ABA SECTION OF

ANTITRUST LAW

Promoting Competition Protecting Consumers

Summer 2017 Issue

Transportation, Energy & Antitrust

A publication of the Transportation and Energy Industries Committee of the Section of Antitrust Law, American Bar Association

Message from the Chair

Welcome to the Summer 2017 edition of the Transportation and Energy Industries Committee's Newsletter. On behalf of the entire Committee I would like to thank you for your participation and welcome you to sit back and enjoy the content we

hope to provide, or – if you have the interest and energy – to contribute actively to the dialogue and work of the Committee. Obviously we are also eager to hear from you about how we might contribute more usefully to your practice – please reach out to any of us with your ideas or preferences.

Turning to this edition of our Newsletter, we are proud to present four full-length articles that we hope will be of interest. In the first, Matthew J. Piehl and Daniel S. Graulich of Hogan Lovells discuss the implications of the district court decision in In re Delta/AirTran Baggage Fee Litigation granting summary judgment against the plaintiffs' claimed conspiracy claims, largely predicated on earnings call statements by the two airlines. Shifting focus to energy markets, Shaun Ledgerwood and Jeremy Verlinda of The Brattle Group examine antitrust and other theories of liability advanced in the recent *Brent* and *Merced* cases against alleged "manipulation" of market indices in petroleum and electricity markets; and Andrea Asoni and Yianis Sarafidis of Charles River Associates examine two economic tools – the so-called "mHHI" and "mGUPPI" – that may be useful in evaluating partial acquisitions in the energy sector. Finally, drawing our attention south of the border, Gerardo Calderon of Baker & McKenzie Abogados in Mexico City examines COFECE's (the Mexican competition authority) recent heightened focus on antitrust issues in the transport and energy sectors, and what we might expect going forward.

Next, we offer brief summaries of the three sessions the TEI Committee sponsored at this year's Antitrust Section Spring Meeting: "*Competition and Consumer Policy in the Green Economy*;" "*Competition and Consumer Law Issues with Customer Profiling*;" and "*HSR Exemptions: Running Out of Gas?*" Each of these sessions was well attended and well received, and we express again our appreciation to the presenters and session chairs who made them happen

Finally, as in past issues, we provide a (non-comprehensive) synopsis of some of the matters we have been following in the energy and transportation sectors and a few that will have our attention in the coming year.

Meanwhile, we are busy working on several programming offerings in the coming year, which will dovetail with important Section-wide programming, in particular:

- The Merger Practice Workshop - September 28, 2017 in Washington, D.C.
- Antitrust Fall Forum - November 16, 2017 in Washington, D.C.

Please stay tuned for more information about our brownbags and other programming, and in the meantime, happy reading!

David L. Meyer
dmeyer@mofo.com
Chair, Transportation and Energy Industries Committee
2016-2017

When Talk is "Cheap": Antitrust Risk for Earnings Calls After *In re Delta/AirTran Baggage Fee Litigation*

By Matthew J. Piehl and Daniel S. Graulich[1]

The antitrust laws clearly prohibit agreements between competitors to fix prices. But determining whether an "agreement" exists is often a matter of contentious debate. While many typically envision conversations in the proverbial private, smoke-filled back-room, courts have shown an increased willingness to consider whether statements made by high-level executives in public forums may also point to illicit collusion. The long-running multi-district litigation involving Delta Air Lines, Inc. ("Delta") and AirTran Airways, Inc. ("AirTran"), despite a summary judgment win for the defendants, highlights the less commonly understood antitrust risks associated with public statements and corporate communications.

On March 28, 2017, the United States District Court for the Northern District of Georgia granted summary judgment in favor of Delta and AirTran, rejecting claims that the competing airlines violated Section 1 of the Sherman Act by colluding to institute a fee on a passenger's first checked bag.[2] The court's lengthy ruling concluded that the evidence did not tend to exclude the possibility that the companies acted in their independent economic interests and therefore that a reasonable jury could not infer the existence of a conspiracy to fix prices.[3] Of particular relevance to corporate executives and antitrust counsel is the district court's comprehensive discussion of whether public statements constitute illicit, conspiratorial signals, particularly where such statements reference rivals or competitively sensitive[4] issues.

Background on the Companies' Communications

The district court's opinion culminates a saga that began when non-legacy, low-cost air carriers first introduced a fee for passengers' checked luggage in 2006.[5] In early 2008, the legacy airlines followed suit, introducing fees for the second checked bag. Delta announced on March 18, 2008, that it would implement a $25 fee for the second checked bag as of May 1. AirTran followed suit on April 11, announcing a fee of up to $20 beginning May 15. The legacy airlines quickly moved

---

[1] Matthew J. Piehl is a Senior Associate in the Minneapolis office of Hogan Lovells US LLP. Daniel S. Graulich is an Associate in the Washington, D.C. office of Hogan Lovells US LLP.
[2] *In re Delta/AirTran Baggage Fee Antitrust Litigation*, Civil Action No. 1:09-md-02089 (N.D. Ga.).
[3] *Id.* at 94.
[4] "Competitively sensitive information" refers to proprietary, confidential or other "information relating to pricing or pricing strategies, costs, revenues, profits, margins, output, business or strategic plans, marketing, advertising, promotion, or research and development." See e.g. *In the Matter of Bosley, Inc., Aderans America Holdings, Inc., and Aderans Co., Ltd.*, Docket No. C-4404, Complaint.
[5] As explained by the court, "legacy carriers" include Delta, United Airlines, and American Airlines, companies that operated interstate routes "at the time of airline deregulation in 1978." In general, airlines that first operated after 1978 are "low-cost carriers," a "catchall name for post-deregulation new entry and, in fact, [a] diverse [group of] airlines and heterogeneous strategies." *In re Delta/AirTran.* at 2-3 (internal citations omitted).

to first-checked bag fees later that year, and, by October 8, 2008, the only legacy carriers without a first-bag fee were Delta and Alaska Airlines. AirTran was one of the few low-cost carriers without such a fee.

Throughout the summer of 2008, Delta and AirTran separately engaged in extensive internal discussions regarding whether to institute a first-checked bag fee. And each company's public statements echoed their cautious approach to adding the fee. In June 2008, AirTran's CEO stated at a Merrill Lynch transportation conference that AirTran was "pretty uncomfortable" implementing a first-checked bag fee while maintaining competition in Atlanta against Delta, who did not yet have such a fee.[6] On an earnings call in July 2008, Delta reported that it had "no plans to implement" a first-checked bag fee "but would 'continue to study' the question."[7]

On October 15, 2008, in its third-quarter earnings call, Delta stated that "a la carte pricing is where we need to go as an industry" and that its pending merger with Northwest Airlines—which charged a first-checked bag fee—would give it "another opportunity to look again" at implementing an additional baggage fee.[8] AirTran held its third-quarter earnings call eight days later. In response to a question regarding first-checked bag fees, AirTran's representative responded that it would "prefer to be a follower . . . rather than a leader," especially since its main competitor in Atlanta (presumably referencing Delta)[9] did not yet charge such a fee. Responding to a follow-up inquiry, AirTran confirmed that it would "strongly consider" a first-checked bag fee if its competition instituted one.[10]

On November 5, 2008, Delta announced a $15 fee for the first checked bag. AirTran announced a matching fee on November 12. Lawsuits alleging an unlawful collusion in violation of Section 1 of the Sherman Act followed soon thereafter.

Unilateral Public Statements and Competitive Effects

As a general rule, antitrust law favors the disclosure of accurate information.[11] The dissemination of information is typically viewed as being procompetitive, as markets operate more efficiently when market participants convey and make decisions based on relevant information.[12] For example, providing information about a future pricing decision may allow customers to better plan future purchases and help companies better respond to investor concerns, which can in turn improve company performance by holding managers accountable.

---

[6] *Id.* at 13.
[7] *Id.* at 10.
[8] *Id.* at 19.
[9] Delta is headquartered in Atlanta and has its largest hub at Atlanta's Hartsfield-Jackson International Airport. AirTran maintained its principal hub in Atlanta until 2014, when it ceased operations several years after having been acquired by Southwest Airlines.
[10] *Id.* at 20.
[11] *See e.g. Maple Flooring Manufacturers' Assn. v. United States*, 268 U.S. 563 (1925).
[12] *See e.g. E.I. DuPont de Nemours & Co. v. Federal Trade Commission*, 729 F.2d 128, 134 (2d Cir. 1984).

However, unilateral information disclosures that are public in nature also can create antitrust risk. For example, when companies know that their competitors actively monitor one another's decisions, a unilateral disclosure of a price strategy, under certain circumstances, can "signal" to competitors how a given company intends to act. When such communications indicate that the company's strategy is contingent on a competitor following suit, these communications may allow companies effectively to coordinate their pricing strategies. To the extent such "signaling" represents a credible commitment by the firm to engage in a specific course of action and can be said to affect materially the decision of a competitor, such behavior may be characterized as an "invitation to collude"[13] that, if accepted, will lead to higher prices. Note, however, that while plaintiffs must show that a competitor assented to and acted upon a defendant's "invitation to collude" in order to bring a claim under Section 1 of the Sherman Act, the FTC can bring claims against standalone "invitations to collude" under Section 5 of the FTC Act.

The practical difficulty, as alluded to in the district court's discussion of the various economists' expert opinions, is that it is not often apparent whether public statements can be said to constitute a credible commitment or merely "cheap talk."[14] In economics, "cheap talk" refers to non-binding forward looking statements. To the extent such statements reflect uncertainty or demonstrate reluctance to commit to a particular strategy, such statements are less likely to influence a competitor's strategic choices or facilitate an "agreement." The signaling-cheap talk distinction continues to be a subject of much debate among economists and game theorists.

The Legal Standard for Inferring an "Agreement"

To survive summary judgment under Section 1 of the Sherman Act, plaintiffs "must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently."[15] In other words, plaintiffs must demonstrate that it is reasonable to infer an illicit conspiracy took place and that the defendants' actions are not solely attributable to independent action or "conscious parallelism."[16]

As explained by the district court, the challenge for government enforcers and courts is to "discern when lawful coordination crosses the line and becomes unlawful collusion."[17] This is because, from a legal (and economic) perspective, it is only the agreement, and not the underlying conduct standing alone, that is at issue. More specifically, it is only the agreement between the parties—the so-called "meeting of the minds"—to fix prices that is considered illegal; the underlying

[13] The Federal Trade Commission ("FTC") has defined an "invitation to collude" to mean, more generally, an "improper communication from a firm to an actual or potential competitor that the firm is ready and willing to coordinate on price or output or other important terms of competition". *In re Fortiline, LLC a N.C. Ltd. Liab. Co.*, File No. 151-0000, 2016 WL 4379041, at *11 (F.T.C. Aug. 9, 2016).

[14] *In re Delta/AirTran* at 49-51.

[15] *Id.* at 57 (citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986) (quoting *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984)).

[16] The court defined "conscious parallelism" as "synchronous pricing and related behaviors that 'are the product of a rational, independent calculus by each member of an oligopoly'". *In re Delta/AirTran* at 56 (citing *Williamson Oil Co., Inc. v. Philip Morris USA*, 346 F.3d 1287, 1299 (11th Cir. 2003)).

[17] *Id.* at 56.

actions of the parties affecting prices may not be unlawful "even when [such actions] result in the setting of prices 'at a profit-maximizing, supracompetitive level.'"[18] For this reason, plaintiffs must put forth evidence that leans to an illegal conspiracy rather than prices reached through firms' independent decision-making.

The Court's Decision Relating to AirTran's Public Statements

The district court in *In re Delta/AirTran* evaluated plaintiffs' arguments through a three-step approach: (1) the plaintiff must establish a pattern of parallel behavior, or "conscious parallelism," (2) the plaintiff must demonstrate the existence of one or more "plus factors" that tend to exclude the possibility the alleged conspirators acted independently, and (3) the defendant may rebut the inference of collusion by presenting evidence that it acted independently.[19]

After showing that AirTran and Delta had instituted baggage fees within months of one another, the plaintiffs argued that two sets of communications were particularly key in allowing the companies to coordinate their decisions. First, plaintiffs argued that statements made by an AirTran executive in a Q&A during the company's October 2008 third quarter earnings call constituted an invitation to collude and should be considered as a "plus factor" since the answer referred to the company's "largest competitor" in Atlanta in discussing the company's strategy related to baggage fees.[20] Second, the plaintiffs highlighted the fact that the AirTran executive's statement directly referenced competition with Delta in Atlanta as the reason it would not institute a fee during at an investor conference in June 2008.[21]

Holding for the defendants, the court fist rejected the plaintiff's contention that statements made by an AirTran executive during an earnings call constituted an "invitation to collude." The court noted that corporate communications containing "the type of information companies legitimately convey to their shareholders" are typically not invitations to collude unless, perhaps, the communication contained detailed, sensitive information with no public purpose.[22] As an example, the Court cited direct correspondence between high level executives at competing companies that exchanged internal pricing memos.[23] At the same time, the court then went on to note that it was "significant, though not dispositive, [that] in the context of antitrust conspiracy claims have almost universally been private communications, not public disclosures."[24] By contrast, baggage fees were a general topic of interest to the airline industry at the time, as evidenced by the fact that the topic of baggage fees had been widely discussed by the press and the fact that such fees were discussed during other airlines' earnings calls that same year.[25] The court then went on to note two additional facts that cut against the Plaintiff's argument: (1) the implementation of the baggage fee was part of an industry wide trend in which the

---

[18] *Id.* at 56 (quoting *Williamson Oil*, 346 F.3d at 1299).
[19] *Id.* at 59. (quoting *Williamson Oil*, 346 F.3d at 1301 (internal citation omitted)).
[20] *Id.* at 66.
[21] *Id.* at 75.
[22] *Id.* at 69.
[23] *Id.* at 70.
[24] *Id.*
[25] *Id.* at 71.

defendants were not the first movers, and (2) AirTran had produced evidence that it was not firmly committed to implementing a baggage fee at the time it made the call.[26]

Since there was no invitation to collude, the court then determined that AirTran's statements during the investor conference did not give rise to an agreement. The Plaintiffs had failed to proffer evidence that Delta actually acted on the AirTran executive's statement or any evidence this executive otherwise directly communicated with anybody involved in Delta's first-bag fee decision.[27] Based on the lack of evidence to the contrary, the court concluded that defendants' communications "are perfectly consistent with conscious parallelism by members of an oligopoly."[28]

Practical Considerations

All communications in an open forum, whether an earnings call with shareholders or an offhand comment at an investor conference, may create antitrust risk and create a public record that can (and will) be used by future plaintiffs. What sounds like a mixed message or "cheap talk" can quickly turn into a "signal" seized upon by potential plaintiffs looking to bring an antitrust suit. While Delta and AirTran ultimately prevailed at summary judgment, the companies lost on their motion to dismiss and a motion to deny class certification, resulting in years of litigation. The companies were also subject to extensive and costly discovery and faced significant damages if the plaintiffs had succeeded.

