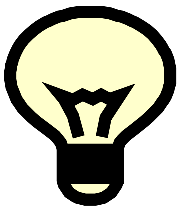

Recent changes to ACPERA: the Leniency Program

Page 6

The latest on Leegin and Resale Price Maintenance

Page 10

Developments in Merger Review in Canada

Page 15

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Comcast/NBCU and the Resurgence of Vertical Merger Enforcement

By Logan Breed

The Federal Communications Commission ("FCC") and the Antitrust Division of the Department of Justice ("DOJ") recently approved a joint venture between Comcast Corporation ("Comcast"), General Electric ("GE"), and NBC Universal, Inc. ("NBCU"). GE had an 88 percent ownership interest in NBCU. The transaction forged a uniquely vertically integrated media and entertainment company that controls both the largest cable programming distribution network in the US and one of the largest creators of television programming and feature films in the US. The deal required the approval of both the FCC and DOJ, and their review of the transaction lasted over a year. Both agencies ultimately approved the deal, but not before they required significant concessions from the parties.

While there was horizontal overlap between the parties because both contributed programming assets to the venture, the primary regulatory concern was related to vertical issues – the likely effect on competition caused by the participation of a cable company, like Comcast, in a venture which would own and control such significant programming content. The agencies believed that the venture would be able to disadvantage Comcast's competitors by withholding "highly valued video programming needed by Comcast's video distribution rivals to compete effectively."[1]

In addition to giving insight into the current cooperative relationship between FCC and DOJ in the merger review process, the Comcast/NBCU deal provides several important lessons for antitrust practitioners and in-house counsel considering future transactions. First, as DOJ demonstrated in this deal and in other recent merger reviews, vertical transactions will receive close scrutiny if DOJ perceives that the transaction may change the parties' incentives to serve competitors of one or both parties. Second, the steps that DOJ will take to correct the perceived potential harm in vertical transactions may include divestitures, behavioral remedies, or both. Third, DOJ is willing to take action to protect competition even in nascent markets. Finally, antitrust merger clearance

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[1] Competitive Impact Statement, *U.S. v. Comcast Corp.*, Case No. 1:11-cv-00106 (D.D.C. Jan. 18, 2011) ("CIS"), at 1.

increasingly requires remedies that address the specific concerns of individual competitors who have taken an active role in the merger review process.

"The transaction marks the first time that a US cable company has owned a major television network, and therefore it received significant scrutiny at both the DOJ and FCC."

The Transaction

Comcast is the largest cable company in the US, with $34 billion in revenue from its cable business in 2009, and it is the largest Internet Service Provider ("ISP") in the US, with over 16 million subscribers. Comcast also owns or has partial ownership interests in national cable programming networks such as E!, Versus, G4, Golf, Style, MLB Network, NHL Network, PBS Kids Sprout, Retirement Living Television, and TV One. Comcast also has controlling or partial interests in numerous regional sports networks. Finally, Comcast has an Internet video service called Fancast.

NBCU has a wide stable of programming networks and other content providers. It owns the NBC and Telemundo broadcast networks, as well as 26 local owned and operated television stations. In addition, NBCU owns or has a partial interest in national cable programming networks such as Bravo, CNBC, MSNBC, USA, Oxygen, A&E Television Networks (including the History, Biography, and Lifetime networks), and The Weather Channel. NBCU also owns Universal Pictures, Universal Studios, and Focus Films, which produce films for theatrical and DVD release. Finally, NBCU is a founding partner and 32 percent owner of Hulu LLC, a joint venture with News Corp., the Walt Disney Company, and a private equity investor. Hulu has become one of the most successful US online video distributors ("OVDs"), which are websites that offer broadcast and cable network programming over the Internet.

Comcast and GE announced the deal on December 3, 2009. Comcast agreed to pay $6.5 billion to GE, and both parties agreed to contribute assets to the new joint venture. Comcast contributed all of its cable programming assets, but not its cable systems or Fancast. GE contributed all of the assets of NBCU, including its Hulu interest, and GE also promised to acquire and contribute the 12 percent of NBCU that it did not already own. The agreement gave Comcast a 51 percent interest in the joint venture, with GE holding the other 49 percent. The joint venture has its own Board of Directors, with Comcast controlling three directors and GE controlling two. Board decisions are made by a simple majority, so Comcast has the unilateral ability to control the board.

The marketplace shifted considerably in the nearly two years since the parties began negotiating the transaction. In particular, OVDs have grown in popularity, and their popularity appears only to be growing further. The number of adult Internet users who watch full-length television shows online is expected to reach 72.2 million in 2011. Significant beneficiaries of the consumer movement toward online video include Netflix (which has started to pivot from the DVD-by-mail business model to become a streaming video company), Apple, Amazon, and Hulu. The success of OVDs creates significant risk for Comcast's core business – selling subscriptions to cable television – because it creates a more flexible and possibly cheaper method of consuming the same content that is available in a Comcast cable package. Comcast believed that the joint venture would enable Comcast to compete more effectively in this new world. According to the parties, one prominent business justification for the transaction was that it would "facilitate the launch of new content as well as innovative distribution opportunities through multiple platforms in and out of the home."[2]

The Antitrust Review Process

The transaction marks the first time that a US cable company has owned a major broadcast television network, and therefore it received significant scrutiny at both the DOJ and FCC. DOJ reviewed more than one million business documents from the parties, interviewed more than 125 third parties, consulted with industry and economic experts, and even organized product demonstrations. DOJ and FCC both stated that they consulted extensively with each other

[2] Brian Roberts, "Comcast and GE Announce NBC Universal Joint Venture," December 3, 2009, available at http://blog.comcast.com/2009/12/comcast-and-ge-announce-nbc-universal-joint-venture.html.

throughout the review process to ensure that they created "effective, efficient and consistent remedies."[3]

As noted above, DOJ's investigation focused on the likely vertical effects of the transaction. Vertical mergers have the potential to harm competition by changing the combined company's incentive or ability to serve upstream or downstream rivals. For example, the vertically integrated company may be able to undermine competition in a downstream market by denying, raising the price of, or diminishing the quality of a necessary input to its downstream competitors. The antitrust agencies have not challenged vertical mergers frequently in the past decade. However, under the current Administration, DOJ has expressed an interest in "explor[ing] vertical theories and other new areas of civil enforcement, such as those arising in high-tech and Internet-based markets,"[4] and it has acted to reinvigorate antitrust review of vertical transactions. For example, in April 2011, DOJ approved Google's vertical acquisition of ITA Software, a company that provides the software used by travel websites such as Orbitz to produce flight search results. The transaction involved no horizontal overlap because Google did not have any flight search software that competed with ITA; in fact, it did not even have a travel website that competed with ITA's customers (although the purpose of the acquisition was to facilitate the creation of a travel search website). DOJ required the parties to agree to several remedies, including a commitment to continue providing ITA's software to competing travel websites and a firewall provision that prevents non-ITA Google travel employees from receiving other ITA customers' competitively sensitive information.[5]

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DOJ articulated two potential manifestations of vertical harm in the Comcast/NBCU deal. First, DOJ believed that the transaction "had the potential to stifle new online competition."[6] DOJ feared that Comcast would have an incentive to discriminate against OVDs and impede their development by (1) charging higher license fees for NBCU content, (2) imposing different terms than Comcast negotiated for itself, or (3) withholding NBCU content entirely. DOJ noted that NBCU "has been one of the content providers most willing to experiment with different methods of online distribution,"[7] and the transaction could undermine that willingness to encourage innovation because it "removes NBCU content from the control of a company that supported the development of OVDs and places it in the control of a company that views OVDs as a serious competitive threat."[8] DOJ also found that NBCU's 32 percent ownership interest in Hulu was problematic because Hulu competes with Comcast's cable subscription business, and Comcast would have the ability to hamper Hulu's development by blocking new major strategic actions. In short, DOJ feared that Comcast would act to stifle OVDs in their infancy before they had the chance to become significant competitors to Comcast's traditional cable business.

