

Complaint

IN THE MATTER OF

TIME WARNER, INC.CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3972; File No. 9710070
Complaint, August 30, 2000--Decision, August 30, 2000*

This consent order addresses Time Warner's practices that restricted competition in the domestic market for prerecorded music. The complaint alleges that Time Warner adopted, implemented, and enforced Minimum Advertised Price ("MAP") provisions in their Cooperative Advertising Programs. By defining advertising broadly enough to include all in-store displays and signs, the MAP policies effectively precluded many retailers from communicating prices below MAP to their customers. The order requires Respondent to discontinue its MAP program for a period of seven years and contains several prohibitions to ensure that Respondent is unable to maintain the anticompetitive status quo in some other way.

Participants

For the Commission: *William L. Lanning, Karin F. Richards, James W. Frost, Geoffrey M. Green, Karen Mills, Jeffrey Goodman, June Casalmir, Kent Cox, Kristin Malmberg, Beverly Dodson, Brynna Connolly, Lorenzo Cellini, Veronica G. Kayne, Michael E. Antalics, John Howell, Daniel P. O'Brien, and Gregory Vistnes.*

For the Respondents: *Robert Joffe, Cravath, Swaine & Moore.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended,¹⁵ U.S.C. ' ' 41 et seq., by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Time Warner Inc. has violated the provisions of Section 5 of the Federal Trade Commission Act, 15

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U.S.C. ' 45, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues this complaint, stating its charges as follows:

PARAGRAPH ONE: Respondent Time Warner Inc. (ATime Warner@) is a corporation organized and existing under the laws of the State of Delaware with its principal place of business at 75 Rockefeller Plaza, New York, New York. Time Warner has interests in businesses that produce, manufacture, distribute, and market prerecorded music, among other things. Warner Music Group Inc. (AWMG@) is a wholly owned subsidiary of Time Warner, and is a corporation organized and existing under the laws of the State of Delaware with its principal place of business at 75 Rockefeller Plaza, New York, New York. Warner-Elektra-Atlantic Corporation (AWEA@) is a wholly owned subsidiary of Time Warner, and is a corporation organized and existing under the laws of the State of New York with its principal place of business at 111 N. Hollywood Way, Burbank, California.

PARAGRAPH TWO: Five major distributors sell and distribute over 85% of all prerecorded music in the United States. WEA is one of the five Amajor distributors@ of prerecorded music. Sony Music Entertainment Inc., Universal Music and Video Distribution Inc., EMI Music Distribution, and Bertelsmann Music Group, Inc. are the other Amajor distributors.@"

PARAGRAPH THREE: The major distributors sell prerecorded music to numerous retailers including independent retailers, large national chains, mass merchandisers, regional chains and consumer electronics stores. They also sell prerecorded music to sub-distributors who in turn supply retailers not serviced directly by the prerecorded music distributors.

PARAGRAPH FOUR: There are two relevant markets in this matter. First, the commercial development, distribution and wholesale sale, by any means, of prerecorded music (hereinafter Awholesale market@). Second, the retail sale, by any means, of prerecorded music (hereinafter Aretail market@). The geographic

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scope of the wholesale market is the United States of America. The wholesale market is characterized by high entry barriers that seriously limit the likelihood of effective new entry.

PARAGRAPH FIVE: In the early 1990=s, several large consumer electronics chains began selling compact discs and other prerecorded music products. These new entrants competed aggressively on price and offered consumers substantial savings on some prerecorded music products. A retail price war ensued and music retailers lowered their prices.

PARAGRAPH SIX: Some retailers, faced with newly invigorated price competition in the retail market, requested margin protection from WEA. In 1992, WEA was also concerned that declining retail prices could have wholesale price effects. Thereafter, WEA decided to introduce a Minimum Advertised Pricing (AMAP@) policy. In 1992 and 1993, the other major distributors adopted MAP policies. These policies set forth minimum advertised prices for most prerecorded music products. As discussed below, these MAP policies were modified between 1995 and 1996. In 1995 and 1996, retail prices increased. Since 1997, wholesale prices have also increased.

