# NYSBA

## 2006 Antitrust Law Section Symposium

**January 26, 2006**
**New York Marriott Marquis**

**New York State Bar Association**
**Antitrust Law Section**

# Annual Meeting

**January 26, 2006**
**New York Marriott Marquis**

**Section Chair**
**STEVEN TUGANDER, ESQ.**
United States Department of Justice
Antitrust Division
New York City

**Program Chair**
**ILENE KNABLE GOTTS, ESQ.**
Wachtell Lipton Rosen & Katz
New York City

**Dinner Speaker**
**HONORABLE DEBORAH PLATT MAJORAS**
Chairman
Federal Trade Commission
Washington, D.C.

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# Introductory Remarks

**MR. TUGANDER:** It is my pleasure to have you join us for our 2006 Annual Meeting. Our Program Chair, Ilene Gotts, has worked very hard to put together a full day CLE program that will include a variety of panels on timely antitrust topics. We hope you enjoy the program.

We also hope most of you will join us this evening for the annual cocktail hour and dinner. We are very fortunate to have Deborah Majoras, Chairman of the FTC. And our Service Award Recipient is past Chair Alan Weinschel.

One more note before I turn the program over to Ilene. Immediately before the lunch break we will be visited by Richard Raysman, Director of the New York Bar Foundation. Some of you may be aware the Foundation is the Bar's charitable arm. He's going to make a brief presentation, and we encourage you to stay and listen to his brief presentation.

With that I'm going to turn it over to Ilene Gotts.

# Annual Review of Antitrust Developments

**MS. GOTTS:** Good morning. Has everyone gotten their coffee?

We have a pretty exciting day ahead of us. We are going to start out the morning hearing from Elai Katz and Molly Boast. Unfortunately, Bill Lifland was not well enough to join us today. They will be providing their Annual Review of Antitrust Developments.

Right after that we will have a short break. I'm going to try to ask people to stay within the time designated for the breaks so we can really give you a full agenda. And then we are going to move into our morning panel, which will be a discussion of dominant firm conduct, that I think you'll find that pretty interesting. It is clearly a cutting-edge area on which there is divergence internationally.

We will then have a very short Business Meeting, followed by remarks from a representative of the Foundation, and then lunch will be on your own, except for the Executive Committee members who are going to work through lunch.

In the afternoon we are going to have something for everyone. First a discussion of cutting-edge issues in class actions, followed by a overview of the Antitrust Modernization Commission, and what they are doing, what their agenda might be, and how we can play our role on that.

This evening we are going to have our cocktail reception followed by the Service Award. And FTC Chair Debbie Majoras has promised us a very exciting speech on antitrust and political process.

With that I'm going to introduce our two speakers for the Annual Review, first, Elai Katz, who is a partner of Bill's at Cahill Gordon & Reindel. He concentrates in antitrust law, including a wide gamut of litigation counseling, mergers and acquisitions. He is a graduate of Yale University and Columbia Law School.

After Elai we are going to hear from Molly Boast, for whom this is becoming an annual appearance. Many of you know her already. Molly is a partner with Debevoise & Plimpton, a firm that practices in a broad spectrum of areas, but Molly's primary area is within the litigation department. I know from Molly's years in Washington, where she served in the Bureau of Competition at the FTC, first as the Senior Deputy Director and then as the Director of the Bureau of Competition, she has been involved in some of the landmark cases. Molly is a graduate of Columbia Law School, and her undergrad degree was from the College of William & Mary.

With that I am going to turn it over to Elai.

**MR. KATZ:** Thanks. I'll try my best to convey the thoughts and ideas that Bill had, and hopefully it will be informative to you.

2005 saw a number of interesting antitrust developments, but we'd like to start with a development that occurred not in 2005, but very early this year. It's the Volvo Robinson-Patman Act case (V*olvo Trucks North America v. Reeder-Simco GMC,* 126 S. Ct. 860 (2006)). It is the first Robinson-Patman Act decision by the Supreme Court in about a decade. The Court held that a manufacturer may not be liable for secondary line price discrimination under Robinson-Patman Act without proof that the manufacturer discriminated between dealers competing to sell its products to the same retail customers. The Act was held not to reach discrimination between sellers competing to serve different customers.

This case involves heavy duty trucks. Volvo had organized its distribution by having dealers serve particular regions, although the regions were not necessarily exclusive in the sense that one dealer was permitted to bid for business in another dealer's region. Otherwise, they were regional and generally expected to be separate.

What would happen is a customer who was interested in a heavy duty truck would usually put in a specification, a request for a quote to a dealer. Typically, there would be only one dealer for a given manufacturer that would receive a request for a quote. The dealer would then go to Volvo—or if it is for another manufacturer—put in the specifications and request some kind of discount off the list price in order to submit the best bid.

The complaining dealer here had alleged that over the years it had received higher prices or smaller discounts than the other Volvo dealers. The Court concluded that the Robinson-Patman Act did not cover a case where the better prices offered to other dealers were for a different ultimate customer and usually in a different region. The Act regulates, according to the Court situations where a sale is made to two separate sellers who are competing over the same purchaser. Here there was no such competition.

It is worth mentioning that the opinion acknowledged the Act was meant to protect small retailers from the competition of chain stores and other volume purchasers. At the same time the Court said that the Act is to be interpreted in accordance with the overall procompetitive purposes of the antitrust laws. This seems inconsistent with protecting some firms from competition. It seems to indicate the Court is disposed to apply the Robinson-Patman Act narrowly in competitive markets.

To go back to the case below, the jury had awarded a verdict for the plaintiff and the defendant was required to pay around $4 million when the damages were trebled. It was affirmed in the Court of Appeals, and the Supreme Court reversed. The Court devoted a substantial portion of its opinion to observations regarding the application of the Robinson-Patman Act. The Court noted that enhancing or fostering interbrand competition is the primary concern of antitrust law. The scope of this observation seems unclear. Its concern with the broader antitrust policies is superfluous if the supplier extends the same discount to all dealers trying to land the same order. In that case there should be no discrimination in price. If the discounts varied, with larger discounts going to dominant dealers, smaller dealers would be left with substantially higher costs. Then the situation begins to resemble more the small retailer-chain store model, in which the Court says Congress meant to protect the small dealer. Yet the manufacturer may wish to favor the larger dealer to advance interbrand competition. The larger dealer may be willing to invest in modern service facilities for example, which the supplier may wish to encourage in order to stimulate the customer to buy its brand of truck rather than another.

In this situation, should broader antitrust concerns trump the Robinson-Patman Act? The issue may be masked as a practical matter because a defense to a Robinson-Patman claim, such as meeting competition, may be present or the FTC may find no public interest in looking at the Robinson-Patman Act in the absence of a dominant party or because a private challenge is deemed unwise for commercial reasons. Absent some such reason for inaction, a Robinson-Patman Act claim may be put forward and courts may have to decide whether broader antitrust policies or the Congressional intent underlying Robinson-Patman should carry the day.

It seems therefore that Volvo may not have completely resolved the tension between antitrust policies and the protectionism underlying the Robinson-Patman Act.

I would like to talk just a little bit about the dissent. There's an interesting dissent in this case written by Justice Stevens but joined by Justice Thomas—not a very common combination. In addressing this very issue of the conflict between general antitrust principles and the Robinson-Patman Act's goals of protecting small sellers from larger chains, Justice Stevens says that Judge Bork's characterization of the Robinson-Patman Act as "wholly mistaken economic theory" may be correct (126 S. Ct. at 876). Nevertheless, Justice Stevens thought that in applying the statute the jury's decision should have been upheld.

The next case that we would like to discuss here is the *Twombly* case. (*Twombly v. Bell Atlantic Corp.*, 425 F.3d 99 (2d Cir. 2005)). It's a case where Section 1 of the Sherman Act was invoked in a class action against an alleged conspiracy not to compete in the conspirator's respective geographic markets. The markets were local telephone and high-speed telecommunications services.

The District Court concluded the amended complaint did not allege enough facts to warrant inferring a conspiracy. It dismissed the complaint under Rule 12(b)(6), and the Second Circuit vacated. The Second Circuit stated the District Court wrongly applied the Circuit's case law. The Second Circuit said that the lower court, the Southern District, had used summary judgment law rather than the less demanding "notice of pleading" standard.

The complaint here involved Verizon, SBC and the other incumbent telephone companies. What the complaint stated was that it seemed unusual that following the 1996 Telecommunications Act there was not geographic competition between these entities. As one example, the plaintiff alleged that SBC had served customers in the Connecticut area while Verizon was serving customers in the surrounding states, and at least as alleged, it didn't make sense for them not to compete.

The way we would like to proceed here is in some circumstances where Molly may have something to add, I'll invite her to give us her views.

**MS. BOAST:** Sure. I think this case is actually not unique to the antitrust world. The Second Circuit is quite hostile to motions to dismiss. If you've ever had the occasion to practice outside the antitrust area, you certainly know this.

I hesitate to put too stark a cast on this, but it does seem to me that this decision is sort of the death knell to motions to dismiss in conspiracy-based antitrust claims. The Court basically sets out a standard that says that the motion to dismiss could survive only if one could show there was no state of facts in which parallel conduct could lead to a conclusion of conspiracy by a jury. It flatly rejects the notion that you would import the summary judgment standard, the "plus factor" test that we are all familiar with, into the motion to dismiss.

The Second Circuit gets there partly by revisiting some of its own precedent, but also by blaming this on Congress, and falls back on Rule 8 and the "notice pleading" standards, all the while opining that they are quite mindful of the colossal burdens this could impose along the way.

If you combine this decision with some of the class action decisions in the antitrust world that have come out of the Second Circuit, I think you just start thinking summary judgment for your cases.

**MR. KATZ:** Another significant development in the conspiracy front is a government complaint, *United States v. National Association of Realtors* (Civ. Action No. 05C-5140, N.D. Ill. Sept. 8, 2005), but as many of you know,

there is more of a general focus by the antitrust agencies in Washington in this area.

As everyone who has bought a house is aware, access to the listings in the local multiple listing service ("MLS") saves time for buyers, sellers and brokers. Seller-brokers typically provide printouts of such listings to buyers for properties listed by them and other area brokers. With minor exceptions, sellers are obligated to list all properties they have for sale. If a buyer purchases a listed property, the listing broker will share its commission with the selling broker. If the selling broker is also the listing broker, it will retain the entire commission.

The Department of Justice alleged that National Association of Realtors ("NAR"), which according to the complaint governs the conduct of local realtor boards, suppressed new competition in violation of Section 1 of the Sherman Act. This new competition was the delivery of MLS listings through the internet.

According to the complaint, there was a concern in the industry of downward pressure on commission rates because brokers who provided the listings through the Internet would be able to lower their commissions as their costs are lower.

The alleged suppression that troubled the Department of Justice was allowing seller brokers to withhold listings from brokers that provide the data to prospective buyers through password-protected web sites rather than by traditional means, which is by hand, mail or fax. The Government claims the policy permitting limitation on distribution of listing information through such web sites can result, and has resulted, in depriving consumers of the benefits of competition and also inhibiting the use of new technology.

The complaint states that NAR did notify the Government that it intended to change its business practices, but in the complaint the Government states that those changes were not enough, and discrimination continued against those brokers who used the Internet. That litigation, as far as I understand, is ongoing.

Now we are going to turn to Section 2 of the Sherman Act, where there are a number of monopoly cases of interest. One of them is an airline predation case. The one in this case is Spirit Airlines against Northwest Airlines (*Spirit Airlines, Inc. v. Northwest Airlines, Inc.*, 429 F.3d 190 (6th Cir. 2005)). Spirit, which is a low-cost airline, claimed that Northwest responded with predatory pricing and other exclusionary practices when Spirit tried to serve two of Northwest's principal routes, the Detroit-Boston and Detroit-Philadelphia routes.

The district court granted summary judgment for Northwest, but the Sixth Circuit reversed. The Court commented that even if the jury were to find that Northwest's prices were not predatory—because they had exceeded an appropriate measure of average variable costs—the jury must also consider other factors to determine whether Northwest had injured competition. One of the interesting issues I think in this case had to do with whether it would be appropriate to define separate relevant markets for business customers and leisure customers, or whether instead one had to count all people who fly on a certain route.

As we all know, prices can vary substantially on a given flight between the last-minute "business" traveler and the advance-purchase "leisure" traveler. As you might imagine, the competing economic reports turned out very differently in their analysis of pricing and margins, depending on whether one looked at the market as including or excluding the higher-priced business customers.

Would you want to comment on that?

**MS. BOAST:** This was actually one of my favorite decisions of 2005, I think in part for the reasons Elai mentioned, that is to say, this focus on the price sensitive customer as a potentially separate market. But I also like it because the behavior of the major airlines against some of the discounters is something that has been difficult for the Government to attack successfully, as we saw in the Department of Justice's case against American Airlines. Yet, there is a consumer-level distaste for the behavior.

In this instance this court said we really ought to let this get to the jury, and found a way to get around the fairly difficult Supreme Court standards to do that. Whether this is an approach that will be adopted by other circuits or whether other discount airlines will have occasion to—Spirit had a particularly compelling case of course here— But it is an interesting development in this long history of trying to tackle dominance of our major airlines.

**MR. KATZ:** Moving onto another maybe less well-noted Section 2 case, this is an after-market case involving hot air balloons, which Bill and I thought was interesting, especially because it involves hot air balloons that fly over New Jersey, where Bill Lifland lives and where he is today, though I know he would have liked to be here.

The name of the case is *Harrison Aire v. Aerostar* (423 F.3d, 374 (3d Cir. 2005)). In this case the Third Circuit had affirmed summary judgment for the defendant, which had supplied hot air balloons and also sold replacement fabric in the after-market. The opinion is quite extensive, and it relies primarily on evidence of competition in the balloon market, coupled with the absence of evidence of information barriers to lifecycle pricing, or other evidence disassociating competitive conditions in the balloon fabric market from those in the market for balloons.

The point that the Court makes here is if you look at after-markets and just look at market shares, it is common to expect that the manufacturer of the original product would have a high market share in the after-market.

But that really shouldn't end the inquiry in these kinds of cases. Depending on a number of other factors, one should look at what the level of competition is in the market for the original product.

Here the plaintiff had no allegation that there wasn't sufficient competition for hot air balloons. The question then is, when one buys a hot air balloon, is there enough information to incorporate in one's decision the pricing for maintenance and repair in the after-market? The Third Circuit found that there was and ruled for the defendant.

Turning now to a merger decision that we found of interest. The Federated/May decision is one that I know Molly will want to speak about, but I'll introduce it.

This was a $17 billion acquisition of the May Department Stores Company by Federated Department Stores. It involved about 500 department stores under a variety of names. The FTC had investigated and found no cause to sue, but it issued a very detailed statement of its reasons which is a highly welcome development in itself. That was certainly not the first time, but we are seeing more of these closing statements and they are very helpful. The statement provides a useful checklist of factors that one should consider in evaluating acquisitions.

The principal factor in the FTC's analysis was the evolution of suburban shopping malls and other retail formats providing competition to the department stores. So the thinking there was—and I think Molly will be able to elaborate better than me on this—that stores like the Gap and other stores in the modern mall pose competition to Bloomingdale's or Macy's or department stores of that kind. What used to be the department store's role in the past has now become the role of the mall itself and the variety of stores in it.

This history led the FTC to the conclusion that conventional department stores were not in a distinct product or service market. The FTC noted that proper geographic markets were at least as large as Metropolitan Statistical Areas, with the result that there were many alternatives for customers of the merged enterprise.

Another interesting point the FTC noted in its explanation of its decision not to challenge the transaction was that depending on the price and type of product, the relevant geographic market may be different. So as you might imagine, someone would be willing to travel much farther to buy an expensive evening gown than they would to buy underwear.

The fact that the FTC chose not to challenge the transaction doesn't bar others from doing so under our legal system. In fact, five states did mount such a challenge. The states and the merging parties settled the charges by agreeing to divest some 26 stores. The FTC and state attorneys general announcements were released on the same day.

It is not possible to be absolutely certain that the states in such a situation are applying only the antitrust policies of the Clayton Act. They may also be applying other policies, such as maintaining tax rolls against reduction resulting from store closings and other issues of local concern. As in the Robinson-Patman case that we began with, antitrust and other considerations may be intertwined in determining the appropriate outcome of antitrust controversies.

**MS. BOAST:** Let me add a couple of comments on Federated/May. As you can tell, there was a little overlap in the way we each proposed to proceed, so I will pick up later and cover a couple of additional cases that were on my hit list for 2005.

In the interests of disclosure, my firm represents one of the owners of shopping malls that was involved in the interview process in the investigation of the Federated/May merger, so I have a little insight into the industry from that experience.

I found this decision, or this result I should say, interesting for multiple reasons. First of all, over the years looking at grocery store mergers, for example, the FTC had taken a pretty narrow view of competition. It tended to exclude certain types of grocery stores. There was always a big debate about whether Wal-Mart Superstores should be included in the market. And there was a tendency to divide geography by physical barriers, such as highways. It was a convenience shopping standard essentially.

Clearly, although this is a different type of retail outlet, some of the assumptions that were taken in the merger analysis in those cases seem to be falling away. In this particular instance it was pretty clear from what some of the fact sources had to say that you could replicate the variety of a department store today through a constellation of other shops in a mall.

That said, as Elai put it, there is a very clearly understood hierarchy as a sort of unilateral effects approach to which stores competed against which stores. So considerable attention was given to that as well, and whether there was something unique about the retail formats and price points of these chains and how they competed against one another.

Without taking a view on the merits, I will say that I think this is the kind of case where the states' role was completely appropriate; where it was a matter of local impact as much as national impact, perhaps more. It was pretty clear to me, looking at it more or less from the outside, that the states and the FTC didn't see totally eye-to-eye on what the basic theory of competition harm should be.

Hopefully when we finish our comments we will get insight from Jay Himes or some of his staff who are here, who may have something to add, in particular on

how the condition they imposed on the merger is actually working out in practice. I understand they are monitoring closely what's been going on.

Let me back up a bit here, if I can, and just touch on a couple of other cases. When I think about these end-of-the-year reviews, which I am privileged to do because if you get to a certain point in your life they have to find something for you to do, I am always influenced by my own experience but am also trying to think about what I would really care to know if I knew nothing about antitrust law. So the first little cluster of cases that we touched on in our presentation all involve intellectual property. The Independent Ink case—which probably will be discussed by others later in the day, so I won't go into it in great detail—is now in the Supreme Court. This is a case in which an ink manufacturer claimed that its competitor, who also manufactured printer heads, was illegitimately tying purchases of ink to the purchases of the head. In the federal circuit, our antitrust unfriendly appellate court, the Court held that a rebuttal assumption of market power attached to the patent and reversed the District Court's dismissal of the complaint.

When you look at the decision and you see the authorities cited in the brief, you're really left with the impression that the appellants here were trying to position this case for a grant of cert. They brought up things like the Guidelines the FTC and Department of Justice have issued where they take a different position on the assumption of market power, and a lot of lower court authority.

The Federal Circuit seems to make no effort to distinguish all of the Supreme Court cases that are out there. In other words, even though there is some kind of market power in any kind of brand, this doesn't mean that the market power a brand or patent infers is a relevant antitrust market. The court doesn't go there. It just sticks to the Supreme Court precedent and says, sorry, this is where we are under governing precedent. And so the case is, I think, well positioned for the Supreme Court to address its own prior decisions. And needless to say many people will be watching this one.

The second IP related case, one near and dear to my heart, although I am watching it go down, is Schering-Plough, which is one of the several cases involving settlements between branded and generic pharmaceutical manufacturers that we have all watched over the years. In this case the Eleventh Circuit reversed the Commission and said that the question had to be whether the settlement exceeded the scope of the patent. This was of course one of the principal hurdles that the Commission always knew it would have to try to overcome.

But interestingly, the one area where the economists and the lawyers who were suspicious of some of these arrangements seemed to line up was on the question of reverse payments; that is payments that were alleged to keep the generic out of the market. In the FTC's own consideration of some of these cases, this was the feature, although the cases did not depend solely on this feature, this was the feature that had the economists so concerned about the practice.

In this decision the Eleventh Circuit sort of dismisses that as a frivolous concern. It's not enough to raise the level of suspicion that the FTC seemed to give to it. The court was fairly critical of the Commission in this decision.

Still it is a very fact-driven decision. I don't think you can take the Schering-Plough case and apply it to the whole category of Hatch-Waxman cases that we have observed over the years.

Very quickly, the related case, the Tamoxifen case out of the Second Circuit I thought I should touch on, since it is our circuit. The Second Circuit for all intents and purposes adopted the same formula used in *Schering-Plough*. That is to say, you must show that the monopoly is being extended beyond the patent scope. If you can't do that, then you have to show that the patent settlement was truly a sham in the sense of the objectively baseless test under Noerr-Pennington.

I wanted to touch briefly on this *Daniel v. American Board of Emergency Medicine* case, again because it is a Second Circuit case. Again, in the interests of disclosure, I worked on this, but it was so many years ago that I can barely remember. That is another way of saying it has been around for a long time. The case involved a practice of the certification board in the field of emergency medicine that required a residency period before you could sit for the certification exam. I won't bore you with more of the factual details, but it had been up and down on class action issues.

The district court finally dismissed the case on standing grounds, theorizing that the emergency physicians who were seeking certification but hadn't completed these residencies simply wanted to be part of this higher-priced pool of doctors. That wasn't an argument in favor of competition; it was just an argument for their joining the more expensive elite.

The Second Circuit upheld the dismissal on that ground, although there was a dissent by Judge Katzman that I'll address in a moment. I think precedentially, the more important part of the case is the Second Circuit's conclusion that service of process provisions of Clayton Act Section 12 permit personal jurisdiction only where you can satisfy the venue provision. This puts the Second Circuit at odds with the *Go Video* case in the Ninth Circuit. And it's an issue that has bedeviled practitioners for many, many years. So we at least now have another circuit split through which we might look forward to getting some clear guidance from the Supreme Court at some point along the way.

Returning to the standing point for a moment, Judge Katzman I think actually correctly points out that the majority and the District's Courts approach to the standing argument is a little bit too simplistic. In his analysis, if these additional doctors, the nonresidency-trained physicians, had been allowed into the pool of the elite, there would have been more output and prices may well have gone down.

Sticking to my Second Circuit theme here, we had a section in this presentation that covered the *Twombly* case and the *Spirit Airlines* case that Elai had discussed where we note that these were all cases where the courts were reversing more conservative decisions than the courts below, which seemed a little counter-intuitive to me.

The *Twombly* case is probably familiar to many of you. I actually think on the facts there is nothing particularly novel about this case, but since it is a Second Circuit case and many people were involved in it I thought I should mention it. This was one of the cases that came out of the allegations there was the post IPO post allocation process that had various kinds of antitrust problems. The District Court had held that there was an implied antitrust immunity because this was all really subject to regulation by the FTC.

The SEC filed a brief in the Circuit Court that was surprising to me because it said if the following things ensued, then maybe there is a conflict. It wasn't a very strong brief. When you read the Second Circuit's decision you see that they note that there was no statement by the SEC that these "tie-in" and laddering agreements that were the practices at issue in this particular case were prohibited by the SEC, so the room for conflict between SEC regulations and antitrust law application was low to nonexistent. But I think the holding, the tenor of the decision suggests that they don't think very much of this immunity approach in this setting at all.

**MR. KATZ:** Even though, as Molly said, the Court didn't find there was antitrust immunity, the Second Circuit suggested that in these kinds of cases where there is regulation, but not immunity, perhaps rule of reason analysis rather than per se treatment should apply. And I think this flows a little bit from the Supreme Court's *Trinko* decision from a couple of years ago, where that notion is also present. That is, even if the antitrust laws aren't impliedly repealed by some sort of regulatory scheme, the regulation should be taken into consideration, and if it's a case that would otherwise be per se, perhapsCand this is not the holding, but I think the Court suggests it—something like the rule of reason should apply.

**MS. BOAST:** I wanted to touch briefly on a decision out of the FTC in the series of consummated merger investigations that they were conducting. This one involved, and I am sure you all are familiar with it, the Evanston Northwestern Healthcare hospital merger outside of Chicago. The Administrative Law Judge determined, with the benefit of the post-facto evidence of course, that the merger had violated Section 7 of the Clayton Act, and appeal to the Commission is pending.

This is a great opportunity for everybody to sort of take a look at what happens in a merger and for the Commission to demonstrate that it is willing to continue to monitor. Remember that the hospital mergers were the class of mergers where case after case after case the Government lost, and they finally just gave up. So this is a great opportunity to go back and take a look at a particularly sensitive market.

The other thing is that the Commission staff has lodged its own appeal at this point, arguing that they don't need to do a structural market analysis where they had direct effects post-merger. This is another one of these issues that you see briefed all the time and you see it bedeviling people. And my own view is that the case law is relatively clear, that the structural market analysis is a proxy for competitive effects. But as the staff is arguing here, if you have competitive effects, why take the Court or a jury through the structural analysis?

I think one of the concerns would be that if you could have a sort of false positive problem if it's not really a competitive effect attributable to the merger, then maybe you should go through the market analysis to test that. But that wouldn't necessarily make it mandatory in every situation.

And finally, again another case I am sure everyone is familiar with, the *Dagher* case, which we talked about last year. This is a case where the service station owners are challenging the Texaco-Shell joint venture—which has now been unwound in any event—as a form of price fixing. Once the venture was formed, the new entity decided that the two brands would price the same way.

I do recall from talking about this before that there is one speck of evidence in the record suggesting that this agreement to reach this pricing decision predated the existence of the merged entity. But certainly there is no evidence that I am aware of that this was put into effect before the merged entity was created.

The Government has filed a brief in favor of the oil companies in this instance, and I believe oral argument takes place in March.

**AUDIENCE MEMBER:** It already happened. January 10th.

**MS. BOAST:** Okay, good. Maybe somebody can tell us what happened there.

Those are the points I wanted to cover. And we are both available to answer questions. But I'll also invite comments from this sophisticated and knowledgeable audience, who I always feel could be standing up here just as well as I am.

**AUDIENCE MEMBER:** Molly, do you have a view on how the Solicitor General might respond to the invitation for the Supreme Court to submit its views in *Schering*?

**MS. BOAST:** No, I have no insight into how they might respond. I mean to the extent the decision is left to the two agencies, the unfortunate part of it to me—putting on my enforcement hat for the moment, is that this is the hardest case in the whole series of Hatch-Waxman decisions. Bringing the first case was an enormous internal struggle, and there was an enormous sort of backlash in the IP community from the first case.

That said, I remember going up to the Hill one time to talk about whether the Hatch-Waxman Act needed to be amended because of the incentives it created. Jim Griffin from the Department of Justice was there wearing his criminal hat, and he was there to talk about something completely different. But when I outlined the features of the cases that at that point the Commission had brought, he turned to me afterwards and he said you know I am beginning to think we should be pursuing these criminally.

By the time we got to *Schering-Plough* the facts were different, and the Commission is looking at what the boundaries should be, without knowing the answer. One of the hallmarks of the Pitofsky administration was his willingness to take cases into court where he wasn't absolutely certain he would win, but on the theory that everybody should know what the rules are, and the courts are the ultimate decision makers.

So with that predicate, I am not totally sure that both agencies will line up in the same place on this one. I think the facts are hard, but I think there is a way for them to position this so that they argue for reversal. But I bet you money they look for a middle way out, or they say that it is too early—this case shouldn't be the one on which this decision rests.

**AUDIENCE MEMBER:** I just wanted to mention that the Tamoxifen case in the Second Circuit is up for petition for rehearing *en banc* and the FTC has been supportive of the petition.

**MS. BOAST:** Okay.

**AUDIENCE MEMBER:** As an administrative law issue, what do you make of the Eleventh Circuit deference to the findings of the Administrative Law Judge against the findings of the Commission, the factual findings?

**MS. BOAST:** Oh, interesting. I guess without this—I should probably be able to claim more expertise than I can here, but my understanding of administrative law would mean that the Commission is free to make its own factual findings. They are the administrative agency, and they don't have to rely on the fact-finder alone. Which is what happened, is it in Polygram, where the Commission went back and revisited the factual record themselves?

Putting aside that model, I don't see why the Commission should be bound by ALJ's facts, unless their decision is flatly inconsistent with the facts, which I think is part of what was bothering the judge in *Schering-Plough*. But it is such a fact-specific analysis, the Eleventh Circuit in *Schering-Plough*. What is your view?

**AUDIENCE MEMBER:** Well, I think at least there was a statement by the Eleventh Circuit that the fact-finder was the ALJ. And they say, well, the Commission couldn't be right because the facts they found were inconsistent with the facts the ALJ found.

**MS. BOAST:** Yes, I think that is probably not correct under administrative law, but I do think that the Commission is in a better position to argue that point in a situation where they have in fact done their own fact finding which is not a practical model for many of these complicated cases. It's clear that it took an enormous amount of time to get the decision out just because of the fact finding exercise that the Commission had to go through once the decision was reached.

Commissioner, do you have a view on this?

**COMMISSIONER JONES-HARBOUR:** Since it is still pending, I am going to just listen. But I think you characterized it right.

**MS. BOAST:** Thanks, Jay.

**MR. JAY HIMES:** You speculated that the state enforcers and the FTC did not necessarily see eye to eye on the Federated-May analysis. And Elai speculated that maybe we took into account diminished tax revenues or others in nonantiturst considerations. I don't know what happened in other states, but I never heard anybody talk about tax revenues or anything other than traditional Section 7 considerations, and that goes for the Bureau and AG's Office in general. So that was our view of the competitive analysis.

You know, what's going on, I have to say I think I know what's going on, but I am not sure whether it's all public. So I'd better keep my mouth shut in those circumstances. There are people here that work directly on that particular investigation, and they could speak to it if they want.

**MS. BOAST:** Yes, my comment that I wasn't sure the states and FTC saw eye to eye on the antitrust theory was intended to point out what I saw through my little window on it was that it was purely driven by Section 7 type considerations. Yes, sir.

**MR RICHARD GRIMM:** Yes, Dick Grimm, I am in the Antitrust Bureau, in the State Attorney General's Office. I think on overall antitrust issues in the Federated matter, we and the FTC did not have radically different

views. It simply was as you suggested, Molly, that we focused more on the local and micro effects than the FTC did. It was also our perception that in certain markets there probably was more head-to-head competition in a traditional sense between department stores than was the case in a lot of other markets. That included New York, where consumers had decided preferences for traditional department stores. So you can still make that same kind of case.

I think what I would characterize as a settlement in this case also stemmed from the five states' willingness to perhaps compromise more than the federal agencies are in certain situations. The federal agencies traditionally have taken the view, and we usually do ourselves but not always, that one identifies precisely the full anticompetitive effect and then the decree, if there is a consent decree, has to solve that.

We in this particular one, it was our view that there was a certain force to some of the arguments on the other side about an erosion of traditional department store markets and we certainly faced some of the arguments that some of the properties that Federated was acquiring were not any longer very suitable for being traditional department stores, because the stores weren't large enough and for other reasons. Therefore, we were willing to enter into the deal we did. And as Jay suggests, it is still being worked out, so I don't want to comment exactly on where things are.

**MS. BOAST:** But I think your observation that the greater flexibility that the states may have in thinking about what's an appropriate remedy is a very legitimate concern. It was obvious to me that the traditional FTC approach to remedies was going to be a problem.

**MR. KATZ:** Insofar as the speculation about the state AG's motivation was incorrect, I stand corrected. But in a situation such as this where the FTC provided in more detail than usual an explanation of why they thought there wasn't an issue, the silence from the states may have fueled such speculation, even though it may very well be incorrect. I think it would be interesting to hear, although I understand it may not be the right time now to hear it, how the application of the same statute by the states which perhaps have better knowledge of their local conditions might result in a different conclusion.

**AUDIENCE MEMBER:** I have a question. I didn't have any involvement in this matter. But up to now most of what we are talking about is the product market and whether the department stores compete head on, you know, whether the division between department stores and shopping centers has changed. But your comments about the micro level made me think was there a distinction in the way the FTC views the geographic markets as well; would that have led to a different outcome?

**MR. HIMES:** As to the different properties, that was an assurance of discontinuance was the document that we came up with rather than a traditional consent decree in federal court.

Yes, I think the states did tend to think that in most, as to most of the stores the markets were geographically somewhat tighter than the FTC thought.