Second, DOJ also expressed concern that the transaction would affect competition between Comcast and other traditional multichannel video programming distributors ("MVPDs") such as competing cable and satellite companies. DOJ postulated that NBCU as a standalone entity had an incentive to make its content available in multiple ways to maximize its license fees and advertising revenues. However, the joint venture may have a different incentive – its profit maximizing strategy may be to withhold NBCU content or extract supracompetitive fees for the content from competing MVPDs, thereby weakening Comcast's rivals. DOJ noted that Comcast has already engaged in such behavior, citing as an example Comcast's refusal to provide a regional sports network to competing satellite providers in Philadelphia.

As is often the case in high profile antitrust merger reviews, third parties played an active role in the process. One example is Bloomberg, which strongly advocated before the FCC and DOJ to encourage the agencies to prohibit Comcast from discriminating against competing content

3 Assistant Attorney General Christine Varney, Remarks at Briefing on Comcast/NBCU Joint Venture, Jan. 18, 2011, available at http://www.justice.gov/atr/public/speeches/266156.htm ("Varney Statement").

4 Assistant Attorney General Christine Varney, "Vigorous Antitrust Enforcement in This Challenging Era," May 12, 2009, available at http://www.justice.gov/atr/public/speeches/245777.htm.

5 US Department of Justice, Competitive Impact Statement, *US v. Google Inc.*, (April 8, 2011), available at http://www.justice.gov/atr/cases/f269600/269620.pdf.

6 Varney Statement at 1.

7 CIS at 8.

8 *Id.*

providers.[9] Bloomberg was concerned that Comcast would place its news channels such as CNBC and MSNBC together with some other news channels in the Comcast channel lineup (also known as a “neighborhood” of channels), but would exclude other news channels from the neighborhood in an attempt to discriminate against them.

The Consent Decree

DOJ’s consent decree, which was issued in tandem with the FCC’s order, addressed both of the vertical harms discussed above. Since the FCC decision focused primarily on remedying potential harm to MVPDs and DOJ was largely satisfied that the FCC had addressed that issue, the DOJ consent decree provisions were primarily directed at protecting OVDs. DOJ required both conduct remedies and structural relief (i.e., divestiture).

"Since the FCC decision focused primarily on remedying potential harm to MVPDs and DOJ was largely satisfied that the FCC had addressed that issue, the DOJ consent decree provisions were primarily directed at protecting OVDs. DOJ required both conduct remedies and structural relief (i.e., divestiture)."

First, the joint venture must license its programming to OVDs under two scenarios. Comcast agreed to license NBCU content to OVDs on terms that are “economically equivalent” to the terms on which it licenses that content to MVPDs.[10] DOJ used NBCU’s current contracts with MVPDs – including those that do not compete with Comcast – as proxies for the content and terms under which the joint venture must license to OVDs. The joint venture also must license content (whether broadcast, cable, or film) to OVDs on terms that are economically equivalent to those offered to the OVD by competing content providers. For example, if CBS provides an OVD with a primetime television show within 48 hours of its original airing, then NBCU must also provide “a comparable set” of similarly situated shows to the OVD within 48 hours. DOJ believed that this provision would ensure that NBCU’s licensing practices will “reflect the licensing trends of its peers as the industry evolves.”[11]

Second, the consent decree contains several provisions designed to protect Hulu. It ordered Comcast to relinquish its management rights in Hulu so Comcast cannot use NBCU's partial ownership of Hulu to diminish its competitive significance. DOJ also prohibited Comcast from receiving any competitively sensitive information from Hulu. Finally, DOJ required NBCU to continue providing content to Hulu that is commensurate with the content provided by Hulu’s other media owners (i.e., Disney and News Corp.).

Third, the consent decree prohibits the joint venture from discriminating against, retaliating against, or punishing any content provider, production studio, broadcast network, affiliate, or cable programmer for licensing their content to OVDs. The provisions also prohibit Comcast and NBCU from retaliating against OVDs that invoke any provisions of the consent decree or the FCC order or provide information to DOJ regarding Comcast’s compliance with the consent decree.

Fourth, the consent decree prohibits Comcast from using its influence as the largest US MVPD or as the licensor of “important video programming” to enter into restrictive agreements, including most types of exclusive licensing provisions. While short-term exclusive rights are fairly common in the industry, DOJ’s concern was that Comcast would use exclusivity provisions to prevent content providers from licensing to OVDs “for a longer period than the content producer ordinarily would find economically reasonable.”[12] Therefore, the consent decree limits Comcast’s ability to enter into exclusive arrangements to those that are “common and reasonable in the industry” as defined by (1) the parties’ practices before entering into the joint venture and (2) the practices of NBCU’s video programming peers.

Fifth, the joint venture must adhere to the net neutrality provisions recently enacted by the FCC, as well as related restrictions. This is intended to ensure that Comcast does not discriminate between its own managed services and other broadband content such as traffic from OVD services.

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9 *See, e.g.,* Letter from Stephen Diaz Gavin (representing Bloomberg LP) to Marlene Dortch (FCC Secretary), Oct. 18, 2011, available at http://fjallfoss.fcc.gov/ecfs/document/view?id=7020917582.

10 Proposed Final Judgment, *US v. Comcast Corp.*, Case No. 1:11-cv-00106 (D.D.C. Jan. 18, 2011) at IV.A, available at http://www.justice.gov/atr/cases/f266100/266160.htm.

11 CIS at 10.

12 *Id* at 11.

Comcast also has agreed to maintain the high-speed Internet service it currently offers to its customers.

Finally, the FCC decision, with which DOJ agreed, contained several provisions designed to protect competing MVPDs. It also included remedies that primarily benefitted small groups of specific competitors. For example, in response to Bloomberg's concerns regarding discrimination against rival news channels, the FCC decision required that "if Comcast 'neighborhoods' its news (including business news) channels, it must include all unaffiliated news (or business news) channels in that neighborhood."[13]

" These lessons may seem to create a tougher road for future vertical transactions, but the key lesson is that practitioners and in-house counsel considering vertical transactions should engage in detailed up-front antitrust analysis of the transaction to ensure that the parties understand the antitrust risk and can work proactively to address any possible antitrust issues early in the process."