PARAGRAPH SEVEN: The MAP policy changes which occurred in 1995 and 1996 significantly tightened the programs. By February 1, 1997, each of the major distributors had implemented similar policies. The new MAP policies provided that any retailer who advertised the distributors= product below the established MAP would be subject to a suspension of all cooperative advertising and promotional funds for either 60 or 90 days. BMG=s policy varied slightly and provided that any retailer who violated the policy three times within a twelve month period would be subject to a suspension of all cooperative advertising and promotional funds for up to twelve months. For each company, the suspension would be imposed whether or not the retailer paid for the offending advertisement or promotion. In

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addition, the suspension would be imposed for in-store advertising and promotion@ that included virtually every method of communicating the price of the product to the consumer other than the pre-printed price sticker on the product.

PARAGRAPH EIGHT: With the exception of the BMG policy described herein, a single violation of the new MAP policies resulted in a total loss of all cooperative advertising and promotional funds for the specified suspension period. The severity of the new MAP penalties ensured that even the most aggressive retail competitors would stop advertising prices below MAP. By defining advertising broadly enough to include all in-store displays and signs, the MAP policies effectively precluded many retailers from communicating prices below MAP to their customers.

PARAGRAPH NINE: Shortly after adopting the new MAP policies, the distributors began aggressively enforcing the policies. Several high profile enforcement actions that resulted in long periods of suspension were widely publicized by the trade press.

PARAGRAPH TEN: WEA=s stricter MAP policy, in effect since December of 1995 and continuing to date, was implemented to eliminate aggressive retail pricing and to stabilize overall prices in the retail marketplace. This policy was successful.

PARAGRAPH ELEVEN: The purpose, effects, tendency or capacity of the acts and practices described in PARAGRAPHS SIX, SEVEN, EIGHT, NINE, and TEN relating to the implementation and enforcement of MAP policies are and have been to restrain trade unreasonably and hinder competition in the retail and wholesale markets for prerecorded music in the United States, and constitute a violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. ' 45.

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CONCLUSION

PARAGRAPH TWELVE: The aforesaid acts and practices of the respondent were and are to the prejudice and injury of the public. These acts and practices constitute unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. ' 45. These acts and practices may recur in the absence of the relief requested.

WHEREFORE, THE PREMISES CONSIDERED, the Federal Trade Commission on this thirtieth day of August, 2000, issues its complaint against said respondent.

By the Commission.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of Respondent, Time Warner Inc., and Respondent having been furnished thereafter with a copy of the draft of Complaint that the Bureau of Competition presented to the Commission for its consideration and which, if issued, would charge Respondent with violations of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. ' 45, and

Respondent, its attorneys, and counsel for the Commission having thereafter executed an Agreement Containing Consent Order (AConsent Agreement@), containing an admission by Respondent of all the jurisdictional facts set forth in the aforesaid draft of Complaint, a statement that the signing of said Consent

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Agreement is for settlement purposes only and does not constitute an admission by Respondent that the law has been violated as alleged in such Complaint, or that the facts as alleged in such Complaint, other than jurisdictional facts, are true, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that Respondent has violated said Act, and that a Complaint should issue stating its charges in that respect, and having accepted the executed Consent Agreement and placed such Consent Agreement on the public record for a period of thirty (30) days for the receipt and consideration of public comments, and having duly considered the comments filed thereafter by interested persons pursuant to ' 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and issues the following Order:

1. Respondent Time Warner Inc. is a corporation organized and existing under the laws of the State of Delaware with its principal place of business at 75 Rockefeller Plaza, New York, New York. Warner Music Group Inc. is a wholly owned subsidiary of Time Warner Inc., and is a corporation organized and existing under the laws of the State of Delaware with its principal place of business at 75 Rockefeller Plaza, New York, New York. Warner-Elektra-Atlantic Corporation is a wholly owned subsidiary of Time Warner, and is a corporation organized and existing under the laws of the State of New York with its principal place of business at 111 N. Hollywood Way, Burbank, California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the Respondent, and the proceeding is in the public interest.

