RECENT ANTITRUST DEVELOPMENTS INVOLVING PRICING AND DISTRIBUTION ISSUES

Practical Advice to Minimize Antitrust Risk

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Introduction

• Today we are going to discuss recent developments involving pricing and distribution issues that arise in the ordinary course of business, each of which could trigger antitrust scrutiny.
  • Most Favored Nation Clauses ("MFNs")
  • Resale Price Maintenance ("RPM")
  • Exclusive Dealing
• Our focus will be on ways to assess and minimize the litigation risk associated with such practices.
Federal & State Antitrust Laws

• Our discussion centers primarily on litigation and enforcement actions under federal law:
  • Sherman Act
  • Clayton Act
  • FTC Act
• We will also discuss state laws, particularly where treatment of an issue under state law may differ from how the issue is treated under federal law.
MFNs – Overview

- An MFN is a commitment by a seller to treat a buyer as well as the seller treats its best (i.e., “most favored”) customers.
  - Usually MFNs appear in a contract between the seller and buyer; MFNs may also be a unilateral policy of the seller.
- MFNs often involve pricing; they may involve other contract terms (e.g., payment terms or access to supply).
  - As-good-as or better-than pricing/terms.
MFNs – Recent Litigation

  - Apple introduced a new agency model in its distribution agreements with e-book publishers and included MFN provisions in the agreements in an effort to avoid a price war with Amazon. Those MFNs ensured that e-books offered by the iBookstore would be sold for the lowest price available from any other e-retailer.
  - This new model prompted publishers to renegotiate with Amazon, effectively requiring Amazon to switch to the agency model employed by Apple.
MFNs – Recent Litigation

• United States v. Blue Cross Blue Shield of Mich.
  • DOJ alleged that MFN and MFN-plus provisions in BCBS contracts with hospitals would raise BCBS’s rivals’ costs, would deter entry, and would lead to higher prices for hospital services in Michigan.
    • DOJ argued that hospitals would seek a portion of the profit that BCBS was reaping because of the competitive advantage it enjoyed under the MFN provisions.
  • Parties filed stipulated dismissal without prejudice after Michigan enacted laws banning use of MFNs by insurers, HMOs, and nonprofit healthcare corporations.
MFNs – Antitrust Analysis

- Courts analyze MFNs under the rule of reason whereby pro-competitive benefits are weighed against the potential for competitive harm.
- Potential antitrust concerns:
  - The main concern is that MFNs may be used by a dominant firm to exclude competition.
  - Another concern is that MFNs may be used to facilitate tacit or express collusion: widespread use of MFNs in a concentrated industry diminishes the likelihood that sellers will cheat on a collusive arrangement.
MFNs – Guidance

• Is the MFN a result of vertical arrangement, or horizontal agreement (*i.e.*, did each seller act independently or unilaterally)?

• Are MFNs ubiquitous?
  • If some sellers don’t engage in MFNs, they may undermine a collusive scheme.

• Is the market highly concentrated; do any of the parties have market power?
  • An MFN can’t lessen competition unless it affects prices of products in markets in which buyers or sellers either individually or collectively have market power.
MFNs – Guidance

- **Less risk** when MFNs are:
  - Received by small buyers.
  - Provided by small seller that lacks market power.
  - Offered in a product/service market that is not concentrated.
  - Provided in exchange for significant investment (especially by an initial customer or technology sponsor).
  - Provided as part of a settlement of one of several lawsuits brought against the seller.
MFNs – Guidance

**More risk** when MFNs are:
- Provided by a large seller with market power or to large buyers.
- Applicable to a highly significant input into the end product.
- Presented as MFN-plus.
- Received by a large buyer and agreed to:
  - in response to entry of a low cost and/or innovative new seller.
  - in exchange for exclusive dealing agreement with large seller.
- Received by the largest buyer, and the buyer’s rationale is that the buyer deserves the lowest price.
RPM – Overview

- RPM involves agreements between parties at different levels in the supply chain and governing the resale price of a product or service.
  - RPM agreements often set a price floor – minimum RPM, or a price ceiling – maximum RPM.
RPM – Recent Litigation

  • New York AG sued mattress manufacturer alleging that provisions relating to discounts in its distribution agreements violated the state’s antitrust law.
  • Appellate court ruled in favor of defendant, finding that the challenged provisions were not illegal, they were unenforceable.
**RPM – Antitrust Analysis**

