Introduction

1. Business-to-business electronic marketplaces ("B2Bs") use the Internet to electronically connect businesses to each other. They have the potential to generate tremendous efficiencies, which can result in lower prices, higher quality, and greater innovation.

2. The Federal Trade Commission hosted a public workshop on B2B, "Competition Policy in the World of B2B Electronic Marketplaces" in June 2000.[1] Organized by the FTC's Office of Policy Planning, the event included over 65 panelists, with input from more than 200 sources, and was attended by more than 600 people. Most of the participants were business people either operating or forming B2Bs and antitrust practitioners who have already been working with B2Bs to structure them so as to avoid antitrust problems. As the FTC's Policy Planning Director Susan DeSanti noted at the workshop, the FTC is "very much in a learning mode."

3. There was widespread agreement that just as competition plays a pivotal role in more traditional offline markets, it has an important role to play the context of emerging online markets. Like other collaborations, B2Bs have the potential to raise antitrust concerns.

4. The Antitrust Guidelines for Collaborations among Competitors ("Competitor Collaboration Guidelines"), recently issued jointly by the Federal Trade Commission and the Antitrust Division of the Department of Justice,[2] provide a useful starting point for questions that those organizing or participating in a B2B e-marketplace should consider.

5. This submission reflects several key themes that dominated the FTC's public workshop. First, there was widespread recognition of the potential for tremendous efficiencies. Second, antitrust practitioners report that when antitrust issues arise, they can generally be solved through practical solutions. Lastly, B2B electronic commerce is still a relatively new phenomenon; business people, attorneys, and regulators should keep abreast of developments.

Efficiencies

6. Administrative costs are the costs of effecting the transaction itself. These include the time and energy firms expend for everything from placing an order to issuing a check upon receipt of the goods. Regardless of the industry, these costs are uniformly described as substantial and uniformly thought to be subject to substantial reduction through B2Bs. The current phone and fax method that some firms use takes its toll in time and accuracy. Electronic transmission of such transactions can dramatically reduce both costs. In fact, decreasing administrative costs may be the most immediate and widespread effect of B2Bs.

7. Price transparency is the ability of buyers to see different prices and the ability of sellers to have their prices be seen by many buyers. By reducing search costs and fostering efficient bidding mechanisms, B2Bs can increase price transparency. Buyers can save money when B2Bs make it easier to comparison-shop and to find more suppliers, while sellers can profit by having greater and cheaper access to more

1 Materials from the workshop, including all written submissions, are available on the FTC website at www.ftc.gov/bc/b2b/index.htm|.

2. *Reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,160; also available at www.ftc.gov/os/2000/04/ftcdojguidelines.pdf.

potential customers. In B2Bs that set their prices through catalogs, buyers can, with a few mouse clicks, compare the prices of several vendors of a given product. In B2Bs that host reverse auctions, a buyer can invite sellers across the globe to bid against each other for its business; likewise, sellers can auction items such as used machinery in B2Bs that allow them to reach more potential buyers – and higher sales prices – than before.

8. B2Bs can also let suppliers all along the supply chain know what the buyer wants and when, reducing inventory costs and delays. The process can be even more streamlined for businesses with automated inventory systems, which may be connected to a B2B so that the buyer's internal inventory system can more seamlessly convey the buyer's needs as they arise.

9. Joint purchasing can help reduce transaction costs through scale economies in purchasing and may produce other efficiencies. For example, some participants stated that small purchasers who purchase jointly through a B2B may be able to take advantage of quantity discounts and truckload pricing.

10. At this relatively early stage of B2B marketplace development, it is important to recognize that while some B2Bs are operational and have achieved certain kinds of efficiencies, many more are in the planning stage, with the potential to realize yet more and different kinds of efficiencies. Thus it may be too early to tell whether all of the promised efficiencies of B2Bs will be achieved.

Information Exchange

11. Several participants were concerned that information-sharing agreements in the context of B2Bs could facilitate price coordination and thereby injure competition in the market for the goods and services traded on the B2B. As one panelist stated, "The Internet is ... an extremely efficient mechanism for exchange of information ... and that's only going to exacerbate the difficulties of identifying when it's collusive."[3]

12. Participants noted a variety of ways in which such information-sharing agreements through B2Bs could facilitate price coordination. They asked, for example, whether sellers in a concentrated market could agree to a practice that would let them see each other's bids in online B2B auctions, and whether that would allow them to tacitly fix prices or police cheating on a price-fixing agreement. These concerns were not limited to sellers' actions; they also questioned whether buyers could agree, through a B2B, to share information about their purchases of inputs such that each would know the other's cost structures, making it easier for them to collude on their selling prices. They likewise raised the concern that buyers could agree through a B2B to reveal to each other the input purchases they each have made, making it easier for them to police cheating on an output-fixing plan.

