porterwright

Antitrust Law Alert

A Litigation Department Publication

May 2009

Donald M. Barnes
202-778-3056
dbarnes@porterwright.com

Salvatore A. Romano
202-778-3054
sromano@porterwright.com

Helen J. Kim
202-778-3020
hkim@porterwright.com

Please see our other publications at www.porterwright.com/publications.

The Emergence of Vigorous Antitrust Enforcement

After eight years of relative inactivity, it is time for the business community to dust off its antitrust compliance programs and reinvigorate its compliance efforts with a clearer and sharper view of increased and more vigorous antitrust enforcement. The significant downturn in the economy over the last year, combined with a new administration fixed upon increased regulatory oversight, translates into rigorous antitrust enforcement. Although it is difficult to predict with specificity the areas or segments of the economy that will be most impacted by increased enforcement, certain areas stand out because of the prior administration's lax enforcement and recent pronouncements by the newly installed enforcement agency leaders. The courts, however, may present potential hurdles to the anticipated increased enforcement initiatives.

The New Administration and Increased Antitrust Enforcement

The newly installed heads of the antitrust enforcement agencies, the Antitrust Division of the Department of Justice (DOJ) and the Federal Trade Commission (FTC), have provided early indicators of increased enforcement policies. Christine Varney was recently appointed Assistant Attorney General for Antitrust at the DOJ. Ms. Varney, an attorney who specialized in Internet law, previously served President Clinton as a Senior White House Adviser and later as a Federal Trade Commissioner. At her confirmation hearing before the Senate Judiciary Committee, Ms. Varney expressed disappointment with the Bush administration's lack of antitrust enforcement and stated her intentions both to reverse that trend and to collaborate more effectively with the FTC. *The Nominations of Lanny A. Breuer, Christine Anne Varney, and Tony West Before the S. Comm. on the Judiciary*, 111th Cong. (2009). She declared support for legislation to remove long-standing antitrust exemptions for the railroad industry and for the FTC's efforts to outlaw "pay-for-delay" drug settlements in which brand-name pharmaceutical companies pay other drug makers to delay the introduction of competing generic drugs. Ms. Varney also mentioned that one of her focuses in the antitrust enforcement role would be to "rebalance" economic theory by shifting from the Chicago school analysis to a newly rigorous prosecutorial economic analysis. She noted that the Chicago school analysis reflected a reluctance by the government to block mergers in the marketplace and expressed her intent to stop using economic theory to inhibit prosecution of mergers. In addition, Ms. Varney indicated that she would have challenged mergers that had been approved by the Bush administration, such as the transaction between Whirlpool and Maytag in 2006.

In a recent speech presented to the Center for American Progress, Ms. Varney set the tone of the new enforcement focus by emphasizing two basic points: (1)

there is no adequate substitute for a competitive market, particularly during times of economic distress; and (2) stronger antitrust enforcement must play a significant role in the government's response to economic crises to ensure that markets remain competitive. Christine A. Varney, Assistant Attorney General, Antitrust Division, Vigorous Antitrust Enforcement In This Challenging Era at 4 (May 11, 2009). Ms. Varney also withdrew the Section 2 Report of the prior administration, which reflected a lax approach to dealing with abuses of monopoly power. Instead, she espoused tough enforcement against exclusionary or predatory conduct by firms with monopoly or dominant market power. *Id*. at 11. She also indicated that the Division would continue criminal enforcement of price fixing and related cartel-like activity under Section 1 of the Sherman Act. *Id*. at 14-15. Merger and non-merger enforcement activity will also take place with an emphasis on high-tech and Internet-based markets. Finally, the Division will interact more frequently with other regulatory agencies to address antitrust concerns relating to agency policies and proposed regulations. Ms. Varney concluded by noting: "Antitrust must be among the frontline issues in the Government's broader response to the distressed economy." *Id*. at 19.

At the recent American Bar Association (ABA) Antitrust Spring Meeting, the newly appointed Chairman of the FTC, Jon Leibowitz, indicated that more rigorous antitrust enforcement was also part of the FTC's agenda. Chairman Leibowitz emphasized that the Commission would build on enforcement of Section 2 of the Sherman Act and Section 5 of the Federal Trade Commission Act to challenge the abuse of monopoly prices and attempts to unlawfully attain monopoly power. He also pointed out that the Commission would continue to challenge resale price maintenance programs that harm consumers and that the Commission would use all of the tools it has available to try to stop anticompetitive behavior.