Now, bear in mind that the FTC was looking at the whole country and was considering many, many markets, and therefore, they had a fairly standard way they looked at the situation. There wasn't all that much focus during the investigation on differences that we might have observed between one market and another. So you know, basically the answer to your question is yes, even though if you talked to say the FTC staff, they would probably concede that markets are geographically tighter in some places than in others.

**MS. BOAST:** I think we are going to have to cut off this conversation and continue it during the break. There is a little paper summarizing all of the decisions both of us have discussed out on the table, with the exception of the balloon case because before today I didn't know there was a market for balloons.

Thank you very much for your attention this morning, and enjoy the rest of the day.

# Efficient Integration or Illegal Monopolization? Package Licensing, Economic Bundling and the Antitrust Principles Applicable to Common Business Strategies of Leading Firms

**MS. GOTTS:** The next panel I think actually wins the award for the longest title: "Efficient Integration or Illegal Monopolization? Package Licensing, Economic Bundling and the Antitrust Principles Applicable to Common Business Strategies of Leading Firms." I am a merger lawyer, so I think that means dominant firm conduct, short and simple. But we'll hear from the panel to know whether my translation works or not.

Actually, when I was asked to put together this program the first person I called was Mark Popofsky, who is going to be the panel coordinator here. Because Mark actually lives this stuff. So I asked him to put together a panel, and the panel he put together exceeded my wildest expectations. This is just wonderful to see the panelists he was able to recruit. I look forward to learning everything there is in this area.

I will introduce Mark and then turn it over to him. Mark is a partner at Kaye Scholer in the D.C. office. Prior to joining Kay Scholer, Mark was at the Department of Justice where he was both an attorney in the Antitrust Division's Appellate Section, handling among other things the Nippon paper case, which is something I even knew about. At the end of his term there he was senior counsel to the Assistant Attorney General.

He is currently not only practicing law, but an adjunct Professor at Georgetown University Law Center. He is a graduate of Harvard Law School, and a law clerk on the Ninth Circuit.

With that, Mark, I am going to turn it over to you to introduce your panel.

**MR. POPOFSKY:** Thank you, Eileen. It is a pleasure to be here. I thank the State Bar Association. It is a pleasure to also see so many familiar and friendly faces.

Well, our title today may be long, but hopefully our presentations will be crisp, at least that is our hope.

Some of you may remember back in the Jurassic period of the *Nippon* paper case another case called the *Microsoft* case. I was privileged enough to work on this case, alongside Doug Melamed, my former colleague, and Rick Rule also had been involved in that case.

*Microsoft* is important among other things because it brought to the public fore the issue of bundling items, IP rights, the whole practice that spans the spectrum we call tying or quasi-tying arrangements. Bundling is not only ubiquitous in the *Microsoft* cases, it is ubiquitous in the American economy, from the multiple services we acquire from cell phone providers and cable companies to the software installed on our PC. Bundling is not only ubiquitous in the economy, it has been ubiquitous to us in the antitrust arena. Well before the *Microsoft* case we had the Motion Picture cases, *Jefferson Parish* and all of the cases most of you are familiar with.

Those cases and *Microsoft* it turned out were only the beginning and not the end of the antitrust issues respecting bundling. *Microsoft* has spawned a number of what I'll call the post-*Microsoft* issues in this area, which we are going to focus on today. One is the packaging of IP rights in licensing, and the practice known as economic bundling of royalty discounts, which reached its public fore in the *LePage's* case.

These are issues which are not only important to many of our clients in the real world, but are also frequent topics of antitrust litigation. Plaintiff's lawyers, which I occasionally am, love tying cases. You get the benefits of the per se rule, and we'll see if the Supreme Court leaves in place, or as everyone believes, will overturn the presumption of market power that arises from a patent in the *Illinois Toolworks* case. And the *LePage's* case in the Third Circuit has certainly led to a whole cottage industry of suing dominant firms over their practice of economic bundling.

We have a distinguished panel here to explore those issues today. At my far right Dara Diamond. Dara is corporate counsel of Pfizer Inc. and former attorney at the Hughes Hubbard firm. Her responsibilities are in the antitrust area at Pfizer. She's an alum of Federal Trade Commission where she served, among other positions, as attorney advisor to then Commissioner Thomas B. Leary.

To my immediate left, Doug Melamed, old friend and colleague. A partner at Wilmer, Cutler, Pickering, Hale & Dorr in Washington D.C. I think now they call it Wilmer Hale. Maybe he can give a tutorial later on law firm mergers. His 30-year antitrust practice has spanned the gamut of litigation, counseling, mergers. He is a noted author and frequent speaker on the issues we are going to discuss here today. Doug served in the antitrust division, among other positions, as Deputy Assistant Attorney General and as acting AAG at the end of the Clinton Administration.

To Doug's left is Rick Rule. Also an alum of the Antitrust Division. Indeed, Rick was the youngest AAG ever confirmed at the Justice Department, 31 or 32. We were just trying to figure it out when Congress confirmed him.

Rick is a partner at the Fried, Frank firm in Washington, D.C. He is a distinguished antitrust litigator and counselor and expert on the issues here being discussed.

Last but certainly not least, to my immediate right is Professor Bobby Willig. Bobby is Professor of Economics and Public Affairs at the Woodrow Wilson School in Princeton, New Jersey. He is a former Deputy Assistant Attorney General at the Antitrust Division for Economics, and has served on numerous editorial boards and government agencies and is eminent in the area of antitrust and industrial organization.

With that our format here today is going to be as follows. We are going to have short presentations to tee up these issues by three of the speakers. We will then have moderated discussions, and we will leave plenty of time at the end for your questions.

With that I would like to turn it over to Doug to kick us off to discuss the issue of bundling IP rights. Doug.

**MR. MELAMED:** I am going to talk briefly about recent developments in patent pools because patent pools, I am sure you all know, are increasingly important in our economy, particularly in the information technology sector and because I think these developments illuminate more broadly some of the principles and analytical issues that arise with bundling questions in other areas.

A patent pool of course is a package of patents that are held by multiple firms, although you could use the term pool I suppose to include a package of patents held by a single firm. But the important point is that multiple patents are licensed together in a package. Patent pools have a number of procompetitive benefits. They reduce transaction costs by providing in effect one stop shopping. They can integrate complementary technologies like a product tie, a car and radio for example. They can clear blocking positions among patents. This is a little more than just the other two. What I have in mind here is this: Suppose that in order to build the widget you need a license to Company A's patent and to Company B's patent; they are both essential or blocking patents that can prevent the development of the product. If they were licensed separately by individual firms, the combined price that one would predict would exceed the price that a single firm or single licensor would charge for those patents. That is the familiar double marginalization point. Patent pools can avoid the risk of infringement disputes, because by throwing a lot of patents together in a package you eliminate the possibility that you would have a dispute over an alleged infringement of a patent that might have otherwise not have been licensed because it wasn't in the package.

On the other hand, patent pools can possess competitive risks. One risk which I am not going to spend much time on but I want to pause over is that they can be in the nature of price fixing. Imagine that Company A has a patent that would enable the manufacturer of a widget, and Company B has a patent that would enable the manufacturer of a widget. They are not blocking of one another, but rather they are substitutes for one another. They are alternative or substitute technologies for what is a functionally equivalent purpose. They could be sold in competition with one another, but if they were combined into a pool, it could be like Coke and Pepsi combining their products into one package. You could characterize that as a kind of price fixing.

The issue I want to talk about is different. It is the anticompetitive risk that could come about that is similar to tying— the bundling of patents that may not be substitutes for one another but are not necessarily blocking patents either. That is to say patents for which there might be substitutes elsewhere offered by others. In other words, even if none of the patents is a substitute for another patent in the pool, and even if they are complements for one another, the pool might harm competition between patents in the pool and substitutes outside the pool. The reason is that if the pool gives you a license to a set of patents, and then the competitor comes along and says why not take my technology, why not buy my radio for your car, if you're a car manufacturer. And the car manufacturer might well say I've already paid for a radio, why should I buy yours? And so the pool can have the effect of excluding or at least disadvantaging suppliers of competing technologies.

It's worth noting that the harm that a patent pool can cause comes only because of the reduced incentive to purchase the substitute technology outside the pool. Because ordinarily a patent pool does not require a licensee to use all the patents in the pool. So there is no contractual prohibition. It is not like exclusive dealing or a tie out clause in the contract. But there can be an effect in the sense that I already paid once, which means that the competing technology outside the pool has to be that much better than the technology in the pool in order for the licensee to choose to pay a second time to get it.

One other element. There probably can't be any competitive harm from a patent pool, anymore than from any other bundling or tying arrangement, unless at least some of the patents in the pool have market power. If for example, there is a technology that is essential to making a car, and it is essential to either all cars or a particular car that has market power, then the technology would have market power. Absent market power, one wouldn't worry about the competitive effects of the pool.

Now, none of the competitive harms can occur if all of the patents in the pool are essential for the purpose for which they are licensed. If they are all essential, they are all blocking patents in the sense you need them all to make the car or widget, then by definition they are not substitutes for one another but rather complements of one another. And by definition there are no substitutes for any of them outside the pool. I am assuming of course that the license has an effective field of use, and that all of the patents are essential for the licensed use.

Under principles applicable to ordinary tying arrangements, a patent pool that includes only essential patents would not be unlawful. *Jefferson Parish* I think is the key case here. It held that tying involves mandatory packaging of separate products, and that separate products means that there is a separate demand for each of the products in the package. If you need all the patents for the licensed use, there will not be separate demand for the different patents for that use.

In a series of business review letters beginning in 1997, the Justice Department said, to oversimplify, that it would not challenge pools that included only essential patents. The first of these business review letters approved a patent pool that was confined to patents for which there was no technical alternative. That is to say patents for which there was no infringing alternative. There is no other way to make a product comply with the standard for which the pool was being licensed, that didn't literally infringe the patents in the pool. Later, the DOJ business review letters broadened the notion of essentiality to include patents for which there is no commercially realistic alternative. The notion being maybe there is a way to design around one of the patents in the pool, but if it's more costly or impairs functionality in some material way, it wouldn't be a commercially realistic alternative. And in that case, you would deem that patent to be an essential patent.

So there was I suppose at the turn of the millennium a conventional wisdom: Patent pools are okay if they include essential patents, but they are not okay if they include both patents that have market power and nonessential patents. That is to say, patents for which there might be commercially realistic alternatives. This shorthand conventional wisdom was consistent with *Jefferson Parish* in the notion of separate products, and it was consistent with the *Paramount-Loews* cases, which in a somewhat different context had condemned block booking of copyrighted films and the lower court cases that dealt with patent pools.

That conventional wisdom is not quite right, both as a matter of policy and as a matter of law. After the Federal Circuit's decision of the *Philips* case in the fall of '05, I think it is clear that even where the licensor has market power, a patent pool cannot be regarded as anticompetitive simply because it includes patents that turn out not to be essential.

To explain why I think this makes sense and a little bit of the logic in the *Philips* case, I am going to back up for a minute and talk about why bundling is anticompetitive. A patent pool can injure competition in the same way that a tying arrangement or any kind of mandatory product bundle can injure competition if one of the products in the bundle has market power. The anticompetitive story is that instead of maximizing its profit on the product or the patent over which the seller or the licensor has market power, the seller or licensor uses some of the market power of that product to induce customers to pay for or use a second product, a tying product (such as nonessential patents in the pool).

In effect, the seller sacrifices profits from the first or tying product, or leverages that product, in order to enhance the value or generate additional sales of the second or tying product. And under some circumstances, that can enable the licensor, the seller to gain additional market power.

Now, in a patent pool the situation might be very different. The reason it might be different has to do with an attribute of patents that is different from most other kinds of property. And it is that patents are deliberately, profoundly uncertain. For reasons having to do with the efficiency of the patent process, our laws have a relatively perfunctory review of a patent application prior to the issuance of a patent and leave for later litigation the hard digging to determine whether the patent really is valid and what is the real scope of the claim. What does it really mean? And are our competing technologies truly infringing or not? So at the time one gets a patent, there is substantial uncertainty as to the validity and proper scope of the patent.

So imagine the following, probably common story. A bunch of firms get together to develop a new product. In *Philips* case it was recordable CDs. They get together to develop a new product. They pool their patents and know-how; they develop a standard for the product. There is no market for it. They go to manufacturers and say, I've got a great idea; I want you to invest a few billion dollars in fabricating plants to make this new product. And all you need from us is a license to our patents. The manufacturers, being in the electronics products business, are familiar with this and they study it, and say this is a great idea. Risky to be sure. It's a new product, untested in the marketplace, but it is a new product we are willing to invest millions of dollars in. And we want a license to your technology.

Then the would-be licensees and would-be licensors come to the following realization: We are not sure exactly which patents we are going to need. Which patents we might wind up infringing in order to make this new product. And the would-be licensees are presumably thinking, or the licensors are thinking they will think: If I get a license to the ten patents these guys came to me

with, how do I know they are not going to come back to me two years from now, after I make sunk investments in the business, and say I happened to find in my drawer another patent, and you're infringing it, so please pay me a second time.

So what the licensee will say or want is some insurance, as it were, that he is not going to be sandbagged. And I am not talking about deliberate sandbagging or fraud. But I am talking about discovery by all these parties that there are more patents and claims out here than the initial patent.

So the licensors create a package and say, I am going to give you a license to everything I can imagine that might be in this field. What I am really giving you is not a license to individual patents; I am giving you a license to make this new product without fear that I am ever going to sue you for infringing. So we have a broad patent pool.

Now, in this situation the licensor is not trying to use the strong concededly blocking products to enhance the value of the questionable patents. He in effect is using questionable patents to enhance the value of the strong patent. One might think of an anticompetitive tie as a "leverage tie"—from the strong to the weak—and of a patent pool as entailing an "insurance tie," where what the licensors are providing to the licensee is insurance that he is not going to wind up being sandbagged. In that situation the licensor does not gain additional market power by licensing additional patents. The market power comes from the fact that he owns blocking patents, and everybody needs to pay the toll to him to make the product. The value to the licensor from the package comes from the insurance benefit to the blocking position, not leverage into new market power.

The *Philips* court basically held that that is okay. That even if it turns out in hindsight, five or ten years later when you're having litigation, that some of the patents in the pool prove not to be essential, that the pool does not become anticompetitive or tying, because essentially of this insurance notion.

I think that in order to be regarded as an insurance pool the following conditions are probably necessary. First, that the licensors had a reasonable good faith belief in the outset that the patents might be essential when they included them in the pool, or at least that the licensees were uncertain about that and wanted some assurance on this.

Second, that the royalty—this was important to the Federal Circuit--that the royalty charged for the pool of licenses did not vary depending on how many patents were in the pool. Because if you change the price when you add a new patent or take one out, you begin to create the impression that you're licensing each patent for its incremental value rather than simply selling an insurance policy.

Even in a pool, first, regarded as an insurance pool, rather than as a leverage tie, competition can be injured. It can turn out that the supplier of a competing technology is disadvantaged, because if everybody had known the patents in the pool were not essential and they had taken the nonessential patents out of the pool, he would have had a better crack at selling his competing technology.

So one might not say that a so-called insurance pool is a safe harbor. Rather, that on certain facts, a disadvantaged rival might be able to make out an antitrust claim against even a so-called insurance pool. In order to do that, and I think this is implicit in the *Philips* analysis, you would have to find, first, market power with the blocking patent. Second, that the licensors had fair notice that the licensees didn't want certain patents in the pool, and that there is a legitimate basis for their view that they don't need this patent, and nevertheless insisted on keeping it in the pool thereafter. Third, that the licensor knew or should have known that there really was a bonafide alternative—that the patent wasn't essential, and that there were noninfringing ways to make standard-compliant products. Because without that, for reasons I won't take the time now to explain, there are ways that licensees can opportunistically try to reduce the royalty. And finally, that there is some reason to believe the pool really does have an exclusionary effect. And that probably means that the challenger has to prove that the price of the pool was increased because of the inclusion in the pool of the particular nonessential patents that it does not want.

But short of proving all of that, it seems to me a patent pool that has this insurance feature is, after the *Philips* case and correctly so, not anticompetitive. And I think some of these principles about what's the purpose of the pool, what product is being promoted by it may have broader ramifications for bundling law.

**MR. POPOFSKY:** Okay, Doug, thanks for setting the table with that topic. We will switch gears to Dara to talk about our second topic, economic bundling and royalty discounts.

**DARA DIOMANDE:** Good morning. Let me start off by saying that the position and views I express here are my own, and they don't necessarily reflect a position or stance by Pfizer Inc.

My goal here today is to give you an overview of the evolving legal treatment of economic bundling, commonly referred to as royalty or bundled rebates and discuss how broad prohibitions on certain forms of bundling can actually harm incentives by leading firms to innovate.

Economic bundling in particular is somewhat relevant to the pharmaceutical industry in that the limited case law that is out there primarily involves pharmaceutical companies and has a significant impact

on them. In fact, just two or three months ago a subsidiary of Johnson & Johnson filed an antitrust case against Amgen, claiming that Amgen's bundled rebate programs violated the antitrust laws. So the topic is particularly timely.

So let's start off by defining what bundling is. Essentially, a bundling arrangement is an arrangement to sell products either at a rebate or a discount as long as they are sold together. The difference between a bundling arrangement and a tying arrangement is that in a tying arrangement a seller can distance the sale of one product upon the purchase of another. In a bundling arrangement, the products are sold actually as either part of a package at a discounted price, or individually.

Now, volume discounts also offer rebates and lower prices. However, those prices and rebates are based on the purchase of one single product, and based on the quantity of the product that you're purchasing. Some common benefits and examples of bundling that we use in our everyday lives are the package services that we all use by the phone companies. We would get call waiting and call forwarding and voice mail at a discounted rate. Also using travel web sites that bundle airline, hotel and rental car services at a lower price is another common example of bundling. And the most common I think that we use in our pop culture today is these combo meals that you get at fast-food restaurants where you get a hamburger and a drink and a side for a lower price. Unfortunately, I take advantage of that. But that is a typical use of bundling that we see in our everyday lives.

The case law in 2003, the Third Circuit, for reasons known best to God, since they failed to provide any guidance on the matter, issued an *en banc* decision that has brought the law of economic bundling from a point of coherence into chaos. And although order often comes out of chaos, I think it is important to understand how we got from point A to point Z.

So let's start off with the first reported case really focusing on bundling, a case that is the *Smith Kline/Eli Lilly* case. In that case Eli Lilly had a legal monopoly in a specific segment of the antibiotics market. Two of Eli Lilly's drugs were patent protected and the third drug was off patent and did not face significant competition until Smith Kline entered the market. When Smith Kline entered the market, Eli Lilly offered a bundled rebate program which conditioned the rebates on the purchase of at least three of Eli Lilly's drugs.

Smith Kline was actually able to show that in order to match the impact of the rebate it would have practically needed to give its products away and could not profitably compete with Eli Lilly's bundling scheme, and because Smith Kline was able to make this showing, the Third Circuit ruled that bundling violated the antitrust laws.

Now, critics of the *Smith Kline/Lilly* case argued that this was essentially really a de facto tying case. The theory is that the rebates being offered by Eli Lilly were so attractive that it was essentially not economically viable or realistic for anyone to purchase these three drugs individually.

We then move from 1978 to 1993 to the *Brooke Group* Supreme Court decision, which in fact is a Robinson-Patman monopolization case, but it is often used in analyzing the legality of bundling rebates. So it is worthwhile mentioning here.

In this case a small cigarette manufacturer sued Brown and Williamson alleging a scheme or predatory pricing for generic cigarettes. Brown and Williamson had about a twelve percent market share and the Supreme Court ruled that their alleged predatory pricing was not an antitrust violation, unless the pricing was below cost.

The next case focusing on bundled rebates is the *Ortho v. Abbott* case in 1996. In that case, Abbott, a manufacturer of five commonly used tests to screen viruses in the blood supply, had about 70 to 90 percent market share in three out of five of those tests. Ortho, a competing manufacturer of blood screening tests, alleged that Abbott abused its monopoly power by packaging these five tests together and offering a bundled rebate that allegedly foreclosed competition. The Court actually ruled in favor of Abbott and held that a plaintiff to prevail on such a monopolization case involving bundling rebates either had to show that the challenged pricing was below cost or that their plan could not profitably compete with the challenged pricing plan.

What's interesting about this case is that it adopts the rationale previously articulated in the *Smith Kline/Eli Lilly* cases as well as *Brooke Group* and uses it as support for its ruling.

Then we get to 2003, which is the infamous *LePage's* case, and where we leave coherence and go into a round of chaos for economic bundling. In the *3M* case, 3M Scotts had a 90 percent monopoly share of the brand. LePage entered that market with a private label tape priced significantly lower than branded tape. 3M responded by offering its open private label tape, which is fine. It's actually behavior we want to see in a competitive market. Then what happens is 3M sets up a rebate program where in order to get the rebate customers have to meet purchase quotas across all of 3M's product lines, which include their branded scotch tape as well as their private label and some other 3M products. Now, it is important to note that even with the rebates all the pricing offered by 3M was above cost.

The Third Circuit ruled that the bundled rebates triggered antitrust liability even though they were not below cost pricing, and that a plaintiff wasn't required to

demonstrate it was unable to compete in order to find a Section 2 violation.

Unfortunately, the Third Circuit did not articulate or provide any guidance of what plaintiff did need to show to find an antitrust violation for bundled rebate programs. The Third Circuit distinguished *Brooke Group* by alleging that *Brooke Group* didn't apply, because it was a Robinson-Patman case and didn't involve a firm with monopoly power. This is a classic example of bad facts equaling bad law, one of the reasons why the Government urged the Supreme Court to deny cert in this case.

I think a final twist that is important to note on this matter is that 3M had a lot of documents which said that the purpose of the bundled rebate program was not to compete in the private label market but actually to destroy it. And they want to do that so they can preserve their monopoly power in the branded tape market.

So the truth about bundling is this: Price cutting is competition in its most classic socially desirable form. It results in more goods to more people at lower prices and significant pro-competitive benefits.

I think the Second Circuit said it best, in that the antitrust laws should not be used to require businesses to price their products at unusually high prices so that less efficient competitors can stay in the market.

There is a legitimate concern about bundling with firms that may possess monopoly power. And I think the concern is obvious, that dominant firms can drive competitors out of the market and then use their market power to recoup losses, increase prices and enjoy monopoly profits. This can occur even if the pricing is below or above costs, because even with above-cost pricing, if it is so attractive it can amount to a de facto tie.

The problem with the *LePage's* case is that it essentially holds that the mere linkage of a monopoly product with a competitive one is the relevant factor that triggers antitrust liability. The other problem with the *LePage's* case is that it is being used now by firms that do not want to lower their profits to insulate themselves from competition. This hurts not only consumers and competition itself, but it hurts innovation. The research based pharmaceutical companies are the champions of innovation, and the *LePage's* decision threatens that incentive to innovate.

The social value of the pharmaceutical industry is profound. It extends lives and improves the quality of them. The opportunity to financially benefit from innovation provides the necessary investment in funding needed to back the research and development that is necessary to provide new drugs and discover them. In 2004 alone, the investment in research and development by research-based pharmaceutical companies topped $50 billion.

So what we are left with is an understanding that bundling is good, particularly if you like fast food. But bundling by monopolists can possess some risks, now that we are in the post-*LePage's* era. Now there is no brightline between above and below-cost pricing. And since firms value predictability with no brightlines and no safe harbors, we are down around where innovation as well as consumer welfare is threatened.

Thanks so much.

**MR. POPOFSKY:** Thanks, Dara.

We are going to hear from Professor Willig to give some economic context to these issues, and then I'll open it up for moderated discussion, and we will go on from there.

**PROFESSOR WILLIG:** I like it when you look at me instead of the slides. I want to control your eyeballs. A bundling sort of thing, the left eyeball and the right one should move together.

So it's been presented to you that we really have two different themes for our discussions today, one "the economic view of bundling" and the other the "IP view of issues that arise squarely on the patent side of the ledger." I think it's really all one. Integration is always good on the intellectual front, and I am going to come back and yell at Doug later about how we usually agree on these things, and we are not agreeing enough yet on this dichotomy between intellectual property and pharmaceutical and other kinds of product issues.

I can't tell you about the law with any degree of professional expertise, but I am here to talk about the economics of bundling, tying, bundled discounts and such practices when they are monopolizing and when they are only merely allegedly monopolizing but not really. I think there is a spate of cases with those allegations that when it comes to economic analysis the revelation is that there is no real monopolization at stake whatsoever.

Nevertheless these are tough issues. It's tough to truly assess monopolization from an analytic perspective for two intrinsic reasons. The first reason is that these practices really can in principle harm competition. There is no doubt about it, there is coherent logic that suggests that bundling and tying and even bundled discounts, which on their face might be attractive for consumers, do conceivably have the potential of foreclosing markets to rivals where rivals need the unforeclosed scope of the market to be effective competitors. The bundling and tying practices really might be weakening competitors, forcing them to exit and creating a longer lasting position of monopoly power for the firm that starts out dominant and becomes more entrenched through these kinds of business practices.

These are the plaintiff's theories that one hears, and there is absolutely a logical possibility for the reality of such a strategy on the part of dominant firms. That is what makes it tough. Because there is another side to it which in my mind is more often predominant, and that is these very same kinds of practices that have that potential are quite generally good practices for consumers, good practices for competitive profits, and very much a part of the competitive interaction in very ordinary markets of the kind that we see clear across the economy.

There is a marvelous fact of which I am proud to be part of the genesis in economic theory, holding that volume discounts, as an example of "complex pricing," nonlinear pricing, bundling within the same product or bundling across products or bundling of different patents or all manner of linkages between products and their pricing is the kind of practice that is actually necessary in frequently encountered kinds of modern economic markets and necessary for true optimality and for the true full realization of consumer benefit.

This is not advocacy, this is not kind of pop legal economics. This is a classic result in pure economic theory, which I think, for an economist anyway, sets the context over on the other side, saying that sophisticated pricing is generally a good thing in a modern market. I do want to show you the economist version of that picture. Look at that. Who is taking economics here?

I don't have time to set the groundwork for you, but if you look at the bottom picture, that is a demand curve and the price of 300, the high price is the ordinary uniform or linear price. What's going on here is the demonstration that if we have one alternative and that is a price at 300, the amount that people choose to buy at that price is given by the anchor of the vertical dotted line. That is the amount that people would be buying at a price of 300. Our vendor is setting a price of 300 above marginal cost, not necessarily because of monopoly power, but perhaps because of the need to recover the fixed costs of pharmaceutical R&D or the fixed costs that lie behind the creation covered by the patents, or even the costs of mounting the aircraft in an aviation market. Fixed costs abound, and therefore the need to price above marginal cost is quite generally prevalent in a modern economy like ours.

Wherever that price is above marginal cost, it makes sense to do what that diagram shows that our firm is doing. The firm says look, pay $300, but if you'll buy 10,000 units in that example, at $300 per, we'll give you a break on any additional units you care to buy. You can have anything else you like at $150 a unit. It is a volume discount; it is a nonlinear price. It is the simplest example of such. The diagram reveals that that added option to buy at the volume discount is first of all obviously good for consumers. Some consumers will avail themselves of that opportunity, so it's good for them. It is also good for the seller, because the seller gets the opportunity to make more sales at the $150 price, which is still above this marginal cost. There is still a margin there. It is a smaller margin, but it is still in addition to the firm's net returns, helping the firm to compensate for the fixed cost that it expended to get the product going, to invent the product, to allow the aircraft to fly and so forth.

So the economic theory says that the opportunity to do nonlinear pricing in the form of the volume discount is actually necessary for what we call Pare to Optimality, the simplest measure of social welfare. You can make everybody better off by permitting a firm like this to implement nonlinear pricing.

The very same construct, the very same diagram applies to bundling. Instead of those 10,000 units going off at $300, that could have been the customer's normal purchases of branded scotch tape, in a case like *LePage's* for example. And the offer to the customers could be "look, if you buy some normal amount of scotch tape at the normal price we will let you have all this unbranded private labeled stuff, at a special discounted price. And you can't have that discount price unless you have first bought your normal amount of the branded tape." The very sort of thing that exercised the Court is just another labeling of the axes on a diagram like this that economics says is really essential for full consumer benefits in a market where fixed costs are prevalent so that ordinary pricing has to be above marginal costs.

The whole concept of thinking that sophisticated pricing is an object of suspicion is really antithetical to classical economics. Those who go on and make a career out of saying the opposite are simply not representing the state of our quasi scientific knowledge accurately, in my view anyway. You can say I take a dim view of some of my colleagues on this subject.

So I think when we come to an actual assessment of a set of practices for monopolization, there are two overarching phases to what we need to do to reach a sound analytic conclusion. The first phase asks whether the challenged practice of sophisticated pricing has actually harmed competition or whether, if it is in the incipiency, there is in fact a dangerous probability that it will do so. I would like to say that for most of the cases that I've seen, not all perhaps but for most of them, the charge of monopolization through bundling should have foundered on that step alone. And that is not a particularly sophisticated step. It is more of a just heads up, keep your eyes open, keep your eyes on the right question, sort of a phase of the analysis. It doesn't need a lot of deep economics. The question is: Was competition really harmed? Or was it just that some rivals couldn't really make it in the environment where consumer benefits are being optimized through the use of sophisticated pricing.

I'll go through a check list if I have time to show you how to do that kind of analysis.

The second phase I think validly comes up less often, although if you are sensible and mounting a multifaceted defense, then of course one has to proceed right to the second phase simultaneously with the first. The second phase posits well, maybe the practice really did harm competition in the sense that it knocked out rivals who really had no place in a fully efficient equilibrium because they are less efficient, but the demise or the weakening of those rivals actually did support some more monopoly power on the part of the dominant firm.

Suppose we have that situation. How do we know whether nevertheless that practice ought to be condemned or whether instead it should be applauded as being part of competition? And I have four synonymous ways to articulate that step. To a lawyer they are probably not exactly the same, but to my economist ears they sound the same. First, is the harm from the practice willful, using Grinnell language? To me that is much the same as asking whether the practice is actually part of competition, which will not often eliminate an efficient rival. So willfulness and being part of competition I think are true opposites in this kind of analysis.

Today, DOJ talks about whether the practice "makes economic sense." Which to me is a fine way to articulate the very same kind of analysis, and often courts will talk about whether there is a sound business rationale. I would like the lawyers actually to come back and tell me whether those are really all the same or not. Seems to me like they ought to be. But if they are not I would like to learn why.

So how to assess harm to competition? We start out with the relevant market. We have to ask whether the practices were causal in terms of eliminating or weakening rivals, not just any rivals but rivals whose number is scarce and whose ability to be replaced is not necessarily strong. So if a particular firm were knocked out with a sound practice, is that going to weaken competition as a side effect, because there are not enough rivals and the weakened firm won't be replaced by another one which is perhaps stronger, since the market doesn't have those opportunities. This is obviously a structural analytic step and clearly a very important one.

I think the most important point here is to get us all to agree that a finding of loss of share or loss of margin by the rival is simply not enough to show harm to competition. That is not what competition is about. Competition is in fact jockeying over market share, where the margins are very much at stake. In most of the cases that I've seen, actually the sum total of plaintiff's evidence just comes to, oh, we lost share, we can't price the way we'd like to, there is harm to competition because we are an important part of competition. That is not enough for a responsible finding of harm to competition. After all, the bundled discounts may very often be good deals for the consumers. And so the real bottom line question focuses on those consumers who are not availing themselves of the sophisticated pricing of the bundled discounts.

What is their loss? Has their ability to shop been deteriorated by the impact of the sophisticated pricing? Have their prices gone up? Has the R&D necessary by rivals to offer better products to them, has that R&D dried up because of the sophisticated pricing? These would be the legitimate indicators of possible harm to competition, but usually, at least in the cases that I have seen, plaintiffs don't bring forward evidence of that kind. And the defendant's evidence, which often does go to those issues, is sometimes ignored by the Court which just sees bad facts or unpleasant internal memoranda and allows that to replace the pertinent economic analysis.

Okay, so let's say there is harm to competition. Now, analytically we are in a more difficult frame. The question is whether the practices that caused that harm ought to be condemned or not. The reasons for great caution here of course is that competition is the valid policy goal for antitrust as well as lots of other economic policy, and so conduct that is a part of competition should not be discouraged by condemnation just because it turns out to be successful in stealing market shares from rivals. This would be a counterproductive use of the whole framework of antitrust law. And I fear in this area of bundling and sophisticated pricing, that is very much the state of policy post *LePage's*.

