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**WISCONSIN'S
MINIMUM MARKUP
LAW:
*GOVERNMENT-MANDATED PAIN AT
THE PUMP***

By Christian Schneider
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EXECUTIVE SUMMARY

During the hot summer months, many motorists are looking to the government to alleviate the distress wrought by high gas prices. Yet, in many cases, governments themselves are contributing to the pain at the pump.

Wisconsin is currently one of 18 states which have "below cost" laws that apply to motor fuel. Wisconsin's "minimum markup" law generally requires a markup of 9.18% on gas sold in the state, to prevent businesses from undercutting the prices of their competitors. Yet the law actually prevents consumers from getting a good deal on gas.

This report finds the following:

- Wisconsin's minimum markup law adds \$990 million to the annual price paid by consumers, between \$267 and \$278 million of which is beyond what a normal profit margin would yield.
- Wisconsin motorists currently pay 30.2 cents per gallon as a result of the minimum markup law. As a result, minimum markup has almost eclipsed the state's 32.9-cent auto fuel tax, which is currently 9th highest in the nation.
- As the wholesale price of gas grows, so does the amount per gallon motorists have to pay as a result of minimum markup. In January of 1998, when the wholesale price of gas was 64 cents per gallon, the minimum markup stood at 5.9 cents per gallon. In July of 2008, the wholesale price of gas stands at \$3.29 per gallon, with the per-gallon minimum markup amount at 30.2 cents - an increase of 400% in ten years.
- In the past year, the amount the minimum markup law adds to a gallon of gas has increased 44% - from 21 cents per gallon in July of 2007 to 30.2 cents per gallon in June of 2008.

The report recommends the Legislature and Governor repeal the minimum markup law as applied to motor fuel entirely. At a minimum, the Legislature should act to cap the per-gallon markup at 21 cents per gallon, where it stood twelve months ago.

INTRODUCTION

In the summer of 2008, politicians are scrambling to cobble together plans to hold gas prices down. Tax the oil companies more, some say. Others propose more domestic drilling. Yet despite their disparate solutions, they all recognize that people are fed up with paying over \$4.00 a gallon for gas.

But what if it is actually the government keeping gas prices high? What if Wisconsin state government had a law on the books that legally prevented customers from getting a good deal on motor fuel? In fact, that is exactly what Wisconsin's minimum markup law accomplishes.

In 1939, Wisconsin passed the minimum markup law - or as it formally known, the Unfair Sales Act - which purported to help keep small businesses afloat during the Great Depression. The Act required retailers to mark up their products a certain percentage over their wholesale price. In theory, this was supposed to keep large retailers from undercutting the prices of smaller "mom and pop" stores, which could drive the smaller stores out of business (commonly referred to as "predatory pricing.")

In 2003, the U.S. Federal Trade Commission (FTC) analyzed the scholarship on "predatory pricing," concluding:

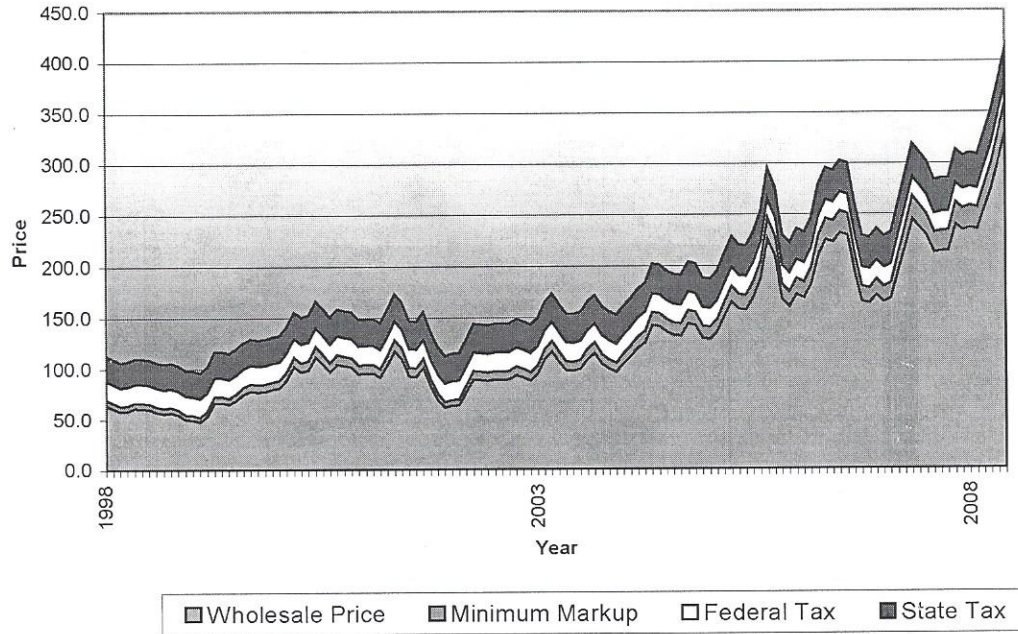
"Economic studies, legal studies, and court decisions indicate that below-cost pricing that leads to monopoly occurs infrequently. Below-cost sales of motor fuel that lead to monopoly are especially unlikely. For these reasons, we believe Wisconsin's Unfair Sales Act likely harms consumers and restricts competition. Moreover, at best, the Act is unnecessary because the federal antitrust laws already protect against predatory pricing."¹

In the 1980's, many of the Unfair Sales Act's provisions were repealed, such as the application of the minimum markup provision to groceries. Yet minimum markup still applies to auto fuel in Wisconsin. According to state law, gas retailers are required to mark up the price of gasoline by at least 6% over the wholesale rate, or 9.18 from the posted terminal (or "rack") rate. (For a full explanation of the law, see Appendix A.)

