



Antitrust Update

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DOJ Adopts Tough Enforcement Stance Against Single-Firm Conduct

By Irving Scher and Brianne Kucerik

This May, in her first major speech as the new Assistant Attorney General in charge of the Antitrust Division of the U.S. Department of Justice (“DOJ” or “Department”), Christine Varney announced that she had jettisoned the DOJ Report issued just last September regarding the Department’s then current enforcement policy under § 2 of the Sherman Act (prohibiting monopolization and attempts to monopolize).¹ Although the substantive value of the eight-month-old Report was already limited by criticism from Federal Trade Commissioners, Varney’s very public repudiation of the Bush Administration DOJ enforcement policy signaled her intent to pursue investigations against companies with dominant market positions and to apply possibly creative theories of anticompetitive harm.

According to Varney, “the greatest weakness” of the Bush Administration DOJ Report is that it “raises many hurdles” to enforcing the Sherman Act. Varney said that the Report “sounds a call of great skepticism” about the ability of the antitrust enforcement authorities to distinguish between anticompetitive and lawful conduct, and that failing to make the proper distinctions may deter procompetitive conduct. Varney flatly rejected this view – pointedly stating that “antitrust enforcers are able to separate the wheat from the chaff in identifying exclusionary and predatory acts.” Additionally, she stressed that the Report improperly overstates “a dominant firm’s ability to act efficiently” while understating “the importance of redressing exclusionary and predatory acts that result in harm to competition, distort markets, and increase barriers to entry.” According to Varney, “[t]he ultimate result is that consumers are harmed through higher prices, reduced product variety, and slower innovation.”

Varney joined the FTC Commissioners who criticized the September 2008 Report’s view that “anticompetitive harm must substantially outweigh procompetitive benefits” in order for conduct by a monopolist to be actionable. In her opinion, the prior Administration’s “substantially outweighs” standard (which is not articulated in any case law) is “an overly lenient approach to enforcement” that “advocates extreme hesitancy in the face of potential abuses by monopoly firms.” She emphasized that while it is important to preserve the right of companies with market power or dominant positions to compete, the DOJ would not allow predatory or unjustified exclusionary acts to continue without sanction. Accordingly, she withdrew the prior DOJ Report, effective immediately.

Varney placed a large part of the blame on Chicago School economics, which she declared allows markets to “self-police,” and requires enforcement authorities to wait for markets to “self-correct.” This has not worked, she commented, and factors including ineffective government regulation, ill-considered deregulatory measures, and inadequate antitrust oversight have contributed to the current economic conditions.

Varney intends to turn away sharply from what she characterized as the non-interventionist § 2 enforcement policy of the Bush Administration

Although Varney stressed that the DOJ would not use “one specific test to govern all Section 2 matters,” she did suggest that several “leading cases” would guide the Department’s analysis: *Lorain Journal*,² *Aspen Skiing*,³ and *Microsoft*.⁴ According to Varney, these cases provide “tried and true standards that set forth clear limitations on how monopoly firms are permitted to behave.” However, she relegated to a footnote the Supreme Court’s more recent 2004 *Trinko*⁵ decision, in which Justice Scalia opined that a monopolist’s charging of monopoly prices “is an important element of the free-market system,”⁶ and that the 1985 *Aspen Skiing* decision was “at or near the outer boundary of Section 2 liability.” Varney remarked that *Trinko* and this year’s *linkLine*⁷ decision, in which Chief Justice Roberts emphasized that there are “only rare instances in

which a dominant firm may incur antitrust liability for purely unilateral conduct,” only apply to “limited, specific sectors subject to significant and specialized regulator overlay,” and “there is no question that these decisions reaffirmed *Aspen Skiing*’s limits on a monopolist’s ability to engage in exclusionary or predatory conduct.” She described such limits as requiring dominant firms to deal with their rivals when “cooperation is indispensable to effective competition,” citing a decision by Seventh Circuit Judge Richard Posner.⁸

Varney concluded by noting that “the Department is committed to aggressively pursuing enforcement of Section 2 of the Sherman Act in furtherance of the principles embodied in these cases,” and she specifically identified the Obama Administration pledge for “broad reforms” in the banking, healthcare, energy, telecommunications, and transportation industries.

In the few months since Varney withdrew the Report, there have been reports of multiple DOJ investigations of potential § 2 violations. Given its network platform position, many considered Google a likely early target of the Department’s enforcement policy, and the DOJ has acknowledged in a letter to the U.S. District Court for the Southern District of New York that it is pursuing an investigation into whether a proposed litigation settlement agreement between Google and authors and publishers for its book-search service violates the Sherman Act. There also have been reports of a preliminary review to determine whether AT&T Inc., Verizon Communications Inc., and

other telecom companies have abused their market power. Although the DOJ has not commented on the potential investigation, some speculate that the Department is analyzing the telecom companies’ exclusive arrangements with handset makers, such as AT&T’s exclusive right to service Apple Inc.’s iPhone devices. Finally, the *New York Times* recently reported that the DOJ is “preparing to rein in a host of major industries,” indicating that companies in the airline, railroad, cable, agricultural, and financial services industries may be targets of investigation.⁹

As evident from the withdrawal of the Report and the investigations launched by the DOJ in recent months, AAG Varney intends to turn away sharply from what she characterized as the non-interventionist § 2 enforcement policy of the Bush Administration and to adopt instead a tough, aggressive enforcement stance. Although § 2 does not prohibit the mere possession of monopoly power, the DOJ under the Obama Administration will scrutinize the actions of companies with dominant positions, particularly companies that hold dominant positions in high-tech or network industries, and will investigate and consider new theories of anticompetitive harm.

1 The text of Varney’s speech can be found here: <http://www.usdoj.gov/atr/public/speeches/245711.htm>.

2 342 U.S. 143 (1951).

3 472 U.S. 585 (1985).

4 253 F.3d 34 (D.C. Cir. 2001) (*en banc*).

5 540 U.S. 398 (2004).

6 *Id.* at 407.

7 125 S. Ct. 1109 (2009).

8 *Olympic Equip. Leasing Co. v. Western Union Tel. Co.*, 797 F.3d 370, 377-78 (7th Cir. 1986).

9 Stephen Labaton, “Antitrust Chief Hits Resistance in Crackdown,” *New York Times*, July 26, 2009.

DOJ Allies with FTC in Antitrust Attack on Reverse Payment Settlements; While FTC Also Seeks Legislative Solution

By Alan R. Kusnitz and Ausrá Pumputis

The term “reverse payment” in the context of pharmaceutical settlements encompasses agreements reached between patent holders and an alleged infringing manufacturer of a generic version of the patent holder’s branded drug in which monetary or other consideration flows from the patent holder to the alleged infringer. On July 6, 2009, the Department of Justice (“DOJ”) ended an apparent policy split with the Federal Trade Commission (“FTC”) regarding the legality of such settlements by filing an amicus brief in the United States Court of Appeals for the Second Circuit¹ that supports the FTC’s view that such settlements are presumptively unlawful.² The brief advances President Obama’s goal of banning reverse payments³ and Assistant Attorney General Varney’s confirmation hearing promise earlier this year that she would “align the Federal Trade Commission and the DOJ on the issue.”⁴

Background

During the Bush Administration, the FTC had contended in court and administrative proceedings that reverse payments settling patent disputes between pioneer drug companies and their generic rivals were presumptively illegal under a rule of reason analysis.⁵ At the same time, the Commission advocated in congressional hearings and speeches, that reverse payments should be outlawed entirely.⁶ The Bush DOJ, on the other hand, opposed the FTC’s petition for certiorari to the Supreme Court in the *Schering-Plough* reverse payments case that the FTC had lost

in the Eleventh Circuit,⁷ criticizing the FTC’s efforts to condemn as a practical matter all reverse payment settlements as per se violations of the antitrust laws,⁸ its advocacy of a subjective standard,⁹ and its contention that there was a split of authority among the circuits justifying Supreme Court review.¹⁰

