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U.S. Developments

3D Printing and Tied Ink: The Federal Circuit Upholds Tying Arrangement

By John J. Elliott and Irving Scher - New York, NY

On April 18, 2014, the Federal Circuit ruled that a restriction that required purchasers of one company's printer to use approved resin – the "ink" – in the high-end physical-object printing market (colloquially known as "3D-printing") was not an actionable tying arrangement. *DSM Desotech Inc. v. 3D Systems Corp.*, No. 2013-1298.[1]

The lawsuit was brought by DSM Desotech (Desotech), which manufactures resin used by stereolithography (SL) printing machines. Desotech accused 3D Systems, a manufacturer of SL machines and of SL resin, of improperly preventing its customers from using Desotech's resin.[2] The court affirmed the District Court's finding that Desotech could not ultimately prove that 3-D Systems' printing machines constituted a product market separate from the overall SL printing machine market. It also rejected Desotech's argument that 3D Systems' customers were improperly "locked-in" to purchasing approved resin products for as long as they used their printers, declaring that customers' awareness of 3D Systems' aftermarket requirements precluded such an argument.

Background

A tying arrangement occurs when a seller conditions the sale of a product or service (the "tying" product) to the purchase of a

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separate product or service (the "tied" product). Tying arrangements imposed by suppliers with market power have been considered per se unlawful for more than 50 years.[3] To establish a per se unlawful tying arrangement, a plaintiff must show, *inter alia*, 1) that the tying product and tied product are, in fact, two separate and distinct products; 2) that the seller conditioned its sale of the tying product on the buyer's purchase of the tied product; 3) that the seller possesses sufficient economic power in the tying product to restrain competition in the tied product; and 4) that competition in the tied product is adversely affected by the tying arrangement.[4]

The third factor, market power, is a threshold issue common to most antitrust claims challenging vertical restrictions.[5] As applied in tying claims, the plaintiff must first establish the relevant product market (*i.e.* the market that includes the tying product and its reasonably interchangeable products), and then show that the defendant has market power in that market; otherwise, it would not have the ability to force sales of the tied product.[6]

The Federal Circuit Decision

The parties in *DSM Desotech* vigorously disputed which machines were in the relevant market. 3D Systems was the only manufacturer of SL machines, which "use lasers to create solid parts or objects" from resins.[7] SL is a type of "rapid-prototyping technology" used to create or manufacture products through an "additive" or a "subtractive" process. SL is one of many additive processes, which create parts by "building layer upon layer with materials such as plastics, metals, or ceramics," while subtractive processes start "with a mass of material and remove portions to create a part."[8] At issue in *DSM Desotech* was whether SL machines were a distinct product market (*i.e.* a submarket of rapid-prototyping technologies), as Desotech argued, or if machines using other rapid-prototyping technology were "reasonably interchangeable by consumers for the same purposes."[9] The Supreme Court has offered several "practical indicia" to determine the boundaries of a particular market, including (1) whether the products had distinct prices; (2) the product's peculiar characteristics and uses; (3) industry or public recognition of the market as a separate economic entity; and (4) sensitivity to price changes.[10] Interestingly, the Federal Circuit began by noting that the Seventh Circuit requires economic evidence to prove which products "are 'good substitutes' and therefore in the same market."[11] Because Desotech did not offer economic analysis (which "might reveal whether customers switch between SL machines and other rapid-prototyping technologies,") the Federal Circuit held that "the district court properly granted summary judgment on Desotech's antitrust claims."[12]

The court went on to address evidence concerning the four "practical indicia," concluding that while two of the four factors "weigh in Desotech's favor," Desotech could not survive summary judgment "[g]iven the limited and tenuous nature of the evidence."[13] Specifically, it declared that testimony offered by Desotech established that SL machines had "peculiar characteristics and uses," and that there was "industry or public recognition of the [SL machine] submarket as a separate economic entity."[14] This, though, did not establish that SL machines and other rapid-prototyping technologies "are in separate markets;" only that there was a "potential distinct market."[15]

To finally determine if there was an actual distinct product market, the Federal Circuit panel reviewed Desotech's evidence that "customers are insensitive to price changes in SL machines."[16] Desotech had argued that the testimony of four customers, who indicated they would "still buy an SL machine if faced with a 5-10% price increase," raised a sufficient question of fact about the existence of a submarket to survive summary judgment.[17] The Federal Circuit panel disagreed. It found that "such a small sampling (four) from only a single category of customer" was insufficient to show that all of 3D Systems' customers were indifferent to a SL machine price change, particularly where the testimony was offered "without regard to the broad range of price points of the various SL models."[18]

The court then addressed Desotech's remaining tying argument, that a "distinct product market exists for SL resin" that customers are locked into purchasing.[19] This argument relied on the Supreme Court's decision in *Eastman Kodak Co. v. Image Tech. Servs., Inc.*,[20] in which Kodak, *inter alia,* implemented a policy, well after first selling copiers, of limiting or preventing sales of replacement copier parts to companies that serviced its copiers.[21] According to the plaintiffs in that case, in the after-market for its copiers, Kodak, as a result of its policy, controlled "nearly 100% of the parts market and 80% to 95% of the service market for its copiers, with no readily available substitutes," while it only had 23% of the original equipment market for copiers.[22] The Supreme Court ruled that despite not having market power in the original equipment market for copiers, it engaged in an unlawful tying arrangement in the after-market for the purchase and servicing of Kodak copiers, because customers were "locked-in" to using and servicing the expensive Kodak copiers they had purchased. The cost of switching to a competitive copying machine was too high for most customers, although they would "tolerate some level of service-price increases before changing equipment brands."[23] In his dissent in that case, Justice Scalia suggested that Kodak could have avoided antitrust risks "had Kodak—from the date of its market entry— consistently pursued an announced policy of limiting parts sales … so that customers bought with the knowledge that aftermarket support could be obtained only from Kodak."[24] Numerous lower courts have since applied Justice Scalia's hypothetical by ruling that sellers can avoid tying arrangement illegality by making aftermarket policies known to customers when they purchase the allegedly tying product.[25]

