Economics 420 **Mr. Elzinga**
Final Exam **Spring 1999**

ALL STUDENTS: Please write your name and section number (or class time) on the cover of your blue book, pledge the front of the blue book, and insert this copy of the test inside your blue book when you complete the examination. Both documents are to be turned in.

STUDENTS **NOT** WRITING TERM PAPERS are to answer, in order:
1-10; <u>either</u> 11a <u>or</u> 11b;
and <u>any 12</u> of the 18 short answers (again, in order).
This totals to 100 points maximum.

TERM PAPER STUDENTS are to answer, in order:
<u>either</u> 1 <u>or</u> 2; 3 <u>or</u> 4; 5 <u>or</u> 6; 7; <u>either</u> 8 <u>or</u> 9;
and <u>any 6</u> of the first 9 short answers (again, in order).
This totals to 50 points maximum.

1. (5 pts.)
You, a veteran of Econ 420, know that grocery stores, in order to be competitive in the marketplace, want to know their rivals' retail prices. Indeed, in class you saw (or heard reference to) an example of grocery store shelf prices gathered by a fake shopper who was an employee of another grocer. Price verification information gathered this way is costly and subject to error.

Scanning technology in retail grocery stores means the retail price of virtually every item is encoded in a grocery store's computer (fresh vegetables being the main exception). You start a business -- "Grocery Price Verification, Inc." -- which secures the computerized retail prices from grocery chains and you sell these prices. Your main customer base consists of grocery chains who want to know their rivals' prices. These chains never communicate directly to one another regarding their prices. They buy the data from you. In other words, Kroger buys from you, in digitized form, all the retail prices charged by Giant and Safeway. You purchase Kroger's price data and sell it at a profit to Giant and Safeway (and any other interested buyers). For most grocery chains, you are both a buyer and seller, e.g., Kroger buys price data about its rivals from you as well as selling its price data to you.

a. Can you make a buck doing this for long or will you find yourself in Sherman Act trouble? Why or why not?

b. Whether or not you are in trouble, are the grocery chains who buy or sell data to you in antitrust hot water? Why or why not?

2. (5 pts.)

In a Wall Street Journal article you were given in class, the writer, staff reporter John R. Wilke, described the unusually large number of price fixing cases brought by U.S. antitrust authorities against firms based in other countries, notably Japan. The sub-heading of a section of the paper was entitled "Overstepping Bounds?" and mentioned critics of these cases. Responding generally, what are the boundaries, as you understand them from this article, that make this kind of case delicate? What was the recent court ruling that may thwart this type of case?

3. (10 pts.)

In 1997, Staples and Office Depot planned to merge. Both firms run mega-retail office supply stores. The deal is not a small one: Staples offered $3.5 billion for Office Depot. According to the Wall Street Journal, the FTC staff opposes the deal. Under the Merger Guidelines, how is the FTC staff to structure its analysis? That is, without offering answers, set out the main questions the FTC will seek to answer in assessing such a merger.

4. (10 pts.)

Masterwork, Inc., a manufacturer of fine wall papers, markets its product line through independent home decoration and wall paper stores. It supplies these stores with pattern books at a cost to Masterwork of $5000 per store. These books show samples of Masterwork's paper, identifying it by product number, and giving its characteristics. Retail stores make clerks available to answer customer questions and to show merchandise samples by Masterwork and rival manufacturers.

Masterwork has a policy that its wall paper is to sell at retail at the prices it suggests. In 1996, Masterwork received complaints from four of its retailers that someone was discounting the Masterwork line. Masterwork also noticed that a firm called Tele-Wall-Paper, an 800 phone number order house, has been purchasing sizable amounts of Masterwork's wall papers and selling them to home owners who place orders over the phone at prices below Masterwork's suggested retail price.

You are Masterwork's legal counsel. Masterwork tells you they want to cut off Tele-Wall-Paper and "squish 'em like a bug." Based on current antitrust law, how do you help your client?

5. (Either a. or b., 4pts.; (that's 2 pts. for each part of a. or b.))

a. The defendants in Goldfarb offered at least 4 reasons why the per se approach to price fixing did not apply to them. What were two of them?

b. Kodak offered 3 reasons why it should be able to cut off ISOs from Kodak parts. What were two of them?

6. (4 pts.)