Another FTC Setback at the Supreme Court

Those hoping for judicial clarity on the reverse payment issue were disappointed when the Supreme Court, on June 22, 2008, denied another certiorari petition to review the antitrust challenge of Bayer AG’s reverse payment settlement with generic drug maker Barr Pharmaceuticals, which kept generic “Cipro” drug off the market.¹¹ One day after this latest Supreme Court setback, FTC Chairman Jon Leibowitz, in a speech before the Center for American Progress, acknowledged that “waiting for a potential judicial solution is a time consuming and expensive prescription,”¹² and advocated a legislative resolution of the debate. Arguing that American consumers would save \$35 billion or more over ten years – \$12 billion of which would be a savings to the federal government – if reverse payment settlements were prohibited, he called on Congress to pass legislation banning reverse payments.¹³ He also countered arguments by brand companies that barring reverse payment settlements would mean less innovation by reminding Congress that “competition rather than collusion fosters creativity.” He also indicated that

there was growing support within Congress for a legislative solution. Early this month, he achieved a promising win when a House subcommittee approved a bill titled “Protecting Consumer Access to Generic Drugs Act of 2009” that would establish a clear, bright-line standard prohibiting reverse payment patent settlements.¹⁴

The DOJ *Cipro* Brief – Reversal on Reverse Payments

The DOJ *Cipro* Brief affirms the Obama Administration’s determination to stop reverse payment settlements.¹⁵ In contrast to its earlier position articulated in the *Schering-Plough* case, the DOJ *Cipro* Brief advocates a rule of reason analysis that treats reverse payment settlements as “presumptively unlawful” without an objective assessment of the merits of the patent claims involved.¹⁶ This standard generally mirrors the FTC’s approach advocated in *Schering-Plough*.¹⁷ However, the DOJ *Cipro* Brief endeavors to put the standard on a firmer theoretical foundation than that articulated by the FTC, describing the types of proof needed under the “presumptively unlawful” standard in substantially more detail than the FTC has done to date.

DOJ’s Rationale

According to the DOJ, a patentee has a choice. It can enjoy either antitrust immunity by litigating patent validity to judgment, thereby assuming the risk of patent invalidity, or it can preserve validity through a private settlement, thereby subjecting the settlement contract to antitrust

scrutiny like any other private contract.¹⁸ According to the DOJ, any other rule would allow patent holders “to contract their way out of the statutorily imposed risk that patent litigation could lead to invalidation of the patent while claiming antitrust immunity for the private contract.”¹⁹ The DOJ contends that this provides “no protection to the public interest in eliminating undeserved patents.”²⁰ Thus, according to the DOJ, while “settlement of patent litigation is generally to be encouraged,” it must not do so “while evading the risk of patent invalidation.”²¹

If the settlement route is chosen by the patent holder and the generic challenger, DOJ contends that the settlement should be tested under the rule of reason, not the per se rule.²² The rule of reason is the appropriate instrument because it allows the courts to balance the efficiency-related justifications of settlements with the anticompetitive potential of reverse payments.²³ Settlements are efficient, not only conserving judicial resources, but also avoiding unnecessary litigation costs. Indeed, the DOJ believes that the vast majority of settlements in patent cases are likely to be efficiency enhancing and lawful.²⁴ Moreover, settlements without a payment divide “the remaining life of the patent into a period of exclusion and a period of competition ... adequately accommodat[ing] the public interest in freeing the market from undeserved monopolies.”²⁵ Such settlements appear to be presumptively legal under both the FTC’s and the DOJ’s analysis.²⁶

To the DOJ, however, a settlement involving a reverse payment is a “red flag” that the generic company is relinquishing the opportunity to compete beyond the point that would otherwise reflect the parties’ shared

view of the likelihood that the patentee would ultimately prevail in the litigation.²⁷ In other words, the DOJ believes that such a payment is evidence that the patent holder purchased reduced competition that it would not ordinarily have been entitled to under the Patent Act.

The Proposed DOJ Standard

Under the rule of reason, the court must balance the anticompetitive effects of the payment, as well as the potential justifications for the payment. The DOJ proposes a rule of reason standard under which the antitrust plaintiff would at the outset be required to establish a prima facie case by showing that (i) the generic manufacturer withdrew its challenge

The chance that the [reverse payment] issue will be addressed by the Supreme Court . . . likely is increased

to the patent’s validity; (ii) money (or other consideration serving the same purpose) flowed from the patent holder to the generic drug firm; and (iii) the payment accompanied an agreement to withdraw the validity challenge.²⁸ Once the plaintiff makes this showing, the settlement would be considered presumptively unlawful, and the burden would shift to the defendants to show that competition under the settlement did not differ substantially from what was expected had the patent infringement suit been litigated to judgment.²⁹ The DOJ strongly recommended against an approach that “could reduce parties’ incentive to settle the patent litigation” and would embed a patent trial within an antitrust trial.³⁰ Instead, under the DOJ’s suggested standard, the defendants could rebut the presumption of illegality if they

could show that the payment was no more than an amount commensurate with the patent holder’s avoided litigation costs.³¹ According to the DOJ, such a settlement demonstrates that the parties have not obtained more exclusion than they subjectively believed would have been the outcome of a full patent trial.

If it is shown that the payment was greatly in excess of avoided litigation costs, the DOJ’s proposed standard fleshes out the FTC’s proposed standard,³² by focusing on the competitive implications of others terms in the settlement; in particular, on the nature and the extent of the generic competition permitted.³³ For example, if the settlement allowed no generic competition until patent expiration, the reverse payment would be found unlawful. On the other hand, if the settlement allowed generic competition before the patent expired, the defendants would carry their burden by showing that the settlement preserved a degree of competition reasonably consistent with what had been expected if the infringement litigation went to judgment.³⁴ In other words, the defendants can carry their burden by providing a reasonable explanation that the payment bought something other than an additional limitation of competition.³⁵ However, under the proposed DOJ standard, defendants will not prevail by simply showing that they reasonably believed (as opposed to actually proving in a mini-trial) that their patent would be upheld.³⁶

The Likely Outcome

Now that the two federal antitrust agencies see eye to eye regarding reverse payment settlements, the chance that the issue will be addressed by the Supreme Court in the *Cipro* case likely is increased. If the Second Circuit adopts the DOJ’s suggested rule of reason analysis in this case, a

significant split among the circuits would arise which could not be distinguished by a narrow interpretation of the case as most courts and commentators had done regarding the Sixth Circuit's decision in *Cardizem*, striking down a reverse payment settlement as per se illegal.³⁷ In addition, the FTC is currently litigating reverse payment settlement challenges in federal district court in Pennsylvania. On appeal, this case would go to the Third Circuit, which at times is more sympathetic to antitrust plaintiffs than the Second, Eleventh or Federal Circuits. Therefore, a more substantial split among the circuits could occur which would present an even more enticing case for the Supreme Court. In the meantime, pharmaceutical companies should closely evaluate future settlement agreements to establish whether they would violate the rule of reason standard now proposed by both antitrust agencies.

1 Brief for the United States in Response to the Court's Invitation, *Arkansas Carpenters Health and Welfare Fund v. Bayer AG*, No. 05-2851 (2d Cir. July 6, 2009) [hereinafter *DOJ Cipro Brief*]. The DOJ filed the brief after the Second Circuit asked for its views in a case brought over an agreement in which Bayer AG allegedly paid Barr Laboratories Inc. and others \$398 million to delay marketing a generic version of the antibiotic Cipro. Specifically, the Second Circuit asked "whether settlement of patent infringement lawsuits violates the federal antitrust law as when a potential generic drug manufacturer withdraws its challenge to the patent's validity ... and ... in return offers the generic manufacturer substantial payments." The court's question is significant given its decision in *In re Tamoxifen Citrate Antitrust Litig.*, 466 F.3d 187 (2d Cir. 2006), *cert. denied*, 127 S. Ct. 3001 (2007), in which the court held that while a substantial reverse payment might be "suspicious," it is not unlawful to receive a substantial sum of money "as long as the patent litigation is neither a sham nor otherwise baseless" and the settlement agreement does not extend the scope of the patent "monopoly." *Id.* at 208, 212-214.