The district court's opinion therefore provides key guideposts for companies in all industries, but especially companies navigating public statements in highly concentrated markets. Oligopolistic markets generally present a greater risk for public statements since, as the court put it, these companies "watch each other like hawks" in order to make strategic decisions. As a result, such communications are more likely to have a material effect on near-term business plans and tend to facilitate consciously parallel activities given the characteristics that define these markets (i.e. few competitors, high market shares, product homogeneity, similar cost structure across firms, and high barriers to entry).

While certain facts like industry structure are beyond an individual corporation's control, a company should be cognizant of these conditions and should tailor public statements to avoid raising antitrust risk. With *In re Delta/AirTran* in mind, companies and antitrust counsel may consider the following:

- *Consider the nature and quantity of the information disclosed to the public.* Public disclosures should contain only relevant information for a public audience and not reveal highly sensitive or specific information that would not typically be provided to shareholders or potential investors. As the district court stated, "[C]ourts have refused to construe corporate

[26] *Id* at 74-75.
[27] *Id.* at 78.
[28] .*Id.* at 79.

communications as invitations to collude where the communications contain 'the type of information companies legitimately convey to their shareholders,' instead restricting such findings to cases involving 'far more detailed communications with no public purpose.'"[29] By contrast, disclosing extensive information about pricing (particularly future pricing), output, capacity cuts or expansions, and major costs is more likely to raise questions from regulators and private plaintiffs.

- *Evaluate industry trends and timing prior to making public statements.* If several industry participants have already moved in one direction, a public announcement in a similar direction is less likely to be construed as a market signal—particularly on a topic that has already been the subject of significant press coverage. Conversely, if a company is viewed as a first-mover or leader, statements by the company considering a potential business decision may be given more scrutiny. Delta and AirTran bolstered their case by pointing out that most legacy carriers and low-cost carriers had already instituted a first-checked bag fee and showing that the both the investment community and business press was paying close attention to the issue.

- *Be cautious to the context and specificity with which information is shared, and communicate a flexible business approach where possible.* The more committal and specific the information disclosed appears, the easier it is for a plaintiff to argue that a company is "signaling" an intended course of conduct and trying to influence competitors. Here, the plaintiffs pointed to the fact that AirTran referenced direct competition with Delta in Atlanta as evidence that AirTran had taken active steps at the time to charge for the first bag. It was only once AirTran had produced evidence prior to summary judgment that showed it had not committed to a specific strategy at the time that led the court ultimately to conclude that AirTran's statements were not an invitation to collude. By contrast, Delta's public statements were more equivocal, for example, acknowledging in its July 2008 earnings that while other airlines had moved ahead in charging fees it had "no plans to implement" a first bag fee but would "continue to study" the issue.

- *Resist references to specific rivals and opining on how others firms or the "industry" should act on a going forward basis.* Plaintiffs pointed to AirTran's reference in its third-quarter earnings call in October 2008 to "our largest competitor in Atlanta" as a targeted signal to Delta that AirTran was prepared to institute a first-checked bag fee as soon as Delta began charging passengers such fee. Plaintiffs had also pointed to statements made during a Delta earnings call in April 2008 that referenced the need for "the industry" to address excess capacity issues. These arguments would have been harder had the companies done more to limit discussion to addressing broader economic forces and how these trends affect their own respective business decisions. Plaintiffs may find less to bolster their arguments if companies

[29] *Id*. at 69 (quoting *Holiday Wholesale Grocery v. Philip Morris Inc.*, 231 F. Supp. 2d 1253, 1276 (N.D. Ga. 2002)).

discuss what they are doing individually and avoid references to what the "industry should do."

- *Make the business case for the disclosure.* Internal documentation of analyses and communications regarding the business decision prior to public disclosure may help counteract an argument that the public communication was designed to signal competitors. Delta helped its own case by pointing to a trail of internal memoranda and analyses on the baggage fee issue, demonstrating that the company was engaged on the matter regardless of any supposed collusive activities of competitors. In addition, companies generally have a stronger case for making public statements when discussing topics that are in the public eye and already of general interest to consumers, investors, and other market participants.

Conclusion

Though Delta and AirTran won summary judgment, the long history of the baggage fee litigation and the district court's opinion make clear that public statements can present antitrust risk. The opinion, however, also provides several guideposts to help companies avoid alleged signals that will be quoted in a future antitrust complaint. Companies that stray from "cheap talk" may end up in expensive litigation.

Market Manipulation in Energy-Related Markets

By Shaun Ledgerwood and Jeremy Verlinda[30]

Introduction

A market manipulation occurs when an economically rational actor deliberately uses a false or fraudulent act to cause demand or supply to deviate from their economic fundamentals in order to benefit from that deviation. The act can take the form of an output restriction (an uneconomic act of withholding), output expansion (through intentionally uneconomic purchases or sales) or can be purely information-based. Such deviations can result in unjustifiable transfers of wealth and inefficient long-term investments. Market manipulation also undermines trust in the prices that guide the economy and can reduce economic efficiency even after the manipulative behavior has stopped.

This article reviews two recent energy-related manipulation cases where the plaintiffs claimed antitrust harms but received very different outcomes following Motions to Dismiss. The district court in the first case, involving the alleged manipulation of a benchmark for North Sea Brent Crude Oil in possible violation of the Commodity Exchange Act, Sherman Act Sections 1 and 2, and various state laws ("*Brent*"),[31] recently granted defendants' motions to dismiss each of the plaintiffs' complaints.[32] The second complaint, filed by Merced Irrigation District[33] alleging manipulation of four western power indices ("*Merced*"), saw dismissal of the alleged Sherman 1 claims, but the alleged Sherman 2 claims were allowed to proceed.[34] The rulings in these two cases contribute to a nascent but growing case law on the reach of the antitrust laws with regard to market manipulation.

Brent – Summary and Current Status

In *Brent*, two separate sets of plaintiffs have alleged that Brent crude oil producers, traders, and affiliates conspired to manipulate exchange prices for Brent crude oil and its futures and derivatives contracts. Plaintiffs allege that Defendants manipulated the Platts Dated Brent benchmark, which summarizes daily over-the-counter physical trades of Brent crude oil, by submitting fraudulent information

---

[30] Dr. Ledgerwood is a Principal with The Brattle Group specializing in the analysis and proof/disproof of market manipulation claims in energy, commodity, financial, and securities markets. Dr. Verlinda is a Senior Associate with The Brattle Group specializing in the economics of antitrust claims, focusing on issues of monopolization, criminal price fixing, and merger analysis. Drs. Ledgerwood and Verlinda work from the company's offices in Washington, D.C.

[31] In re: North Sea Brent Crude Oil Futures Litigation ("Brent"), No. 1:13-md-02475 (S.D.N.Y. 2017), Amended Consolidated Class Action Complaint.

[32] *Brent*, "Opinion and Order on Motions to Dismiss" (2017).

[33] Merced Irrigation District is an electric utility that serves 8,500 retail customers in the San Joaquin Valley of Northern California. See http://www.mid.org/about/default.html.

[34] Merced Irrigation Dist. v. Barclays Bank PLC, No. 15-cv-04878 (S.D.N.Y. 2015) ("Merced Complaint").

about those trades to Platts during the benchmarking period and engaging in "spoof orders" and "wash sales".[35] Following a similar procedural history for *Libor*,[36] *Aluminum*,[37] and other recent manipulation cases, Defendants filed motions to dismiss based principally on issues of antitrust standing.[38]

The court noted that (a) Plaintiffs do not participate directly in the physical Brent crude oil market; (b) Plaintiffs only allege that the manipulation occurred in the physical Brent crude oil market; (c) Plaintiffs participated mainly in the NYMEX and ICE Brent futures and derivatives markets; and, critically, (d) all of the Brent futures traded on NYMEX and ICE are pegged to the "ICE Brent Index", which does not incorporate the Platts Dated Brent in its calculation.[39] Consequently, although Plaintiffs alleged a market that encompassed both physical trades and the NYMEX/ICE futures and derivatives, the court concluded that Plaintiffs do not have antitrust standing because they participate neither in the direct market where the alleged manipulation occurred nor in a market that is "inextricably intertwined" with the physical market where the alleged manipulation occurred.[40]

The court's decision in *Brent* mirrors the decisions in *Aluminum* and the *Forex* end-user class actions.[41] Plaintiffs in those cases were found to lack antitrust standing on grounds that they did not participate in the market where the benchmark was manipulated.[42] However, this ruling differs factually from several other

---

[35] "Spoofing" refers to the placement of bids or offers into the market with the intent to cancel the bid or offer before execution. See *Antidisruptive Practices Authority*, Commodity Exchange Act Release No. 3038-AD96 (May 20, 2013). "Wash sales" (or, more generally, "wash trades") are purchases and sales that match each other in price, volume and time of execution such that they involve no change in beneficial ownership. The CFTC prohibition against wash trades resides in 7 U.S.C. § 6c(a) (2006).

[36] In re Libor-Based Financial Instruments Antitrust Litigation, No 1:11-md-2262-NRB (S.D.N.Y. 2012).

[37] In re Aluminum Warehousing Antitrust Litigation, Nos 1:14-cv-03116, 1:14-cv-03121, and 1:14-cv-03122 (S.D.N.Y.).

[38] Defendants also submitted motions to dismiss based on extraterritoriality claims. See *Brent* Opinion and Order on Motion to Dismiss (June 18, 2017), at 7-8. The district court has ruled that the Commodity Exchange Act claims are dismissed on grounds that they are impermissibly extraterritorial. See *Brent* Opinion and Order on Motion to Dismiss at 16.

[39] The court acknowledged that some derivatives traded on NYMEX and ICE Futures Europe incorporated Platts Dated Brent. However, because plaintiffs did not allege to buy or sell such derivatives contracts, the court found no antitrust standing in this space either. See *Brent* Opinion and Order on Motion to Dismiss at 22-23.

[40] Judge Carter dismissed Plaintiffs' combined market definition as a legal claim, not a factual one. See *Brent* Opinion and Order, at 20.

In *Aluminum*, the appellate court wrote in its opinion that "[I]n Blue Shield of Virginia v. McCready, 457 U.S. 465, 102 S.Ct. 2540, 73 L.Ed.2d 149 (1982), the Supreme Court 'carved a narrow exception to the market participant requirement for parties whose injuries are `inextricably intertwined' with the injuries of market participants' " (In re Aluminum Warehousing Antitrust Litigation, 833 F.3d 151, 157 (2d Cir. 2016) at 158, citing Am. Ad Mgmt., Inc., 190 F.3d at 1057 n.5). The court's decision in *Brent* relies on this interpretation of *McCready*.

[41] See Nypl v. JP Morgan Chase & Co.. No. 15 Civ. 9300 (LGS) (S.D.N.Y. 2017).

[42] In *Aluminum*, Plaintiffs were purchasers of physical aluminum, while Defendants allegedly manipulated warehouse storage costs for non-physically traded aluminum. The appellate court writes

antitrust-based manipulation cases where Plaintiffs have (ultimately) been found to have antitrust standing because they participate in the same market that is allegedly manipulated—see *Libor*, *Silver Fixing*,[43] and the *Forex* exchange class.[44]

Merced – Summary and Current Status

Merced Irrigation District ("MID") brought antitrust claims against Barclays Bank, PLC and four traders (collectively, "Barclays") for the alleged manipulation of price indices at four western power trading hubs over the period November 1, 2006 through December 31, 2008.[45] The lawsuit ties to an enforcement action brought by the Federal Energy Regulatory Commission ("FERC") under its anti-manipulation Rule 1c,[46] which assessed $487.9 million in disgorgement and civil penalties against the accused.[47] Barclays was found to have used uneconomic purchases and sales of power to bias index prices up or down, in benefit to much larger financial derivatives positions it held that were long or short to those indexed prices.[48]

MID's complaint sought class certification based on three antitrust claims: (1) a Section 1 claim, based on the allegation that the contracts that Barclays used to bias the relevant indices created an unreasonable restraint of trade; (2) a Section 2 claim, that Barclays acquired, maintained and exercised the monopoly power needed to profitably increase or decrease the index prices at issue; and (3) attempted monopolization under Section 2 (as an alternative to Count 2).[49] Ruling on a subsequent Motion to Dismiss, the *Merced* court dismissed the Section 1 claim, finding that the contracts allegedly used to bias the indices did not constitute agreements to restrain trade.[50] However, the Section 2 claims survived due to facts alleging direct evidence of Barclays' unilateral exercise of market power "to distort

---

"…Consumers and Commercials [Plaintiffs at issue in the appellate decision] allege…that the injuries Consumers and Commercials suffered by paying a higher Midwest Premium were "inextricably intertwined" with that scheme. This gets McCready backwards. Even assuming a plausible allegation that the defendants conspired to corrupt the primary aluminum market, the purported injuries of Consumers and Commercials were not "the very means" by which the defendants achieved that illegal end; insofar as anyone's injury could be "the very means," it would be the injury suffered by participants in the market for LME-warehouse storage…Injury to Consumers and Commercials remains collateral damage." In re Aluminum Warehousing Antitrust Litigation, 833 F.3d 151, 157 (2d Cir. 2016) at 162-163.

[43] See In re London Silver Fixing, Ltd. Antitrust Litig. ("Silver Fixing"), ___ F. Suppl. 3d ___, No. 14-MD-2573, 2016 WL 5794777 (SDNY 2016) at 10-11.