Conclusions

The Comcast/NBCU consent decree yields several important lessons for antitrust clearance of future transactions. First, DOJ may subject a transaction with possible vertical issues to intense scrutiny and will extract significant remedies if it believes that the transaction may harm competition in a downstream or upstream market because it may change the merged company's incentives to deal with competitors. Moreover, DOJ may intervene even where the transaction does not threaten to eliminate completely competition in a downstream or upstream market. Traditional vertical merger theory is predicated on the concept of "foreclosure," i.e., a complete or near-complete foreclosure of an essential input. In other words, if downstream competitors can get the input from someone else, the transaction cannot be anticompetitive. Here, DOJ did not allege that NBCU's content was essential to MVPDs or OVDs – NBCU merely has "important" programming. This suggests that DOJ may now believe the bar for foreclosure in vertical transactions is lower than in the past. Second, while the traditional remedy for a vertical transaction with anticompetitive implications has been a conduct remedy prohibiting the merged entity from abusing its power over downstream or upstream competitors, the remedy in Comcast/NBCU included both a robust set of conduct remedies and some structural remedies involving Comcast's ownership of Hulu. This may indicate that DOJ is willing to pursue divestiture or other structural relief in vertical deals, as it did in both Comcast/NBCU and the Ticketmaster/Live Nation transaction. Third, DOJ clearly intends to take action to protect nascent markets where the nature and extent of competition is still unclear (and therefore prior administrations have been reluctant to impose merger remedies). As Assistant Attorney General Christine Varney noted, the consent decree "demonstrates how the antitrust laws offer critical protection to nascent markets as well as consumers in the digital age." These lessons may seem to create a tougher road for future vertical transactions, but the key lesson is that practitioners and in-house counsel considering vertical transactions should engage in detailed up-front antitrust analysis of the transaction to ensure that the parties understand the antitrust risk and can work proactively to address any possible antitrust issues early in the process.

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[13] Federal Communications Commission, Memorandum Opinion and Order, *In the Matter of Comcast Corp.*, Jan, 18, 2011, at 4, available at http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-11-4A1.doc.

Will the Recent Changes to ACPERA, the Civil Damage Limitation Statute, Actually Harm the Antitrust Division's Leniency Program?

By James M. Griffin & Kevin R. Sullivan

The United States Department of Justice Antitrust Division's 1993 Corporate Leniency Policy, is the Division's "most effective investigative tool," providing government prosecutors "unparalleled information from cartel insiders about the origins and inter-workings of secretive cartels."[1] Since 1996 over 90% of the more than $5 billion in corporate fines imposed in antitrust criminal cases have resulted from investigations assisted by leniency applicants. In 2004 Congress passed the Antitrust Criminal Penalty Enhancement and Reform Act of 2004 ("ACPERA"), which was designed to further enhance the Division's Corporate Leniency Policy and improve the efficiency of damage recovery by victims of antitrust crimes by relieving the leniency applicant of the threat of treble damage and joint and several liability so long as it cooperates with antitrust civil damage plaintiffs. Specifically, section 213(a) of ACPERA provides that the amnesty applicant can limit its civil damage exposure to single damages caused by its own sales, *i.e.*, it can obtain relief from treble damages and from joint and several liability faced by all other participants in the cartel. However, last year, apparently in reaction to the heightened pleading standards in civil cases established by *Bell Atlantic Corporation, et al. v. William Twombly, et al.*, 550 U.S. 544 (2007) and in response to the urging of certain elements of the antitrust plaintiffs bar, Congress amended ACPERA in ways that threaten to undermine the effectiveness of both the Division's "most effective investigative tool" and the legislation designed to enhance recovery of damages on behalf of the victims of antitrust criminal conduct.

When ACPERA came into force on June 22, 2004, it was widely believed that its reduction in civil damage exposure would remove a significant disincentive to those corporations considering whether to seek amnesty[2], thus potentially exposing criminal conduct that might otherwise go undetected, and would enhance the efficiency and amount of recovery by victims of the conduct. In order to receive the potential benefits conferred by ACPERA, the amnesty applicant must cooperate with the civil plaintiffs in the damage case in order to assist them to more efficiently establish liability and damages against the other participants in the cartel. The sufficiency of the amnesty applicant's compliance with the cooperation requirements of the act was to be determined on a case-by-case basis by the court in which the civil case is brought.[3] In order to avoid interference with an ongoing criminal investigation, the sufficiency of the amnesty applicant's cooperation obligations was not specifically tied to the timing of the cooperation except in a very limited circumstance.[4] Furthermore, whether to take advantage of the potential benefits of ACPERA and provide the required cooperation was left entirely to the decision of the amnesty applicant, apparently in order to prevent the forced premature disclosure of the identity of an amnesty applicant and potentially chilling future amnesty applications in other jurisdictions.

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[1] *The Evolution of Criminal Antitrust Enforcement Over The Past Two Decades*, by Scott D. Hammond, Deputy Assistant Attorney General, Antitrust Division, before the 24th National Institute On White Collar Crime (February 25, 2010) at 3, *available at* http://www.justice.gov/atr/public/speeches/255515.htm.

[2] See, e.g., 149 Cong. Rec. S23520 (October 29, 2003) (remarks of Senator Kohl: the damage limitation "will remove a significant disincentive to those who would be likely to seek criminal amnesty"); and 150 Cong. Rec. S3614 (April 2, 2004) (remarks of Senator Hatch: treble damage liability is "a major disincentive to self-reporting").

[3] ACPERA § 213(b).

[4] ACPERA § 213 (c) made timeliness of cooperation relevant only when the amnesty applicant's initial contact with the Antitrust Division occurs after a State has begun an investigation of the conduct.

ACPERA passed both Houses of Congress without dissension and was supported by members of both parties, as well as representatives from the antitrust plaintiffs and defense bar. However, because there was little empirical data supporting or undermining the widely held view that ACPERA would be beneficial to both the criminal and civil prosecution of cases against antitrust cartels, Congress provided a sunset provision in the act so that its actual benefits, or lack thereof, could be reassessed before making it permanent.[5]

In the first several years following the enactment of ACPERA, little happened that would cause either the antitrust plaintiffs bar or the antitrust defense bar to question their support for the *Act* and virtually no case law developed. Then, on May 21, 2007, the Supreme Court decided *Twombly,* and held that in order to avoid dismissal, an antitrust civil complaint must contain enough factual matter, accepted as true, to "state a claim to relief that is plausible on its face."[6] In *Twombly*, the Court specifically rejected the test for dismissal established by the Court in *Conley v. Gibson*, 355 U.S. 45-46, (1957) ("a complaint should not be dismissed . . . unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief") and substantially altered the pleading requirements for Sherman Act claims. Now, pleading facts that are "merely consistent with" a defendant's liability falls "short of the line between possibility and plausibility of entitlement to relief" and will not survive a motion to dismiss.[7] Rather a Section 1 complaint must plead sufficient facts as to the defendant to "nudge [plaintiffs'] claims across the line from conceivable to plausible."[8] In *Twombly*, the Court noted that the complaint had alleged "no specific time, place, or person involved in the alleged conspiracies," and concluded that the allegations of the complaint failed to plausibly suggest an agreement.[9]

"Following the Court's decision in Twombly, the lower courts dismissed numerous antitrust cases that many believe would have survived a motion to dismiss under the prior formulation of the test."