2 See *In re Schering-Plough Corp.* (Opinion of the Comm'n), FTC Dkt. No. 9293, 136 F.T.C. 956 (Dec. 8, 2003), *vacated*, 402 F.3d 1056 (11th Cir. 2005), *cert. denied*, 126 S. Ct. 2929 (2006) [hereinafter *FTC Schering-Plough Opinion*].

3 See President Barack Obama, Office of Mgmt. & Budget., Exec. Office of the President, Budget of the United States Government,

Fiscal Year 2010 (2009) (proposed) at 28, available at http://www.whitehouse.gov/omb/assets/fy2010_new_era/A_New_Era_of_Responsibility2.pdf (promising to prevent "collusion between brand-name and generic drug manufacturers intended to keep generic drugs off the market.")

4 *Nomination of Christine Anne Varney to be Assistant Attorney General in the Antitrust Division, Hearing of the S. Comm. on the Judiciary*, 111th Cong. (2009), available at Fed. News Service, Mar. 10, 2009.

5 See *FTC Schering-Plough Opinion*, *supra* note 2 ("Absent proof of other offsetting consideration, it is logical to conclude that the *quid pro quo* for the payment was an agreement by the generic to defer entry beyond the date that represents an otherwise reasonable litigation compromise."); see also Petition for Writ of Certiorari at 18, *FTC v. Schering-Plough Corp.*, 548 U.S. 919 (2006) (No. 05-273), available at <http://www.ftc.gov/os/2005/08/050829scheringploughpet.pdf> ("[I]f the parties simply compromise on an entry date prior to the patent's expiration, without cash payments, the resulting settlement would reflect the parties' own assessment of the strength of the patent.")

6 See, e.g., Richard Feinstein, Director, Fed. Trade Comm'n, *Anticompetitive Pay-For-Delay Settlements in the Pharmaceutical Industry: Why Consumers and the Federal Government are Paying Too Much for Prescription Drugs*, Prepared Statement of The Federal Trade Commission before the Subcomm. on Courts and Competition Policy of the H. Comm. on the Judiciary (June 3, 2009), available at <http://www.ftc.gov/os/2009/06/P859910payfordelay.pdf>; see also *How Pay-For-Delay Settlements Make Consumers and the Federal Government Pay More for Much Needed Drugs: Hearing Before the Subcomm. on Commerce, Trade, and Consumer Protection of the H. Comm. on Energy and Finance*, 111th Cong. (2009) (statement of J. Thomas Rosch, Comm'r, Fed. Trade Comm'n) (advocating a rule of per se illegality), available at <http://www.ftc.gov/speeches/rosch/090331payfordelay.pdf>; see also Prepared Statement of the Fed. Trade Comm'n, *Anticompetitive Patent Settlements in the Pharm. Indus.: The Benefits of a Legislative Solution 1* (Jan. 17, 2007), available at http://www.ftc.gov/speeches/leibowitz/070117anticompetitivepatentsettlements_senate.pdf [hereinafter *Anticompetitive Patent Settlements in the Pharm. Indus.*] (supporting a legislative approach banning reverse payment settlements).

7 Brief for the United States as Amicus Curiae, *FTC v. Schering-Plough Corp.*, No.-05-273 (U.S. May 17, 2006), available at <http://www.usdoj.gov/atr/cases/f216300/216358.htm>, *cert. denied*, 126 U.S. 2929 (2006).

8 *Id.* at 11-12.

9 *Id.* The DOJ suggested that the proper standard for evaluating reverse payment settlements should include an objective assessment of the merits of the patent claims, viewed *ex ante*, rather than the FTC's view that the settling parties' subjective views of the strength of the claims as reflected in the settlement.

10 *Id.* at 16-20. Compare *In re Ciprofloxacin Hydrochloride Antitrust Litigation*, 544 F.3d

1323 (Fed. Cir. 2008); *In re Tamoxifen Citrate Antitrust Litig.*, 466 F.3d 187, 206-07 (2d Cir. 2006), *cert. denied*, 127 S. Ct. 3001 (2007); *In re Schering-Plough Corp.* (Opinion of the Comm'n), FTC Dkt. No. 9293, 136 F.T.C. 956 (Dec. 8, 2003), *vacated*, 402 F.3d 1056 (11th Cir. 2005), *cert. denied*, 126 S. Ct. 2929 (2006) (upholding reverse payment settlements where the terms of the agreement do not restrict competition beyond the exclusionary potential of the patent) with *In re Cardizem CD Antitrust Litigation*, 332 F.3d 896 (6th Cir. 2003) (the district court and the Sixth Circuit holding that an interim settlement of the patentee's infringement claim was a per se illegal market allocation agreement). However, in *Cardizem*, the settlement provided that the challenger would not enter the market before a final and unappealable judgment of non-infringement and would receive cash payments. The Sixth Circuit's succinct discussion of the merits could be read literally to say that paying a competitor to stay off the market in a patent settlement is always per se illegal. However, most courts and commentators considering the decision have read it more narrowly to hold that the settlement was per se illegal in that case due to several egregious circumstances. In particular, the *Cardizem* settlement (1) covered generic products whether or not they infringed a patent held by the branded firm, (2) used certain Hatch-Waxman provisions to "game the system" so that third party generics were precluded from entering, and (3) did not settle the patent litigation, but granted a private preliminary injunction on terms different from those a real court would have ordered. The *Cardizem* settlement agreement, therefore, exceeded the scope of the restrictions inherent in the patent grant, and in that respect the court's decision was consistent with earlier case law regarding the relationship between antitrust law and patents.

11 *Arkansas Carpenters Health and Welfare Fund et al. v. Bayer AG and Bayer Corp. et al.* No. 08-1194 (U.S. June 22, 2009).

12 Jon Leibowitz, Chairman, Fed. Trade Comm'n, Address at Center for American Progress: "Pay-for-Delay" Settlements in the Pharmaceutical Industry (June 23, 2009).

13 See *id.* The calculated savings are the result of a new empirical study conducted by the FTC's Bureau of Economics. The Chairman explained that the study was based on relatively conservative assumptions about consumer savings from generic competition, the likelihood of future reverse payment settlements and the volume of drugs for which settlements are likely. According to the FTC, reasonable alternative assumptions would result in even bigger consumer savings of \$75 billion.

14 Protecting Consumer Access to Generic Drugs Act of 2009, H.R. 1706, 111th Cong. (2009). Representatives Rush, Waxman, Dingell, Schakowsky, and others introduced the bill. It was approved by a 16 to 10 vote in the House Energy and Commerce Subcommittee. The Subcommittee also rejected a variety of industry supported amendments which would have substantially weakened the bill. Another bill has also recently been introduced to Congress which would prohibit reverse payment settlements. See Preserve Access to Affordable Generics Act, S. 369, 111th Cong.

(2009) (to prohibit brand name drug companies from compensating generic drug companies to delay the entry of a generic drug into the market).

15 *DOJ Cipro Brief, supra* note 1.

16 *Id.*

17 *See FTC Schering-Plough Opinion, supra* note 2.

18 *DOJ Cipro Brief, supra* note 1, at 14.

19 *Id.* at 14.

20 *Id.* at 15.

21 *Id.* at 16.

22 *Id.* at 21.

23 *Id.* at 9-10.

24 *Id.* at 20.

25 *Id.* at 22.

26 *Id.*

27 *Id.*

28 *Id.* at 23.

29 *Id.* at 28.

30 *Id.* at 25-26.

31 *Id.* at 28-29. The relevant cost measure includes the cost of business disruption and a modest reverse payment to “bridge the gap” between parties with different expectations about litigation outcomes. The DOJ concedes that “precision is impossible.”

32 Acceptable explanations for a reverse payment according to the FTC are a reverse payment based on estimated saved litigation costs and a royalty to the patent holder or compromising on a damage claim. *See* Thomas B. Leary, *Antitrust Issues in the Settlement of Pharmaceutical Patent Disputes, Part III*, 30 *Seattle U. L. Rev.* 377, 391-92 n. 69 (2007). The FTC has never articulated what other reasonable explanations for a reverse payment it would accept.

33 *DOJ Cipro Brief, supra* note 1, at 29.

34 *Id.* at 29-30.

35 *Id.* at 31-32.

36 *Id.* at 31.