- Maximum RPM has been treated under the rule-of-reason analysis for several years.
- Prior to the U.S. Supreme Court’s 2007 decision in *Leegin*, minimum RPM had been treated under federal antitrust laws as per-se unlawful for almost one-hundred years, since the Court’s 1911 decision in *Dr. Miles*.
  - The Court in *Leegin* – after determining that minimum RPM may have procompetitive and anticompetitive effects – overruled *Dr. Miles* and held that minimum RPM should be treated under the rule of reason.
  - A plaintiff challenging a minimum RPM program now bears the burden of proving – based on a review of relevant market facts – that the program’s likely anticompetitive effects outweigh its likely procompetitive benefits.
RPM – Antitrust Analysis

- Most state laws contain provisions either requiring or encouraging courts to be guided by federal case law in their interpretations of counterpart state provisions
  - **BUT**, there remains support for retaining per se illegality among various state AGs.
- Treatment of RPM in some states may differ from treatment under federal laws, notably:
  - California
  - Kansas
  - Maryland
  - New York
• “Suggesting” minimum resale prices has long been generally O.K.

• Minimum Advertised Price (“MAP”) programs restricting use of manufacturer-supplied advertising funds to ads featuring the manufacturer’s products at (or above) suggested prices has long been O.K.

• Notice to resellers of the manufacturer’s “unilateral” policy not to deal with resellers that sell at prices below the MSRP (under the Colgate doctrine) has long been lawful in theory but still problematic, particularly in states applying a per se RPM rule.
RPM – Guidance

• Does impetus come from retailers or the manufacturer?
  • From retailers may suggest facilitation of a retailers’ cartel.
  • From manufacturer is consistent with potential “procompetitive” justification.

• Evidence of reasons for and effects of use.
  • If the justification is to incent resellers’ investment in pre-sale service or promotional support, has that investment actually occurred after implementation?
  • Can the manufacturer demonstrate some appreciable consumer benefit outweighing, or at least compensating for, adverse price effect?

• Dual distribution with resulting downstream competition between the manufacturer and its resellers.
  • Could allow claim of horizontal price-fixing, which is illegal *per se*.
  • Extent of actual downstream competition may be relevant.
Exclusive Dealing – Overview

• A supplier prohibits a distributor or dealer from selling or marketing other suppliers’ products or services.
  • In the case of de facto or partial exclusive dealing, a supplier provides incentives to a distributor or dealer so that the distributor/dealer focuses its sales efforts on the supplier’s products.
Exclusive Dealing – Recent Litigation

  - Exclusivity policy imposed by a dominant manufacturer of artificial teeth monopoly on its dealers violated Section 2 of the Sherman Act.
  - The Court expressly noted that, among other things, the exclusivity policy at issue was "imposed by a manufacturer on its dealers," 399 F.3d at 184.
  - Antitrust claims by downstream dental laboratories against both Dentsply and dealers dismissed.
  - The court found that the “rim” (a dealer agreement) was missing from the alleged “hub and spoke” conspiracy.
Exclusive Dealing – Recent Litigation

  • Court upheld jury verdict that found Eaton in violation of the Clayton Act and Sherman Act.
  • ZF Meritor’s allegations focused largely on Eaton’s exclusive dealing provisions – including a loyalty discount program – in its long-term agreements with each of the nation’s four direct purchasers of heavy-duty truck transmissions.
  • Long-term agreements, which conditioned rebates on the purchase of a specified percentage of each direct purchaser’s requirements, were evaluated under the rule of reason, rather than under the Brooke Group predatory pricing test.
Exclusive Dealing – Guidance

- **Less risk** when exclusive dealing is:
  - Imposed by a supplier with little or no market power.
  - Not subject to a long-term contractual commitment.
  - There are few barriers to entry in the market.
- Ways to **reduce risk further** once antitrust litigation begins:
  - Evaluate the availability of insurance coverage.
  - Consider the practicality of joint representation among co-defendants, for some or all of the litigation activity.
  - Assess possible indemnity from upstream supplier, in case of alleged vertical conspiracies.
  - Judgment sharing agreements.
Practical Considerations

- Educate and engage your client.
  - What are business people looking to do?
  - What is the reason for the requested approach?
- Know your market(s).
  - What products or services are involved?
  - What is your market share?
  - What is your customer’s market share?
- Know your potential adversaries.
  - Who is the pricing/distribution policy likely to impact?
  - How litigious are those who might be adversely impacted?