There are several reasons the Unfair Sales Act causes problems when the wholesale cost of gas escalates. Naturally, with minimum markup applied as a percentage standard, the markup per gallon of gas increases as the cost of that gallon increases. Chart 1 demonstrates the different components that make up the price of gas, including the wholesale price, federal taxes, state taxes, and the minimum markup:

Chart 1

Cost of Fuel by Source, 1998-2008



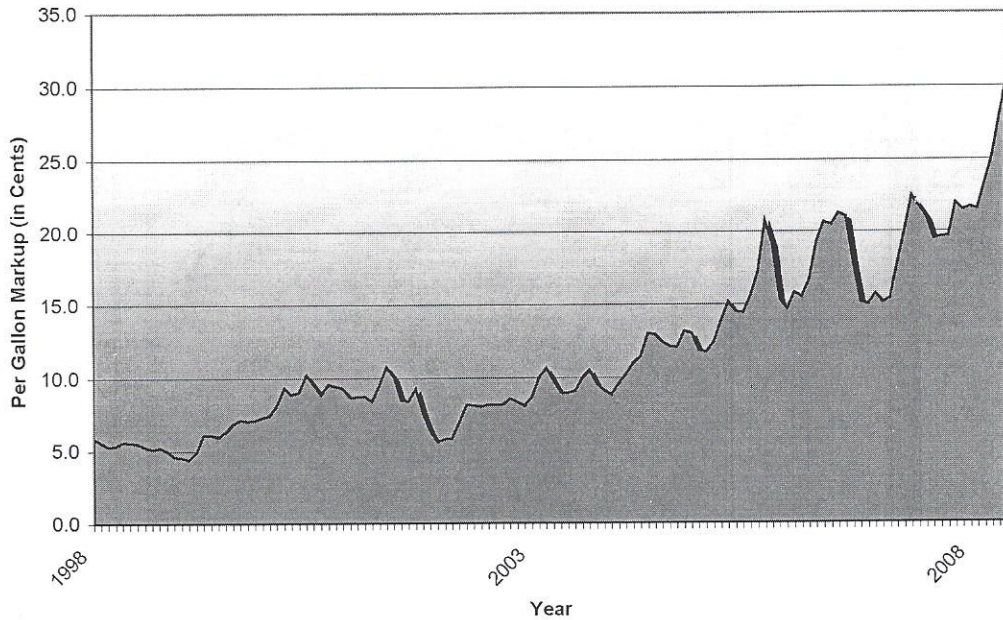
Source: U.S. Energy Information Administration

As can be seen in the chart, minimum markup was a small sliver of the cost of gas when the wholesale price was cheap, and grew as the wholesale price increased. In January of 1998, the wholesale cost of gas was 64.1 cents per gallon, resulting in a markup of 5.9 cents per gallon. Just a decade later, the wholesale cost of gas has risen to \$3.29 per gallon, and the per-gallon markup has quintupled to 30.2 cents per gallon. As a result, the per-gallon markup on gas (30.2 cents) almost now equals the state's per-gallon gas tax (32.9 cents).

Chart 2 demonstrates the growth in the per-gallon minimum markup over the past decade. Of course, given that it is a percentage of the wholesale price, it mirrors the fluctuation in the wholesale price of gas demonstrated in Chart 1.

Chart 2

Markup Per Gallon (in Cents)



Source: U.S. Energy Information Administration

For most other commodities sold in Wisconsin, their markup depends on the business model of the retailer. Businesses can accept either a higher or lower markup, depending on competitive circumstances. Yet the markup on auto fuel in Wisconsin doesn't have anything to do with business models or competition. Rather, the markup consumers pay is determined by the complex dynamics of oil pricing. As the price of wholesale gas goes up, so does the markup for local gas stations, regardless of the cost of doing business.

When that markup is applied to the billions of gallons of gas purchased in Wisconsin, it shows just how much it costs Wisconsin consumers. According to the Wisconsin Department of Transportation, nearly 3.3 billion gallons of auto fuel were purchased in Wisconsin in calendar year 2007. When those gallons are multiplied by 30.2 cents per gallon, the Wisconsin minimum markup provision would increase the cost of gas to consumers by over \$990 million per year at current prices.

It is estimated that the Unfair Sales Act costs Wisconsin drivers between \$267 million and \$278 million per year beyond what they would be paying without the minimum markup law.

THE HISTORY OF MINIMUM MARKUP IN WISCONSIN

The Wisconsin Unfair Sales Act was enacted on June 3, 1939. According to the original drafting file for the law, it was based on the Model State Unfair Sales Act, prepared by the National Food and Grocery Committee. This committee was comprised of representatives of the leading associations in the retail, wholesale, and manufacturing branches of the food and grocery trade.²

Through its history, the Unfair Sales Act underwent several minor legislative changes (1941, 1947, 1949, 1965, 1973), but none changed the central theme of the law until 1986, when groceries were removed from the list of goods to which the law applied. In the mid-1980s, some grocers began to turn against the law, as they felt it was unevenly enforced. Many believed since enforcement was spotty, those who actually adhered to the law were placed at a competitive disadvantage. In 1987, Madison grocer Fred Lange told the Associated Press that due to confusion surrounding the minimum markup law, he wasn't even sure if he could offer a "double coupon" promotion, as many of his competitors were.³

Several statewide interest groups agreed. "In these days of budgetary problems, the state Department of Agriculture, Trade and Consumer Protection, the state Justice Department and local district attorneys have more important things to do than see what people are charging for Twinkies," Wisconsin Merchants Federation president Chris Tackett told the Capital Times in January of 1986.