In line with Chairman Liebowitz's comments, the FTC acted in a related context involving a trade association encouraging its members to develop minimum advertised pricing (MAP) policies. *In the Matter of National Association of Music Merchants (NAMM)*, Docket No. 2455 (Apr. 14, 2009). NAMM is a trade association of manufacturers, distributors, and dealers of musical instruments. In its complaint, the FTC alleged that NAMM sponsored meetings and programs where it steered the discussion toward the exchange of information on competitively sensitive subjects, such as prices, margins, MAP policies, and overall strategies for raising retail prices. The FTC contended that these actions crossed the line between legitimate trade association activities and conduct that had the likely effect of harming competition and consumers. As part of the final consent order (FTC order) settling the charges, NAMM agreed to cease coordinating the exchange of price information among its members, to stop aiding musical instrument manufacturers or retailers from forming anticompetitive agreements, and to begin implementing an antitrust compliance program. The FTC order required that the compliance program include: (1) the appointment and maintenance of an Antitrust Compliance Officer, who would serve as antitrust counsel for three years; (2) annual in-person training for NAMM's board of directors and training for the association's employees and agents regarding their obligations under the FTC order as well as a review of applicable antitrust laws; (3) the Antitrust Compliance Officer's review and written approval before distribution of all written material and speeches by any of NAMM's board of directors, employees, or agents that relate to price terms, margins, profits, MAP policies, or resale price maintenance policies for musical products or any materials distributed at the board of directors or executive committee meetings; (4) establishment of a procedure allowing NAMM's members, officers, directors, employees, and agents to confidentially report violations of the FTC order or any applicable antitrust laws to the Antitrust Compliance Officer and antitrust counsel; and (5) implementation of disciplinary measures for any members, officers, directors, employees, or agents of NAMM who fail to comply fully with the FTC order.

The FTC has also announced an agenda for a series of workshops to consider the issues raised by the *Leegin* decision, including economic analysis of the effects of resale price maintenance (RPM), the history of the use of RPM in the United States, and application of the rule-of-reason analysis.

Congressional Initiatives

The antitrust enforcement agencies can expect backing by Congress as it, too, has begun to focus on the need for greater antitrust enforcement. Since 2007, when the U.S. Supreme Court handed down its decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 127 S. Ct. 2705 (2007), that ruling has faced increasing criticism as having gone too far in limiting consumer protection under the antitrust laws. *Leegin* overturned the Court's *per se* rule, established under the almost century-old precedent in *Dr. Miles Medical Co. v. John D. Park & Sons, Co.*, 220 U.S. 272 (1911), barring minimum resale price agreements on their face.

Those disapproving of the Court's decisions have ranged from FTC members to state attorneys general to a coalition of retailers and consumer advocates who argue that the decision, which allows manufacturers to set minimum resale

prices, has led to higher prices for consumers. In December 2008, this coalition held a meeting, sponsored by the American Antitrust Institute, urging Congress and regulators to overturn the decision. At the conference, FTC Commissioner Pamela Jones-Harbour criticized the Supreme Court's *Leegin* decision and urged legislation to overturn it.

In response to these and other concerns, the Senate Committee on the Judiciary's Subcommittee on Antitrust, Competition Policy and Consumer Rights (Senate Judiciary Antitrust Subcommittee) has announced that part of the 111th Congress's agenda will be to implement tougher pricing and competition policies. The subcommittee plans to address: (1) strengthening antitrust enforcement in certain industries, including railroads, crude oil and gasoline markets, pharmaceutical companies, and airlines; (2) enacting new regulations for corporate consolidations for companies, especially in the banking and financial sector, who receive "bailout" funds; (3) commissioning a study on the effect of agricultural consolidation on food prices to be completed in 2009; and (4) significantly, considering whether the relaxed minimum resale price regulations in *Leegin* should be overturned.

In January 2009, Senator Herb Kohl (D-WI) re-introduced legislation that would restore the *per se* bar against minimum resale prices and overturn the Supreme Court decision in *Leegin*. The bill, entitled Discount Pricing Consumer Protection Act, S. 148, originally floundered in committee. The current version is designed "to restore the rule that agreements between manufacturers and retailers, distributors, or wholesalers to set the minimum price below which the manufacturer's product or service cannot be sold violates the Sherman Act." *Id*. The bill states that abandonment of the *per se* rule against resale price maintenance will "likely lead to higher prices paid by consumers and substantially harm the ability of discount retail stores to compete." *Id*. at § 2(a).

In announcing the active agenda for the subcommittee, Senator Kohl and Senator Orrin Hatch (R-UT), respectively the chairman and ranking member of the subcommittee, emphasized that the current economic climate requires even more vigorous enforcement of the antitrust laws to protect competition. They noted that the goal of the subcommittee was to ensure that consumers receive the benefits of dynamic competition, including lower prices and improved quality and innovation.

Other legislative initiatives are also percolating. Two members of the U.S. House of Representatives, Gene Taylor (D-MS) and Peter DeFazio (D-OR), have introduced legislation to remove the federal antitrust exemption for the insurance industry, which the representatives claim was partly responsible for allowing the insurance company American International Group Inc. (AIG) to become "too big to fail."