[44] See Forex, No. 13 Civ. 7789, 2016 WL 5108131, (S.D.N.Y. 2016).

[45] Merced Complaint, ¶ 1.

[46] 18 C.F.R. § 1c (2010).

[47] Barclays Bank PLC, 144 FERC ¶ 61,041 (2013), ¶ 8. The case is now under de novo review in the Eastern District of California. FERC v. Barclays Bank PLC, 2:13-cv-02093-TLN (E.D. Cal. 2013).

[48] Merced Complaint, ¶ 2.

[49] Merced Complaint, ¶¶ 126-144. MID also claimed relief under the California Business & Professions Code and the theory of unjust enrichment. *Id.*, ¶¶145-152.

[50] Merced Irrigation Dist. v. Barclays Bank PLC, No. 15-cv-04878 (S.D.N.Y. 2016) ("Merced Order on Motion to Dismiss"), pp. 31-32.

ordinary forces of supply and demand[…] through uneconomical physical trading positions[.]"[51] The case is presently awaiting a ruling on class certification.

Remaining Questions & Unresolved Issues

Antitrust law increasingly is used as the legal basis for bringing civil claims against manipulative acts,[52] particularly if no anti-manipulation laws were in place at the times the behavior occurred or when the existing manipulation laws fail to provide a cause of action. However, because none of the claims filed to date have been fully litigated, it remains unclear as to whether the transient market distortions typical of manipulative acts give rise to an actionable antitrust injury, with or without the presence of collusive behavior. This uncertainty raises several economic questions that help to determine the applicability of antitrust law to remedy injuries arising from market manipulation.

For example, does the ability to profitably manipulate a price index to benefit financial positions traded in a separate, related market but valued from that price constitute a market power abuse? Would more remote sources of recoupment tied to the index that would increase the profitability of the manipulative scheme increase the actor's alleged market power? How should intentionally uneconomic behavior be viewed under antitrust law when it is used to manipulate prices? What is the relevance of the actor's intent to this calculus? If manipulative acts executed unilaterally do not raise a viable claim under Section 2, should otherwise identical manipulative conduct with an identical effect give rise to a claim under Section 1?

At the present time, neither *Brent* nor *Merced* answers these questions, although they and other manipulation cases yet may, pending full trial. Concerning Section 1 claims, the appellate court in *Gelboim*[53] vacated Judge Buchwald's original decisions in *Libor*, concluding that allegations of horizontal price fixing of benchmarks may constitute per se antitrust violations, preserving the potential for antitrust injury in market manipulation cases alleging conspiracy. Since *Libor* and most other cases focus on conspiracies to manipulate benchmark prices, they are unlikely to illuminate questions around Section 2 monopolization.

Merced, however, may lead to guidance on unilateral market manipulation and the antitrust laws. The *Merced* court's dismissal of MID's Section 1 claim may reflect that parties transacting standardized contracts multilaterally on exchanges

---

[51] *Id.*, p. 40. MID's claim under the California Business & Professions Code also survived, but its claim of unjust enrichment was dismissed. *Id.*, pp. 45, 48.

[52] See, for example, *In re Libor-Based Financial Instruments Antitrust Litigation*, No 1:11-md-2262-NRB (S.D.N.Y. 2012) (alleged manipulation of Libor); *In re Foreign Exch. Benchmark Rates Antitrust Litig.*, 13-cv-07789-LGS (S.D.N.Y. 2014) (alleged FOREX manipulation); *Alaska Elec. Pension Fund v. Bank of Am.*, No. 14-cv-07126 (S.D.N.Y. 2014) (alleged manipulation of ISDAfix); and *In re Zinc Antitrust Litig.*, No. 14-cv-3728 (S.D.N.Y. 2016) (order dismissing Clayton Act claims but allowing the remaining Sherman 2 to proceed against an alleged zinc warehousing manipulation).

[53] Gelboim v. Bank of Am. Corp. ("Gelboim"), 823 F.3d 759, 770 (2d Cir. 2016), cert. denied, 137 S.Ct. 814 (2017). The court remanded to the district court the question of further antitrust standing based on whether Plaintiffs are "efficient enforcers" of the antitrust laws.

trade will typically have no communication with their direct counterparties.[54] However, in addressing whether manipulative acts could give rise to an antitrust injury, the court reasoned that “Merced has pled an antitrust injury causally linked to Barclays’ practices: it is a purchaser of electricity on the daily markets in which it alleges it paid higher supra-competitive prices or received lower sub-competitive prices as a result of Barclays' rate-manipulation.”[55] Finding that “[t]his is an injury ‘of the type the antitrust laws were intended to prevent’,”[56] the court allowed MID’s Section 2 claims to survive, possibly opening the door for antitrust to take a broader role in civil claims brought against unilaterally-executed manipulative behavior.

---

[54] This is especially true when the party’s sales or purchases are intentionally-uneconomic, for the counterparty then benefits from the exchange by (respectively) paying or receiving a favorable price.

[55] Merced Order on Motion to Dismiss, pp 13-14.

[56] *Id.*, p. 14, citing *Brunswick Corp. v. Pueblo Bowl-0-Mat, Inc.*, 429 U.S. 477, 488 (1977).

Economic Tools for Gauging the Competitive Effects of Partial Acquisitions in the Energy Sector

By Andrea Asoni and Yianis Sarafidis[57]

I. Introduction

Joint ventures and other joint ownership relationships are prevalent in the energy sector. For example, companies may collectively own a pipeline that is used to transport the natural gas that they produce or oil exploration companies may jointly work to develop a new oil field. As a result, mergers in this sector often involve the acquisition of minority positions, referred to as "partial acquisitions." While partial acquisitions do not completely eliminate competition between the merging parties, they have the potential to change the incentives of the merging parties and harm competition, and thus are routinely reviewed by the U.S. antitrust agencies. In fact, under certain conditions, a partial acquisition might be predicted to lead to worse competitive outcomes than a full merger, as discussed in the following sections. The two economic tools discussed hereafter, the modified HHI and the modified GUPPI, are key to understand the effects of partial acquisitions on the incentives of the merging parties, on prices, and other aspects of competition.

Two recent examples are the FTC's review of the *Enbridge/Spectra* merger and of the acquisition of *The Williams Companies* by *Energy Transfer Equity* ("ETE"). The review of the *Enbridge/Spectra* merger was concerned with a competitive overlap in the transportation of natural gas in three production areas off the coast of Louisiana: *Enbridge* was the sole owner of the Walker Ridge Pipeline, while *Spectra* indirectly owned a 40% interest in the nearby Discovery Pipeline. The review of *ETE/Williams* was concerned with a competitive overlap in firm (i.e., guaranteed) capacity to deliver natural gas in Florida between Florida Gas Transmission ("FGT") and Gulfstream, two pipeline operators. *ETE* owned a 50% interest in FGT, while *Williams* owned a 50% interest in Gulfstream. In both cases, the FTC investigated, among other things, the post-merger firms' ability to influence the firm in which it holds a minority position and how the respective transactions would alter the parties' incentives to compete.

The prevalence of partially-owned midstream operations[58] and their implications for merger analysis also was recently discussed by John R. Seward in the Winter 2016-2017 issue of this newsletter. Seward noted that "in examining areas of overlap, the parties will need to account for not only wholly-owned operations, but also partially-owned operations. This is particularly pertinent to

---

[57] Andrea Asoni is an Associate Principal and Yianis Sarafidis is a Vice President in the Competition practice in the Washington office of Charles River Associates. The views expressed herein are the views and opinions of the authors and do not reflect or represent the views of Charles River Associates.

[58] For example, the gathering, processing, transportation, storage, and wholesale marketing of oil and gas.

midstream deals because pipelines are commonly owned through a joint venture structure."[59]

In light of the prevalence of partially-owned and joint-ventures operations in the energy sector, in this article we discuss two economic tools used by economists, including those at the antitrust agencies, to gauge the competitive effects of partial acquisitions: (1) the modified Herfindahl Hirschman Index ("HHI") and (2) the modified Gross Upward Pricing Pressure Index ("GUPPI"). The modified HHI ("mHHI") and the modified GUPPI ("mGUPPI") generalize their traditional counterparts (the HHI[60] and GUPPI,[61] respectively) to account for partial ownership relationships between market participants. The mHHI serves as a tool for measuring market concentration and the change in market concentration induced by a merger, as is the traditional HHI when firms are wholly-owned. As such, it is used in the context of a structural analysis of a merger. The mGUPPI serves as a tool for scoring the unilateral effects of a merger and, as such, it is used in the context of a competitive effects analysis, as is the traditional GUPPI when firms are wholly-owned. Both the mHHI and the mGUPPI (like their traditional counterparts) are meant to be used as screens early on in a merger investigation and cannot substitute for a more complete and thorough economic analysis of the likely competitive effects of a merger.

This article is intended to illustrate the intuition behind these two indices and, in turn, open a window on how the economists at the Agencies may use these tools to analyze partial acquisitions and joint ventures.

II. The Modified HHI ("mHHI")

The traditional HHI is the most widely accepted methodology for measuring market concentration. It is calculated as the sum of the squares of the market share of each market participant. For example, if a market consists of four firms each with a 25% share, the HHI would be equal to $25^2 + 25^2 + 25^2 + 25^2 = 2{,}500$. In merger analysis, antitrust agencies consider the absolute post-merger HHI and the change in the HHI (referred to as the "delta HHI") resulting from the merger. Returning to our earlier example, if two firms in that market merged, then the post-merger HHI would be $50^2 + 25^2 + 25^2 = 3{,}750$, with a delta HHI of 1,250 (= 3,750 – 2,500). In general, if the change in the HHI resulting from the merger is relatively small, or if the post-merger HHI is low, then a merger normally is deemed to be unlikely to have any adverse competitive effects.[62]

---

[59] John R. Seward, "With the Midstream Industry Ripe for Consolidation, Firms Must Remain Mindful of Potential Antitrust Concerns as they Evaluate Prospective Deals" Transportation, Energy, & Antitrust. Winter 2016-2017. Page 9.

[60] HHI is discussed in Section 2 *infra*.

[61] GUPPI is discussed in Section 3 *infra*.

[62] Notice that the delta HHI is equal to two times the product of the merging firms' market shares that is 2 x 25 x 25 = 1,250. This is a general property that extends beyond this example when firms are wholly-owned. As we shall see below, when firms are partially-owned, the delta HHI can be more or less than two times the product of the merging firms' market shares. That is, a partial merger may increase market concentration by more than the full merger.

The mHHI is a generalization of the traditional HHI that accounts for partial cross-ownerships among the market participants.[63] To calculate the mHHI one needs to know: (1) the market shares of the various market participants (as for the traditional HHI), (2) the ownership (*i.e.*, financial) interest that each owner has in the various firms in the market, and (3) the degree of influence (or partial control) that each owner has over the competitive decisions (e.g., price, quantity, advertising, innovation) of the firms that are partially owned.

A. The underpinnings of the HHI and the mHHI

The traditional HHI can be derived formally from an economic model of quantity competition commonly also known as Cournot competition. When firms are wholly-owned, it can be shown that the traditional HHI is equal to the product of (1) the elasticity of the market demand and (2) the weighted average price-cost margin of the firms in the market, using the firms' market shares as weights. Holding the elasticity of market demand constant, a higher HHI is associated with a higher average price-cost margin, which explains the intuitive appeal of the HHI: the higher the HHI, the higher the average price-cost margin and, in turn, the higher the degree of market power that firms have.

The mHHI can be derived in a similar fashion. The derivation accounts for partial cross-ownership interests among the various market participants in the following way. It is assumed that the quantity decision of firm A is controlled by a manager whose objective is to maximize the weighted average profits of the owners of firm A, taking into account the financial interests that these owners have in other market participants. The weights that the manager uses are assumed to be the degrees of influence that each owner has over the decisions of firm A. The degree of influence depends on the governance structure of the firm. In the context of the formal Cournot model, it can be shown that the mHHI is equal to the product of the market elasticity and the weighted average price-cost margin, just as the traditional HHI for the case of wholly-owned firms.

B. Examples and economic intuition for the mHHI

Returning to our prior example, suppose that firm A acquired a 50% financial interest in firm B. Suppose also that following this partial acquisition firm A would be deemed to have 60% influence over the decisions of firm B, such that the degree of influence is more than the financial interest. For example, this might be the case if firm A would control 60% of the seats on the board of directors of firm B.

---

[63] The mHHI was formulated in Steven, C. Salop and Daniel P. O'Brien, "Competitive Effects of Partial Ownership: Financial Interest and Corporate Control," 67 Antitrust Law Journal 559-614 (2000). For earlier predecessors, see also Timothy F. Bresnahan and Steven C. Salop, "Quantifying the Competitive Effects of Production Joint Ventures," 4(2) International Journal of Industrial Organization 155-175 (1986); and Robert J. Reynolds and Bruce R. Snapp, "The Competitive Effects of Partial Equity Interests and Joint Ventures," 4(2) International Journal of Industrial Organization 141-153 (1986).

Then, post-acquisition the manager of firm A will choose the quantity of firm A so as to maximize the sum of the profits of firm A (Π_A) and 50% of the profits of firm B (Π_B), that is $\Pi_A + 0.5 \times \Pi_B$. In other words, the manager of firm A behaves in a more accommodating way than pre-acquisition, but less so than in a full merger where the manager would maximize the sum of the profits of firms A and B. Likewise, post-acquisition the manager of firm B would maximize the weighted sum of the profits of the owners of firm B across all firms in the market, using as weights the degrees of influence that each owner has over firm B. That is, post-acquisition the manager of firm B would maximize: $0.4 \times (0.5 \times \Pi_B) + 0.6 \times (\Pi_A + 0.5 \times \Pi_B)$. The two terms in the parentheses are the profits of the two new owners of firm B; the manager gives 0.4 weight to the profits of the old owner of firm B and 0.6 weight to the profits of the new owner of firm B. As shown below, the change in the mHHI resulting from this partial acquisition would be 1062.5.