Desotech argued that 3D Systems' policy failed to meet the Scalia test to avoid illegality. 3D Systems began selling SL machines in 1988, and did not activate its technological lock until 2007.[26] The machines cost "hundreds of thousands of dollars," and only worked with resin made for SL machines.[27] The Federal Circuit panel disagreed, however, because there were only 268 purchasers of SL resin-- the tied product -- and only seven of them purchased their SL machines before learning of the technological "lock-in." Because a "substantial number of customers" were not locked in, the appellate court affirmed the District Court's grant of summary judgment for 3D Systems.

Conclusion

The Federal Circuit's *3D Systems* decision is a further illustration of the fact that the lower courts have adopted the view expressed by Justice Scalia in his dissent in *Eastman Kodak Co. v. Image Tech. Servs., Inc.* Sellers can defeat "lock-in" tying claims in cases involving after-markets by announcing a restrictive after-market policy prior to the original purchasing decision by customers. Courts also have adopted the view in franchising cases—no antitrust violation exists if the franchisor's restrictions are announced up-front to prospective franchisees.[28] It also demonstrates that such a claim can likely be avoided when an insignificant number of purchasers are harmed by the policy, even if it is announced after the original purchasing decision.

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[1] *Slip Opinion (Slip Op.) is available [here](#).*

[2] *According to the Federal Circuit opinion, 3D Systems excluded the use of Desotech's resin with 3D Systems' machines through a technological tie. It equipped some of its machines with Radio Frequency Identification (RFID) capability, which allowed the machine to communicate with a transmitter on the cap of a resin bottle. "To ensure that customers use only 3DS-approved resins, a software-based lockout feature shuts the machine off if the RFID detects a resin that 3DS has not approved." Slip Op. at 4*

[3] *International Salt Co. v. United States, 332 U. S. 392, 396 (1947).*

[4] *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 12, 24 (1984) ("the essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of a tied product").

[5] *See Leegin Creative Leather Products, Inc. v. PSKS, Inc.* 551 U.S. 877, 896-99 ((2007).

[6] *See Illinois Tool Works, Inc. v. Independent Ink, Inc.,* 547 U.S. 28 (2006); *Jefferson Parish*, 466 U.S. at 24.

[7] *DSM Desotech, Inc. v. 3D Systems Corp.*, 08 cv 1531, 2013 WL 389003, at *1 (N.D. Ill. Jan. 31, 2013).

[8] *Slip Op.* at 10 ("Actual data and analysis are necessary."), *quoting Reifert v. S. Cent. Wis. MLS Corp.*, 450 F.3d 312, 318 (7th Cir. 2006).

[9] *Slip Op.* at 9, *quoting United States v. E.I. du Pont de Nemours & Co.,* 351 U.S. 377, 395 (1956); *see also Brown Shoe Co. v. United States,* 370 U.S. 294, 325 (1962) ("The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it.").

[10] *Slip Op.* at 14-15, *citing Brown Shoe*, 370 U.S. at 325.

[11] *Id.*

[12] *Slip Op.* at 15.

[13] *Slip Op.* at 19.

[14] *Id.* at 16-17.

[15] *Id.* at 17. The court also noted that there were no price difference between some of 3D Systems' cheaper machines and other rapid-prototyping technologies. *Id.* at 15.

[16] *Id.*

[17] *Id.* at 17.

[18] *Id.* at 19.

[19] *Id.* at 20.

[20] 504 US 451 (1992).

[21] *Id.* at 458.

[22] *Id.* at 481.

[23] *Id.* at 476.

[24] *Id.* at 491.

[25] *See, e.g., Smugglers Notch Homeowners' Ass'n, Inc. v. Smugglers' Notch Mgmt. Co., Ltd.*, 414 Fed. Appx. 372, 377 (2d Cir. 2011); *Lee v. Life Ins. Co. of N. Am.*, 23 F.3d 14, 20 (1st Dep't 1994).

[26] *Slip Op.* at 4, 21.

[27] *Id.* at 21.

[28] *See Queen City Pizza, Inc. v. Domino's Pizza, Inc.,* 124 F.3d 430 (3d Cir. 1997).

FTC Upheld Again in Healthcare Merger Challenge

By Mary K. Marks - New York, NY

In a long-awaited decision, on April 22, 2014 a Sixth Circuit panel unanimously upheld a 2012 Federal Trade Commission (FTC) decision ordering the divestiture of a Toledo-area hospital acquired by rival ProMedica Health System in 2010.[1] This decision closely follows the Idaho District Court January ruling in favor of the FTC, which successfully sought to require a Boise-area hospital group to divest a large provider group acquired in 2012.[2] Notably, neither healthcare transaction was required to be reported to the federal antitrust agencies under the Hart-Scott-Rodino Act prior to consummation.

In ruling for the FTC, the Sixth Circuit noted that the FTC's administrative hearing had "lasted over 30 days and produced more than 8,000 pages of trial testimony and over 2,600 exhibits."[3] According to the Court of Appeals, "[t]he Commission's analysis of this merger was comprehensive, carefully reasoned, and supported by substantial evidence in the record," and the FTC did not abuse its discretion in requiring divestiture of the rival hospital.

