**Analysis to Aid Public Comment**
***In the Matter of Pool Corporation, File No. 101-0115***

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The Federal Trade Commission has accepted for public comment an Agreement Containing Consent Order to Cease and Desist ("Agreement") with Pool Corporation ("PoolCorp"). PoolCorp is the world's largest distributor of products used in the construction, renovation, repair, service and maintenance of residential and commercial swimming pools. The Agreement resolves charges that PoolCorp used exclusionary acts and practices to maintain its monopoly power in the pool product distribution market in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45.

The administrative complaint that accompanies the Agreement ("Complaint") alleges that PoolCorp used its monopoly power in local geographic markets to prevent manufacturers from supplying pool products to new entrants since at least 2003. As a result, PoolCorp foreclosed rival distributors from obtaining pool products – a necessary input to compete – and significantly raised its rivals' costs, thereby lowering output, increasing prices, and diminishing consumer choice.

The Commission anticipates that the competitive issues described in the Complaint will be resolved by accepting the proposed Order, subject to final approval, contained in the Agreement. The Agreement has been placed on the public record for 30 days for receipt of comments from interested members of the public. Comments received during this period will become part of the public record. After 30 days, the Commission will again review the Agreement and comments received, and will decide whether it should withdraw from the Agreement or make final the Order contained in the Agreement.

The purpose of this Analysis to Aid Public Comment is to invite and facilitate public comment concerning the proposed Order. It is not intended to constitute an official interpretation of the Agreement and proposed Order or in any way to modify their terms.

The Agreement is for settlement purposes only and does not constitute an admission by PoolCorp that the law has been violated as alleged in the Complaint or that the facts alleged in the Complaint, other than jurisdictional facts, are true.

## I. The Complaint

The Complaint makes the following allegations.

### A. Industry Background

This case involves wholesale distribution in the swimming pool industry. There are over nine million residential pools in the United States, and over 250,000 commercial pools operated by hotels, country clubs, apartment buildings, municipalities, and others. In 2010, the distribution of pool products was an estimated $3 billion industry in the United States.

Manufacturers use distributors to sell the products used to build, repair, service and maintain residential and commercial swimming pools ("pool products"). Pool products include, among others, pumps, filters, heaters, covers, cleaners, diving boards, steps, rails, pool liners, pool walls, and the parts necessary to maintain pool equipment. Distributors purchase pool products from manufacturers, warehouse them, and then resell the products to pool retail stores, pool service companies and pool builders (collectively, "pool dealers" or "dealers"). Dealers, in turn, sell the pool products to the ultimate consumer: owners of residential and commercial swimming pools.

The swimming pool industry is very fragmented and wholesale distributors make it more efficient for manufacturers and dealers to sell their products. Distributors purchase most, if not all, brands of pool products that are produced by manufacturers so that they can provide convenient one-stop shopping for their dealer customers. Distributors also extend credit and provide quick delivery of pool products to thousands of dealers. The vast majority of dealers are mom-and-pop operations that are too small to buy directly from manufacturers; for these dealers, distributors are their only source of pool products. Distributors also allow manufacturers to operate their factories year-round by purchasing large quantities of pool products throughout the year, even though the pool industry is seasonal.

In general, manufacturers are willing to sell their products to any credit-worthy distributor that has a physical warehouse and personnel with knowledge of the pool industry. Manufacturers typically prefer to have two or more distributors selling their products in a local geographic market in order to ensure that the distributors compete and give competitive service and prices to their dealer customers.

To compete effectively as a distributor, a firm must be able to buy pool products directly from manufacturers. There are no cost-effective alternatives. While there are over 100 manufacturers of pool products, there are only three full-line manufacturers that produce almost all of the products used to operate or repair swimming pools: Pentair Water Pool & Spa; Zodiac Pool Systems, Inc.; and Hayward Pool Products. Collectively, these manufacturers represent more than 50 percent of all pool product sales. To be successful, a distributor must sell the products of at least one of these manufacturers. As recognized by PoolCorp, a positive relationship with these and other manufacturers is "critical" to the success of a distributor.

### B. PoolCorp's Monopoly Power

The relevant market is no broader than the wholesale distribution of pool products in the United States and numerous local geographic markets. With the exception of large national retail chains that purchase pool products for their retail centers located throughout the United States, competition among distributors for sales to dealers occurs locally. PoolCorp has monopoly power in numerous local markets, as evidenced by a persistently high market share of 80 percent or more for the past five years. PoolCorp's conduct of foreclosing new distributor entrants from obtaining pool products directly from manufacturers represents a significant barrier to entry.

