HALE AND DORR LLP

December 2001

antitrust and trade regulation bulletin

VISA and MasterCard Found Guilty of Sherman Act Violation

In 1998, amid much fanfare and attention, the United States Department of Justice (DOJ) sued both MasterCard and VISA alleging that their policies preventing credit card issuers from issuing competing credit cards such as American Express or Discover cards were an unreasonable restraint of trade in violation of the Sherman Act. Years later, the United States District Court for the Southern District of New York issued its ruling, which passed nearly unnoticed. *United States v. VISA U.S.A. Inc., et al.,* 163 F. Supp. 2d 322 (S.D.N.Y. 2001).

The government alleged, and the court accepted, that MasterCard's and VISA's arrangements permitting issuers to issue either MasterCard or VISA cards, but terminating the relationship in the event an issuer issued either American Express or Discover cards, injured competition in the credit card industry. In fact, the court found that since 1996, when American Express decided to allow bank issuance, not a single U.S. bank gave up its VISA and MasterCard portfolios in order to begin issuing American Express cards.

The court found that while there are other ways to issue credit cards – both Discover and American Express issued cards without bank issuers – banks provided essential attributes to credit card network competitors. Bank customers offered a credit card from their primary bank are more likely to accept the offer, more likely to use the card regularly and less likely to cancel the account. As a result, the exclusionary practices caused significant competitive harm with no countervailing procompetitive benefit. The court-ordered remedy prevents VISA and MasterCard from terminating

The exclusive agreements which required credit card issuers to forfeit their VISA and MasterCard portfolios if they issued American Express and/or Discover cards violated antitrust laws.

contents

issuers who issue rival cards, but does not demand that VISA and MasterCard treat those issuers on par with those who do not issue rival cards.

The government also alleged, and the court rejected, an argument that the dual membership of issuers in the MasterCard and VISA associations harmed consumers by reducing competition between the two cards. Both MasterCard and VISA have moved, since the initiation of the litigation, from a dual system to one which encourages issuers to issue only a single card, but does not require it. Although the government argued that this "fix" resulted directly from the litigation, the court found the firms were considering these new loyalty programs prior to the filing of the litigation. Either way, the government's complaint became stale, making allegations about the way things had been instead of the way things were at the time of trial. Accordingly, any prospective relief on this issue seemed unnecessary to the court.

Balancing competitive concerns and incentives to innovate will be the subject of discussion at a series of hearings beginning in January.

Public Hearings Scheduled to Address Interplay of Intellectual Property and Antitrust

In November, Tim Muris, chairman of the Federal Trade Commission (FTC), announced a series of public hearings entitled "Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy" to be co-hosted with the DOJ. The first hearing should be held sometime in January with additional sessions into the spring.

In announcing the hearings, Muris observed that in the 1970's, antitrust law and policy lacked a sufficient appreciation of the innovation incentives which intellectual property (IP) rights create. More recently, some commentators have come to believe that "it is the intellectual property doctrine that is not showing proper appreciation for the innovation that competition may spur."

Muris listed a variety of recent events which impact the interplay between antitrust and intellectual property, including: the vast increase in the number of patents issued; the expanded scope of issued patents; the increased incidence of antitrust claims brought in patent cases, many of which are decided at the appellate level by the Federal Circuit Court of Appeals; and the tensions between antitrust and IP doctrines caused by unilateral refusals to license intellectual property. The hearings intend to address a multitude of questions created by these events, all designed to assist the FTC and DOJ in developing antitrust policy which promotes competition without quashing incentives to innovate.

DOJ Vigorously Enforcing "Gun Jumping"

Antitrust practitioners consistently advise merging parties that until a merger is final, the two parties must continue to behave as competitors. Nevertheless, it is also true that during the time it takes for the transaction to be formally consummated, the buyer has a legitimate interest in protecting the business and the assets it has contracted to purchase. There has been little legal precedent relevant to the resolution of these conflicting interests.