Background

In January 2011, the FTC, along with the Ohio Attorney General, challenged ProMedica Health System's (ProMedica) August 2010 acquisition of control over St. Luke's Hospital (St. Luke's) through a Joinder Agreement, concerned that it would significantly harm competition in the Toledo area (which is located in Lucas County, Ohio). The FTC believed that the elimination of competition between ProMedica and St. Luke's would enhance the merged entity's ability to obtain supra-competitive reimbursement rates from commercial health plans and their members. The FTC claimed that the transaction would reduce the number of competitors in general acute-care[4] inpatient hospital services in Lucas County from four to three, with a combined market share of close to 60%. According to the Commission, the transaction would also reduce the number of competitors in inpatient obstetrical services in Lucas County from three to two, with a combined market share of more than 80%. On March 29, 2011, the district court granted the FTC's motion for a preliminary injunction and required the hospitals to maintain St. Luke's as an independent competitor pending completion of the FTC's investigation.

After a full administrative trial, the FTC Administrative Law Judge (ALJ) issued an Initial Decision on December 5, 2011, agreeing with the FTC staff that the transaction reduced the number of competitors in the market for general acute-care inpatient hospital services from four to three, and would increase ProMedica's bargaining power with commercial health plans, leading to higher reimbursement rates that would be passed on to the plans' customers (local employers and their employees). The ALJ did not agree with the staff's definition of "inpatient obstetrical services" as a separate relevant product market, but on the basis of the expected increase in consumer prices in the general acute-care inpatient hospital services market, he ordered that ProMedica divest St. Luke's to an FTC-approved buyer within 180 days after the final order.

On March 22, 2012, the Commission upheld most of the ALJ's Initial Decision, finding that the merger increased ProMedica's market share far above the threshold required to create a presumption that the merger would lessen competition. The FTC ruled that ProMedica's acquisition of St. Luke's was likely to substantially lessen competition and increase prices for general acute-care inpatient hospital services and inpatient obstetrical services sold to commercial health plans in Lucas County. The FTC's Opinion defined the relevant market somewhat differently than the ALJ, but noted that "the outcome of this case is the same whether or not [inpatient obstetrical] services are included in the [general acute-care] inpatient hospital services market … As the ALJ found, regardless of which market definition is used, market shares and concentration levels exceed the thresholds for presumptive illegality provided in the 2010 Horizontal Merger Guidelines and the case law. Respondent does not dispute this."

The FTC rejected ProMedica's contentions regarding the commercial health plans' countervailing bargaining power, lack of competitive effects evidence post-transaction, likely repositioning by competitors, and St. Luke's questionable financial viability. Thus, the Commission agreed with the ALJ and ordered ProMedica to divest St. Luke's.

The parties appealed the decision to the Sixth Circuit. The appellate court analyzed what it believed to be extensive data considered by the FTC at the administrative level regarding product markets, concluding that the relevant product markets were: (1) a cluster market of primary (but not OB) and secondary inpatient services, and (2) a separate market for OB services. Then the court turned to ProMedica's arguments that the FTC incorrectly presumed the merger illegal based solely on significantly high market concentration (HHI) levels, contending that such an analysis "applies only in 'coordinated-effects' cases, rather than in 'unilateral-effects' ones."[5] The Sixth Circuit responded by considering ProMedica's pre-merger market shares and relatively higher price levels, and concluded that ProMedica's pre-merger bargaining power, coupled with the HHI data, were sufficient for the FTC to apply a presumption of illegality with respect to the merger.

The court considered the merging parties' failure to show any efficiencies or benefits to consumers. Though these types of arguments can enable merging parties to overcome the presumption of illegality, the court noted the lack of evidence contrary to the presumption, while declaring that there was "a wide range of evidence"[6] supporting the FTC's views on the merger. Finally, ProMedica's use of a "weakened firm" defense was identified by the court as a "Hail-Mary pass" and, as did the FTC, the court rejected the argument due to St. Luke's pre-merger increase in market share and "sufficient cash reserves."[7]

Analysis

Mergers involving hospitals and health care providers remain very much on the radar of federal and state antitrust enforcers, regardless of the size of the transaction or the fact that the merger was not challenged pre-consummation. Moreover, the *Pro-Medica* decision reconfirms that while a "failing firm" defense to a merger suit rarely succeeds, a "weakened firm" defense has even less of a possibility of success.

Recently, in response to the FTC's success in the *St. Luke's* case, Rep. Jim McDermott asked the Commission to issue additional guidance on potential antitrust issues raised by Affordable Care Act (ACA)-inspired health care mergers.[8] As noted in that court's decision, and by Rep. McDermott, health care organization mergers can be in violation of Section 7 of the Clayton Act even when they would improve patient outcomes and quality of care -- goals of the ACA. Additional guidance would provide such organizations more clarity as they attempt the coordination encouraged by the ACA.

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[1] *ProMedica Health System, Inc.v. Fed. Trade Comm'n*, case number 12-3583, in the United States Court of Appeals for the Sixth Circuit (*ProMedica*).

[2] *St. Alphonsus Medical Center-Nampa et al. v. St. Luke's Health System Ltd.*, case number 1:12-cv-00560, in the U.S. District Court for the District of Idaho (*St. Luke's*).

[3] *ProMedica* Opinion at p. 6.

[4] According to the court's opinion, "[General acute-care] comprises four basic categories of services. The most basic are "primary services," such as hernia surgeries, radiology services, and most kinds of inpatient obstetrical (OB) services. "Secondary services," such as hip replacements and bariatric surgery, require the hospital to have more specialized resources. "Tertiary services," such as brain surgery and treatments for severe burns, require even more specialized resources. And "quaternary services," such as major organ transplants, require the most specialized resources of all. Different hospitals offer different levels of these services." *ProMedica* Op., at 1-2.

[5] *ProMedica* Opinion at pp. 12-13.

[6] *Id.* at p. 16.

[7] *Id.* at p. 18.

[8] Congressman Urges FTC to Take Action on Health M&A, Law 360, April 24, 2014, available here.

