Report from North America

Editor: Christopher Pleatsikas

UPDATE ON ANTITRUST ENFORCEMENT IN THE UNITED STATES

In a recent issue of *The Economist*, the lead editorial and the lead article set forth the view that competition had declined in recent years in the United States in many of the major industries.[1] According to statistics cited in *The Economist*, returns on equity in the United States for American firms were 40% higher than returns on equity for operations outside the United States, and return on capital had increased significantly since the turn of the century. As one example of the current competitive situation, *The Economist* noted that the airline industry, after a wave of consolidation that had left just four major airlines serving the domestic market, made more money in 2015 than Alphabet, widely perceived as one of the most profitable firms in the world. Moreover, as fuel prices, one of their major costs, declined rapidly in 2015, airline ticket prices remained high, enabling the airlines to reap record profits.

Industry consolidation in the United States has proceeded in several waves over the past century, but many analysts view the current wave as one of the most powerful. *The Economist* noted that industry concentration is much higher today than 20 years ago. In addition, consolidation in the financial sector and in holdings by large investment firms means that relatively few investment firms hold significant ownership stakes in all or most of the major competitors in many industries. This has prompted concerns that common ownership of significant stakes across an industry by relatively few investors may influence the managements of these competitors to mute their competitive responses. While this theory is still controversial among many regulators and antitrust economists, it has gained some adherents and points to an additional possible threat to competition.

More broadly, *The Economist* contended that industry consolidation, profit increases and lower competitive activity in the economy could serve to exacerbate socioeconomic inequality and dampen demand. These developments, in turn, would reduce gross national product growth.

Against this backdrop, the "Report from North America" shifts its focus in this issue from a review of important antitrust cases in the United States to a broader review of antitrust developments in the United States. Reviews of an important legislative development, regulator performance, and regulator policy pronouncements on intellectual property (IP) and internet access concerns follow.

Legislative Development

The so-caller SMARTER Act (*Standard Merger and Acquisition Rules Through Equal Rules Act*) was introduced in the House of Representatives of Congress in 2015.[2] In March 2016, the House of Representatives passed the Bill by essentially a party-line vote, sending it to the Senate for further action.[3] The Bill was passed as proposed, without being amended.

Under the relevant antitrust Acts in the United States,[4] two agencies, the Department of Justice (DOJ) and the Federal Trade Commission (FTC), have responsibility for reviewing and assessing the competitive effects of mergers. Under the authority granted by the *Clayton Act*, the agencies seek to ensure that mergers do not substantially lessen competition and/or create a monopoly.[5] While there is no formal division between the two agencies as to which industries each has responsibility for reviewing and there is some overlap, the DOJ and the FTC tend to assign merger reviews based on

[1] "The Problem With Profits" and "Too Much of a Good Thing", *The Economist*, 26 March 2016.

[2] The Act was introduced as Bill HR (for House of Representatives) 2475, sponsored by Representative Blake, a Republican from Texas.

[3] The vote was 235-171, with 230 Republicans and 5 Democrats voting for the Bill and 170 Democrats and 1 Republican voting against.

[4] The *Sherman Act of 1890* and the *Federal Trade Commission Act of 1914*.

[5] See *Clayton Act of 1914* § 7.

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their respective areas of expertise. Consequently, as examples, the DOJ tends to investigate mergers in the financial services, telecommunications[6] and agricultural industries, while the FTC typically reviews mergers in the defence, pharmaceutical and retail industries.[7]

There is an important legal procedural difference that has evolved over the years in the manner by which the agencies approach proposed mergers that they have decided to oppose (a very small minority of merger proposals as detailed in subsequent discussion below). When DOJ or the FTC concludes that a proposed transaction would violate § 7 of the *Clayton Act*, the agencies pursue an injunction against the transaction in Federal Court. If the Court grants the injunction, the merger parties usually abandon the transaction, although, in a few cases, the merger parties pursue further action in the courts.