37 *See In re Ciprofloxacin Hydrochloride Antitrust Litig.*, 514 F. Supp. 2d 514, 526 (E.D.N.Y. 2005), *aff'd*, 544 F.3d 1323 (Fed. Cir. 2008) (discussing the district court’s examination of *Cardizem*).

38 *FTC v. Cephalon, Inc.*, 551 F. Supp. 2d 21 (D.D.C. 2008) (granting transfer motion to E.D.P.A.), complaint available at <http://www2.ftc.gov/os/caselist/0610182/080213complaint.pdf>; *FTC v. Watson Pharm.*, No. CV-09-00598 (C.D. Cal. complaint filed Jan. 29, 2009), available at <http://www2.ftc.gov/os/caselist/0710060/090202androgelcmpt.pdf>. (alleging that Solvay paid the generic companies to delay generic competition to Solvay’s branded testosterone-replacement drug AndroGel).

Eighth Circuit Reiterates Distinction Between Vertical and Horizontal Agreements in Dual Distribution Arrangements

By Robert Yezerski

The characterization of conduct as either vertical or horizontal in nature is a critical factor in many cases arising under § 1 of the Sherman Act. Horizontal “contracts, combinations or conspiracies” are per se unlawful in most circumstances, particularly when the horizontal restraint amounts to an agreement on price or a division of geographic or customer markets.¹ By contrast, vertical arrangements generally are evaluated under a rule of reason standard, pursuant to which the anticompetitive effects of the conduct are weighed against the conduct’s procompetitive benefits.² The result is that the distinction between horizontal and vertical conduct is not simply one of academic taxonomy, but rather has significance for the juridical standards to be applied in evaluating the lawfulness of the conduct at issue.³ Unsurprisingly, this differential treatment creates strong incentives for plaintiffs to categorize a restraint as horizontal, and for defendants to classify the same conduct as vertical. This is a particular concern in dual distribution systems in which a supplier – usually a producer – is vertically integrated downstream so that it actually or potentially competes with its distributor or dealer customers. When it places restraints on those customers, the issue is whether the restraints should be classified as horizontal because it may be a competitor of one or more of its customers, or vertical because its basic role may be as their supplier.

A good example of the difficulties that can arise in classifying conduct as

either horizontal or vertical in a dual distribution system is the Eighth Circuit’s recent decision in *Nitro Distributing, Inc. v. Altacor, Inc.*⁴ The case involved former distributors of Amway’s products who brought a claim under § 1 of the Sherman Act alleging that Amway (and certain affiliates) had entered into a per se unlawful horizontal market division with various independent Amway distributors with whom it actually competed as a vertically integrated distributor. At its core, the case concerned Amway’s involvement in mediating the disintegration of one of its distribution networks into two separate networks. The issue was whether, in facilitating this disintegration (which included a non-compete clause among the previously integrated entities), Amway had entered into a per se unlawful horizontal market division, particularly given that the separated entities competed with Amway’s own proprietary distribution system.

Amway, the manufacturer of a wide variety of consumer products, distributes its products via a “pyramid system” that it calls a “network marketing” model.⁵ Under this system, its “sponsor” distributors recruit new sub-distributors into the Amway distribution network. Sub-distributors recruited by a sponsor become that sponsor’s “downline.”⁶ It is in each sponsor’s interest to promote sales by its downline because the downlines will generally purchase all of their supplies from the sponsor. Unsurprisingly, a significant business has developed in motivational tools and aids designed to help

sponsors recruit new distributors or encourage sales by their downline. This motivational “tools” business operates in the same manner as the Amway products business: generally, each sponsor’s downline purchases its entire demand for “tools” exclusively from its sponsor.⁷

Nitro Distributing involved the decision by certain tools distributors to break away from their existing distribution chain and form a new distribution network. Amway helped facilitate this breakaway by providing the departing distributors with Amway’s antitrust primer, and by appointing a mediator for discussions between the breakaway distributors and their former sponsor. These parties subsequently negotiated terms for the separation of their distribution networks, which included an agreement not to solicit each other’s downlines.⁸ The plaintiffs in *Nitro Distributing* were downline “tools” distributors in the same line as the departing distributors, who claimed that they were injured when the breakaway distributors left the line. As Amway itself also sells and distributes motivational “tools” to Amway distributors, the plaintiffs alleged that Amway’s involvement in the separation arrangement constituted a horizontal market allocation in violation of § 1 of the Sherman Act.

The Eighth Circuit rejected the plaintiffs’ attempt to characterize the conduct as a horizontal arrangement. While the court acknowledged that Amway had its own “tools” business that competed with the breakaway distributors’ businesses, it noted that the overlap was only “a small fraction of Amway’s overall business,” and that Amway did not “meaningfully compete with companies like [the breakaway distributors].”⁹ Though, as a factual matter, there existed some horizontal overlap between Amway

and the breakaway distributors, the court reasoned that Amway’s conduct, considered in context, was more properly characterized as vertical in nature. The court stressed that “the role Amway played in this separation was not as a horizontal competitor, but as a vertical quasi-parent company interested in the survival of its primary business.”¹⁰ The classification of the conduct as vertical, rather than horizontal, took the conduct outside the realm of per se treatment. As such, Amway’s conduct could not be condemned absent a full rule of reason analysis.

The Eight Circuit’s opinion has important implications for vertically integrated suppliers that operate dual distribution systems

The Eighth Circuit went on to conclude that Amway’s actions were lawful efforts to peacefully disentangle its distribution lines. The court noted that “the parties were involved in contentious negotiations, and making lawful concessions to maintain peaceful business relations does not violate antitrust laws.”¹¹ While the non-solicitation term of the breakaway agreement did amount to a market division among the Amway distributors involved, the Eighth Circuit referred to Federal Trade Commission precedent involving Amway in concluding that Amway’s “line of sponsorship system is vertically imposed and is reasonably ancillary to compensation, efficient distribution, and training.”¹² The court adopted the Federal Trade Commission’s reasoning that the non-solicitation term was justified by Amway’s overall goal of maintaining an efficient distribution system, which in turn would foster greater inter-

brand competition between Amway and its rivals.

The Eighth Circuit’s opinion has important implications for vertically integrated suppliers that operate dual distribution systems. The mere fact that a supplier maintains its own proprietary distribution network in competition with distributor or dealer customers does not necessitate the conclusion that an agreement between the supplier and its independent distributors is horizontal in nature. Nor does a dual distribution system preclude a supplier from imposing reasonable, ancillary restraints on its independent distributors for the purpose of fostering greater interbrand competition. The critical consideration for any court in evaluating the lawfulness of such restraints is not the degree of competitive overlap between the supplier and its distributors, but the overall competitive effect in the relevant market of the restraint imposed. Nevertheless, as the *Amway* case demonstrates, it is in the interest of suppliers operating dual distribution systems to maintain a detailed documentary record of the procompetitive rationale and intended effects of restraints imposed on independent distributors or dealers as a shield against later claims of unlawful horizontal conduct.

1 See, e.g., *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) (horizontal price fixing); *Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46 (1990) (horizontal geographic market division).

2 See, e.g., *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977) (vertical territorial restraint); *Tampa Elec. Co. v. Nashville Coal Co.* 365 U.S. 320 (1961) (exclusive dealing).

3 Courts look to substance over form in determining whether conduct is horizontal or vertical in nature. A restraint that is implemented by a supplier on its dealers may nevertheless be treated as a horizontal restraint when it emanates from an agreement among the customers (so-called “hub and spoke” conspiracies). See, e.g., *United States v. General Motors Corp.*, 384 U.S. 127 (1966) (manufacturer’s restriction on dealers selling

to discounters was instituted at the request of dealers and condemned as part of horizontal conspiracy); *Dickinson v. Microsoft Corp.*, 309 F.3d 193 (4th Cir. 2002) (a per se unlawful hub and spoke conspiracy requires “rim” of horizontal agreement among distributors; series of independent vertical agreements between supplier and each distributor alone is insufficient.) *Lovett v. General Motors Corp.*,

998 F.2d 575 (8th Cir, 1993) (“Section one does not prohibit a manufacturer from taking independent action against a dealer,” but manufacturers cannot engage in “concerted action” with their dealers to effect a restraint of trade.)