DOJ and FTC Opine on Information Sharing: When Cybersecurity Is Threatened, Antitrust Laws Are Not – If Properly Done

By Scott Martin – New York, NY

In an April 10, 2014 joint policy statement (Policy Statement),[1] the Antitrust Division of the Department of Justice and the Federal Trade Commission expressly reassured entities seeking to share information concerning cybersecurity threats that it could be accomplished without raising antitrust concerns. While Assistant Attorney General Bill Baer said in his prepared remarks[2] that the legitimacy of "properly designed" cyber threat information sharing is an "antitrust no-brainer," the Policy Statement is noteworthy for several reasons.

First, the issuance of the joint Policy Statement by the two federal antitrust enforcement agencies underscores not only the generally heightened public concern about cybersecurity in view of recent attacks on retailer databases, among others, but also the visible focus on information security and privacy issues by federal antitrust leadership in the current Administration. For example, FTC Commissioner Julie Brill (a Democrat appointed in 2010) has been outspoken on issues of robust data security measures as well as data collection practices, even appearing at length on "60 Minutes" earlier this year to raise awareness concerning the data brokering industry. Similarly, Commissioner Maureen Ohlhausen (a Republican appointed in 2012) focused on data protection and cybersecurity law during her years in private practice in Washington, D.C.

Second, information exchanges among competitors have been the subject of increasing scrutiny in recent years – not only as potential indicators of cartel behavior and other unlawful agreements in restraint of trade that may be subject to criminal prosecution by the DOJ, but also as potential concerns standing alone. Indeed, just last year, the FTC utilized its exclusive enforcement authority under Section 5 of the Federal Trade Commission Act to challenge "unfair methods of competition" in order to obtain a consent order regarding exchanges of competitively sensitive information (including future product offerings, price floors, discounting, forward-looking expansion and contraction plans, and operations and performance) between two competitors in the hair restoration business.[3] Although the FTC did not allege that any agreement resulted from these exchanges, it asserted that they facilitated coordination and created the potential for reduced expansion and price fixing, as well as lacking any procompetitive justification.

Third, the policy statement provides some guidance – even if only in the form of reiterating danger areas in types of information being exchanged and specifically reinforcing a Clinton-era business review letter – concerning information exchanges generally.

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The DOJ/FTC Policy Statement is not the first step undertaken by the Administration to facilitate or encourage information sharing concerning cyber threats, among private entities as well as between private entities and the government. The Administration's February 12, 2013 Executive Order 13636: "Improving Critical Infrastructure Cybersecurity,"[4] recognized cyber threats as "one of the most serious national security challenges we must confront" and required certain federal agencies to share cyber threat information (unclassified *and* classified) with targeted companies. A year later, pursuant to that

Executive Order, the National Institute of Standards and Technology (NIST), an agency of the U.S. Department of Commerce, issued its "Framework for Improving Critical Infrastructure Cybersecurity," in which it stated that there should be a process for receiving cyber threat information from public-private information-sharing fora.[5]

Because well-counseled competing businesses could nevertheless be expected to harbor antitrust concerns about information sharing generally, the Policy Statement can be seen as the logical and necessary next step in the Administration's efforts. In the statement, the agencies referred to guidance in a 2000 business review letter the DOJ provided to the Electric Power Research Institute (EPRI), stating that it had no intention at that time of bringing an action against EPRI regarding a proposed information exchange designed to reduce cybersecurity risks in energy industries resulting from increasing reliance on computers and interconnectivity. Then, as now, antitrust enforcement agencies would examine the business purpose, nature, and likely competitive effect of information exchanges.[6] As set forth in the *Competitor Collaboration Guidelines*, an information-sharing agreement is typically evaluated under the rule of reason to determine the overall competitive effect of the agreement in a relevant market, taking into account its business purposes.

The basic principles and analysis of the 2000 EPRI business review letter hold true for the agencies' 2014 Policy statement: (i) sharing cyber threat information can improve efficiency and network security – a valuable purpose; (ii) cyber threat information is typically highly technical in nature (threat signatures, IP addresses, and the like), as opposed to competitively sensitive information such as future prices, output, or strategic plans; and (iii) exchanging cyber threat information is unlikely to harm competition (*e.g.*, by increasing the ability or incentive of the participants in the exchange to raise price or reduce output, quality, service, or innovation).

None of this is to say that information-sharing protocols for cyber threats will be exempt from antitrust scrutiny -- only that they "should not raise antitrust concerns" if "properly designed."[7] Companies should still carefully examine both the nature and procedure for such information sharing, as well as any protocol's actual implementation, to ensure not only that it fits within the limitations and analysis of the Policy Statement but also, as the agencies expressly cautioned, that it is not "being used as a cover to fix prices, allocate markets, or otherwise limit competition."[8]

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[1] This joint Policy Statement is available here.
[2] The remarks as prepared for delivery by Assistant Attorney General Bill Baer (April 10, 2014) are available here.
[3] *See In the Matter of Bosley, Inc., et al*., FTC File No. 10184 is *available here.*
[4] Available *here*.
[5] *See* February 12, 2014 NIST press release is *available here.*
[6] These principles are set forth in, among other things, the DOJ's & FTC's joint *Antitrust Guidelines for Collaborations Among Competitors* (2000) ("*Competitor Collaboration Guidelines*") is *available* here and joint *Statements of Antitrust Enforcement Policy in Healthcare* (1996) is *available here.*
[7] Policy Statement at 9.
[8] *Id.* at 9 n.21.

European Developments

Beware: Enterprises Facilitating, But Not Operating In, a Cartelized Market Can Be Fined For Participating In the Cartel

By Hans E. Urlus and Emily van Hasselt - Amsterdam*

A recent ruling of the General Court of the European Union (GC) affirmed that enterprises that are not active in the same market as other cartel members, but facilitated the cartel, can face fines under EU competition law.