ORDER**I.**

Decision and Order

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

- A. ATime Warner@ or ARespondent@ means Time Warner Inc., its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its subsidiaries, divisions, groups, and affiliates controlled by Time Warner, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- B. AWMG@ means Warner Music Group Inc., its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its subsidiaries, divisions, groups, and affiliates controlled by WMG, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- C. AWEA@ means Warner-Elektra-Atlantic Corporation, its directors, officers, employees, agents, representatives, predecessors, successors, and assigns; its subsidiaries, divisions, groups, and affiliates controlled by WEA, and the respective directors, officers, employees, agents, representatives, successors, and assigns of each.
- D. ACommission@ means the Federal Trade Commission.
- E. ARecord Clubs@ means the divisions of The Columbia House Company and BMG Music Service that operate as club-based direct marketers of prerecorded music, and manufacture or have manufactured for them product pursuant to a club license.
- F. AProduct@ means prerecorded music in physical or electronic format that is offered for sale or sold in the United States, including, but not limited to, compact discs (ACDs@), audio DVDs, audio cassettes, albums and digital audio files (i.e., digital files which are delivered to the consumer

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electronically, to be stored on the consumer=s hard drive or other storage device). AProduct@ does not include prerecorded music in physical or other electronic format manufactured or distributed by or for Record Clubs pursuant to Record Club licenses.

- G. ADealer@ means any person, corporation, or entity that in the course of its business offers for sale or sells any Product in or into the United States, including, but not limited to, wholesale distributors, retail establishments, and Internet retail sites, but excluding Record Producers.
- H. ARecord Producer@ means any person, corporation or entity that in the course of its business produces sound recordings for recording artists and manufactures Product from such sound recordings.
- I. ACooperative Advertising or Other Promotional Funds@ means any payment, rebate, charge-back or other consideration provided to a Dealer by WMG in exchange for any type of advertising, promotion or marketing efforts by that Dealer on behalf of WMG. This term also includes advertising, promotion, or marketing efforts by WMG on behalf of one or more identified Dealers. Examples of cooperative advertising include, but are not limited to, free goods provided to a Dealer by WMG, and payments for newspaper advertisements, radio and television advertisements, internet banner advertisements, posters and signs within a Dealer=s retail stores, pricing or positioning of Products within a Dealer=s retail stores, and point-of-purchase merchandising.
- J. AMedia Advertising@ means any promotional effort by a Dealer outside of the Dealer=s physical location or Dealer-controlled internet site, including but not limited to, print, radio, billboards, or television.
- K. AIn-Store Promotion@ means any promotional effort conducted in or on the physical premises of a Dealer or a

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Dealer-controlled internet site, including but not limited to, signs, bin cards, end caps, hit walls, listening posts, internet banner advertisements, and promotional stickers.

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L. AAdvertised or Promoted@ means:

- (1) any form of advertising, promotion, or marketing efforts by WMG on behalf of one or more of its Dealers;
- (2) any form of Media Advertising efforts including, but not limited to, print, radio, billboard, or television; and
- (3) any form of In-Store Promotion efforts including, but not limited to, signs, bin cards, end caps, hit walls, listening posts, internet banner advertisements and promotional stickers.

II.

It is further ordered that for a period of seven (7) years, WMG, directly, indirectly, or through any corporation, subsidiary, division or other device, in connection with the offering for sale, sale or distribution of any WMG Product in or into the United States of America in or affecting Acommerce,@ as defined by the Federal Trade Commission Act, shall cease and desist from directly or indirectly adopting, maintaining, enforcing or threatening to enforce any policy, practice or plan which makes the receipt of any Cooperative Advertising or Other Promotional Funds contingent upon the price or price level at which any WMG Product is Advertised or Promoted.

III.