### C. PoolCorp's Conduct

Beginning in 2003 and continuing to today, PoolCorp has implemented an exclusionary policy that effectively impeded entry by new distributors by preventing them from being able to purchase pool products directly from manufacturers. Specifically, when a new distributor attempted to enter a local geographic market, PoolCorp threatened manufacturers that it would not deal with them if they also supplied the new entrant. PoolCorp threatened to terminate the purchase and sale of the manufacturer's pool products for all 200+ PoolCorp distribution centers located throughout the United States. PoolCorp's policy did not exclude existing rivals from obtaining pool products from manufacturers.

PoolCorp's threat was significant. The loss of sales to PoolCorp could be "catastrophic" to the financial viability of even major manufacturers. No other distributor could replace the large volume of potential lost sales to PoolCorp, particularly in markets where PoolCorp is the only distributor. New entrants could not offer any economic incentive to manufacturers that would offset the risks imposed by PoolCorp's threats.

After receiving these threats, manufacturers, including the three "must-have" manufacturers, refused to sell pool products to the new distributors and canceled any pre-existing orders. PoolCorp thus effectively foreclosed new distributors from obtaining pool products from manufacturers that represented more than 70 percent of all pool product sales.

In some cases, the new distributors were able to purchase pool products from other distributors. This counterstrategy, however, did not mitigate the effects of PoolCorp's conduct. As a general rule, distributors do not sell pool products to other distributors. Even when possible, this alternative is not a viable long-term strategy because it substantially increases the entrant's costs and lessens its quality of service. For example, buying pool products from a distributor forces the new distributor entrant to pay transportation costs from the distributor's location rather than receiving free shipping under manufacturer programs. The purchases are also at a marked-up price and do not qualify for key manufacturer year-end rebates.

By effectively increasing its rivals' costs, PoolCorp's exclusionary policy prevented the new distributor entrants from being able to compete aggressively on price. Additionally, without full control of their inventory, the entrants' ability to provide quality service to their dealer customers was diminished. PoolCorp specifically targeted new entrants, rather than established rivals, because the new distributors represented a significant competitive threat due to their likelihood to compete aggressively on price in order to earn new business. PoolCorp's conduct, therefore, had the purpose and effect of maintaining and enhancing PoolCorp's monopoly power in numerous local markets where its dominance would otherwise be threatened by new entrants. PoolCorp's exclusionary policy, therefore, has likely resulted in higher prices and reduced output.

There are no procompetitive efficiencies that justify PoolCorp's conduct.

## II. Legal Analysis

The offense of monopolization under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market; and (2) the willful acquisition, enhancement or maintenance of that power through exclusionary conduct.[1] A monopolist's refusal to deal with a firm if that firm also deals with a rival has long been recognized as exclusionary conduct. Exclusionary practices violate Section 2 of the Sherman Act when the challenged conduct significantly impairs the ability of rivals to compete effectively with the respondent and thus to constrain its exercise of monopoly power.[2]

The factual allegations in the complaint regarding market structure support a finding of monopoly power and competitive harm. PoolCorp's "all or nothing" threats acted as a powerful deterrent to manufacturers against dealing with new distributor entrants by jeopardizing a large and irreplaceable percentage of the manufacturer's sales. PoolCorp's conduct effectively foreclosed new entrants from manufacturers representing more than 70 percent of pool product sales. New entrants were unable to provide any economic incentive to manufacturers that could offset the risk posed by PoolCorp's threats. Raising rivals' costs by restraining their supply of inputs can be a "particularly effective method of anticompetitive exclusion."[3]

Additionally, the work-around strategy employed by some new entrants of purchasing pool products from other distributors significantly raised their costs and reduced their ability to provide quality service. PoolCorp's exclusionary policy therefore prevented these firms from providing a meaningful constraint on PoolCorp's monopoly prices.

Notably, PoolCorp's conduct targeted new entry and did not exclude existing rivals. The test for exclusionary conduct, however, is not total foreclosure, but "whether the challenged practices

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[1] *Verizon Commun's. v. Law Offices of Curtis V. Trinko LLP*., 540 U.S. 398, 407 (2004); *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966).