Following the Court's decision in *Twombly*, the lower courts dismissed numerous antitrust cases that many believe would have survived a motion to dismiss under the prior formulation of the test. For example in, *In re Elevator Antitrust Litig.*, No. 06-3 128-cv, 2007 U.S. App. LEXIS 21086, at *6-8 (2d Cir. Sept. 4, 2007), the Second Circuit dismissed Section 1 conspiracy claims under *Twombly* because allegations that defendants attended meetings together and engaged in multiple conversations regarding pricing constituted only "general terms without any specification" and amounted to "nothing more than a list of theoretical possibilities, which one could postulate without knowing any facts whatever."[10]

The new heightened plausibility pleading standard was criticized by many and legislation designed to restore the *Conley v. Gibson* standard was introduced in both houses of Congress.[11] In addition, members of the plaintiffs' bar, particularly in the antitrust bar, began to question how they could force amnesty applicants to provide specific facts sufficient to meet the new pleading standard at an early stage of the civil litigation. In *In Re TFT-LCD (Flat Panel) Antitrust Litigation*, the court denied the plaintiffs' motion for an order to require the amnesty applicant to identify itself and provide cooperation to the plaintiffs.[12]

Having lost their initial attempt to force an amnesty applicant to provide *Twombly*-sufficient facts prior to a court's decision on a motion to dismiss, the plaintiffs focused on obtaining changes to ACPERA itself. The opportunity to amend ACPERA was afforded by the fact that the statute would expire, if not renewed by Congress, on June 22, 2010. In addition to extending ACPERA for an additional ten years and making clear that a person who receives a marker prior to the extended sunset date is eligible to retain the benefits of the statute even if it should expire,[13] the House adopted (and the Senate accepted) some of the changes proposed by the plaintiffs bar, specifically providing that the court consider the "timeliness" of the

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5 ACPERA § 211(a).
6 *Id.* at 570.
7 *Id.* at 557.
8 *Id.* at 570.
9 *Id.* at 565, n.10.
10 *Id.* at *8 **[What case is this?]** (citing *In re Elevator Antitrust Litig.*, No. 04-CV-1 178, 2006 U.S. Dist. LEXIS 34517, at *9 (S.D.N.Y. May 30, 2006)).
11 See. S. 1504 and H.R. 4115. Neither bill passed prior to the expiration of the 111th Congress.
12 No. M 07-1827 SI, 2009-1 Trade Cases (CCH) ¶76,626 (N.D. Cal. May 19, 2009).
13 Pub. L. No. 111-190 §§ 1 & 2 (June 9, 2010).

amnesty applicant's cooperation in determining its sufficiency under ACPERA.[14] In addition, the legislation as adopted provides that once a stay or protective order in the private civil proceedings (should one be obtained by the government) expires or is terminated, the leniency applicant must provide the plaintiffs a full account of all facts known to the applicant and all documents relevant to the civil action "without unreasonable delay." [15]

These "minor" modifications to ACPERA, have the potential to seriously interfere with the Antitrust Division's criminal investigations and prosecutions. Any evidence provided to the plaintiffs in the civil case by the amnesty applicant would be subject to discovery by the other parties to that litigation, *i.e.*, the other defendants, which are subjects of the criminal investigation by the Department of Justice. There is very little that has greater potential to impede or otherwise interfere with a criminal investigation than the disclosure of the government's evidence to the subjects of the investigation. Such disclosure rightly is viewed by the Department of Justice as the very antithesis of the "full, continuing, and complete cooperation" with the government's criminal investigation required under the Corporate Leniency Policy. Yet, amnesty applicants now well maybe faced with that Hobbsian choice – early disclosure of the evidence it provided to the government to the parties to the civil litigation, perhaps at the risk of losing its conditional amnesty, or refusing to disclose that evidence, at the risk of losing the damage limitation benefits provided by ACPERA. An "incorrect" decision in these circumstances could do substantial harm to the criminal investigation and could cost the amnesty applicant dearly. In fact, the wrong choice here could cost the leniency applicant both its amnesty from criminal prosecution and its benefits under ACPERA. If the leniency applicant takes action that is viewed by the Antitrust Division as a violation of its obligation to provide its full and complete cooperation, the Division could void the conditional leniency agreement with the applicant. Furthermore, losing its status as a leniency applicant disqualifies the defendant under ACPERA and could result in it being ineligible for relief from treble damages and joint and several liability provided by the statute. This modification also has the potential to chill future amnesty applications, which would be detrimental to both the Antitrust Division's Corporate Leniency Program and to the victims of antitrust crimes.

" These "minor" modifications to ACPERA, have the potential to seriously interfere with the Antitrust Division's criminal investigations and prosecutions."

While it is much too early to tell just how detrimental the ACPERA amendment will be to the Antitrust Division's Corporate Leniency Policy – and in turn to the victims of criminal cartel conduct – it is certain that these unintended consequences could have been avoided. If the heightened plausibility pleading standard established by the Supreme Court in the *Twombly* and *Iqbal* decisions is considered questionable public policy by the plaintiffs' bar, the appropriate response is to have a responsible debate on the merits of the legislation designed to restore the pleading standard to that adopted in *Conley* in 1957. Instead, the plaintiffs' bar – and Congress – in an effort to achieve a quick fix to the dismissal of perhaps meritorious antitrust cases, have adopted a "solution" that in the long run likely will do more harm than good to both the criminal prosecution of antitrust crimes and the pursuit of civil cases seeking recompense for those harmed by antitrust cartels.

One of the cornerstones of a successful leniency program is its transparency and predictability. According to the current Deputy Assistant Attorney General for Criminal Enforcement, a Corporate Leniency Program is successful only if "a company can predict with a high degree of certainty how it will be treated if it reports the conduct and what the consequences will be if it does not."[16] Yet, future potential amnesty applicants will have to face the fact that they likely will be caught between the demands of cooperation with the Department of Justice in the criminal investigation, which assures the non-prosecution of the company and its employees, and the demands of "timely" cooperation with the civil plaintiffs, which could result in relief from treble damages and joint and several liability. Thus, they will not be able to predict with a high degree of certainty whether they will be able to obtain the benefits of both the Corporate Leniency Policy and ACPERA. While ACPERA as originally drafted sought to remove a major disincentive to self-reporting, i.e., treble damages and joint and several liability for the corporate leniency applicant, ACPERA as

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[14] Id. § 3.
[15] Id. § 2.
[16] *Cornerstones of an Effective Leniency Program*, by Scott D. Hammond, Deputy Assistant Attorney General, Antitrust Division, before ICN Workshop On Leniency Programs (November 23-24, 2004) at 18, *available at* http://www.justice.gov/atr/public/speeches/ 206611.htm.

reauthorized in June 2010 has introduced perhaps an even greater disincentive, i.e., a lack of predictability and certainty in the outcome, which can "kill an amnesty program."[17]