It is further ordered that WMG, directly, indirectly, or through any corporation, subsidiary, division or other device, in connection with the offering for sale, sale or distribution of any WMG Product in or into the United States of America in or affecting “commerce,” as defined by the Federal Trade Commission Act, shall not directly or indirectly:

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- A. Adopt, maintain, enforce or threaten to enforce any policy, practice or plan which makes the receipt of any Cooperative Advertising or Other Promotional Funds contingent upon the price at which any WMG Product is offered for sale or sold;
- B. Adopt, maintain, enforce or threaten to enforce any policy, practice or plan which makes the receipt of any Cooperative Advertising or Other Promotional Funds contingent upon the price or price level of the WMG Product in any In-Store Promotion or Media Advertising where the Dealer does not seek any contribution from WMG for the cost of said Media Advertising or In-Store Promotion;
- C. Adopt, maintain, enforce or threaten to enforce any policy, practice or plan which makes the receipt of any Cooperative Advertising or Other Promotional Funds contingent upon the price or price level of the WMG Product in any In-Store Promotion or Media Advertising if WMG's contribution exceeds 100% of the Dealer's actual costs of said Media Advertising or In-Store Promotion;
- D. Agree with any Dealer to control or maintain the resale price at which the Dealer may offer for sale or sell any WMG Product;
- E. For a period of five (5) years, announce resale or minimum advertised prices of WMG Product and unilaterally terminate those who fail to comply because of such failure. Notwithstanding the foregoing, nothing herein shall prohibit WMG from announcing suggested list prices for WMG Product.

IV.

Nothing herein shall prohibit WMG from providing Cooperative Advertising or Other Promotional Funds on the

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condition that such funds are passed through in whole or in part to the consumer (hereinafter APass-Through Funds@). WMG shall maintain records that specifically identify by title or collection of titles the amount of Pass-Through Funds provided to each Dealer and the date said amount was provided. Whenever WMG provides Pass-Through Funds to a Dealer, WMG shall specifically notify the Dealer in writing either that these funds are intended to be passed through to the ultimate consumer in whole, or that the Dealer may determine what portion of the funds are to be passed through, provided that some portion of the funds must be passed through to the ultimate consumer. The documents described in this Paragraph IV shall be provided to the Commission upon request.

V.

It is further ordered that for a period of seven (7) years:

- A. WMG shall amend all policy manuals applicable to the distribution of WMG Product to state affirmatively that WMG does not maintain or enforce any plan, practice or policy of the type prohibited in Paragraph II of this Order, and not otherwise permitted by Paragraph IV of this Order.
- B. In each published full catalogue or published full price list in which WMG states suggested list prices or codes indicative of such prices, WMG shall state affirmatively that it does not maintain or enforce any plan, practice or policy of the type prohibited in Paragraph II of this Order, and not otherwise permitted by Paragraph IV of this Order.

The documents described in this Paragraph V shall be provided to the Commission upon request.

VI.

It is further ordered that within 10 days after this Order becomes final, WMG shall mail by first class mail a letter containing the language attached as Exhibit A to:

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- A. All of its directors, officers, distributors, agents and sales representatives in the United States, and
- B. All Dealers to which WEA sells directly and that are engaged in the sale of any WMG Product in or into the United States of America.

VII.

It is further ordered that for a period of seven (7) years WMG shall mail by first class mail a letter containing the language attached as Exhibit A to:

- A. Each new director, officer, distributor, agent, and sales representative of WMG in the United States, and
- B. Each new Dealer to which WEA sells directly which is engaged in the sale of any WMG Product in or into the United States of America, within thirty (30) days of the commencement of such person=s employment or affiliation with WMG or WEA.

VIII.

It is further ordered that annually for five (5) years on the anniversary of the date this Order becomes final, and at such other times as the Commission may by written notice to Time Warner require, Time Warner shall file with the Commission a verified written report setting forth in detail the manner and form in which Time Warner has complied and is complying with this Order.

IX.

It is further ordered that this Order shall terminate on August 30, 2020.

Decision and Order

By the Commission.

EXHIBIT A
[COMPANY LETTERHEAD]

Dear [Recipient]:

WEA announces several important changes in policy. All of these changes will be reflected in the new Policy Manual.