On February 6, 2014, the GC issued its judgment in *AC-Treuhand AG* (*Treuhand II*).[1] The judgment involved a review of one of the fines imposed by the European Commission (Commission) in 2009 on 24 companies in the heat stabilizers industry for having participated in cartel activities. The total fine was EUR 174 million, of which EUR 348,000 was imposed on Treuhand.

Treuhand is a consulting company offering a full range of services to professional associations. It is not in the market for heat stabilizers. However, the Commission ruled that by: (i) making its offices available to cartel members, (ii) collecting and supplying sales data relating to the relevant markets to the cartelists, and (iii) encouraging alignment among the cartelists, Treuhand had played a central role in the organization and facilitation of cartel activities.

Treuhand appealed the Commission's decision before the GC. It first argued that it had not infringed Article 101 of the Treaty of the Functioning of the European Union (TFEU) – also known as the cartel prohibition – because it had not entered into any anti-competitive agreement or participated in a concerted practice in the relevant heat stabilizers market. Second, Treuhand argued that the Commission had erred in imposing a high fine because the unforeseen application of Article 101 TFEU with respect to Treuhand justified no more than a symbolic fine and additionally that the Commission had erred in its application of its guidelines on the methods of setting fines (fining guidelines).[2]

The GC rejected the first argument out of hand.[3] In a prior *Treuhand* ruling (*Treuhand I*),[4] the GC had ruled that the crucial element in finding an infringement of Article 101 TFEU is a joint intention to engage in infringing conduct. There is no requirement that the market in which an infringing company is active must be the same as the one in which the restriction in competition was deemed to materialize.[5] The GC added that like any other company, a consulting company, although not active in the cartelized market, should be in a position to reasonably foresee the applicability of the Article 101 prohibition when it actively acts and deliberately contributes to an anti-competitive, albeit other, market.

As for Treuhand's second argument, the GC concluded that the Commission had not erred in the implementation of the fine. First, the GC stated that the Commission is under no obligation to impose symbolic fines. In *Treuhand I*, the Commission had in fact imposed a fine of only EUR 1000 on Treuhand for facilitating a cartel in the organic peroxides sector. However, *Treuhand I* was the first time a fine was imposed on an enterprise that was not itself involved in the production or distribution of the goods concerned. Therefore, a symbolic fine was considered appropriate at that time. But it was not appropriate with respect to a second violation.

As to application of the fining guidelines in this instance, the GC recognized that the Commission is supposed to determine the basic amount of a fine by reference to a company's sales of goods or services to which an infringement directly or indirectly relates in the relevant geographic area. Treuhand was not active in the market in which the infringement took place and consequently the value of the services it provided relating to the infringement was recognized as being null. However, the Commission had not referred to any value Treuhand had received for supplying the services to the infringement. The GC noted, however that a specific provision of the fining guidelines provides that the particularities of a given case or the need to achieve deterrence in a particular case may justify departing from the methodology set out in the fining guidelines.[6] The GC concluded that the particular circumstances of the present case justified a departure from such methodology.

Explaining, the GC stressed that any undertaking engaging knowingly in a cartel should incur liability. According to the GC in *Treuhand I*, a sufficiently definite and decisive causal link is enough to fine a facilitating company.[7] The fact that a company has participated in a cartel only in a subsidiary or passive way, or as an accessory, is not sufficient to rule out its liability for the entire infringement. *Treuhand II* is an affirmation of this concept.

Importantly, while the Commission showed mercy in *Treuhand I*, its ruling in *Treuhand II* implies that it will not hesitate to impose significant fines on complicit undertakings in the future. The ruling by the GC is a fair warning to all facilitating enterprises. With a legal maximum of 10% of the total turnover in the preceding business year of a company participating in an infringement[8], the mere facilitation of cartel activities can come at a high price.

[*] *The authors appreciate the invaluable assistance of Anoek Baars in the preparation of this article.*

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[1] Case T-27/10, AC-Treuhand AG v. European Commission, February 6, 2014.
[2] Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003.
[3] Cases 41/69, ACF Chemiefarma v Commission, July 15, 1970, paras 172 to 176.
[4] Case T-41/96, Bayer AG v. Commission, para. 67, October 26, 2000.
[5] Case T-99/04, AC-Treuhand AG v. Commission, July 8, 2008, par. 122.
[6] Treuhand II, paras 301 to 305.
[7] Treuhand I, par. 154.
[8] Article 23 of Regulation 1/2003 on the implementation of the rules on competition laid down in Articles 101 and 102 TFEU.

The Deterrent Effect of EU Competition Law; Higher Fines and Extended Targets

By Hans E. Urlus and Emily van Hasselt - Amsterdam*

Over the past few years, the fact that any "hardcore" cartel activity poses a real threat to the economy and to consumers in the EU has become ever more accepted. However, how to reflect the serious nature of these activities and to ensure that they are detected, deterred, and punished is still being debated. Across the Atlantic and even within the EU, varying opinions exist as to which enforcement approaches enhance the deterrent effect the most. What is definitely happening, however, is increases in fines for violations and the extension of potential liability to facilitators of cartels who are not actually operating in a cartelized market (as discussed in the Article preceding this one), parents of companies participating in a cartel, and the extradition to the U.S. of indicted participants in cartels involving U.S. conduct.

Increasing trend of higher fines for EU competition law infringements

As first discussed below, the level of recent fines implemented in the EU has been increasing in order to heighten their deterrent effect. Actions in the Netherlands also reflect this trend. For example, the Dutch Minister of Affairs recently announced plans to strengthen the fining policy of the Dutch competition authority (Authority for Consumers and Markets, ACM).