Going forward companies considering self-reporting under the Antitrust Division's Corporate Leniency Policy, and lawyers advising them, must consider: (1) the fact that the company's cooperation may not be considered "timely" by the lawyers representing the plaintiffs in the damage cases, possibly denying the company the benefits of ACPERA or, at a minimum, increasing the litigation costs of establishing to the satisfaction of the court that the cooperation was "timely;" (2) the possibility that the company's obligation to fully cooperate with the Division's criminal investigation may come in conflict with its obligation to provide cooperation to the civil plaintiffs at the earliest stages of the damage litigation, possibly causing the company to have to decide to forego the benefits of ACPERA, or at a minimum greatly increasing the legal costs necessary to preserve those benefits; and (3) in multi-jurisdictional matters, the possibility that the company's carefully developed strategy for self-reporting and cooperating with multiple enforcement agencies may be undermined by the demands to publicly identify itself and provide "timely" cooperation to the plaintiffs in the hastily filed U.S. class action damage cases. These and other collateral uncertainties arising from the 2010 amendments to ACPERA will make it far more difficult for companies know "with a high degree of certainty" the consequences and benefits of applying for amnesty. In addition, it is clear that should any of these uncertainties arise, at a minimum, the cost of preserving the benefits of leniency and ACPERA will increase substantially. While the introduction of these uncertainties may not "kill [the Division's] amnesty program", it will needlessly complicate and increase the costs associated with a company's consideration of the leniency decision. To a certain extent, Congress unnecessarily has reintroduced into the leniency mix that which it sought to eliminate with the 2004 ACPERA legislation – "a major disincentive to self-reporting."

"These and other collateral uncertainties arising from the 2010 amendments to ACPERA will make it far more difficult for companies know "with a high degree of certainty" the consequences and benefits of applying for amnesty."

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[17] *Id.*, at 19.

The Latest on *Leegin* and Resale Price Maintenance – Should Manufacturers Rest Easy after the Tempur-Pedic Decision?

By Barbara Sicalides

For nearly a century, federal antitrust law (the Sherman Act) prohibited resale price maintenance ("RPM" or "vertical price fixing") agreements as a *per se* illegal form of price-fixing. See 15 U.S.C. § 1 (1997). In 2007, however, the Supreme Court's 5-4 decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007), held that RPM arrangements are not illegal *per se* under the Sherman Act. In so doing, the Court overturned *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). Instead, RPM agreements are subject to "rule of reason" analysis, which allows RPM if its procompetitive benefits outweigh its anticompetitive effects.[1]

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Despite the passage of more than three years since the Supreme Court's decision, it is unclear what, if any, long-term effect *Leegin* will have, particularly with respect to state antitrust laws and the cases filed alleging claims under those laws. While many states interpret their antitrust laws in conformity with federal law, some states specifically prohibit RPM agreements, including states like Maryland that enacted *per se* statutes in response to *Leegin*.[2]

Most recently, the state antitrust authorities advocating for *per se* treatment of vertical price fixing have had mixed results. They suffered at least a temporary set back in *New York v. Tempur-Pedic International*, No. 0400837 (N.Y. Sup. Ct., N.Y.C. Mar. 29, 2010). There, the trial court granted Tempur-Pedic's motion to dismiss on the grounds that the state had failed to establish the existence of a contract or agreement between Tempur-Pedic and its retailers and that N.Y. law did not make RPM illegal. On the other hand, in *People of the State of California v. Bioelements, Inc.*, No. 10011659 (Cal. Sup. Ct. Jan. 11, 2011), California obtained another consent judgment permanently prohibiting the manufacturer from fixing vertical prices.

Leegin Creative Products, Inc. v. PSKS, Inc. on Remand

Leegin, a manufacturer of Brighton brand women's accessories introduced a marketing initiative designed to provide incentives to retailers that created a separate section for the Brighton brand within their stores. To participate in this initiative, retailers had to pledge to "follow the Brighton Suggested Pricing Policy at all times." In 2002, Leegin learned that PSKS had violated its pricing policy by discounting Brighton merchandise. In response to this violation, Leegin suspended all shipments to PSKS.

Generally, the Supreme Court decided that RPM agreements should not be *per se* illegal. The Court wrote that minimum price agreements can benefit consumers by enabling retailers to invest in customer services without fear of being undercut by discount rivals, by giving consumers more options to choose among low-price, low-service brands; high-price, high-service brands; and brands that fall in between and by allowing new entrants to attract resellers with the guarantee of certain margins. The Court explained that such pricing agreements should encourage retail services that increase competition between different brands, which is good for the consumer. RPM

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[1] *Leegin* did not change the fact that the *per se* rule would still apply to claims that a horizontal agreement to implement RPM existed among competitors at either the manufacturer or reseller level. Id. at 886.

[2] See Michael A. Lindsay, *Overview of State RPM*, http://www.antitrustsource.com [under References] (summarizing RPM-related state law). There also continues to be proposed federal legislation pending to overrule *Leegin* and declaring RPM illegal *per se* under the Sherman Act.

agreements also could make it easier for new products to enter the market because competent retailers will be more willing to invest the effort and expense required to distribute a new product if they are able to charge a higher price. Although the Court acknowledged that there could be negative effects on competition, it concluded the fact that negative effects were possible was not sufficient reason to treat RPM agreements as automatically illegal.

The Supreme Court changed the legal standard that courts use to examine RPM, but did not give a "green light" for all RPM agreements. Instead RPM practices will be examined by the courts, which will weigh a number of factors, but may still find vertical pricing agreements to be illegal. The Court explained that resale price agreements are dangerous and warned the lower courts "to be diligent in eliminating their anticompetitive uses from the market." The Court gave examples of situations where such pricing agreements will be particularly treacherous. Specifically, when a significant number of manufacturers in a given industry decide to use this practice, when there is evidence that pressure from the resellers was the impetus for the price minimums, or when the manufacturer implementing such an agreement is dominant, the Supreme Court warned that setting resale price floors is particularly dangerous.[3]

"The Supreme Court changed the legal standard that courts use to examine RPM, but did not give a "green light" for all RPM agreements."

On remand after its Supreme Court defeat, PSKS filed a second amended complaint, apparently attempting to fit is claims within one of the Supreme Court's examples of how RPM might result in harm to competition. Specifically, PSKS alleged that: (1) independent retailers were involved in the enforcement of Leegin's RPM policy; (2) at a meeting more than 100 retailers reached a consensus regarding special discounts and incentives which was later adopted as Leegin's policy; (3) Leegin was the hub in a hub-and-spoke conspiracy by intervening to resolve pricing disputes between and among competing retailers; and (4) Leegin, acting at the retail level, agreed with other retailers on the resale price. The court noted that PSKS did not, however, claim that retailers were the "source" of the RPM policy or that Leegin established the policy at the retailers' urging or that there was any agreement among retailers or between competing manufacturers to set resale prices.[4]

The Fifth Circuit rejected PSKS' argument that the rule of reason was inapplicable because Leegin is a dual distributor. In addition, the Fifth Circuit held that PSKS failed to plead a proper relevant product market because, despite having alleged two alternative markets, neither proposed market included interchangeable substitute products or recognized the cross-elasticity of demand for Leegin's products. Next, the court rejected PSKS' claim that Leegin's RPM program artificially inflated consumer prices, and stated that the "claim defies the basic laws of economics. Absent market power, an artificial price hike by Leegin would merely cause it to lose sales to its competitors." The court further found that PSKS' complaint failed because it did not plausibly allege harm to interbrand competition.[5]

The Supreme Court denied PSKS' petition for certiorari on February 22, 2011.