4 565 F.3d 417 (8th Cir. 2009).

5 *Id.*, at 420.

6 *Id.*

7 *Id.*

8 *Id.* at 422.

9 *Id.* at 425.

10 *Id.* at 424.

11 *Id.* at 425.

12 *Id.* at 426, citing *In the Matter of Amway*, 93 F.T.C. 618 (1979).

Supreme Court Grants Certiorari to Hear NFL Single-Entity Licensing Case, Despite DOJ/FTC Amicus Brief Urging Denial

By Jeff L. White

On May 29, 2009, the DOJ and FTC filed a joint amicus brief in the U.S. Supreme Court urging the Court to deny certiorari in *American Needle, Inc. v. National Football League*, No. 08-661 (U.S. Sup. Ct.). The Court of Appeals for the Seventh Circuit had held that the National Football League (“NFL”), including its 32 teams, constituted a single entity for purposes of licensing team trademarks and logos for use in headwear. Thus, the NFL’s licensing decisions are unilateral acts not subject to liability under § 1 of the Sherman Act, which addresses only concerted conduct among independent entities.¹ The Seventh Circuit also held that the NFL’s decision to grant an exclusive headwear license to an apparel vendor was not monopolistic conduct in violation of § 2 of the Sherman Act. Despite the government’s amicus brief arguing that review of the Seventh Circuit’s decision was not warranted, on June 29, 2009, the Supreme Court granted certiorari to hear the case.²

Background

In 1963, the NFL teams formed a separate corporate entity, National Football League Properties, LLC (“NFLP”), to develop, license, and market the intellectual property

owned by NFL teams, including their trademarks and logos. The NFL teams subsequently granted NFLP the exclusive right to license their trademarks and logos. For many years, the NFLP licensed multiple vendors (including American Needle) the right to manufacture, distribute, and sell headwear bearing these marks, such as baseball caps and stocking hats. In 2001, however, NFLP entered into an agreement with Reebok International Ltd. (“Reebok”) under which Reebok became the exclusive headwear licensee of NFL team trademarks and logos for ten years. Accordingly, NFLP did not renew American Needle’s headwear license.

In 2004, American Needle filed an antitrust lawsuit against NFLP, the NFL, the NFL teams, and Reebok in the U.S. District Court for the Northern District of Illinois alleging that the exclusive headwear licensing agreement violated §§ 1 and 2 of the Sherman Act. The district court ultimately granted summary judgment to the defendants on American Needle’s § 1 claim on the ground that the NFL and its 32 teams are, in the jargon of antitrust law, acting as a single entity in the “exploitation of intellectual property rights.”³

The court concluded that the NFL teams “have so integrated their operations that they should be deemed to be a single entity rather than joint venture[rs] cooperating for a common purpose.”⁴

Before the Seventh Circuit, the defendants again argued that their conduct was immune from liability under § 1 because they function as a single entity, relying in part on *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984).⁵ American Needle argued that the NFL teams potentially compete against one another when licensing and marketing their intellectual property, and thus should not be viewed as a single entity for antitrust purposes. The Seventh Circuit ultimately ruled that the NFL’s single-entity status in the present context does not entirely turn on whether the league’s members might compete with each other in the licensing and marketing of their intellectual property. Indeed, the Seventh Circuit noted that Copperweld did not afford single-entity status to only those entities that are conflict-free, and it concluded that “the NFL teams can function only as one source of economic power when collectively producing NFL

football.”⁶ Because the antitrust laws encourage cooperation within a business organization, the Seventh Circuit declared that “the NFL teams are best described as a single source of economic power when promoting NFL football through licensing the teams’ intellectual property.”⁷

The Government’s View

In a joint amicus brief filed in the Supreme Court in opposition to the certiorari petition, the DOJ and FTC argued that even though the Seventh Circuit’s analysis was problematic, Supreme Court review was not warranted because the appellate court specifically limited its holding to the facts of the case.⁸

Specifically, the government’s brief noted that American Needle’s alleged injury appeared to flow from the NFLP’s decision to contract with an exclusive licensee, rather than any anticompetitive effects of the teams’ collective agreement to market their trademarks and logos together. Additionally, the brief contended that Copperweld only affords single-entity treatment to a parent and its wholly owned subsidiary, and thus the Seventh Circuit improperly extended single-entity treatment to the NFL and its separately owned teams in connection with their collective licensing of intellectual property. Despite conceding that NFL football is an efficiency-enhancing activity, the DOJ and FTC maintained that an agreement to restrict competition among separate firms does not necessarily cease to be concerted action in all circumstances. According to the government, the Seventh Circuit’s decision has the effect of precluding the possibility that a reduction in competition among NFL

teams outweighs the efficiency-enhancing potential of the joint licensing activity. Despite these problems in the Seventh Circuit’s analysis, the government’s brief concluded that the court’s fact-specific holding did not warrant the Supreme Court’s review in this case.

Despite the government’s amicus brief . . . [opposing review] the Supreme Court granted certiorari to hear the case

In addition, the DOJ and FTC argued that the Seventh Circuit’s decision does not conflict with any prior decisions of the Supreme Court or other appellate court decisions. Specifically, they stated that prior Supreme Court decisions have not squarely addressed the issue of single-entity treatment, and that no other circuit court has held that “the NFL and its member teams are separate entities when collectively licensing their intellectual property.”⁹

Finally, the government argued that the questions presented by the parties in this case do not warrant the Supreme Court’s review. They suggested that whether single-entity treatment is appropriate requires a fact-specific inquiry into the nature of the case. Contrary to the NFL’s position, the government stressed that a broad holding applying single-entity treatment to every § 1 lawsuit against the league would be inappropriate. Invoking the complex and fact-specific inquiry applied in *Texaco Inc. v. Dagher*, 547 U.S. 1 (2006), the government noted that “the somewhat idiosyncratic nature of the

relationship between individual NFL teams and the league as a whole makes this case an unsuitable vehicle for resolving broader questions of the kind the NFL respondents identify.”

The NFL supported the plaintiff’s certiorari petition, but not its arguments. It can only be speculated as to whether this support was a significant factor in the Supreme Court’s acceptance of the petition.¹⁰

Implications

Now that the Supreme Court has granted certiorari to hear this case, it will be interesting to see whether the Court affords single-entity treatment under § 1 to virtually all joint activities of the NFL and its teams, or whether it adopts the government’s narrower view that single-entity treatment is only appropriate in certain limited instances. The government, all major sport leagues, antitrust practitioners, and many other interested parties eagerly watch from the sidelines in anticipation of the Court’s ruling.

1 *Am. Needle, Inc. v. NFL*, 538 F.3d 736 (7th Cir. 2008).

2 *Am. Needle, Inc. v. NFL*, 2009 U.S. LEXIS 4899 (U.S., June 29, 2009).

3 *Am. Needle, Inc. v. New Orleans La. Saints*, 496 F. Supp. 2d. 941, 943 (N.D. Ill. 2007).

4 *Id.* The § 2 claims were dismissed as well, on the basis of an unduly narrow market definition.

5 467 U.S. 752 (1984).

6 538 F. 3d at 743.

7 538 F. 3d at 744. The § 2 dismissal was affirmed as well. See “Professional Sports League Licensing Arrangements Survive Antitrust Scrutiny But Under Different Analytical Frameworks,” *Antitrust Update* Fall 2008.

8 Brief for the United States as Amicus Curiae, *American Needle, Inc. v. National Football League*, No. 08-661 (May 29, 2009), at 6.

9 *See id.* at 15.

10 *See id.* at 21.