Efforts to completely repeal the minimum markup law have been numerous, and usually bipartisan. In the early 1980s, Republican State Senator (and future Governor) Scott McCallum and Democratic State Senator (and future Milwaukee Mayor) John Norquist both supported repeal of the minimum markup law. Democratic Attorney General Bronson LaFollette endorsed a full repeal, deeming it a "relic of the past," that required consumers to pay higher prices for goods.

After the repeal of minimum markup on groceries, lawmakers continued to work in bipartisan fashion to push for elimination of the law as applied to motor fuel. While Republican Speaker of the Assembly Scott Jensen and Democratic Minority Leader Shirley Krug were political rivals, they joined forces in 1995 to propose a full repeal. They continued their partnership in subsequent sessions, re-introducing their bill several more times over the next decade. In 2000, Krug was prescient when she accused elected officials of "political hypocrisy" surrounding the law. "I don't buy the rationale for running around Washington pointing fingers and filing lawsuits when we could tackle part of the problem at home,"⁴ she said.

In fact, 2000 was a landmark year with regard to the current debate over gas prices. In 2000, the price per gallon of fuel crept over the \$2.00 mark for the first time. In a poll conducted by the Wisconsin Policy Research Institute, more Wisconsin residents listed gasoline prices as their number one priority for state government than any other issue. 25% of respondents listed gas prices as their top issue, outpolling taxes (17%), crime

(9%), and education (8%.) This was especially astonishing given the fact that it was the first year gasoline prices even registered as an issue at all in the annual poll's results.⁵

As a result of public displeasure over high gas prices, a provision to exclude auto fuel from the Unfair Sales Act was included in the Senate version of the 2001-03 biennial budget. The provision was removed in conference committee before final passage of the budget on July 26th of 2001. Some groups claim it was removed due to heavy campaign finance contributions by interests that support the law (primarily convenience stores and gas stations), saying these groups outspent opponents of the law 4 to 1 in campaign contributions.⁶ (Incidentally, this may be the only time you see Wal-Mart, which supports repeal, portrayed as a victim.)

The most recent serious attempt to repeal the minimum markup law on gasoline occurred in 2006, when a bill (2005 SB 215) authored by Republican State Senator Dave Zien made it to the floor of the Wisconsin Senate. The bill was effectively killed by sending it back to committee for the remainder of the session, which ended a week later. The vote to thwart the bill was bipartisan, with 12 Democrats and 7 Republicans voting to send it back to committee, thereby ending its chance of passage. Prior to that vote, proponents of minimum markup repeal appeared as though they had momentum, considering Democratic Governor Jim Doyle's expressed support for eliminating the law on gasoline. In fact, in 2006 Governor Doyle directed his administration to stop enforcing the minimum markup law on ethanol-based fuel, hoping to spur sales of the biofuel.⁷

Lobbying on the 2006 effort to repeal the Unfair Sales Act on gas broke down primarily into two camps: those who buy a lot of gas (for) and those who sell a lot of gas (against.) Registering with the Wisconsin ethics board in favor of repeal were groups like AAA Wisconsin, the Wisconsin Counties Association, Wal-Mart, and a front group calling itself "Lower Gas Prices - Now!" Registering against the bill were the Wisconsin Petroleum Marketers & Convenience Store Association, Kwik Trip, the Wisconsin Independent Business Association, the Wisconsin Grocers Association, The Wisconsin Farm Bureau, the Wisconsin Tavern League, and the Wisconsin Alliance of Cities. Remaining neutral in the fight were the Transportation Builders Association, the Wisconsin Merchants Federation, the American Petroleum Institute.

Despite widespread legislative support for repealing minimum markup on gasoline, the law's supporters have always been able to thwart legislative attempts to do so. They have argued effectively that repealing minimum markup would harm small gas stations and eventually cause gas prices to rise more quickly when competition is eliminated. As a result, the law has remained in place virtually unchanged, despite skyrocketing gas prices.

The Wisconsin law has been challenged several times in various courts. In 1951, the law was held to be constitutional by the Wisconsin Supreme Court in *State v. Ross* [259 Wis. 379 (1951)], then upheld again in 1967. In October of 2007, the law was declared unconstitutional by U.S. Eastern District of Wisconsin judge William Callahan, who determined that the law was not "actively supervised" by the state, and therefore

invalid [*Lotus Bus. Group LLC v. Flying J Inc.*, No. 07-CV-0144 (E.D. Wis. 2007)] Callahan's decision echoed the complaints of Wisconsin grocers during the 1980s – that the law is too sporadically enforced, and penalties are too uneven. However, since the lawsuit was filed between two private companies and the state didn't enjoin enforcement of the law, minimum markup will continue to be enforced, despite Callahan's ruling. At the very most, this decision could be used as precedent in a future case to invalidate the minimum markup law altogether.

ARGUMENTS FOR AND AGAINST MINIMUM MARKUP

With efforts to repeal the Unfair Sales Act underway since the law took effect 69 years ago, the arguments for and against the law are fairly familiar.

ARGUMENTS FOR:

Those that support the law make the following points:

- The Unfair Sales Act prevents large corporations with substantial financial resources from offering gas as a "loss leader," whereby gas is sold below its wholesale price to harm smaller competition.
- Once small gas stations are driven out of business, the large companies will be able to raise gas prices above what consumers were paying before, as there would be less competition in the market.
- Some gas station owners claim the statutory markup doesn't even guarantee their business makes a profit.