The issues the SMARTER Act addresses are the important differences in the standards applied and the manner by which the two agencies approach the injunction process:

- The standard applied by the courts for a preliminary injunction sought by the FTC is set forth in § 13(b) of the *Federal Trade Commission Act* (FTC Act), which requires "a proper showing that, weighing the equities and considering the Commission's likelihood of ultimate success, such action would be in the public interest, and after notice to the defendant, a temporary restraining order or a preliminary injunction may be granted without bond". The DOJ seeks injunctions under a different standard, under § 15 of the *Clayton Act*, which does not set forth a specific standard for courts to apply in order to determine whether to grant injunctive relief. Instead, the DOJ must satisfy the requirement that there be "a reasonable likelihood of success on the merits" with "the balance of equities" favouring the DOJ.[8] While there are differences in views among economists and regulators on the subject, some believe that these different standards result in different treatment by the courts of injunctions sought by DOJ as compared with injunctions sought by the FTC.[9]
- There are differences as well in the character and procedure of the injunctive process practised by the two agencies in merger cases. In most cases, the DOJ, in agreement with the merger parties, combines proceedings for a preliminary and permanent injunction. The FTC generally only seeks a preliminary injunction, although it has the same authority as the DOJ to seek both a preliminary and permanent injunction. By seeking only a preliminary injunction, the FTC preserves its ability to continue to review the merger in parallel administrative proceedings, even if its preliminary injunction request is denied. While administrative proceedings cannot be used to prevent consummation of the transaction, they introduce more uncertainty into the process because an adverse (to the merger parties) decision in administrative proceedings could cause the transaction to be abandoned.

The Antitrust Modernization Commission (AMC) was a bi-partisan commission established in 2003 under the *Antitrust Modernization Act*.[10] Its brief was to undertake "comprehensive review of US antitrust law to determine whether it should be modernized".[11] Among its recommendations (published in 2007) were:

- The FTC should adopt a policy that, when it seeks injunctive relief in *Hart-Scott-Rodino Act* (HSR Act)[12] merger cases in Federal Court, it will seek both preliminary and permanent

[6] The DOJ shares responsibility for reviewing telecommunications mergers with the Federal Communications Commission (FCC).

[7] For example, see House of Representatives Judiciary Committee (United States), *Standard Merger and Acquisition Review Through Equal Rules Act of 2015*, Report No 114-449 (2016) fn 7.

[8] See, for example, *United States v Siemens Corp*, 621 F 2d 499, 505-506 (1980) (citations omitted).

[9] For example, see House of Representatives Judiciary Committee, n 7, 2-3, fn 7.

[10] *Antitrust Modernization Commission Act of 2002*, Pub L No 107-273, § 11054(h), 116 Stat 1856, 1857 (2002).

[11] Antitrust Modernization Commission, *Antitrust Modernization Commission: Report and Recommendations* (April 2007) i.

[12] The *Hart-Scott-Rodino Antitrust Improvements Act of 1976*, Pub L No 94-435, commonly referred to as the *Hart-Scott-Rodino Act* or the HSR Act, was signed into law by President Gerald Ford on 30 September 1976. The HSR Act provides that parties must not complete certain mergers, acquisitions or transfers of securities or assets until they have made a

injunctive relief, and will seek to consolidate those proceedings so long as it is able to reach agreement on an appropriate scheduling order with the merging parties.[13]

- Congress should amend § 13(b) of the FTC Act to prohibit the FTC from pursuing administrative litigation in HSR Act merger cases.[14]

Thus, the AMC recommended that the FTC adopt the DOJ policies for process, but was silent on the injunctive standard the FTC should use. Of course, following the AMC's recommendation in this matter leaves the question of the role of the FTC's administrative machinery in merger cases somewhat murky. While there was some dissension among the AMC's members concerning these recommendations, the dissension was not along party lines.[15]

The SMARTER Act proposes to adopt these recommendations. How the change has become one of political contention can best be understood in terms of two arguments. First, as noted above, there are some who believe that the standard for seeking injunctions used by the FTC is somewhat easier to satisfy. Secondly, many Democrats, particularly given the context of a presidential election year, are concerned that recent trends in merger activity have harmed competition and, by concentrating economic power in fewer hands, are a significant factor in the increasingly unequal distribution of income, wealth and power in the United States. The FTC, with its allegedly somewhat more easily satisfied injunction standard and with a backup ability to institute administrative proceedings (and, under a Democratic President, with a built in 3-2 Democratic majority of FTC Commissioners) is seen as a more valuable and reliable bulwark against too much concentration in economic power through mergers.

