# Antitrust and Trade Regulation Bulletin

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**Department of Justice Developments**

Joel I. Klein, the acting Assistant Attorney General in charge of the U.S. Department of Justice Antitrust Division, has been nominated by President Clinton to fill the vacancy left by the departure of Assistant Attorney General Anne K. Bingaman. Klein formerly served as Deputy Assistant Attorney General in the Antitrust Division and as Deputy Counsel to President Clinton.

Over the past year, there has been a dramatic increase in the number of merger investigations initiated by the Department of Justice. The Antitrust Division commenced 237 investigations under Section 7 of the Clayton Act in 1996, an increase of over 100 investigations over the prior year. The number of non-merger investigations under Sections 1 and 2 of the Sherman Act remained relatively constant, and the number of criminal indictments continued to decline. The Division's stated policy with respect to criminal indictments is to bring "fewer but more significant prosecutions involving bigger firms, larger industries and higher volumes of commerce and to target national and international companies." This policy is clearly reflected in the Archer Daniels Midland Company enforcement action which resulted in a $100 million fine, the largest criminal antitrust fine in the history of the Antitrust Division. ADM, as well as two Japanese companies and a Korean subsidiary, entered guilty pleas for restraint of trade in connection with an alleged international price fixing conspiracy.

**Federal Trade Commission Developments**

Following the expiration of Commissioner Janet Steiger's term, President Clinton nominated Sheila Foster Anthony to fill that position. Ms. Anthony previously served as Department of Justice liaison to Congress and to the White House.

One of the most significant FTC merger cases over the past year was the Time Warner, Inc./Turner Broadcasting, Inc. merger in which the FTC negotiated a complex settlement of the multi-billion dollar deal. The Commission currently is seeking an injunction from the Federal District Court in Washington, D.C. to prevent completion of the Staples, Inc./Office Depot, Inc. merger pending further FTC proceedings. The FTC claims that the proposed merger would substantially reduce competition in the retail sale of office supplies in areas where the firms presently compete. The Commission rejected proposed divestiture plans which the proponents of the merger believe would have adequately addressed the competitive concerns expressed by the Commission.

We also saw record civil penalties for Hart-Scott-Rodino Act premerger notification violations, including payment of $3.1 million in civil penalties by Sara Lee Corporation to settle charges that it failed to timely file. In February of this year, Mahle GmbH, a German automotive and diesel engine parts manufacturer with businesses in the United States and a competing Brazilian manufacturer agreed to pay over $5 million in civil penalties for their failure to file a pre-merger notification. In addition, Mahle agreed to a substantial divestiture of the assets acquired from the merger.

Finally, the Commission brought a highly publicized administrative complaint against the toy retailer, Toys `R' Us, Inc., alleging that the toy retailer used its market power to maintain super-competitive profits and to reduce consumer choice with respect to place of purchase. The complaint alleges that Toys `R' Us extracted agreements from toy manufacturers to stop selling certain toys to warehouse clubs, or to put the toys into more expensive combination packages, so consumers could not obtain lower-priced toys from the clubs or compare prices easily. The case is in administrative litigation.

We have begun to see a response by the antitrust enforcement agencies to two reports issued last year by the Federal Trade Commission Staff -- *Anticipating the 21st Century: Competition Policy in the New High-Tech, Global Marketplace* and *Consumer Protection Policy in the New High-Tech, Global Marketplace* . The Report on Competition Policy addressed various aspects of merger analysis, including the treatment of efficiencies, the failing firm defense and market definition, as well as the assessment of competitive effects, the development of antitrust policy for new technologies and intellectual property, issues involving access to networks and standards, joint venture analysis and a review of themes for the future. The substantive analysis contained in these Staff Reports is reflected in the new Guidelines on Efficiencies in Mergers and the Joint Venture Project, currently underway, as well as in remarks by agency officials in recent speeches, all discussed below.

**Premerger Review**

In 1996, the Commission adopted new rules to reduce filings under the HSR Act. The new rules exempt the following categories of transactions that are unlikely to raise competitive concerns:

- certain purchases of goods or realty in the ordinary course of business, including certain purchases of used durable goods where the purchase is designed to replace or expand production capacity;

- certain real estate acquisitions, such as acquisitions of shopping centers and hotels and motels, not likely to violate the antitrust laws;
- acquisitions of oil and natural gas reserves and certain associated production and exploration assets valued at $500 million or less;
- acquisitions of coal reserves and certain associated productions and exploration assets valued at $200 million or less;
- acquisitions of voting securities of companies that hold real property or carbon-based mineral reserves the direct acquisition of which would be exempt, and other assets valued at $15 million or less; and
- acquisitions of realty acquired solely for rental or investment purposes.