So getting beyond that admonition, how do we do the analysis? The first question again is whether the accused practices have been proven to be good for consumers. One way to test the validity of the practice is to see whether other firms use that kind of a practice in a similar setting, other firms who are not involved in being accused of predation or of monopolization. If so then, this is truly an ordinary business practice. That is a fairly easy analytic step to go through on the defense side.

Doug and I usually agree on the question of sacrifice. Do the challenged practices make sense for the business? Are they profitable for the business, even without taking into account any of the impact on monopoly power that is alleged by the plaintiffs? It's the ordinary kind of sacrifice test, and I think that applies here in a very unique form.

Take this example, because the way the Court talked about *LePage's* and other courts talked about what is the applicable measure of cost doesn't exactly meet I think the rigor of economic analysis. Suppose there is a firm with a terrific product, such as scotch tape say. This is the cartoon version of scotch tape though, since I don't know the facts of that case very well. Everybody is buying a certain amount of this must-have product since it is terrific stuff and as a result the firm has monopoly power. The firm also has another product, say the generic version or some other much more competitive product. The firm says to its buyers, "look, I'll tell you what I'll do, I'll give you 25 percent off the must have product, if you'll also

buy my more generic stuff." The competing sellers of the generic stuff say, "Oh, this is terrible, we are losing business, and we have no must-have branded scotch tape ourselves to bundle for a discount, and so we can't compete. We have to leave the market. We will make our antitrust case before the Court."

What would be a valid economic analysis of that situation? Well, is this a sensible practice absent any possibility of monopolization for the seller of the must-have product? What's the cost of the offer to the dominant firm? The dominant firm is giving up 25 percent of the price of the must-have product in order to make the sales of the generic stuff. So the net price, the incremental price, the incremental revenue to the dominant seller is not the market price of the generic stuff. It's the market price less the 25 percent that it is giving up on the must-have product. So the pertinent incremental revenue indicator to be compared against cost is not the price of the generic product, it is a tougher standard than that. It's the price of the generic product minus the 25 percent discount on the must-haves.

Thus an economic analysis of sacrifice or predatory bundling here would not just compare the price of the generic to the incremental cost of the generic, but instead the net price which would include the discount if it's only there to effect the sales of the generic product. And that would become the valid test for sacrifice, the return version of the test that economics would suggest would make sense here. That is an analysis that ought to replace the somewhat nonsensical view of the courts and the plaintiffs of whether rivals can match. Rivals say: "We have no must-have product. We have no pharmaceuticals in this category to bundle with our pharmaceuticals in the competitive category, so we can't match and therefore the bundled discount is anticompetitive." This test of ability to match makes no sense because money is fungible. The issue is not whether a rival can assemble an equivalent bundle, but whether rivals can offer the same financial discount that the bundle can be analyzed to represent.

So back to my example. How can the rival compete with the dominant firm for the generic tape even though the rival has no equivalent must-have product? Yet if the rival is able and willing to give the same 25 percent discount off the net price of the generic tape, it is in business and able to compete then. So if the dominant firm meets the test of incremental revenue against incremental cost, then in fact the rival can compete if it is efficient, if it would survive in a competitive environment. And if the test goes the other way, then the test shows that efficient rivals are in fact frozen out.

So in conclusion, I would say that there is a right way to make these assessments, not based on a superficial reading of what might appear to be ugly facts or locker room language about oh, we are going to beat up on our rivals. Business is tough that way. But there are standards for analysis that are well grounded in economics for the antitrust context that really conduce to social welfare in this area.

**MR. POPOFSKY:** Thanks, Bobby. Since Doug's name has been taken in vain, I think it is fair to give a two-minute rebuttal to Doug.

**MR. MELAMED:** Actually, based on what Bobby said at the outset I anticipated two things. One, we would disagree, and two, he would actually spell out why he thought we didn't agree. But it turns out that we agree.

**PROFESSOR WILLIG:** Surrebuttal to that.

**MR. MELAMED:** Here is why I think we agree. He talked about the scotch tape example. The bundle that says if you buy 300 units of the scotch tape then and only then we will let you have the crappy stuff at discounted price. He said that is okay. I agree with that, because as stated, the example is intended to protect against cannibalization of the scotch tape. If you didn't condition the discount for the crappy product on maintaining your purchase levels at 300 for the scotch tape, the fear is there would be arbitrage, people buy only 200 of the scotch tape and buy more of the crummy tape, and the seller would be disadvantaged by that. In other words, in the sense that I was talking about an insurance tie and leverage tie, this is all about promoting the strong product and protecting the strong product. It is not about sacrificing revenues from the strong product in order to promote the tied product.

The willful test that Bobby had I think is the same as the fair notice test I talked about in the patent pool context. The uncertainty of patents creates a factual context that explains how a benign package works in patent ties. It wasn't intended to say there were no other factual contexts that could make other kinds of mandatory ties or bundled discounts benign.

One final thing. In the *Ortho* example or I think the example Bobby said, you attribute the entire discount to in effect the crappy tape or the weak product. That is the proper test, where the fact finder concludes that the buyer must have 300 units of scotch tape. That is not contestable at all, and the seller says, once you buy what you must have, then you get the discount on everything when you buy the marginal product. I agree that is the proper way of thinking in that case.

But what if the seller is selling to differentiated demanders, some of whom want the so-called must buy product, others of whom don't want the must buy product, and in order to sweeten the deal for the latter group he throws in this opportunity to buy the package of the must buy product and the second product at a really good price. In that case I would suggest that the discount is not appropriately entirely attributed to the crummy product. Some of it ought to be attributed to

the marketing of the strong product. It is like my *Philips* patent pool, and I don't think you should attribute all of that discount to the crummy product in applying the test that Bobby was talking about.

**PROFESSOR WILLIG:** Surrebuttal. Thank you.

Actually, I agree with Doug pretty much. Your last point I absolutely agree with. I was taking the simpler example because it is easier to illustrate where all of the sales of the must-have product would not change because of the discount. The case is only strengthened, and it ought to be strengthened if indeed another function of the discount is to promote the sales of the must-have. And then those extra sales go on the positive side of the incremental top of the ledger for asking whether profits are sacrificed because of this business practice or not. So I totally agree with that.

Where I really disagreed with you was when you were overly cautious in your description of the insurance motive in the patent pool. The insurance motive makes a lot of sense to me, but you were saying it only applies if the patents aren't too essential. It only applies if there are all these other conditions. It strikes me that the mere fact of the insurance motive makes these products be what economists would describe as very strong complements. There is much more demand for the weaker patents if you're getting access to the strong patents, because they serve the insurance function to protect your use of the stronger ones.

So this is like left shoes and right shoes. It makes a whole lot of economic sense to sell them together, and it makes a whole lot of sense to allow firms to sell them together. Because like any complement, a firm that is in possession of the intellectual property will sell them both at a lower price per unit if they can be sold together. That is always the case for products that are complements in demand. And as you described your insurance motive, they are very much demand complements. So I think it is actually a stronger case than you presented here. I was shaking my head, why do we need all those caveats? That bundling is a very sensible business way to sell economic complements.

**MR. POPOFSKY:** Okay, now that we have finished this 300 grad level seminar on this issue, I would like to throw this first question. Rick has had nothing to say yet and he has a page worth of notes. Keep with the *LePage's* theme and bundled discounts and ask those to my right the following level question, which is this: We can all agree that *LePage's* decision is a mess, has no standard, has created uncertainty and spawned a lot of uncertainty on the part of major companies who have no guidance on this area. One very strengthened thing about the *LePage's* case that Dara touched upon, and I was there at the *en banc* oral argument in the Third Circuit, when asked to explain what was in it for consumers, what were the procompetitive justifications for the practice at issue in the *3M-LePage's* case, not just what's good for 3M, but how did it benefit consumers as a whole? 3M was left to mumble things such as consumers benefited from a single invoice for multiple products. 3M benefited. . . . They didn't really have a crisp story of what was good for consumers from the arrangement at issue. Certainly nothing as sophisticated as Professor Willig's graph explained how it just led to recovery of fixed costs.

Now you can chalk that up to bad lawyering alone or the bad documents such as Dara described, such as kill Scotts, which I think was Plaintiff's Exhibit 1 in that trial. But I would ask at a simple level—maybe Dara, because you are in the real world on this—what are the real world business reasons as to link products this way when going out and making their pricing decision?

Basically at bottom, 3M said this is a good way of incentivizing our division to sell more and getting our sales force out there. So what is the real world story behind economic bundling? And anyone can answer. I didn't mean to put Dara on the spot.

**MS. DIOMANDE:** Well, I'll start.

One of the benefits for consumers, besides the lower costs that result from the economic bundle, is that it promotes competition. One option that may be used is that the other firm, let's say they don't have a diverse portfolio, but they may create a joint venture with another firm that does have a diverse portfolio and then compete with the firm that initiated the bundled rebate. I think ultimately that ends up with a better result altogether.

But when my clients come into my office and say we want to do this bundling rebate program, can we do it, what's the deal after *LePage's*? The first question of course I ask is why do you want to do this? What's the real reason, besides trying to gain a market share? And the reasons vary. Sometimes it's because there is a particular product that they really want to get out into the marketplace, and no one is really buying it, and they quite honestly want to use it as an incentive to get to more consumers. I think that is fine. I think that is legitimate. And I think it is a basis for engaging in a bundling rebate program.

**MR. POPOFSKY:** Any other responses on that? Doug?

**MR. MELAMED:** I think the question Mark asked is a really important one for reasons that go beyond bundling. In Europe in particular and I think some of the courts in private litigation, there is a tendency to think of efficiencies in a very narrow sense—limited to what I think an economist would call productive efficiencies, such as lowered costs—and to ignore allocative efficiencies.

Bobby's chart was all about allocative efficiencies. He basically says, I am going to sell more widgets to people who otherwise couldn't afford to buy them. It seems to me that would be the first justification to note in these pricing cases, which is that I am simply trying to have a sweeter deal for consumers and sell more products.

**MS. DIOMANDE:** Although if that is the true purpose, then why don't you just lower the price of the drugs without bundling them?

**MR. MELAMED:** I agree. You have to show that the bundle has some unique ability to provide that efficiency.

**MS. DIOMANDE:** Exactly.

**PROFESSOR WILLIG:** Also market segmentation. And you said it right, although with a negative spin earlier, you're protecting your ability to charge $300 for those first 10,000 units in my graph by not offering the $150 price for all of the units. But for those consumers who are already committed to a relatively large volume, they are the ones who can get the benefit of the extra purchases at the lower price without eroding the ability of the firm to get $300 for the smaller amounts of purchases from the other consumers. It's a way to segment the market where the aim of the segmentation is to offer more at a better price to some segments of the market, the ones who qualify for the bundle.

**MR. POPOFSKY:** Staying on the economic bundling theme, another theme that you touched on, Professor Willig, is the harm side of the ledger.

The basic problem I want to focus on is this: Suppose you have a rival who is holding a single product firm, like LePage's was, like 3M-LePage's the transparent tape, but it has a story, which LePage tried to tell, not based on anything in the record but based on effective appellate counsel, that what 3M was up to, Your Honor, was preventing us from reaching efficient scale. That if we reached scale, that is if we were able to expand our generic tape sales of transparent tape, we would actually end up being more efficient a producer than 3M was. We might be less efficient now, and that is why we can't match. But there is some long-run dynamic harm to consumers here, because if we are excluded, long run prices will be higher, and in the long run, output will be lower.

How do you in an economic context trade off that potential long-term harm that is substantiated against the types of benefits we have just been discussing? What's the right framework for doing that trade-off?

Anyone want to take that on?

**PROFESSOR WILLIG:** Oh, yeah, thank you. There is economic logic to that plan. If that was the story alleged by appellate counsel, then they were very wise and read the right economist. That is the coherent story. The question is does it fit the facts? Does the firm making generic transparent tape really need X percent of the market in order to hit the bottom of the cost curve to get to the minimum efficient scale that achieves the kind of production efficiency that they would need to be an effective competitor.

In the cases that I've seen that analysis has not been done by the plaintiff. Just oh, if we have lost share, then we have lost effectiveness, end of story. And the more you actually look at what kind of scale is needed for cost efficiency in that market, you find that they are asking as an entitlement for far more share than that.

**MS. DIOMANDE:** And it actually is rewarding them for being inefficient. It is rewarding them for not being an efficient competitor or being innovative and thinking of ways to compete with the firm that has a monopoly power in the market, if you read *LePage* the way it is now.

**MR. POPOFSKY:** What then is the implication of that? Should we give a free pass to the defendant if the plaintiff is inefficient and can't compete today?

**MS. DIOMANDE:** I think basically what would optimally happen in *LePage's* case is that you look at above cost, to see if they are pricing above cost, and to see if that above cost pricing is so attractive to amount to a de facto tie.

But I truly believe that the result in *LePage's* which forces firms with dominant firms in a market to price their goods unreasonably high because you have an inefficient competitor in there who doesn't want to lower their profits ultimately hurts consumers as well as competition and innovation.

**MR. POPOFSKY:** Doug.

**MR. MELAMED:** There are two elements to these claims. One is bad conduct, and the below cost issue and how you allocate the discount to that. If you don't satisfy that the defendant is going to win. But if you satisfy that, then you have the second issue, which I think is what Mark's question was, what does the plaintiff have to show with respect to the effect on exclusion, assuming he is the only competitor, in order to show that this really enhanced the defendant's market power?

One of the problems I have with the notion that it is just too bad if you're small and inefficient is that, to the extent the defendant by engaging in conduct that is anticompetitive on the first element of the offense is able to keep the rival at a small scale, he is able to keep prices artificially high because he has reduced the competitive vitality of his existing competitor by preventing him from becoming efficient. I don't think you have to prove that the anticompetitive conduct had a more enduring impact on structure than that in order to satisfy the second element.

**MR. POPOFSKY:** Where then do we see the doctrine going here with respect to bundled discounts after

*LePage's*? Do the people on this panel believe that we are going to see some test adopted by the Supreme Court, or are we going to see some sort of mushy Microsoft balancing test? I say that because one of the great ironies in the Microsoft case is the Government did not argue for the Section 2 test Microsoft articulated. The Government argued for a version of the profit sacrifice test you've heard about. That violates Section 2 because and frankly only because it made no sense for Microsoft absent maintaining its operating system monopoly. What the Government got back from the D.C. Circuit was invoking nothing less than Standard Oil itself and saying something like a four-part Rule of Reason standard.

With that as background do we see the Supreme Court going with Microsoft with this issue on bundled discounts or ultimately going with rubric on this issue? Anyone have a prognostication? Doug?

**MR. MELAMED:** I believe that almost all antitrust cases in this area reflect, however inarticulate it usually is, the Court's belief, however mistaken it may be about the economics, that the defendant's conduct didn't make any sense except as a scheme to drive away competition. You go back to all the old cases, I think that is really what the courts were thinking, even though they didn't say it quite that way. That is certainly what the courts thought in Microsoft. So I think that something like that will drive decisions. If you're litigating cases, I would advise you, persuade the fact finder that that is not what's going on, and somehow you're going to win. And if you don't persuade the fact finder of that, you're in big trouble. So I expect that the courts will ultimately begin to articulate that with greater clarity than in the past.

**MS. DIOMANDE:** But, Doug, what makes sense to the court? How do you define that?

**MR. MELAMED:** Well, we were just talking about whether it has to be productive efficiency or allocative efficiency or whatever. But I think the courts will hear the story if you tell it in an intelligible way. Get Bobby on the stand for you, and he'll get them believing him.

**PROFESSOR WILLIG:** Judges yes, juries no.

**MR. POPOFSKY:** That makes a lot of sense especially in terms of the gestalt litigation thing. What do you do about Justice Scalia's remark in *Kodak*, where he says: Practices which are ordinarily done by ordinary competitive firms can take on an exclusionary hue when undertaken by a monopolist.

Does that indicate a counter theme in the cases that somehow what the Sherman Act is all about, and in some sense is some net reckoning of static and dynamic benefits and harms?

**MR. MELAMED:** I believe that the proper interpretation of the Scalia idea is that even if the conduct doesn't otherwise make much business sense, it is harmless and therefore not illegal in the absence of market power. But when you combine it with market power, it injures competition and is therefore illegal. But I understand that it is widely read in the more troublesome way that you suggested in your question.

**MR. POPOFSKY:** What do we do in the meantime, before we get to the Supreme Court deciding this issue in bundled discounts, what do we advise clients as a practical matter?

Dara, you were saying about the clients coming to your office and asking them: Why do you want to do this? What guidance can we give clients on how to navigate the bundled discount mine field?

**MS. DIOMANDE:** Besides me calling my outside counsel.

**MR. POPOFSKY:** And you should.

**MS. DIOMANDE:** The difference between being in-house and outside is your clients are next door to you, you don't have to say let me get back to you in an hour. They are standing right there. I think generally what I advise clients is first of all I ask why do you want to do this. And they always give me the caged answer that you're supposed to give to your attorneys, so they don't say no. But if it's a case where we have a high share of the market, which may be the case particularly since we have patents, we are very cautious, we really are. I counsel them—it really depends what the market looks like, how many players are in the market, what products are being considered as part of the bundle. So it depends on the facts, but I will tell you that it does make us second guess a lot of bundling, rebate programs that ultimately not only fund research and development to produce new drugs by pharmaceutical companies but get those drugs into the hands of consumers at lower prices. It does make us second guess our action.

I don't have a brightline answer as to yes or no. It just depends on what the market looks like.

**MR. POPOFSKY:** There has been some chilling of the—

**MS. DIOMANDE:** Oh, absolutely.

**MR. POPOFSKY:** I would like to return, before we open it up to questions from the floor, to the very first topic we discussed in this larger theme of bundling, which is a patent licensing bundling situation. It certainly makes a lot of sense to me if I am the manufacturer developing a DVD player. I am a little guy out there, and I want to make sure that the big guys out there who have the brand and IP rights aren't going to come after me later saying, oh, you missed a patent. I am going to put Doug on the spot in this. You said basically the theme of your remarks it is okay in substance to bribe the licensee as long as you're not coercing the licensee into taking a

product it didn't want. The theme of the insurance side, it seems to me, is something a licensee should want and not something you should have to coerce out of them for this to be an okay practice.

What if though it turns out there is another harm to that analysis, if I've characterized it properly, which is this. Suppose the licensee who was being given the benefit of this insurance tie happens to be the one or two companies out there that would be willing to challenge the validity in a patent litigation of the "tied license" because it competes against a licensor in another product market where that technology might be necessary and the fellow who is taking the license might not in that market want to be subject to tying.

How do you handle that sort of competitive harm scenario in the market, if you will, for challenging IP rights? Is this something the antitrust laws can get their arms around? Is this something we should or should not worry about?

Any thoughts from that on the panel?

**MR. MELAMED:** So you are imagining, to extrapolate a bit, this: I have a patent. I sue you for infringement. I get a glimpse of your defenses. I get nervous, and I say, ah, I'll just give you a license to the patent if you drop your claim.

**MR. POPOFSKY:** Something like that with a temporal twist that before you even do the patent infringement suit you've already given off that possibility by giving up the license.

**MR. MELAMED:** Yes, I think it is very hard to make it an antitrust claim. Even if you could imagine—I think it would be very unusual—a situation in which no one else would challenge the patent. The patent is weak enough that it ought to be challenged and yet there are people excluded from the marketplace because of the existence of that.

**MR. POPOFSKY:** Okay, that is certainly one answer to that problem.

Sticking with the issue of the insurance tie, is the implication of your analysis, Doug, that we shouldn't worry about those ties if the licensee is not basically coerced, sticking with this coercion theme, because they are presumably given the benefit from this insurance tie. Is the fact that the licensee voluntarily accepts the package and doesn't scream bloody murder in defense, in your view?

**MR. MELAMED:** I think voluntarily accepting without screaming bloody murder is not the same as not being coerced. Because after all, a lot of people will accept it, although I think we might regard it as coercion for tying purposes if the implicit threat is "I won't give you what you need unless you take the package."

But the short answer is yes. If you are not saying to this guy the only way you can get what you really want is to take something you don't want or give up or reduce your incentive to take an alternative, then that ought to be lawful.

**MR. POPOFSKY:** Just so the audience is clear with the case you mentioned, the *Philips* case, which I gather you argued. The holding of that case as I recall wasn't per se misuse to engage in the practice at issue, the bundling of the patent licenses. A broader question that raises is does that kind of analysis in the panel's view have implication as to whether that sort of tie should be held unlawful under the Rule of Reason or should we read the law as to the per se misuse in question?

**MR. MELAMED:** Well, actually the Court also held on the facts there, that there was no Rule of Reason violation. But I think it is probably right that any claimant ought to be able in principle to say this may not fit into a per se category but let me tell you our Rule of Reason story.

**MR. POPOFSKY:** Rick, you've been awfully quiet. On any of the subjects we have touched on today, is there anything you're dying to say?

**MR. RULE:** I've only got 20 more minutes without saying anything, with all my experience. Why don't you let me answer a couple of questions.

**MR. POPOFSKY:** I think that is a fine suggestion.

Are there questions from the audience on this question we touched on today?

Yes, Steve Houck.

**MR. HOUCK:** All of you have talked about the reasons people bundle. I was curious what your views were with respect to the significance, if any, of intent evidence either economically or legally regarding the reason why somebody bundled. For example, if you have a case where it is clear the intent behind the bundling was to protect the monopoly product, that that evidence be weighed?

**PROFESSOR WILLIG:** My view on this is that a good economic analysis actually does go very much to intent, while making use of fact and structural analysis impacts rather than making use of explicit articulations inside the business documents. The sacrifice test is about whether there is a good business rationale for the practice, or whether instead the intent is revealed to be knocking off rivals because that is the best explanation.

Of course, the trouble is often businesses will write documents and e-mail conversations will be reported with a lot of passion behind them and some good competitive kind of passion that says I want more market share, I want to make more sales, steal from those damn rivals, from my children if necessary, which sounds

predatory, like monopolization, but is often a human way to talk about what's a good competitive passion in the marketplace.

So I think intent is good as an element, but it ought to be revealed by economic analysis.

**MR. POPOFSKY:** Doug.

**MR. MELAMED:** Slight variation on what Bobby said. I think intent really oughtn't to be an element. I think the objective business case ought to be the element. Extrinsic evidence, the documents and depositions are probably relevant evidence, not the stuff that says I want to gain market share, can be illuminating about the economics. For example, if you had extrinsic evidence that showed there was no question that this patent you put in the pool really wasn't essential, and that everybody agreed was not essential. Then you might use it to rebut the effort of the defendants in court to tell you this was an insurance package to protect you. The point is that the extrinsic evidence is useful because it illuminates the underlying economics of the transaction, not because it shows a motive to gain market share or exclude competitors.

**MR. POPOFSKY:** Further questions? Yes, sir.

**AUDIENCE MEMBER:** I want to try to reach for a type of objective analysis. What is the counter of the sacrifice test, the idea of putting all of the discount from the monopoly products onto the "tied product" and if it makes sense, Professor Willig, would that kind of formula all but eliminate the Smith Kline type paradigm where there are three or four monopoly products?

**PROFESSOR WILLIG:** That is a good question. This idea of loading all the markup onto the most competitive product is a convenient formula, but it is not the real avenue to the truth in complex situations. I mean the way I think the calculations should be structured is to go to the issue: If you didn't do the challenged thing, what would be the state of the revenues and the costs? So if you didn't bundle the two with the three, what would you otherwise have been doing? Well, you would have set other prices for the three and perhaps the market price for the two, and in comparison to that scenario, how do your revenues and costs look from the bundle? That is really the question, and how you get to the answer depends upon the details of the circumstances.

**MR. POPOFSKY:** That provokes a follow-up from the moderator here, which is this: One criticism of applying this sacrifice test in the bundled discount arenas is this notion of asking whether the conduct makes business sense but for the practice, requires a well-defined baseline, as you said Professor Willig, of what you would have done absent the practice. That is often very difficult to establish in the real world. One can hire Professor Willig to write his expert report. Someone else will come in with their expert report; you can have an inconclusive battle of the experts. The experts might not even know.

From a practical litigation perspective, if one is trying to design these rules to govern these situations, a judge for example, is the sacrifice test when you cannot find this but for scenario, what do we do?

**PROFESSOR WILLIG:** There is a very simple and often obvious starting place for analysis before it gets hopelessly complex and self canceling. Like where your normal price is $300 and you're offering the bundled discount on the margin for $150, the obvious starting place isn't okay to offer the $150 at all, because it is clear that that would undermine your ability to sell at $300. It is pretty easy to do costs and benefits in terms of revenues and marginal costs that compares those two business alternatives. Then someone can come back, like Doug did, with traditional wisdom, and say yes that does affect the elasticity of the additional sales. But there is very often an indicated starting place that I think sets the tone and is basically persuasive.

**MR. POPOFSKY:** So you challenged the hypothetical, but stick with it. What if one cannot simply find a but-for scenario. What do you do at that point? Do you say plaintiff loses because that was their burden of proof, or do we say some other legal standard should apply subjective intent with the but-for test.

**PROFESSOR WILLIG:** It is hard for me to imagine a situation where you couldn't find an indicated but-for. There is a practice that is challenged. I think the plaintiff ought to be held to an articulation of what it is that is the offensive or allegedly offensive practice. Where a plaintiff that just comes in and says, oh, they are too tough and too sophisticated in a thousand ways, there is no benchmark and that case ought to be thrown out on that obscurity alone. If the plaintiff says there is a particular kind of bundling there, which you let by your office because you were otherwise engaged you let your clients do it, it makes no business sense, it is killing us. There is then a well-articulated practice on the table and the relevant simple but-for is without that practice what would pricing have been?

**MR. POPOFSKY:** Let me extend that example to another area which will bring it closer to home, which is this. And this will prompt Rick to speak I am sure. When we were litigating the Microsoft case—Rick has to speak before this panel ends. In the Microsoft case we asked the following question to ourselves. We were blessed to some extent by Microsoft. And I am putting on my former DOJ hat. Which is Microsoft had a feature for removing some functionality of the Internet Explorer browser through the add/remove menu that most of us are familiar with, and lo and behold when we go to a later version of Windows the ability to remove that functionality through the add/remove method had been deleted. Another way of putting the point is Microsoft gave us a clearly defined

but-for scenario with respect to that conduct. They gave consumers the option of hiding parts of the browser, and then they took it away, which prompted thought: What if they had simply designed Windows from point ab initio to have the Internet browser be part of the operating system in a sense that they had not chosen to do as the facts actually were, where it had somewhat of a separate existence.

Does a legal regime that basically says it is a plaintiff's burden always to demonstrate what the but-for scenario was and show there is a sacrifice from it lead to opportunism on the part of defendants to basically hardwire the analysis by hardwiring their products a certain way? Does it distort product design to have a legal regime which forces the plaintiff to prove the but-for scenario?

Anyone have thoughts on that issue?

**MR. RULE:** I have no thoughts on that.

**MR. POPOFSKY:** No one has thoughts on that question?

**MR. RULE:** Okay, I guess I'll say something.

**MR. POPOFSKY:** Thanks, Rick.

**MR. RULE:** Look, I am on record as saying that the profit sacrifice test is not a good one. It's not a good one for a number of reasons. First, an initial question ought to be what's the harm to competition. I think a lot of cases, including arguably the *Microsoft* case, would have been eliminated at that point.

I think when you get into the question of whether or not there is a sacrifice of profits you end up inevitably, regardless of what Doug says, looking at intent. (A) because trying to understand what the objective rationale is, you are inevitably going to look at what the parties thought they were trying to accomplish. (B) the problem is that as much as we all love judges and lawyers and economists, the fact is their record in terms of evaluating justifications is not very good. And as Doug said—I don't think he intended it this way, but if you look at the Supreme Court decisions, there is a pretty uniform history of the Supreme Court looking at cases and being bewildered as to why these practices could possibly be justified. And that is because either they just couldn't comprehend them or because the litigants didn't do a very good job of presenting them. So inevitably I think courts discount the reason for various practices.

Just to use *Microsoft* as the example, part of what the Government pushed in that case was the fact that Microsoft spent literally hundreds of millions of dollars in developing and improving its Internet browser. Then it put it in the operating system. I don't think the fact that at one point certain aspects of it were subject to the add/remove button and later aspects of it weren't was dispositive in that case. It was a helpful factor for the Government, but it was to some extent inevitable in an industry like software where you constantly have changes and the products are always going to change. There is always going to be a point at which a product group looks like X, and then at a subsequent stage it will look like X plus Y. Well, was Y a problem. It is pretty hard for Microsoft to go back at the outset in 1980s put an Internet browser in Windows and not make it add/remove. Because as a practical matter there wasn't one at the time.

Now I am not sure that is why the Government whined. But one of the notions was Microsoft spent hundreds of millions of dollars in improving browsers and then put it in the operating system for free. That can't make any sense. The only reason Microsoft must have done that and spent all that money was to basically put Netscape out of business. The problem with that analysis is that in an industry like software—frankly, most industries, you know those of you who advise clients on these things, where a company is basically trying to respond to the demand in a very quickly changing technological dynamic, they oftentimes don't have the opportunity to sit down and say, well, if I spend this much money, how much of a return am I going to get? It is very difficult to do that. They don't have time to do that. So instead they see something is happening out there, in Microsoft's case the importance of the Internet and the inextricable link between competing generally and the Internet. And they say we make this product that fits integral to personal computing. We have got to make sure it works better with the Internet. So they continued to improve it. In their mind they are improving their basic product, making it more attractive, so they price it as that bundle.

To the Government it looked like they were able to persuade the district court but not the Court of appeals as something that made no economic sense because Microsoft was spending hundreds of millions of dollars and giving the product away. But of course that really wasn't what was happening. To me it sort of goes back to this notion that it's very hard sometimes to convince triers of facts who tend to be skeptical about this sort of product, what makes economic sense and why at the end of the day the sort of economic sense for lost profit test is ultimately doomed to failure.

It's a great idea for lawyers and for keeping lawyers employed. It is a bad idea in terms of making the world safe for people doing procompetitive efficient means.

**MR. POPOFSKY:** Do you have any response to that, Doug?

**MR. MELAMED:** Well, how much time do we have? I always love talking about Microsoft.

Rick is clearly right. There can be false positives with a sacrifice test. I don't think it is quite as easy as Bobby thinks it may be in many cases. But there can be false positives I believe.

On the other hand, if we had a rule that said no or a much narrower Section 2, sort of Judge Easterbrooke's view of the world, we'd have a lot of false negatives because there can be anti-competitive conduct by dominant firms. So the question is, thinking of type one, type two error trade-offs, what's the best? Yes, there are problems with the sacrifice test, but I think it is better than the alternatives I am familiar with. The issue is not simply, are there false positives with the sacrifice test. It is whether the sacrifice test does better than the alternatives taking into account both false positives and false negatives.

**MR. POPOFSKY:** Yes, question.

**AUDIENCE MEMBER:** Years ago they used to say a practice could be unlawful if it was anticompetitive in purpose or effect. We then evolved to the point where we are saying of course a bad purpose can't make something unlawful. There is a need to prove anticompetitive effect, and we started talking about plaintiff's burdens of proving anticompetitive effect in a Rule of Reason case.

I just happened to read Judge Ginsburg's opinion in *Three Tenors* last night where it again said, well, the Commission really didn't have to prove anticompetitive effect there. And during most of this panel I am hearing most of the discussion focusing on the intent of the monopolist or the company perpetrating the tactic as to why they did it and they have to prove that it was really justified.

I guess what I'd ask the panel to comment on is whether or not we are really at the point again now where litigation is going to focus largely on the intent and the purpose of the defendant and relieve the plaintiff of a lot of their burden of showing there has been an anticompetitive effect without regard to what the intent was?

**MR. RULE:** I'll start us off.

I think that the *Three Tenors* case, in my opinion, is important to distinguish from Section 2 and unilateral conduct. I think if you look at the jurisprudence over the last 20 years in Section 2, this concern about the ambiguity of intent evidence has been noted with particularity in Section 2 cases. Because as several people have said today, somebody who is engaged in competition on the merits would use the exact same phraseology that somebody who is engaged in some anticompetitive conduct. I think that is why Doug said that he'd look at objective evidence.

That is why even today people who would say in Section 2 cases you only look at that kind of evidence only to try to understand objective facts and try to throw some light on the objective facts. I think even in that circumstance the evidence is too potentially prejudicial to be helpful.