Minimum markup supporters still use a 2001 study funded by the Petroleum Marketers Association of Wisconsin as evidence the law is having its intended effect.⁸ According to the study, conducted by University of Wisconsin-Whitewater professors James Peltier, Ph.D. and Mark Skidmore, Ph.D., Minnesota's gas prices increased by 1.91 cents over the price that Wisconsin consumers paid following Minnesota's repeal of its sales-below-cost law. Their study claims the markup Minnesota consumers paid relative to Wisconsin consumers increased by 1.33 percent after Minnesota's version of minimum markup was repealed.⁹ (Minnesota has since re-enacted their unfair sales act, requiring a markup of 6 percent.)

The second portion of the Peltier/Skidmore report criticizes a study issued in 1999 by the Wisconsin Policy Research Institute, entitled "Pumping Up Gas Prices in Wisconsin: The Effects of the Unfair Sales Act on Retail Gasoline Prices in Wisconsin." The report, written by J. Isaac Brannon, then of the University of Wisconsin-Oshkosh, and Frank Kelly, a senior tax analyst with the Indiana State Board of Tax Commissioners, argued that Wisconsin's Unfair Sales Act added between 2 and 3 cents per gallon when compared with Minnesota, which didn't have a minimum markup provision at the time.¹⁰ Brannon and Kelly's calculations claimed repealing Wisconsin's Unfair Sales Act on gas could save consumers up to \$50 million per year. The Petroleum Marketers

called the Brannon/Kelly report “bad science,” and Peltier and Skidmore themselves said the Brannon/Kelly \$50 million claim “is not only wrong, it is misleading and irresponsible in terms of the actual benefits such laws provide consumers.”¹¹

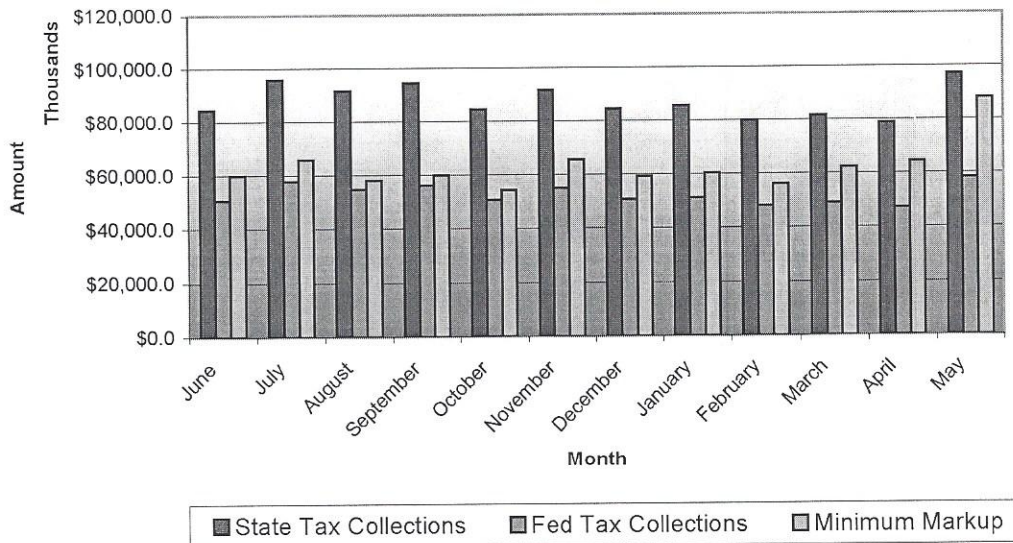
ARGUMENTS AGAINST

Those that oppose government-mandated markups point out that such laws pull off the difficult trick of being both pro-business and anti-competition. Minimum markup laws certainly benefit certain select businesses (gasoline retailers) by guaranteeing profits. Furthermore, these per-gallon profits rise as the wholesale cost of gas rises – thus, the markup doesn’t have any relationship to the actual cost of doing business, as it would in the free market.

Chart 3 demonstrates how the cost of minimum markup to consumers increases as gas prices rise. The chart details state and federal tax receipts for the past year, compared with the total markup for gas:

Chart 3

State Tax, Federal Tax, and Minimum Markup Amounts, June 2007-May 2008 (In Thousands)



Source: Wisconsin Department of Revenue

In June of 2007, with the wholesale price gas at \$2.37 per gallon, minimum markup per gallon stood at 21.8 cents per gallon. By May of 2008, with the wholesale price of gas increasing to \$3.02 per gallon, minimum markup had jumped to 28 cents per gallon – an increase of 28% in one year. (In June of 2008, the minimum markup per-gallon amount increased to 30.2 cents, the figure most commonly cited in this report.) As can be seen in the above chart, the total minimum markup Wisconsin consumers were paying in May of 2008 had almost caught up to the amount the state was collecting in gas taxes.

Between March and May of this year, the increase in the minimum markup per gallon amount cost consumers \$33.6 million.

The reason gas stations fight so vigorously to retain the law is self-evident: it protects them from having to offer competitive prices in the marketplace and guarantees profits, especially when oil prices climb. While minimum markup proponents warn that predatory pricing will eventually lead to price collusion among large gas retailers, the law skips the “eventually” part and essentially mandates anti-competitive collusion. Price collusion is illegal, yet the Unfair Sales Act mandates it, in an effort to maybe *one day prevent it*.

Minimum markup proponents are fond of pointing out that Minnesota reinstated their mandatory markup law in 2001, after having repealed it in 1984. Yet the Minnesota Legislature voted to reinstate the law not because of any actual effects of gas price competition, but because of *perceived* threats brought on by the advent of Wal-Mart entering the gasoline business.¹² When word hit Minnesota that giant retailer Wal-Mart would be teaming with Murphy Oil to offer gas at their stores, the same arguments we now hear in Wisconsin spread in Minnesota like wildfire. The Legislature moved quickly to add a minimum gasoline markup of 6 percent (8 cents per gallon at the time), in order to prevent Wal-Mart from supposedly driving small gas stations out of business – a phenomenon that they had no evidence would occur. And as a result, Minnesota consumers are now “protected” from paying lower gas prices.