Specifically, in March 2014, the European Commission (the Commission) fined cartel participants active in the market for automotive ball-bearings a total of EUR 953 million. The initial fines were even higher, but were reduced due to the willingness of the companies to settle and to cooperate in the ongoing investigation. The companies were accused of secretly coordinating their pricing strategy vis-á-vis customers for more than seven years throughout the European Economic Area. Ball-bearings are just one of about a hundred automotive components, and this decision was only a "small" part of a larger effort to investigate cartels in the automotive parts industries. More high fines can be expected. The Commission's Vice President Joaquín Almunia expressed the hope that "the fines imposed will deter companies from engaging in such illegal behavior and help restore competition in this industry."[1]

As previously noted, the Dutch Minister of Economic Affairs announced plans to amend the fining policy of the ACM. After research conducted by a third party agency indicated the low deterrent effect of the current fines, the Minister proposed to increase the absolute fine from EUR 450.000 to EUR 900.000, and to change the base of the relative fine from the yearly turnover of a wrongdoer involved in a cartel to its combined turnover during the years that the cartel took place (limited to a maximum of four years). Additionally, in case of recidivism, the ACM will be able to double the legally permitted maximum amount.

Whether the imposition of higher fines is the most effective way to improve compliance with competition law is arguable. The tendency of EU member states to adopt laws enabling the criminalization of cartel activities suggests that monetary penalties may not be sufficient.

Liability for the cartel conduct of a subsidiary or facilitator

Under EU law, liability for a competition law breach by a particular company attaches to the entire economic entity of which that company forms part. As a result, a parent company can be held liable for the infringement of a subsidiary when it exerted influence over the subsidiary. Influence is presumed, however, when the parent holds (nearly) all of the subsidiary's shares.

On April 2, 2014, the Commission related that a private equity firm exercised decisive influence over a wrongdoing portfolio company solely because of the parent's voting rights and board representation.[2] This was the first time that liability has been extended to private equity firms for the competition law infringement of a portfolio company.

Additionally, as noted in the preceding Article, facilitators of cartels are subject to all of the potential liability of those companies that actually carried the cartel forward through their direct business operations. The fact that the facilitator did not in fact participate directly in the cartelized market is of no matter.

The prosecution of international cartels—extradition

On April 4, 2014, the U.S. Department of Justice announced the first successful extradition of a foreign national to face a prison sentence in the U.S. for an antitrust violation. This could mark the start of an aggressive pursuit to prosecute foreign nationals who have infringed U.S. competition rules, thereby increasing the level of deterrence by means other than high administrative fines.

Romano Pisciotti, an Italian national and former executive of Parker ITR Srl, was indicted in 2010 for participating in a conspiracy to fix prices, rig bids and allocate market shares for marine hose products. In 2013, he was arrested in Germany while on a layover at the Frankfurt airport on his return to Italy from Africa. Because he was not a German citizen, he was extradited to the U.S. this year pursuant to a German treaty with the U.S. Last month, he pleaded guilty to one count of conspiracy in the U.S. District Court in Miami and was sentenced to two years imprisonment (with credit for the time he was held in German custody pending extradition).

Successful extradition to the U.S. requires: (i) an extradition treaty with the country in which the individual is located, (ii) an existing law in the relevant jurisdictions criminalizing the same conduct, and (iii) the permissibility of extradition in both countries. German law has criminalized bid-rigging, and the country had an extradition treaty with the U.S. Pisciotti, as an Italian national, was not given the same protections to extraditions as German nationals, and the extradition application was successful. The U.S. Department of Justice views extradition as "a significant step forward in our ongoing efforts to work with our international antitrust colleagues to ensure that those who seek to subvert U.S. law are brought to justice."[3]

However, more successful U.S. extraditions in the future will depend on the 'criminalization' of cartel activities. EU member states do not see eye to eye regarding such criminalization. For example, while the Netherlands intends to increase its administrative fines, the UK has already adopted criminal sanctions for cartel activities. Accordingly, it is unclear how much of a trend was started with the recent extradition of an Italian national.

Conclusion

The implementation of higher fines, extension of liability to parent companies and facilitators of antitrust conspiracies, and the use of extradition of foreign nationals should deter companies and individuals from participating in cartel activities. However, this increasing trend to capture and punish cartel activities should not overshadow the main goal of EU competition law: to promote and maintain competition in the marketplace.

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[1] http://europa.eu/rapid/press-release_IP-14-280_en.htm.

[2] Commission, Press Release of February 2, 2014, IP./14/358.

[3] Press release Department of Justice, Friday, April 4, 2014.

The European Private Enforcement Regime Reaches a Milestone

By Hans E. Urlus and Emily van Hasselt - Amsterdam*

On April 17, 2014, the European Parliament approved the European Commission's (Commission) proposal for a Directive on damages actions for competition law infringements (the Directive).[1] The Directive, which is intended to enhance private enforcement of competition law by facilitating damages actions for direct and indirect purchasers in the EU Member States (Member States), represents a significant milestone following a decade-long debate about whether damages claims for antitrust infringements should be facilitated in the European Union.

Approval of the Directive follows the European Court of Justice's (ECJ) rulings in *Courage & Crehan*[2] and *Manfredi*[3] that the full effectiveness of Article 101 of the Treaty of the Functioning of the European Union (Article 101 TFEU), and in particular, the practical effect of the prohibition laid down in Article 101 would be put at risk if it were not open to any individual to claim damages for loss caused by conduct that restricts or distorts competition.

A 2004 study assessing the actual condition on claims for damages within the European Union had identified obstacles to successful individual damages actions in the EU.[4] The study revealed a "total underdevelopment" of actions for damages for breach of EU competition law as well as an "astonishing diversity" in the approaches taken by the Member States on the subject. Consequently, the Commission commenced its plans for harmonizing private enforcement rules in the EU by issuing its Directive.