Therefore, in this example, the change in the mHHI (1062.5) is less than the change in the HHI in a full merger (1,250). But, this is not always the case. In general, starting from a market with wholly-owned firms, if firm A acquires a financial interest α (e.g., $\alpha = 50\%$) into firm B, which grants firm A a degree of influence β (e.g., $\beta = 0.6$) over the competitive decisions of firm B, the delta mHHI is equal to the product of market shares of firms A and B and the term $\mu = \alpha + \beta / [\alpha \times \beta + (1 - \alpha) \times (1 - \beta)]$. The first term ($\alpha$) reflects the fact that post-acquisition the acquiring firm A has a reduced incentive to compete against the acquired firm B. The second term ($\beta / [\alpha \times \beta + (1 - \alpha) \times (1 - \beta)]$) reflects the fact that the acquiring firm A has now the ability to influence the competitive decisions of firm B to its benefit, thus influencing firm B to behave less aggressively. If the term μ is less than 2, then the partial acquisition would raise the level of market concentration by less than a full merger would. But, if the term μ is greater than 2, then the partial acquisition would raise the level of market concentration by more than a full merger would.

For example, suppose that firm A acquired a relatively small financial interest in firm B, say 20%, which granted, however, full control over the competitive decisions of firm B. This might be the case, for example, if the 20% ownership interest made firm A the owner with the largest financial interest in firm B. Then, we would have $\alpha = 0.2$ and $\beta = 1$, and the delta HHI is equal to the product of the market shares of the two merging firms times $\mu = 5.2$, that is 3,250 (= 5.2 x 25 x 25). This is because post-acquisition the decisions of firm B are in the hands of a manager who puts more weight on maximizing the profits of firm A, not of firm B. As a result, the manager for firm B would want to restrict output for the benefit of firm A, much more so than in a full merger. Said differently, because firm A has a relatively small financial interest in firm B, firm A does not bear the cost of firm B restricting output to a greater degree than a wholly-owned firm B would find it profit maximizing.

C. The mHHI in practice

While the discussion of partial acquisitions in the U.S. Department of Justice and Federal Trade Commission's 2010 Horizontal Merger Guidelines (henceforth,

"Guidelines") does not explicitly mention the mHHI, the framework it offers for analyzing partial acquisitions is consistent with the Guidelines, and indeed, the antitrust agencies and private practitioners commonly use mHHI in assessing partial acquisitions. Specifically, the Guidelines emphasize and distinguish (1) the ability to influence the decisions of the acquired firm, and (2) the reduced incentive of the acquiring firm to compete against the partially acquired firm.[64] The European Commission also has used modified concentration indices that account for partial ownership, for example in its decision in the Exxon/Mobil merger.[65]

III. The Modified Gross Upward Pricing Pressure Index ("mGUPPI")

The traditional GUPPI is an index for scoring the unilateral effects incentives of a full merger in an industry where firms compete on price to sell differentiated products. In a merger of two firms A and B, there is a GUPPI from the perspective of firm A, which scores the incentives of firm A to increase price post-merger, and there is also a GUPPI from the perspective of firm B, which scores the corresponding incentives of firm B. The GUPPI from the perspective of firm A is calculated as the ratio between (1) the product of the pre-merger price-cost margin (measured in dollars) of firm B (M_B) and the diversion ratio from firm A to firm B (DR_{AB}), and (2) the pre-merger price of firm A.[66] The first term (that is, the product of the margin and the diversion ratio) is referred to as the *value of diverted sales*, a concept from the most recent Guidelines that has received much attention from antitrust commentators.[67] The GUPPI from the perspective of firm B is calculated in an analogous way.[68]

The GUPPI can be generalized to partial acquisitions. This generalization, which we refer to as the "mGUPPI", requires one to know (1) the ownership interest and (2) the degree of influence that each merging firm has into its merging partner (pre- and post-acquisition). Of note, the mGUPPI does not require knowledge of market shares, just like the traditional GUPPI. This is because market shares and market concentration do not have a direct impact on unilateral effects. Rather,

---

[64] Guidelines at §13.

[65] Regulation (EEC) No 4064/89, Merger Procedure, Case No IV/M.1383 – Exxon/Mobil. Paragraph 256 (page 42) states that "[i]n order to appreciate the level of concentration in this market pre-merger and the impact of the merger, the Commission has estimated HHI indices that take into account the existence of cross shareholdings among most of the players in that market. This calculation was based on the work of Bresnahan and Salop."

[66] That is, the GUPPI from the perspective of firm A is equal to: M_B x DR_{AB} / P_A.

[67] Guidelines at §6.1.

[68] The economic literature on upward pricing pressure includes: Gregory J. Werden, "A Robust Test for Consumer Welfare Enhancing Mergers Among Sellers of Differentiated Products," 44(4) Journal of Industrial Economics 409-413 (1996); Steven, C. Salop and Daniel P. O'Brien, "Competitive Effects of Partial Ownership: Financial Interest and Corporate Control," 67 Antitrust Law Journal 559-614 (2000); Joseph Farrell and Carl Shapiro "Antitrust Evaluation of Horizontal Mergers: An Economic Alternative to Market Definition," 10(1) The B.E. Journal of Theoretical Economics, Article 9 (2010); and Yianis Sarafidis, "Unilateral Effects in Horizontal Mergers," Antitrust Economics for Lawyers (LexisNexis), Chapter 2 (Forthcoming).

unilateral effects analysis is focused on head-to-head competition between the merging firms. As stated in the Guidelines, "Agencies rely much more on the value of diverted sales than on the level of the HHI for diagnosing unilateral price effects in markets with differentiated products."

A. The economic principles behind the GUPPI and the mGUPPI

As mentioned, the GUPPI is a relevant index when analyzing differentiated products. While natural gas or oil molecules are homogeneous, there are many aspects of differentiation such as location, supply assurance, the extent to which the product may have different levels of contaminants, the level of customer service, or even the cost of supply.

In industries where firms compete on price to sell differentiated products, a merger creates upward pricing pressure because a unilateral price increase by one of the merging firms that would be unprofitable absent the merger becomes profitable post-merger (all else equal).[69] To see this, consider first the firm's pre-merger incentives. Pre-merger, the firm is reluctant to increase price, because a higher price would drive down unit sales to the point that the price increase would be unprofitable; or else, the firm would have increased its price. Post-merger, if our firm revisits this calculus, it will realize that a fraction of the lost sales following a price increase will be diverted to the merging partner, and hence will be recaptured by the merging firm. The higher the margin of the merging partner and the higher the fraction of lost sales that are diverted to the merging partner (referred to as the diversion ratio), the greater is the *value of these diverted sales*. And, in turn, the more the merger relaxes the pre-merger constraint not to increase price. The GUPPI is nothing more than the value of diverted sales, but expressed as a fraction of the pre-merger price. That is, the GUPPI indexes the value of diverted sales.

When firms are partially-owned, one can generalize the traditional GUPPI in the same way as the traditional HHI was generalized to the mHHI, but focusing instead on pricing decisions (as opposed to quantity decisions). That is, we assume that the pricing decision of firm A is controlled by a manager whose objective is to maximize the weighted average profits of the owners of firm A, taking into account the financial interests that these owners have into other firms. The weights that the manager uses are again assumed to be the degrees of influence that each owner has over the decisions of firm A.

It can be shown that the mGUPPI will be a multiple of the traditional GUPPI, where the multiple will depend on the financial interest and degree of influence parameters.

[69] The same economic principle may also be applied to bidding markets where firms compete by placing bids. See, Serge Moresi, "Bidding Competition and the UPP Test," Public Comment to Horizontal Merger Guidelines Review Project (2009), available at https://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Feb10_Moresi2_25f.authcheckdam.pdf.

B. An Example and economic intuition for the mGUPPI

Consider a partial acquisition where a (wholly-owned) firm A acquires a financial interest α (e.g., $\alpha = 0.5$) in a (formerly wholly-owned) firm B, which grants firm A degree of influence β (e.g., $\beta = 0.6$) over the competitive decisions of firm B. This partial acquisition will give rise to two effects.

First, post-acquisition the manager of firm A will choose the price of firm A so as to maximize the sum of the profits of firm A (Π_A) and 50% of the profits of firm B (Π_B), that is $\Pi_A + 0.5 \times \Pi_B$. This means that post-acquisition the manager of firm A will take into account the value of diverted sales to firm B. But, unlike what would occur in a full merger where the manager would internalize the full value of diverted sales, now the manager will internalize only a fraction α of the value of diverted sales. This is because firm A acquired only a partial interest into the profits of firm B. In other words, the mGUPPI from the perspective of firm A will be only a fraction $\alpha < 1$ of the value of the GUPPI in a full merger. Therefore, from the perspective of firm A (the acquiring firm), while the partial acquisition still induces upward pricing pressure, this is less pronounced than in a full merger.

Second, the partial acquisition will grant firm A influence over the pricing decisions of firm B. Naturally, firm A would like firm B to increase its price, as this would divert sales from firm B to firm A. Specifically, post-acquisition the manager of firm B will maximize the weighted average of the profits of the two new owners of firm B, giving weight $(1 - \beta) = 0.4$ to the profits of the old owner and weight $\beta = 0.6$ to the profits of the new owner. That is, the manager of firm B will maximize: $0.4 \times (0.5 \times \Pi_B) + 0.6 \times (\Pi_A + 0.5 \times \Pi_B)$. It can be shown that the GUPPI from the perspective of firm B will be equal to the product of the traditional GUPPI from a full merger multiplied by the term $\beta / [\alpha \times \beta + (1 - \alpha) \times (1 - \beta)]$.[70] Notice that this is identical to the second term in the expression for μ in the mHHI section. And, as we previously saw in the example in Section II.B, when the acquiring firm's degree of influence is significantly higher than its financial interest in the acquired firm, this term can be greater than one.[71]

Therefore, from the perspective of firm B (the acquired firm), the partial acquisition may induce more or less upward pricing pressure relative to a full merger. The intuition is the same as discussed in the mHHI section: when the acquiring firm's degree of influence over the acquired firm is significantly higher than its financial interest, then the acquiring firm can induce the acquired firm to increase its price by "too much," since the acquiring firm obtains the benefits of this action, while passing on the costs to the remaining, non-controlling owners of the acquired firm.

---

[70] To see this, notice that maximizing the expression $0.4 \times (0.5 \times \Pi_B) + 0.6 \times (\Pi_A + 0.5 \times \Pi_B)$ is equivalent to maximizing $\{\beta / [\alpha \times \beta + (1 - \alpha) \times (1 - \beta)]\} \times \Pi_A + \Pi_B$, where $\alpha = 0.5$ and $\beta = 0.6$.

[71] For example, when firm A acquires a 20% financial interest into firm B, which grants it full control of firm B, we have $\alpha = 0.2$ and $\beta = 1$. Accordingly, the GUPPI from the perspective of firm B is 5 times the GUPPI from a full merger.

IV. Conclusion

Both the mHHI and the mGUPPI were developed by antitrust practitioners to assist in assessing the potential for competitive concerns arising from partial acquisitions and joint ventures. A key insight from the development of these two tools has been that a partial merger may not necessarily be predicted to be less problematic—and may even be more problematic—relative to a full merger. This tends to be the case when the acquiring firm's degree of influence over the target resulting from a partial acquisition is significantly higher than the financial interest acquired. A high degree of influence combined with a low degree of financial interest has the potential to generate perverse competitive incentives: in the extreme case where the acquiring firm acquires a miniscule financial interest but full control of the acquired firm, the acquiring firm might find it optimal to shut down the operations of the acquired firm entirely. In doing so, it will in fact benefit from the diverted sales but pay a small financial cost, as most of the cost will be borne by the other, non-controlling, owners of the target company. This outcome is worse, from a competitive standpoint, than what would happen under a full merger, where the acquiring firm would internalize the cost of shutting down the operations of the acquired firm.[72]

We reiterate that both the mHHI and the mGUPPI are helpful tools during the early stages of an investigation. They can help identify areas and products of concern as well as those that are unlikely to raise red flags. In other words, they can help focus the investigation, saving resources of both the antitrust agencies and the merging parties. However, like their traditional counterparts, they are not meant to be substitutes for a full economic analysis.

While not explicitly mentioned in the Guidelines, the mHHI and the mGUPPI are consistent with the discussion of partial acquisitions in the Guidelines. In particular, the Guidelines emphasize three avenues through which partial acquisitions might affect competition.[73] First, a partial acquisition might lessen competition by giving the acquiring firm influence over the decisions of the acquired firm. Second, a partial acquisition might reduce the acquiring firm's incentive to compete against the target because of the newly acquired financial interest in its profits. Third, it might facilitate the flow of competitively sensitive information between the two firms, potentially increasing the risk of coordination. While the first two competitive concerns mentioned in the Guidelines are incorporated into the mHHI and mGUPPI, the third concern is outside their scope, thus further underlining the importance of a full merger investigation that goes beyond mHHI and mGUPPI, and looks at all possible ways in which a partial acquisition affects competition.[74]

---

[72] This, of course, also ignores other potential competitive benefits that could accrue to the acquired firm, such as the addition of the acquired firm's intellectual property, know-how, key employees, supply contracts, etc.

[73] Guidelines at §13.

[74] For example, the consent agreement between the FTC and the parties in *Enbridge/Spectra* requires *Enbridge* to establish firewalls to limit its access to non-public information.

Mexico's Antitrust Regulator Continues to Focus on the Transportation and Energy Industries

By Gerardo Calderon[75]

The transportation and energy industries are among the main drivers of many countries' economic growth, and this is especially true in so-called developing countries like Mexico. Because of their importance, these industries and those closely related to them are often in the crosshairs of the competition authorities. In Mexico, the Mexican Economic Competition Commission ("Cofece")[76] has always been vigilant in the transportation and energy industries, in particular with respect to the energy industry, as it has moved from one that is wholly controlled by the Government to one funded by private investment.[77] Indeed, officials from Cofece have recently mentioned in multiple forums that these two sectors are areas of focus for the agency[78]. In addition, Cofece's Annual Work Plan for year 2017 refers to actions to proactively promote effective competition in the energy sector, particularly in the gasoline, diesel, and liquefied petroleum gas ("Gas LP").[79]

Among the most notable recent actions that Cofece has carried out in the transportation and energy sectors, are: (i) its preliminary resolution on the competitive conditions of air transportation services in Mexico City's International Airport; (ii) its resolution on the Delta-Aeromexico cooperation agreement; (iii) its preliminary resolution on the competitive conditions of railroad interconnection services; (iv) its resolution on an international cartel in the market for maritime transportation of motor vehicles; (v) its opinion with recommended actions to eliminate restrictions on establishing and operating new service stations

---

[75] Gerardo Calderon is an associate in the Mexico City, Mexico office of Baker & McKenzie Abogados, S.C.