What Minnesota lawmakers were reacting to was a desire to protect “mom and pop” businesses from the effects of predatory pricing. As expressed by J. Isaac Brannon, predatory pricing is “a quaint idea that no economist has taken seriously for 20 years.”¹³ The underlying theory of predatory pricing is that one large business will undercut the prices of all their competitors, driving them all out of business. The large business, then holding a monopoly, would raise prices to above what consumers were paying before.

There are several problems with this scenario. First, after consumers initially benefited from low prices, the theory assumes the remaining business would be able to realize monopolistic profits. Yet there would be nothing to keep new businesses from starting up in an effort to offer competition to the monopoly once prices escalated. The big business would actually have to be able to prohibit new entries into the market to prevent competition. Furthermore, the idea that one business could drive all others to fold up shop is somewhat far-fetched.

In fact, as pointed out by Baumol, Panzer, and Willig in 1982, it may not even be necessary for new businesses to crop up to provide competition. The *mere threat* of yet-unformed businesses popping up to provide competition is likely enough to hold prices down, in the event a dominant business gains a large market share.¹⁴

Secondly, the law purports to protect “mom and pop” gas stations from undue competition. There are undoubtedly fewer such businesses today. In fact, the demise of the small family station has occurred in spite of minimum markup.

In many cases, smaller gas stations have been driven out of business due to excessive environmental regulations imposed by various levels of government. According to Brannon and Kelly:

“Beginning in 1988, the federal government began imposing strict environmental regulations on gas stations to minimize environmental damage from leaking gas tanks, and the costs of adhering to these regulations drove many smaller, less efficient stations out of business. New double-hulled fiberglass tanks, elaborate spill-catch systems, and systems that prevent pipes from freezing have all become required in the past ten years. The result is that government essentially weeded out the smaller stations that did not have the cash flow capable of supporting such a large fixed investment, and any stations currently selling gas should have no problem meeting environmental standards for some time.”¹⁵

Brannon reports that a past president of the Wisconsin Petroleum Council once told him that minimum markup should be retained simply to pay back small gas retailers for the cost of excessive environmental regulations. “If the government was going to impose costly restrictions on stations, many of which actually did little to improve the environment, then the least it could do is help stations make a few more cents per gallon with the Unfair Sales Act,” he was told. Brannon notes that this argument, coupled with substantial campaign donations, likely struck a chord with state politicians.¹⁶

Furthermore, the effect of subjecting these “small” gas stations to competition, to the extent they exist, is unknown. However, recent history suggests that the repeal of minimum markup would have no effect, or small businesses would adapt to the change. As noted, the Legislature removed groceries from the Unfair Sales Act in the late 1980s. If the theory of predatory pricing held true, large grocery stores would have undercut the prices of smaller grocers and put them out of business two decades ago. Yet Wisconsin still has small grocers who have been able to compete with the large chains by either adapting to price changes or providing other services valuable to consumers. As a result, consumers have a choice about where they want to shop, and have been able to save money on groceries.

In fact, gasoline, tobacco, and alcohol remain the only products left in Wisconsin to which minimum markup applies. Yet with all other consumer goods, market pricing continues to function as it should, providing value to consumers. As argued by the Wisconsin State Journal in 2001, it shouldn’t be government’s priority to keep consumers from getting the best deal. “If that were so,” said the State Journal’s editorial, “there would be more laws to protect Joe’s Hamburger Stand from lower hamburger prices at McDonald’s, or to shield Ann’s Hardware Store from cheaper tool prices at Wal-Mart.”¹⁷

Actually, there’s a long history of the government trying to involve itself in keeping gas prices down by interfering with the free market. In the 1970’s the federal government imposed a price ceiling for gas, which kept prices artificially low, but resulted in gas shortages, long lines of cars at the pump, and alternating days on which consumers could purchase gas.¹⁸

As noted, federal antitrust law already prevents predatory “below cost” pricing. Yet, as described by the U.S. Federal Trade Commission, antitrust law shouldn’t prevent legitimate competitive price cutting:

“Although anticompetitive below-cost pricing is illegal, the United States Supreme Court has cautioned that antitrust law should not prevent pro-competitive price-cutting. Congress designed the antitrust laws for “the protection of competition, not competitors.” In other words, the federal antitrust laws promote and maintain legitimate, vigorous price competition, irrespective of how individual competitors may fare. Vigorous price competition allows consumers to reap the benefits of lower prices, greater variety, and higher quality goods and services.”¹⁹

With minimum markup on gasoline, as was the case with groceries, enforcement has also been a problem. The Department of Agriculture, Trade, and Consumer Protection (DATCP) consistently claims it does not have enough staff to effectively monitor the law. “While the law is enforceable, we cannot do an adequate job with our existing staff,” said DATCP compliance officer in 1986.²⁰

Currently, the minimum markup law is primarily enforced by the DATCP Trade Practices Bureau. DATCP also has investigative staff in offices around the state that are tasked with investigating both consumer complaints against business and unfair trade practice complaints. DATCP has 6.8 investigators in Madison, 3 in Green Bay, 3 in Wauwatosa and 2 in Eau Claire,²¹ for a total of 14.8 regional staff to enforce minimum markup provisions on over 3,000 Wisconsin gas stations.²²

Even more confusing is the provision of the law that allows gas stations to exempt themselves from the minimum markup requirement to meet competitors’ prices, as is done often times in border communities. Furthermore, enforcement of the law is dependent on a claim being filed by an aggrieved competitor – without such a complaint, the law goes unenforced. It was this spotty enforcement and lack of clarity that persuaded Judge William Callahan to invalidate the Wisconsin law several months ago, as noted.