MERGER ENFORCEMENT

The latest comprehensive figures are from the 2014 HSR Annual Report, although some more recent information is available. The Annual Reports set forth the number of merger transactions reported to the DOJ and FTC.[16] The number of transactions increased about 25% in FY2014 (as compared with FY2013) to 1,663. For FY2015, the number of transactions reported increased again to more than 1,800.[17] Figures for both FY2014 and FY2015 were more than double the low point in the number of reportable transactions, which occurred in 2009, shortly after the nadir of the financial crisis, but were lower than the peak over the previous 10 years of 2,201 reportable transactions in 2007.

The proportion of reported transactions subject to a second request declined slightly in FY2014 to 3.2%. In other words, initial concerns about possible competitive effects were expressed by the agencies in only 3.2% of the transactions (53 transactions in FY2014). In FY2014, 33 transactions were challenged by the agencies (17 by the FTC and 16 by the DOJ). In most cases, the proposed transactions were modified by the parties (generally by divesting certain assets).

detailed filing with the FTC and DOJ and waited for those agencies to determine that the transaction will not adversely affect competition. All transactions above a threshold dollar amount are subject to scrutiny under the HSR Act (see n 16 for current dollar thresholds). In most cases, the FTC or the DOJ allow the merger to proceed without requesting additional information. However, in a small proportion of cases, one of the agencies requests additional information (a so-called HSR Second Request), triggering further analysis of the competitive implications of the proposed transaction.

[13] This is Recommendation 24: see Antitrust Modernization Commission, n 11, 131. Two Commissioners dissented from this recommendation.

[14] This is Recommendation 25: see Antitrust Modernization Commission, n 11, 131. Four Commissioners dissented from this recommendation.

[15] There were 12 members of the Antitrust Modernization Commission. Under the legislation that established the Commission, it was to be comprised of six Democrats and six Republicans.

[16] The HSR threshold for the minimum size of transaction to require reporting to the antitrust agencies was US$75.9 million in 2014, US$76.3 million in 2015 and US$78.2 million in 2016.

[17] Statement of Bill Baer, Assistant Attorney General, Antitrust Division, to the Subcommittee on Antitrust, Competition Policy and Consumer Rights, Committee on the Judiciary United States Senate, at its hearing "Oversight of the Enforcement of the Antitrust Laws" on 9 March 2016, 5 (Bill Baer Statement) <https://www.justice.gov/opa/file/831686/download>.

As noted above, merger activity increased in 2015 and the number of challenges at the DOJ increased as well,[18] including challenges to several high-profile mergers. For example:

- Time Warner/Comcast: The DOJ (and the FCC) opposed the merger of Time Warner and Comcast, two of the largest providers of pay television services, based in large part on concerns that the combination would become a "gate-keeper" internet services provider for a very large percentage of consumers. As a result of agency opposition, the proposed merger was abandoned in April 2015.
- Sysco/US Foods: The FTC, along with several State Attorneys General, opposed this merger on the grounds that the combined company would supply 75% of the market for "broadline food-service distributors" to large national customers. Sysco and US Foods attempted to resolve these concerns by proposing to sell several distributors to a competitor, but a Federal Court found the remedy insufficient to allay competition concerns, and the transaction was abandoned.
- General Electric/Electrolux: This merger was opposed on the grounds that the resulting combination would control a large share of sales of certain white goods (large kitchen appliances) to "contract-channel purchasers" (eg builders and large-scale building managers). The DOJ rejected settlement offers from Electrolux and took the case to trial. After about a month into the trial, the transaction was abandoned. General Electric subsequently proposed to sell its relevant assets to Haier, a Chinese maker of white goods.
- Staples/Office Depot: These companies tried to merge 18 years ago, but the merger was opposed by the FTC and abandoned at that time. The merger has been proposed anew and is again opposed by the FTC on the grounds that the combined companies would reduce competition in the market for "the sale and distribution of consumable office supplies to large business-to-business customers in the United States". A Federal Court blocked the merger, and it was abandoned by the parties.

One theme that emerges from enforcement activities of the DOJ and the FTC in large mergers that they have opposed is that markets are being defined more narrowly and are more targeted to particular segments within an industry. This is consistent with the thrust of the most recent *Merger Guidelines*,[19] which has emphasised the need to examine the impact of mergers between close competitors.