New York v. Tempur-Pedic International, No. 0400837 (N.Y. Sup. Ct., N.Y.C.)

On January 14th, the New York Supreme Court issued its eagerly anticipated RPM decision in the case filed by New York's Attorney General's Office ("NYAG") against the mattress manufacturer, Tempur-Pedic International, Inc ("Tempur-Pedic"). The N.Y. court struck a blow to the AG's often repeated and forceful position that N.Y. law barred automatically any and all minimum resale price agreements.

After publishing articles and making public statements regarding their intention to enforce rigorously state laws prohibiting RPM, on March 29, 2010 the NYAG's office filed a petition against Tempur-

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3 In *Toledo Mack Sales & Service, Inc. v. Mack Trucks, Inc.*, 530 F.3d 204 (3d Cir. 2008), the Third Circuit applied the *Leegin* factors in its rule-of-reason analysis.

4 *PSKS, Inc. v. Leegin Creative Leather Products, Inc.*, 615 F.3d 412 (5th Cir. 2010), cert. denied, 179 L. Ed. 2d 301 (U.S. Feb. 22, 2011)

5 In a separate case filed on behalf of a purported class of purchasers of retail products manufactured by Leegin, the court's analysis tracks, for the most part, the analysis of the Fifth Circuit. See *Spahr v. Leegin Creative Leather Products, Inc.*, 2008 U.S. Dist. LEXIS 90079 (E.D. Tenn. Aug. 20, 2008).

Pedic. New York challenges Tempur-Pedic's minimum advertised price policy, under Section 369-a of the N.Y. General Business Law and Section 63(12) of the N.Y. Executive Law, alleging that Tempur-Pedic entered into RPM agreements that required resellers of its products to charge prices dictated by Tempur-Pedic. The NYAG's petition does not include claims under the Sherman Act or under New York's antitrust statute -- the Donnelly Act, General Business Law § 340 *et seq*.

Section 63(12) provides for equitable relief when the defendant is "engage[d] in repeated fraud or illegal acts" and Section 369-a makes unenforceable "any contract provision that purports to restrain a vendee of a commodity from reselling . . . at less than the price stipulated by the vendor or producer." New York contends Tempur-Pedic's establishment and enforcement of a RPM policy violated Section 63(12) and Section 369-a. According to the petition, Tempur-Pedic's Retail Partner Agreements with its authorized retailers prohibited discounting, free gifts with purchases, rebates, coupons, free gift cards, or other in-store credit. The petition further alleges that Tempur-Pedic implemented an RPM program through "a series of letters to all accounts from its president" stating that Tempur-Pedic "will not do business with any retailer that charges retail prices that differ from the prices set by Tempur-Pedic." The petition also states that retailers assisted Tempur-Pedic's enforcement of its RPM restrictions by "monitoring the prices of their competitors and reporting to Tempur-Pedic any pricing below the retail prices set by Tempur-Pedic."

"The N.Y. court rejected the NYAG's arguments and held that N.Y. law does not prevent a vendor from insisting that retailers use the prices specified by the vendor or otherwise restrain the reseller's right to discount the resale price."

New York contends, as it did in its earlier public comments, that Section 369-a does more than simply make RPM provisions unenforceable, instead, it affirmatively "provides that a vendor or producer cannot set a minimum price at which its product can be resold." Additionally, the state maintains that the Uniform Commercial Code's definition of a "contract" governs whether a contract exists within the meaning of Section 369-a. Under this theory, the state can rely on Tempur-Pedic's course of dealings with its resellers to prove the existence of an agreement.

It is likely that the AG did not bring a federal antitrust claim because of earlier unsuccessful (11th Circuit) federal private litigation challenging Tempur-Pedic resale pricing practices and because of *Creative Leather Products, Inc. v. PSKS, Inc*., 552 U.S. 877 (2007). Perhaps the NYAG omitted the state antitrust claim because the Donnelly Act has long been construed consistent with the Sherman Act.

The N.Y. court rejected the NYAG's arguments and held that N.Y. law does not prevent a vendor from insisting that retailers use the prices specified by the vendor or otherwise restrain the reseller's right to discount the resale price. The court concluded that RPM does not constitute "an illegal act" and that the text of the statute itself clearly did not bar any and all RPM. Because the court found that the language of the statute was clear, it refused to consider the title of the statute – "Price Fixing Prohibited" – or look any more deeply into the intent of the N.Y. legislature. The court stated "[t]here is no ambiguity in the text of General Business Law §369-a. Contracts for resale price restraints are unenforceable and not actionable, but not illegal."

The court also rejected the NYAG's arguments that Tempur-Pedic's advertised price agreement violated Section 369-a. The court noted that the advertised policy did not prohibit discounts, rebates, promotional items or coupons; instead the policy only barred the advertisement of these types of promotions "in conjunction with Tempur-Pedic products." Although Tempur-Pedic's advertised pricing program was part of a contract with its retailers (not a unilateral policy), the court found the advertising restriction was not a retail price agreement. Thus, because the advertised price policy did not actually bar discounting, the court found that it could not be illegal under Section 369-a.

Interestingly, the NYAG was not the first to challenge Tempur-Pedic's distribution and pricing methods. In *Jacobs v. Tempur-Pedic International, Inc*., 2007 WL 4373980 (N.D. Ga. Dec. 11, 2007), customers of a Tempur-Pedic distributor claimed that the mattress manufacturer had established resale price agreements that artificially inflated mattress prices by eliminating competition between retailers and distributors in violation of Section 1 of the Sherman Act. Plaintiffs claimed that Tempur-Pedic required its distributors to charge a minimum resale price and to advertise that price as the "lowest factory authorized pricing" or the "Lowest Possible Price."

In *Jacobs*, Tempur-Pedic moved to dismiss the plaintiffs' price-fixing claims under *Leegin* and argued that the plaintiffs might have had a valid price-fixing claim under the pre-*Leegin per se* standard, but that the plaintiffs failed to state a claim under the new rule of reason standard. Id. The court concluded that plaintiffs failed to state a claim under the rule of reason because, among other reasons, the complaint did not identify the relevant market and found the plaintiffs' allegation about inflated mattress prices was unpersuasive. Consequently, the court dismissed the plaintiffs' price-fixing claims under the rule of reason standard articulated in *Leegin*.

As expected, in the New York case, the NYAG has filed an appeal.

People of California v. Bioelements, Inc., No. 10011659 (Cal. Sup. Ct. Jan. 11, 2011)

On January 14, 2011, California's Attorney General announced that it settled a dispute with a Colorado cosmetics company that prohibited retailers from selling its products over the Internet at a discount. California alleged that since 2009, Bioelements contracted with dozens of resellers requiring them to sell Bioelements products online for at least the manufacturer's suggested retail price. Under its settlement with California, Bioelements must pay $51,000 in civil penalties and attorney fees as well as refrain from fixing resale prices and inform its distributors the contracts at issue are void.