The Commission estimates that the new rules have reduced filings by an estimated 7 to 10 percent.

In a recent speech, FTC Bureau of Competition Director William J. Baer outlined current government efforts to make the premerger review process more efficient and effective. According to Baer, the Antitrust Division and the FTC have attempted to speed up the clearance process during which the agencies determine which agency will review a transaction. There also is an effort underway to reduce the burden of second requests, including a uniform second request model, as well as a "quick look" process that provides for document production in stages. Under the "quick look" process, an agency will first focus on issues which would lead it to conclude that the proposed merger does not raise competitive concerns. Baer reiterated this theme in his remarks before the ABA Antitrust Section Spring Meeting in April, emphasizing the Commission's efforts to make the HSR process more "userfriendly." HSR filing information is available on the Internet at the Commission's Web page: http://www.ftc.gov .

FTC Bureau of Competition Deputy Director George S. Cary also recently spoke on efforts to improve the efficiency and quality of the Bureau's investigations. Cary noted, in particular, the effort to improve the effectiveness of divestiture orders by reducing the allowable time for divestitures to not more than 6 months and by seeking alternative divestiture arrangements when the original proposal cannot be accomplished. Baer also addressed this subject at the ABA Antitrust Section Spring Meeting. He described the Commission's use of "crown jewel" provisions which call for divestiture of a broader group of assets when the initial divestiture does not succeed within the prescribed time. Such provisions have been used in several recent cases, and Baer noted that "[t]he incentive force of crown jewel provisions is suggested by the fact that no such provision in a Commission order has ever been triggered to date."

**Efficiencies Guidelines**

On April 8, 1997, the Department of Justice and the Federal Trade Commission revised the efficiencies section of the 1992 Horizontal Merger Guidelines to clarify when and how the agencies will consider efficiency claims. The new Guidelines were prompted by Staff recommendations in the Report on Competition Policy regarding the treatment of efficiencies in merger analysis and the proposal in that Report to reconsider the approach to efficiencies set forth in the 1992 Merger Guidelines. Bureau of Competition Director William Baer commented on the new Guidelines at the ABA Antitrust Section Spring Meeting:

"In a nutshell, efficiencies that are *merger-specific* and *cognizable* will be considered in the analysis. To be cognizable, an efficiency must be verified and it cannot arise from anti-competitive reductions in output or service... . It is necessary to assess how the claimed efficiencies will play out in affecting market behavior. If the other evidence indicates that the potential anticompetitive consequences of a merger are very large, the merger will likely be anticompetitive unless the efficiencies are extraordinarily great."

Efficiencies from a merger include, for example, better integration of production facilities, plant specialization, lower transportation costs, reduced administrative and overhead expenses, etc. The Staff Report on Competition had specifically noted the increased competitive pressure on businesses to achieve efficiencies -- often in order to respond to foreign competition or to keep up with consumer demand for faster, new product introduction. The Revised Guidelines on Efficiencies in Mergers provide generally that "[t]he Agency will not challenge a merger if cognizable efficiencies are of a character and magnitude that the merger is not likely to be anticompetitive in any relevant market. To make that determination, the Agency considers whether cognizable efficiencies likely would be sufficient to reverse the merger's potential harm to consumers, *e.g.*, by preventing price increases in the market."

**Joint Ventures**

On January 23, 1997, the FTC announced a plan to clarify and update its policies regarding analysis of joint ventures, strategic alliances, and other forms of collaboration among competitors. The "Joint Venture Project," like the FTC Staff Reports on Competition Policy discussed above, arises out of public hearings held by the FTC in the fall of 1995 on global competition in the high-tech marketplace. The Staff Report had concluded that antitrust policy had not always been effective in analyzing business justifications for joint ventures or in identifying competitive concerns. In its Report, the Staff announced that "the time has come for a significant effort to rationalize, simplify, and articulate in one document the antitrust standard that Federal antitrust enforcers will apply in assessing collaborations among competitors." We anticipate that the Joint Venture Project will produce such a standard for assessing competitor collaborations, perhaps in the form of guidelines such as those presently in effect with respect to joint venture activity in the specialized areas of health care and intellectual property.

## Legislative Developments

On January 9, 1997, Representative Henry Hyde proposed legislation (H.R. 401) entitled "Intellectual Property Protection Act of 1997." The proposed legislation provides that an intellectual property right would not be presumed to define a relevant market or to establish market power in an antitrust action against the holder of the intellectual property right. This protection is significant to the holders of patents in any action alleging anti-competitive conduct.