The bill, entitled Insurance Industry Competition Act of 2009, H.R. 1583, would amend the McCarren-Ferguson Act of 1945, 15 U.S.C. § 1011, *et seq*., which gives the insurance industry a limited exemption from federal regulations under the Federal Trade Commission Act and allows insurance companies to share related information through practices such as cooperative ratemaking efforts and to fix prices and allocate markets. The Insurance Industry Competition Act would also allow the DOJ and FTC to address unfair methods of competition in the insurance business. The bill was introduced in 2007 but failed to make it out of committee.

At the state level, Maryland has become the first to amend its antitrust law to reject the rule–of-reason approach articulated in *Leegin* and has, instead, established that minimum resale price agreements are *per se* illegal. The amendment to Maryland Commercial Code § 11-204 (1992) provides that "a contract, combination, or conspiracy that establishes a minimum price below which a retailer, wholesaler, or distributor may not sell a commodity or service is an unreasonable restraint of trade or commerce" and will take effect October 1, 2009. The law covers transactions that take place in-state as well as those involving out-of-state retailers from whom consumers in Maryland purchase items on the Internet.

Supreme Court Pushback

Although the enforcement agencies and Congress are moving in the direction of increased and more vigorous antitrust enforcement, the courts, particularly the Supreme Court, appear to be putting the brakes on some of these initiatives. Recently, the Supreme Court took a distinctly negative approach toward Section 2 enforcement.

In particular, the Court reversed the Ninth Circuit Court of Appeals and held that price-squeeze claims cannot be brought under the antitrust laws where the defendant has no clear antitrust duty to deal with the competitors at wholesale. *Pacific Bell Telephone Co. d/b/a AT&T California, et al. v. LinkLine Communications., et al.*, 129 S. Ct. 1109 (2008).

The Court's ruling overturned federal court precedent that had been in place since 1945 when *United States v. Aluminum Co. of America*, 148 F-2d 416 (2nd Cir. 1945) was decided. The *Alcoa* decision first established antitrust

liability for price squeezing against dominant vertically integrated firms. Price squeezing occurs when a vertically integrated firm, which sells inputs at wholesale as well as finished goods or services at retail, raises the wholesale price of goods while at the same time cutting the price it charges for its own finished goods at retail. This has the effect of squeezing the profit margins of any rivals in the wholesale segment of the market. The competitors are then forced to purchase inputs at the higher wholesale prices and compete for customers against the supplier's lower prices. *Alcoa* held that price-squeeze claims were viable under a four-part test where: (1) there is monopoly power; (2) the monopolist charges a wholesale price that is higher than a "fair price"; (3) the monopolist competes downstream (that is, is vertically integrated); and (4) the monopolist's downstream or retail price is so low that competitors cannot match it and still earn "a living profit."

In the 2008 *LinkLine* case, AT&T had been required by the Federal Communications Commission (FCC) to provide Internet service providers (ISP) with access to its networks and equipment since 2005. Internet service provider LinkLine Communications Inc. (LinkLine) and three other ISPs alleged that an AT&T subsidiary charged unreasonable wholesale prices for access to the company's phone networks and engaged in a price squeeze aimed at driving out competition in the market for digital subscriber line (DSL) service. LinkLine further contended that, at times, AT&T's price to retail customers was below the wholesale price for DSL access charged to LinkLine. The Ninth Circuit ruled that AT&T had been setting its wholesale prices so high that ISPs could not compete and had engaged in price squeezing in violation of Section 2 of the Sherman Antitrust Act. *LinkLine Communications Inc., et al. v. Pacific Bell Internet Services, et al*., 503 F.3d 876 (9th Cir. 2007).

The Supreme Court, however, ruled that AT&T was not required to charge more market-friendly wholesale prices and could only be challenged if the retail prices charged by the company met the predatory pricing prohibitions enumerated in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). The Court also added that, under *Verizon Communications Inc. v. Law Offices of Curtis v. Trinko*, 540 U.S. 398 (2004), AT&T did not have an independent antitrust duty to deal with its competitors and could not be liable to ISPs for failing to provide a sufficient level of network service to them. As a result, the Supreme Court has virtually precluded viable price-squeeze claims brought under the antitrust laws. This decision, as well as *Trinko*, indicates a contrary approach on the part of the highest court in the land to permit the antitrust laws to aggressively deal with the abuse of monopoly or dominant firm market power as contemplated by the newly-installed enforcement heads.

Conclusion

Although the antitrust enforcement agencies may need to overcome potential court resistance, the business community should re-evaluate its antitrust compliance efforts to conform to the newly focused antitrust policies. Otherwise, it risks enforcement agency scrutiny and challenge.

Porter Wright Morris & Arthur LLP
www.porterwright.com

Cincinnati, Ohio
800-582-5813
Cleveland, Ohio
800-824-1980
Columbus, Ohio
800-533-2794
Dayton, Ohio
800-533-4434
Naples, Florida
800-876-7962
Washington, DC
800-456-7962