[76] And before Cofece was created (by means of a reform to the Mexican Federal Constitution in June 11, 2013), its predecessor the Mexican Competition Commission ("Cofeco").

[77] The Constitutional amendment base of the reform was published on December 20, 2013. A number of new laws and amendments have been enacted since then to implement the reform.

[78] Alejandra Palacios (Head Commissioner of Cofece) mentioned during a meeting with North American competition agencies that transportation and energy will be two sectors for the agency to focus on. See related press release at: https://www.cofece.mx/cofece/ingles/images/Comunicados/Comunicados_ingles/COFECE-029-2016.pdf. Likewise, Carlos Mena (Head of Cofece's Investigation Authority) mentioned in an interview with GCR that Cofece has "*seen third-party analysis of certain industries that have a problem. We don't know exactly what the problem is, or what is the issue to tackle. For us, for example, public procurement is a big issue, in the energy sector, the financial sector and the transport sector*." Full text of the interview is available at: https://blogdelacompetenciacofece.wordpress.com/2015/05/25/an-interview-with-carlos-mena/. *See also Mexico: COFECE to focus on transport sector* published in CPI at: https://www.competitionpolicyinternational.com/mexico-cofece-to-focus-on-transport-sector/; *Investigation finds lack of competition in Mexican rail interconnections*, available at: http://automotivelogistics.media/news/investigation-finds-lack-competition-mexican-rail-interconnections.

[79] Cofece's Annual Work Plan also refers to action in other strategic sectors that are economic and socially sensitive, including the financial sector, the pharmaceutical sector, and public procurement processes.

(*gasolineras*); (vi) its request to the Federal Government to file a constitutional action (*accion de inconstitucionalidad*) against an amendment to a state law dealing with service stations regulation; and (vii) its resolution on G500 (a purchasing joint venture to acquire gasoline and diesel).

Overall, it is clear that Cofece is particularly concerned with network issues as well as ensuring access to the network/essential facilities. Moreover, it is clear that Cofece will use the many tools at its disposal to enforce Mexico's antitrust laws and promote competition in the transportation and energy industries.

I. Transportation

A. Competitive Conditions in Air Transportation Services[80]

Closely related to the Delta-Aeromexico case discussed in Section I.B below, in February 2016 Cofece issued a Preliminary Resolution (*Dictamen Preliminar*) on a special proceeding[81] which identified certain infrastructure of Mexico City's International Airport ("AICM") as an essential facility (*i.e.*, runways, taxiways, visual aids, and platforms), found that there is potential for anticompetitive effects in the market resulting from the existing rules to access to the abovementioned infrastructure, and found that AICM is not currently being efficiently used due to issues in allocating and monitoring procedures for takeoff and landing schedules ("slots"). Cofece's findings included: (i) barriers to entry and expansion were caused by reduced availability of slots and high market concentration; (ii) itineraries with arrivals to or departures from AICM had higher prices; (iii) there was a lack of transparency on critical information regarding allocation, evaluation and monitoring procedures; (iv) air carriers were incentivized to keep idle slots, carry out operations without an assigned slot, and transfer or exchange slots in a way that does not allow the entrance or expansion to other air carriers; and (v) market shares of air carriers were directly linked to their tenure of slots at AICM.

As a result of these findings, in its Preliminary Resolution, Cofece proposed corrective measures aimed to eliminate the restrictions on access to the essential facilities, including establishing an independent body to assign slots, retrieve those slots not being used by air carriers, and to create a Reserve Fund of takeoff and landing schedules for new entrants. In response, the AICM submitted an alternative plan of action to address Cofece's concerns, but it was rejected by the authority. This process is now ongoing and the final resolution could include binding recommendations for AICM. This is the first time Cofece has initiated a proceeding of this nature,[82] and is quite unique in that it involved a competition authority conducting an antitrust investigation of an airport.

---

[80] *See* file IEBC-001-2015.

[81] As of July, 2014 when the current Mexican Competition Law entered into force, Cofece is able to initiate proceedings to resolve on the existence of barriers to free competition (not to be mistaken with entry barriers) or essential inputs. This type of proceeding might result in Cofece (i) issuing recommendations to Regulatory Authorities; (ii) ordering undertakings to eliminate barriers; (iii) issuing guidelines to regulate essential facilities; and/or (iv) ultimately, divestment assets of shares from undertakings to eliminate competition issues.

[82] Proceeding to resolve on the existence of essential inputs regulated in Article 94 of the MCL.

B. Delta-Aeromexico[83]

Probably one of the most high profile cases of 2016 for Cofece was the cooperation agreement between Delta and Aeromexico to jointly operate flights between Mexico and the U.S. Following a review of the proposed transaction, Cofece found that the transaction would eliminate the competitive pressure on Aeromexico in cross-border routes by Delta, and given the high concentration of slots in AICM, price increases on flights between Mexico and the U.S. were likely. In view of the foregoing, Cofece conditioned the transaction on the parties yielding eight pairs of slots at AICM to other carriers and required that one of the two parties to give up a route that both parties had been assigned. The transaction was also approved subject to conditions by the U.S. Department of Transportation.

The authorized joint cooperation agreement now allows Delta, who currently owns more than 36% of Aeromexico,[84] and the latter to coordinate fares and schedules, as well as jointly market and sell tickets in the Mexico-U.S. market.[85] Notably, Cofece analyzed the transaction based on a *hub-and-spoke* (instead of a *point-to-point*) market, which allows the authority to assess the potential risks associated with the network as a whole, not just on specific overlapping routes (as is typically done in the U.S.). Moreover, Cofece also weighed public interest factors to reach its decision on the case, although the substance of the analysis was mostly focused on core antitrust issues.

C. Railroad Interconnection[86]

In March 2017 Cofece issued a Preliminary Resolution (*Dictamen Preliminar*) on a special proceeding,[87] which concluded that in the market for interconnection services between rail networks is not competitive. According to the Preliminary Resolution, the three undertakings that control 72.3% of the total railway network in Mexico are able to fix prices, restrict supply, and foreclose competitors' access to their respective networks. Cofece found that this lack of effective competitive conditions resulted in increased fees, excessive freight transportation times, higher logistic costs, and underuse of interconnection services, which significantly impacts the rest of the Mexican economy.

Comments on the Preliminary Resolution have already been submitted by the undertakings with legal standing in the case, and later this year Cofece will issue a Definitive Resolution on the case. If Cofece's Preliminary Resolution is confirmed,

---

[83] Files CNT-050-2015 & CNT-127-2016.

[84] Delta plans to raise its stake in Aeromexico to 49% by the end of the second quarter of 2017.

[85] Delta and Aeromexico first entered into a codeshare agreement in 1995. Both airlines received approval for a prior transaction in 2012 from Cofece in which Delta acquired approximately 3.5% of Aeromexico's shares.

[86] *See* file DC-002-2016.

[87] Proceedings to resolve on the existence market conditions regulated in Article 96 of the MCL. This type of proceeding is intended for the Sector Regulator to issue a specific regulation or eliminate existing regulation. A Final Resolution on this process is a precondition to initiating that action.

The Railway Transport Regulatory Agency[88] would be entitled to establish new running or trackage rights[89] and fee guidelines.

D. Maritime Shipping Cartel[90]

On May 25, 2017, Cofece issued a resolution imposing fines on seven roll-on-roll-off shipping companies for cartel conduct totaling approximately 582 million Mexican pesos (~$33 million). The alleged anticompetitive conduct involved the allocation of maritime transport routes with a point of origin or destination in Mexican ports,[91] resulting in reduced competitive pressure and increased prices for services rendered to the automotive industry.

This case is noteworthy as the alleged anticompetitive conduct affected the automotive industry, which is highly important to the Mexican economy, and one of the sectors that receives substantial foreign direct investment. Although most do not know this, Mexico is the seventh-largest automobile producer in the world and the fourth-largest exporter – according to The Offshore Group, Mexico has 19 plants operated by 8 OEMs, including Ford, GM, and Volkswagen.[92] The sanction will only become definitive after being confirmed by the Specialized Courts or if the affected undertakings do not challenge it within the applicable statutory term.[93]

II. Energy

A. Service Station Regulations[94]

In December 2016 Cofece issued a non-binding opinion addressed to local governments and state legislatures aiming to eliminate restrictions on establishing and operating gasoline and diesel service stations. Cofece's opinion covered the 32 States of the Mexican Territory and its major cities. The restrictions identified by Cofece were mainly related to: (i) minimum distance requirements; (ii) unjustified establishment requirements; (iii) inconsistencies with federal regulations; and (iv) unclear provisions related to permits, licenses, or authorizations. To eliminate the identified restrictions, Cofece recommended that local and state governments take the following actions:

- Eliminating regulations providing for minimum distance requirements between service stations.

---

[88] This agency created in 2016 as part of the Railway Service Regulatory Law amendments.
[89] Trackage rights are defined as agreements between railroad licensed operators (*concesionarios*) to grants rights of use of their tracks in exchange of a payment.
[90] File IO-005-2013 & CNT-127-2016.
[91] Nine agreements on routes to or from Argentina, Brazil, Chile, Japan, Thailand, Indonesia and Belgium were identified. The Mexican ports involved are Altamira, Veracruz, Manzanillo, Mazatlán and Lázaro Cárdenas.
[92] See https://offshoregroup.com/industries/automotive-manufacturing-in-mexico/.
[93] Parties affected by a resolution from Cofece are able to file a constitutional trial to challenge it within the following 15 business days from being served with this resolution.
[94] File OPN-012-2016.

- Eliminating regulations establishing minimum surface and main front requirements for service stations.
- Updating regulations governing the establishment of service stations to be consistent with the federal regulatory framework.
- Establishing transparent and public criteria regulating granting of authorizations, licenses, and permits to built and operate service stations, to provide legal certainty to potential entrants.

To issue this opinion, Cofece undertook an in-depth analysis of 319 state and municipal regulations governing the establishment and operation of service stations. The opinion is preceded by its report entitled “Transition to competitive retail gasoline and diesel markets” from July 2016,[95] where Cofece analyzed both upstream and downstream gasoline and diesel markets.

B. Constitutional Action Regarding Service Stations in Coahuila[96]

In February, 2017 Cofece asked the Federal Executive Branch to initiate a constitutional action (*acción de inconstitucionalidad*) before the Mexican Supreme Court to challenge the state of Coahuila’s[97] law that establishes minimum distance requirements between gasoline service stations. Cofece considers that recent amendments to the Coahuila’s State Law for Human Settlements and Urban Development violates the constitutional right of free trade and free competition, by preventing the establishment of service stations in certain geographical areas, thus guaranteeing higher profit margins for incumbents and foreclosing other options that might provide better quality and price for consumers.[98] This case is notable as is the first time Cofece used its power to request the Supreme Court to analyze competition impact from State legislation.

C. G500 Purchasing Joint Venture[99]

In December 2016, Cofece authorized, under a merger control process, a purchasing collaboration between 54 retail service station operators to jointly purchase fuels and other related products. This collaboration, called Grupo G500, was aimed at obtaining efficiencies in purchasing products sold in their service stations, including gasoline and diesel fuel. Cofece authorized the transaction based on the following considerations:

---

[95] 72 pages full report available at: https://www.cofece.mx/cofece/ingles/attachments/article/38/DOCUMENTO-GASOLINAS-FINAL-INGLES.pdf. The report was awarded by the World Bank Group and the International Competition Network.
[96] File OPN-011-2015.
[97] Coahuila is a state in Northeast Mexico that borders Texas.
[98] In September 2015, Cofece recommended to the Governor of Coahuila not to enact the amendments approved by the State Congress, but the bill containing the amendments was approved as originally submitted. Therefore, Cofece initiated the constitutional action.
[99] File CNT-058-2016.

- Members of G500 would have a low participation (*i.e.*, combined market share) in the purchase of fuels in the markets in which they participate
- It was expressly stated that the partners will operate independently in the retailing of these products.
- New partners can join the agreement, but are required to notify and provide information to Cofece (originally G500 did not provide enough information for Cofece to analyze the incorporation of potential new members of the agreement).

This case is notable as it is the first purchasing collaboration scheme analyzed by Cofece following the liberalization of the retail fuel markets.

III. Final Remarks

As the cases discussed above clearly evidence, Cofece has already used a number of its available tools—including some for the first time—to promote competition in both the transportation and energy sectors. These include fining companies engaged in cartel practices (in the maritime transportation cartel); special proceedings to eliminate barriers to competition and/or regulate essential inputs (AICM and railroad interconnection); merger control processes (Delta-Aeromexico and G500); the issuance of opinions dealing with these sectors (service stations); and indirectly requesting Supreme Court intervention to eliminate restrictions in competition at a state level.

The main rationale Cofece's focus on the transportation industry is that it is critical to a smooth functioning of the supply chain for numerous other sectors of the national economy. Promoting competition in this industry furthers Mexico's goal of serving as an efficient and reliable logistics platform for domestic and international trade.

As for the energy industry, Cofece is playing an important role in the entire distribution chain as it is privatized and deregulated. Therefore, Cofece's actions are aimed to lowering entry barriers and increasing competition. A clear example of this are the actions being carried out by Cofece for the purpose making the retail fuel market more competitive. In particular, companies engaged in or hoping to be engaged in the operation of service stations should evaluate the potential antitrust risks and develop a strategy to eliminate or mitigate them. For instance, collaboration agreements through acquisitions, mergers, partnerships or alliances, most likely would be considered as a concentration, and therefore it may be convenient to report to Cofece to avoid being investigated. On the flip side, prospective entrants should consider ways in which to use Cofece's efforts to increase competition in order to advance their own cause.

Going forward, it is foreseeable that Cofece will continue focusing in the transportation and energy sectors, and indeed, the agency already announced its plan to issue later this year a report on the entire value chain of the Gas LP market in Mexico later this year.