This may soon change because the DOJ recently sued Computer Associates International, Inc. (Computer Associates) alleging that while its 1999 cash tender offer for Platinum Technology International, Inc. (Platinum) was pending, it acquired too much control over its soon-to-be subsidiary. *United States v. Computer Assoc. Int'l, Inc.,* Civ. Action No. 1:01CV02062 (S.D.N.Y, filed Sept. 28, 2001). The DOJ alleges that Computer Associates violated both the HSR waiting period rules as well as the Sherman Act. The resolution of this case should provide useful insight with respect to the appropriate scope of pre-merger activities between competitors who are intending to merge.

In 1999, Computer Associates made a cash tender offer for Platinum. In connection with that transaction it filed a pre-merger notification under the Hart-Scott-Rodino Act of 1976. The DOJ investigated the transaction and after about two months allowed the transaction to close subject to divestitures it believed were necessary to prevent competitive harm. Two years later, the DOJ filed this action based upon the contractual terms that governed Platinum while the transaction was pending. According to the government, the transaction documents limited Platinum's ability to discount its products beyond 20% and also limited its ability to amend its standard contract terms. In addition, the DOJ alleges that Computer Associates assigned a person to work at Platinum to review and approve Platinum's customer contracts. The government contends that Platinum regularly discounted its products far more than 20%, making the restriction a change in its normal business practice, rather than a mere continuation of what had been its practice. The government seeks civil penalties from each party to the merger at the statutory maximum of $11,000 per day for the fifty-eight days the violations allegedly continued and an order preventing Computer Associates from engaging in similar conduct in the future.

After the DOJ filed its suit, Computer Associates issued a press release and observed that the disputed contractual language had been standard language used for fourteen years and was necessary to protect the assets to be acquired. In addition, it contended that the government made no complaint about the contractual language until two months after the completion of the Platinum acquisition.

The Ties Have It

Since Tim Muris became the new chairman of the FTC, there have been two prominent and controversial transactions in which the FTC has not acted because Muris' recusal left the FTC in a 2-2 tie. The FTC cannot act without a majority vote in favor, so the tie votes became decisions to take no action.

The FTC staff recommended a challenge to the Pepsi acquisition of Quaker Oats, but the FTC inaction allowed the merger to close. The staff recommended a consent decree to resolve competitive issues connected with the sale of Pillsbury to General Mills, but with two commissioners voting to reject the decree in favor of litigation and two voting to accept the decree, the FTC inaction allowed the transaction to close without a formal enforceable decree imposing the conditions the staff negotiated.

In *Pepsi*, the staff became convinced that the sale of Quaker's Gatorade brand of sports drink to Pepsi, one of the two dominant soft drink companies in the market, would harm competition. It reached this conclusion even though Pepsi contracted to sell its competing drink, All Sport, to a third party. This approach, often called "fix it first," failed to persuade the staff who were convinced that selling All Sport to a company less powerful than Pepsi would decrease its competitive significance in the sports drink segment of the marketplace.

In the General Mills matter, the FTC staff was concerned about reduced competition between the Pillsbury Doughboy baked goods mixes and those offered by General Mills' popular Betty Crocker line. The staff's negotiated solution would have given General Mills ownership of the Doughboy trademark, but would have required General Mills to license that trademark to a new competitor who would have purchased the baked goods assets and marketed those products using the Doughboy mark. Two commissioners thought that the proposed solution to split the Doughboy mark, allowing General Mills to use it on some products and a third-party purchaser to use it on the baked goods mixes, was an acceptable solution

The recusal of the new FTC chairman leaves Democrats and Republicans split over what action to take in two recent mergers.

because they believed the product lines were sufficiently distinct so that consumers would not be confused. However, the two other commissioners thought the remedy would, in fact, confuse consumers. In addition, they worried that the third-party purchaser might not be sufficiently large and influential to market the Pillsbury branded products as widely and prominently as Pillsbury previously had, given its broad line of grocery products.

One would expect that the longer Muris is at the FTC, the fewer recusals he will be required to make. His future participation will, obviously, be very significant given the demonstrated tendency for the other four commissioners to align in a 2-2 tie.