The Directive announces two main objectives:

i. to ensure full compensation for actual loss, loss of profit and interest of any individual harmed by competition law infringements; and

ii. to improve the interaction between leniency programs and private actions.

The Directive undoubtedly was inspired by the legal remedies available in the United States, where private enforcement of competition law is well established. However, the Directive departs from the U.S. system in several significant respects, which can be explained by the different policy objectives across the Atlantic. In the U.S. private damages claims serve both compensation and deterrence functions, with the focus 2 on deterrence. The Directive, however, centers on full compensation -- deterrence plays a lesser role.

The following summarizes several of the Directive's most important features:

1. Passing on defense and indirect purchaser standing

According to the Directive, defendants will have the right to defend themselves against damages claims by proving that the claimant passed on a cartel-driven price increase (overcharge) to its customers (the "indirect" purchasers). This defense is called the "passing on" defense. A successful passing on defense means that the losses incurred by direct purchasers that are then passed down the distribution chain to indirect purchasers no longer constitute harm to the direct purchasers. The burden of proving the passing on defense will lie with the defendant.

In order to assist national courts with estimating the portion of an overcharge passed on, the Commission is expected to issue estimating guidelines. The complexity of calculating a passed on amount is one of the reasons that the U.S. Supreme Court has rejected the passing on defense and indirect purchaser standing in Sherman Act cases.[5]

Linked to the passing on defense is an indirect purchaser's right to claim damages, explicitly acknowledged in the Directive. If national courts reject indirect purchaser standing, competition law infringers may escape liability by successfully invoking the passing on defense.

To support indirect purchasers in their claims, the Directive contains a presumption in their favor: the indirect purchaser must prove only that an infringement of competition law occurred and the direct purchaser passed on the overcharge to the claimant.

2. Disclosure of evidence

Pursuant to the second objective, the Directive contains extensive rules on evidence disclosure, one of the most intensely debated aspects of the Directive. The ECJ has held that no category of documents may be exempted from disclosure requests. However, the final decision on which evidence is to be revealed rests with the national courts.[6] This opened the debate on the protection of leniency applications. The Commission has a leniency policy whereby companies that provide information about a cartel in which they participated might receive full or partial immunity from fines. In the EU most cartel cases have been discovered as a result of leniency applications. In order not to deter cartel members from applying for leniency when exposed to vulnerability in follow-on private damages actions, it was argued that not all evidence should be disclosed for use in such actions.

The Directive provides for a sliding scale of documents protected. Evidence can belong either in a "black", "grey" or "white" list. The black list contains leniency corporate statements and settlement submissions. Those documents may never be disclosed. The prohibition on disclosure extends to extracts from such documents that appear in otherwise grey or white list documents.

3. Joint and several liability

According to the Directive, infringers of competition law will be held jointly and severally liable for the entire harm. This is in line with the Directive's full compensation objective. Nonetheless, the rule is subject to several exceptions:

i. leniency recipients will only be liable for the harm caused to their own direct and indirect purchasers; and

ii. small and medium-sized enterprises that did not lead or coerce other companies into the infringement nor previously committed a competition law infringement will only be liable for damages to their own direct and indirect purchasers if their market share was below 5% during the infringement and application of the normal rules would jeopardize their economic viability.

4. Limitation periods

In order to ensure the exercise of the right to full compensation, Member States will be able to maintain or introduce generally applicable absolute limitation periods. The minimum limitation period for bringing an action will be five years.

The limitation period will only begin to run from the moment the claimant knew or could reasonably be expected to have known that the particular defendant infringed competition law and caused harm to the claimant.

The period will be tolled if:

i. a competition authority has commenced an investigation or proceeding. The suspension will last until at least one year after an infringement decision has become final or proceedings have been terminated; and

ii. the infringer and victim are involved in consensual dispute resolution. In such an event, the period will be suspended for a maximum of two years.

5. Quantification of harm

A main obstacle to private damages claims is the recognition of the claimant's actual harm. National courts are often unable to precisely estimate harm caused to direct or indirect purchasers with the available evidence. In order to remedy this difficulty, the Directive empowers national courts to estimate the harm themselves. Additionally, the Directive introduces a rebuttable presumption that a competition law infringement causes harm.

The Future

The EU Council of Ministers is expected to formally approve the Directive in the coming weeks. Once adopted, the Member States have to implement the Directive within two years.

So far, in theory, the Directive appears to achieve the Commission's aim of enhancing private enforcement of competition law in the EU. Moreover, the Directive may signal the end to national debates about whether or not to accept the passing on defense, or which documents should be exempt from disclosure to private claimants.

** The authors appreciate the invaluable assistance of Anoek Baars in the preparation of this article.*

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[1] Directive of the European Parliament and of the Council on rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union.

[2] Case C-453/99, Courage Ltd v Bernard Crehan [2001] ECR I-6297.

[3] Joined Cases C-295/04 to C-298/04 Manfredi v Lloyd Adriatico Assicurzaioni SpA [2006] ECR I-6619.

[4] In 2004, the law firm Ashurst completed a study into the possibilities for bringing damages actions for infringements of EU and national competition law in the legal systems of 25 EU Member States.

[5] *See Illinois Brick Co v. Illinois*, 431 U.S. 720, (1977) (*Illinois Brick*); *Hanover Shoe, Inc. v. United Shoe Machinery Corp*., 392 U.S. 481(1968) (*Hanover Shoe*). The U.S. Supreme Court considered that the passing on defense and indirect purchaser standing to sue for damages would introduce additional allocation of damages complexity into an already complex case. Additionally, the Supreme Court considered that deterrence is best achieved by giving direct purchasers the right to recover full damages as they are most motivated and capable.