2017 ABA Spring Meeting Panel Summary: Competition and Consumer Law Issues With Customer Profiling

By Lillian Okamuro[100]

With the increasing prevalence of "big data," the Consumer Protection, Privacy & Information Security and Transportation & Energies Industries Committees brought together regulators, private practitioners, and academics to discuss the consumer protection, competition, and practical implications of counseling in this rapidly evolving area. This 2017 ABA Antitrust Section Spring Meeting panel was chaired and moderated by Hill Wellford of Morgan Lewis & Bockius LLP, and speakers included Thomas Pahl, Acting Director of the Bureau of Consumer Protection, Federal Trade Commission ("FTC"), Lydia Parnes, Partner at Wilson Sonsini Goodrich & Rosati LLP, David Meyer, Partner at Morrison & Foerster LLP, and Maurice Stucke, Professor at University of Tennessee College of Law.

In his opening remarks, Mr. Wellford provided three common adjectives that describe and distinguish big data, namely, the "3Vs": volume (the quantity of information being gathered, analyzed, and stored by companies); velocity (the speed and acceleration at which companies are accumulating and analyzing data); and, variety (the breadth of sources from which information is being collected). In addition, Mr. Wellford offered a fourth "V" – vague – to set the tone for the morning's panel.

Mr. Wellford explained that, today, businesses are experiencing unprecedented access to information in terms of scope, scale, and sophistication of analysis. For example, Ms. Parnes explained that the ability to capture conversational dialogue through voice recognition and to shorten commute times through a mobile application, Waze, were previously inaccessible to consumers due to the sheer size of the data. Indeed, Ms. Parnes noted that the future of big data technology will also bring consumers things like self-driving cars, targeted healthcare treatments, and advanced grocery store marketing. The net impact on consumers, however, is still hotly debated. In the discussions that followed, the panelists offered their perspectives and practical advice on counseling in the consumer protection and competition contexts of big data.

Perspectives on Consumer Protection Issues

The panel began with Mr. Wellford recognizing the tension between the consumer benefits received from big data technology and the need to limit the storage and abuse of personal information.

---

[100] Lillian Okamuro is an associate in the Washington, DC office of Dechert LLP.

With regards to consumer protection risks, Mr. Pahl introduced the issue of fair lending practices and, in particular, the potential harms of redlining (*i.e.*, the practice of drawing figurative lines around classes of borrowers for the purpose of determining loan eligibility or rates). Mr. Pohl explained that the Equal Credit Opportunity Act ("ECOA"), implemented by Regulation B and combined with the sound advice of counsel, should limit blatant acts of lending discrimination. There remains, however, a concern that the facially neutral corporate policy may cause disparate impact discrimination such that even a well-meaning corporate policy may come back to bite a company.

Ms. Parnes added that in the context of privacy by design, an ethical question arises regarding whether the lawyer should engage with her client's technical teams when deciding what classes of data should be included in an algorithm. For example, Mr. Pohl explained that, under the Fair Credit Reporting Act ("FCRA"), there are limits and standards that must be adhered to when transferring personal information of credit applicants and, ultimately, when making determinations of creditworthiness. With the advent of big data, however, Ms. Parnes explained that the predictive analyses used by clients to assess credit scores often incorporate non-traditional factors that are not intuitively correlated with creditworthiness. So, a common question arises regarding when the use of big data becomes covered by the FCRA?

To help provide clarity, Mr. Pohl explained that the FTC's enforcement power would be applied to big data in the same fundamental manner as with other subject matters, referencing for support the FTC's 2012, 2015, and 2016 reports on the issue.[101] Furthermore, Mr. Pohl reminded the audience that the Dodd-Frank Act conferred on the Consumer Financial and Protection Bureau ("CFPB") exclusive rulemaking authority over the ECOA and FRCA. The consequence is that any rulemaking undertaken by the FTC with respect to big data, would have to fall within its authority under the FTC Act, which, in practice, has taken between three and ten years to complete. The industry is evolving so rapidly that any rulemaking by the FTC would likely be an ineffective tool. Faced with this reality, the FTC's interests will instead focus on studies and analyses to promulgate best practices and industry guidance. Mr. Pohl cautioned, however, that when advising clients, counsel should remain mindful of applicable laws and court opinions. For example, Ms. Parnes referenced the U.S. Supreme Court's decision in *Spokeo Inc. v. Robins* as a "wakeup call" to the industry.[102] In *Spokeo*, the Court applied the FCRA to a company that did not fit within the traditional understanding of a consumer reporting agency.

---

[101] *See* Protecting Consumer Privacy In an Era of Rapid Change, FTC Report, March 2012, https://www.ftc.gov/sites/default/files/documents/reports/federal-trade-commission-report-protecting-consumer-privacy-era-rapid-change-recommendations/120326privacyreport.pdf; Internet of Things: Privacy & Security In a Commercial World, FTC Report, January 2015, https://www.ftc.gov/system/files/documents/reports/federal-trade-commission-staff-report-november-2013-workshop-entitled-internet-things-privacy/150127iotrpt.pdf; and 2016 Big Data: A Tool for Inclusion or Exclusion, FTC Report, January 2016.https://www.ftc.gov/system/files/documents/reports/big-data-tool-inclusion-or-exclusion-understanding-issues/160106big-data-rpt.pdf.

[102] *Spokeo, Inc. v. Robins*, 578 U.S. __, 136 S.Ct. 1540 (2016).

For final takeaways, Messrs. Pohl and Parnes reminded the audience that the FTC has taken a technology-neutral position with respect to big data and will apply the law in the same manner as it does to other uses of information exchange, but the audience should remain mindful of the potential to trigger the CFPB's enforcement authority. In particular, Ms. Parnes explained that because the law remains relatively undeveloped, counsel should advise clients to take steps against inadvertently becoming a consumer reporting agency and triggering the implications of the FCRA.

Perspectives on Competition Issues

Turning to the topic of competition risks, Mr. Meyer, Mr. Stucke, and Mr. Wellford discussed areas of risk in the big data context:

Behavioral price discrimination. With behavioral discrimination, Mr. Stucke explained that there is a shift from third-degree to first-degree price discrimination[103] as companies track and collect data of consumers, segmenting the group into smaller and smaller pieces. The result being an increased risk of consumer welfare reductions, including movement towards an individual price, not a competitive price. Mr. Meyer replied that the issue of behavioral discrimination is not unique to big data. For example, for years car dealer have been sizing up customers and negotiating with them on an individual basis.

Collusion. Deferring discussion of issues related to *per se* price fixing, Mr. Stucke instead focused on algorithmic tacit collusion by explaining four potential scenarios:[104]

i. <u>The Messenger</u>: Conspirators can use algorithms to facilitate and perfect collusion. *United States v. Topkins*[105] is a good example.

ii. <u>Hub-and-Spoke</u>: Multiple companies may utilize the same algorithm to determine the market price and prevent price cutting.

iii. <u>Predictable Agent</u>: Mr. Stucke described this scenario as "tacit [collusion] on steroids" because machines, unlike humans, have the advantage of speed of response and increased market transparency. Each company is developing its algorithm unilaterally, so there may be evidence of intent, but insufficient evidence of an agreement.

---

[103] First-degree (or "perfect") price discrimination is the practice of charging each customer his or her reservation price. By comparison, under third-degree (or "imperfect") price discrimination, the company can only identify separate demand curves for two or more groups of customers. The company will charge different groups different prices. *See* Robert S. Pindyck & Daniel L. Rubinfeld, MICROECONOMICS, Chapter 11.2 (7th ed. 2009).

[104] For additional background, the panel directed the audience to the Organisation for Economic Co-operation and Development's ("OECD") workshop on algorithms and collusion.

[105] David Topkins pled guilty to criminal charges that he and his co-conspirators had used algorithm-based pricing software to set the prices of posters sold on Amazon. *See* Information (Apr. 6, 2015) and Plea Agreement (April 30, 2015), *available at* https://www.justice.gov/atr/case/us-v-david-topkins.

iv. <u>The Digital Eye</u>: Machine learning allows companies to monitor customers and rivals, anticipating actions of both to optimize profit. Indeed, Mr. Stucke noted that a company may be unaware of the evolution or final decision of the algorithm such that there may be insufficient evidence of both an agreement and intent.

Barriers to entry. Mr. Wellford noted that big data is everywhere, yet there are claims it has become a barrier to entry by competitors. Mr. Stucke added that there may be aspects of a first mover's advantage, as they leverage their repositories of information to prevent or limit new competition.

Information exchange agreements. Mr. Meyer explained that companies have substantial latitude to share data in order to create or comply with efficient industry standards. Different issues are raised by the potential for big data and advanced algorithms to lead to more effective "tacit coordination." One of the interesting issues is whether there is a principal-agent relationship between the firm and the pricing algorithm that is finding ways to signal or monitor competitors' behavior more effectively. If machine learning and speed of response leads to prices finding higher equilibria levels, will courts see the underlying behavior as humans seeking *to communicate* more efficiently using machines or simply as the next evolution in the entirely-lawful recognition by oligopolists that their market behavior is often interdependent?

Data-driven mergers. Mr. Meyer noted that when data or data services are the product, traditional horizontal merger analysis will be relatively straightforward, with the usual questions such as market definition and product substitution. More difficult issues will arise when data is a key input and the deal would cause a shift in control of essential inputs. In other words, one question will be whether post-acquisition there is less of an incentive to provide critical data to the acquiring company's rivals. For further discussion of issues involved in data-driven mergers, Mr. Stucke referred the audience to his 2016 publication with Allen Grunes entitled "Big Data and Competition Policy," which discussed issues of multi-sided markets and mergers that seek to combine non-overlapping sets of data. Likewise, Mr. Stucke noted that the European Commission's ("EC") investigations into the Facebook/WhatsApp and Google/DoubleClick mergers show that the EC is grappling with issues of data-driven efficiencies.

During the question and answer session, one audience member inquired whether Mr. Meyer or Mr. Stucke had any thoughts on potential remedies for tacit collusion. Mr. Stucke directed the audience to review the OECD's research, exploring potential factors that facilitate or destabilize tacit algorithmic collusion. Mr. Meyer cautioned about any effort to regulate independent pricing behavior, and noted that doing so would inevitably intrude into the efficiencies available from the unilateral use of algorithms, which we know allows more efficient utilization of existing data – making it cheaper to hold, access, and analyze information.

Intersection of Consumer Protection and Competition

Finally, Mr. Pohl and Ms. Parnes explained that the FTC's Bureau of Consumer Protection ("BCP") and Bureau of Competition ("BC") may implement a joint investigation, if necessary. While not typical, it has happened in the past. Ms. Parnes noted that a good example is the Google/DoubleClick merger where there were privacy and competition issues such that the BC brought an enforcement action, while BCP published a proposal that called on the industry to self-regulate.

2017 ABA Spring Meeting Panel Summary: HSR Exemptions: Running Out of Gas?

By John R. Seward and Ryan B. Will[106]

The Federal Trade Commission ("FTC") and U.S. Department of Justice ("DOJ") have recently revisited several HSR exemption interpretations and sought penalties from investors relying on others. The Mergers & Acquisitions and Transportation & Energy Industries Committees presented a panel on March 31, 2017 at the ABA Antitrust Section Spring Meeting that addressed these recent developments and examined whether certain exemptions, such as those for acquisitions of investment rental property and warehouses, are especially vulnerable in the energy or any other industry. Karen Kazmerzak of Sidley Austin LLP chaired the panel, which was moderated by William R. Vigdor of Vinson & Elkins LLP. Speakers included Kay Lynn Brumbaugh of Andrews Kurth Kenyon LLP,[107] Steven J. Kaiser of Cleary Gottlieb Steen & Hamilton LLP, Kara Kuritz, Attorney Advisor in the DOJ's Legal Policy Section, and Kathryn E. Walsh, Deputy Assistant Director of the FTC's Premerger Notification Office ("PNO").

Mr. Vigdor opened the discussion by outlining the basic thresholds for determining whether a transaction is subject to the requirements of the HSR Act, noting in particular that the current size-of-transaction threshold is $80.8 million. Mses. Kuritz and Walsh then outlined the resources available to explain the HSR requirements and process. These resources include: the statute (15 U.S.C. § 18a), which sets forth the HSR thresholds, waiting period, and exemptions; the HSR Regulations (16 C.F.R. §§ 801-803); the Statement of Basis and Purpose, which explains the rationales behind the specific rules; and the PNO's formal and informal interpretations. Ms. Walsh stated that the PNO Staff welcomes requests for informal interpretations and is happy to work with parties to determine whether a particular transaction is reportable. She also stated that when seeking an informal interpretation, HSR counsel should email all members of the PNO Staff to ensure that the request is not missed. Ms. Walsh went on to highlight the materials on the PNO website, including a searchable database of informal interpretations, blog posts, the Style Sheet for HSR Filings, and the instructions for completing the form. Ms. Walsh noted that late last year the agencies released revised instructions, which included changes to Items 3(a), 4(b), and 7(c).

Ms. Walsh then explained how HSR filings are processed. Each Wednesday the PNO circulates a package of all HSR filings received the prior week for a screening review by the FTC and DOJ. The package includes a summary sheet with recommendations on which transactions should be granted early termination. To ensure an HSR filing is included in the Wednesday package, parties should submit their filings by the previous Friday, although sometimes filings submitted on a

---

[106] Mr. Seward is a Counsel at Andrews Kurth Kenyon LLP and Mr. Will is an Associate at Vinson & Elkins LLP.

[107] Subsequent to the Spring Meeting, Ms. Brumbaugh joined GIACT Systems, LLC as its Chief Legal Officer & Secretary.

Monday can also be included depending on Staff's workload. The filing fee must also be received before the HSR notification will be included in the screening package. Finally, Ms. Walsh noted that email is now the preferred way of sending waiting period and early termination letters.

Oil & Gas Hypotheticals

The discussion was then turned over to Ms. Brumbaugh, who went through a number of hypotheticals designed to highlight common exemptions applicable to transactions in the oil and gas industry. The first two hypotheticals dealt with the formation by "Big Tex" of a wholly owned master limited partnership (called "Little Tex") and the transfer of various assets from Big Tex to Little Tex. Ms. Brumbaugh explained that the formation of Little Tex was an exempt transaction under § 802.30(b), which applies to the formation of wholly-owned entities, and that the transfer of assets from Big Tex to Little Tex was therefore also exempt under § 802.30(a) for intraperson transactions.