Parties Abandon Blood Plasma Products Merger After FTC Challenge Grounded in Coordinated Effects Theory

By Vadim Brusser

On May 27, 2009, the Federal Trade Commission (“FTC”) filed an Administrative Complaint against CSL Limited (“CSL”) and Cerberus-Plasma Holdings, LLC (“Cerberus”), alleging that the parties’ proposed merger threatened to substantially lessen competition in the markets for four plasma-derivative therapies.¹ The FTC also moved for a preliminary injunction in the U.S. District Court for the District of Columbia seeking to stop the merger until resolution of the FTC’s administrative claim. Despite initial statements by the parties that they would fight the FTC’s challenge, they abandoned the transaction two weeks after the FTC filed its Administrative Complaint.²

The FTC’s Claims

CSL first announced its proposed \$3.1 billion acquisition of Talecris Biotherapeutics Holdings Corporation (“Talecris”) from Cerberus on August 12, 2008. CSL, an Australian company, and Talecris, based in the United States, both manufacture and sell plasma-derivative protein therapies. According to the FTC’s Complaint, CSL and Talecris are two of the three largest makers of these plasma products in the world.³ Their plasma products treat a wide range of serious illnesses, including immune deficiency diseases, blood disorders, and neurological disorders.⁴ The cost of the parties’ plasma products can exceed \$90,000 a year if a patient requires extended treatment.⁵

The Complaint alleged that the proposed acquisition would substantially reduce competition in four relevant product markets: immune

globulin (“Ig”), albumin, Rho-D, and Alpha-1. The transaction would reduce the number of significant competitors in both the Rho-D and Alpha-1 markets from three to two. According to the Complaint, Ortho Clinical Diagnostics would have been the only other post-merger competitor in the market for Rho-D. Baxter International (“Baxter”), the largest plasma-product firm in the world, would have been the only other post-merger competitor in the market for Alpha-1.⁶ It was also contended that after the merger, CSL’s Rho-D market share would have been 42 percent and its Alpha-1 market share would have been 82 percent.⁷

According to the Complaint, the merger would have reduced the number of competitors in the markets for both Ig and albumin from five to four. CSL’s post-merger share of the Ig market would exceed 48 percent and its post-merger share of the albumin market would exceed 45 percent.⁸ Further, two of the remaining competitors, Grifols, S.A. (“Grifols”) and Octapharma AG (“Octapharma”) are small and it was alleged that they would have only a limited ability to expand their output.⁹

Alleged Coordinated Interaction

The Complaint’s allegations were based primarily on a coordinated effects theory. According to the Complaint, the plasma industry is a “tight oligopoly,” and the industry players were already coordinating their competitive behavior.¹⁰ It was alleged that the removal of Talecris as a competitor would increase the

ability of the remaining competitors to control the supply of plasma products. The complaint is notable in that the FTC alleged a wealth of evidence that showed ongoing coordination between the market participants. It also shows the FTC’s readiness to challenge a merger in an industry that is already behaving anticompetitively.

The Complaint contained a number of arguments to support the coordinated effects claim. First, it was contended that market conditions in the plasma industry already were conducive to coordinated interaction.¹¹ Consolidation among blood plasma product competitors, which had reduced the number of competitors from 13 to 5 since 1990, had resulted in a highly concentrated industry.¹² Further, plasma products

The Complaint’s allegations were based primarily on a coordinated effects theory

are mostly homogenous, and pricing is largely uniform, which makes it easier for firms to predict their competitors’ prices. Firms can also more easily track the supply of plasma products because demand for these live-saving products is consistently high.¹³

Second, it was alleged that plasma product competitors use “widely available” competitive information to “closely monitor each others’ activities with respect to plasma collection, manufacturing, and output.”¹⁴ Plasma firms also intentionally share certain

competitive information to “signal” their competitors in an effort to reach accord on output decisions.¹⁵ The Complaint also referred to a number of public statements by Baxter, the largest plasma competitor, to highlight the transparent nature of the plasma product industry.¹⁶ According to the Complaint, plasma competitors use the competitive intelligence to control the supply of plasma products and ultimately keep prices for these products at supra-competitive levels.¹⁷

Third, it was alleged that aggressive expansion by Talecris creates a unique competitive constraint in the plasma product markets.¹⁸ The Complaint maintained that competition between Talecris and CSL was particularly aggressive in the market for Rho-D.¹⁹ It was alleged that the remaining competitors could more effectively detect and punish deviating firms if competition from Talecris was eliminated. To support this claim, the Complaint referred to a public comment by Baxter stating that the proposed acquisition of Talecris would be “a positive stabilizing move within the industry.”²⁰

The Complaint also alleged that entry by new firms or expansion by existing

firms is unlikely to counter output reductions.²¹ Potential entrants face significant entry barriers, including high upfront and sunk costs, intellectual-property hurdles, and multiple stages of regulatory review by the U.S. Food and Drug Administration and state health agencies.²² It was contended that these same hurdles also limit expansion by Grifols and Octapharma.²³

Implications of the Suit

The FTC’s challenge to this transaction continues the agency’s active merger enforcement efforts. It also exemplifies the FTC’s practice of conducting administrative proceedings while simultaneously litigating a motion for a preliminary injunction in Federal Court – a practice that some commentators have criticized.

This recent FTC merger challenge also highlights the Commission’s continued reliance on the parties’ internal documents to support its enforcement actions. The parties documents appeared to be particularly problematic in this case. In fact, the FTC’s press release pointedly noted that its “staff had gathered an impressive amount of evidence.”²⁴

1 Complaint, CSL Ltd., Dkt. No. 9337 (FTC May 27, 2009), available at <http://www.ftc.gov/os/adjpro/d9337/090527cslcmpt.pdf>.

2 Statement of the FTC’s Bureau of Competition Regarding the Announcement that CSL Will Not Proceed with its Proposed Acquisition of Talecris Biotherapeutics (June 6, 2009), available at <http://www.ftc.gov/opa/2009/06/csl.shtm>.

3 Complaint, ¶¶ 10, 14 CSL Ltd., Dkt. No. 9337 at (FTC May 27, 2009), available at <http://www.ftc.gov/os/adjpro/d9337/090527cslcmpt.pdf>.

4 *Id.* ¶¶ 10, 45.

5 *Id.* ¶ 20.

6 *Id.* ¶¶ 67-73.

7 *Id.* ¶ 60, Appendices A-D.

8 *Id.* ¶ 60, Appendices A-D.

9 *Id.* ¶ 2.

10 *Id.* ¶ 4.

11 *Id.*

12 *Id.* ¶ 24.

13 *Id.* ¶ 20-21.

14 *Id.* ¶ 37.

15 *Id.* ¶ 29.

16 *Id.* ¶ 36.

17 *Id.* ¶ 33-39.

18 *Id.* ¶ 7.

19 *Id.* ¶ 72.

20 *Id.* ¶ 7.

21 *Id.* ¶ 75.

22 *Id.* ¶¶ 75-80.

23 *Id.* ¶ 80.

24 Statement of the FTC’s Bureau of Competition Regarding the Announcement that CSL Will Not Proceed with its Proposed Acquisition of Talecris Biotherapeutics (June 6, 2009), available at <http://www.ftc.gov/opa/2009/06/csl.shtm>.

FTC Challenges Outpatient Clinic Acquisition Consummated in August 2008

By Katherine A. Ambrogi

Continuing its policy of challenging consummated acquisitions, including transactions that fall below the Hart-Scott-Rodino (“HSR”) reporting threshold, the Federal Trade Commission (“FTC”) issued an administrative complaint on July 23, 2009, challenging Carilion Clinic’s (“Carilion”) August 2008 acquisition of two outpatient clinics in Southwestern Virginia – the Center for Advanced Imaging (“CAI”) and the Center for Surgical Excellence (“CSE”).¹

Virginia-based outpatient services provider Carilion purchased outpatient clinics CAI and CSE, both owned by Odyssey IV, LLC, in August 2008 for approximately \$20 million, and therefore it was not likely subject to HSR filing with the FTC or U.S. Department of Justice (“DOJ”).

Carilion issued a statement to a Roanoke newspaper stating that it is currently reviewing the FTC’s charges, and is “concerned that the complaint appears to be based on inaccurate information ... [T]here have been no changes in the center’s prices since their purchase last year, and no changes are planned.”²

An evidentiary hearing before an administrative law judge is scheduled for March 24, 2010.