Cartel Enforcement

Cartel enforcement continues to evolve and expand at DOJ. Total criminal fines collected increased almost seven-fold between 2011 and 2015, to more than US$3.6 billion.[20] The most prominent case in 2015 involved guilty pleas obtained against several major banks for the alleged conspiracy to rig foreign currency spot markets.

Over the past 30 years, there has been a shift in the DOJ's priorities in prosecuting alleged conspiracies. One manifestation of this shift has been an increased emphasis on prosecuting individuals, as opposed to corporations, as the agency has determined that prosecuting executives may be even more effective at deterring cartel activity than prosecuting firms. During the 1990s, roughly an equal number of firms and individuals were prosecuted (480 firms and 476 individuals), while in the 2000-2009 period more than twice as many individuals were prosecuted as firms (453 versus 220). In the most recent five-year period, this ratio has increased to almost three-to-one (352 individuals versus 123 corporations).[21]

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[18] Bill Baer Statement, n 17, 5.

[19] United States Department of Justice and the Federal Trade Commission, *Horizontal Merger Guidelines* (August 2010).

[20] The Antitrust Division of the DOJ has noted that antitrust enforcement is a "good value proposition", with about 50% of its funding offset by pre-merger HSR fees and criminal fines collected representing more than 10 times its annual direct appropriation. See Bill Baer Statement, n 17, 2.

[21] Brent Snyder, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, "Individual Accountability for Antitrust Crimes" (Paper prepared for the Yale School of Management Global Antitrust Enforcement Conference, New Haven, Connecticut, 19 February 2016) 4-5 <https://www.justice.gov/opa/file/826721/download>.

With the shift in emphasis to prosecuting individuals, two other shifts in prosecutorial trends have also occurred. The average prison sentence for convictions has increased more than three-fold, from 7.3 months during 1986-1995 to 23.9 months during 2006-2015.[22] Over the same timeframe, the number of foreign individuals living abroad sentenced to prison in the United States has increased from zero in 1986-1995 to 69 during 2006-2015.[23]

Standard Setting Efforts and Intellectual Property

Antitrust enforcement, particularly by the DOJ, has over the past few years become increasingly concerned with the impact of IP disputes relating to Standard Essential Patents (SEPs) incorporated into standards adopted by Standard Setting Organizations (SSOs), such as the standards for mobile telecommunications and Wi-Fi networks. SSOs have tried to reduce the frequency and character of these disputes by eliciting commitments from IP contributors to license their technology on FRAND/RAND (Fair and Reasonable and Non-Discriminatory / Reasonable and Non-Discriminatory) terms. While some economists view disputes as to what constitutes FRAND/RAND terms as essentially contract disputes, the DOJ has viewed attempts by IP contributors to seek injunctions against alleged infringers as exclusionary conduct that inherently invokes hold-up issues.[24] Therefore, the DOJ (along with other antitrust enforcement agencies in Europe) has enunciated the principle that injunctions are inappropriate in most instances for SEPs (instead requiring parties to engage in good faith negotiations before any injunction could be sought), particularly where monetary damages are available to SEP owners.

A further development in 2015 concerns DOJ's response to a request by the Institute of Electrical and Electronics Engineers, Incorporated (IEEE), for a business review letter from the Department of Justice pursuant to the Department's Business Review Procedure.[25] The business review letter was sought in reference to the DOJ's antitrust enforcement intentions with respect to a proposed update to the IEEE Standards Association's Patent Policy.[26] Several aspects of the proposed IEEE update are notable.

(1) The IEEE proposed to adopt a policy that prohibits a patent holder from seeking an injunction against an alleged infringer unless the alleged infringer fails to participate in or comply with an adjudication process when there is a dispute as to appropriate IP compensation.

(2) The IEEE Policy proposed to define a FRAND royalty as one that "exclud[es] the value, if any, resulting from the inclusion of [the patent claim's] technology in the IEEE standard".[27]

(3) The IEEE Policy proposed that consideration should be given to applying any FRAND royalty to the "smallest saleable Compliant Implementation that practices the Essential Patent Claim".[28]

(4) The proposed IEEE Policy "prohibits licensors from demanding licenses to applicants' patents that are not essential to the same standard as part of their licensing terms and from forcing an applicant to take a license to patent claims that are not essential to the referenced standard".[29]

These proposed changes significantly clarify IEEE Policy in relation to SEPs and the meaning of FRAND/RAND. Most significantly, the IEEE Policy appears somewhat more favourable to patent users than previous IEEE Policy (although, in many cases, firms are both SEP users and owners, so the situation is not so straightforward). While the DOJ recognised that not all participants in IEEE's

[22] Bill Baer Statement, n 17, 3.