WEA has dropped its Minimum Advertised Price (AMAP@) policy effective _____. Cooperative advertising and other promotional funds will not be conditioned upon the price at which WMG product is advertised or promoted. As many of you know, the Federal Trade Commission has conducted an investigation into WEA=s MAP policies. To end the investigation expeditiously and to avoid disruption to the conduct of its business, WEA has voluntarily agreed, without admitting any violation of the law, to the entry of a Consent Agreement relating to MAP and other related matters.

WEA=s customers can advertise and promote our products at any price they choose. WEA will not withhold cooperative advertising or other promotional funds on the basis of the price at which WMG product is advertised in the media or promoted in your stores. WEA may announce suggested retail prices, but retailers remain free to sell and advertise WMG product at any price they choose.

Concurrence:

William L. Lanning, Esq.
Federal Trade Commission
Bureau of Com

Statement of the Commission

STATEMENT OF CHAIRMAN ROBERT PITOFSKY AND
COMMISSIONERS SHEILA F. ANTHONY, MOZELLE W.
THOMPSON, ORSON SWINDLE, AND THOMAS B. LEARY

The Commission has unanimously found reason to believe that the arrangements entered into by the five largest distributors of prerecorded music violate the antitrust laws in two respects. First, when considered together, the arrangements constitute practices that facilitate horizontal collusion among the distributors, in violation of Section 5 of the Federal Trade Commission Act. Second, when viewed individually, each distributor's arrangement constitutes an unreasonable vertical restraint of trade under the rule of reason. A discussion of these violations is spelled out in our Analysis to Aid Public Comment. See Attached.

The Commission considered carefully whether the anticompetitive vertical restraints should be evaluated under a *per se* rule or a rule of reason. In the past, the Commission has employed the rule of reason to examine cooperative advertising programs that restrict reimbursement for the advertising of discounts, because such programs may be precompetitive or competitively neutral. *Statement of Policy Regarding Price Restrictions in Cooperative Advertising Programs & Rescission*, 6 Trade Reg. Rep. (CCH) & 39,057. The cooperative advertising programs that were the subject of previous Commission actions involved only advertising paid for in whole or in part by the manufacturer, but did not restrain the dealer from selling at a discount or from advertising discounts when the dealer itself paid for the advertisement. See, e.g., *The Advertising Checking Bureau, Inc.*, 109 F.T.C. 146, 147 (1987) (The restraints . . . do not prohibit retailers from selling at discount prices or advertising discounts or sale prices with their own funds).

The Minimum Advertised Pricing (AMAP) policies of the five distributors in this matter go well beyond the cooperative

Statement of the Commission

advertising programs with which the Commission has previously dealt: the distributors' MAP policies prohibited retailers from advertising discounts in all advertising, including advertising paid for entirely by the retailer; the MAP policies applied to in-store advertising, excepting only the smallest price labels affixed to the product; and a single violation of a distributor's MAP policy carried severe financial penalties, resulting in the loss of all MAP funds for all of the retailer's stores for 60 to 90 days (see Paragraph 7 of each Complaint).

Retailers were free to sell at any price, so long as they did not advertise a discounted price. In fact, there was evidence that some retailers on rare occasions did sell product at a discount without advertising the discounted price, instead advertising simply that the product was available at a Guaranteed low price. We are therefore reluctant to declare that compliance with the MAP policies by retailers constituted *per se* unlawful minimum resale price maintenance, because we cannot say that there is sufficient evidence of an agreement by retailers to charge a minimum price. As stated by a majority in *In the Matter of American Cyanamid Co.*, Both the courts and the Commission have judged cooperative advertising cases under the rule of reason, as long as the arrangements do not limit the dealer's right: (1) to discount below the advertised price, and (2) to advertise at any price when the dealer itself pays for the advertisement. 123 F.T.C. 1257, 1265 (1997) (Statement of Chairman Robert Pitofsky and Commissioners Janet D. Steiger and Christine A. Varney).¹

In *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 735-36 (1988), the Supreme Court held that a vertical restraint is not illegal *per se* unless it includes some agreement on

¹ In *American Cyanamid*, the manufacturer conditioned financial payments on its dealers' charging a specified minimum price, which the Commission found to be *per se* unlawful minimum resale price maintenance. By contrast, financial payments under the distributors' MAP policies here were conditioned on the price advertised, not on the price charged.