In Section 1 cases I think it is a little different. In Section 1 cases where you have multiple parties sitting down and by definition having agreement. What they communicate to one another about their agreement and the purpose of that agreement and what they are trying to achieve with that agreement, whether they think the agreement is going to result in them obtaining higher prices than would otherwise be the case seems to me is relevant.

Typically when people articulate the Rule of Reason that is why they say the purpose is relevant. I think it will continue to be relevant in Section 1 cases. But even in Section 1 cases, I guess notwithstanding what Ginsburg said in that decision, I think the trend continues to be the direction of requiring greater and greater amounts of objective efforts. And while purpose evidence I think still is relevant in Section 1 cases, I don't think that pendulum has swung back. I think probably over time it will continue to probably play second fiddle to what the objective evidence suggests.

**MR. POPOFSKY:** Well, I can't think of disagreeing with Rick that we should be objective. I am not going to commit to having this linger beyond the time to finish before lunch. Thanks to our panel for their efforts here today.

**MS. GOTTS:** Meg has a two-minute business meeting, and then we are going to hear from the representative from the Foundation.

# Section Business Meeting, Election of Officers and Members of the Executive Committee

**MS. MARTHA GIFFORD:** Thank you. This is for members of the section. If you're not actually a member of the section, you can leave.

This is the report and voting on the nominations report of the Nominations Committee and voting on nominations. The Nominating Committee proposes the following individuals for election for a two-year term on the Executive Committee effective as of today:

Paul Bartel, Davis Polk & Wardwell.

Paul Braunsdorf, Harris Beach.

Beau Buffier, Shearman & Sterling.

Aimee Goldstein, Simpson Thacher & Bartlett.

Leslie Harris, of Buchanan Ingersoll.

Barbara Hart of Labaton Sucharow & Rudoff.

Hanno Kaiser, Latham & Watkins.

Eamon O'Kelly, Dewey Ballantine.

Doug Richards of Milberg Weiss.

William Rooney, Willkie Farr & Gallagher.

Fiona Schaeffer, Weil, Gotshal & Manges.

Mark Siemens, Siemens Corporation.

April Tabor, McDermott Will & Emery.

And Douglas Tween, Baker & McKenzie.

May I have a motion to second.

**AUDIENCE MEMBER:** So moved.

**MS. GIFFORD:** Thank you, and a second.

**AUDIENCE MEMBER:** So moved.

**MS. GIFFORD:** All in favor? (Audience votes aye.)

**MS. GIFFORD:** Thank you.

Our second piece of business. The Nominating Committee nominates the following current members of the Executive Committee for election to one-year terms in the offices that I will identify:

Ilene Gotts, as Chair of the Section.

Saul Morgenstern, Vice Chair and Program Chair.

Susan Raitt, Secretary.

May I have an motion to second.

**AUDIENCE MEMBER:** Second.

**MS. GIFFORD:** Thank you. All in favor.

(Audience votes aye.)

**MS. GIFFORD:** Thank you.

The business of the Nominating Committee is concluded.

**MR. TUGANDER:** I just encourage everybody to stay for a couple more moments. We are going to have a very brief presentation from Richard Raysman from the New York Bar Foundation, which is the charitable arm of the New York Bar Association.

**MR. RICHARD RAYSMAN:** My name is Richard Raysman. I know this is approximately three to four minutes I think. I might go a little bit over.

I am on the board of the New York Bar Foundation, which is the charitable arm of the New York State Bar Association. And the New York Bar Foundation gives about $500,000 a year currently to worthy causes throughout the state for legal services. It has a very high level board. There are about nine former Bar Association Presidents on the board. And Bob Haig of Kelly Drye has taken over the presidency about two years ago and has really tried to make it a much more active foundation.

The reason I am here is that we as lawyers—law has been good to me and it has been good to a lot of us. We give money to religious organizations and medical organizations and things like that. I am here to suggest that when you get your dues statement, you might want to think about giving something to the Bar Foundation as well.

The Bar Foundation supports charitable and educational programs throughout the State of New York. It helps delivery of legal services for those in need. It helps in improving the justice system. And it enhances professional competence and ethics.

I just want to in my time allotted, which is close to zero, I just wanted to give some examples of some of the grants given out over the last year so you have a sense of what it does. It is throughout the state, not just New York.

Gave a grant to Unity House in Troy, New York. It was grant to help victims of domestic violence in Rensselaer County.

We gave a grant to an entity called My Sister's Place in White Plains, which is legal assistance and relief for

immigrant victims of abuse that is documented and undocumented.

It gave a grant to Workers Rights Law Center in Kingston, New York. They had 64 stand-alone workshops. It was a know-your-rights education to workers in the Hudson Valley.

It gave a grant to an organization in Albany called New York State Commission on Quality of Care For the Mentally Disabled, and they produced a video on transitioning from school and adult living to real life for people with disabilities. And that video actually aired on public TV for 60 stations.

It gave a grant to the Legal Assistance of Western New York. It was a Finger Lakes Geneva region on a clinic program for low-income people on how to act pro se in matrimonial actions.

So those are just a few of the examples of grants that it has given. I think it's important for us as attorneys to help the legal system in New York State, and that is what the Bar Foundation is doing. I just wanted to bring that to your attention. Thank you to Steve for giving me these few minutes, and thank you for being patient and lasting for a few minutes prior to lunch. Nice to be here. Thank you.

# A Touch of Class: Latest Developments in Antitrust Class Actions

**MS. GOTTS:** We are now going to start with the afternoon panel. In planning this year's session, I attempted to cover the areas that my own practice doesn't cover, thinking that would be a good way to learn.

This morning's topic, as far as the title went, took the award of being the longest topic, this one is the—no pun intended, the classiest of the topics, has a nice little ring to it.

The session is called "A Touch of Class: Latest Developments in Antitrust Class Actions." The panel chair for this is someone that many of you know, having been a prior chair of this committee, this Section, Steve Edwards. Steve is a partner in the New York office of Hogan & Hartson, where he focuses on complex litigation of all types. He is a graduate of the University of Iowa and the University of Virginia Law School. Among other things, he has litigated many antitrust class actions and has been involved in a number of arbitrations. I am going to ask him to introduce his panel. Thank you.

**MR. EDWARDS:** Let me start out first of all by saying that I've had some sort of respiratory problem lately, so occasionally I break out into coughing spasms, and I'll apologize for that in advance. It means I won't be able to talk very much, but perhaps that is a good thing.

We are going to present this program in three courses. The first course, the appetizer course, is on the issue of predominance. To discuss that issue we have two well-known economists. Immediately to my left is Dr. John Beyer, who has appeared frequently on the plaintiff's side. And if you look through the course materials, which include many of the leading antitrust class action cases that have been decided in the last four or five years, you'll see that John's name pops up in almost every one of them.

Next to him is Dr. Brian Palmer, who is also an economist, and he is with Charles River Associates. He appears frequently for defendants, so he is going to take the defendant's side of the discussion.

Our second course, or our main course, is going to be on class action arbitrations. For that discussion we are very fortunate to have Bob Davidson, who is head of the arbitration practice at JAMS/Endispute. He is also Chair of the Arbitration Committee of the City Bar Association. Before he was with JAMS he was a partner at Baker, McKenzie and did many, many arbitrations all over the world.

On the other side of the podium we have Bernie Persky of the Labaton, Sucharow & Rudoff firm, and Bernie is a well-known plaintiff's class action lawyer who has litigated class actions all over the country and is currently involved in an antitrust class action arbitration with the person immediately to his left, Steve Cherry.

Steve Cherry, of Wilmer, Cutler, Pickering, Hale & Dorr, is also a well-known antitrust litigator who practices primarily on the defense side, and they are going to have some interesting things to say about the particular class action arbitration that they are involved in.

Then for our dessert we are going to be talking about the Class Action and Fairness Act or CAFA. For that discussion we have Hollis Salzman, also of the Labaton Sucharow firm. She has spoken and written about the Class Action Fairness Act, and again has litigated many, many class actions generally on the plaintiff's side.

And finally, originally Saul Morgenstern was supposed to be on this panel, but he couldn't make it, so Andy Schau of Patterson Belknap is our very able substitute. Andy is a litigator; he is head of the technology practice at Patterson Belknap. And Andy and I are actually involved right now in a series of—depending on how you count them, pre MDL, approximately 50 class actions all over the country.

So we'll start with the predominance issue: As many of you may know, if you do class action litigation, there are a number of criteria that plaintiffs have to satisfy in order to persuade a court to certify a class. There is numerosity; there is typicality; there is adequacy, commonality. Those issues are generally pretty easy. The real battleground is predominance. In order to certify a class, a court has to conclude that common issues predominate over individual issues, and this becomes very interesting in the context of your typical antitrust class action.

Let's say it is a price-fixing case, and let's say it's the kind of industry where there is a lot of individual negotiation. So you have individual negotiation; you have prices varying all over the place, and yet the plaintiffs claim that they can demonstrate impact through common evidence. How do they do that? Well, they retain Dr. John Beyer, who does it for them. Perhaps John can explain the secrets of the trade.

**DR. BEYER:** I am not sure I will do that, but if it were only a matter of retaining John Beyer and Nathan Associates to have a class certified, I'd go into retirement. We would be very wealthy, and there would be a lot of classes certified. It's a lot more difficult than that.

The reality is that in every industry that I am aware of, with one exception I have had familiarity with, other than the classical agricultural markets of wheat and corn and that, prices vary tremendously depending on who purchased those items at the same point in time for exactly the same commodity, same product, same service. That is due to a lot of what I call market realities. Some are big, some are small, some are continuous purchasers, some are intermittent. Some spend a lot of time being purchasers, being in a better position to negotiate and evaluate. Other purchasers simply take it on face value, and don't bother spending that time. And as a result, in most products and services if you look at one point in time, the variation can be very large.

Now, how can all of them have been affected or impacted by a common course of anticompetitive behavior? In my judgment, if there are several criteria that are present and where price becomes the end instrument that purchasers use to make share decisions, then the likelihood is that all purchasers, the largest purchaser at the very bottom, the purchaser at the very high end who only buys a little bit occasionally will have been affected.

Economists use two terms. Lawyers have used other words to describe this. One is called undifferentiated products or services; that means there is no brand loyalty. If you think of most intermediate goods, it is very difficult to think of purchasers who continue to buy from one supplier compared to another because they think that supplier has something unique, has a brand. It is able to differentiate its product and charge a premium for it. If there is no differentiation, then purchasers compete on the basis of price. Again, regardless of the level at which they are buying.

The other principle is what I call and economists call substitution, supply substitution, which means that most of the suppliers in an industry are able to make the most, if not all of the products that are actually sold in the marketplace. So for example I use cardboard boxes, because I've done a lot of corrugated containers. Every box plant in North America can make every type of corrugated container; the kind that they ship refrigerators in and the kind that I am really interested in, those they ship beer in. But the plants don't always make everything because they decide they want to specialize. But the same raw materials go in, and if the right competitive opportunity comes along, every box plant can make every other container. So there is a supply substitution. A lot of alternatives for purchasers. And again, price becomes the principal consideration.

When those two considerations are present, the likelihood—not that it will be guaranteed, but the likelihood is that predominance will prevail. That all purchasers, again regardless of whether it is a negotiated price or a list price—very few industries sell entirely off a list price anyway, again with one exception that I am aware of, and as a result, the price is affected by the alleged anticompetitive behavior. There are other considerations, but those two seem to have been predominant in most of the cases that I have dealt with over the last fifteen, twenty years.

What that means for me is that most consumer products, which aren't often the object of an anticompetitive cartel, probably (1) is going to have a more difficult time certifying a class. So most of the antitrust level action really is at the federal level. All of this is focused on federal, not the end purchaser, as with intermediate profits. Corrugated containers, chemicals, rough diamonds, various products that are used, that are manufactured that are intermediaries to some other process, production or final consumption.

**MR. EDWARDS:** Well, one of the things that defendants often say in reaction to what John just said is, wait a second, if you've got an industry in which every deal is negotiated individually, why shouldn't it follow from that that individual issues predominate? I suppose one response to that is economists deal with individual issues on a global basis all the time. For example, economists take every transaction in the economy and attempt to determine the gross national product. So why isn't that the case, Brian, with respect to individual issues in connection with price-fixing cases?

**DR. PALMER:** Well, I think you really need to look at what is the industry structure and also the data generating process. Obviously plaintiffs wouldn't bring a class action unless they thought there was a class. From the defendant's view point you really need to look at it and say is there something here?

A lot of times it seems that plaintiffs say, well, we can't really tell what it is, but we'll take an average. We see things moving around, let's take an average of everything and go with that. Well, the average doesn't really describe what is occurring and why things happen. So it's the big why. It is important to not just look at the output and say we see prices or we see movement, but to examine why do things happen. You need to know the foundation, the underpinnings of it.

For example, an industry with inflation adjusted long-term contracts, you may see a group of people moving up and down together in terms of their pricing, and you may see a lot of variation in individual prices, depending upon quantities purchased and other things. You may say, well, look, here's a common price movement. But it could be that the alleged class period occurred all within a long-term contract period. So those on long-term contracts who look like prices were moving together may be completely insulated from any price fixing. Whereas the individual transaction, the spot transactions, may be the ones affected. So you really have to dig into the industry and not take a broad brush and

say, well, we see what average prices are doing or we see something, and we are going to take that as a given.

**MR. EDWARDS:** John, why don't you give us a little thumbnail sketch of the econometric tools you use to try to demonstrate impact through common proof.

**DR. BEYER:** There is a predecessor to that question, which is usually the predecessor doing any serious analysis of the impact on purchasers, which means the impact of alleged behavior on prices. This is all about price behavior during the period of the alleged cartel or anticompetitive behavior. And that is easier said than done. Because in most industries there may be millions of transactions that are affected or that are to be examined. And often this means understanding and using that data, which is really historical records that companies have kept about their invoices, their transactions that they have with their purchasers over time. From my experience it is quite varied, and it depends a lot on the firms in an industry, what type of data they decide to keep to reflect what they think is important about their transactions.

Once that is done, before I even get to looking at a way of trying to set aside looking at the effect of the cartel as distinct from other economic factors, is answer this question: Have prices, regardless of whether they are high to the small purchaser or very low to the large purchaser, and regardless of the categories or types of product, have they tended to move over time similarly? If they have not, then there is a real question, because then the issue of negotiation and factors that both suppliers and purchasers take into account do affect on an individual basis the final outcome, which is the price.

I have found in several cases where we have been able to examine—and this is an empirical question, it is not preordained; it is a demanding empirical condition made easier in this current day because in this day most of the data is being kept electronically. Although I have to say there are a few firms that like paper, and it gets very expensive to use.

One can look at the behavior of prices by mining, by looking at this rich empirical basis of how suppliers have related to their purchasers, to their customers. Econometrics is a tool, a statistical tool that economists use to measure the effect of various parameters on price, on income, on savings, on other esoteric considerations. It takes into account the various factors that likely are to explain price changes in a given economy. More often than not, if there is a pattern where prices tend to move together, then the change will be similar, even though the absolute levels are miles apart. And therefore, something that Brian talked about just a moment ago, the averaging can take place, because suppliers all react to the same cost changes in an industry. They tend to have the same cost structure and use the same raw materials. The demand for the product by purchasers will generally be affected whether it be a small purchaser or a large one by how the industry as a whole is doing in the economy.

There are various measures by which those changes can be reflected and can be incorporated and will enable an economist to distinguish whether an alleged cartel has had an effect on prices, in a decision to the general economic factors of changes in cost and changes in demand.

However, it is not always possible to do that because it's a demanding empirical test. And like many analytical tools that economists and other social scientists use, it is a tool that can be abused. So it has to be used with care by both the lawyers who are retaining the specialists or the experts as well as by the experts.

**MR. EDWARDS:** Brian, it seems to me what John is saying is I can deal with individual issues simply by averaging, because averaging by definition eliminates individual issues. Is that an appropriate economic approach?

**DR. PALMER:** Well, it depends. I mean it's almost setting the conditional first. So if you say, well, there is a common impact and there is something that exists, so I can tease that out. But a lot of times what is used is a regression analysis, which is basically just a sophisticated averaging technique—it is a conditional mean. What the person using the regression analysis is looking for is to see if they can control for a couple of different factors. To examine the alleged behavior, again as I said before, is a need to go back to what it is that generates the observed differences or what is the theory behind how the alleged damage occurred. So it's not just, well, there is a common impact. But the question is: How did it occur? Because then that will help to guide the analysis as to what to look for.

A lot of times the regression analysis may include variables that, while they may be interesting, but they may not be the descriptive ones. So what happens is that you may throw in a couple of regressors and they may be correlated with something else and you say, oh, look, here is a common impact. But if some things are excluded and the included regressors are correlated with some of the things that are excluded, then you get screwy (i.e., erroneous) results.

So a lot of times the claims can be made, again by only looking at the empirical results, but without having a good motivation behind it.

**MR. EDWARDS:** John, have you ever looked at a class and concluded that you couldn't determine impact through common proof? And if so, what were the characteristics of that class that made that so?

**DR. BEYER:** I have, and the common dimension in each case that has run through it is that the product

involved or the service involved was—you can use the economist's horrible phrase—a differentiated product. In other words, brand loyalty. As a result of brand loyalty, there could be—not always—but there could be price premiums that are charged to some customers, and therefore the prices don't move together.

The example was—I have to be careful how I say this because I am involved in a case now involving Mercedes Benz. But there was a case some years ago where a class action was being proposed for owners of Mercedes Benz who were buying or could have bought Mercedes-like spare parts from non-Mercedes dealers. And it became clear to me that we are really dealing with something in a purchaser's mind, and probably as well in suppliers, that is clearly a differentiated product. So the prices today could be something and tomorrow something very different for the exact same part. There have been several examples like that, and not only products, but also services. And when you think about it in terms of particularly end products where consumers are involved, I go through the supermarket, and it amazes me the amount of money that companies spend to differentiate their products. I use often the example of salt. Now, salt, if we had a blind test here, I don't think anybody could pick out Morton salt. But Morton sells for more than any other salt, because they have managed to differentiate their product through advertising. So what do I do? Now, I am dumb, I pick up Morton quality because I think it is better, yet I know it's the same bloody salt that I get from somebody else. Now that is why consumer products are more difficult to deal with.

An example, disposable diapers, a big industry these days. I haven't bought them recently. But when I was looking in the supermarket, a young mother looked at me and kept looking at me and wondering what am I doing looking at disposable diapers. But Huggies and Pampers are able to garner a substantial price difference, because they have managed to convey to consumers as a whole that they produce a lot better product, compared to the generic store brand disposable diapers, which—I don't know—I haven't tried them, but I think that they are probably just as good and they sell for a lot less. So I have found when dealing with consumer products and consumer services it tends to be a more complex issue.

**MR. EDWARDS:** So let me pose the same question to Brian. Brian, have you ever analyzed a class and concluded that, notwithstanding individual negotiation, this class should be certified because impact can be demonstrated through common proof? And if so, what were the characteristics of that class that made that so?

**DR. PALMER:** Well, I think looking at things—I am trying to think back—and the thing that would be common is that a factor would be the same, some cross factors or some input factors or because there was a list price change; if there is a finding of liability or something.

Part of the problem in looking at these is that the class is often defined as all the people who were damaged. So you may be in an industry and there may be a subgroup or part of a group that may be different. So you say well, not everyone is the same. But then the class is defined, who is damaged, but we can't find out who is damaged until after the trial is adjudicated, yet we still have to define the class.

One of the big problems it seems is that the courts are often willing to certify classes and then you have this huge thousand-pound gorilla on the back of the defendants. It takes a very small probability of anything going awry, and there is a huge damage award so defendants most often settle. So it is a real problem, even if there may be a subgroup or something like that, the class is often defined very broad. Plaintiffs can point to some similarities in a small group, but say "well, everyone is like this," and the potential liabilities are so huge, the Court says we can always examine it

**MR. EDWARDS:** John, in looking through the materials, one of the cases that you lost or I should say the Court decided not to certify a class, notwithstanding your report, was the Agricultural Chemicals case down in Florida. I think one of the things the Court focused on in that case was market power. Basically, the Court concluded that because the alleged price fixers did not have market power as a group you could not show impact through common proof. What do you think of that? Was that decision correct?

**DR. BEYER:** I disagree. Actually the decision was correct, but the reasons offered were wrong.

It turned out this was a complex case where AstraZeneca was a supplier of astro chemicals to its three or four large distributors. It turned out that the prices that the distributors gave back to AstraZeneca were not the true prices, because they got rebates based on no reselling below a certain price. However, the reality was there were prices below that rebate price. And it's that information that came out just before trial that I found particularly troublesome.

The judge in that case—and I am not a lawyer, but from what I understand from the case law put the cart before the horse. He was looking at merits issues, and the question here is—and I didn't want to revisit it, did AstraZeneca through its brand name chemicals have sufficient market power to persuade farmers to buy its product versus others. And that would have been a tough issue.

Now, the judge at that point, he and I had a long discussion—less of a discussion than it was a heated argument. And I lost of course. But the real compelling issue for me in that case was the fact that the brokers, the distributors who really sold the product to the farmers had negotiated in some cases prices that were very

different than the prices they told AstraZeneca that they sold for. So that in fact, contrary to what we thought, there wasn't a similar price that was pervading among the purchasers who were farmers, but rather a wide variety of prices that didn't appear to behave in a logical, cohesive manner.

Now again, this is a differentiated product. AstraZeneca was able to sell some of its chemicals because of its brand name, and distinguish its product from Monsanto's or Dow chemical or whoever else is selling out to the farmer.

**MR. EDWARDS:** Brian, it seems to me what happens in most of these cases is you have individual negotiation. The plaintiff says well, I can deal with that on a common basis because my economist is going to do a multiple regression analysis. The defendant hires CRA. CRA does its own multiple regression analysis, purporting to demonstrate that there are many, many individual issues. The judge's eyes glass over. The judge says, well, I don't really understand all of this multiple regression stuff anyhow, so the judge ends up assuming impact, even though as a technical matter you're not supposed to assume impact in a private treble damage suit, even though it's a per se violation.

Do you think that is what's really going on here, the judges just can't figure it out and they just make a presumption one way or the other?

**DR. PALMER:** Well, I think the judges are probably concerned that if they don't certify the class, the case will go away; yet, if they do certify the class, well, it may or may not go away. It often does go away, because, as I talked about earlier, the defendants don't want the exposure. So the judges always think, well, if I certify I have an option down the road of decertifying the class. Chances are that doesn't happen, and it seems that it is very rare, if it ever happens. But it often seems that the plaintiff's brief says, well, you're supposed to assume certain things for the sake of class certification arguments, so essentially we are going to assume the class and go through a bunch of stuff, and lo and behold they get the class they assumed. So I think judges often do not understand. That is why I think it probably behooves the experts to say what it is that is causing the commonality or the lack of commonality and not just looking at the regression analysis, which examines the data that results from what is alleged as being common. And so sometimes, you know, it almost seems that the class certification phase should be after the merits phase, so we should figure out what it is that is actually at issue.

**MR. EDWARDS:** And there was a very interesting case that John and I were involved in, and Steve Tugander was involved in as aspect of this case, an antitrust case against Mercedes Benz. There were very, very good thorough reports by the economists from both sides. At the end of the day Judge Wallen wrote an opinion in which he said: I understand that I am not supposed to assume impact. But under the Bogosian case in the Third Circuit there is something called the Bogosian shortcut which essentially enables me to assume impact. My own personal view is that is what a lot of courts around the country are doing, because they don't fully understand all of the things that our economic colleagues are telling us.

That being said, I want to move on to the second course here, which is antitrust arbitrations, actually antitrust class action arbitrations. And I want to start off by asking Bob Davidson, who is our arbitration expert: What is the authority for having a class action arbitration, and how frequently do they actually occur?

**MR. DAVIDSON:** Thanks. The Supreme Court put arbitrators in the business of arbitrating class actions. It did that in a case in 2003 called *Green Tree Financial v. Bazzle*. I'll get into *Bazzle* in a minute, because we should all understand what it says in order to appreciate what arbitrators can do and what they cannot do. The Supreme Court has only opined once on the issue of class arbitration.

First, is class arbitration common? As far as class actions go the two major providers are the AAA and JAMS. On the AAA web site I counted today 92 class arbitrations on its docket. Now, that is overstated a bit, because many of the defendants in the listed cases are the same, and the list sometimes duplicates cases, but you can see it's quite a number. I would say probably upwards of 80 different cases. JAMS, which does not publicize its cases—that is one of the main differences in this area between the two providers--has about 15 active class arbitrators. Of those listed with the AAA, there are one or two that I know are antitrust oriented, have antitrust issues. JAMS has one antitrust class arbitration that is active now. None of these class arbitrators has gone to a final award. Several of them, however, have gone to a clause construction award.

Let me just briefly tell you what *Bazzle* said, because it's a complex case. The Supreme Court has nine justices. There are four opinions. A majority was formed when Justice Stevens sided with four other justices in order to provide the fifth vote in order to create a controlling decision.

There is a big debate about what *Bazzle* really decided. Essentially what *Bazzle* determined was that an arbitrator and not a judge was the appropriate person to decide whether or not an arbitration clause, which is silent on the issue of class arbitration, permits the case to go forward as a class arbitration. The four Justices who formed the plurality decided that the Supreme Court of South Carolina acted improperly when it determined as an initial matter that the underlying dispute could go forward as a class arbitration. Instead, these four Justices held that the South Carolina Supreme Court was not the

correct decision-maker. The correct decision-maker was the arbitrator.

That is all those four Justices said. Stevens, who concurred, concurred on a different basis. He thought that the four Justices who came to the conclusion that the arbitrator was the correct decision-maker made a gratuitous ruling because no one asked for a ruling on that basis. The parties simply said they wanted the decision that had been affirmed by the South Carolina Supreme Court to be affirmed by the Supreme Court. Stevens reasoned that because the case should have gone forward as a class arbitration, the South Carolina Supreme Court got it right, and the judgment below should have simply been affirmed.

So as a technical legal issue, only four of nine justices said that an arbitrator is the correct decision-maker in this area. The decision, however, has had broader implications. Two things have happened. One, since 2003, many class actions have now been thrust into an arbitration forum. Second, there has been considerable uncertainty as to how these class arbitrations are to be conducted. *Bazzle* dealt only with clause construction. It didn't say anything about what should happen after that. And, as you know, a lot of things happen in class arbitrations beyond construing whether an arbitration agreement permits an arbitration to go forward as a class arbitration.

The courts have indicated and have stated, in certain cases, that an arbitrator has the power to run with the ball, that is, not only determine whether an arbitration can proceed as a class (the issue of clause construction) but perform all the other functions of a judge in a class context. This includes the certification of a class and all of the other attendant issues that go with the process.

So all of a sudden these provider organizations (like JAMS and the AAA) were put in the business of administering class action arbitrations. And it is interesting because no one asked for it, neither the AAA nor JAMS nor any of the provider organizations filed any amicus briefs or expressed any opinions on it. All of a sudden we woke up one morning and, to our surprise, the Supreme Court all of a sudden put us in the class action arbitration business. That is really what started the movement.

**MR. EDWARDS:** Let me pose a question to Bernie. Bernie, you're a plaintiff's lawyer. Let's say your client has a contract. The defendant has violated the antitrust laws in your view. You want to sue the defendant. You decide to invoke the arbitration clause. An arbitration clause is a creature of contract, right, so on what basis can you turn that into a class action? The other members of the putative class are not parties to your contract; how does it become a class action?

**MR. PERSKY:** Well, normally in the first instance we wouldn't as a matter of choice go into arbitration seeking a class. Normally we would go to court, assert our claims on a class action basis. But if we are compelled to go to arbitration, the question would arise what does that arbitration clause encompass? It's really a misnomer to say the absent class members have no contract. The absent class members by definition in any proposed class would have a contract similar to my clients' contract. And the question arises, what does that contract encompass? What does that contract mean? What kinds of arbitration claims can be brought? And how far does it go? If the contract says you can't have a class, that answers the question, we won't be able to seek a class. If the contract is silent and there has been no agreement not to have a class, so my client and the action class members are in a contract where there has been no agreement not to have a class. But what kinds of disputes would be encompassed by this arbitration clause? If it's a broad clause, as many clauses are, it would say any normal disputes of any kind in any way shape or form affecting the contract. Well, that is the kind of clause that the Supreme Court was interpreting in *Bazzle*. And the Supreme Court held that every arbitration panel faced with this question since that time has also held that if it is a broad clause and the clause is silent in not prohibiting a class, the clause can include a class claim. Every single AAA clause construction award decision has so held with respect to their clause construction awards. There are 30 such decisions I believe and at least 23 or 24 of them have so held. The others punted on the issue.

One of the things that Bob didn't mention is that after *Bazzle* the AAA and later JAMS adopted supplementary rules, class arbitration rules. And they do set out a rather detailed procedure as to how the panel should operate and how the parties should proceed.

**MR. EDWARDS:** Steve Cherry, why don't you give us the defendant's perspective on this. Is this a good thing from a defendant's point of view, that a plaintiff can commence an arbitration not only based on its own contract but it can draw in a class of plaintiffs with similar contracts?

**MR. CHERRY:** I think we would not view it as a good thing particularly. I think the key from our perspective is that all of this is about consent, and it really is construing the contract. We view *Green Tree* as not being such a change in the law, but simply it is changing who makes the decision. That rather than having the courts construe the contract and make that decision, now that they have said this is not a gateway issue, you have an agreement to arbitrate, so why are you reading the contract and making that decision. That is a decision for the arbitrator.

Prior to *Green Tree-Bazzle*, virtually all the federal courts that had previously been construing these contracts had all held that where there is silence there

is no agreement to arbitrate, and so you can't have a class action arbitration, you can't have a consolidated arbitration. So we don't see this as a sea change in the law. It is simply who makes the decision. The arbitrator now construing the contracts is making that decision and ought to be looking at the contracts to determine if the parties actually agreed to have a class action arbitration or not.

We disagree with Bernie's position, that if it's silent somehow the parties have not agreed not to have a class, and therefore they can get one. Particularly I think that is so today, but I think it's particularly the case for parties who contracted prior to *Bazzle*, who certainly had a right to rely on all the federal cases which were telling them if you want a class action arbitration, you'd better put it in your contract, because if it's not there, you're not going to get one.

**MR. EDWARDS:** Well, let me follow up on this, and this is a question for Bob. It seems to me you have three possibilities here: The contract may be silent whether there should be an arbitration; the contract may affirmatively say not only should there be an arbitration, but it can be a class arbitration. Then again, the contract could say you can have an arbitration, but no class arbitrations. I guess one question I have for you, Bob, is where the contract is silent, where it has an arbitration clause but it is silent on whether there can be a class action arbitration, is it the case that so long as all the class members have similar contracts, an arbitrator is likely to go ahead and find that the case can proceed as a class action? And I guess a second question is: Are there people who are putting in their contracts a clause that yes, there is an arbitration clause but no class actions?

**MR. DAVIDSON:** Several parts to that question. First, if the clause is silent, truly silent—but you have to understand something about *Bazzle*. The Justices characterized the arbitration clause there as a clause that was silent on the issue of class arbitration. But it really wasn't that silent. The contract in *Bazzle* was a contract between one lender and one borrower. It said that if "you," the borrower, have a problem with "me," the lender, "I" the lender, will select an arbitrator and then you, the borrower, can either say "okay" or "no" to my selection. If you say "no," "I," the lender will select another name and so on until we get a mutually acceptable arbitrator. The arbitration clause in *Bazzle* always spoke in the singular as if it was a contract between only two entities. So it's not quite right that it was "silent," even though it was characterized as being silent in the opinion.

To my knowledge, an arbitrator will generally construe a "silent" clause ("silent" in the *Bazzle* sense), as maintainable as a class arbitration.

That being said, one of the antitrust class arbitration cases in your material is *Direct TV v. Cable Connection*. We have a news flash here. The Superior Court of California, County of Los Angeles has vacated the arbitrators' order in that case that permitted that arbitration to proceed as a class arbitration. The arbitrators' award in that case was 2-1. The underlying arbitration clause was silent (like in *Bazzle),* and the majority of the panel held that a class arbitration could be maintained. (Actually, the one dissenting arbitrator was a JAMS arbitrator who was appointed to sit in this AAA case.) The reviewing Court agreed with the dissent and said that, notwithstanding "silence" in the arbitration clause, the case could not go forward as a class action.

However, the majority of cases that go through a clause construction exercise do find a class arbitration permissible when the applicable arbitration clause is silent on the issue.