The FTC’s Complaint

According to the complaint, the transaction reduced competition in the markets for advanced outpatient imaging services and outpatient surgical services, and will result in higher prices and reduced non-price competition for services. Although it is not alleged that Carilion actually imposed anticompetitive price

increases, the complaint charges that these increases will occur once Carilion implements its fee structure at the purchased clinics. In particular, the complaint states that out-of-pocket price to many patients for a brain MRI may go from \$40 to \$350, an increase of approximately 900 percent.³

Before acquiring CAI and CSE, Carilion provided outpatient imaging services at three locations, and offered outpatient surgical services at four locations, in the Roanoke area, including a joint venture with physicians.⁴ In addition, Carilion is characterized as “the dominant

The federal antitrust agencies show continued willingness to challenge even consummated, non-reportable deals

hospital system in Southwest Virginia,” with about 80 percent of hospital beds in the Roanoke, Virginia area.⁵

The complaint states that the relevant geographic market in which to analyze the transaction is “the Roanoke area,” which encompasses the Counties and Cities of Roanoke and Salem, Virginia, that extend approximately 15 to 20 miles around the two cities. The complaint alleges that few patients who live in the Roanoke area travel outside its borders to seek outpatient clinical services, and generally expect to access these services within 30 minutes of their homes.⁶ Before the acquisition, CAI and CSE allegedly were the only independent, or non-hospital affil-

iated, providers of advanced outpatient imaging and surgical services in the Roanoke area.⁷

Alleged Effects of the Transaction

According to the complaint, the transaction will result in both unilateral and coordinated anticompetitive effects, and creates a duopoly in outpatient imaging and surgical services in the Roanoke area. The only remaining competitor for these clinical outpatient services is claimed to be HCA Lewis-Gale (“HCA”).⁸

According to the complaint, competition from CAI and CSE had prompted Carilion to reduce its prices and improve services. Post acquisition, however, health plans cannot exclude these clinics from their networks, which in turn increases Carilion’s leverage with the plans. Furthermore, HCA has little reason to continue to compete aggressively against the lone remaining imaging and surgical services provider,⁹ the FTC says.

Finally, the complaint contends that entry is unlikely to occur in a manner that deters any anticompetitive effects stemming from the transaction. Any imaging or surgical outpatient clinic must be certified under the Virginia COPN Program before it can operate, a process that can take up to two years. Carilion and HCA allegedly also routinely oppose COPN applications from new clinics, which adds to the time frame required to enter.¹⁰

Relief Requested

In its complaint, the FTC asks that the administrative law judge require

Carilion to divest CAI and CSE in a way that restores the outpatient centers as viable, independent competitors. It calls for Carilion to divest certain physician practices that were sources of referral support to CAI or potentially participating surgeons for CSE. The proposed relief would also prohibit any future transaction between Carilion, CAI, and CSE that combines any assets or facilities in the Roanoke area, absent FTC approval.

Implications

This FTC action presents several important implications in federal antitrust enforcement:

- The federal antitrust agencies show continued willingness to challenge even consummated, non-reportable deals. For example, in December 2008, the DOJ sued to unwind Microsemi Corporation's purchase of certain assets belonging to Semicoa Inc., a consummated deal in the semiconductor industry valued at only \$25 million.¹¹
- In other FTC challenges to closed transactions, such as *FTC v. Ovation Pharmaceuticals* and *In re Evanston Northwestern Health Corp.*, the complaints contained allegations that the acquiring party actually raised prices above the competitive level. No such allegation is present in the *Carilion* complaint. However, given a *Wall Street Journal* article questioning Carilion's pricing power published around the same time of the clinic purchases, it is unclear when the FTC became aware of or began its investigation into the transaction.¹²
- Unlike other challenges to consummated transactions where the FTC sought not only divestiture but also disgorgement of profits, such as *FTC v. Ovation*, that relief is not sought in the *Carilion* complaint. Presumably, because the FTC has not alleged any actual anticompetitive price increases in this case, disgorgement is not an option at this time. However, the complaint leaves open the potential for the Commission to order "any other relief" that may be appropriate.
- The FTC will not overlook transactions that involve relatively few facilities or that affect a relatively small geographic area.
- Here, Carilion purchased two outpatient services clinics and the alleged geographic market includes just two counties and cities in Southwestern Virginia. Similarly, the FTC challenged Inova Health System Foundation's

purchase of Prince William Health System, consisting of one hospital, in 2008 and defined the relevant market as "Northern Virginia." The proposed market in *Inova* encompassed four counties and five cities in the state of Virginia, and did not include the nearby state of Maryland or the District of Columbia.¹³

- Obviously, the FTC's action underscores its continued enforcement focus on the health care industry.

1 Complaint, In the Matter of Carilion Clinic, No. 9338 (F.T.C. July 23, 2009), at <http://www.ftc.gov/os/adjpro/d9338/090724carilioncmpt.pdf>.

2 Sarah Bruyn Jones, "Carilion Target of FTC Antitrust Complaint", *The Roanoke Times*, July 25, 2009, at <http://www.roanoke.com/news/roanoke/wb/213045>.

3 Complaint at 7.

4 *Id.* at 2-3.

5 *Id.* at 2.

6 *Id.* at 4-5.

7 *Id.* at 1.

8 *Id.* at 7.

9 *Id.*

10 *Id.*

11 See Verified Complaint, *U.S. v. Microsemi*, No. 1:08-cv-1311 (E.D. Va. Dec. 18, 2008), at <http://www.usdoj.gov/atr/cases/f240500/240537.htm>.

12 John Carreyrou, "Nonprofit Hospitals Flex Pricing Power," *The Wall Street Journal*, Aug. 28, 2008.

13 Complaint at 9, *FTC and Commonwealth of Va.*, No. 1:08-cv-460 (E.D. Va. May 12, 2008), at <http://www.ftc.gov/os/caselist/0610166/080513complaint.pdf>.

International Antitrust Update

European Antitrust Developments

By Clementine Baldon, Caroline Genevois, and Amandine Jacquemot

European Commission Imposes Record Fine on Intel for Abuse of Dominance

On May 13, 2009, the European Commission (the "Commission") imposed a fine of €1.06 billion, the largest individual fine in EU antitrust history to date, on Intel for abuse of its alleged dominant position in the market for x86 central processing units (CPU), a type of microprocessor constituting the core component of personal computers (PCs). (Intel had a market share in excess of 70 percent). This decision followed a nine-year investigation in the wake of complaints lodged by AMD – Intel's only competitor in the CPU market – and a series of "dawn-raids" across Intel's European premises.

Although the decision has yet to be published, it follows from the Commission's public statements¹ that it believed Intel breached Article 82 of the EC Treaty (which prohibits abuses of a dominant position) in two ways: (i) by offering conditional rebates to several PC manufacturers (Acer, Dell, HP, Lenovo and NEC) and to one retailer (Media Saturn Holding), and (ii) by awarding PC manufacturers payments on condition that they postpone or cancel the launch of products containing AMD's CPUs ("pay-for-delay"), and/or placed restrictions on the sales channels available to these products.

As regards the conditional rebates, the Commission concluded that Intel's rebate scheme amounted to an abuse, contending that:

- Intel pursued a strategy aimed at preserving its market share and excluding AMD;
- Intel's rebates were conditioned upon major PC manufacturers purchasing 80 percent or more of their CPU needs from Intel;
- Intel was an unavoidable trading partner for a great part of PC manufacturers' CPU needs; and
- for the limited part of their needs that was open to competition, PC manufacturers still had strong incentives to purchase from Intel in order not to lose their rebates on their total Intel purchases. As a consequence, Intel's competitors, even if as efficient as Intel, had to sell their CPUs below cost in order to match Intel's rebates.

As regards the so-called "pay-for-delay" breach, the Commission declared that Intel had interfered directly in the relationship between PC manufacturers and AMD by awarding the manufacturers payments on condition that they postpone or cancel the launch of AMD-based PCs, and/or impose restrictions on the distribution of such products. According to the Commission, such conduct had the potential effect of preventing competitive products from coming into the market for which there was a consumer demand. In adopting such conduct, Intel allegedly failed to exercise competition on the merits so that it rendered itself liable for an abuse of dominance.

Even though this filing signals the end of the Commission's investi-

gation, Intel's decision to appeal the matter ensures that this case is far from resolved. Moreover, Intel is facing the prospect of similar or other charges by the U.S. Federal Trade Commission, which opened a formal investigation in June 2008 in an Obama Administration reportedly keen on increasing antitrust enforcement.