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price or price levels.@ In our view, *Sharp* requires something more than a showing that an agreement has some influence on price. Restrictions on advertisements that include discounted prices in advertisements funded in whole or in part by the manufacturer are not *per se* illegal, notwithstanding the fact that they are likely to have an influence on resale prices. Indeed, the pervasive practice of publishing suggested retail prices is also likely to have some influence on actual prices, but it is well established that this practice is not *per se* illegal. See, e.g., *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984).

Nonetheless, we conclude that the distributors' MAP policies are unlawful under a rule of reason analysis. The five distributors together account for over 85 percent of the market (see Paragraph 2 of each Complaint), and each has market power in that no music retailer can realistically choose not to carry the music of any of the five major distributors. The MAP policies were adopted by each of the distributors for the purpose of stabilizing retail prices (see Paragraph 10 of each Complaint). The MAP policies achieved their purpose and effectively stabilized retail prices with consequential effects on wholesale prices, ending the price competition that previously existed in the retail marketplace and the resulting pressure on the distributors' margins (*id.*). Compliance with the MAP policies B which was secured through significant financial incentives B effectively eliminated the retailers' ability to communicate discounts to consumers (see Paragraph 8 of each Complaint). Even absent an actual agreement to refrain from discounting, this inability to effectively communicate discounts to consumers meant that retailers had little incentive to actually sell product at a discount.

In the future, the Commission will view with great skepticism cooperative advertising programs that effectively eliminate the ability of dealers to sell product at a discount. The Commission

Statement of the Commission

will, of course, consider *per se* unlawful² any arrangement between a manufacturer and its dealers that includes an explicit or implied agreement on minimum price or price levels,³ and it will henceforth consider unlawful arrangements that have the same practical effect of such an agreement without a detailed market analysis, even if adopted by a manufacturer that lacks substantial market power.

² Commissioners Swindle and Leary have previously stated that the Supreme Court should reassess the applicability of the *per se* rule to the practice when the appropriate case arises. *Nine West Group Inc.*, Dkt. No. C-3937 (Statement of Commissioners Orson Swindle and Thomas B. Leary). However, they agree that, so long as this *per se* rule is the law, summary treatment is appropriate for resale price agreements and other agreements with the same practical effect.

³ In addition, the Commission will continue to consider *per se* unlawful any cooperative advertising program that is part of a resale price maintenance scheme. *Cf. The Magnavox Co.*, 113 F.T.C. 255, 262 (1990) (AOf course, any cooperative advertising program implemented by Magnavox as part of a resale price maintenance scheme would be *per se* unlawful . . . @).

*Analysis to Aid Public Comment***Analysis to Aid Public Comment on the Proposed Consent Order**

The Federal Trade Commission ("Commission") has accepted agreements containing proposed consent orders from the corporate parents of the five largest distributors of prerecorded music in the United States. The five distributors, Sony Music Distribution ("Sony"), Universal Music & Video Distribution ("UNI"), BMG Distribution ("BMG"), Warner-Elektra-Atlantic Corporation ("WEA") and EMI Music Distribution ("EMI"), account for approximately 85% of the industry's \$13.7 billion in domestic sales. The agreements would settle charges by the Commission that these five companies violated Section 5 of the Federal Trade Commission Act by engaging in practices that restricted competition in the domestic market for prerecorded music.

The proposed consent orders have been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this period will become part of the public record. After thirty (30) days, the Commission will review the agreements and the comments received and will decide whether it should withdraw from the agreements or make final the agreements' proposed orders.

The purpose of this analysis is to invite public comment concerning the consent order. This analysis is not intended to constitute an official interpretation of the agreement and order or to modify its terms in any way.

There are five separate complaints and proposed consent orders in this matter, one for each of the distributors, which are virtually identical with the exception of minor variations related to the corporate structure of each respondent.