Chubb plc Completes Divestiture of Door Hardware Companies to Assa Abloy AB

As described in our October, 2000 bulletin (see www.haledorr.com/publications/archive_pub.asp) last year Chubb plc (then known as Williams plc), owner of Yale Security and Corbin Russwin, contracted to sell its worldwide door hardware businesses to Assa Abloy AB (Assa), owner of Sargent, Arrow, Medeco and Mul-T-Lock. Chubb and Assa also compete in the hotel card-activated electronic lock business through other subsidiaries not involved in the transaction. However, because some of the Chubb door hardware companies supplied certain products to the Chubb hotel lock subsidiary, the FTC objected to the sale of those supply companies, but allowed the rest of the door hardware transaction to close last August.

Recently, with our assistance, Chubb demonstrated to the FTC's satisfaction that effective new supply arrangements had been located for the hotel lock company and that it had received sufficient intellectual property and trademark protection such that the separation from the door hardware companies would not harm it. As a result, the completion of the entire transaction as originally contemplated occurred in late November with the sale of the supply companies to Assa.

FTC Investigates Two Mergers Among Online Job Recruiters

In June, 2001, TMP Worldwide, owner of the dominant online job board Monster.com, agreed to purchase the second largest online board, HotJobs. The FTC requested additional information about the transaction in August. Also in August, Career Holdings, Inc., parent company of the popular job board CareerBuilder, announced a cash tender offer for all of the shares of another competitor, Headhunter.net.

With our assistance, CareerBuilder provided information to the FTC that convinced the agency to close its review in early November, without the need for full compliance with the second request. Career Holdings has now completed its acquisition of Headhunter.

Meanwhile, the Monster.com investigation continues. It would seem that if the FTC staff were determined to define a market that includes only online job recruitment firms, it would be difficult not to challenge the Monster.com transaction. On the other hand, if the staff were inclined to consider newspapers and placement agencies in the same market, the transaction should be cleared. The market definition the agency chooses to pursue will provide valuable insight into the FTC's view on whether bricks and clicks compete with each other, which could well be applicable to a variety of future mergers in other industries.

DOJ Lets Microsoft Go; Several States Continue Their Cases

In October, the DOJ and Microsoft announced that they had reached a settlement. While the DOJ touts the settlement as a government success, its terms are generally considered less than

Hale and Dorr assists Chubb plc in divesting its remaining door hardware assets.

spectacular. California, Massachusetts and several other states have reached that conclusion, and announced that they will continue to prepare for a trial to determine an appropriate remedy for the monopolization violation upheld last summer by the United States Court of Appeals for the District of Columbia.

What may prove to be the most interesting aspect of the settlement is the strange posture the case now takes. It is widely expected that the district court will provisionally accept the settlement and then, pursuant to the Tuney Act, publish it in the *Federal Register*. The publication will initiate a sixty-day public comment period. Meanwhile, discovery will get underway in contemplation of the trial on remedies. This kind of double-track settlement by some and trial by others is unprecedented, at least in antitrust jurisprudence, and may present a variety of challenges. Not the least among these will be a trial in front of a judge who may already have determined that a settlement is consistent with the public interest.

In addition, the non-settling states may find the DOJ, their former co-plaintiff, contending that more drastic remedies than those in the settlement will actually harm competition.

Failure to Provide a Complete HSR Filing Results in $4 Million Fine

Hearst Corporation has agreed to pay the largest HSR fine ever for its failure to submit all of the required documents with an initial HSR filing. As part of the HSR filing, companies are required to submit all studies and analyses prepared by or for officers and directors to evaluate various specific aspects of a transaction (commonly called 4(c) documents). Hearst neglected to include all responsive documents with respect to its 1997 filing related to its acquisition of Medi-Span. Initially, the FTC allowed the transaction to proceed.

Subsequently, however, and after numerous customer complaints, the FTC challenged the merger in court seeking a permanent injunction barring the combination. Discovery connected to that court action resulted in the production of the missing 4(c) documents, which lead to an independent civil penalty proceeding. The FTC alleges that the company's failure to supply these documents with the HSR filing back in 1997 impaired its ability to analyze the merger at that time. Hearst settled the civil penalty action by agreeing to pay a $4 million fine.