The big issue presently is the validity of class preclusion clauses. After all my years of being a practicing lawyer and doing this now as an arbitrator full time, I've never seen a clause that says "In the event there is a dispute, the plaintiff can proceed as a class." I've never seen that.

**MR. EDWARDS:** Have you ever seen the opposite though?

**MR. DAVIDSON:** Often. It's gotten to be in vogue now, and all of you with credit cards which includes a hundred percent of you I am sure, if you read your card agreement will find new arbitration clauses in the card agreements recently sent out to you. The agreements all have now what are known as "class action preclusion clauses." These clauses say that, if there is a dispute, you, the cardholder, cannot be a member of a class. Those clauses, called class action preclusion clauses, were first met with hostility, but are now on a roll. Just about all courts, except those in the Ninth Circuit most notably in the State of California, will in fact generally honor those clauses. So people are getting smarter, putative defendants, and they are putting class action preclusion clauses in their arbitration agreements. You'll find this especially so in credit card and other consumer areas. The courts will generally enforce those preclusion clauses.

Now, there is a paper that should be in your materials that I wrote about a year ago, that actually lists all the states, at least as of that date, that had decided the issue of the validity of class action preclusion clauses. The vast majority of courts will honor class action preclusion clauses.

**MR. EDWARDS:** There is a recent significant Second Circuit decision in this area, the JLM decision, which is in your materials. Doug Richards, who is in the audience I think argued that case on behalf of the plaintiffs. And Steve Cherry argued that case on behalf of the

defendants. And Bernie Persky is also involved in either that case or a related case.

Bernie, can you tell the audience a little about the JLM case?

**MR. PERSKY:** Sure, but before doing that I wanted to correct one thing. It is not just an arbitration clause that is silent that has been interpreted to permit a class. It is silence plus language which encompasses a very broad reference to the types of disputes that could be arbitrable. So silence plus the notion that all kinds of disputes in any way related to the parties' issues can go to arbitration. And that has been held to permit the possibility of a class.

**MR. EDWARDS:** So it is a little bit like price fixing, conscious parallelism plus.

**MR. PERSKY:** Silence plus broadens.

In addition, one other thing, the AAA has a large number of clause construction award decisions generally consistent. Actually there have been some certification decisions; I think two went against certification. I think three have gone forward with certification, and at least one of them has provided for class notice in the arbitration context.

**MR. EDWARDS:** Tell us about the JLM case.

**MR. PERSKY:** Getting to the JLM case, it followed on indictments of certain parcel tanker shipping companies, companies which owned specialized ships, parcel tankers which transport over the oceans liquid chemicals. And after these companies were indicted, and some of which were guilty and paid fines, class actions, as is usually the case, followed on the publication of those indictments and pleas. And class actions were filed in the Districts of Connecticut and in Pennsylvania and in Texas. Our case, brought by a company whose name has about 26 letters in it, was brought in Houston, Texas; other cases were brought in Connecticut. Our case was faced with a motion to compel our arbitration—our case of course was a class action of direct purchasers of parcel tanker shipping services. We lost that motion and were directed to go to arbitration, which we commenced.

In the meantime, a similar motion made by the same defendants was made in the District of Connecticut and again, in the meantime, an MDL petition was filed in all the cases filed around the country were concentrated before Judge Sofrito in the District of Connecticut. And the plaintiffs in the District of Connecticut actually won the motion. They defeated the motion to compel arbitration. The defendants then took that up to the Second Circuit Court of Appeals, which ultimately resulted in the JLM decision, which held that the contracts at issue, these tank charter party contracts, contracts for the shipment of liquid chemicals and parcel tankers, literally standard form contracts that had standard form arbitration clauses provided for arbitration generally in either London or New York. The Supreme Court rejected the contentions of the plaintiffs and held that the price fixing and market allocation disputes, which plaintiffs contend really had not that much to do with the charter party contracts, were in fact arbitrable, citing *Mitsubishi* and a bunch of other cases, and then sent the matter back down to the district court. And then cases were referred to arbitration.

**MR. EDWARDS:** Steve, as I recall, the Second Circuit also said something about the ability of nonsignatories to compel arbitration. Can you talk about that a little bit?

**MR. CHERRY:** Yes. First, two seconds about this threshold issue again, and I just respond to Bernie. I just would emphasize to people who are particularly on the defense side of this, that the vast majority of these AAA decisions to me seem to turn on the fact that they are contracts of adhesion and construing any ambiguity, and inevitably the company is the draftsman and that is what happens. I just want to make that distinction. But also, in terms of rules, anybody seeing any rules that allow class actions, there are actually industry specific arbitration rules out there that do allow consolidated arbitration. There may be arguments that support a class action, but you do have that.

On the JLM case, there is what you're alluding to. In that case one of the issues was whether the plaintiffs were trying to avoid arbitration by taking the position that they were—by not suing the people with whom they had contracts. So instead of suing say the subsidiary that was providing the service, they sued the parent or an affiliate. And then even beyond that they said besides that, we have claims against said company X for being a coconspirator and affecting the price of company Y's contracts. We don't have an arbitration agreement with them covering that, so that was their approach to avoid arbitration.

What the Second Circuit held in a footnote, footnote seven which has become very significant now, is that non-signatories under those circumstances can compel the signatory to the agreement to arbitrate these types of claims. That under those circumstances the claims are intertwined enough that the claims against everybody turn upon a contract that contemplates arbitration.

**MR. EDWARDS:** Bob, maybe you can tell us a little bit about what actually happens in one of these class action arbitrations. Do they differ at all from litigations in court? Are there any unique issues that come up?

**MR. DAVIDSON:** Yes, they do differ. The goal of arbitration, to make things faster and less expensive, has proved illusory perhaps in some complex commercial settings. However, in these class action cases, which are very expensive cases to prosecute and to defend, arbitrators and the arbitral institutions are seeking to do a better job. The AAA, which has the most class actions

pending, provides in its rules for two stages in the proceedings. The first stage is when the arbitrator engages in clause construction. The second is when the arbitrator deals with class certification. The AAA rules provide that the arbitrators' award regarding clause construction must be embodied in a partial final award. The arbitrator must then wait 30 days to allow the party who lost to go to court and seek to overturn the clause construction award. Similarly, there is a 30-day waiting period after the class certification award. By the way, that is one way the JAMS class action procedures differ from those of the AAA. JAMS has an optional procedure. It is not mandatory that the arbitrator write a partial final award on these issues and then wait for 30 days after his award.

But the things that happen thereafter in arbitration are similar to the way a court proceeding is handled. The institutions are very careful to appoint people as arbitrators or to send out lists of only people qualified to handle these cases. These lists include only people who have been in practice for many years, people who had experience, or former judges who have had experience with these cases. One of the worst things that can happen in this area is that someone that doesn't understand the process winds up sitting in one of these cases.

The other thing is an arbitration proceeding is faster and a little more efficient, because, for example, the arbitrator is also the magistrate for discovery and other purposes. It's the same person. So if you have a problem with discovery, if you want discovery in a class certification context, for example, you can get it. But you'll be before the same person who is going to decide the entire case. Things go a lot faster I think and the rulings are a lot more consistent in that way. The big issue of course in arbitration is you generally get to select the person who is going to be deciding and administering the case, so you don't have to worry about someone without the expertise.

Just as an aside, I'll mention one of the big issues not yet decided is what the scope of review of these awards will be. The *Direct TV* opinion in California did not go into an explanation that it was dealing with an arbitration award that should be subject to great deference under the Federal Arbitration Act. It just went ahead and decided to vacate the award as if it came from a referee, for example. It is still an open question as to whether or not greater scrutiny will be given to arbitration awards in a class action context.

**MR. EDWARDS:** Can you bind absent class members just as effectively in a class action arbitration as you can in a class action litigation?

**MR. DAVIDSON:** Why not? If the arbitrators are supposed to do what the courts do, if the courts can do it, now the arbitrator presumably can do it. Sometimes it gets a little complicated. What if you've got some members of the class that have silent arbitration clauses (if I can call them that) and some members of the class that have arbitration clauses with class preclusion clauses contained in them. Query: Can you bind class members who signed arbitration agreements with class action preclusion clauses? It gets more complicated if you want to look closely because some states hold these preclusion clauses valid and others do not. Maybe a claimant in California can be a member of the class and maybe one in Ohio cannot. So you get into these issues as well.

**MR. EDWARDS:** Well, let's go back to Bernie. Bernie, in the JLM case or the CPT litigation, you were resisting class arbitration. Why is that? Was it the availability of discovery? Why don't you like to arbitrate?

**MR. PERSKY:** Well, as plaintiffs in an antitrust case we would prefer to be in federal court under Rule 23. Arbitration is not our choice of forum, as to whether or not we were pursuing it in arbitration, I think I've been asked not to discuss the details of pending proceedings. But just to pick up on some—

**MR. EDWARDS:** Yes, you don't have to tell us the details. We just want to know why didn't you want to be in arbitration to begin with?

**MR. PERSKY:** Well, normally defendants are the ones that pick arbitration as a forum. The industry normally does that, and their customers are normally subjected to it. It's not the most customer or plaintiff-friendly forum, but it can be pursued effectively. The AAA's rules set up procedures for it. And I believe absent class members can appropriately be bound with the supplementary rules the AAA provides for in essence a triple judicial review. That is first, you need to succeed in persuading the panel that it's a class arbitration. That goes before a judge. Assuming you win that, you then go forward with a class certification award before the panel. You win that, that goes before the judge. And go back to the panel after having won that and you get an actual class arbitration award. Go back to court and you get a judgment on your award. You have three chances for judicial review. People who don't like the procedure may object upon the attempt to confirm the award; presumably before the award was issued notice went out to the class. And the class notice would probably have to be the best notice trackable as it would be under Rule 23.

Just as a personal view, I would suggest maybe publication notice, and conceivably in an arbitration context maybe slightly less defensible. But you have tripartite judicial review; and you have a judgment in a federal court which may be enforced internationally.

**MR. EDWARDS:** Steve, it seems to me there is a little bit of a role reversal in the JLM case where Bernie was resisting class action arbitration, you were embracing it. Is there something about arbitrations that make class actions more palatable from the defendant's standpoint? And do you think perhaps some defendants or potential

defendants would be well advised to include in their arbitration clauses a clause that says that the arbitration can proceed as a class action on the theory that if you're going to have a class action, you might as well do it in the context of an arbitration as opposed to as part of a court proceeding? What do you think?

**MR. CHERRY:** Yes, I think there are a number of issues. These threshold issues we have talked about. I think there are concerns that I am sure Bernie had that led him to want to litigate. I think he probably mentioned there are concerns about you're going to get the discovery you need. Some of the other things I think where there is an alleged cartel with multiple defendants, there may be a concern we talked about whether one defendant in the case can have a class action with all the plaintiffs. But can a plaintiff rope in all the defendants in one class action without their consent? I don't know that there is any authority to support that. I don't know that that is the case.

And I think there is concern about enforcement, particularly if there are international parties involved. Is a foreign court going to enforce this type of award? We'll see.

But I think once you pass that I think there is no reason where you wouldn't necessarily prefer to do this in arbitration. I think particularly if you're talking about claims among commercial entities that have a relationship, particularly if they're customers or something like that where you would rather be in a private forum, tailor it to your needs, protect private information maybe in a way that you're more comfortable with than in court. You can choose arbitrators that you feel have the expertise you need. I don't know if there is any reason you couldn't do it and make it work.

**MR. EDWARDS:** It seems to me that the big disadvantage of class action arbitrations is the availability of third-party discovery, particularly third-party depositions.

What do you think about that Bob; do you agree with that?

**MR. DAVIDSON:** I did before a recent Second Circuit case. There is a little trick arbitrators had been using for years that was finally challenged, and the Second Circuit said that this procedure was all right. Basically, the weight of authority says arbitration under the Federal Arbitration Act does not permit discovery depositions. However, the way you legitimately get around that restriction is that you say, okay, we can't take a discovery deposition, but we can hold a hearing. Either arbitrators or lawyers in New York of course can issue subpoenas to appear and give testimony at a hearing. There is no doubt about that. So an arbitrator, who is sympathetic to this and realizes there has to be some discovery if the parties cannot get voluntary compliance can say "Look. Let's have a hearing. Mr. Witness is going to show up and we'll take his testimony. I will attend, so it will technically be considered a hearing and not a discovery deposition." There is an additional expense with this procedure in that you have to have an arbitrator sitting there but the testimony is taken prior to the main hearing. Against the objection that this procedure is really a sham, it's not really a hearing; it is really a way to circumvent the rule that you cannot have deposition discovery, the Second Circuit recently said "So what. Have a hearing." Thus, the courts are sympathetic with the fact that arbitrators are handling more complex cases now.

If you're outside the U.S. of course you've got 28 U.S.C 1782. Because of a fairly recent Supreme Court decision you may well have a possibility to invoke Section 1782 in the context of an international arbitration.

So to sum it up, if the place of arbitration is, for example, in New York, but you need to take the testimony of a third-party witness in California, you can now (with the arbitrator's cooperation) travel to California and hold a hearing. Local counsel, whoever it is in California, will issue a subpoena and compel the third party to appear. Presumably, arbitrators who hear these cases understand there is often a need for this type of discovery.

**MR. EDWARDS:** So Bernie, why don't you comment on the same question. Do you think the difficulty of getting third-party discovery is a big disadvantage of class action arbitrations?

**MR. PERSKY:** Yes. I think that though it's not clear that you can't get under the Federal Arbitration Act deposition discovery from nonparties. So most cases say no, but according to the Second Circuit's decision it is split on the point. But I think it would be more difficult certainly than in litigation to take the deposition of a nonparty witness, particularly outside, more than 100 miles from where the arbitrators are sitting and where the Courthouse is. There is the 100-mile bulge with respect to the issuance of court subpoenas, and the Federal Arbitration Act permits the enforcement of an arbitration subpoena. What do you do with a witness in some other locality beyond that? Bob mentioned reconvening the arbitration in California somewhere and having that done. Yes, if everybody is in agreement then you can do that; that is nice. But it's not so easy.

**MR. EDWARDS:** So Steve, what are the disadvantages of a class action arbitration, or would you take a class action arbitration over a class action litigation any time?

**MR. CHERRY:** I think there is the concern, and granted there are some creative ways to get around a lot of this, but it becomes a little unwieldy. I think the real concern in terms of whether I would take one at the outset is whether I believe it's what my client

consented to. I mean because the real difference is all of this wrangling at the beginning about whether this is something you even contemplated or not, which slows things down considerably, as it should. Because you may be about to embark on something that you didn't agree on and that is outside the arbitrator's jurisdiction, so you have to deal with that. If you're in court you wouldn't have to deal with that. And that causes some delay. Under the AAA rules you have immediate judicial review, so hopefully you get some certainty.

The way I read the JAMS's rules there is the availability of that but it isn't certain. So you could have a situation where you have clause construction that goes against the defendant, you're proceeding with class discovery, briefing class cert, and having invested quite a bit into this and not have a definitive ruling on whether you should have been doing any of that to begin with and be vacated by the district court and maybe the court holds you're not required to have the class action anyway.

**MR. EDWARDS:** Bob wants a brief rejoinder here.

**MR. DAVIDSON:** Yes, that is correct. Under JAMS' procedure, a partial final award on clause construction is not mandatory. But all of the class certification awards that have come out of JAMS have always been in the form of partial final awards.

**MR. CHERRY:** On that issue though, maybe you mentioned this, there is a split among the courts as to whether they will review that type of award. It appears that most of the courts have taken them up, but I think there is at least one decision I've seen where a court has said, you know, it is premature. The AAA can have whatever rules it has, that doesn't give it access to the courts. So come back when you have a real final award.

**MR. PERSKY:** Yes, that is an issue that has come up. The supplementary AAA rules that structured what the arbitrators do in calling a clause construction award a partial final award. The Federal Arbitration Act provides for review of arbitration awards. And a couple of courts have refused the jurisdiction to entertain that, saying the FAA doesn't grant subject matter jurisdiction. Most courts to my knowledge have actually permitted the review, and whereas there is this one I think state court opinion which vacated that antitrust clause construction award. The vast majority of decisions so far that have reviewed clause construction awards have granted jurisdiction and have used the review standards of the Federal Arbitration Act which provides for extreme deference to the arbitrator's decisions. Yet the AAA has sections on what you need to show to vacate an arbitration award.

**MR. EDWARDS:** Let's go ahead and turn to the dessert, which is the Class Action Fairness Act, which Hollis Salzman is going to tell us all about.

**MS. SALZMAN:** Well, as many of you probably know, the Class Action Fairness Act, or CAFA as it's known, was signed into law February last year, so it hasn't quite made its first birthday. The primary purpose of the law was to federalize class action litigation, and I think that is what is actually happening. Except in very few circumstances, which have the criteria that are set forth for federal courts denying federal jurisdiction, almost all class actions now can be heard in federal court. There are other elements to the CAFA, that is the primary element.

The other way that CAFA has affected class action litigation involves the settlement of class action litigation where the settlement for class members is basically a coupon settlement. It also provides additional notice requirements for the defendant of settlement of a class action litigation in that they need to notify certain government officials.

**MR. EDWARDS:** Andy, is this good for defendants or bad for defendants?

**MR. SCHAU:** The short answer is it's good, and there are a couple of buts to that short answer. But the way I look at it, there are essentially four real benefits. The obvious one is efficiency. The case that Steve and I have, he describes there are multiple state cases in one MDL. I think Steve and I would like nothing better than to have all of those state cases brought and consolidated in front of one single judge so we could have one round of depositions, one round of briefing on the principal issues in the case, one set of discovery requests, etcetera, etcetera. I mean it's very hard I think to overstate the value of efficiency.

I think the second benefit, and I don't mean to malign the state courts in saying this, but I think that typically you can expect a more rigorous analysis of all sorts of issues from the federal courts. You can expect more rigorous Rule 23 analysis. I think you can expect more rigorous analysis on the merits, and I think you can expect more rigorous analysis across the board.

**MR. EDWARDS:** Federal courts are going to give Dr. Beyer a harder time.

**MR. SCHAU:** Perhaps. And I don't think that rigor stems from any lack of intelligence in state courts. I think we all know that state courts are under-staffed and under-resourced. Frequently they don't even have a law clerk. And I think it is just more difficult for state courts to give the kind of scrutiny that federal courts can give to any issue.

Consistent with that of course is that in federal court you have the benefit of the Dalbert decision which scrutinizes expert opinion and may or may not have an opinion on the acceptance of Dr. Beyer. But probably would not.

Lastly, in federal court you have the opportunity to at least ask for interlocutory appeal under Rule 23(f) of the

class certification decision. In state courts typically you have to seek interlocutory appeal; it is more common to receive interlocutory review in federal court rather than state court.

I think overwhelmingly the answer: Is it good for defendants? Yes.

A couple of buts. Number one, I think with all the indirect purchaser cases that are now going to be heard in federal court, you will see a lot more discussion about the desirability of overruling *Illinois Brick*, since the federal courts are now going to be hearing those cases. I think that defendants frankly can expect to see a more sophisticated and perhaps better funded group of plaintiff's counsel in Federal Court than they might see in a state court of similar action.

**MR. EDWARDS:** I think John was about to say something in defense of state court judges?

**DR. BEYER:** No, no. The indirect purchaser decision or the implication of the state courts is really a tough issue. And unless *Illinois Brick* is dealt with, it gets very complicated.

It's interesting, Canada, which is now experiencing class action, and we have some experience there, does not have *Illinois Brick*. And they are very proud of the fact it is an anti-American stand among the lawyers. We don't have *Illinois Brick*, and you have to show to the courts some reasonable empirical analytical tool for deciding how much of the elevation in price has been worn by the different layers, and that is a demanding set of issues.

**MR. EDWARDS:** Let me turn it back to Hollis and ask her from a plaintiff lawyer's perspective: Has Class Action Fairness Act had any real impact?

**MS. SALZMAN:** Well, speaking from my own practice as counsel for plaintiffs or indirect purchasers, we have always been trying to be in federal court. So in many respects we like the CAFA law. When we filed the brand name prescription drug cases, and those were cases filed in various state courts, it required a lot of parallel litigation going from state to state to defend motions to dismiss, to seek class certification. And even when the case ultimately settled we then had to make applications for preliminary approval and then final approval in eleven jurisdictions. As time went on, in the early 2000 period, the case of Coumadin was one of the first cases that was filed in federal court on behalf of indirect purchasers. What we did there was file for federal injunctive relief and used the court's supplemental jurisdiction to seek state law remedies, still in federal court. That was a successful model for cases to come.

So as far as it impacting my particular practice, I think it is a good thing and we prefer to be in federal court. Direct purchaser litigation is going forward in federal court and we think it is a better model to be coordinated with direct purchasers. There are plaintiff lawyers that do prefer state court, and I would believe that they are probably unhappy with the fact that they for the most part do not have that option available to them anymore.

The class certification process for indirect purchasers in federal court has been a complex matter, and some courts have actually taken the time to go state by state and really analyze the various state laws. At least I am hopeful that CAFA will promote the idea, that federal courts take the time to really look at the various causes of action and the various states' law. Because if they deny class certification post-CAFA, indirect purchaser plaintiffs will not have the state forum to seek remedy.

**MR. EDWARDS:** Now Andy, as I understand it, the way this is supposed to work is all these cases that are brought in state courts, Marion County, Illinois, Beaumont Texas, Mississippi, Alabama, they all get removed to federal court under CAFA; they all get consolidated in an MDL. Then when the MDL court addresses class certification, the defendants will inevitably argue well, judge, you can't certify a class under the laws of multiple states.

Is that argument now sort of contrary to public policy as articulated by Congress when it passed CAFA to begin with?

**MR. SCHAU:** Well, there are plaintiffs lawyers who are making that argument eloquently in the press, and I think there is some logic to it.

A couple of things that I would respond. Number one, I don't think Congress had indirect purchaser cases in mind when it enacted CAFA. So the effect that CAFA has had on antitrust cases is unintentional, but real.

Secondly, CAFA by design was not meant to change the substance of the law but was merely designed to change procedure. Now, that may be a distinction that sophisticated attorneys understand is fluid. But the idea that CAFA enacted a policy that now favors indirect purchaser cases is I think incorrect by reason of the fact that it wasn't intended to affect substance at all. That said, the federal courts will now have indirect purchaser cases before them. They are going to be there anyway. You can fairly ask the question of why should the citizens of one state not get the benefit of the *Illinois Brick* or the problems of *Illinois Brick* when other citizens do. It's a fair question. If Congress is thinking about addressing that, I would only hope that they would also recall *Hanover*.

**MR. EDWARDS:** Hollis, when CAFA was passed a number of commentators suggested that plaintiffs would try to take advantage I think of what people call the Home State Exception. And that would actually result in more class actions rather than fewer class actions. Can you explain a little bit what the home state exception is,

and tell us whether in fact that has resulted in more class actions?

**MS. SALZMAN:** I think you're referring to home state exception to the diversity—

**MR. EDWARDS:** Yes.

**MS. SALZMAN:** There is an exception, one of the very narrow exceptions that I was referring to in the beginning which is referred to as Home State Exception, which allows class actions to remain in state court if basically two-thirds of the class are residents of a particular state and the defendants are primary defendants, either the defendants reside in that state or the injury occurred in that state. I think that is a pretty narrow carveout, and I am not sure it is possible. I don't know any cases that have used that Home State Exception. To me it just seems like such a narrow carveout that except in very limited situations, where you maybe have something that is just occurring in one particular state and nowhere else and that is the only place you can capture it because that is where the defendants reside, that it is not going to impact class action.

**MR. EDWARDS:** Andy, maybe we can talk a little bit about whether CAFA has any *Erie* implications. What if you have a state, a situation where a state procedure makes it easier for a plaintiff to prove a claim, and then that case ends up in federal court under CAFA. Is that federal court obligated under *Erie* to apply the state procedure because it has a substantive impact?

**MR. SCHAU:** That is a very difficult question. Obviously, *Erie* requires the federal courts to apply their procedures and apply state substantive law. That said, there are some instances where, like we said earlier, the line between procedure and substance isn't entirely clear. I'll give you an example of that. Chief Judge Young up in Massachusetts was confronted with a multistate claim. He had to apply in his judgment state law to determine whether or not to certify classes, and he was therefore required in each instance to consider whether or not the state class certification rules were substantive or procedural. I think the most interesting example that he looked at is New York law. New York law I think it is 901(b) of the CPLR says there are no class actions in cases where the plaintiff is seeking a penalty unless the law that authorizes the penalty specifically provides for class actions. The Donnelly Act, which is our state court antitrust law, obviously or at least from the conclusion of Judge Young, and I agree with this, allows a penalty in as far as it allows for enhanced damages. And so he concluded that he would not allow in Massachusetts pursuit under New York law of a class claim. The plaintiffs argued vigorously however that 901(b) was merely a procedure, not substance, and that as a consequence Rule 23 applied under *Erie*. It came out in favor of what I would expect, which is the denial of class by a federal judge out of state as applied to the citizens of the state that don't have class action remedies.

**MR. EDWARDS:** Yes, I think actually there was also a recent decision by Judge Bear in the Southern District that I believe came out pretty much the same way.

Let me turn it back to Hollis and ask her to comment a little bit about the settlement provisions of CAFA. No more coupons?

**MS. SALZMAN:** That is a good question. I don't know if there will be no more coupons, but I think that plaintiff lawyers who pursue coupon settlements may be less likely to do so because of the application of review of attorneys' fees.

Just to back up for a minute. There are about six different ways that CAFA regulates. One is that it imposes standards for judicial review of coupon settlements, and it permits unclaimed benefits to be distributed to charities. These two parts of CAFA are really what's common practice now. Because the courts generally have written findings when you have a class action settlement approval, and courts have permitted class counsel to provide some kind of cy pres distribution either with remainder funds or with a bulk of the class action settlement funds. Some additional requirement, one that I alluded to earlier, was that federal and state agencies now have to be notified of proposed class action settlements. That obligation is on the defendants, and if notification is not properly served and given, class member will not be bound by the final judgment. There are very specific requirements for what the notice has to provide. It's almost in the same type of notice that you would see going out to class members, but now it is going out to state and federal government officials. If that notice is not properly drafted and served, it can be grounds for a class member that otherwise would be bound by a settlement to not be bound by the settlement.

It also provides for judicial review of attorney's fee awards and coupon settlements. It no longer allows an attorney's fee award to be premised on the full amount of the settlement fund, but will actually look at the amount of coupons that are redeemed. So if only 50 percent of the coupons are actually redeemed by class members, the attorney's fee award will only be based on that part of the fund.

In addition, the courts, instead of looking at the percentage of the fund, they will be looking at the actual hours that the lawyers spend on the case. I think this in many ways may be a disincentive for early settlement for plaintiffs lawyers, because if they have to show that they worked the case enough to merit an award of a percentage of the fund, that they may have to work further on into the case, rather than settle early.

**MR. EDWARDS:** You said that attorney's fee awards will be based on the percentage of coupons actually redeemed. Does the same thing hold true for cash settlements? If you have a reversionary fund, is the attorney's fee going to be based on the amount of the fund that class members actually claim?

**MS. SALZMAN:** CAFA does not speak to non-coupon, the review of attorney fee awards in non-coupon settlements.

**MR. EDWARDS:** So Andy, are these developments good or bad for defendants? I mean it sounds to me like defendants are going to have to pay more cash to get rid of these cases.

**MR. SCHAU:** I think that is right. I think that Congress intended through this provision to benefit the citizens who have had antitrust injury. I think everyone, plaintiffs and defendants, agree that should be the first priority, and it does do that for them.

To answer your more parochial question, I think it's probably bad for defendants, and I think it's probably bad for plaintiff lawyers who represent plaintiffs who don't have good cases. The reason for that is obvious. Defendants and plaintiffs have always managed to use coupons in an unseemly way, perhaps to bridge a gap between perceptions of a case. The plaintiff lawyers are happy because they get reimbursed on the full value of coupons, even if they are unredeemed. The defendants are happy because not all the coupons are redeemed. So I think it takes away that kind of cheap and easy settlement for the defendants. I think it also encourages plaintiffs and now plaintiff counsel, we now realize they have to be compensated on a lodestar basis to pursue their cases longer and spend more money on them, and I don't think that is particularly helpful for defendants, regardless of the merits of the case.

So that is a long-winded way of saying I think it is bad for defendants but good for the right people.

**MR. EDWARDS:** I am going to open it up to the audience right now, if there are any questions from the audience for any of our panelists. Yes.

**AUDIENCE MEMBER:** Yes, I wonder if Mr. Davidson could address settlements of class actions within the context of ADR or arbitration, and how does that work? Are there any lockout rights for example?

**MR. DAVIDSON:** Yes, if you look at both the JAMS and the AAA procedures, any settlement is supposed to be vetted before the arbitrator. It is the same basic standard as would prevail in court. While the differences between Rule 23, and at least the JAMS rules (and I think the AAA's as well), there is nothing explicit about appointing counsel or setting a fee. But that would be done in the usual course of these events.

One of the things that is not written into these rules is that—and I can speak to JAMS about this—is the mediation possibilities, not with the arbitrator, who may just arbitrate the case, but when you're sitting in the middle of a place well-known to mediate and resolve cases, many of the arbitrations, whether they be class actions or not, do not go the route because people decide to mediate them mid-stream. But the answer to your specific question is that settlements will be done in the same way, that is, under the same basic standards set forth in Rule 23.

Let me commend you to a publication which is going to come out soon, the end of next month. The College of Commercial Arbitrators is putting out a book entitled *Best Practices in Commercial Arbitration.* There is an excellent chapter in that book on class actions, which we all think will probably be the best guide for arbitrators who are faced with this and do not have the requisite experience with Rule 23.

**MR. EDWARDS:** Other questions? Yes.

**AUDIENCE MEMBER:** I am curious whether any of our panelists have thought about the applicability of CAFA to these things called class arbitrations?

**MR. DAVIDSON:** Not me.

**MR. PERSKY:** Speaking for myself, I certainly haven't, and I'd be hard pressed to understand how it would work. You're in arbitration.

**AUDIENCE MEMBER:** I am hard pressed how arbitration itself works, so it's not much of a stretch here.

**MR. PERSKY:** The supplementary rules of the AAS for example track Rule 23 very closely, and presumably settlements and things like that would be somewhat similar, so to pick up on the prior questioner's query—

**AUDIENCE MEMBER:** That is cool, but what if the contract is done by state law. Why would it make sense to have private rules of procedure on this strange device which may indeed differ completely from state laws because they have to be modeled on federal rules?

**MR. PERSKY:** If the parties have agreed that the applicability of certain rules, substantive or procedural, that is what's going to bind the situation. If they haven't specified the rules or the substantive law, then perhaps the arbitrators would themselves look to CAFA for guidance. But I really have no idea what the answer to that question is.

**MR. CHERRY:** Yes, I think I have the same answer. It is really a matter of consent as to what rules you incorporate. The awkward situation would be I think people are running into where the agreements have no rules. It is a blanket ad hoc arbitration provision, and you see something brought as a class action, how do you deal with that. I think what people tend to do is, even

though they didn't incorporate some rules, they go out and agree to incorporate at that point. Because they need some structure to deal with that situation, even though it wasn't contemplated, the manner and the country.

**MR. EDWARDS:** We have time for one more.

**AUDIENCE MEMBER:** I have a question for the experts. I was wondering if you could picture an industry where on a price-fixing allegation an expert would not be required to certify a class to prove common impact, and conversely, where the industry is so complex that plaintiffs would require an expert to certify the class. What would be the features of those industries, if you have any thoughts on that?

**DR. BEYER:** I shouldn't say this because it affects my living, and that part of my firm, Nathan & Associates. But in fact, many industries have characteristics that I described before that don't need an expert. It's just a question of somebody articulating what these are. One that comes to mind, although the experts were involved, I was involved, was infant formula. I mean it is, every can of infant formula, whether it's made by Mead or Ross, two or three of the pharmaceuticals out there, Abbott, are exactly the same. Why is it exactly the same? Because the FDA specifies what goes into it. You can't make infant formula without having the FDA recipe. And also the one exception that I referred to earlier is infant formula, there is no negotiation. The suppliers simply say this is a price. You want it? You get it. You don't pay it, yes, too bad, go somewhere else. There is nowhere else to go. So even Wal-Mart, we think as a great giant, it says please, give us enough of the infant formula at the price you demand that we pay. And it's the same for everybody, mom and pop, Wal-Mart.