Analysis to Aid Public Comment

Analysis

The complaints allege that all five distributors have engaged in acts and practices that have unreasonably restrained competition in the market for prerecorded music in the United States through their adoption, implementation and enforcement of Minimum Advertised Price ("MAP") provisions of their Cooperative Advertising Programs.

These five companies, which collectively dominate this market, adopted significantly stricter MAP programs between late 1995 and 1996. Under the new MAP provisions, retailers seeking any cooperative advertising funds were required to observe the distributors' minimum advertised prices in all media advertisements, even in advertisements funded solely by the retailers. Retailers seeking any cooperative funds were also required to adhere to the distributors' minimum advertised prices on all in-store signs and displays, regardless of whether the distributor contributed to their cost.

Failure to adhere to the respondents' MAP provisions for any particular music title would subject the retailer to a suspension of all cooperative advertising funding offered by the distributor for an extended period, typically 60 to 90 days.¹ The severity of these penalties ensured that even the most aggressive retail competitors would stop advertising prices below MAP. The complaints further allege that by defining advertising broadly enough to include all in-store displays and signs, the MAP policies effectively precluded many retailers from communicating prices below MAP to their customers.

The MAP provisions were implemented with the anticompetitive intent to limit retail price competition and to

¹ BMG's policy differed slightly. Under the BMG MAP provisions, the suspension of all cooperative advertising funding required a finding of two MAP violations. However, BMG MAP provisions also established a suspension of up to a year for repeated violations.

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stabilize the retail prices in this industry. Prior to the adoption of these policies, new retail entrants, especially consumer electronic chains, had sparked a retail "price war" that had resulted in significantly lower compact discs prices to consumers and lower margins for retailers. Some retailers, who could not compete with the newcomers, asked the distributors for discounts or for more stringent MAP provisions to take pressure off their margins.

The complaints allege that the distributors were concerned that declining retail prices could cause a reduction in wholesale prices. Through these stricter MAP programs, the distributors hoped to stop retail price competition, take pressure off their own margins, and eventually increase their own prices. The distributors' actions were effective. Retail prices were stabilized by these MAP programs. Thereafter, each distributor raised its wholesale prices.

While some vertical restraints can benefit consumers (known as "efficiencies") by enhancing interbrand competition and expanding market output, plausible efficiency justifications are absent in this case. Beneficial vertical restraints encourage retailers to provide better services to consumers than would have been provided in the absence of the restraint. However, in this case, the distributors' MAP policies provided no benefits to consumers. In particular, the new retailers that charged lower prices to consumers provided services that were as good as, and in some cases, superior to the services provided by the higher priced retailers they were moving to replace. These policies were plainly not motivated by "free-riding" concerns.

The substantial anticompetitive effects of these programs, balanced against the absence of plausible efficiency rationales for them, give us reason to believe that these programs constitute unreasonable vertical restraints in violation of Section 5 of the FTC Act under a rule of reason analysis. Although the Commission has concluded that compliance by retailers with these programs did not constitute per se unlawful minimum resale

Analysis to Aid Public Comment

price maintenance agreements, it should be noted that the MAP provisions implemented here go well beyond typical cooperative advertising programs, where a manufacturer places restraints on the prices its dealers may advertise in advertisements funded in whole or in part by the manufacturer. Such traditional cooperative advertising programs are judged under the rule of reason. *American Cyanamid*, 123 F.T.C. 1257, 1265 (1997); *U.S. Pioneer Electronics Corp.*, 115 F.T.C. 446, 453 (1992); *The Advertising Checking Bureau, Inc.*, 109 F.T.C. 146 (1987).

The market structure in which the distributors' MAP provisions have operated also gives us reason to believe that these programs violate Section 5 of the FTC Act as practices which materially facilitate interdependent conduct. The MAP programs were implemented with an anticompetitive intent and they had significant anticompetitive effects. In addition, there was no plausible business justification for these programs. *E.I. du Pont de Nemours & Co. v. FTC*, 729 F.2d 128 (2d Cir. 1984).

The wholesale market for prerecorded music is characterized by high entry barriers which limit the likelihood of effective new entry. In this industry, the respondents can easily monitor the pricing and policies of their competition.