The third and fourth hypotheticals were used to explain the exemption for acquisitions of carbon-based mineral reserves under § 802.3. In these hypotheticals, Big Tex took Little Tex public, resulting in its economic interest in Little Tex dropping from 100 to 49 percent. Big Tex then sold to Little Tex producing oil and gas wells along with field pipelines and treating and metering facilities that exclusively serve the wells. In the third hypothetical, the wells and associated assets had a fair market value of $400 million, and in the fourth hypothetical they had a fair market value of $550. Ms. Brumbaugh used the two hypotheticals to explain that the § 802.3 exemption applies to acquisitions of carbon-based mineral reserves and associated asset valued at $500 million or less. The transaction in the third hypothetical was therefore exempt while the transaction in the fourth hypothetical was not.[108] Ms. Brumbaugh also noted that $500 million limit is not adjusted annually for inflation, and once this amount is exceeded, the entire value of the transaction is used to determine the filing fee.

The fifth and sixth hypotheticals involved acquisitions by Little Tex of a natural gas processing plan and associated gathering pipeline and a storage facility, respectively. Ms. Brumbaugh explained that acquisitions of pipelines often used to be covered by the exemption for investment rental property under § 802.5 and storage facilities were often covered by the exemption for warehouses under § 802.2(h), but that the PNO changed its position in 2015, making both acquisitions reportable. Ms. Walsh added that the change in position was intended to bring the exemption back in line with its original intent. The key question in applying §§ 802.2(h) and 802.5 is whether the buyer intends to act like a traditional landlord, profiting only from the investment in the real estate, or intends to participate in the business conducted on the real estate.

[108] These transaction no longer qualified for the intraperson exemption because Big Tex's economic interest in Little Tex dropped below 50 percent (*i.e.*, it no longer has the right to 50 percent of Little Tex's profits or assets upon dissolution).

The last oil and gas hypothetical involved an acquisition by Little Tex of 100 percent of the economic interest of Big D Partners LP, a limited partnership whose only assets were oil and gas reserves valued at $800 million that were not yet in production and had not generated any income. Ms. Brumbaugh explained that this transaction is not reportable because under § 802.4 you look through the entity's legal structure to the underlying assets, which were all exempt under § 802.2(c) as unproductive real property. Ms. Brumbaugh also pointed out that in practice it can often be complicated to determine whether this exemption applies, making it important to talk to clients about which assets are producing and non-producing. Ms. Walsh added that the PNO is happy to work with counsel to determine whether the exemption applies.

Finally, Ms. Brumbaugh advised that if a deal involves any pipeline overlap, even a seemingly *de minimis* overlap, counsel should be ready to provide Staff with pipeline maps and explain why the overlaps are not a concern.

Passive Investment Exemption Hypotheticals

The second set of hypotheticals dealt with the acquisition of voting securities and the passive investment exemption. The first hypothetical, in which Big Tex acquires preferred shares worth $75 million in a company called Red River, was designed to illustrate how securities purchased on the open market are valued for HSR purposes. The panel explained that pursuant to § 801.10, securities purchased on the open market are valued at the greater of the acquisition price, which is the amount actually paid for the securities, or market price, which is defined as the lowest closing price within forty-five days prior to filing or closing. The hypothetical also points out that if the acquisition falls under the current $80.8 million threshold, then the acquirer's intent with respect to control is irrelevant.

The second, third, and fourth hypotheticals illustrated how convertible voting securities are treated under the rules. The second hypothetical showed that acquisitions of preferred shares are exempt from the reporting requirements under § 802.31 to the extent that the shares do not convey present voting rights to the owner. However, when these securities are converted, they must be aggregated with other voting securities held by the acquirer to determine whether an HSR threshold is met. The third hypothetical asked how Big Tex calculates its holdings upon conversion of the preferred shares. The panel explained that Big Tex's conversion of $75 million in voting securities are valued at market price pursuant to § 801.10(a)(1)(ii); the shares have no acquisition price because they are being converted. They must then be aggregated with Big Tex's existing $75 million in securities, which would thus exceed the current $80.8 million threshold and render the conversion reportable. Ms. Brumbaugh noted that counsel should consider the timing and market value of conversions in light of the aggregation rule. The fourth hypothetical served as a reminder that an HSR filing is valid for one year after the waiting period expires pursuant to § 803.7, and the conversion must be made within that timeframe to avoid having to refile.

The fifth and sixth hypotheticals focused on the passive investment exemption under § 802.9. The fifth hypothetical asked whether Big Tex, holding

less than 10% of Red River, could rely on the investment-only exemption. As a preliminary matter, Big Tex's holdings need to be aggregated pursuant to § 801.13. If Big Tex still holds less than 10% of Red River, the parties must then look to Big Tex's intent to see whether the passive investment exemption applies. In this hypothetical, Big Tex's intent was to participate in the formulation, determination, or direction of the basic business decisions of Red River. Thus, the passive investment exemption does not apply. Ms. Kuritz explained that the facts of this hypothetical are similar to those in the DOJ's 2004 enforcement action against Manulife Financial Corporation. She said that given the exemption's fact-specific nature, parties who have doubts about the exemption's applicability should seek guidance from the PNO, and also pointed out that parties seeking to apply the exemption bear the burden of showing its applicability. Ms. Kuritz also provided an overview of the DOJ's most recent enforcement action regarding the passive investment exemption—the 2016 case against ValueAct. Ms. Walsh explained several indicia of conduct inconsistent with the passive investment exemption, as set forth in the rule's Statement of Basis and Purpose: (1) nominating a candidate to the board of directors of the issuer; (2) proposing corporate action requiring shareholder approval; (3) soliciting proxies; (4) having a controlling shareholder, director, officer, or employee simultaneously serving as an officer or director of the issuer; (5) being a competitor of the issuer; or (6) doing any of the foregoing with respect to any entity directly or indirectly controlling the issuer.

The sixth hypothetical considered how the analysis changes if, at the time of filing, Big Tex really did have a passive investment intent but subsequently took actions inconsistent with passive investment. This question raised a difficult and fact-specific issue of whether Big Tex had the requisite intent at the time of filing; in theory, subsequent changes in intent are not considered. Mr. Kaiser explained that the question, therefore, is one of proof, and circumstances showing that Big Tex lacked intent inconsistent with the passive investment exemption support the argument that the company remains exempt from the filing requirements.

The seventh hypothetical was similar to the fourth hypothetical, and illustrated that so long as Big Tex completes the acquisition within one year of filing, the company may acquire additional shares of Red River up to the next filing threshold over the next five years. If, however, Big Tex's subsequent acquisitions exceed the next transaction value threshold (keeping in mind that the value of voting securities are aggregated), another filing would be required.

Foreign Investment Exemption Hypotheticals

The final set of hypotheticals dealt with foreign exemptions. In the first and second hypotheticals, Big Tex acquired 100% of the voting securities of Big Royal, a British company with its principal offices in London, for $5 billion. Big Royal has $1 billion in assets located outside of the United States and $45 million in assets located in the United States, but no sales in or into the United States. Although this transaction certainly exceeds the minimum HSR thresholds, it is exempt from the reporting requirements under § 802.51 as an acquisition of voting securities of a foreign issuer. The second hypothetical asked whether the transaction would be reportable if Big Royal was a U.S. person. Here, the § 802.51 exemption does not







apply because Big Royal is a U.S. person. The panelists emphasized the need to look at U.S. assets separately from foreign assets—in this case the parties would apply the "look through" test under § 802.4, which exempts the acquisition of an issuer holding assets which would be exempt if acquired directly. Here, the $1 billion in foreign assets is exempt under § 802.50 and the $45 million U.S. asset acquisition does not meet the size of transaction test. Thus, this transaction is not reportable. Ms. Walsh highlighted the § 802.4 tip sheet on the PNO's website, which helps parties analyze these types of transactions.

Even if the foreign assets contributed $45 million in U.S. sales in the most recent year, as posited by the third hypothetical, the transaction would not be reportable because the $45 million in revenue does not exceed the filing threshold. However, if those foreign assets contributed $125 million in U.S. sales in the most recent year, as posited by the fourth hypothetical, the transaction would be reportable because it would exceed the current $80.8 million filing threshold. For the fifth hypothetical, the panelists pointed out that § 802.4 does not affect the size of the transaction or filing fee; it simply makes the transaction reportable or non-reportable. Thus, to the extent that this transaction is reportable, the filing fee is based on the entire value of the transaction, $5 billion, and therefore would be $280,000. The sixth hypothetical explained that under § 802.4, sales attributable to U.S. assets are irrelevant; if the foreign asset part is not reportable, then whether the transaction is reportable depends on the value of the U.S. assets, not the sales attributable to those assets.

The seventh and eighth hypotheticals looked at the reporting requirements for acquisitions of foreign issuers with product sales into the U.S. The seventh hypothetical asked whether the transaction would be reportable if Big Royal had no U.S. assets but sells products to unaffiliated distributors who then sell the products to U.S. customers. The panelists explained that the transaction is not reportable because third party sales of Big Royal's products do not count as sales "in or into the U.S." by Big Royal unless the products are specifically designed for the U.S. market and would not be sold in any other market. Mr. Kaiser explained that certain pharmaceuticals may meet this U.S. market requirement. If the products were sold directly to U.S. customers, as proposed by the eighth hypothetical, the rules require the parties to look at where title and risk of loss pass to the buyer. If title and risk of loss pass outside of the U.S., the sale is not "in or into the U.S." even if the buyer is a U.S. company.

The ninth hypothetical asked whether the analysis would be different if Big Royal provided services to U.S. customers instead of products. The answer depends on where the services are rendered. If the services are provided outside of the U.S., then they are not considered sales "in or into the U.S." and would not contribute towards reporting thresholds. The panel emphasized that in this analysis, the nationality of the customer is irrelevant.

The tenth hypothetical dealt with moveable assets. It asked whether the transaction would be reportable if Big Royal was a shipping company owning $100 million in assets with no sales in or into the U.S. and $200 million of ships. Here, the registration of each ship determines whether it is a U.S. or foreign asset. If the

fair market value of the ships registered in the U.S. exceeds the current $80.8 million threshold, the transaction is reportable. Regarding foreign ships, revenues derived from shipping *to or from* the U.S. would be considered sales "in or into the U.S." Ms. Walsh then discussed how the PNO treats other types of movable assets, such as satellites and undersea cables, and referred the audience to interpretations on the PNO website for further information.

Finally, hypotheticals eleven and twelve examined minority acquisition of foreign issuers. In the eleventh hypothetical, Fund A, formed and having its principal place of business in the Cayman Islands, acquired 40% of the outstanding securities of Big Royal, a foreign issuer with $100 million in assets in the U.S., for $5 billion. Mr. Kaiser characterized this transaction as a "foreign-on-foreign" transaction, which is exempt from reporting requirements under § 802.51(b)(1) so long as, as a result of the transaction, the foreign person will not hold 50% or more of the outstanding voting securities of the issuer. Hypothetical twelve illustrated that this exemption for acquisitions of less than 50% of the voting securities of a foreign issuer only applies where the acquiring person is a foreign person; if Fund A had its principal offices in New York, the transaction would be reportable.

2017 ABA Spring Meeting Panel Summary: What Next for the Green Economy

By James Henry Metter[109]

Clean technology and renewable energy have become increasingly important parts of the U.S. economy in recent decades. On March 29, 2017, as part of the ABA Antitrust Section Spring Meeting, the Exemptions & Immunities and Transportation & Energy Industries Committees presented a panel to explore the role of antitrust in the development of clean technology and the expansion of renewable energy. The speakers were Bruce McCulloch, a partner in Freshfields Bruckhaus Deringer US LLP; Neely Agin, a partner in Norton Rose Fulbright US LLP; David Zlotow of the California Independent System Operator ("ISO") Corporation; Katherine Phillips, counsel at Caldwell Boudreaux Lefler PLLC; and Jeremy Verlinda of the Brattle Group. Ms. Phillips also served as chair for the discussion.

Mr. McCulloch began the discussion. Drawing on his experience in mergers, he explained that, instinctively, one would not expect policy objectives like a "green agenda" to play a role in merger review. He then considered a number of recent mergers with a clean technology dimension, including Panasonic / Sanyo (2010), which concerned rechargeable batteries, and GE / Alstom (2015), which concerned environmentally-friendly gas turbines. He noted that the approach of the Department of Justice ("DOJ") and Federal Trade Commission ("FTC", and together with the DOJ, the "U.S. Antitrust Agencies") in these cases had been based on orthodox antitrust principles. This is also true of the recent approval by the European Commission (EC) of the Siemens / Gamesa deal (2017).

Mr. McCulloch noted, however, that there are ways in which government regulation and policy affects the antitrust analysis. For instance, in the 1990s and early 2000s, the FTC adopted a relatively aggressive position towards mergers affecting the market for gas that was compliant with the standards imposed by the California Air Resources Board (known as "CARB gasoline"). In so doing, the FTC noted that the State of California's gasoline regulations had created distinct geographical and product markets for CARB gasoline and, further, identified new product markets as the State of California tightened regulations over time (e.g., a market for "CARB 1 gasoline", "CARB 2 gasoline," etc.).[110] More recently, in 2013, concerns regarding the market for CARB gasoline were again raised in the context of Tesoro Corporation's proposed acquisition of BP's southern California refining and marketing business. However, in contrast to the aggressive enforcement position the FTC had taken a decade earlier, the FTC chose not to take enforcement action against the acquisition. This was on the basis that improving vehicle efficiency and the use of renewable transportation fuels had reduced demand

---

[109] James Henry Metter is a Trainee Solicitor at Freshfields Bruckhaus Deringer LLP.
[110] Examples of mergers involving CARB gasoline in the 1990s and early 2000s include: Exxon / Mobil (2001), Valero / UDS (2002), and Chevron / Texaco (2002).

for CARB gasoline and that this would restrain Tesoro's ability to raise prices post-acquisition.

