

Harassed By The FTC

In concluding a costly, two-year investigation into price fixing and anti-competitive practices in the music industry, the Federal Trade Commission triumphantly announced that “The Commission order will protect consumers from paying higher prices by ensuring that NAMM does not facilitate anticompetitive coordination.” If we had been allowed to write the press release, we would have selected slightly different wording; to wit: “After tormenting a small and hard-pressed industry with a costly and pointless fishing expedition, FTC officials saved face by threatening endless legal harassment to coerce NAMM into saying ‘even though we didn’t do anything wrong, we won’t do it again.’” We would have added, “FTC staffers received notes of gratitude from law firms in seven states that took in an estimated \$12.0 million in fees representing music industry firms during the investigation.”

If you think we’re being heavy-handed in our indictment of the FTC, consider the trajectory of their investigation and its ultimate conclusion. On March 12, 2007, the agency sent a 17-page subpoena demanding a decade’s worth of sales, marketing, and production records from Yamaha, Fender, Hoshino, Gibson, Zildjian, Martin, Korg, Kaman, TEAC, Roland, Guitar Center, NAMM, GAMMA, IAEKM, NABIM, NASMD, and the Percussion Marketing Council. Although the Commission didn’t accuse anyone of wrongdoing, it was “concerned” that the industry’s minimum advertised price agreements might violate Section 5 of the FTC act, which prohibits “unfair or deceptive practices in or affecting commerce.”

Based on conversations with subpoenaed suppliers and their law firms, we estimate that the legal costs of answering questions like, “what is the precise advertising and promotional expenditure for every product sold since 1999?” topped \$12 million. To put that number in perspective, it’s equal to about 6% of the industry’s total advertising and promotional budget.

Ironically, as the FTC was investigating whether the industry was harming consumers with higher prices, the average selling prices of all categories of music and audio gear were plummeting. (If the industry was trying to fix prices, it apparently wasn’t doing a very good job.) Between 1999 and 2007, guitar prices dropped 33%, hard-disk recorder prices dropped 40%, and guitar amps were off 45%. Amidst these declines, the lament of retailers has been, “unit sales volume is not expanding fast enough to offset drops in unit prices.” So at a time when prices were falling, what credible evidence of collusion did the FTC have to justify an investigation? The only people who know the answer are FTC staffers, and they’re not talking.

FTC sources and evidence are all shrouded in the dense fog of bureaucracy, beyond the scrutiny of a collection of accused music companies. Was the investigation triggered by a complaint from some drunk who was fired for embezzling and wanted to extract revenge from a former employer? Or did it come about after an FTC staffer had a bad experience with one of the accused companies? One guess is as good as another, and that’s the problem. Unlike a criminal or civil action, where the credibility of both the accused and accuser are on trial, in an



FTC case, the Commission’s accusations are above criticism, unless you feel like spending millions contesting them in front of a judge.

The net result is that merely being accused by the FTC is a punishment in itself. In the case of our industry, companies concluded that battling a government agency with unlimited time and resources was a losing battle, and that it was better to limit damages with a hasty retreat.

Comments from a few lawyers who participated in the investigation paint a picture of incompetence at the FTC that rises to the level of slapstick. After securing a few terabytes worth of sales data, FTC staffers became so bogged down in product minutiae that any thoughts of proving collusion vanished. Unlike their previous action against the CD retailers and manufacturers, whose new releases carry the same selling price, it’s hard to find comparables in the music industry. If a Fender American Deluxe Stratocaster has a street price of around \$1,600, at what price would a Les Paul Standard have to sell to provide evidence of collusion? The FTC investigation was further undermined by a haphazard selection of targets. Martin Guitar was subpoenaed, but its nearest competitor, Taylor, was not. Zildjian was subpoenaed, but no other cymbal makers were. We suppose only a genius from Washington could detect unacceptable market behavior by comparing the pricing of cymbals and synthesizers.

The FTC likes to say that it only levies fines on corporations, not consumers. But the reality is, corporations don’t pay fines, people do, and the de facto \$12 million fine the FTC levied on our industry came directly out of the pockets of all of us in terms of reduced promotional expenditures, smaller year-end bonuses, lowered R&D budgets, and most importantly squandered time complying with exhaustive information requests.

Although the FTC has officially closed the book on its investigation, we will be reminded of this fishing trip for years to come. A key part of the settlement entails that from now until eternity, at every NAMM sponsored gathering, someone will have to waste two minutes reading a bit of cumbersome “legalese” that can be summarized as follows: “Price fixing is bad. Don’t do it. If you see anyone doing it, quickly leave the room.” Oh, and NAMM will also have to hire a special attorney to report to the FTC in perpetuity that the critically important statement is being read. This may count as one of the 3.5 million jobs the current administration is promising to create.

And some people wonder why the statement “I’m from the government and I’m here to help” is such an effective punchline.

Brian T. Majeski
Editor

Email: brian@musictrades.com