**DR. PALMER:** I think in addition, you wouldn't need an expert if there was something clearly that defined how something happened, and you could lay that out very clearly. Often the experts get involved because there is not really a theory of what goes on or there is some common impact and you can't identify it. If there were some other criminal proceeding or something that clearly laid out something ahead of time, where you have something very clearly identified of how it happened and it wasn't subject to negotiation or adjudication or there weren't issues involved, then I think you wouldn't need an expert in that case. But often it is not clear if there is a theory of how prices move or something like that, where you do need an expert to examine it and put forward how it actually happened

**MR. EDWARDS:** You know, I was hoping I could provoke a fist fight between John and Brian, but I guess I wasn't successful. Perhaps, that is because they both have been affiliated with the Fletcher school and they have that in common. In any event, that concludes our panel. It is 3:00 o'clock, and I thank our panelists very much.

**MS. GOTTS:** Our next session is on the Antitrust Modernization Commission and we'll shift to what ought to be.

# Antitrust Modernization Commission: What Has it Done? What Will it Do?

**MS. GOTTS:** Our next panel is going to look at how the world ought to be. We have been talking throughout the day about various aspects of the law—i.e., "what is the law," starting out with the annual update of developments, followed by a discussion of single firm conduct, and the last panel on class actions and arbitration. One of the interesting developments over the last few years was the formation of the Antitrust Modernization Commission.

When I first asked Makan Delrahim to plan this session, he had just left the Government and was not even sure where he was going to work. He is going to be our moderator for this panel. Makan is the former Deputy Assistant Attorney General for the Antitrust Division of the U.S. Department of Justice. He has a long history of dealing with issues of antitrust and intellectual property and extensive experience in his capacity at the U.S. Department of Justice with the International Competition Network. So he was well suited for his appointment as a Commissioner of the U.S. Antitrust Modernization Commission.

Prior to his service at the U.S. Department of Justice, Makan served as the Staff Director and Chief Counsel of the Senate Judiciary Committee, working as a policy advisor for then Chairman Orrin Hatch.

With that I am going to turn it over to Makan to introduce his panel. Thank you.

**COMMISSIONER DELRAHIM:** Thanks, Ilene. I apologize to you, I started losing my voice, so I am going to keep my speaking to a minimum. Let me introduce our panels and my fellow Commissioners on the Modernization Commission.

John Jacobson is a partner at Wilson Sonsini Goodrich & Rosati.

He was appointed by the then Senate Majority Leader Daschle. I will go through some of the makeup of the Modernization Commission. We are fortunate to have him here. I was personally grateful he agreed to be here.

Roxane Busey is kind of familiar to each of you. She chairs the ABA's Antitrust Section Task Force on the Antitrust Modernization Commission, which has been very helpful to the Commission in organizing the hearings, setting the agenda for a lot of the things that we have been discussing and very thoughtful comments that many of you have participated in.

Debra Valentine is a Commissioner on the Modernization Commission, one of the original appointees and from the House leadership.

And finally, and not unfamiliar to many of you in New York, Don Kempf, who is an appointee also from the House leadership.

Let me give you just a little background on the Modernization Commission. It was legislation passed in 2002, and for several years it had been pending by Chairman Sensenbrenner of the House committee. He had concerns about the antitrust law particularly dealing with a new economy and anti-intellectual property. He was one of the biggest critics of the case against Microsoft. So some have written he might have been motivated by the case and the concerns raised surrounding the case.

Nevertheless, he introduced legislation with some specific goals to look into those issues. The legislation did not advance until late 2002 as part of a conference report on the reauthorization of the Department of Justice. It was modified to have a very broad mandate, because I guess people didn't want to look at specific things where there is something wrong. So the language of the direction to the Commission became—it doesn't really say much—look at the antitrust laws and recommend if there is anything you think should be changed. It is a very loose direction of looking at antitrust in the new economy. But it was this mandate to the Commission which granted the wholesale look at the antitrust laws, which has become a challenge.

Twelve Commissioners structured in a bipartisan manner. The President appoints four, the House and the Senate leadership each get to appoint four, and no more than two can be from a particular political party.

After it got its funding and final appointments were made, the Commission began its work March 31, 2004. Its mandate is to study the laws for three years and report back to Congress and to the President with its findings. We do not have any authority to change any regulatory process or the law. We are just an advisory committee to Congress and the President in this role. Thank God.

We had an initial meeting, and public meetings, which are governed by the Federal Advisory Committee Act, and so everything we have to do falls within the Government and the Sunshine Laws. A lot of times that is a good thing. Sometimes it can be a challenge because we may want to look at a particular issue, but all of a sudden you have interest groups going to Congress threatening budgets of the Commission or otherwise, writing letters, and it becomes very difficult for us to have a candid debate and discussion and make a recommendation which may not be politically salient. However, from a matter of policy, a wise recommendation.

Looking at the antidumping laws for example, was one issue that the Commission considered looking at until it got very heated in Washington, and then it decided it was outside of our mandate.

Public hearings have been held starting June 2005; and it is going to be going until next month. The final one will be February 15. It will deal with international issues as well as a wrap-up that will include hopefully by then fully Senate confirmed Tom Barnett in the Antitrust Division and Deborah Majoras the chairman of the Federal Trade Commission. As I mentioned the report is due April 2007. The committee's work is on the web site AMC.gov. The transcripts from the hearing are all on the web site and available to you should you wish to look at what we have been up to.

One of the first things we did was issue selection. We looked at public comment from various folks to where do we start, what do we look at and how do we look at these issues. Everybody has views, but what is an organized way we can go to this and really finish this task in three years?

So we held some hearings. We had some subcommittees that were formed to look at and suggest various issues, and the full Commission agreed with those. We have had some public comment. Then we began looking at each of these at different hearings that have been held. There have been over 25 issues, and many of them subissues, some controversial, some mundane and boring, that the Commission has selected to look into.

I will be turning to each of my colleagues on the panel asking them to elaborate more within each particular area. But you can imagine we are looking at civil enforcement, the structures of the enforcement agencies, mergers, second requests, criminal procedures, issues that were discussed in the previous panel, *Illinois Brick* and *Hanover Shoe*. We even looked at patent reform issues currently before Congress and the Supreme Court with E-Bay which they are considering, and how those affect competition.

There are many views and great testimony the Commission got from various experts within the field. I think in every Commissioner's view it was informative. I think many Commissioners found, regardless of political strike, some of their colleagues' views surprising, thoughtful at different times. For me personally it has been a great experience just seeing the different issues that have been presented and the comments made about them. It doesn't follow the Republican model that the antitrust laws should be repealed, or that every Democratic appointment is out there trying to bring a Section 2 case to the grocery store next door. Hopefully, one of the things the Commission will do is throw those views away. I think antitrust has become, and thank God, one of the areas that is really apolitical. And hopefully the direction that the Commission recommends and will give to Congress and the Administration will hopefully begin a debate and a useful discussion of some of the areas where we can improve competition and the competitive process.

With that I would start with Commissioner Jacobson. He was the chair of the Section 2 Monopolization Working Group Subcommittee of the Commission and looked into those issues. I will turn to him to discuss what his views are, the issues that were presented and what the issues that the Commission decided to study. That will give you a better idea of the direction, and then we'll open it up to debate and then go to each of our colleagues who have looked at the specific issues.

Commissioner Valentine was one of the leaders, not only in the area of the international field, but looked at and helped the Commission look at the merger review process, the Hard-Scott-Rodino process as well as the enforcement institutions. Having been from the FTC she didn't want some of us DOJ folks try to take jurisdiction away from the FTC.

Commissioner Kempf has very strong views on privileges and immunities. I think the Commission is unanimous in that area as far as trying to limit immunities in the antitrust laws, but also views on the civil enforcement process. And so he'll touch on those. Then we'll hopefully have a lively debate.

Roxane Busey has provided great comments on many of these issues to the Commission. She will help let us know what the Antitrust Section's views have been and what direction they have given us.

With that, Commissioner Jacobson.

**COMMISSIONER JACOBSON:** Thanks a lot, Makan. Being on the Modernization Commission is fun. If you're an antitrust lawyer there is nothing better to do than to get a mandate from Congress to look at everything and decide what's good and what's bad. So among my list of things that I like to do, being a Commissioner is really at the top of the list.

When you get twelve people together and your first assignment is what issues are you going to look at, it's a challenge to get a narrow list. And I think each of us came into the process thinking well, gee, we ought to have a narrow list so we can look carefully at these issues. Our narrow list was 25 issues, some of which are sort of shockingly large just themselves. Like what do you think of each of the 40 exemptions that are out there in the antitrust laws? What do you think of merger enforcement? What do you think of private enforcement? What do you think of governmental enforcement? And there were also a few things, like dumping, where every international trade lobbyist in Washington came to our

meeting to make sure we didn't evaluate that issue. But apart from that one, just about everything else is opened up and is part of what we are looking at. It was going to be a challenge to do a good job on all of them, and hopefully we will do a capable job on all and maybe a good job on a few.

I am going to talk briefly about single firm conduct. But also one of the areas we have been looking at is remedies, in particular private remedies, and I want to talk about that first just for a few minutes.

Among the issues that we are looking at are should there continue to be a treble damage action? Should there be a right of recovery of plaintiffs for treble damages? Is a single damages multiplier as effective? Do we need private enforcement at all? We had a really excellent panel on that subject. It was fairly early on in the hearing process, but at the end of the day there was really not much of a case for cutting back on the treble damage awards. The one witness who we had who was designated to speak sort of against treble damages, at the end of the day took the position that, well, only where it is really an uncertain area of the law, like joint ventures, should you go the single damages route. There was quite a bit of evidence submitted to the Commission that since you don't have prejudgment interest, a lot of courts also look askance at opportunity cost as a measure of damages. If you look at it economically, when people actually recover treble damages, which is not all that often, it really turns out to be single damages when you take all factors into consideration.

So I don't know how the Commission is going to come out on this, but I will say that any objective observation of the record that was created would not provide much, if any, support for cutting back on treble damages. And Don Kempf is here, so to the extent I got this wrong, I am sure we will hear about that a little later on in the program.

We also looked at the contribution among joint tort-feasors in the antitrust context which has been a major antitrust issue for 20 some years since the *Professional Beauty* case came out of the Eighth Circuit I think in 1978. And our hearing covered those issues as well, although not in the depth that we covered the basic treble damage remedy. I do believe that the Commission will give a fair shot to the argument that the day for contribution in antitrust cases has come, and the case for continuing the no contribution rule is questionable.

If you go back to the Supreme Court's decision in *Texas Industries* back in 1981, they basically didn't say a no contribution rule is better. They said, well, we can't change the law without some mandate from Congress. Now, they did that in a Congress where Congress had never said what the law is. So it's an appropriate subject; maybe some of the others that we are looking at aren't, but clearly an appropriate subject for the Modernization Commission.

**COMMISSIONER VALENTINE:** And you know, John, one interesting thing-—and I am not sure we have woven this together very effectively—we were also looking at some criminal issues that you might want to talk about, including the latest amendments to the statute that covers cartels and allows first-in leniency applicants to just get single damages, which is effectively getting out of their joint and several obligations to their other tort-feasors.

**COMMISSIONER JACOBSON:** Right. We have two decisions when you qualify for single damages treatment, but no one yet has come to grips with the impact on the other defendants of a decision to award single damages to the amnesty claimant. And I think that is another issue lurking out there. We don't know if that is going to completely upset the apple cart on contribution among the other defendants or at least claim reduction among the other defendants. This is one of the subjects that hopefully the Commission will address in some detail in its report.

The other sort of remedial hearing that I wanted to talk about is we had a public hearing; it was actually our first hearing on the *Illinois Brick* set of issues. We had Dick Steuer come to present the ABA's position. We had a representative of the indirect plaintiffs bar, a representative of the direct plaintiffs bar, and some other witnesses. At the end of the day that hearing generated an awful lot of support for some variant of the American Bar Association's proposal, the gist of which is fundamentally repeal *Illinois Brick*, repeal *Hanover Shoe*. Have all the cases been brought to a single forum, which certainly has been made easier already by CAFA, as you heard from the last panel. Will there be a single treble damage recovery rather than multiple recoveries?

Among what legislative recommendations the Commission considers, I think that one will be viewed pretty favorably at the end of the day. As I said there was quite a bit of support for that in the hearing. Although there was some disagreement at the edges I think, the direct plaintiffs bar, in particular, isn't very happy with *Illinois Brick* reform as it is under the status quo, but I think everyone else would be quite content with the ABA's position.

On single firm conduct, we initially decided to look at the broad question of what is anticompetitive conduct under Section 2, and then looked back and said wait a minute, with all the other stuff we are doing, if we have a three-year life, this is a twelve-year project in itself. So the Commission made a decision to narrow the evaluation of single firm issues to the bundling issues raised in *LePage's* and *Concord Boat*, and to the issue of the appropriate standard for unilateral refusals to deal, such as the *Trinko* type case.

Again, we had a really excellent panel, very high quality presentations, and a window, at least, on a consensus in a couple of areas.—one on bundling. Clearly, everyone agrees that you need a little more clarity than the *LePage's* decision gives you in terms of what bundling practices are procompetitive, what bundling practices are anticompetitive. You can't just give it to a jury and say is this okay. The standard that seemed to emerge with pretty good consensus, even among this diverse group, is some sort of incremental cost versus incremental revenue standard. Such, that you take the bundled product against which the plaintiff has a single product, but the defendant has two products and those are the products being bundled in by the multi-product defendant firm. And you look at the defendant's incremental cost on the tied product and the incremental revenues associated with the pricing structure with regard to that incremental product, and you determine whether it's above or below cost on that basis. Not a *Brooke Group* test of looking at the total cost and the total price, but looking at the price associated with the tied product and the costs associated with the tied product. Although I think a lot more study needs to be done in that area, I think at least this very high quality panel seemed to think that this was a fruitful direction in which to go.

The other subject on which there was absolutely no consensus at all and where it will come out on this is anyone's guess, is the standard for single firm refusals to deal. There was a useful distinction made between two types of unilateral refusals. One, the refusal where you're dealing with your customers and suppliers, so that you're disadvantaging a horizontal rival by cutting off their customers or their source of supply. You call that a vertical refusal to deal; and there is the so-called horizontal refusal to deal, where a rival is asking for access to your own asset, as in the *Aspen* type situation, or at least arguably, in *Trinko*.

There was a lot of testimony that the no economic sense test that the Justice Department has been parading for a few years might make some very good sense, at least in the context of the horizontal refusal to deal. There was quite a bit of advocacy to look at the overall impact on consumer welfare. Again, on this particular set of issues there was certainly no consensus among the panelists. As to where we are going to come out on this, I think is anyone's guess.

Each of us could talk for many hours on all of the various issues that we have covered, but that gives you a sense in two areas of what we were looking at and where I think we might be coming in.

**COMMISSIONER DELRAHIM:** Okay, we will go to Debra.

**COMMISSIONER VALENTINE:** I'll take mergers and some of the issues associated with the various enforcement agencies—our federalism so to speak—that we have been addressing.

I would like to start with the thought that there has been a lot of modernization in antitrust simply going on incrementally over the last decades. The concept that we would make any major changes or radical surgery to antitrust concepts on which there is essentially a bipartisan consensus seems to be an act of either extraordinary hubris or amazing stupidity.

So while this may not be as exciting for you, do not think that one we will be seeing radical changes coming out of this group. On the other hand, as an historian before I was a lawyer, while certainly we can learn from the past, antitrust enforcement will not go on forever. In moving forward, we will quite frankly only be as good or effective as we are persuasive. So that again suggests that unless we can reach consensus on some of the more important issues, we are not going to be terribly effective. So it is going to be an interesting balance as it all plays out.

When we get to the merger issues, the questions that were asked were relatively broad on the merger side: Has current U.S. merger policy and particularly enforcement under the existing horizontal guidelines been effective? Has it impeded U.S. companies from competing internationally, things like that. What was extraordinary here is that the testimony from all panelists whom we heard demonstrated amazing consensus. Everyone thought the guidelines were just fine. And while there might be some quibbles, they were not from the panel addressing Merger Guidelines and enforcement. Rather, the panel addressing new technology and high tech markets said that we ought to think about encouraging the agencies to update the guidelines to focus on how they impact innovation and innovation markets. But the people who were testifying on the guidelines themselves said "those Guidelines are fine, people understand them, the courts understand them, don't tinker with them." Maybe some learning will get us to the point in ten years from now where we'll want to change, but certainly not today.

Our second question was: Do the horizontal guidelines accurately reflect how the agencies analyze mergers? I think some of the recent FTC reports indicate that enforcement may well be occurring far above the 1,800 threshold. But there is a pretty good understanding of what current merger enforcement is about and how the agencies are proceeding and where they are going. And again, there was no hue and cry to alter things in any major way there. I think we'll also want to defer somewhat to some of the work that Chairman Majoras is currently spearheading on the guidelines.

In terms of whether our federal enforcement agencies and courts appropriately consider efficiencies from mergers, this may well have been the one area where

people considered whether there should be some move away from what is a strong consensus on a consumer welfare standard. Some asked whether the analysis of efficiencies should employ a total welfare concept the way that Canada does. I can't say they were strong advocates here. There were people that spoke somewhat persuasively about trying to give the public, the companies and the bar a better sense for what constitutes innovation efficiencies, when will they really count and can they be analyzed somewhat more flexibly. So even if one isn't approaching it from a total welfare perspective, one may be accommodating for efficiencies over a longer period of time or taking account of the greater disruptiveness in some of those markets.

And finally, how do we improve Hart-Scott-Rodino merger process, and particularly the second request. Here there were some very thoughtful and constructive, not earth-shattering again, suggestions largely about amending the second request process, largely about trying to say to the agencies: Can't you limit either the number of custodians whom you're going to search, the number of issues that you will search, the number of questions that you can ask. And I think at the end of the day there will be some strong effort to work with the agencies at trying to get them to agree to something that makes more sense.

I am not sure that anyone was more enamored of any other system worldwide. We didn't hear a strong cry for actually having a finite time to the second request process. But there is no doubt that with the increased amount of electronic discovery, the process of production is becoming virtually unbearable; a burden that is only right to think about.

One of the interesting things is that many of us, at the end of the day, would say that the process can work well right now, if you have fair and honest lawyers on the defense side and some of the smartest staffers on the agency side. And when you have staffers on the agency side who know what they are doing, who understand the case and don't mind paring or honing requests because they know what they want to look at, you're really in great shape. So maybe one answer here is simply better training at the agencies.

When we move to enforcement institutions, here too I think we may propose what's practical as opposed to what would be ideally desirable. It is certainly strange when you go overseas to say: "We have got this great merger enforcement system and two federal agencies enforcing mergers." On the other hand, no one said get rid of one of the agencies. We did hear some of this in private conversations we had with individuals before we actually selected questions to investigate and opened up for public hearings. One ex-DOJ official was very strong in urging us to get rid of the FTC. I'll let you guess who it was. But when you get right down to it, it works relatively well. Again, continuing with two agencies seems to be the prevailing opinion so long as you can work out clearance. And what I think one might be seeing coming out of the Commission, and again this is just my view, is a strong recommendation to Congress that it ask the agencies to implement a clearance procedure along the lines proposed in 2002. Getting Congress involved proactively up front, rather than having Congress hear about it at the last second as it did in 2002, convincing Congress that the business community, the bar, the Commission, everyone thinks that some simple rational process for clearance and for dividing up which mergers go to which agency all makes a ton of sense. Have Congress ask the agencies to do it, and I think that the agencies could sit down and at least at the senior level reach a pretty simple consensus with a simple way to resolve disputes in those few areas where there are overlapping jurisdictions, or industries that are changing (in the telecom and healthcare areas), or trade arrows or whatever.

Roxane and the ABA made a sensitive submission on the role of state attorneys general and private parties. Don may have some strong feelings about that. But again, if you were to canvas everything that we got on what role the states should play, while there may be sotto voce sentiments that this isn't a rational system, I don't think there is anyone who thinks you can get the states out of antitrust enforcement tomorrow. And there are a fair number of people who are willing to think constructively about how the federal agencies and the NAAG task force can work more proactively to try to allocate mergers. So that when you have relatively local issues, let's say some funeral homes or some shopping issues, maybe dry cleaners, you give them to states. When you have other very nationwide or cross-border types of situations you have the feds largely looking at them. Same idea could go for cartels. There are a lot of small bid-rigging cartels that are hideously impactful on local markets, and then there are cross-border cartels that the feds probably should be coordinating with Europeans. So those will be my initial tentative thoughts on our state and federal system. I'll be interested to hear from our other panelists on what they thought they were hearing from all the witnesses who testified to us.

**COMMISSIONER DELRAHIM:** Thanks, Debra.

Don.

**COMMISSIONER KEMPF**: Thanks, Makan. To me the antitrust laws are like Rodney Dangerfield. They don't get no respect, or at least not the respect they deserve. The reason they don't is because there are so many antitrust exemptions and immunities. And I am always reminded of what I call the tale of two guys. John Doe and his brother Jim, farm boys raised out in Smallville, Iowa. When they grew up they went into the farming business, John as a farmer and Jim as a seller of farm implements.

John ran a very successful dairy farm and Jim ran a very successful dairy farm equipment business. One year they both engaged in price fixing and they were both good at it, and at the end of the year they both got their picture on a cover of a magazine. John Doe got his picture on the cover of Iowa Farmer Monthly as the man of the year and they held a big banquet for him. Jim got his picture on the cover of the Iowa Police Gazette and they took him off to jail, both for doing price fixing. The difference between them is one does it under the auspices of antitrust exemptions and immunities and the other does it without that benefit.

Since so much of the economy is burdened by price fixing and so many people engage in price fixing so often with complete non-risk of liability, there is not a healthy sense that I think there should be that price fixing is something wrong.

One of the things as has been mentioned previously that we as a group have studied is the possible elimination, repeal, sunsetting, etcetera of antitrust immunities and exemptions. But when we talk about it, I am always bothered that we seem to focus on what I'll call unimportant ones and never seem to address what I would call important ones. What do I mean by that? There is a lot of discussion about should we eliminate the baseball exemption? The baseball exemption says that baseball cannot have free agency, like the other sports do, and it is not a problem under the antitrust laws. But baseball is so worried about losing their antitrust exemption that they act as 318 if they didn't have it to start with. So I do not think we ought to invest a lot of time in trying to repeal antitrust exemptions that people don't use. Similarly, the Webb-Pomerene Act that says if you and I want to form a widget company, you and I each have competing widget makers in the United States and we want to sell them in Bolivia and Bulgaria there are certain actions we can do jointly--set our price. There are very few Webb-Pomerene things, especially new ones, and they have almost no impact on anybody who buys anything in America. Is it a high national priority to make sure that widget buyers in Bolivia and Bulgaria don't pay a couple pennies more? I don't think so.

Now I would contrast that with the substantial number of farm antitrust exemptions. Those impact everybody in the United States every day and cost us billions of dollars and the Norris-LaGuardia and Wager Act, which affect everything we eat or drink all day, everybody in America, and costs billions of dollars. When I think about that, I say well, do we really "believe in antitrust" or is that just a lot of rhetoric. I think of cases like *Northern Pacific* that have the wonderful language about how we stake our bedrock on free and open competition, and believe that not only leads to the best economic outcome, but the best political and every other kind of outcome as well. But when I see people who say, you know, we got to be tougher on antitrust, we can't have all of these exemptions and immunities, I say, well, should we get rid of the two big ones? They say well, I don't know about that. When I hear that, I also say doesn't that raise the per se rule? If across a wide spectrum of activity in Congress, and at agencies, they can enact rules and regulations and laws and enable people to price fix willy nilly, shouldn't we also allow the courts to consider the same arguments and not have a per se rule that does not apply in other places where the test presumably in Congress is a question of reasonableness?

So I sort of say to myself, if we are going to have a Rule of Reason, maybe we ought to go back to what we had and have it open for all arguments, many of which are not permitted in court but are routinely successful in Congress or with agencies.

Let me add one thing to what Commissioner Jacobson said, and that it has been a lot of fun to serve on the Antitrust Modernization Commission. There are widespread views on the Commission, and notwithstanding, there is a tremendous sense of collegiality. We work very hard and we work together, and it has been a pleasure for me to do that. I do have always a bit of a concern that there is perhaps a bit too much of what I'll call inside baseball perspective that predominates both among the Commissioners and among those who testified in front of us. I remember I was called up by a journalist, harkening back to something Makan said in his introductory remarks. The journalist said are you one of the Commissioners? I said yes. He said I've heard there is a lot of right wing fanatics that want to completely redo the antitrust. I said that is absolutely not true, only one Commissioner comes close to that. He said who is that? I said that would be me. And my view, which my fellow Commissioners know, is Section 1 is very important, very important. We would do wonders for the economy if it were more strictly enforced as it is, and if there weren't so many exemptions and immunities to it. 99 percent of the immunities and exemptions are to Section 1, which is price fixing. We should have less of those and more enforcement. As for the rest of the antitrust laws, you know, there is some new scholarship that has been published by Bob Crandall of the Brookings Institute and others that say that antitrust enforcement may do as much harm to America as it does good, perhaps even more. Outgoing Assistant Attorney General for the Antitrust Division Hewitt Pate said that is something we ought to look at. We decided not to do it as an assignment of ours, partly because of the time considerations. But also, it is something we could end up perhaps recommending be done longer term by someone other than ourselves.

In any event, I have comments on a number of other things, but we'll save those for the free-flowing discussion.

Makan, back to you.

**COMMISSIONER DELRAHIM:** Thanks, Don.

Roxane.

**MS. BUSEY:** First of all, thank you, Makan, for inviting me. As you can tell I am the only non-Commissioner here, so I can speak a little bit more freely. But what I have to say is probably less important to you all.

I was selected to be chair of the ABA Antitrust Section's Task Force on Modernization. When I accepted the position I thought h-mm, we'll just look at a couple of topics, and then lo and behold they picked 25 topics, so my job expanded. I chair a task force that has about twelve people on it, and it is a very good task force, but I want to give you a quick lesson in ABA 101. The task force is liaison to the Commission. Its function is to monitor what the Commission is doing and also to coordinate the preparation of comments, and so literally the task force works with a number of people in the Antitrust Section. I know Bob Hubbard and Ilene Gotts who are here actually worked on some of the comments submitted. Those comments were reviewed by the task force and then sent to the Council of the Antitrust Section. Nothing can be submitted to the Commission until it has been approved by the Section's Council. Then those comments have to go through the rest of the ABA. There is actually what I call veto power. If we are commenting on criminal antitrust remedies and the Criminal Section of the ABA doesn't like what we say, they can veto our comments.

I am telling you this because the comments you have in your book and hopefully more that will be coming are the work of many people. They have been vetted through a lot of ABA procedure. So far we have submitted comments on ten subjects, and I think you have all of them. We have another handful about eight, that have been approved by our Council, so they have gotten through those first two steps that I mentioned, but they have not yet been vetted through the ABA. We hope to do that shortly.

A couple of those eight are based on prior positions of the ABA, so I will feel free to talk about the ten that have been submitted and that you have, and I will also feel free to talk about the three that haven't been submitted yet but reflect existing ABA policy.

Just to be clear as to what those are, there is a prior position on Robinson-Patman which actually nobody has mentioned up here. There is a prior position on McCarran-Ferguson which actually no one has directly mentioned up here, and then we did submit an amicus brief in the *Independent Ink* case, the Supreme Court case dealing with the presumption of market power for patents and copyrights. So those are three other things that I feel that I can talk about.

What I would like to do today is briefly go through the comments that have been submitted, to give you some idea of what the position of the ABA Antitrust Section is. I will tell you though, if I don't get through everything, every one of them has a summary. You can very easily go to the particular comment and get a sense of it just by reading the summary.

I would like to start with a few that have been mentioned already, just to give you some sense of where the Antitrust Section is coming out. If you don't agree with these, join the Antitrust Section and express your views.

One Jon Jacobson mentioned is on contribution. The Antitrust Section does support contribution and claim reduction after trebling. This was a position that we took in 1979. You should know there was legislation that was pending in 1979. Don and I think you might have been involved there—

**COMMISSIONER KEMPF:** Which one?

**MS. BUSEY:** The '79 legislation on contribution.

**COMMISSIONER KEMPF:** Yes, I testified in Congress.

**MS. BUSEY:** We continue to advocate that point of view. The legislation did not pass, because although there was support for it in Congress, there was a feeling that it should not apply to pending cases. That killed it, all of it. So it wasn't even applied to future cases. We feel strongly enough that we have not only taken that position but we have actually submitted to the Commission draft legislation, so we hope they seriously look at that. There are a lot of issues pertaining to how it would actually be implemented, but that is one I would bring to your attention.

On indirect purchasers, which Jon also mentioned, we did not submit a paper. But as he mentioned, Dick Steuer did talk about what the Section has called its illustrative legislation. This is a topic near and dear to my heart. When I was chair of the Section I did the chair's showcase program on Duplicative Remedies. It was picked up the next year, and a couple day forum was held on what to do about indirect purchasers. From that a task force was formed, which Dick Steuer chaired, and there was no consensus, no position other than something should be done about *Illinois Brick*. There was also illustrative legislation that was set forth. The concept being that there are a lot of different ways to improve upon the indirect purchaser problem that we have. None of them is perfect. All of them will be difficult to pass, and illustrative legislation might be a way to go.

Now, this was before the Class Action Fairness Act, and you heard about that. So there may be some feeling that that has improved the situation. Nevertheless, the

illustrative legislation suggested that *Illinois Brick* should be overturned so there could be a federal right of action, *Lexecon* should also be repealed to allow consolidation not only at the discovery level but also at the trial level. As a compromise position for plaintiffs, who will vigorously oppose this or so we thought, there should be recovery of prejudgment interest by the plaintiffs. And although controversial, there was no preemption of state repealers. So we think that is an important one.

No one has mentioned criminal remedies, so let me just say we did take a look at criminal remedies, and we did suggest to the Commission that they should ask Congress to ask the Sentencing Commission to study the basis for the use of the 20 percent of commerce as a proxy for affected harm. There was also some discussion about "twice the gain of loss" under the alternative fine statute. In that context it is not clear whether twice the gain of loss would be that of the individual defendants or entire conspiracy. That is obviously an area that needs clarification, but the Antitrust Section thought that should be something decided by the courts, not by the legislature.

With respect to the topics that Debra talked about, one thing that Debra didn't address was the different standards on merger review. The ABA came out fairly strongly and said we think there is a difference, depending on which agency reviews it, and we think there are different standards that apply. So the Section came out and said we think there is a difference, but even if there isn't, there is certainly a perception of difference. That isn't right. It shouldn't depend on which agency reviews the transaction as to the standard for merger review.

**COMMISSIONER VALENTINE:** Actually, if I can interrupt there, since I did mean to address this. There was an impression that when you are taken to court and challenged by the DOJ and FTC on your merger, there seems to be a different standard of review, although no one could point to a single case that they thought might have come out differently had the FTC standard been applied to the DOJ case or the DOJ standard applied to the FTC case. I think there is a sense of "why not have the same standard."

But what was interesting during the course of that particular hearing and the discussion of the panel was that they also seemed to be increasingly advocating a very interesting concept, which was that the FTC should not have the right to pick between part 3 or going to court. Rather both agencies should have to go to court and the proceeding should be a combined PI permanent injunction, using the same standard, which might be slightly more deferential than what the DOJ currently has in court. But it was one of the those interesting issues that evolved as we discussed it with the panelists who were testifying.

**MS. BUSEY:** What the Section said is they would recommend that the Commission recommend that 13(b) be amended to exclude mergers, so that the different standard in 13(b) would not be applicable to FTC proceedings.

**COMMISSIONER JACOBSON:** I think there is a widespread concern among the Commissioners if there is a different standard, which a lot of people don't believe, it shouldn't make a whit of difference whether your deal is reviewed by the DOJ or FTC, and I am confident we'll say something like that.

**MS. BUSEY:** Right. The other question that came up before the Antitrust Section is whether there should be any administrative proceedings challenging mergers. And actually the Section backed away from that and said they respect the administrative process for mergers, but they don't think that it should immediately follow the failure to win a preliminary injunction.

**COMMISSIONER VALENTINE:** That is interesting. In terms of the FTC being be able to choose, I think many voiced the concept that the only way you go to Part 3 is if both the party and agency agreed and/or if it involved consummated or vertical or conglomerate mergers or something like that.

**MS. BUSEY:** The Section also commented on the second request process, which Debra has mentioned, and on the role of state enforcement which I think has also been mentioned.