In conclusion, Mr. McCulloch argued that it is encouraging that the U.S. Antitrust Agencies have not allowed non-economic factors to affect their analysis. He stressed the importance of antitrust authorities remaining neutral with respect to policy initiatives, given the speed with which political and technological changes can affect the market. To do otherwise would be to inject an element of uncertainty into the marketplace that would risk destabilizing business confidence.

Ms. Agin began her remarks with a discussion of the electric power market. She noted that the traditional electric power model relied on large generating power stations, located far from the power center, and that the supply chain was dominated by heavily integrated companies who enjoyed monopoly status. This has now transformed into more of a network model, with the introduction of competition at certain levels of the supply chain (e.g., generation and retail) while monopolies remain at others (e.g., distribution). Incumbents still control distribution, but there are now a greater number of power sources, including local power plants and on-site generation (e.g. solar panels). Recent technological developments (e.g., in the ability to store energy), combined with pressure from climate change advocates and government incentives (e.g., feed-in tariffs) have further affected the dynamic. In the context of such a dynamic and complex market, Ms. Agin agreed with Mr. McCulloch's view that authorities should stick to orthodox antitrust principles, while demonstrating an understanding of the peculiarities of the electric power market where appropriate. Antitrust, she noted, is not the proper place for carrying out the public policy exercise of balancing the demands for a competitive marketplace with environmental concerns.

Ms. Agin pointed to a number of examples that highlight the particular issues in the electric power market. Outside the merger context, she noted the ongoing litigation being brought by SolarCity Corporation against the Salt River Project in Arizona, which highlights the potential for conflict between incumbents and new market entrants (and was discussed further by Mr. Verlinda - see below).[111] Ms. Agin also drew the audience's attention to the concerns regarding anti-competitive effects that arose in the context of Exelon / PepCo (2016) (regarding the merged entity's control over both generation and distribution) and the abortive Exelon / PSE&G (2006) deal (regarding the merged entity's incentives to increase prices combined with its ability to influence supply).

Mr. Zlotow began his talk with a brief description of the role played in electricity markets by ISOs. He explained that the RTO / ISO model is used in most of North America and Europe and outlined the regulatory framework for electricity markets. He noted that antitrust rests on top of existing regulation from the Federal Energy Regulatory Commission ("FERC"), which has its own statutory merger review authority and that ISOs also have their own rules to mitigate market power.

---

[111] SolarCity Corp. v. Salt River Project Agric. Improvement & Power Dist., No. 15-17302 (9th Cir., filed Nov. 23, 2015).

Mr. Zlotow highlighted a number of features of the electricity market that are relevant to the antitrust analysis:

(a) *Variability*. A degree of variability is inherent in certain renewable sources like solar and wind. Variability can be planned (e.g., through weather forecasting) or unplanned (e.g., if the weather forecast is wrong).

(b) *Over-generation*. This is a particular issue in California - especially at night, when winds increase and also when natural gas plants have to be brought online to ensure they are ready in the morning. It can result in pricing going negative (i.e., paying generators not to produce, or to shut-off production).

(c) *The duck curve*. The so-called "duck curve" is a graph showing the total energy load on the California grid, net of energy from solar and wind sources. The duck-like shape demonstrates that the load increases (in the early evening) just as renewable energy production falls away (i.e. sunset) which creates a ramping problem as energy from non-renewable sources have to be quickly brought online. Mr. Zlotow used the duck curve to demonstrate the need for flexibility in the market in order to satisfy the sudden ramp that occurs around sunset. Absent energy storage solutions, this can currently only be provided by fossil fuels.

Based on these factors, Mr. Zlotow suggested a number of reasons why antitrust has not yet played a significant role in the market for renewables:

(a) *Intermittency / dispatchability*. The intermittent nature of renewable sources has meant, historically, it has been difficult for generators to exercise market power, because they have not been able to control their output.

(b) *Renewables as a small part of capacity*. Historically, renewable energy has played a small role in the overall supply of energy.

(c) *Renewables as incremental capacity*. Historically, renewable energy has played an incremental role in the supply of energy, i.e., it has supported, but not supplanted, existing fossil fuel sources.

(d) *Incentives*. Currently, government incentives (e.g. tax credits) incentivize renewable energy operators to maximize generation irrespective of demand. As a result, there is no real incentive for companies involved in renewable generation to engage in anti-competitive behavior, as they are paid by the government to run flat-out regardless of market conditions.

Mr. Zlotow, however, suggested a number of reasons why, looking to the future, antitrust might play an increased role. First, improvements in weather

forecasting and technological developments (e.g., the use of feathering in wind turbine control systems) have made renewable energy more dispatchable. Second, renewables are playing an increasingly significant role regarding total capacity, especially in certain regions. For example, California has passed legislation aiming to source 33% of its energy from renewable sources by 2020 and 50% by 2030. Third, renewable generation is beginning to affect thermal generation and so may no longer be incremental. For example, the success of renewables is leading owners of gas units to retire their units before the end of their lifecycles. Renewables are also becoming more attractive to generators, because a generator does not need to spend money procuring wind or solar in the same way a generator needs to procure fossil fuels. Fourth, owners of solar generation are currently claiming to face economic pressure and so there may be a degree of consolidation, which could give rise to antitrust scrutiny. Mr. Zlotow concluded by noting that, to the extent antitrust has been a backburner issue with regard to renewables, that is likely no longer to be the case going forward.

Ms. Phillips approached the subject from a different perspective, focused on liquid pipeline work. She explained that the rates liquid pipeline owners can charge is subject to statutory regulation, which requires FERC to be satisfied that the rates being charged are "just and reasonable". In certain circumstances, however, it is possible to argue that there is sufficient competition to regulate the pricing and so "market based" rate-setting will lead to fair and reasonable rates, with no need for further intervention on pricing.

Ms. Phillips outlined how changes in clean energy policies could affect the regulatory analysis of pipeline rates. For example, electric vehicles are likely to decrease demand for crude oil. Similarly, as emission standards are changed, trucking may become a less viable alternative to pipelines and so increase demand for pipeline transportation.

The final speaker, Jeremy Verlinda, sought to build on Ms. Agin's earlier discussion of the SolarCity v. Salt River case to demonstrate how conflicts can develop between traditional energy and the growing green energy sector, and the role antitrust might play in this context. Mr. Verlinda explained how SolarCity operates, namely that it brings together investors who buy tranches of solar panels, thus providing the large capital investment required to install rooftop solar paneling, and makes a profit because effectively the states pay customers to buy the energy their solar panels produce (under a system known as "net metering"). The growth of solar, however, poses problems for the grid, which depends on its rate base to recoup its costs. The traditional mechanism by which the grid recovers its costs is by volumetric rates (i.e. those who draw more energy pay more). A significant switch from traditional energy sources to solar will have a marked effect on volumetric rates, leaving distributors facing a shortfall. At the same time, however, the demand for an effective grid system remains, given the need for a flexible energy supply that currently can only be provided by traditional energy sources. Faced with this shortfall, distributors can either raise volumetric rates (but this penalizes consumers who have not switched to using solar) or introduce a fixed fee for solar users, which resembles a discriminatory fee.

This dynamic is at the heart of the SolarCity litigation. In response to the imposition of a fee on solar users, SolarCity brought an antitrust action against Salt River, alleging that the Salt River Project - which also owns a large amount of generation (which directly competes with rooftop solar) has committed an abuse of monopoly power and is deterring competition and market entry. Should the case progress beyond the issue of whether Salt River is immune from the action under the state action immunity doctrine, Mr. Verlinda suggested a number of key questions that will determine its outcome:

(a) whether the Court finds that rooftop solar is actually in competition with traditional power generation and the distribution network (thereby opening up grounds for pursuing antitrust harm); and

(b) whether the Salt River Project can mount an efficiency / offset defense, essentially arguing that if they did not implement the solar fee, the network would fall apart. This would draw on arguments and fears about the potential for a utility "death spiral", where the grid's inability to recover costs causes it to shrink.

Mr. Verlinda concluded by highlighting that as renewable energy's role in power generation increases, the tension with the grid - which remains vital in order to maintain the ability to service flexible demand - will become ever more pronounced.

CASE UPDATES / MATTERS TO WATCH

ENERGY

Judge Enjoins Energy Solutions' Proposed Acquisition of Waste Control Specialists

Following a trial on the merits, on June 21, 2017, U.S. District Court (D. Del.) Judge Sue Robinson permanently enjoined the proposed acquisition of Waste Control Specialists ("WCS") by Energy Solutions. In her opinion released on July 12, 2017, Judge Robinson found that the proposed merger was likely to substantially lessen competition in the market for disposal of higher-activity low level radioactive waste ("LLRW") and lower-activity LLRW. In reaching this conclusion, Judge Robinson rejected the defendants' defense that WCS was a "failing firm." She found that the defendants' failed to establish that Energy Solutions was the only available purchaser—a required element of the failing firm defense—because WCS's parent company Valhi did not make a good faith effort to elicit reasonable alternative offers for WCS. On June 23, 2017, two days after the order was issued blocking the transaction, Valhi announced that it terminated the purchase agreement for the sale of WCS to Energy Solutions.

GE/Baker Hughes Merger Cleared by DOJ with Consent Decree

On July 3, 2017, General Electric announced the completion of the combination of its oil and gas business with Baker Hughes to create the world's second-largest oilfield service provider by revenue. The transaction was previously made public on October 31, 2016. On June 12, 2017, DOJ announced it was requiring the parties to divest GE's Water & Process Technologies business to resolve competition concerns. According to the DOJ's complaint, which was filed at the same time as the proposed settlement, the combined company would control 50% of the U.S. market for specialty chemicals and services used by refineries to process crude oil and natural gas, resulting in higher prices, reduced service and diminished innovation. The divestiture is to take place after the closing of the Baker Hughes transaction. GE agreed in March 2017 to sell the divestiture assets to Canadian pension fund manager Caisse de Dépôt et Placement du Québec and French waste and water company Suez.

In conducting its investigation, the DOJ cooperated closely with competition authorities around the world, including the European Commission, Canadian Competition Bureau, and Australian Competition and Consumer Commission. The European Commission cleared the deal without conditions on May 31, 2017.

California AG Attempts to Block Valero's Acquisition of Plains All American Assets

California Attorney General Xavier Becerra filed suit on June 30, 2017, seeking to block an acquisition by Valero Energy Corporation of certain assets currently owned by Plains All American Pipeline, L.P. as being in violation of federal antitrust laws. However, the Attorney General's request for a temporary restraining order to block

the transaction was recently denied by the U.S. District Court for the Northern District of California. Both Valero and Plains seek to challenge the blockage of the deal, which would expand Valero's capacity at the terminals in Martinez and Richmond, California. The terminals would serve Valero's refinery in Benecia, in the Bay Area. According to the merging parties, the FTC reviewed the deal and concluded that no action was warranted.

TRANSPORTATION

Qatar Airways Announces Plan to Acquire a 10% Stake in American Airlines

On June 22, 2017, Qatar Airways announced its intent to purchase 10% of the stock of American Airlines. Qatar Airways is initially planning on acquiring 4.75% of American on the stock market, however, any additional purchases above 4.75% would require approval by American's board of directors. American announced that it was informed that Qatar Airways pulled and refiled its HSR filing for the initial stock acquisition on July 10, 2017. American has been a vocal critic of the Gulf carriers, including Qatar Airways, claiming that they are subsidized by their governments, in breach of the Open Skies agreements between the Qatar and the UAE.

Recently, Qatar Airways has acquired minority stakes of several other airline groups, including LATAM in Latin America and Meridiana in Europe. Qatar Airways also owns 20% of British Airways' parent, IAG, a close partner to American.

Couche-Tard/CST Gas Station Deal Cleared by FTC with Divestitures

On June 26, 2017, ten months after Alimentation Couche-Tard Inc. ("ACT") agreed to a proposed $4.4 billion acquisition of CST Brands through its wholly owned subsidiary, Circle K Stores Inc., the FTC announced its conditional clearance of the transaction. Under the terms of the proposed consent agreement, ACT must divest retail outlets and associated assets in 71 local markets in 16 metropolitan statistical areas ("MSAs") to Empire Petroleum Partners, an FTC approved buyer, to address concerns that the transaction would lessen competition for the retail sale of gasoline and retail sale of diesel in those markets. The FTC determined that the geographic markets for each local retail gas and retail diesel market are highly localized, ranging from a few blocks to a maximum of three driving miles from an overlapping fuel outlet. Were the transaction to proceed without divestitures, the complaint alleges that the transaction would have resulted in a monopoly in ten local markets, reduced competition from three to two independent firms in 20 local markets, and reduced competition from four to three independent firms in the remaining 41 local markets, increasing the likelihood that ACT would unilaterally exercise market power and facilitating collusive or coordinated interaction among the remaining competitors.

Delta and Korean Airlines Seek Approval of Proposed Joint Venture

On June 29, 2017, Delta Air Lines and Korean Airlines announced their agreement to enter into a "fully integrated" joint venture for the operation of trans-Pacific flights between the U.S. and Asia. On July 18, 2017, the parties announced that they

filed an application for approval with South Korea's Ministry of Land, Infrastructure, and Transportation. Delta and Korean Airlines already received antitrust immunity from the Department of Transportation ("DOT") for an alliance agreement back in 2002, however, both Jet Blue and Hawaiian Airlines and have filed letters with DOT requesting that it review the proposed joint venture *de novo*, citing significant changes in the trans-Pacific market. And, on July 19, 2017, JetBlue filed a formal motion asking the DOT to institute a proceeding to review the 2002 grant of antitrust immunity.

FTC Reportedly Investigating Uber for Data Privacy Violations

Amidst other reported turmoil at ride-hailing company Uber, including founder Travis Kalanick stepping down as CEO, reports surfaced in June 2017 that the FTC is investigating the company for potential data privacy violations. According to those same reports, the investigation appears to be focused on data-handling mishaps and it is speculated that this may include Uber's "god view," a tool that allows Uber employees to monitor the location of users. This reported investigation follows the FTC's January 2017 announcement that Uber agreed to pay $20 million to settle charges that it made misleading claims about the annual and hourly wages its drivers were likely to earn.

Transportation and Energy Industries
COMMITTEE OFFICERS