WHAT DOES MINIMUM MARKUP COST CONSUMERS?

Several studies have been conducted to ascertain the cost of the Unfair Sales Act to Wisconsin gas consumers. Most recently, a 2004 study by David E. Clark and Steven C. Crane, both professors of economics at Marquette, found that the Act added at least 1.3 to 1.8 cents to the cost of every gallon of gas sold in Wisconsin. Their study, funded by a group calling themselves the Coalition for Lower Gas Prices (which includes AAA and Wal-Mart) found that most of the small gas stations that might need protection from large competitors in Wisconsin are those in a few select rural areas in Northern Wisconsin. But statewide, the authors concluded the minimum markup law cost state consumers over \$40 million per year. At the time the report was issued, the average gallon of gas in Wisconsin cost \$1.87.²³

These findings are similar to the previously referenced Brannon/Kelly WPRI paper in 1999, which concluded the Act added between 2 and 3 cents to every gallon of gas at a time when gas cost \$1.27 nationwide.²⁴ Both the Clark/Crane study and the Brannon/Kelly study calculate how much more Wisconsin consumers are paying per gallon than motorists in markets without a mandated markup law.

Obviously, comparing gas prices over multiple markets is a difficult endeavor. For one, states impose different gas taxes. In Wisconsin, state and federal gas taxes total 51.3 cents per gallon, while in Minnesota, taxes total 42.4 cents per gallon.²⁵ One could conclude this is why the average gas price in Wisconsin in July of 2008 (\$4.07) is higher than that in Minnesota (\$3.95). However, Minnesota also has a statewide mandate that requires gas sold in their state contain 10% ethanol, which some estimate adds between five and ten cents per gallon to the cost of gas.²⁶ Furthermore, Minnesota's minimum markup provision differs from Wisconsin's, and the Southeastern Wisconsin non-attainment area requires a reformulated gas blend that is more expensive to purchase. All told, the different markets are difficult to compare statewide.

In their study, Brannon and Kelly did the best they could to control for these factors. They essentially compared similar markets in both Wisconsin and Minnesota (which didn't have minimum markup at the time) to produce their price differential. They compared gas prices in Beloit and Eau Claire, Wisconsin, and Duluth, Minnesota. The attempt was made to compare markets with as many similarities as possible to ascertain the effect of the minimum markup law.

Aside from merely examining raw data on prices, Brannon and Kelly looked at the dispersion of prices in the three test markets. They found that prices were much more volatile in the Duluth market, which demonstrated more robust competition. Their research found that Eau Claire had the lowest dispersion of prices, both significantly below the other markets, and that the Beloit market was more competitive, due to its status as a border community.

They conclude:

"The net cost of this law to consumers is easy to calculate: Given that over 2.5 billion gallons of gasoline were sold in the state in 1998, the two cents to three cents price increase translates to Wisconsin drivers spending at least \$50 million more on gasoline than without the law, with most of that money going to large, multinational oil companies that own stations in Wisconsin. As this law adds to the overall transportation costs in the state and results in an outflow of funds from Wisconsin to external markets, this number probably understates the true cost of this law to Wisconsin residents."²⁷

Peltier and Skidmore deem the Brannon and Kelly study "invalid" because they argue studies of gas prices need a long-term perspective. They argued that the "conclusion that prices are higher in the entire state forevermore is unwarranted and misleading," instead saying their more "comprehensive" study shows minimum markup laws keep prices lower.

However, the Federal Trade Commission undercut the validity of the Peltier/Skidmore study in 2003, claiming the authors “do not fully report the statistical significance of the price changes in subsequent years” following enactment of a minimum markup law. (Peltier and Skidmore argue that minimum markup laws raise prices initially, but keep them lower over a longer period of time.) The FTC claims the study suffers from “methodological problems that make it unclear whether they are measuring the impact of sales below cost laws or something else,” instead pointing out a study from the FTC’s Bureau of Economics that found that the laws had no effect on retail prices.²⁸

Brannon and Kelly estimated the minimum markup law contributed 2% to the cost of a gallon of gas. At \$1.27 per gallon, they calculated a markup of between 2 and 3 cents per gallon. They contend this the “excess” cost motorists are paying because of the minimum markup law, versus a market with no such law.

Yet in 2008, gas prices have exploded. In July of 2008, the average gallon of gas in Wisconsin sells for \$4.07 per gallon. Naturally, as the wholesale cost of gas increases, so will the per-gallon minimum markup amount. Using the Brannon/Kelly methodology, the minimum markup increase can be extrapolated and applied to today’s gas prices. If 2 percent on \$1.27 gas meant 2 to 3 cents markup, 2 percent on \$4.07 gas means markup would be 8 cents, relative to a market without the law. (This is a rough calculation, to be sure – for instance, the gas tax now is 7.5 cents higher than it was in 1999, which would inflate today’s price.)

A 9.18% markup on fuel sold in Wisconsin adds about 30.2 cents per gallon at the pump, costing Wisconsin motorists \$990 million per year at today’s prices. However, that figure accounts for a markup of zero – even if Wisconsin were to repeal the Unfair Sales Act, gas stations would continue to mark up fuel, as they have to make a profit.

