

Antitrust Issues for Associations

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Roadmap

- Antitrust Basics
- Application of the Antitrust Laws to Associations
- Compliance Programs and Associations
- Discussion and Q&A

Antitrust Basics

- Most countries use the term “competition law” rather than antitrust
- **Basic idea** – prevent firms or groups of firms from obtaining the power to control a market through means other than competition on the merits
 - Generally not a violation to exercise that power
 - Nothing wrong with winning by innovating or running a better business

Basics – Different Types of Antitrust Rules

- Agreements and other coordinated and multilateral conduct – Section 1 of the Sherman Act
 - Most of the issues for associations relate to this
- Monopolization – Section 2 of the Sherman Antitrust Act
- Mergers – the Clayton Antitrust Act

Basics – Agreements and Coordinated Conduct

Sherman Antitrust Act §1:

“Every contract, combination in form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal.”

Basics – Agreements and Coordinated Conduct

“Every contract, combination in form of trust or otherwise, or conspiracy,...”

- This means agreements
- Often it is hard to show that there is an agreement – Firms generally don’t enter into formal agreements to fix prices

Basics – Agreements and Coordinated Conduct

Proof of Agreement

- Actions of an association are often taken as evidence of an agreement among the members of the association to take that action.
- Even actions of an individual working for the association can be evidence of an agreement among the members to the association.

Basics – Agreements and Coordinated Conduct

“...in restraint of trade or commerce...”

Does the agreement harm competition – two types of potentially anticompetitive agreements:

- Those that are deemed to be anticompetitive on their face – *per se* illegal agreements
- Those that might be anticompetitive but that must be analyzed under the “rule of reason”

Basics – *Per se* Illegal Agreements

***Per se* illegal agreements**

These are agreements that always or almost always restrict competition and reduce output

- **Price fixing** – including components of price and price-related terms like discounts, credit terms and trade-in allowances
- **Market allocation** – where firms agree to stay out of each others' markets so they don't compete
- **Bid rigging** – where the parties agree to not bid against each other
- **Some group boycotts** – competitors get together to enforce a price fixing agreement or harm a rival

Basics – Agreements and Coordinated Conduct

Per se violations like price fixing, market allocation and bid rigging can be crimes, leading to jail time for those found guilty

Basics – Criminal Violations

- Associations have been used as cover for criminal antitrust violations
 - Lysine price fixing cartel created a subcommittee of the European Feed Additives Association as a pretext for meeting at association meetings to fix prices
- Penalties are severe
 - Incarceration
 - Fines of up to \$1 million for individuals and \$100 million for organizations
- Evidence of criminal violation needs to be reported to the responsible officer of the association immediately

Basics – Agreements and Coordinated Conduct

Rule of Reason – a more or less detailed look at the restraint to see if it promotes competition or suppresses competition:

- Look at the restraint itself
- Look at the market power of the firms imposing the restraint
- Look at potential efficiency justifications for the restraint

Antitrust Issues for Associations

- **Price fixing** through statistical reporting by the association
- **Price fixing** through inappropriate communications between members at meetings
- **Group boycotts** – competitors get together and agree not to deal with a competing firm – sometimes membership issues

Associations and Group Boycotts

- Group boycott issues can pop up in a number of ways for associations (more about each later):
 - Self-regulation and codes of ethics
 - Standard-setting and certification
 - Membership requirements and access to association services and activities
- Might be illegal *per se* or may be looked at under the rule of reason

Association Liability

- Where the association directly violates the Sherman Act – negotiating prices on behalf of members
- Member violates the antitrust laws through the machinery of the association which doesn't have safeguards to prevent that
 - *Hydrolevel* – members in leadership positions use their positions to harm competitor in the market by interpreting safety standards

Antitrust Liability for Officers and Directors of Associations

- There **should not** be personal liability for those who exercise ordinary and reasonable care in the performance of their duties, showing honesty and good faith.
- There **may be** personal liability for those who participate in or knowingly approve of an antitrust violation.

Application of Antitrust Law to Associations

- Discussions at meetings
- Membership requirements and expulsion
- Services to members and non-members
- Statistical reporting
- Standard-setting and certification programs
- Lobbying
- Regulation of business conduct
- Antitrust and the Internet activities of associations

Discussions at Meetings

- Proof of an anticompetitive agreement can start with proof of parallel conduct plus potentially illicit communications between rivals.
 - Because association meetings generally involve communications between rivals, care must be taken to avoid illicit communications
- That means that discussions at meetings are often formalized and laid out ahead of time to a great extent

Discussions at Meetings

- Agendas and presentations prepared and distributed in advance of meetings
- Care should be taken to keep to these materials at the meeting unless there is a good reason to depart
- Minutes of the meetings should be prepared that concisely reflect the discussions
 - Especially where they diverge from the pre-prepared materials

Discussions at Meetings

- There are a number of off-limit topics where discussions could lead to illegal agreements
 - Pricing, including any discussions of methods, strategies, timing, discounts, advertising, or what constitutes a fair or reasonable price
 - Whether to do business with suppliers, customers or competitors
 - Complaints about business practices of other firms
 - Confidential company plans regarding output decisions or decisions regarding future offerings

Statistical Reporting

- There can be *per se* and rule of reason violations as a result of information collection and dissemination
- Recall that *per se* violations include:
 - Price fixing
 - Agreements to restrict output – which is really the same thing as price fixing
 - Market allocation

Statistical Reporting – *Per Se* Violations

- It is hard to succeed at committing these violations unless you know what your competitors are doing
- What if you and your rival agree to raise prices by \$10 but you can't tell what they are actually charging?
 - They might have tricked you into raising prices but didn't themselves
- So when competitors are communicating pricing information it is always possible they are doing that to help make a price fixing agreement stick.