The passage of the Telecommunications Act of 1996 led to significant industry consolidation and increased antitrust enforcement activity. In the wake of the Act, the Antitrust Division reviewed and ultimately approved three mergers of radio station operators. The Act also terminated the historic AT&T antitrust consent decree.

## International Antitrust Developments

On January 22, 1997, the European Commission issued a Green Paper on vertical restraints in E.C. competition policy. The paper addresses all aspects of vertical relationships in the distribution chain, including exclusive buying and selling and selective distribution. Under E.C. law, territorial restrictions for exclusive distributors and resale price maintenance are deemed anti-competitive, except to the extent they fall within a block exemption. The Green Paper seeks comment on four options: (1) maintaining the current system; (2) creating wider block exemptions; (3) creating more focused block exemptions; and (4) reducing the scope of E.C. competition law as applied to vertical restraints. The Green Paper is available on the World Wide Web at: http://europa.eu.int/en/comm/dg04/dg4home.htm .

**Noteworthy Cases**

***Vertical Restraints***

The Court of Appeals for the Seventh Circuit reviewed a maximum price provision in a contract between a gasoline distributor and a gas station operator. Under this contract, the operator was permitted to raise its price above the suggested resale price, but it was required to remit the entire additional profit to the distributor if it raised the price without the distributor's permission. Chief Judge Posner delivered the opinion of the Seventh Circuit, ruling that the contract provision making it worthless for the operator to raise prices beyond the suggested retail price constituted a maximum resale price maintenance arrangement that was *per se* illegal under existing Supreme Court precedent. The Seventh Circuit questioned the continuing validity of that precedent, but nonetheless felt bound to follow it. In particular, the Court noted that a gas station operator, who loses monopoly profits as a result of a price ceiling imposed by a gasoline distributor, probably does not suffer injury cognizable under the antitrust laws.

The Supreme Court subsequently granted certiorari and likely will address whether this maximum price provision should be considered *per se* illegal, and whether the operator's inability to profit from higher prices to consumers constitutes antitrust injury. *Barkat U. Khan & Khan Associates, Inc. v. State Oil Co.*, 93 F.3d 1358 (7th Cir. 1996), *cert. granted* 117 S. Ct. 941, 65 U.S.L.W. 3567 (February 18, 1997).

***International Jurisdiction***

The First Circuit Court of Appeals upheld a criminal complaint that asserted violations of the Sherman Act based on price fixing activities which took place entirely in Japan but were intended to have, and did have, substantial anticompetitive effects in the United States. The First Circuit ruled that the Massachusetts district court erred in dismissing the Complaint for failure to state a prosecutable offense.

The Court noted that existing precedent conclusively establishes that a civil antitrust action predicated on wholly foreign conduct, which has an intended and substantial effect in the United States, comes within the reach of Section 1 of the Sherman Act. The extension of that precedent to a criminal prosecution is a case of first impression. The Court concluded:

[T]he government charges that the defendant orchestrated a conspiracy with the object of rigging prices in the United States. If the government can prove these charges we see no tenable reason why principles of comity should shield NPI from prosecution. We live in an age of international commerce, where decisions reached in one corner of the world can reverberate around the globe in less time than it takes to tell the tale. Thus, a ruling in NPI's favor would create perverse incentives for those who would use nefarious means to influence markets in the United States, rewarding them for erecting as many territorial firewalls as possible between cause and effect.

*United States v. Nippon Paper Industries Co., Ltd.*, 1997 U.S. App. LEXIS 4939 (1st Cir. 1997).

***Antitrust Counterclaims***

The Court of Appeals for the Fifth Circuit recently held that the antitrust claim brought by a tank insulation system manufacturer based upon a competitor's alleged wrongful filing of a patent infringement suit was not a compulsory counterclaim, but rather a permissive counterclaim that could be maintained as a separate action. The antitrust claim, based upon the filing of an infringement action for a patent claimed to be invalid, alleged much of the same conduct as alleged in defense of the infringement action. The Court stated:

The evidence in the two actions is largely the same, and the two claims raise common issues of law and fact, including the allegedly fraudulent procurement of the subject patent, the validity and the existence *vel non* of any infringement.

**The Court went on to conclude:**

Federal Rule of Civil Procedure 13(a) requires that certain claims be asserted as counterclaims to promote judicial economy and fairness. Absent an applicable exception, the present claim should have been raised as a counterclaim under Rule 13(a). The Supreme Court in *Mercoid*, however, created an exception to Rule 13(a) that saves TII's claim.