European Commission Adopts Final Report in Its Competition Inquiry into Pharmaceutical Sector

On July 8, 2009, the European Commission published its final report concerning its inquiry into the pharmaceuticals sector in the European Union (the "Final Report"). As reported in the WGM Antitrust Update Winter 2009 issue, the Commission announced on January 16, 2008, that it had launched an inquiry into the pharmaceutical sector under Article 17 of Regulation 1/2003. The Commission decided to do so because of concerns that competition may have been restricted or distorted in the pharmaceutical sector in Europe with regard to innovative and generic drug products. The Commission published its preliminary findings on November 28, 2008, and invited comments by January 31, 2009.

The Final Report confirms the Commission's provisional findings that the market at issue is not functioning as well as it could. According to the Commission, this is due in particular to delays in the entry of generic drugs into the market when, as revealed by the inquiry,

Member State citizens waited on average more than seven months after patent expiration for cheaper generic drugs to enter. The Commission contends that generic drugs are on average 40 percent cheaper two years after market entry compared to the price of originator drugs. As first set out in the Commission's preliminary report, the inquiry showed to the Commission that originator companies used a variety of practices to extend the commercial life of their products without generic entry as long as possible. The inquiry also noted a decline of new drug products reaching the market, and pointed to certain originator company practices that might have contributed to this phenomenon.

Consequently, the Commission intends to intensify its scrutiny of the pharmaceutical sector under Articles 81 and 82 of the EC Treaty, and particularly of the specific conduct by originator companies the Commission believes are intended to delay generic entry. The Commission declared it will carry out further focused monitoring of industry settlements that limit or delay the market entry of generic drugs.

While the Commission declared that brand name manufacturer practices were among the causes of the delay in generic entry and the decline in new drug products, the Commission recognized in the Final Report that such problems also were caused by shortcomings in the regulatory framework. Therefore, it urged the adoption of a Community patent and a unified specialized patent litigation system in Europe in order to reduce administrative burdens and uncertainties for pharmaceutical companies. The Member States also were encouraged to deliver speedy generic uptake and to improve price competition. To that end, the Final

Report made a number of comments and recommendations in relation to streamlining the marketing authorization process and improving pricing and reimbursement systems in the pharmaceutical industry.

Record Fine Imposed By the Belgian Competition Council In Price-Squeeze Case In The Telecommunications Sector

Only a matter of months after the *linkLine* judgment – an unsuccessful price-squeeze action brought before the U.S. Supreme Court² – the Belgian Competition Council found that the Belgian mobile operator Proximus had engaged in an illegal margin-squeeze by charging end users prices lower than the wholesale prices it charged competitors for access to its cellular network.³ This divergent outcome, reached on a similar issue, reflects significant differences between the European and US approach to price squeeze practices by dominant companies.

Proximus is the mobile phone subsidiary of Belgacom, the incumbent state telecommunications monopoly in Belgium. The decision at issue stems from a 2005 complaint by rival mobile operator Base – owned by the Dutch incumbent KPN – alleging that Proximus was responsible for several exclusionary practices in the market for mobile telephone services – in particular in the segment for business customers. Mobile termination rates were at the heart of the Council's investigation. Base argued that the wholesale prices charged to competitors to use the Proximus network, known as mobile termination rates (*i.e.*, for terminating a call from their network on the Proximus network) were higher than the prices that Proximus charged to end-users for on-net communications (*i.e.*, between two customers on its own network).

In its decision of 26 May 2009, the Belgian Competition Council confirmed that in 2004 and 2005 the margin between Proximus's-net prices and the termination rates it charged to its competitors was clearly negative. According to the Council, competitors were thus unable to offer prices to their clients for communications towards the Proximus network that were competitive with the prices that Proximus could offer to its clients.

Based on this argument, Proximus was held responsible for abusing its dominant position under Belgian and European competition rules (Article 82 of the EC Treaty) and was fined €66.3 million – the largest fine ever levied by the Belgian Competition Authority. When calculating the fine, account was taken of the nature of the infringement, Proximus's market share, the economical impact of the infringement, and the fact that liberalization was a priority in the telecommunications sector. Belgacom has announced that it will appeal the decision.

Mobile operators in Europe have over recent years faced a series of caps on termination rates and roaming charges. As a practical matter, the *Proximus* decision reaffirms that margin squeezing can, in its own right, constitute an abuse of a dominant position under article 82 of the EC Treaty. In that regard, this decision echoes the recent *Telefonica* decision,⁴ in which the European Commission expressly recognized that Article 82 of the EC Treaty applies to margin squeezing, even absent an antitrust duty to deal.⁵

This position is in stark contrast with the US approach to price-squeeze cases, and in particular with the US Supreme Court's recent *linkLine* decision. In that case, although the conduct at issue was similar to that alleged in *Proximus*, the Supreme

Court held that an Internet provider had not violated the antitrust laws by selling wholesale level access to its network at or above its retail prices. In a nutshell, the Supreme Court ruled that, as an independent pricing claim, a price-squeeze cannot constitute a valid antitrust claim absent an antitrust duty to deal or retail sales below cost. Under US antitrust laws, therefore, a dominant firm can avoid liability for price-squeezing if the wholesale and retail prices are both independently lawful. This decision reflects the Supreme Court's aversion to chilling innovation and price competition through its case law, particularly when such issues have been or can be considered under sector-specific regulation.

As mentioned above, this is not the position adopted by the European Commission in its *Telefonica* decision. Nonetheless, other European decisions can be interpreted as being reconcilable with *linkLine*. For instance, in *Deutsche Telekom*, the European Court of First Instance ("CFI") addressed the

margin-squeeze issue as an independent abuse, but took into account the absence of alternative infrastructure that would have provided competitors with a viable means of entry into the market for retail access to telecommunications services.⁶ Similarly, the French Supreme Court recently held that, for a margin squeeze to fall afoul of its antitrust law, it must first be demonstrated that the input at issue was "necessary," strongly suggesting that the conditions required by the case law on refusals to deal should be fulfilled.⁷

In this context, much anticipated clarification is awaited in particular from the CFI's judgment in *Telefonica* on appeal. In the meantime, the absence of a clear and uniform line of case law within the EU leads to an undesirable and confusing legal environment for dominant companies, rendering it more difficult for them to adopt pricing policies believed to be in line with European antitrust constraints.

- 1 See Commission's Press Release IP/09/745, May 13, 2009, *Antitrust: Commission imposes fine of €1.06 bn on Intel for abuse of dominant position; orders Intel to cease illegal practices*, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/09/745&format=HTML&aged=0&language=EN>. See also Commission's Memo MEMO/09/235, May 13, 2009, *Antitrust: Commission imposes fine of €1.06 bn on Intel for abuse of dominant position; orders Intel to cease illegal practices – questions and answers*, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/09/235&format=HTML&aged=0&language=EN&guiLanguage=en> and N. Kroes' speech, SPEECH/09/241, May 13, 2009, *European Commissioner for Competition Policy Commission takes antitrust action against Intel – Introductory remarks at press conference available at* <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/09/241&format=HTML&aged=0&language=EN&guiLanguage=en>
- 2 U.S. Supreme Court's decision of 25 February 2009, *Pacific Bell Telephone Co. D/B/A AR&T California v. linkLine Communications, Inc. et al.* ("linkLine"). See "The linkLine Decision: Section 2 Gets Squeezed Further", *Antitrust Update*, Spring 2009.
- 3 Decision of the Belgian Competition Council n° 2009-P/K-10 of 26 May 2009.
- 4 Commission decision of 4 July 2007, Case COMP/38.784, *Wanadoo Espana v. Telefonica* ("Telefonica").
- 5 *Telefonica*, ¶ 309.
- 6 Decision of the CFI of 10 April 2008, T-271/03, *Deutsche Telekom AG* ("Deutsche Telekom"), ¶236.
- 7 Decision of the French Supreme Court of 3 March 2009, *France Telecom/ SFR Cegetel/ Bouygues*.

Antitrust Update

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