Statistical Reporting

- These types of communications within an industry are often done through 3rd parties (e.g., associations) to avoid direct contact between rivals.
- Important issues for an association when acting as a 3rd party for communications
 - Type of information (price v. cost, current v. older, specific as to parties and transactions v. more general and aggregated, only for sellers v. available to customers also)
 - Purpose of the information reporting – can't be for anticompetitive reasons
 - Can you articulate pro-competitive reasons?

Statistical Reporting

- Make sure that firms can't derive info about their competitors from the disclosures
 - Aggregate info rather than individual firm data
 - Old data rather than forward looking data
 - Only where there is enough firms that it is hard to guess who did what
 - Where there are only a few firms in the industry, it might be easy to pick out their data from the distributed information

Statistical Reporting Example

- The Ductile Iron Fittings Research Association FTC Case
- Three big firms in the industry
- Data aggregated by a third party but it was very current data
- If a firm was losing sales it would have been able to look at the data to see if the market was losing sales
 - If not then that firm would know that the others were competing aggressively – detecting cheating is one of the critical functions of a cartel
 - FTC has sued all three companies and two have settled so far

Membership Requirements and Expulsion

- These are looked at as potential group boycotts.
- Rules and decisions on membership and expulsion are generally considered under the rule of reason not *per se*.
- Exception:
 - The rule or decision relates to access to some business input that is essential for effective competition, and
 - There are no plausible justifications stemming from the association's pro-competitive purposes.

Membership Requirements and Expulsion

- Under the rule of reason we look to see the effect of the requirement or decision
- A number of factors depending on the case
 - Are the rules objective and consistently applied
 - If the rules are subjective, is there a legitimate reason for the rule based on the pro-competitive needs of the association
 - Is due process given to those expelled
 - Notice and opportunity to respond
 - Appeal process
 - Disinterested decision-makers

Membership Requirements and Expulsion

- **Vermont Dairy Herd Improvement Assoc case** – a herd owner was suspended from participating in the association’s milk testing program.
- The herd owner argued that the program was necessary for him to compete
- The court held that the expulsion had to be evaluated under the rule of reason because the expulsion might improve competition if the exclusion was to protect the testing program, which was intended to encourage competition

Services to Members

- Competitive issues closely tied to the membership requirements
 - The more competitively important the services are the more important that firms are not excluded from those services for anticompetitive reasons.
 - Sometimes the courts decide that the service should be provided to non-members rather than requiring that the non-members should be allowed to join the association.
- Rule of reason analysis here generally too.

Services to Members

- Some General Guidelines:
 - Take a look at the services that the association provides periodically to see if any are essential for effective competition by companies in the industry
 - Make sure that services like that are made available to non-members or if not that there is a good reason, tied to the benefits the association provides to members
 - There can be a higher fee for non-members than for members but the fee should be related to the cost for providing those services to non-members

Services to Members – Trade Shows

- Access to trade show sponsored by Association –
 - Rule of reason analysis generally
 - Important questions and issues:
 - Are the rules objective?
 - How important is the trade show to competition in the market?
 - Is there is limited room?
 - replacing one firm with another is not likely to have an impact on competition
 - Why was the firm excluded – don't exclude a firm for competitive reasons?
 - Similar rules apply to decisions relating to allocating space or location

Services to Members – Trade Shows

- Some “Don’ts”
 - Don’t apply rules in a discriminatory manner
 - Don’t base decisions on whether the firm engages in competitive pricing
 - Don’t condition decisions on whether a firm agrees to not appear at a competing trade show
 - Generally don’t use subjective criteria for participation or allocation of resources

Standard-Setting and Certification Programs

- Two kinds of standard setting (with different issues)
 - Health and Safety
 - Industry gets together as experts to figure out best practices for health or safety
 - Example: fire safety for building materials by the NFPA
 - Compatibility – members of a variety of related industries get together to develop a standard that will make sure that their products work together
 - Example: Wall outlets and plugs on electrical devices – different companies make the different devices but they have to work together
 - Happens a lot in computer technology (e.g., JEDEC)
 - Happens in telecommunications (e.g., IEEE and ETSI)

Standard-Setting

The difference between compatibility standards and health and safety standards

- Health and safety standards generally impact the market when they are adopted by federal, state or local governments – if no standard then there will be all the variety that the market can bear
- Whether or not there is an agreement on a compatibility standard, there will generally be only one type of product – even if there is no agreement there will eventually be a *de facto* standard (e.g., Microsoft Windows)
 - Standard-setting can avoid a standards war like Sony Betamax/VHS