I think on clearance, the Section took a very strong position saying we have put up with this inadequate clearance process long enough. There should be a legislative change, and we hope the Commission recommends that. At one point the agencies said they would clear everything within nine business days. That was in 1995. So the Section decided to say we want legislation saying everything will be cleared within nine business days, and if not, there should be some type of penalty. At least some options for penalties are spelled out in the Section's comments. So this is one, where the Section has taken as strong a position as it feels that it can on this particular topic.

**COMMISSIONER VALENTINE:** We, speaking now for the ABA, did say maybe there would be no right to a second request, but also said a number of different things.

**MS. BUSEY:** We don't care what the penalty is as much as we care that there is actually a time frame, it is legislative, and there is a penalty.

Let's see. I think the only other one that I will comment on is merger enforcement. I think the exemptions one is worth noting. Don has mentioned that. We did take a pretty strong view, as you would expect, that there should be limited exemptions and that there should actually be an analytical framework used by

Congress in considering new exemptions and in looking at old exemptions. There was a consultant's report that was presented to the Commission which also set forth an analysis. We didn't have the benefit of that, so we didn't comment on that. But our analysis is pretty strict. Basically, the Section has said that the Magna Carta of our economic capitalistic system is our competition laws, the antitrust laws. So unless there is some policy coming from Congress that is not consumer related, which is the key that trumps that policy, the antitrust laws should apply. So an example would be national security. If we need to have something in place because of national security, that might be an example. Another would be constitutional things, like state action, Noerr-Pennington. Otherwise if it is consumer related, forget it; that is within the gambit of the competition laws which Congress essentially has stated is the law of the land.

That is a brief summary of what we have done. We have taken it very seriously, and we are very encouraged by the Commission and the way it is proceeding. And we are looking forward to seeing what recommendations it ultimately makes.

**COMMISSIONER DELRAHIM:** Thanks, Roxane.

**COMMISSIONER JACOBSON:** May I be allowed one back at Don?

**COMMISSIONER DELRAHIM:** Please do.

**COMMISSIONER JACOBSON:** The good thing about Don is he is not only not afraid of controversial issues but he will bring them to the top of the list. I really don't think there is going to be a lot of controversy among the Commissioners on things like Capper-Volstead. But I think when you talk about repealing the labor exemption, you've really got to sit back and think about it hard. The early Sherman Act enforcement was the Government picking on Eugene Debs and people like that. There is a lot of historical sense that maybe that was not the best way to start enforcement of antitrust laws.

Now, we are all in New York, most of us are residents of New York. For a subway strike to not only violate the Taylor Law but to be a federal crime of price fixing, I think would be a really neat thing. On the other hand, I do think the labor exemption is worth looking at, but it is so historically ingrained in our society and the repercussions of just a flat out repeal of Section 6 of the Clayton Act or Norris-LaGuardia would have such major impacts throughout the economy that I think it would require an awful lot of very careful studying. I think the presumption ought to be that it has worked okay, except for subway strikes, for 50 some odd years. Maybe we ought to give it a chance and study it really hard before we get rid of it.

**COMMISSIONER KEMPF:** Two quick comments. One, the prospect of repealing Capper-Volstead on everything we eat or drink is less than one percent. And the prospect of repealing the Wagner or Norris-LaGuardia act is less than one thousandth of one percent. But what that raises is: Is it all lip service we are giving antitrust because the impact of repealing those is that everything we consume would drop dramatically in price and that everything we don't consume but use all day would drop dramatically in price. It would be phenomenally beneficial to consumers. The supposed focus of Roxane's group, although they never talk about specific laws, because there is some political controversy associated with that.

To me it becomes a question: Is it just all a lot of rhetoric? It's I am in favor of rigorous antitrust enforcement for everyone except me. That is what it sort of boils down to. And I'd also, by the way, illustrate something else I've counseled many business people over the years. Some of the literature says price-fixing is most effective in smoke filled rooms with only a handful of people there. In reality price-fixing is most effective in a gigantic stadium with thousands of people there. Then you have political muscle and persuade somebody to grant you immunity and exemption. Then you can willy nilly price fix, harm everybody in America and do it without a problem. But enough of that.

**COMMISSIONER DELRAHIM:** I think that was leading to a point I was going to ask everyone on this panel. Should the function of the Commission be to give its objective advice on antitrust and competition policy to Congress, what the policy should be, and let Congress decide? They are going to do it anyway. What are the political realities here; should there be this document that the Congress created through this Commission that says this would be the right thing to do for the economy, repealing Capper-Volstead? We all know that some senator from Iowa is not going to allow that to happen. But should that be their concern, or have they given us, have they delegated to us the political judgment to return back to them as well? Because that colors a lot of the issues. When we begin thinking about whether we should repeal *Illinois Brick*, but in exchange for the plaintiff lawyers we should give them something else, is that more of a judgment that should be done within the members of Congress and that is what they get paid and elected to do? Is our job to do that and try to broker a deal for the plaintiff and defense bar? I don't know. That leads into what should this report look like. Should we be recommending legislation? Are we going to be some kind of an authoritative body that maybe somebody will look to and say, look, Judge so and so, the Commission said this shouldn't be allowed, they said this should be a violation.

What's your view on that, John?

**COMMISSIONER JACOBSON:** That is a very, very important question, and I don't have a single answer for

it because I think it really depends on the issue. I think we have to be careful not to say things, even if we believe them, that are simply going to be disregarded. We have to be very careful to say things that may jeopardize the credibility of the whole report.

On that issue I think recommending repeal of the labor exemption might veer into that category. Capper-Volstead I am less sure on. I think the academic and economic case against that exemption is awfully powerful. I personally would not feel embarrassed about talking about it. I don't think we should pull any punches.

In an area where there are viable alternative methods of reform and one is clearly more politically saleable than the other, I don't see why we shouldn't, in the interest of ideological purity, go with the one that politically has no chance of getting off the ground. I think there needs to be some practicality, but we also have to be intellectually honest. I think there is going to be a challenge in writing the report at the end of the day.

**COMMISSIONER KEMPF:** Let me take a quick stab on something we haven't touched on, that is Robinson-Patman Act. I don't know where we'll come out on that. The Commissioners unanimously are of the view this does more harm than good and ought to be repealed. However, if in the discussions in Congress there is disagreement on that issue, we would certainly recommend the following more fine-tuning changes.

I think one of your slides, John, goes through a series of higher standards for this, that, the other thing. We might combine the two in deference to the fact that it has been around for a long time, and it is not a sacred cow in all quarters but certainly in some, and it would generate a powerful lobbying campaign. You might say this is the ideal outcome, but have a fall-back position.

**COMMISSIONER JACOBSON:** I agree with that; in particular on that statute I agree with that.

**MS. BUSEY:** Another thing that I would suggest that you consider is that on some of these things you recommend further study. Because on some of these exemptions—and I don't mean to dwell on those, you didn't really hold a hearing on a particular exemption. I don't know that you can just on the basis of good principle recommend repeal of an exemption without even holding a hearing to discuss the particular exemption and what the consequences would be. So there might be some areas where you've got a lot on your plate, you haven't been able to hold hearings and you might recommend further study. And that may or may not be done, but at least it would put a pin in it so as to say there is a concern here, we think it should be addressed, but we are not ready to recommend something at this particular point in time.

**COMMISSIONER JACOBSON:** I think that is right.

But on exemptions, let me point out that we did specifically ask for public comment on a limited set of specific exemptions, including Capper-Volstead, not including Labor. Pointedly, not including Labor largely for the reasons I gave earlier. But including Capper-Volstead, McCarran-Ferguson.

I see Steve Hogan here, who will wince when I say the Export Trading Act, the Webb Pomerane Act, and the Shipping Act. On those I would personally not feel comfortable opining expressly. I think you're right to say these should not be repealed willy nilly without receiving some evidence.

**COMMISSIONER VALENTINE:** Let me take it back to make it a regional question, which is what is this report going to look like and how should it sound, what's its tone like? I don't think it would be just legislative recommendations. I would like to see recommendation to the agencies as well. Possibly recommendations for kinds of amicus filings that they make, and so I would not limit it to legislation.

Second, I do think that if you try to get too intellectually pure and absolute, one does lose credibility, and the whole report is devalued. I don't think you're going to get consensus, and I don't think a lot of these recommendations are going to be worth much without a substantial degree of consensus. So I would be more for let's say formulations like Don's on the ARP Act.

One thing I am worried about with the immunities and exemptions is I do think there was a strong contingent—there was actually a report presented to us by some academic consultants that think that a politically saleable way to deal with these immunities and exemptions is have them all sunset in three years and then put the burden on Congress to come back and reenact them. I have to say that is sort of a nice easy wiggly way out, but that one doesn't feel principled to me. I am not going to stand up and say repeal Norris-LaGuardia. I will find a principled way to fight, maybe the fact that people are different than products and services. But in any case, I do think that simply saying sunset and hand it over to Congress is a little bit of a wiggle out.

**COMMISSIONER KEMPF:** Let me add a footnote. This is the latest iteration of the study on antitrust law, but there are many such ones, not precisely like this, but ABA, a council of 100, a council of 50, generally they have not been successful. Some with marginal impact. But one of the things that has been useful have been some of the separate statements that have been published over time. Many of the final reports had attached to them either dissenting or separate statements by people like Bob Bork and George Stigler and others that were pretty thoughtful for their time and ended up being influential one way or

another. So there are lots of ways to impact. It may not be that Congress says oh, fine, we'll enact this. They may have rejected it, as they have in the past all of it. But over time some of it might be helpful both in the report and in separate statements.

**COMMISSIONER JACOBSON:** Makan, let me throw something else out that I think goes to the part of the question you asked. When the Commission was first established one of the debates we had is what sort of Commission should we be? At one end—I would associate John Shenefield with this position most directly, there was a vision that we would do something like the 1955 Attorney General's Report, which was fundamentally a restatement of what antitrust law was perceived to be at that time and covered the whole gamut. It was actually the ancestor of the ABA's Antitrust Law Developments. It was the beginnings of the first real Hornbook on Antitrust Law, and so it was that report from which Judge Bork dissented. He dissented from all of antitrust jurisprudence in 1955. By the way, today's laws look much closer to his view than the original book, so maybe he had something.

The other view, of which I guess I was probably the chief proponent, although I think I had some sympathy for Debra anyway, was a much more narrow version of our mission, and basically to say that the common law process of antitrust adjudication works in areas like the substance of Section 7 of the Clayton Act, the substance of Sections 1 and 2 of the Sherman Act. This has been a process for over 100 years of judicial decision making. That which is deemed to be certainly true one day is deemed twenty years later to be certainly wrong. We certainly saw that with *Schwinn* and *Sylvania*, just within a ten-year period. A Commission such as ours is supposed to be longer term. We should not opine on issues that are going to be obsolete within a short period of time. So my view is just let's look at narrow issues on which we could propose legislation or similar fixes that would actually correct narrow, perceived problems and do some good that way. Of course, we wound up with 25 issues covering the gamut of everything, so you can see how persuasive I was on that point.

**COMMISSIONER KEMPF:** I think there will be some areas where we have unanimity not just consensus. Debra referred to one of them, the merger clearance process. That testimony was pretty uniform; that it is in need of repair and it is in need of harmonization across the globe for people who now file 50, 60 different forms. And I don't know where we will come out precisely, but I think among those who have very much a strong view we might be able to make some useful suggestions there.

It is also my consensus that the Commission will likely reject the extensive special pleading requests we see. The antitrust law doesn't need to be reformed to protect my industry or me personally.

**COMMISSIONER DELRAHIM:** As you can see, we could probably sit here and go issue by issue the 25 or so major issues that the Commission has decided, but let me now turn it over to the audience and see if you have any questions?

**AUDIENCE MEMBER:** You explained earlier the Commission's final report will be due to Congress and the President in April 2007. It's my understanding that you plan on issuing a draft report this summer. Could you confirm that? And if that draft report is issued, will the Commission then take comments on your draft report?

**COMMISSIONER DELRAHIM:** The Commission has not decided on exactly the process. We are in that time where we are debating exactly what the procedure of issuing the writing and the form it will take amongst Commissioners, and some of this will be public. We are getting guidance from the GSA and our general counsel within the Commission. There has been a lot more legal wrangle just about the process about doing this, making sure that we comply every step of the way. So no decision has been made exactly as to that. I think many folks would like to see a draft or preliminary report come out, but then there are also counter arguments for that. Because some industries or some folks who may not be supportive of that before the report goes out will engage political supporters of theirs to attack the report before it comes out. But we have not determined that yet.

**COMMISSIONER KEMPF:** Let me add a footnote to that. Let me add that Makan's comments should not be read as that is the way we are inclined or we haven't taken any official action yet or not. There is robust discussion going on among the Commissioners informally as to how that should proceed. There are some who say obviously that way. There are others who say all we will do is get bombarded, and that will be the worst thing. I think it is very unsettled.

**COMMISSIONER JACOBSON:** I do think we need to start the drafting process soon. But it's hard to start the drafting process without having a clue about what you're going to say, and at this point we don't have a clue about what we are going to say. We have our own impressions, and you've heard from three of us about what our impressions are on a lot of the issues. I agree with Don. I think there is going to be a surprising amount of consensus on major issues. But there are some that we know are controversial, and we really haven't taken a straw vote. We don't know where the Commission is going to come out. I think we need to have that sort of debate and analysis first before we start putting pen to paper. I hope we have something in the summer.

**COMMISSIONER DELRAHIM:** Any other questions?

**AUDIENCE MEMBER:** Is the intention to publish a comment on all of the 25 issues that were identified for the Commission to pay attention to or to really focus whatever the publication is on those items about which consensus could be found, unanimity if that is the case?

**COMMISSIONER JACOBSON:** Good question. That is another unanswerable question at this point. Some of the issues may become moot. One of them almost certainly will. We put the *Independent Ink* issue as a specific one, because the question of whether you could infer market power from possession of a patent has been around since *International Salt*, you know, many, many years ago. The Supreme Court has never revisited it in modern times, so we put that issue on our list. The next week the federal circuit decides *Independent Ink* and a couple months later cert is granted. So I think you can carve that one off the list. But everything else, you know, I don't know.

**COMMISSIONER VALENTINE:** Maybe FTAIA will be pretty narrow too, since *Empagram* came out after, or it was at least simultaneous with our proposed issues. And to the extent that courts reach some kind of consensus there, there has been certainly a lot of concern with throwing the drafting of that statute back to Congress, since Congress did such a horrific job the first time around. But other than that, I don't think we know, although I bet a fair number of the issues, a preponderance of the issues will be addressed.

**AUDIENCE MEMBER:** Roxane's presence up there with your four eminences, if that is what your title should be, raises a question how much weight is given to the ABA, especially with the other comments.

**COMMISSIONER JACOBSON:** I think Roxane should answer that question.

**MS. BUSEY:** How would I know that? There have been many comments submitted. I am assuming that they would all be considered, but I can't really answer that.

**COMMISSIONER DELRAHIM:** I think as I said—

**COMMISSIONER KEMPF:** I can only answer individually. No special weight. The views of ABA along with everyone else will be persuasive or not, independently of who authored them in my judgment.

**COMMISSIONER VALENTINE:** And you know, there have been different degrees. The AAI has given also rather long thoughtful statements, as have the state attorneys general on many issues. It is all going to turn on how persuasive any individual comment is.

**MS. GOTTS:** A couple of housekeeping things. We are going to wrap up.

First thank you, Makan, for putting together such a wonderful panel.

Next year we'll do a repeat and hear some of the results after you've deliberated a little bit.

This concludes the CLE portion of our program. I want to thank everyone. This has been absolutely wonderful. Thank you.

# Antitrust Dinner

**Service Award Recipient:**
**ALAN J. WEINSCHEL, ESQ.**
Weil, Gotshal & Manges LLP
New York City

**Dinner Speaker**
**HONORABLE DEBORAH PLATT MAJORAS**
Chairman
Federal Trade Commission
Washington, D.C.

**MR. TUGANDER:** Good evening, everyone. I am Steven Tugander, the current, but very soon to be past Chair of the Antitrust Law Section. It is nice to see such a big turnout tonight.

In thinking about all the material that was covered during today's excellent program, I think it's fair to say that in 2006, the practice of antitrust law is as sophisticated, exciting and challenging as it has ever been. I think we can all agree that whether you're in private practice or government practice, right now is a great time to call yourself an antitrust lawyer.

And speaking of today's program, I just want to acknowledge the great job done by Ilene Gotts, our Program Chair, soon to be our Section Chair. She really did a wonderful job. She's been planning the meeting for many months. She did a fantastic job of putting the full day and evening program today. So Ilene, congratulations on behalf of the whole Section for kicking off 2006 with a great annual meeting.

I want to take a few moments to introduce the distinguished members of the dais.

To my right is Deborah Majoras, Chairman of the FTC, our dinner speaker tonight.

To the right of Deborah is Barbara Anthony, head of the FTC's Northeast Regional Office.

Ralph Giordano, my boss. And Ralph, thanks for letting me come tonight. Ralph, as most of you know, is the Chief of the Antitrust Division's New York Field Office.

Next is Jay Himes, who is the Chief of the Antitrust Bureau of the New York AG's Office.

Molly Boast, partner at Debevoise & Plimpton and Chair of our Annual Review Program this morning.

To Molly's right is Susan Raitt, an attorney with the FTC, also of Northeast Regional office and incoming secretary.

Moving in the other direction, Program Chair Ilene Gotts.

Alan Weinschel of Weil Gotshal and tonight's Service Award recipient.

Dr. Barbara Weinschel, Alan's wife.

And Irv Scher of Weil Gotshal, who will present the Service Award tonight to Alan.

So with that I am going to turn the program over to Ilene.

**MS. GOTTS:** Thank you, Steve.

I would like to first take a minute to thank our sponsors, and to point them out, because they have helped to make this a very good dinner.

First, we have CRA, Charles River Associates. If you could just wave so people can see your table.

Thank you so much.

Second, Competition Policy Associates. Third, We have NERA. Our other sponsors are LECG and Stratify, a discovery group.

We also have something very special tonight that goes beyond the call of duty. Alan is going to receive the Service Award, and in honor of that Weil Gotshal & Manges has decided to sponsor a dessert buffet immediately following this on the ninth floor.

I also want to just take one minute, I promise this is not going to be like the Emmys, but I do want to thank what I call the "Lori squares." There are two Loris who have made this event work and the whole year work; one of them is my colleague, Lori Sherman, sitting at the front table here. The other is Lori Nicoll, who has put up with us. She's in Albany with the New York State Bar Association. Lori, are you still here? There she is. So thank you both.

I was very pleased with today's panels. Part of what was so wonderful was thinking about what to do next year as each of these topics evolve.

After tonight I will be trying to fill some pretty big shoes. Steve has been absolutely incredible as the chair. I've never seen anyone so organized, so energetic, so

willing to answer e-mails any time of the day and night. It has been absolutely incredible. And when I moved to New York ten years ago and Meg Gifford said you need to get involved in this Section, I thought it would be a great way to meet some people. What I didn't realize was that not only was I going to meet members of the private bar, I was also going to meet lawyers who were in the various regional offices for the Justice Department and FTC and New York AG's office. That has been absolutely fantastic.

Steve might think he is done, but I decided there should be a new position, like the ABA, where the Antitrust Section's past chair has to stay and help and assist the Chair. So Steve we are going to start that tradition with you. Because we are not going to let you leave.

I want to give you just a little memento for everything you've done this year. Thank you.

**MR. TUGANDER:** Ilene, I want to thank you very much. I am very appreciative and honored to have been given the opportunity to be the Section Chair in 2006. And I am also very proud of the accomplishments and hard work and dedication of our Executive Committee.

So if you'll just bear with me for a few moments, I would like to acknowledge the many contributions made by our members over the past twelve months.

First Molly Boast, for serving on our nominations subcommittee.

Barry Brett for serving as the Section's House of Delegates rep and for chairing the Section's Service Award Subcommittee.

Bruce Colbath and Alan Weinschel for hosting three of our Executive Committee meetings this year.

B.J. Costello for co-chairing the Legislation Subcommittee and representing the Section at the Government Attorney reception in Albany, and serving as our House of Delegates Alternate.

Steve Edwards for serving on our Section Service Award Subcommittee.

Larry Fox for serving on our Section Service Award Subcommittee.

And for graciously hosting our September Executive Committee meeting.

Meg Gifford, for chairing our Nominations Subcommittee and representing the Section on the Unauthorized Practice of Law Task Force.

Ilene Gotts, not only for serving as Program Chair, but for over the course of the year serving as Vice Chair and graciously hosting two Executive Committee meetings.

Steve Houck, for serving on our Nominations Subcommittee.

Sticking with the AG's office, Bob Hubbard for putting together our Annual Meeting Symposium transcript and for serving on our nominations subcommittee and co-chairing our Legislation Subcommittee.

Patricia Jannaco representing the Section at the Diversity in the Bar reception earlier this week.

Stacey Mahoney for chairing our New Member Outreach Subcommittee, chairing the Summer Associates Program and serving on the Nominations Subcommittee.

Peter Millock for representing the Section at the Government Attorney Reception in Albany.

Saul Morgenstern, who is not here, but serving as the section's Secretary and representing the section on the Sarbanes Oxley Task Force.

Bruce Prager for serving on the Nominations Subcommittee.

Yvonne Quinn, from Sullivan & Cromwell, for graciously hosting our Summer Associates Program.

Susan Raitt, for chairing our Web Site Subcommittee.

Lori Sherman for chairing our Programs Subcommittee.

Eric Stock for representing the Section on the Lawyer Advertising Task Force.

April Tabor, for serving on the Web Site Subcommittee.

Elliot Wales, for coordinating the presentation of Bob Pitofsky.

James Yoon, for serving on the Web Site Subcommittee.

And I also want to thank Lori Nicoll, staff in Albany, for assisting our many miscellaneous tasks throughout the year.

Thank you.

**MS. GOTTS:** What we are going to do now is take a short break and eat our salads, and then I am going to ask for your attention before we serve dinner, so that we can give our attention to the Service Award. So enjoy and bon appetit.

**MR. TUGANDER:** Another great tradition that we have at our annual meeting dinner is to present the section Service Award. In searching for this year's award recipient we decided to honor an attorney who has made significant contributions not only to the Antitrust Law Section but to the field of antitrust, and in New York State in particular. And we found a very deserving recipient

this year in Alan Weinschel and here to present the award is Irv Scher, Alan's partner at Weil, Gotshal, who is a former Chair of this Section and himself a previous award recipient. Irv.

**MR. IRV SCHER:** Thank you. Obviously I am pleased and honored to have been asked to present this award to Alan Weinschel.

For those of you who don't know, the Section's Annual Service Award is intended to acknowledge the significant contribution to the antitrust laws of lawyers, who throughout their careers, have distinguished themselves as leading antitrust practitioners and as scholars, while serving the broader antitrust community, particularly through service to this Section. There have been only a few recipients to date, and Alan is without a doubt exceedingly qualified to join that select list.

Alan is well-known to most of you here. As I look around the room I see family, friends, colleagues, and former adversaries. From a personal standpoint he has been my close friend and colleague at Weil, Gotshal for more than thirty years. During that entire period those in our firm who have been privileged to work with Alan have recognized his outstanding qualities as a leader, advocate and counselor in antitrust matters. He has mentored a number of our antitrust attorneys on to partnership, and his antitrust knowledge, judgment and litigation talents are unsurpassed. In particular, Alan can master complex concepts that arise in massive antitrust suits, and in counseling as well. He is a leader among his colleagues, truly a go-to guy.

Alan commenced his legal career at the New York University School of Law where he received his J.D. with honors in 1969. While he was there he had the good fortune of being selected as student assistant by Professor Robert Pitofsky, the first of Alan's two antitrust mentors. Despite this extraordinary opportunity, Alan's antitrust views today certainly do not necessarily match those of former FTC Chair Pitofsky.

In the fall of 1969, Alan began his professional career at Breed, Abbott & Morgan here in New York. He left in 1974 for Weil Gotshal & Manges, where he continued his career under the tutelage of his second mentor, Ira Milstein, a dean of the antitrust bar and former Chair of this Section.

Alan has been a partner in the Antitrust Practice Group at Weil, Gotshal & Manges for more than 25 years. His practice has encompassed virtually all aspects of antitrust counseling and litigation, most particularly with respect to the interface between antitrust, technology and proprietary rights. He has worked on many antitrust cases. I'll only mention a few: Starting with Ira in *American Electric Power v. General Electric*, which was a leading antitrust conscious parallelism plus case; the uranium industry antitrust case, *Buffalo Broadcasting v. ASCAP*, *Brand Name Prescription Drugs, United States v. Calmar*, which was one of the first merger cases in which ease of entry was successfully raised as a defense; *United States v. Columbia Pictures*, one of the few civil antitrust cases that Bill Baxter prosecuted, involving the proposed Premier Movie Channel, the Movielink joint venture investigation, another matter that was closed by the Department of Justice without action, as was the investigation of the AOL-CompuServe merger. Alan has also worked on many other matters that never saw the light of day, because investigations were closed or cases not filed.

As a scholar, Alan has written extensively on antitrust matters of importance. Of particular note, he served for many years on the Editorial Board of *Antitrust Law Developments*, the two-volume ABA deskbook that the antitrust bar and courts use as a principal source of antitrust information. In 2002, this work was recognized when he received the ABA Antitrust Section's 50th Anniversary Publication Award.

Alan's other publications include: *The Antitrust Intellectual Property Handbook*, which he wrote for Glasser Legal Works and chapters in two West publications, *Antitrust Advisor* and *Drafting License Agreements*.

As many of you know, Alan has lectured extensively before this Section and in other settings, including PLI and Law Journal programs. In addition, he has eloquently presented his well-reasoned and thoughtful views during appearances as an antitrust commentator on Court TV and Bloomberg TV.

I saved the best for last—Alan's dedication, hard work and commitment to the activities of this Section. Alan has been a member of this Executive Committee, believe it or not, for 30 years. The only person I can think of who may have served that long might be Bill Lifland, the first person who was presented with this award. Alan has planned and participated in numerous programs at the Annual Meeting, including, of course, many addressing intellectual property antitrust issues. And he was chair of the Section from 1994 to 1996.

So Alan, on behalf of the entire Antitrust Law Section, I am proud to present you with this Section's Annual Service Award.

**MR. WEINSCHEL:** Thank you, Irv, for those very nice remarks.

In addition to wanting to kill all the lawyers, Shakespeare had some nice things to say as well: There is a line in *The Taming of the Shrew* that goes: "Do as adversaries do in law. Strive mightily, but eat and drink as friends."

The antitrust bar is—and the New York State Bar Association Antitrust Section in particular is—a great

example of doing just that, and it is especially gratifying to receive this award from this Section. My membership goes back more than 30 years, and my colleagues in this Section are very important to me. I am happy that we are eating and drinking as friends, and thank everyone in the Section for the award and for being here tonight.

I also want to thank some other people. I want to thank my partners and associates who came here tonight, with special thanks to Irv of course, who has been a good friend for so many years. But also to Ira Milstein, who deserves special mention. In 1974 Ira hired me away from another firm, took a chance on me (and fired me several times, each time for good cause). But Ira turned me from a law student into a lawyer and taught me, along with many others, not only how to litigate but also how to solve a client's problem, which can be entirely different than litigating.

I want to thank the associates who have worked with me over the years, some of whom are now my partners and who have prevented countless errors of fact and law. I want to thank my secretary, Leslie Halpern, who has been my assistant for 31 years and who has been my "Radar O'Reilly" in every respect.

I want to thank my wife, Barbara, who put me through law school, is my best friend and whose training as a psychiatrist has come in very handy.

My children are here too, and they too get my thanks for putting up with the 24/7 nature of our profession, and for coming to understand that I was not a secret agent, despite mysterious messages on the answering machine from Peter in London about Project Zebra.

Occasions like this tend to make us look backwards, and I have succumbed to the temptation. I feel very lucky to have found antitrust in law school, taking a course and then assisting Bob Pitofsky when I was at NYU. That was in 1968. Consider the sea changes that have occurred since then. I will mention only a few: From populism[1] to the Chicago[2] School and Bill Baxter's *laissez faire*[3] to post- Chicago pragmatism.[4] From *White Motor*[5] to *Schwinn*[6] to *Sylvania*.[7] From "conscious parallelism plus"[8] to *Monsanto*,[9] *Matsushita*,[10] and *Sharp*[11] From *Colgate*[12] to *Aspen Skiing*[13] to *Trinko*[14] From *Brown Shoe* and *Von's Groceries*[15] to Merger Guidelines[16] to new Merger Guidelines[17] to Revised Merger Guidelines[18] to reading between the lines of the Guidelines. From *per se* rules[19] and the rule of reason[20] to quick looks[21] and effects analyses.[22] From relatively small fines in criminal cases to fines in the hundreds of millions of dollars.[23] From the "nine no-no's" on patent licensing[24] to still more Guidelines[25] and to the Federal Circuit's yesyesses.[26] From dormant state enforcement to aggressive state enforcement.[27] We have had International Guidelines,[28] revised International Guidelines and *Empagran*.[29] The EC has developed its own and different approach to competition law,[30] and the Third Circuit seems to have joined the EC.[31] There was no Tunney Law[32] in 1968 and no Hart-Scott-Rodino Law.[33] (I remember making one of the very first filings ever under HSR.)

We antitrust lawyers took all these sea changes and have had to apply them to old industries, new industries, smokestack companies, dot-coms, yesterday's AT&Ts , IBMs, and General Motors, today's Microsofts, today's Intels, and tomorrow's who knows what. Antitrust makes us look at every conceivable kind of business and deal with their everyday dynamics and their life-cycles.

For me, antitrust has provided an opportunity to learn about industries as different as steam turbine generators, uranium mining, motion picture distribution, motion picture exhibition, Internet online services, airlines, book publishing, soft drinks, cosmetics, industrial chemicals, microprocessor fabrication, consumer electronics, health insurance, plastic sprayers, computer leasing, sweeteners, music licensing, DNA analysis, pharmaceuticals, software, chocolate, and too many others to mention. I feel very thankful to have had these kinds of opportunities.

I also feel lucky because practicing antitrust forces us to think about the "why" as well as the "how" and the "what." We get to play roles in the public policy debate about things like consumer welfare, free-riding, long run effects, the persistence—or not—of market power, whether markets really self-correct, about "rational" business decisions (assuming everybody always behaves rationally), about efficiencies and how to define them and what they mean, about presumptions, about deterrence and over-deterrence, and type 1 and type 2 errors. We get to do all this while we litigate, while we try to get deals done, and even while we counsel. All of this makes me very grateful I fell into Bob Pitofsky's class in 1968, and very grateful for this award. It has been a blast and it is still a blast.

Thank you all.

**MS. GOTTS**: We now are going to move into the part of the program where we will have our dinner speaker. We have been very fortunate throughout the years. I look out at this room, and we have an outstanding turnout, and it's not because of anything I did, other than to be fortunate enough to pick up the phone and to have Debbie say she would come and speak. So it's because of you I know that our attendees are here.

I want to acknowledge we have in the audience someone else who is one of our own, someone who is very special and who similarly, when she agreed to speak received a great turnout. We have Commissioner Harbour present, who is a former Chair of the Section sitting right here.

Deborah Majoras was sworn in on August 16th, 2004, after a little bit of a delay with Congress—not of

her making—as chair of the FTC. Debbie is special. She is someone who has served at the highest ranks at both agencies. Having been appointed the Deputy Assistant Attorney General of the Antitrust Division, and at one point I think she was the only Deputy Assistant Attorney General covering everything, and now being Chair of the FTC.

Debbie graduated from Westminster College and received her J.D. from University of Virginia. Now, that is what's on paper, but I want to tell you something about Debbie that I have experienced.

I met you first when you edited one of my papers for the ABA Antitrust Section. Usually when someone edits your paper you think oh, God, whatever they are going to do to my paper is going to make it worse, not better. Well, all I can tell you is we have a very special lady here with us today. Because everything she does she does with vigor, enthusiasm and insight. My paper was better because of what Debbie did. And so as an alum of the FTC, I feel very proud to know that you're the head of that agency.

With that, I am going to turn it over to you.

**CHAIRMAN MAJORAS:** Thank you so much, Ilene, for that really warm introduction. And thank you for having me here tonight. I have never made it a secret that I enjoy very much getting outside the beltway, and it's fun to see so many of my good friends in New York.