California v. DermaQuest, Inc., Case No. RG 10497526 (Cal. Sup. Ct. Feb. 23, 2010)

Last year, California's Attorney General filed a complaint and stipulated final judgment in a California state court action challenging DermaQuest's RPM practices. DermaQuest is a California-based manufacturer of cosmetics. The complaint alleged that DermaQuest entered into minimum RPM agreements with some of its distributors in violation of California's Cartwright Act and Unfair Competition Law. California claimed that DermaQuest's contracts required its wholesalers to represent and warrant that their retailer customers would not resell DermaQuest's products below the manufacturer's suggested minimum price. The complaint does not allege any federal antitrust claims, but does make clear California's position that RPM remains *per se* illegal under state law.

Pursuant to the consent judgment in the case, DermaQuest agreed to send written notice to the relevant distributors that it was disavowing all parts of any agreement that obligated the distributors to maintain certain resale prices and to refrain from entering into any agreements with any third party, including independent contractors, that increase prices or that fix at any standard or figure the price of the products to consumers.

"From the cases above, it is evident that a number of state antitrust enforcers still consider RPM harmful to consumers and commerce and that they intend to seek out opportunities to bring actions that will deter manufacturers considering RPM."

Conclusion

Since *Leegin*, neither the federal nor the state courts have clarified how RPM claims will be handled or how manufacturers seeking to regulate resale prices can safely accomplish procompetitive, lawful goals. From the cases above, it is evident that a number of state antitrust enforcers still consider RPM harmful to consumers and commerce and that they intend to seek out opportunities to bring actions that will deter manufacturers considering RPM.

The *Tempur-Pedic* case could provide lawyers counseling clients on RPM issues with substantial insight into, among other things, the definition of a contract or agreement, the scope of certain key New York statutes, and the way in which courts will weigh the factors deemed important in *Leegin*. Of course, there was uncertainty before the Supreme Court's *Leegin* decision. Thus, even if federal or state legislatures enact statutes repealing *Leegin*, questions will remain, such as, when a manufacturer's conduct crosses the line from a unilateral policy into a coerced agreement with its resellers to adhere to RPM, or, when resellers' actions cross the line from simple complaints into an agreement to terminate or maybe even a boycott of a rival. Regardless of the outcome in *Tempur-Pedic*, questions will also remain regarding the level of activity or effect required within each state to trigger that state's statute.

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Developments in Merger Review in Canada

By Mark Katz and John Bodrug

A recent Competition Bureau challenge to a completed merger below the compulsory notification thresholds and an announced intention to amend certain aspects of the Bureau's Merger Enforcement Guidelines may signal more expansive merger reviews by the Bureau. In particular, the Bureau appears to be reviewing more transactions below the compulsory notification thresholds, and may, in its merger reviews, be focussing more on (i) whether the merger may create anti-competitive buying power, (ii) potential vertical foreclosure of competitors that are also suppliers or competitors of a merger party, and (iii) minority interests and interlocking directorates. The Bureau also appears to be poised to follow recent amendments to the U.S. Horizontal Merger Guidelines and de-emphasize the role of market definition in establishing anti-competitive effects of a merger. Finally, the Bureau's recent merger challenge serves as a reminder that the Bureau considers not only whether a merger lessens existing competition between the parties, but also whether it is likely to prevent future competition from developing.

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The Competition Act's Merger Review Process

Part IX of the *Competition Act* (the "Act") requires the parties to a merger transaction to submit a notification filing when certain financial and voting interest thresholds are exceeded. The filing of the notification triggers a "waiting period" within which the parties are prohibited from closing their transaction.

During that waiting period (and, in rare cases, sometimes beyond), the Commissioner and her staff at the Competition Bureau (the "Bureau") will review the proposed transaction to determine if it is likely to "substantially prevent or lessen competition" (the statutory test). If the Bureau reaches that conclusion, it may apply to the Competition Tribunal to prohibit or dissolve the transaction or to require specific divestitures. Typically, though, the Bureau and the parties are able to negotiate a resolution, which will then be filed with the Tribunal in the form of a "consent agreement".

The Part IX notification requirements and the substantive review process apply independently in the sense that a transaction may be subject to notification even if it clearly does not raise substantive issues. Conversely, a transaction may be reviewed and challenged even if it is not notifiable and has already closed (the Commissioner has one year following closing to bring an application).

The Commissioner v. CCS

Although the Commissioner clearly has the authority to challenge non-notifiable transactions, this authority has rarely been exercised. Indeed, as a general proposition, it is unusual for the Commissioner even to challenge notifiable transactions (the last such challenge was brought in 2005).

But, in a case involving the acquisition of a landfill in British Columbia, the Commissioner has taken the step of not only challenging a merger transaction, but one that is non-notifiable as well.

The transaction at issue involved the acquisition by CCS Corporation ("CCS") of Complete Environmental Inc. ("Complete"), the owner of a landfill in northeastern British Columbia known as the Babkirk Secure Landfill (the "Babkirk Landfill"). The transaction apparently fell under the Part IX thresholds. However, it also appears that CCS voluntarily notified the transaction to the Bureau.

Following what it characterized as "a thorough review", the Bureau concluded that CCS's acquisition of the Babkirk Landfill would result in a substantial prevention of competition in the market for "the disposal of hazardous waste produced largely at oil and gas facilities in northeastern British Columbia". According to the Bureau, with the acquisition of the Babkirk Landfill, CCS would be the only operator of secure landfills in that area. Indeed, the Bureau alleges (based on what it saw in CCS's internal documents) that CCS sought to acquire the Babkirk Landfill with the express purpose of preventing the entry of what otherwise would have been a new competitor.

The Bureau brought its concerns to CCS's attention, but no resolution was reached. In a somewhat unusual step, the Bureau then agreed that CCS could complete the acquisition, subject to a written undertaking that CCS would preserve the Babkirk Landfill as an independent and viable operation pending determination of the Bureau's challenge to the acquisition.

A U.S. Import?

U.S. antitrust authorities also have been focusing their attention on non-reportable transactions recently. (The U.S. merger review system operates on a similar basis to the Canadian system: transactions that exceed certain thresholds must be notified to the U.S. authorities and cannot close until a prescribed waiting period has expired.)

In the last two years, U.S. antitrust authorities have challenged at least a dozen non-reportable transactions following closing. In one instance, the transaction had been approved by a bankruptcy court filing.[1] In another, the value of the entire deal was no more than $5 million (well below the applicable U.S. threshold).

That acquisition, involving two companies providing voting equipment systems, is instructive. Notwithstanding the minimal cash value of the deal, the Antitrust Division of the U.S. Department of Justice (the "Antitrust Division") concluded that the acquisition had combined the two largest providers of such voting systems, which are used to tally votes in federal, state and local elections in the United States. As a result, the merged entity accounted for more than 70% of voting equipment systems sold in the United States. In a settlement with the Antitrust Division, the acquiror agreed to divest certain assets (including intellectual property) to a buyer approved by the Antitrust Division.[2]

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Amendments to Merger Guidelines

On February 25, 2011, the Commissioner announced that the Bureau will undertake "moderate" revisions to the Bureau's 2004 Merger Enforcement Guidelines. The announcement identified the following specific areas that will be revised to better reflect current Bureau practice and economic and legal thinking.