The more relevant calculation to consumers would be to find out *how much more* they are paying in Wisconsin versus a market where there is no minimum markup law. The Brannon/Kelly methodology suggests the minimum markup law adds 8 cents to a gallon of gas over a market without such a law. As a result, the Unfair Sales Act could be costing Wisconsin motorists between \$267 million per year (8 cents per gallon on 3.2 billion gallons, which was the calendar 2007 figure provided by the Department of Transportation) and \$278 million (on 3.4 billion gallons, the figure for the previous 12 months.)

CONCLUSION

There’s a reason gas stations fight so vigorously to keep the Unfair Sales Act as applied to auto fuel. Minimum markup is one of the most overt examples of select businesses reaping the benefits of government-mandated profits at the expense of the consumer. In the times of \$4.00 gas, it makes even less sense, as low-income individuals are subject to a regressive tax when purchasing fuel.²⁹

Aside from the additional cost of fuel to the consumer, high gas prices seep into the price of all goods and services transported throughout the state. When it costs more to truck candy bars to a grocery store, that price will be reflected in the cost of those candy bars. As a result, Wisconsin consumers end up not only paying higher prices at the pump, but they end up paying ancillary costs hidden within goods and services they need.

The Legislature should repeal the state's minimum markup of auto fuel to aid consumers. Rather than government continuing to skew the market and funnel profits to gas stations, they can provide citizens with instant relief – and it won't cost the state treasury a dime.

If the Legislature refuses to act on a full repeal of minimum markup, there are incremental steps that can be taken. For instance, the Legislature can control the rapid growth of the per-gallon markup by considering capping the markup to 2007 levels, which would limit the minimum markup to 21 cents per gallon.

APPENDIX A: "UNDERSTANDING WISCONSIN'S 'MINIMUM MARKUP' LAW"
By the Wisconsin Legislative Council, 2006:

**"MINIMUM MARKUP" AND "COST" OF MOTOR VEHICLE FUEL
REQUIREMENTS OF THE LAW**

In order to implement the policy promoting fair competition, the Act contains the language commonly referred to as Wisconsin's minimum markup law: a specific definition of "cost" that applies only to motor vehicle fuel. This definition is at the core of the minimum markup law. It is complicated by the diverse structure of the motor vehicle fuel market and the need to ensure fairness and consistency between competitors with differing positions in this structure.

The statute defines the "cost" of motor vehicle fuel to include the variable costs of each unit of fuel as well as a proportionate share of the other costs of doing business attributable to each unit of fuel. The statute allows a minimum percentage markup based on each seller's variable costs to satisfy the requirements for including the proportionate share of other costs. The statute categorizes sellers according to their position in the stream of commerce and specifically defines "cost" for each seller category. Different categories use different markups because variable costs in certain categories include prior markups. The statute contains five categories for retailers of motor vehicle fuel and two categories for wholesalers of motor vehicle fuel. For example, there is a category for retail sales by a seller who purchases motor vehicle fuel *from* a wholesaler as well as a category for retail sales by a seller who *is* a wholesaler. Those categories, and the "cost" calculation for each, are described in the Appendix. "Retailer," "wholesaler," and other terms related to the stream of commerce of motor vehicle fuel have specific meanings in the Unfair Sales Act. The Appendix explains those terms.

Additionally, for calculation of retail "cost," the statute allows the substitution of average posted terminal price (AFTP) for the variable costs of each unit of fuel. The AFTP is a price calculated by a petroleum price reporting service based on average price at a "terminal," a distribution facility from which at least three refiners or wholesalers sell fuel. The AFTP is an accurate, timely, and easily verified measure of wholesale prices in a particular area. Accordingly, use of AFTP adds transparency to the markup process and lowers costs of compliance, investigation, and enforcement in state and private actions.

PENALTIES AND ENFORCEMENT

With regard to sales below-cost of any merchandise, DATCP or a district attorney may commence an action on behalf of the state to recover a forfeiture of not less than \$50 nor more than \$500 for a first violation and not less than \$200 nor more than \$2,500 for each subsequent violation. [s. 100.30 (4), Stats.]

With specific regard to below cost sales of motor vehicle fuel, additional state remedies as well as a private cause of action exist. [s. 100.30 (5) and (5m), Stats.] DATCP may issue a cease and desist order, bring an action to enjoin a violation, and recover a forfeiture of not less than \$200 nor more than \$5,000 for each violation involving motor vehicle fuel. A district attorney may bring an action to enjoin a violation and recover a forfeiture of not less than \$200 nor more than \$5,000 for each violation involving motor vehicle fuel.

The private cause of action allows any person who is injured or threatened with injury as a result of the below-cost sale of motor vehicle fuel to bring an action. Available relief includes injunctive relief as well as the recovery of treble damages or \$2,000, whichever is greater,

multiplied by each day of continued violation, and attorney fees and other costs. A private action must commence within 180 days after the date of the violation. In DATCP's experience, a private action often will commence after initiation of a state action in order to take advantage of evidence gathered by the state. In a private action, the plaintiff can gain access to DATCP records through a public records request during the discovery period of the private action. DATCP feels that the private cause of action is a strong deterrent to violation of the "minimum markup" law on account of the potential liability for treble damages and attorney fees in the action.

EXCEPTIONS

The Unfair Sales Act provides several exceptions to the prohibition on sales below cost and, accordingly, exceptions to the minimum markup requirement for sales of motor vehicle fuel. Specifically, there is a broad exception for meeting competition. This exception allows a seller, including a seller of motor vehicle fuel, to sell below cost if the price of merchandise is set in good faith response to a competitor's existing price. [s. 100.30 (6), Stats.] An example of this exception would be a seller in a border city, such as La Crosse, who meets the price of a Minnesota seller. Further, the exception could cascade throughout the state as in-state sellers lower their prices to meet the competition from the border city.