[6] Case 360/09, Pfleiderer AG v. Bundeskartellamt, June 14, 2011 and Case C-536/11, Bundeswettbewerbsbehorde v. Donau Chemie AG and Others, June 6, 2013.

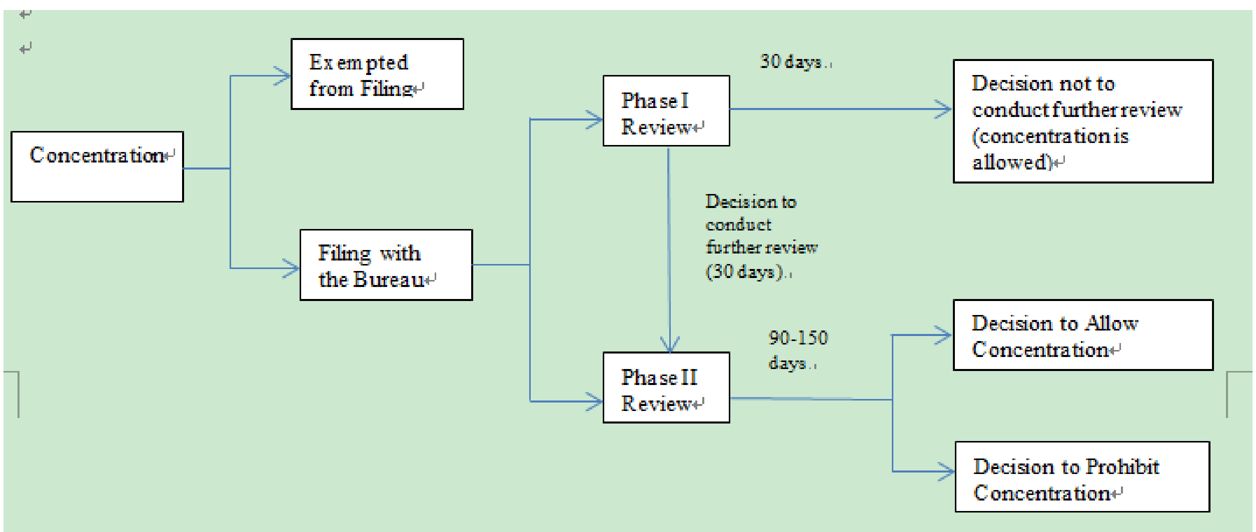
China Developments

MOFCOM Issues Tentative Provisions on Standards Applicable to Simple Cases of Concentration of Business Operations In China

By Dawn Zhang and Feiya Zhong - Shanghai

Background

Under the People's Republic of China (PRC) Anti-Monopoly laws, concentrations of business operations through mergers or acquisitions that exceed certain standards (summarized below) must comply with the filing procedures of the Anti-Monopoly Bureau of the Ministry of Commerce or MOFCOM (the Bureau). The business operations may not go forward with the proposed concentration without complying with the filing procedures. The Bureau is required to conduct a Phase I review of the filing within 30 days of submission and inform the business operations in writing as to whether the proposed concentration is subject to further review. In the event that the Bureau decides to conduct further review (Phase II review), it is to be completed within 90 days of that determination. However, under special circumstances, the Phase II review can be extended up to an additional 60 days upon notice to the business operations involved. Therefore, under common filing procedures, if the proposed concentration undergoes a Phase II review, the total time from submitting the filing documents to receiving a decision from the Bureau can be as long as 180 days.



Standards for Simple Cases

On February 11, 2004, MOFCOM officially released *Tentative Provisions on Standards Applicable to Simple Cases of Concentration of Business Operations* (the "*Tentative Provisions*"), which took effect on February 12, 2014.

General Rules

The *Tentative Provisions* declare that concentration cases that meet the following standards will be classified as “simple” cases. What that will mean from the standpoint of filing requirements and review procedures is still in preparation:

1. Cases in which the business operations participating in the proposed concentration have a horizontal relationship, but the aggregate market share of all the business operators participating in the concentration is less than 15%;
2. Cases in which business operations participating in the proposed concentration have a vertical relationship, and the market share of each business operation accounts for less than 25% in both upstream market and downstream markets;
3. Cases in which the business operations participating in the proposed concentration who neither have horizontal nor vertical relationship and account for less than 25% of market share in their respective markets relating to the proposed concentration;
4. Cases in which the business operations participating in the proposed concentration establish a joint venture outside China, and the joint venture does not engage in any economic activities within China;
5. Cases in which the business operations participating in the proposed concentration acquire the equities or assets of overseas enterprises, and the overseas enterprises do not engage in any economic activities in China;
6. Cases in which a joint venture previously jointly controlled by more than two business operators is to be controlled through concentration by one or more of such business operations.

Simple Case Exceptions

Under the *Tentative Provisions*, even if the above standards for simple cases are met, under certain circumstances the concentration will nevertheless not be treated as a simple case. The special circumstances include difficulty in defining the relevant market of the proposed concentration, and a potential adverse effect on market access, technology improvement, consumers, other operations, or the national economic development.

In addition, the MOFCOM has discretion to revoke its decision to treat a concentration as a simple case, if evidence indicates (1) untruthful filing materials, (2) an effect of eliminating or restricting competition, or (3) a material change in the concentration or competition in the relevant market.

Conclusion

Compared to the common concentration review procedure, which may take up to 180 days to complete the procedure, the *Tentative Provisions* will shorten the time of the review procedure of a concentration that would not likely cause an adverse effect on competition in China. Given that certain concentration will be treated as simple cases in accordance with the *Tentative Provisions*, such cases will likely apply a relatively simple filing procedure, which may lower the filing burdens for business operations participating in such concentrations. The Ministry of Commerce is currently in the process of making ancillary rules to implement the *Tentative Provisions*, such as the procedural rules of application for simple cases.

Contact

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