The history of MAP policies in this industry also indicates a propensity for interdependent behavior among the distributors. All five distributors adopted MAP policies in 1992 and 1993 that generally required adherence to minimum advertised prices in advertisements paid for by the distributors. In 1995 and 1996, all five distributors expanded the restrictions in their MAP programs to require adherence to minimum advertised prices in advertisements regardless of the funding source. In one case, the new MAP provisions were announced four months prior to their effective date. During this four month hiatus, two other distributors adopted similar provisions. By the end of 1996, all five distributors had adopted MAP provisions that were virtually identical. Shortly thereafter, several distributors embarked on high profile enforcement actions against major discounters who

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were discounting prices; these enforcement actions were widely publicized by the trade press.

The Proposed Consent Order

There are five separate consent orders, one for each company.

Part I of the proposed orders establishes definitions. These definitions make clear that the provisions of the order apply to the directors, officers, employees, agents and representatives of the five distributors. This section also makes clear that its provisions apply to cooperative funding efforts regardless of whether the retailer sells prerecorded music in traditional retail stores or over the Internet.

Part II of the orders requires all of the distributors to discontinue their MAP programs in their entirety for a period of seven years. The Commission believes this relief is necessary because some of the challenged MAP programs have been in place for more than four years. Quite simply, it will take several years without the MAP restrictions to restore retail price competition.

Part III of the orders contains several prohibitions to ensure that the distributors are unable to maintain the anticompetitive status quo in some other way. Subsection A prohibits the companies from conditioning the availability of any advertising funds on a retailer's actual selling price. Subsection B prohibits the distributors from restricting the availability of any advertising funds on the basis of an advertisement funded solely by its customers that do not adhere to the minimum advertised price. Subsection C prohibits the distributors from making payments that exceed the retailers' promotional costs to ensure compliance with any MAP program. Subsection D prohibits the distributors from controlling their customers' resale prices. Subsection E prohibits, for five years, the distributors from exercising their

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Colgate rights to unilaterally terminate dealers for failure to comply with any minimum advertised or resale price.

For EMI, BMG, and UNI, Parts IV, V, and VI are various notice provisions requiring the companies to notify their customers and senior management concerning the terms of this order. Part VII establishes that the distributors shall make annual compliance reports concerning their compliance with the terms of this order. Such reports may also be required by the Commission at any time. Part VIII establishes that the order shall terminate in twenty (20) years.

Part IV of the WMG and Sony orders specifically incorporates an exception to the prohibition against RPM that permits distributors to require their dealers to pass-through discounts. The notice and compliance requirements, and term of the order, are the same as for the other three respondents and are found at Parts V, VI, VII and VIII of the orders for WMG and Sony.

Complaint

IN THE MATTER OF

BMG MUSICCONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3973; File No. 9710070
Complaint, August 30, 2000--Decision, August 30, 2000

This consent order addresses BMG Music's practices that restricted competition in the domestic market for prerecorded music. The complaint alleges that BMG Music adopted, implemented, and enforced Minimum Advertised Price ("MAP") provisions in their Cooperative Advertising Programs. By defining advertising broadly enough to include all in-store displays and signs, the MAP policies effectively precluded many retailers from communicating prices below MAP to their customers. The order requires Respondent to discontinue its MAP program for a period of seven years and contains several prohibitions to ensure that Respondent is unable to maintain the anticompetitive status quo in some other way.

Participants

For the Commission: *William L. Lanning, Karin F. Richards, James W. Frost, Geoffrey M. Green, Karen Mills, Jeffrey Goodman, June Casalmir, Kent Cox, Kristin Malmberg, Beverly Dodson, Brynna Connolly, Lorenzo Cellini, Veronica G. Kayne, Michael E. Antalics, John Howell, Daniel P. O'Brien, and Gregory Vistnes.*

For the Respondents: *Robert Bloch, Mayer, Brown & Platt.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended,¹⁵ U.S.C. ' ' 41 et seq., by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that BMG Music has violated the provisions of Section 5 of the Federal Trade Commission Act, ¹⁵