"New" Merger Review Initiative Unveiled

In October, the Antitrust Division of the DOJ released what it represented will be a new approach to HSR merger analysis. The goals of the initiative are to create a more efficient and focused investigation, while identifying critical legal issues and promoting prompt evaluation of evidence.

Under the HSR rules, the government has thirty days after a filing to determine whether or not it needs to issue a formal request for additional information — a "second request." The new program encourages the government staff to more actively use the first thirty days to request information from the parties and to learn about the industry. The policy suggests that this will take the form of informal requests for a variety of different types of documents from the merging parties. Merging parties are free to participate (or not) in this process, but it seems obvious that failure to participate enhances the likelihood of receiving a second request.

Even if a second request is ultimately issued, the DOJ aspires to be able to issue more narrow and tailored requests based upon its learning during the first thirty days. In the past, the government has tended to issue nearly standard (and exceedingly broad) second requests to all merging

While the DOJ and Microsoft have settled their differences, several states find the remedy inadequate and continue to pursue their claims.

parties. The new procedure suggests an effort to modify this approach and achieve greater differentiation among second requests.

After the issuance of a second request, the initiative expresses a willingness to negotiate a schedule suitable to both parties. In some situations, the government suggests it will create what amounts to a scheduling order, committing both sides to dates for modifications to the second request, depositions, data exchanges, meetings with economists and front office staff, among others.

It will take some time to determine whether or not this initiative produces a more streamlined process through the DOJ's review of particular mergers. Ironically, not long after issuing this call for more efficiency, the DOJ refused to accept packages of any kind for nearly two weeks, including HSR pre-merger notifications, because of anthrax concerns. Having opened for business again, they are likely to find an unusually large number of filings that will pose a tough test for this new procedure.

Fraudulent Patent Procurement May Support Monopolization Counterclaim

A patent holder seeking to enforce patents and knowing they were obtained fraudulently can, in particular circumstances, be subject to antitrust counterclaims. In *Medtronic AVE, Inc. v. Boston Scientific Corp., et al.,* 2001-2 Trade Cases (CCH) ¶ 73,388 (D. Del. Mar. 30, 2001), the defendants alleged that Medtronic knew its patents were fraudulently obtained and, therefore, enforcement against Boston Scientific and others was an attempt to monopolize the coronary stent market. The United States District Court for the District of Delaware denied a motion to dismiss the antitrust counterclaims.

Medtronic sought to dismiss the counterclaims by arguing that the alleged fraud on the patent office was not sufficiently material to support an antitrust counterclaim. However, the court found that Boston Scientific had adequately alleged both intentional fraud on the patent office and that, but for the fraud, the patent would not have issued. Medtronic also argued that, without an allegation of market share, Boston Scientific could not support a monopolization claim. The court disagreed, stating that there is no minimum market share a party must allege because market share is but one factor in determining whether or not market power exists.

The courts have developed reasonably high standards for sustaining antitrust counterclaims in patent infringements suits and, as a result, dismiss them with some frequency. However, in some situations they provide the patent infringement defendant with a useful affirmative defense to the infringement suit.

antitrust and trade regulation bulletin

For more information, contact Hale and Dorr's Antitrust and Trade Regulation Group.

James C. Burling
Co-Chair, Boston office
617.526.6416
<james.burling@haledorr.com>

John C. Christie
Co-Chair, Washington office
202.942.8403
<john.christie@haledorr.com>

Michelle D. Miller
Vice-Chair, Boston office
617.526.6116
<michelle.miller@haledorr.com>

Boston
617 526 6000

London*
44 20 7645 2400

Munich*
49 89 24 213 0

New York
212 937 7200

Oxford*
44 1235 823 000

Princeton
609 750 7600

Reston
703 654 7000

Waltham
781 966 2000

Washington
202 942 8400

*an independent joint venture law firm