Buying Power. Typically, when the Bureau has concerns in relation to a merger, they involve a finding that the merger is likely to result in higher prices to customers, or a reduction in the quality or variety of products produced by the parties. On occasion, however, the Bureau may identify concerns about the merger's "upstream" effect on purchases by the merged entity. The Commissioner's announcement states that the Merger Guidelines will be revised to provide additional guidance on these upstream issues in accordance with prior Bureau submissions to the Organisation for Economic Co-Operation and Development ("OECD"). Those OECD submissions state that buying power is anti-competitive where a firm is able to suppress the price that it pays for a product to the point that the overall quantity of the purchased product produced or supplied in the relevant market is reduced below production levels that would otherwise prevail. The Bureau would not be concerned about buying power that enables a purchaser to negotiate lower prices that do

[1] *See* Press Release, Federal Trade Commission, FTC Challenges LabCorp's Acquisition of Rival Clinical Laboratory Testing Company (December 1, 2010), available at http://www.ftc.gov/opa/2010/12/labcorp.shtm.

[2] *See* Press Release, Department of Justice, Justice Department Requires Key Divestiture in Election Systems & Software/Premier Election Solutions Merger (March 8, 2010), available at http://www.justice.gov/atr/public/press_releases/2010/256267.htm.

not diminish overall supply of the product. Examples of enforcement action by the Bureau prompted by buying power concerns include consent resolutions negotiated in the context of a merger of forestry companies that accounted for a large share of timber purchases in certain local markets, and a merger of retail bookstores that accounted for a large share of book purchases from Canadian publishers.

Minority Interests and Interlocking Directors. Again, the Bureau has indicated that revisions to its Merger Guidelines in relation to minority interests and interlocking directors will build on its previous OECD submissions. In those submissions, the Bureau pointed out that it will review minority interests or interlocking directorships only if they are either ancillary to a merger transaction or themselves constitute an ability to materially influence the economic behaviour of the business of a competitor. Acquisitions of as little as a 20% interest in a public company or 35% in a private company can trigger compulsory notification requirements, and the Bureau regularly reviews acquisitions of minority interests in that context. Interlocking directorships, however, do not in themselves trigger any notification requirement in Canada. (Unlike the U.S., Canadian competition legislation does not expressly address or prohibit interlocking directors or officers between competitors.) In a few instances, the Bureau has examined and sought the elimination of interlocking directorships between competitors that came to light in a review of a full merger between two other competitors. However, the Bureau's OECD submission indicates that, in the Bureau's view, it is possible that an interlocking directorship itself could independently trigger a Bureau review. In this context, the Bureau would assess the relevant director's ability to materially influence the economic behaviour of the business and his or her access to confidential information relating to a relevant market.

"In a few instances, the Bureau has examined and sought the elimination of interlocking directorships between competitors that came to light in a review of a full merger between two other competitors."

Market Definition. The Commissioner's announcement states that revisions to the Merger Guidelines will clarify that merger review does not necessarily start with defining a relevant product and geographic market (i.e., by identifying close substitutes that customers would switch to in the event of a certain range of hypothetical price increases). Rather, merger review may be based on other evidence of competitive effects, with the goal of determining whether a merger creates or enhances market power. This comment, and the apparently intended changes, appear to be inspired by the 2010 revisions to the merger guidelines of the U.S. antitrust agencies. The 2010 U.S. Horizontal Merger Guidelines adopted a more flexible approach to assessing likely anti-competitive effects with a reduced emphasis on the need to assess market definition, market shares and market concentration in all cases. For example, the U.S. guidelines now state that, in some cases, where sufficient information is available, the U.S. agencies may be able to assess the degree to which a price increase by one merging party diverts sales of its products to those of the other merging party, such that a post-merger price increase above competitive levels would be profitable. In this case, the U.S. guidelines assert, identifying the price effects of a merger need not rely on the traditional market definition analysis. (It remains to be seen, however, whether U.S. courts – or the Canadian Competition Tribunal – will follow this approach.)

Vertical Foreclosure. The Commissioner has indicated that the revisions to its Merger Guidelines will provide more accurate guidance on how the Bureau assesses vertical issues, focusing on foreclosure effects. The current Guidelines include a brief discussion of circumstances in which a "vertical merger" between a supplier and a customer may raise concerns where the elimination of an independent upstream source of supply (or downstream distribution outlet) leaves (for other competitors) only a small amount of unintegrated capacity at either of the stages or sectors of the industry at which one of the merging parties competes. Alternatively, the current Guidelines indicate that a merger that creates or increases a high degree of vertical integration between an upstream market and a downstream retail market can facilitate coordinated behaviour by firms in the upstream market by making it easier to monitor the prices charged by rivals at the upstream level. To date, the Bureau has not challenged a transaction principally because of vertical foreclosure concerns. However, we have observed of late increased examination by Bureau staff of potential "vertical" issues that can risk delaying the Bureau's review if not addressed pro-actively or expeditiously.

Other Changes. The Commissioner's announcement also said that the revisions to its Merger Guidelines will provide more guidance on the Bureau's current economic thinking with regard to

assessment of both unilateral and coordinated effects of a merger, and that the revisions will incorporate a previously released bulletin discussing the efficiencies defence in the merger provisions of the Competition Act.

The Commissioner stated that the Bureau intends to publish revised draft Merger Enforcement Guidelines during the second quarter of 2011 and to seek public feedback on the revisions prior to publishing final Guidelines in the fall.

Implications

Whether or not influenced by trends in the United States, the Commissioner's challenge to the CCS acquisition underscores that a purchaser whose proposed transaction does not exceed the *Competition Act*'s notification thresholds cannot blithely assume that the deal will float under the proverbial "radar screen". As part of the necessary due diligence, a purchaser in this situation must still consider the potential impact on competition of the transaction. In particular, there must be an appraisal of whether other industry participants (especially customers) are likely to complain to the Commissioner. As demonstrated by the CCS case, purchasers also must carefully review what they say in their internal documents about the rationale for a non-notifiable transaction and the transaction's likely effect on competition.

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If potential issues are identified, purchasers must decide if the Bureau should be pro-actively advised about the transaction prior to closing in an effort to avert any issues. That decision, in turn, could have an impact on the type of closing conditions purchasers will require in their transaction agreements. For example, purchasers may want to condition closing on receipt of positive confirmation from the Bureau that it does not intend to bring an application to the Tribunal (typical in the context of notifiable transactions). On the other hand, vendors might resist this type of condition because they will not be keen about potentially slowing up a deal with a merger notification that is not statutorily mandated. These decisions are not easy ones to make, particularly because pro-actively reaching out to the Bureau is not always a successful strategy.

Whether or not a merger is notifiable, the above-noted developments serve as a reminder of several potential issues (prevention of future competition, buying power, interlocking directors, and vertical foreclosure) that, while not typical bases for Bureau concern, can lead to challenge or delay if not proactively identified and addressed. These issues are clearly on the Bureau's assessment checklist.

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