13. Panelists mentioned a variety of factors that would affect the analysis. For example, they noted the importance of market structure, of determining who is sharing information with whom, and of ascertaining the competitive significance of the kind of information being shared.

14. The panelists also discussed the efficiencies that information-sharing practices may promote and the impact those efficiencies would have on the antitrust analysis. They also discussed less restrictive alternatives, including segmenting online catalogs; restricting the information available to certain participants in online auctions; the use of nondisclosure agreements; and the practice of keeping sensitive

3. Transcript of "Competition Policy in the World of B2B Electronic Marketplaces" Workshop ("Workshop Transcript") at 526 (comments of Harry First).

information from board members employed by participants. They discussed whether such alternatives would adequately safeguard against competitive harm and whether they would sacrifice other efficiencies.

Joint Purchasing

15. Monopsony is “market power exercised on the buying side of the market,” power that lets a buyer or buyer group “reduce the purchase price by scaling back its purchases.”[4] Thus, the Horizontal Merger Guidelines provide that “[m]arket power ... encompasses the ability of a single buyer (a "monopsonist"), a coordinating group of buyers, or a single buyer that is not a monopsonist, to depress the price paid for a product to a level that is below the competitive price and thereby depress output. The exercise of market power by buyers ("monopsony power") has adverse effects comparable to those associated with the exercise of market power by sellers."[5] Under the classical theory of monopsony, a single buyer in the market reduces its purchases of a given input in order to lower the price it must pay.[6]

16. The workshop record reflects that not all B2Bs facilitate, or anticipate facilitating, joint purchasing. However, some workshop participants expressed concerns that B2B participants with a large enough market share might use the B2B to exercise monopsony power. Workshop panelists posited that the necessary coordination could be achieved expressly, through an agent, through consulting services that permit coordination of input purchases, or perhaps through tacit collusion.

17. One factor warranting consideration is whether the buying group in question accounts for a sufficient share of the buying market such that its purchases may influence the price of inputs sought. For this reason, workshop participants expressed the view that the joint purchasing of indirect inputs such as those used for maintenance, repair, or operations is generally less likely to raise concerns than joint purchasing of direct inputs.

18. Panelists emphasized that buyer groups driving prices down through monopsony power are distinct from buyer groups winning better prices through increased efficiencies, such as by enabling their suppliers to save money by selling to the group. In such cases, there may well be savings to suppliers warranting quantity discounts.

Exclusion

19. Workshop participants expressed concern about the potential for disadvantageous treatment of the competitors of the participant-owners of particular B2Bs, which could take various subtle forms short of outright access denials. As examples, participant-owners might receive rebates of fees that are unavailable to their rivals; information might be presented in ways that give preference to participant-owners; and discriminatory operating rules or disadvantageous access to electronic interchange standards could leave rivals with reduced functionality or higher costs. (It should be noted, however, that the workshop record yielded little evidence of current exclusion from B2Bs. To the contrary, several panelists stated that their B2Bs would be open to all comers.)

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4. Areeda, Hovenkamp & Solow, Antitrust Law (1995), at ¶ 574.

5. DOJ & FTC Horizontal Merger Guidelines (April 2, 1992) at § 0.1.

6. See generally Roger D. Blair & Jeffrey L. Harrison, Antitrust Policy and Monopsony, 76 Cornell L. Rev. 297 (1991).

20. Workshop participants expressed concern that denying or disadvantaging competitors in their access to a B2B e-marketplace could, in certain circumstances, raise their costs or maintain them above levels that otherwise would prevail. Antitrust scrutiny might be warranted if this harmed competition, not merely competitors.