**The Court further noted:**

Notwithstanding very little analysis by the Supreme Court, we are persuaded that the Court fully intended to say what it said and that the holding was not dicta. *Mercoid* is, therefore, binding precedent and decides the case before us.

Finally, the Court held that it (and not the Federal Circuit) had jurisdiction over an appeal from dismissal of the antitrust suit because the order consolidating it with the patent infringement suit had been rescinded prior to dismissal of the antitrust suit. *Tank Insulation International, Inc. v. Insultherm, Inc.*, 104 F.3d 83 (5th Cir. 1997).

The United States District Court for the District of Maine also held that a manufacturer's claim that a competitors' patent infringement litigation constituted an attempt to monopolize was not a compulsory counterclaim in a separate patent infringement suit. Instead, the antitrust claim was a permissive counter-claim that could be asserted in a separate action. The issue was certified for an interlocutory appeal to the First Circuit Court of Appeals because it involved a controlling question of law as to which there was substantial ground for difference of opinion. *Longwood Manufacturing Corp. v. Wheelabrator Clean Water Systems, Inc.*, 937 F. Supp. 63 (D. Me. 1996), 1996 U.S. Dist. LEXIS 14262, 20173, 20326.

**Tying, Monopolization Claims**

In a claim arising out of an industrial control equipment manufacturer's refusal to allow a repair company to buy proprietary parts that were essential to repair circuit boards used in the manufacturer's equipment, the Court of Appeals for the Sixth Circuit held that the aftermarket for circuit board parts was not the relevant antitrust market. Rather, the relevant product market for the repair company's tying and monopolization claims was the primary market for the sale of industrial control equipment.

The repair company's argument, that the defendant had monopolized the market for proprietary repair parts and had unlawfully tied the purchase of the parts to the use of the manufacturer's repair service, was based on the United States Supreme Court case, *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451 (1992). In *Kodak*, the Supreme Court held that repair parts could constitute a relevant product market, reasoning that limited pre-purchase access to information and high post-purchase switching costs allowed Kodak to exercise market power in the market for parts without damaging its ability to compete in the equipment sales market.

The Sixth Circuit reasoned that, unlike the manufacturer in *Kodak*, the defendant industrial equipment manufacturer had not instituted its restrictive parts sales policy after a substantial number of customers had bought its products and that its refusal to allow the purchase of proprietary parts was a consistently maintained and generally known policy. The Court further noted that the manufacturer had disclosed expected service costs to its customers during purchase negotiations. The Court went on to rule that the primary equipment market comprises the relevant market for purposes of both Sections 1 and 2 of the Sherman Act, and since the plaintiff had not alleged or shown that the defendant had market power in the primary equipment market, its claims must fail. *PSI Repair Services, Inc. v. Honeywell, Inc.*, 104 F.3d 811 (6th Cir. 1997).

In a suit between a computer manufacturer and a computer distributor after cancellation of the distributorship agreement between them, the Seventh Circuit Court of Appeals ruled that the manufacturer was not obligated to renew the distributorship agreement annually on the same terms. Notably, the Court further held that the manufacturer's policy of including an operating system with each of its mid-range computers was not a violation of Section 2 of the Sherman Act, regardless of whether it was a "tie-in." Judge Easterbrook, delivering the opinion, wrote:

Computer manufacturers are vigorous rivals; prices drop daily; this is one of our economy's most competitive sectors. Calling the selection of components for one's product a "tie-in" does not help to uncover practices that restrict output, drive up prices, and transfer wealth from consumers to producers.

The Court rejected the distributor's argument that *Kodak* required a finding that the computer manufacturer possessed market power in a relevant market for its own products. *Kodak*, the Court reasoned, is distinguishable as a case involving a change in policy with respect to the bundling of spare parts, a policy about which customers were not informed at the time of purchase. ("The material dispute that called for a trial was whether the change in policy enabled Kodak to extract supra-competitive profits from customers who had already purchased its machines.") Accordingly, the Court ruled that purchasers of the manufacturer's computer systems were not harmed, and there was no dangerous probability of monopoly "on the horizon." *Digital Equipment Corporation v. Uniq Digital Technologies, Inc.*, 73 F.3d 756 (7th Cir. 1996).

## *Authors*


**James C. Burling**

RETIRED PARTNER

+1 617 526 6000

**Michelle D. Miller**

RETIRED PARTNER

+1 617 526 6000

**John C. Christie Jr.**

RETIRED PARTNER

+1 202 663 6000