Toys 'R Us is tired of advertising the hot toys of the season and watching customers come to its store, try out the new toys, then go to a toy discounter and buy the toys. TRU announces it has elected "to decline the opportunity to purchase" merchandise from any major toy manufacturer who sells to toy discount operations. The toy manufacturers go along. The toy discounters complain to the FTC, saying: don't be fooled by TRU's courteous language; TRU is engaging in a "unilateral boycott" and "refusal to deal." Do you think TRU can get away with this? Very briefly, why or why not?

7. (10 pts., 2 pts. each)

Gluxo, a drug manufacturer, sells broad spectrum antibiotics to retail drug stores at $10.00 per case. New England Health Plan, an HMO, proposes to Gluxo: "we control the lives of 20,000 patients each month that need broad spectrum antibiotics. If you'll give us a $2.00 per case discount, we'll put your drug on our formulary and recommend that the doctors who are part of our HMO give preference to your drug for patients needing a broad spectrum antibiotic and we'll offer our patients the option of having the prescription filled at NEHP's in-house pharmacy at a lower price reflecting the discount." Gluxo goes along. Independent retail druggists not affiliated with NEHP complain about having to pay a higher price to Gluxo that handicaps them in competing for prescription business. They bring suit against Gluxo.

a. Under what statute will the retail druggists sue?

b. In antitrust lingo, what kind of price discrimination is Gluxo allegedly engaged in?

c. & d. Name two "defenses" Gluxo might try to raise?

e. Under Morton Salt, how will Gluxo fare?

8. (9 pts., 3 pts each)

You are trying to explain the law on predatory pricing to someone who is all confused. They ask you three questions:

a. What did it take to get convicted in the old days under <u>Utah Pie</u>?

b. What is the Areeda-Turner test for predation?

c. What does the Court mean in the Brown & Williamson cigarette case when it says you need to look at "recoupment" in a situation of alleged predation?

9. (9 pts.)

Amalgamated Mega-Monop worries that its success might have made it a "dominant firm" in a properly defined relevant market. It does not want to have Section 2 Sherman Act difficulties. Based on <u>Alcoa</u> and <u>Berkey-Kodak</u> (not <u>Kodak</u>, the ISO case),

a. explain what magnitude of market share may be problematic for AMM;

b. describe at least one situation that could be a Sherman Act pitfall for AMM given its non-trivial market share, and

c. describe one situation that would help AMM be successful in side-stepping the Sherman Act notwithstanding its prominence in its market.

10. (6 pts.) Mathematical Exercise

An amazing coincidence: a market has 10 equal size sellers.

a. What is the HHI?

b. Two of the firms seek to merge. What would be the new HHI if they did?

c. Would this merger be within the "safe harbor" of the Merger Guidelines? Why or why not?

11. (4 pts., 2 pts. each)

a. Define or distinguish "nolo contendere" and "consent decree."

b. Give two reasons why an antitrust defendant, honestly believing himself or herself to be quite innocent of a Sherman Act charge, nonetheless might seek to plea nolo contendere or enter into a consent decree?

12. Short Answer/Identification (24 pts. or 12 pts.) (2 pts. each).
Answer any 12 of a-r (<u>term paper students</u>: just do any 6 of a-i)

Define or describe:

a. The place of "plus factors" in Section 1 litigation

b. spot market

c. The Robert Crandall/Howard Putnam conversation

d. Mr. Joel Klein

e. Senators Hoar and Edmunds

f. The Wall Street Journal reports: "Federal antitrust enforcers are extracting bigger and better fines from companies that try to fly beneath their merger radar." One German company recently paid a $5.1 million. What is the offense that provokes these fines?

g. Sham exception to <u>Noerr</u>

h. from <u>Parke-Davis</u>: what a sales rep can and cannot say to a retailer regarding resale price maintenance

i. Supreme Court case that overruled <u>Schwinn</u>

------------------ TERM PAPER STUDENTS STOP HERE; OTHERS CONTINUE------------------

j. role of maverick firm in Guidelines

k. CSDs, as in "all branded CSDs"

l. exclusive territory agreement

m. volume discount schedule

n. Section 5 of Federal Trade Commission Act

Identify the case containing this quotation:

o. "A construction of the Sherman Act that would disqualify people from taking a public position on matters in which they are financially interested would thus deprive the government of a valuable source of information and, at the same time, deprive the people of their right to petition in the very instances in which that right may be of the most importance to them."

p. "In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal. And, of course, he may announce in advance the circumstances under which he will refuse to sell."

q. ". . . the law does not make mere size an offence or the existence of unexerted power an offence."

r. "Under the Sherman Act, a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal per se."