Standard-Setting Health and Safety

Guidelines:

- There should be a justification for the development of a standard at the outset
- To the extent that the standard is going to limit access to the market for some firms, that exclusion must be justified
- Avoid allowing the process to be dominated by economically interested parties
- Ensure that all parties with a stake in the standard have an opportunity to participate meaningfully in the process
- Avoid if possible any concerted efforts to enforce the standard

Standard-Setting Health and Safety

- Allied Tube & Conduit Corp v Indian Head –
 - National Fire Protection Association standard on conduits
 - Previously conduits made of steel and NFPA was considering approving PVC conduit
 - Steel conduit manufacturers packed the meeting with enough people who voted against the standard to defeat it
 - Since standard was adopted by state and local governments, that meant that PVC manufacturers were excluded from the market

Compatibility Standards

- Some of the same rules apply –
 - To the extent that the standard is going to limit access to the market for some firms, that exclusion must be justified
 - Avoid allowing the process to be dominated by economically interested parties
 - Ensure that all parties with a stake in the standard have an opportunity to participate meaningfully in the process

Compatibility Standards and Patents

- Compatibility standards are often in cutting edge high tech industries where patents are prevalent
- If an industry becomes locked in to a standard that is covered by a patent then the holder of the patent will be able to extract profits from the rest of the industry.

Compatibility Standards and Patents

- Antitrust issues come up when an industry standard is covered by a patent
 - If the patent was not disclosed to the standard-setting body by the owner then the patent holder may be liable for monopolization
 - It may depend on the rules of the organization and the knowledge of the patent holder

Compatibility Standards

Sherman Antitrust Act §2:

“Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, shall be deemed guilty of a felony...”

- DOJ can bring civil suits to enjoin monopolization
- FTC can also stop this conduct

Compatibility Standards

- Patent policies should be clear, consistently enforced and regularly announced
 - When should there be disclosure
 - What should be disclosed (patent applications or just patents)
 - Is there a requirement to search a member's patent portfolio
 - What sort of commitments are required by the patent holder, if any, after disclosure
 - RAND/FRAND
 - License Negotiations
 - Disclosure of most onerous terms
 - License offer

Certification

- Certification programs can determine whether products comply with a standard or whether professionals have sufficient ability, education and experience.
- Not certifying a product or a professional can create competitive harm
- Courts look at the process of how a certification program is implemented to ascertain whether they help customers or are a way to harm rivals

Certification

- Some factors:
 - Who are the decision-makers – competitors or customers or a mix
 - Are the criteria objective and related to the function being certified
 - Were the criteria applied consistently and without discrimination
 - Were the association's procedures followed
 - Important to the extent that it might show that a refusal to certify was due to anticompetitive goals

Regulation of Business Conduct

- Many associations have codes of ethics regulating various aspects of the businesses of the members of the association.
- This sort of regulation can be good
 - Industry members themselves often have the best incentives and the knowledge to maintain the reputation of the industry
 - Can improve the services offered to consumers and improve the truthfulness of advertising for example

Regulation of Business Conduct

- This sort of code of conduct can also be anticompetitive
 - Restrictions on truthful advertising especially relating to price
 - Restrictions on competitive bidding
 - Restrictions on the business hours of members
 - Restrictions on business relationships with suppliers or competitors
 - Restrictions on fees or output set by members
- This type of conduct is often viewed by the courts under an intermediate level of scrutiny.

Internet Activities of Associations

- Really an extension of the rules in the real world
- **Discussion boards** – concern that competitors can use these to violate the antitrust laws in the same way they could at meetings
 - Rules regarding off-limit discussions should be clearly laid out
 - The boards should be monitored by well-trained and responsible association staff
 - The staff should be able to (and should) promptly take corrective action when inappropriate messages are posted

Internet Activities of Associations

- **B2B sites** sponsored by associations
 - firewalls should be established to prevent each participant on the site from being able to view the transactions of others
 - there should be no limitations imposed on the number of buyers or sellers permitted to utilize the site
 - there should be no conditions placed on buyers or sellers that require them to conduct business through the site or only through the site

Lobbying

- In general petitioning the government cannot form the basis of an antitrust violation based on the effect of the petition succeeding
 - E.g., lobbying a legislature or agency to get that body to pass a law that would block the entry of a competitor is shielded from liability under *Noerr-Pennington* doctrine
- But if the petitioning is a sham and itself (rather than the government policy) has an anticompetitive impact then that can form the basis of an antitrust violation.

Compliance Programs

- Antitrust policies have become mandatory for associations
 - Absence of a policy is viewed as poor business practice, can be evidence of wrongdoing and may increase penalties for any violations that occur
 - Antitrust policies can have an effect on the behavior of members
- Responsible Antitrust Practices
 - Legal review of agendas and minutes
 - Legal counsel attendance at meetings

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The Center for Association Leadership