In order to utilize this exception with respect to retail sales of motor vehicle fuel, however, a motor vehicle fuel retailer must submit notification of its lower price to DATCP before the close of the business day on which the seller lowered its price to meet competition. Failure to comply with the notification requirement creates a rebuttable presumption that the seller did not lower its price in order to meet competition. In a dispute, this presumption shifts the burden of proof from the state to the selling retailer, requiring the retailer to prove it lowered prices to meet competition. On the other hand, compliance with the notification requirement provides the seller with immunity from the private cause of action and special department remedies described above.

Other exceptions relate to clearance and liquidation sales, perishable items, and sales related to government contracts or judicial orders.

ETHANOL

Recently, there has been widespread interest in the application of the minimum markup law to ethanol-blended fuels. In the Act, "motor vehicle fuel" means any liquid prepared, advertised, or sold for use as or commonly and commercially used as a fuel in internal combustion engines. [s. ATCP 105.001 (4), Wis. Adm. Code.] Accordingly, ethanol and any ethanolblended fuel would be considered motor vehicle fuel for purposes of the "minimum markup" law.

An August 2006 directive from Governor James Doyle suspended DATCP enforcement of the "minimum markup" law on ethanol-blended fuels. The DATCP staff indicates that the suspension complements the Governor's stated interest in promoting production of ethanol blended fuels in the state. The Governor's directive does not remove the private cause of action as applied to ethanol-blended fuel. However, private plaintiffs may no longer benefit from DATCP records if there is no DATCP investigation.

ENDNOTES

- ¹ United States Federal Trade Commission, "Wisconsin's Unfair Sales Act (Response to Letter by State Representative Shirley Krug)," October 15, 2003.
- ² Wisconsin Legislative Council, "Wisconsin's Unfair Sales Act: An Overview," Staff Brief 80-10, July 9, 1980.
- ³ Associated Press, "Markup Law Called Ineffective," Wisconsin State Journal, April 22, 1987.
- ⁴ Pete Millard, "Krug Targets State's Minimum Markup Law for Gas," *Milwaukee Business Journal*, July 7, 2000.
- ⁵ Gordon S. Black, Ph.D., "The 2000 Wisconsin Citizen Survey," *Wisconsin Policy Research Institute* Volume 13, Number 4, July 2000.
- ⁶ Mike Ivey, "Small Business Interests Save Gas Markup Law," *Capital Times*, July 27, 2001.
- ⁷ Governor Jim Doyle Press Release, "Directs Agency to Suspend Enforcement of Minimum Markup Law on Ethanol," August 8, 2006.
- ⁸ Wisconsin Petroleum Marketers, Matt Hauser letter to Wisconsin Legislators, May 13, 2008.
- ⁹ James Peltier, Ph.D. and Mark Skidmore, Ph.D., "A Report of Motor Fuel Fair Marketing Laws – A National Study of the Effects of Motor Fuel Fair Marketing Laws on Gasoline Markets and a Critical Evaluation of 'Pumping Up Gas Prices in Wisconsin: The Effects of the Unfair Sales Act on Retail Gasoline Prices in Wisconsin,' Published By the Wisconsin Policy Research Institute," July 2001.
- ¹⁰ J. Isaac Brannon and Frank Kelly, "Pumping Up Gas Prices in Wisconsin: The Effects of the Unfair Sales Act on Retail Gasoline Prices in Wisconsin," *Wisconsin Policy Research Institute* Vol. 12, No. 7, October 1999.
- ¹¹ Petroleum Marketers Association of Wisconsin Press Release, "New Study Shows Motor Fuel Fair Marketing Laws Keep Gas Prices Lower," July 2, 2001.
- ¹² D.J. Tice, "Protection For Whom?," *St. Paul Pioneer Press*, August 31, 2001.
- ¹³ J. Isaac Brannon, "How Politicians Blew the Gas Price Issue," *Wisconsin Interest*, Volume 9, No. 3, 2000.
- ¹⁴ William J. Baumol, John C. Panzer, and Robert D. Willig, "Contestable Markets and the Theory of Industrial Structure," *Harcourt Brace Johanovich*, 1982. This study was cited by Isaac and Brannon in their 1999 report.
- ¹⁵ Brannon and Kelly, p. 3.
- ¹⁶ Brannon, *Wisconsin Interest*, p. 43.
- ¹⁷ "Gas Markup Law Runs Low on Logic," *Wisconsin State Journal*, June 21, 2001.
- ¹⁸ "Gas Fever: Happiness is a Full Tank," *Time Magazine*, February 18, 1974.
- ¹⁹ FTC Letter to Krug
- ²⁰ George Hesselberg, "Minimum Markup Law Draws Praise, Criticism," *Wisconsin State Journal*, Jan. 25, 1986.
- ²¹ Wisconsin Legislative Fiscal Bureau 2007 Informational Paper #84, "Consumer Protection Programs," January 2007.
- ²² Petroleum Marketers of Wisconsin memo to Wisconsin State Legislators, February 1, 2005.
- ²³ http://www.wisconsinprices.com/retail_price_chart.aspx
- ²⁴ http://tonto.eia.doe.gov/dnav/pet/hist/mg_tt_usw.htm
- ²⁵ http://www.api.org/statistics/fueltaxes/upload/July_2008_gasoline_and_diesel_summary_pages.pdf
- ²⁶ Brannon and Kelly, p. 4.
- ²⁷ Brannon and Kelly, p. 1.
- ²⁸ FTC Letter to Krug, footnote 34.
- ²⁹ In fact, the minimum markup, state fuel excise tax, and federal fuel tax are all regressive, as they take a larger percentage of income from poorer individuals than wealthy individuals.