21. Workshop participants noted the need to consider carefully the extent of the disadvantage that likely would ensue from denying or limiting access to the B2B, as well as the substitutes to which the disadvantaged firms could turn to avoid or mitigate the disadvantage. In this regard, some panelists stated that any such excluded rivals could readily reach suppliers or buyers through alternative mechanisms at comparable costs; other panelists, however, suggested that strong network efficiencies in an incumbent marketplace B2B might make alternatives unsatisfactory. Workshop participants likewise had mixed views on the ease, and hence the curative power, of entry. Some argued that entry of new B2Bs would quickly provide ready alternatives for disadvantaged rivals, but others questioned the ease of entry into these markets. These are but a sampling of the factors discussed at the workshop, but they illustrate the nature of the concerns.

22. Some workshop participants asserted that some differences in treatment may be warranted to discourage free riding by non-owner participants, or as a means of ensuring access only by "qualified sellers." These participants pointed out that exclusion or other access distinctions may be reasonably necessary to achieve the pro-competitive benefits of a particular B2B.

Exclusivity

23. Finally, several panelists expressed concern that B2Bs may undermine the development of effective B2B competition by improperly requiring or persuading buyers or sellers to deal exclusively with particular B2Bs. They noted that this is an early but potentially critical stage of B2B market development, and that determinations made at the outset may shape B2B competition for years ahead. Of course, to the extent that exclusivity practices also give rise to efficiencies, they may prove on balance to be procompetitive.

24. Workshop panelists suggested a variety of potential competitive concerns that exclusivity practices can raise in the B2B marketplace. These include: (1) higher prices - some stated a B2B with market power could impose supracompetitive prices for their services; (2) less efficient service - some participants were concerned that a B2B with market power might be able to rest on its laurels and offer less functionality; (3) entry barriers - participants voiced concerns that exclusivity practices could sustain any existing market power over time by making entry more difficult.

25. In this regard, participants raised concerns about the potentially powerful network effects at work in B2Bs. Some panelists stated that network effects are strong in B2Bs, and several panelists suggested that whether multiple marketplaces develop to serve any one industry will be affected by the nature and magnitude of network effects in B2Bs in that industry. As one participant noted, "The attractiveness of the marketplace to the seller is often a function of the extent to which the marketplace is used by the seller's major buyers. . . . Sellers who wish to continue their relationships with these buyers will want to participate in the marketplace."[7] However, others predicted that network effects will not lead to one dominant network in any B2B relevant market.

26. The FTC has studied network effects in other contexts. In 1995 the FTC conducted extensive hearings concerning competition policy in high-tech markets. Based on the relevant testimony, case law,

7. See Written Submission of energy Leader, Workshop Transcript at 12.

and analytical literature, the Staff Report noted the pronounced advantage that network effects can give an incumbent operator, and cautioned that conduct that could contribute to achieving dominance warrants heightened scrutiny in settings with prominent network effects and switching costs.[8] Substantial network efficiencies and consumer switching costs might make it difficult for an entrant to start small, compete effectively, and grow to become a significant factor in the market.

Conclusion

27. Antitrust analysis is a highly fact-driven inquiry, and development of federal antitrust policies will be based on the facts of the matters before the antitrust enforcement agencies. One such example is the matter of the B2B venture, called Covisint, formed by five large automotive manufacturers and two information technology firms to provide services for firms in the automotive industry supply chain. Covisint was the first B2B venture that the FTC reviewed following its notification under the premerger notification provisions of the Hart-Scott-Rodino Antitrust Improvements Act (HSR Act). On September 11, 2000, the FTC closed its investigation of whether Covisint violates Section 7 of the Clayton Act, which prohibits mergers and acquisitions that are likely to substantially lessen competition, and terminated the waiting period under the HSR Act. However, in a public statement accompanying the closing, the Commission stated that because Covisint i) was in the early stages of its development and had not yet adopted by- laws, operating rules, or terms for participant access, ii) was not yet operational, and iii) in particular represented such a large share of the automobile market, the Commission could not say that implementation of the Covisint venture would not cause competitive concerns.

28. This is an exciting time in the development of new ways of transacting business over the Internet. B2B electronic marketplaces clearly have great potential to increase business productivity and provide consumers with lower prices, higher quality, and greater innovation. Proper attention must be paid to antitrust issues now, and continuing attention must be paid to them as we go forward, in order to help ensure that B2Bs can deliver their promised efficiencies without threatening competition.

8. 1996 Staff Report, ch. 9 at 13-14, 29 (discussing interface standards); available at www.ftc.gov/opp/global.htm.