[2] *E.g., Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 605 & n.32 (1985) (exclusionary conduct "tends to impair the opportunities of rivals" but "either does not further competition on the merits or does so in an unnecessarily restrictive way") (citations omitted); *see also Lorain Journal Co. v. United States*, 342 U.S. 143, 151-54 (1951) (condemning newspaper's refusal to deal with customers that also advertised on rival radio station because it harmed the radio station's ability to compete); *United States v. Microsoft*, 253 F.3d 34, 68-71 (D.C. Cir. 2001) (condemning exclusive agreements that prevented rivals from "pos[ing] a real threat to Microsoft's monopoly"); *United States v. Dentsply*, 399 F.3d 181, 191 (3d Cir. 2005) (condemning policy that kept competitors below "the critical level necessary for any rival to pose a real threat to Dentsply's market share").

[3] *See* Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over* Price, 96 YALE L.J. 209, 224 (1986) (explaining that this method of exclusion allows a dominant firm to use its vertical relationships to create additional horizontal market power); *see also Dentsply*, 399 F.3d at 195 (holding "all or nothing" ultimatum exclusionary when it "created a strong economic incentive for dealers to reject competing lines in favor of Dentsply's teeth."); *In re Transitions Optical, Inc.*, 75 Fed. Reg. 10799 (Mar. 2010) (proposed complaint and analysis to aid public comment).

bar a substantial number of rivals or severely restrict the market's ambit."[4] New entrants may have a more disruptive impact on the market than established firms because they may have an increased incentive to compete aggressively on price in order to win business. Conduct that artificially raises entry barriers by increasing the scale, cost or time of entry harms consumers by providing a greater opportunity for monopoly pricing.[5]

A monopolist may rebut a *prima facie* showing of competitive harm by showing that the challenged conduct is reasonably necessary to achieve a procompetitive benefit. Any efficiency benefit, if proven, must be balanced against the harm caused by the challenged conduct.

There are no procompetitive efficiencies that justify PoolCorp's conduct. In some cases, for example, exclusive arrangements with suppliers could be necessary to prevent free-riding or to secure adequate supply. Here, however, PoolCorp did not offer any services upon which a new entrant could free-ride. Further, the pool industry is not subject to product shortfalls that could justify exclusive arrangements with suppliers. In short, PoolCorp's practice of foreclosing new entrants from supply did not help PoolCorp compete on the merits by improving its efficiency, quality or prices.

## III. The Order

The proposed Consent Order remedies PoolCorp's anticompetitive conduct. Paragraph II of the Order addresses the core of PoolCorp's conduct. Specifically, Paragraph II of the proposed Consent Order prohibits PoolCorp from:

A. Conditioning the sale or purchase of pool products, or membership in PoolCorp's preferred vendor programs, on the intended or actual sale of pool products by a manufacturer to any distributor other than PoolCorp;

B. Pressuring, urging or otherwise coercing manufacturers to refrain from selling, or to limit their sales, to any distributors other than PoolCorp; and

C. Discriminating or retaliating against a manufacturer for selling, or intending to sell, pool products to any distributor other than PoolCorp.

The definition of "distributor" includes any entity that buys pool products directly from manufacturers and resells those products to dealers or others. The Order explicitly allows

[4] *LePage's, Inc. v. 3M*, 324 F.3d 141, 159 (3d Cir. 2003); *see also Dentsply*, 399 F.3d at 190 (explaining that "it is not necessary that all competition be removed from the market").

[5] Herbert Hovenkamp, ANTITRUST LAW ¶ 1802c, at 64 (2d ed. 2002) ("Consumer injury results from the delay that the dominant firm imposes on the smaller rival's growth"); *see also Microsoft*, 253 F.3d at 79 ("it would be inimical to the purpose of the Sherman Act to allow monopolists free reign to squash nascent, albeit unproven, competitors at will"); *LePage's*, 324 F.3d at 159 ("When a monopolist's actions are designed to prevent one or more new or potential competitors from gaining a foothold in the market by exclusionary, *i.e.*, predatory, conduct, its success in that goal is not only injurious to the potential competitor but also to competition in general.").

PoolCorp to enter into exclusive agreements with manufacturers to purchase private-label pool products.

Paragraph III of the Proposed Order requires PoolCorp to implement an antitrust compliance program. Paragraph IV- VI impose reporting and other compliance requirements. The Order will expire in 20 years.

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