[23] Bill Baer Statement, n 17, 4.

[24] For example, see United States Department of Justice and United States Patent and Trademark Office, *Policy Statement on Remedies for Standards-Essential Patents Subject to Voluntary F/Rand Commitments* (8 January 2013).

[25] 28 CFR § 50.6.

[26] Letter from Renata Hesse, Acting Assistant Attorney General, DOJ to Michael A Lindsay, Dorsey and Whitney, LLP, 2 February 2015 (Renata Hesse letter) <https://www.justice.gov/file/338591/download>.

[27] Renata Hesse letter, n 26, 11.

[28] Renata Hesse letter, n 26, 12.

[29] Renata Hesse letter, n 26, 15.

Policy revision process were in agreement with the proposal and that the proposed changes were more restrictive than DOJ's expressed views, the DOJ concluded that the proposed Policy Update was consistent with the principle that parties should negotiate patent licences voluntarily. Further the DOJ concluded:

> that the Update has the potential to benefit competition and consumers by facilitating licensing negotiations, mitigating hold up and royalty stacking, and promoting competition among technologies for inclusion in standards. The Department cannot conclude that the Update is likely to harm competition. Further, to the extent that there are any potential competitive harms, the Department concludes that the Update's potential procompetitive benefits likely outweigh those harms. Accordingly, the Department has no present intention to take antitrust enforcement action against the conduct.[30]

Internet Access and Video Competition

In recent years, antitrust enforcement in the United States has been concerned about the effect of mergers on the provision of internet services.[31] There is a view, explicitly articulated by the DOJ, that consolidation by providers of internet services may increase the potential for bottlenecks in the provision of broadband services, reducing innovation, particularly in relation to video services. This was one major reason why the DOJ (along with the FCC) opposed the acquisition of T-Mobile by AT&T (the other major reasons being a concern that a reduction in competitors from four to three would significantly reduce competition in the provision of mobile telecommunications services and a concern that T-Mobile was a maverick in the sense of being an innovator in the introduction of new and lower priced service plans). More recently, the proposed combination of Sprint and T-Mobile (the third and fourth largest providers of mobile telecommunications services) was opposed by the DOJ and the FCC for similar reasons and was abandoned by the parties. It is clear that further consolidation in the industry, absent significant de novo entry, is not likely to win the approval of antitrust regulators.

Similar concerns about the potential for bottlenecks in internet and video services provision led the DOJ to oppose the now-abandoned Comcast/Time Warner proposed merger in the cable television industry, even though, unlike in the mobile telecommunications industry, Comcast and Time Warner did not serve the same customer bases in the provision of basic cable and internet delivery services (each having separate geographic footprints for service). The combined company would have controlled access to nearly 60% of high-speed cable households in the United States. The DOJ was concerned that such concentration could lead to Comcast becoming a "gatekeeper", enabling it to exert significant control over video content providers, including rivals such as Netflix and Hulu (and emerging rivals, such as HBO and the free-to-air commercial broadcast networks, which now offer subscriptions to content without the need to subscribe to a local cable television provider) to the detriment of video content competition.

The concern about the future of innovation in video and informational services at the DOJ (and the FCC) manifests long-term concerns that have become critically important in competition analysis. They are an important example of the need to view competition issues through a lens that places increasing emphasis on the need to preserve opportunities for firms, including entrants, to engage in dynamic competition by introducing and promoting new and transformational products and services.

Christopher Pleatsikas
Managing Director, Berkeley Research Group California

[30] See Renata Hesse Letter, n 26, 16.

[31] See also Bill Baer, Assistant Attorney General Antitrust Division US Department of Justice, "Video Competition: Opportunities and Challenges" (Paper presented at the Duke Law Center for Innovation Policy Fall Conference on The Future of Video Competition and Regulation, 9 October 2015) <https://www.justice.gov/opa/file/782401/download>.