I first want to congratulate Alan and Barbara. It is such an honor, Alan. I had the pleasure of working with Alan some years ago in the *Brand Name Prescription Drugs* litigation, which went on and on and on, so there was plenty I could learn from that. But I couldn't help but think as I was sitting here that one of the things that I have always appreciated so much about our bar is that it's very special in the sense that no matter which side of an issue you're on at various times—and it is easier for me to say because I've been on a few sides—ultimately we appreciate very much our discipline and its integrity. And that is why we come together and we have special moments like this where we honor such a distinguished member of our bar like Alan Weinschel. I think we need to continue this and we need to bring all of the new members of our bar into the special relationship that we have with one another, which is something that I've grown up on and truly appreciate.

I am also glad to be on the dais with this great number, I can say I am so pleased I know everybody here. I have admired Irv for years. Ilene and Molly are very, very close friends. I've worked with Jay. I've worked with all the people from the FTC. I've worked with all the people from the DOJ. So it's a great group to be here with, and I am particularly pleased to have my colleague Commissioner Harbour here tonight.

Well, the start of the new year is typically a time of beginnings and resolution, and so of course it is at the FTC. The year's end brought the departure of two very important folks at the Commission in late December. Susan Creighton, Director of the Bureau of Competition, left after years of distinguished service, and Commissioner Tom Leary, a six-year tour of duty. Both of these individuals left a very lasting and important imprint and will be missed.

But last year's losses made possible some gains this year. I have appointed Jeff Schmidt to serve as the FTC's new Director of the Bureau of Competition. Jeff, I hope you know, was a former Deputy and a partner at the Pillsbury firm. He has boundless talent and energy, and we are enjoying working with him already. And of course our entire FTC community has welcomed Bill Kovacic and Tom Rosch in their positions as new FTC Commissioners, confirmed by the Senate in December and officially sworn in the first week of January. We are very pleased to have a full Commission again and obviously to have such distinguished colleagues.

Well, you've spent the day reviewing antitrust developments, discussing package licensing and economic bundling arrangements, debating the merits of antitrust class actions and hearing about the Antitrust Modernization Commission. So I thought I'd just talk about all those things together all at the same time. No, not for a dinner speech. I also think if I got up here and recited everything we are doing at the FTC, even though it makes me very excited, it would quite possibly conspire with your food and drink tonight and make you a little sleepy. So I thought instead what I would do is bring a little bit of Washington to New York. Now don't be horrified at the prospect. I was invited here after all. I want to discuss a topic that I find sometimes is a mystery to those outside of Washington, and surely was a mystery to me some years ago and sometimes remains so. And that is the role of the political process in our work.

Now, ordinarily discussing antitrust and politics in the same sentence sends shudders down the spines of antitrust practitioners, including my own. Because the job of an antitrust enforcer of course is to apply the competition laws fairly and consistently without regard to political interests, meaning partisan interests as we normally think of the term "political." A political application is vital to maintaining the effectiveness of our competition laws, especially today as we gain public support for a culture of competition, not only inside but outside our own borders. But this of course does not mean that competition enforcers are operating in a vacuum, isolated and immune from the political process. The actions produced by legislators in the political process can have a significant impact on competition and on our work. And likewise, the policies and actions of the antitrust enforcers can have an impact on our elected policy makers. And this interaction takes place at all

levels, from nomination and confirmation of our agency leaders, to Congressional appropriations and directives, to issue identification and consideration of legislative proposals, and through to implementing our enacted laws.

Let's start first with nominations and confirmations. And oh, you'll probably expect me to dish all kinds of dirt, but perhaps afterwards if you want to go for a drink we could do that. For now, I'll remind you that all five Commissioners at the FTC are nominated by the President and must be confirmed by the Senate, and then the President designates the Chairman from one of the five. No more than three Commissioners can be of the same political party. And by exerting control during the confirmation process, Senators can attempt to gain leverage or get concessions by threat of holding up nominations until certain conditions are met. Under Senate rules, a single senator can hold up a nomination for a considerable period of time without saying why, and indeed can even do it anonymously.

While we tend not to have it as rough as judicial candidates, the process is long and grueling. As you may recall, my own confirmation was held up by Senator Ron White. He wanted me to give him a detailed plan for how I intended to bring down the retail price of gasoline. As I hobbled up the Hill for my courtesy meetings, I was literally on crutches because I had broken my foot. I walked into Senator McCain's office, and he promptly exclaimed: "Did Senator Wyden do that to you? I thought we weren't allowed to break nominees' legs anymore."

Ultimately, the President gave me a recess appointment, and then three months later—it felt like years—three months later I was in fact confirmed by the full Senate.

Then we get to Congressional appropriations and directives. And Congress can have a great deal of influence. Using funding as both a carrot and stick, Congressional oversight committees and subcommittees influence our actions. For example, displeased with an agency's direction, Congress can sanction the FTC through specific prohibitions on activities and other means. Congress demonstrated this power in 1980 when, to show its displeasure with proposed rulemaking on children's advertising, now affectionately known as KidVid, it did not renew the FTC's operational funding, forcing the FTC to close down operations for a short time. Don't try it. I know you might like it, but don't try to shut us down.

You may also recall back in 2002 that the FTC, together with the Antitrust Division, tried to amend the clearance process. Congress, at the behest of Senator Ernest Hollings, passed a measure that prohibited the agencies from adhering to the new clearance agreements. And in addition, not infrequently through legislative provisos or allocation or earmarking of funds, Congress directs the FTC to conduct specific studies or investigations. Motivated recently by concerns about the volatile nature of energy prices, Congress directed us to conduct two related investigations into gasoline pricing. Passage requires the Commission to conduct an investigation to determine if gasoline is being artificially manipulated by reducing refinery capacity or by any other form of market manipulation or price gouging. So we opened an investigation pursuant to the directive in August and back in November issued a significant number of CIDs to companies.

Then on November 22nd, just two weeks after the issuance of an initial wave of CIDs, the President signed the Fiscal 2006 Appropriations Bill, which included the Commission, and Section 632 of that legislation mandates that not less than one million dollars of funds appropriated to the Commission must be used to investigate post-Hurricane Katrina gasoline prices and to report industry profits, tax incentives and the overall effects of increased gasoline prices on the economy. Now this is an example of an earmark which you may be reading about more generally, if you've been following the calls for lobbying for earmarks, to become quite the subject of discussion, at least inside the Beltway.

Legislation also requires us to provide an initial report to Congress within 30 days, which we did, updates every 30 days thereafter, and a final report no later than 180 days after enactment. So we sent out an additional number of CIDs but were told that we had to target each firm that had more than $500 million in wholesale gasoline distillate sales in 2004, which were subject to formal complaints in September of '05. That amounted to 84 firms that received sanctions.

So as you can imagine these two congressionally mandated investigations are requiring a significant investment of Commission time and resources. We expect to complete this report probably sometime around Memorial Day.

Now, in addition to controlling our purse strings, individual members of Congress have other ways of letting us know their priorities and concerns. Since January 1st of 2005 the Commission has received and answered more than 3,000 letters from members of Congress. Many of these are directed to me as Chairman and include a request for some type of agency action to be taken.

And in the roughly five months since Hurricane Katrina made landfall in the United States, we have received letters from nearly 200 members of Congress expressing concern about gas prices and urging us to take specified action. So in addition to law enforcement, you can see we have our hands full with some other things.

Now, moving onto another phase of the political process, because our existing enabling statutes are

really quite broad, we don't typically recommend a lot of changes to the antitrust laws. But part of our job is to identify market and consumer problems as well as any limitations that we see on our enforcement powers that are inhibiting us or making effective competition or consumer protection enforcement more difficult that could be addressed through legislation. Some of the FTC's major accomplishments over the years derive from this function.

Continuing a long tradition, for example, of involvement with innovation issues, the FTC in recent years is devoting considerable time to patent reform. You may recall back in 2003 the FTC issued a report on patent reform. Last year we co-sponsored a number of Town Hall workshops around the country in which we could talk to various interested parties about their views on patent reform. In June of 2005 Chairman Lamar Smith of the House Judiciary Subcommittee on the Courts, the Internet and Intellectual Property proposed legislation intended to overhaul the patent system. He describes this bill as a holistic approach to patent reform designed to improve the quality of patents that the government issues and reduce unnecessary litigation. Two of the bill's major provisions reflect recommendations originally made by the FTC, and also made by the National Academy of Sciences and leading patent organizations, relating to post-grant review of patents and modification of the criteria for a finding of willful infringement.

Of course, frequently particular industries, private individuals and legislators themselves will identify issues they believe should be addressed through legislation. And when legislative proposals are likely to impact competition, members of Congress and staff often seek our views as competition experts and often, quite frankly, because they believe that we will be the agency that will be designated to enforce whatever it is that Congress is about to pass. It can be any one of a number of things.

You may not know this, but in addition to the FTC Act, the agency has responsibilities under more than 50 federal laws. In fact, recently—although this bill isn't going anywhere at the moment—it was thought that a federal law might be passed with respect to steroids and steroid regulation for sports, and that it would be the FTC that would implement that law. Now, we don't have a lot of expertise in this area, but it might actually have helped my ultimate career aspiration to be Commissioner of Baseball. That doesn't look like it is going to happen, at least for the moment. So we are frequently providing comments to legislators about the competitive impact of proposed laws and whether they are going to alter the competitive environment through restrictions on price, innovation or entry conditions. Some would argue that this is the most important work we do.

Government imposed restraints are among the most durable and effective restraints on competition. In fact, in a 1989 ABA report it was observed: "Because ill-advised governmental restraints can impose staggering costs on consumers, the potential benefits from an advocacy program exceed the Commission's entire budget." And just this week Martin Wolf of the *Financial Times*, who was commenting on William Lewis' recent book that he said showed that "remorseless pervasive, fair and open competition is the key to a nation's prosperity" had this to say, and I quote: "Free and fair competition sounds simple to achieve. Nothing is further from the truth. Competition of such intellectuals who glory in the notion of state benevolence, bureaucrats who administer government programs, businesses that receive state favors and in short all those who gain directly or indirectly from distortions, competition benefits often despised outsiders against those who are well-connected and entrenched. It also requires the courts and government to work honestly." So we do a lot of this.

A recent example of our consideration of federal legislative proposals involves gasoline pricing. As you know, the price of gasoline spiked swiftly and substantially after Hurricanes Katrina and Rita made landfall. At one point over 95 percent of Gulf Coast crude oil production was shut in, and numerous refineries or pipelines were damaged or without electricity. As of the beginning of this month, 27 percent of the normal daily flow of Gulf Coast production remained shut in. While gas prices remained relatively low throughout most regions of the world, the price rises that followed the hurricanes caused great economic distress to Americans and so was of grave concern to officials. One principal concern was that these tragedies enabled the gasoline industry and other providers to engage in some form of price gouging of consumers. Members of Congress responded by introducing bills designed to curb these perceived pricing practices, and the bills ran a large gamut, and still do, of measures intended to put a ceiling on gas prices. Most of the bills would make it unlawful during times of natural disaster to sell oil and gas at unreasonable or unconscionable prices.

Some of the bills provide general guidance about the parameters of unreasonableness and unconscionability, while others request that the FTC engage in a rule making to give added precision to these terms. The bills include substantial penalties, including disgorgement and punitive damages, and in some cases, call for criminal prosecution.

On November 9, I presented Commission testimony regarding the industry before two committees at the same time. The Commerce Committee and Committee on Energy and Natural Resources. Suffice it to say, it was a rather lonely experience. Drawing from the Commission's wealth of experience in these markets, I presented the FTC's testimony that proposed price gouging bills likely would harm more than help. Prices of course are more than just a reflection of input costs. They also inform

producers to increase or decrease supply, and signal consumers to increase or decrease demand. In periods of shortage, higher prices can serve a market clearing function by limiting the duration of shortage. So it is not a trivial matter to try to discern the difference between a necessary market induced price increase and a seller using short-term market power to gouge consumers. Experience teaches that even the best intention of legislation has significant negative unintended consequences.

As the U.S. experienced during the energy crunch in the 70s, restrictions on the prices charged by private firms can result in shortages, rationing and suboptimal investment. And in this critical industry investment is vital to the provision of adequate supplies of gasoline or alternative sources of energy.

Finally, last fall's hurricanes produced significant buying and selling which potentially produced a market disequilibrium significantly above the long-run price. But those circumstances do not necessarily suggest a systematic market failure that requires restrictions on price. Again, short-term price increases can prevent shortages and efficiently allocate a scarce resource. And because the markets may be in a substantial state of flux, calibrating regulations so they do more good than harm presents us with substantial challenges.

Well, not surprisingly the senators who attended the hearing on both sides were not pleased with my views, and some claimed they could not believe that their proposals would not benefit consumers. But our job in the legislative arena is not to increase our popularity. It is not to take the easy road. And it is not to tell people what we think they want to hear. Our job is to provide sound advice based on our experience in markets, competition, our empirical work and solid economic theory.

The interesting thing is I receive a lot of consumer letters on consumer protection issues, but I don't receive that many on competition. I actually received a handful after this hearing, which I was afraid to open. Interestingly enough, every single one was from a consumer who had seen the tape of the hearing and thanked me for standing up for what was right. Which I found to be rather fascinating.

Of course, just as economic theory would predict, in the months after Hurricane Katrina made landfall, normal forces of supply and demand mitigated, not only did the sun rise and gas prices curbed and consumer demand thus relieved the upward price pressure, but higher gasoline prices—by the way I might add that was the first decrease in demand in the United States in 20 years. But the higher prices also signaled suppliers to bring in more product to the most severely affected areas of the country, which further led to the price increases.

For example, we received imports of large quantities of gasoline from Europe. We also had increased refinery utilization and a shift to output from other products to gasoline to increase the production of gasoline outside the hurricane area. And this was profitable for the refineries precisely because the price had increased.

The Commission is also increasingly providing comments to state legislators about the competitive impact of proposed laws and regulations. And you might have heard that in the past year the FTC, together with DOJ, has provided several state legislatures with advocacy comments urging the states not to adopt proposed minimum service regulations for the real estate industry. These laws effectively would eliminate limited service brokerage options for consumers. Most recently we sent a letter to the state of Michigan, at the request of a senator and an agency, urging them not to support such legislation, which would have required that all real estate brokers provide certain services, including negotiation, assistance at closing, and advice on price to consumers, regardless of whether consumers wanted these services or not. We argued that the bill would restrict consumer choice, restrict competition between the limited service brokers who provide services on an a la carte basis, and the traditional services many consumers want who charge for their services in the form of a commission. Oh, just to pick a figure out of the air, six percent. So we say if the bill is enacted, this could cause some home buyers and sellers to pay higher prices for real estate brokerage services. While we have not been successful in all areas, in all states we understand that this bill was influential and a committee's decision has resulted in the bill dying in committee.

Now, there is one last way that I want to talk about how legislation can have an impact on our work. Legislation and any resulting regulation can also have a more indirect impact on our antitrust analysis and enforcement work because it can alter the nature of competition in particular markets. Of course sound antitrust enforcement provides that we have to look at all factors which might have an influence on a market. We can't just ignore a particular regulatory scheme and hypothesize what the market would look like without such government intervention.

I submit that U.S. legislation intended to spur development of generic drugs illustrates the point. Through the Hatch-Waxman Act Congress has tried to accelerate the entry of low cost generic drugs by encouraging challenges to patent claims that impermissibly block such entry. And while some may not agree with where Congress struck the balance, promotion of more generic entry to patent challenge is at least an understandable objective, provided it protects legitimate patent claims and doesn't decrease to harmful levels to innovate.

Generic competition regarding patent challenges has produced substantial benefits for consumers. For

example, successful patent challenges to Zoloft and Paxil probably have saved consumers approximately $9 billion, because generic sellers price the product at a substantial discount. So to encourage generics, Hatch-Waxman allows for accelerated approval of a drug through abbreviated new drug applications. And probably in New York I don't need to explain to you the Hatch-Waxman scheme. But basically Congress created economic incentives for patent holders to commence patent suits upon receiving a certification that it can accelerate resolution of patent claims. So on receipt of notice from a filing, the patent holder receives an automatic 30-month stay of generic entry into the market if it sues the generic with infringement within 45 days.

According to one FTC study between 1992 and 2000, generics prevailed in 73 percent of all patent litigations initiated pursuant to Hatch-Waxman. So the Hatch-Waxman legislation altered the competitive landscape in a manner that does have an impact on antitrust analysis. By increasing the potential economic value of generic entry, it also increased the incentive for brand and generics to conspire to share rather than to compete for the expected profits generated by sales of both brand and generics. For example, a brand and generic now have an incentive to divide up the profits from the exclusivity period, which is a period obviously that didn't exist before passage of the statute. In nearly any case in which generic entry is contemplated, the profit that the generic anticipates will be less than the profit the brand drug company would make from the same sales. So it will almost always be more profitable for the branded manufacturer to buy off the generic, and indeed Congress expressly recognized this risk when it implicitly directed the enforcement agencies to look at such agreements in practice by amending Hatch-Waxman in 2003 to require brand pharmaceutical companies and generic applicants to file their patent settlement agreements with the FTC and Antitrust Division.

In the Schering-Plough matter the Commission sustained a challenge to two agreements in which Schering entered with generic drug manufacturers through which Schering paid the generics and the generics agreed to delay the sale of their products. Schering argued, ultimately successful in the Court of Appeals for the Eleventh Circuit, that the agreements were an appropriate way to settle the patent litigation, and that because the generics were constrained by Schering's patents from entering, the payments to the generics to delay the entry until a certain date could not violate the antitrust laws. And again, we lost on that. The Commission is seeking certiorari in the Supreme Court because we think the Court of Appeals ruling is contrary to antitrust law and Congressional intent in enacting Hatch-Waxman. Because it essentially imposes a rule that a patentee is presumptively entitled to buy protection from all generic competition from the full patent term, even if such payments effectively augment a patent's power.

I know the Commission has exercised its authority to represent itself before the Supreme Court only twice in the 30 years that it has had that authority, both times resulting in cases that delivered important victories. We are taking this unusual step now not only to seek correction of a ruling that we believe conflicts with antitrust and administrative law principles, but also because of the great urgency of the matter in light of the billions of dollars of consumer savings that Congress has said it would like to bring to consumers on prescription drugs.

Now this matter and the reason I raise it has been hotly debated. There are those who disagree with the Commission's position, that unless patent litigation proves otherwise, we must permit parties to settle patent litigation, which they may choose to do regardless of their position on the merits according to their own risk calculation at the time. But the problem is that the argument also ignores law and facts. There is no question that the resulting patent litigation and therefore the timing of generic entry is uncertain. But the antitrust laws prohibit the paying of a potential competitor as well as existing competitor to stay out of a market, even when entry is uncertain. And it cannot seriously be argued that generic entry at the end of a patent term is too uncertain or unlikely to be of competitive concern.

Given that, Congress spoke on the issue, and we know that generic entry has prevailed in almost 75 percent of the patent litigation initiated under Hatch-Waxman.

As to arguing that payoff settlements generally are favored, we reported publicly, as required by Congress, that legitimate settlements give a meaning to others that anticompetitive reverse payments have continued to occur seemingly without hindrance from the Commission. So that is just an example of how we are trying to take a legislative intervention into a market and deal with that in our antitrust analysis.

Well, I hope I've shed a little bit of light on how the political process impacts our antitrust work. I don't know what your timing is, but if you had any questions, I would be delighted to answer them. Thank you very much.

**MS. GOTTS:** Debbie, I want to especially thank you, and say how delighted I am that you said you like to go outside the Beltway. Because I would like to do something that Albany would probably really object to, but I would like to extend to you honorary membership in our Section, and we'd love to have you participate in some of our activities. I will send you e-mails and encourage you to come.

Well, I think we can officially adjourn this meeting. I hope to see as many of you as possible throughout this year at our events. And hopefully next year this time everyone will be able to join us to celebrate another wonderful year.

Remember, we have our dessert buffet, thanks to Gotshal, up on the ninth floor, where we can thank Alan for everything he has done in his many years of service. Thank you all very much.

## Endnotes

1. Dominant during the 1960s, the "Populist School" of antitrust enforcement policy emphasized protecting the ability of small businesses to compete, and was generally hostile to mergers and big corporations. *See* Robert A. Skitol, *The Shifting Sands of Antitrust Policy: Where It Has Been, Where It Is Now, Where It Will Be in Its Third Century*, 9 Cornell J. L. & Pub. Pol'y 239, 253 (1999); *see also* Robert Pitofsky, *Antitrust in the Next 100 Years*, 75 Cal. L. Rev. 817, 822 (1987) (commenting that the Populist School was led by "the notion that big is bad and that small is somehow beautiful"). At the peak of the populist era, in *United States v. Von's Grocery Co.*, 384 U.S. 270, 301 (1966), dissenting Justice Potter Stewart protested that the only consistency he could find in the Court's merger cases of the 1960s was that "the Government always wins."

2. The Chicago School rose to dominance in the late 1970s and its precepts were quickly adopted by the Supreme Court, lower courts and government agencies. Pursuant to the Chicago School's philosophy, the only goal of antitrust law is to ensure the maximization of economic values through efficient production. "Orthodox Chicago School antitrust policy is predicated on two assumptions about the goals of the federal antitrust laws: (1) the best policy tool currently available for maximizing economic efficiency in the real world is the neoclassical price theory model; and (2) the pursuit of economic efficiency should be the exclusive goal of antitrust enforcement policy." Herbert Hovenkamp, *Antitrust Policy After Chicago*, 84 Mich. L. Rev. 213, 215-16, 249-51 (1985).

3. William F. ("Bill") Baxter was appointed as Assistant Attorney in Charge of the Antitrust Division of the Department of Justice ("DOJ") by President Reagan. The Reagan administration sought to minimize government intervention in the economy, including antitrust intervention. One of Baxter's most important initiatives during his 1981-1983 term was the issuance of the 1982 Merger Guidelines, which were considered more lenient than the 1968 Guidelines they replaced. *See* Charles A. James, Assistant Attorney General, Antitrust Division, *Remarks Made at a Conference Celebrating the Twentieth Anniversary of the 1982 Merger Guidelines* (Jun. 10, 2002). Other notable actions taken by the Antitrust Division under Baxter were the agency's abandonment of its high profile antitrust litigation against IBM, *United States v. IBM Corp.*, Civil Action No. 69 Civ. 200 (S.D.N.Y. dismissal filed Jan. 8, 1982), and the breakup of the telecommunication giant, AT&T. *United States v. AT&T Co.*, 1982 U.S. Dist. LEXIS 15263, 1982-2 Trade Cas. (CCH) P64981 (D.D.C. Aug. 24, 1982).

4. The Post-Chicago Pragmatism School began to gain influence during the 1990s. Believing that a free market economy is the best economic model, it nevertheless rejects the neoclassical notion that the market will always correct itself, and acknowledges that, at times, the government must intervene to protect consumers. *See generally* M. Sean Royall, *Post-Chicago Economics: Editor's Note*, 63 Antitrust L.J. 445 (1995). One hallmark of the post-Chicago school is that the DOJ and the Federal Trade Commission ("FTC") have come to rely on data, as opposed to theory alone, in judging how mergers might affect consumers. For example, in the proposed Staples-Office Depot merger in 1997, the companies argued they could not increase prices above competitive levels because their combined businesses would have constituted only a small share of the national office-supply market. After crunching massive amounts of checkout-scanner data, the FTC successfully argued that Staples charged more in markets where it did not face other office-supply mega-stores, that consumers viewed such megastores as a separate niche, and that the postmerger entity would likely gain the ability to charge supra-competitive prices. *See FTC Rejects Proposed Settlement in Staples/Office Depot Merger, available* at www.ftc.gov/opa/1997/04/stapdep.htm.

5. *In White Motor Co. v. United States*, 372 U.S. 253 (1963), the Supreme Court considered whether a manufacturer could restrict the customers and territories that its dealers could serve. The Court held that it had too little experience in such cases to declare these nonprice vertical restraints *per se* unlawful, relegating such restraints to a rule-of-reason analysis.

6. Four years after *White Motor*, in *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), the Court revisited non-price vertical restraints. This time it held that, once a supplier transfers title to its goods to a distributor, any imposition of further restrictions (*e.g.*, a limited distribution territory) by the supplier is a *per se* violation of the Sherman Act, as it is "so obviously destructive of competition." *Id*. at 379.

7. In *Cont'l T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), the Court overruled the *per se* rule for non-price vertical restrictions it had adopted in *Schwinn*, as well as *Schwinn's* distinction between situations in which title has passed and when it has not. It explained that "departure from the rule-of-reason standard must be based upon demonstrable economic effect rather than—as in Schwinn—upon formalistic line drawing." *Id.* at 58-59. It noted that vertical territorial restrictions can be pro-consumer because, by reducing the risk of free riders, they encourage dealers to provide better service. The Court emphasized the difference between intrabrand and interbrand competition, stressing the importance of protecting the latter, and that it may be appropriate to restrain intrabrand competition in order to stimulate interbrand competition. *Id*.

8. Under the rubric of "conscious parallelism plus," plaintiffs could establish a conspiracy in violation of § 1 of the Sherman Act through strong circumstantial evidence: parallel conduct by defendants, and one or more "plus factors," suggesting that the alleged conspirators had entered into an express or implied accord (*e.g.*, defendants' actions were contrary to their independent economic interests). *See Interstate Circuit, Inc. v. United States*, 306 U.S. 208, 231-32 (1939).

9. In *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 768 (1984), the Court held that, in the absence of direct evidence of conspiracy, a plaintiff in a vertical price-fixing case must present evidence "that tends to exclude the possibility" that the defendants "were acting independently." Plaintiff must "present direct or circumstantial evidence that reasonably tends to prove that the manufacturer and others had a conscious commitment to a common scheme designed to achieve an unlawful objective." *Id*. (citation omitted.)

10. In *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), in the context of a horizontal price-fixing claim, the Court held that "To survive a motion for summary judgment or for a directed verdict, a plaintiff seeking damages for a violation of section 1 [of the Sherman Act] must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently" (citation omitted). It further held that a plaintiff seeking to prove a § 1 conspiracy through circumstantial evidence must show that conspiracy, rather than "other, equally plausible explanations," is the reason for defendants' conduct; and that the alleged conspiracy is economically plausible. *Id*. at 596-97.

11. In *Bus. Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 736 (1988), the Court held that a "vertical restraint is not illegal *per se* unless it includes some agreement on price or price levels." Thus, an alleged agreement between a supplier and a dealer to terminate a price-cutting dealer was not *per se* unlawful, "without further agreement on the price or price levels to be charged by the remaining dealer." *Id*. at 726-27. The Court's decision was

motivated by the desire to provide manufacturers with reasonable freedom in deciding how to distribute their products.

12. In *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919), the Court held that the Sherman Act did not restrict the right of a trader or a manufacturer to "engage in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal." Thus, under the *Colgate* doctrine, a manufacturer may declare that it will only deal with distributors that abide by its pricing policy, and then unilaterally terminate distributors that do not adhere to that policy.

13. In *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), the Court held that a ski resort monopolist violated section 2 of the Sherman Act by pulling out of a ticket-sharing arrangement it had long held with a smaller competitor. The Court noted that the arrangement was profitable, and that defendant had advanced no efficiency or any other legitimate business reason for the termination *Id*. at 604. Thus, a jury was entitled to find that the purpose and effect of the defendant's termination of the arrangement was "exclusionary." *Id*.

14. In *Verizon Commc'n, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004), the Court upheld Verizon's decision not to share its telecommunications network with AT&T. In doing so, the Court significantly limited *Aspen Skiing*, noting that "Aspen Skiing is at or near the outer boundary of § 2 liability." *Id.* at 409. It emphasized that § 2 does not impose a general duty on a monopolist to deal with competitors, and that exceptions to the freedom not to deal are few and narrow.

15. *Brown Shoe Co. v. United States,* 370 U.S. 294 (1962) and *United States v. Von's Grocery Co.*, 384 U.S. 270 (1966) demonstrate the Court's general concern with horizontal mergers in the 1960s. This concern stemmed from what the Court described as a "rising tide of economic concentration." *Brown Shoe*, 370 U.S. at 317-18. The Court affirmed Government efforts to block mergers that it believed would increase concentration and reduce competition, even where market shares were fairly low. In *Von's Grocery*, the Court blocked the merger of two grocery chains comprising a total of only 7.5% of the Los Angeles market, and in *Brown Shoe* it blocked a merger that would have increased a footwear company's market share from 5.6% to 7.2% of the national shoe market.

16. In 1968, under the leadership of Assistant Attorney General Donald Turner, the DOJ issued guidelines that were designed to inform companies about the government's enforcement intentions regarding horizontal mergers. The 1968 Guidelines defined a highly concentrated market as one in which the four largest firms maintain a 75% market share, and described the types of mergers that the DOJ would be likely to challenge in concentrated and nonconcentrated markets.

17. The 1968 Merger Guidelines were replaced by the 1982 Merger Guidelines. In general, the 1982 Guidelines were less stringent than the 1968 Guidelines, and were initially portrayed by some critics as "a blank check for corporate consolidation." *See* James, *supra* note 3.

18. In 1984, the DOJ issued revisions to the Merger Guidelines. This version was later largely superseded by the 1992 Horizontal Merger Guidelines, a combined effort of the DOJ and the FTC. The main distinction between the 1992 Guidelines and the earlier versions was a shift from structural presumptions based on market shares and concentration ratios to a greater emphasis on qualitative competitive effects analysis. William J. Kolasky and Andrew R. Dick, *The Merger Guidelines and the Integration of Efficiencies into Antitrust Review of Horizontal Mergers*, 71 Antitrust L.J. 207 (2003). The FTC and the DOJ further revised the Guidelines in 1997, providing clearer guidance on the types of efficiencies to be considered in analyzing the potential benefits of a merger. *Id*.

19. Courts have historically applied two main modes of analysis in determining whether alleged conduct constitutes an unlawful restraint: the "*per se* rule" and the "rule of reason." Over the years, the Supreme Court has changed its mind more than once regarding the type of conduct constituting a naked (*per se* illegal) restraint. William E. Cohen, *Per Se Illegality and Truncated Rule of Reason: The Search for a Foreshortened Antitrust Analysis*, FTC Policy Planning Staff Discussion Draft (Nov. 1997). The Court first applied a *per se* analysis to price-fixing in *United States v. Trenton Potteries Co.*, 273 U.S. 392 (1927), and in *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940), further elaborated: "Under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se*." *Id*. at 223.

20. The rule of reason preceded the *per se* rule. It was first adopted by the Court in *Standard Oil Co. v. United States*, 221 U.S. 1 (1911), in the context of a Sherman Act § 1 case. The Court has repeatedly held that it is the rule of reason, not the *per se* rule, that applies to the majority of conduct challenged under the Sherman Act. *See, e.g., Nw. Wholesale Stationers, Inc. v. Pac. Stationery & Printing Co.*, 472 U.S. 284, 289 (1985). In deciding whether challenged conduct constitutes an unlawful restraint on trade under the rule of reason, a court must balance the anticompetitive effects of that conduct against its procompetitive or efficiencies. *Board of Trade of Chicago v. United States*, 246 U.S. 231, 238 (1918).

21. In many instances, the Supreme Court has recognized that the line between the *per se* rule and rule of reason analyses is often fuzzy, *see Sylvania*, 433 U.S. at 50 n.16; and that the way courts have applied the two standards has been "less a dichotomy than a continuum." *Nat'l Collegiate Athletic Ass'n v. Board of Regents of the & Univ. of Oklahoma*, 468 U.S. 85, 104 n.26 (1984).

22. *Cf., Broadcast Music Inc. v. CBS, Inc*. 441 U.S. 1 (1979) (restraint necessary in order to provide product); *FTC v. Indiana Fed'n of Dentists* 476 U.S. 447 (1986) (restraint not connected to procompetitive purpose).

23. The 1974 Antitrust Procedures and Penalties Act (Pub. L. No. 93-528, 88 Stat. 1706) increased the status of a Sherman Act criminal offense from a misdemeanor to a felony. It also increased the maximum prison sentence for individuals from one to three years. Additionally, fines for individuals were raised from $50,000 to $100,000, and for companies from $50,000 to $1 million. In 2004, President Bush signed into law the Criminal Antitrust Penalty Enhancement and Reform Act (Pub. L. No. 108-237, 118 Stat. 665, 668), increasing the maximum penalty per violation for individuals to a jail term of ten years and a $1 million fine; and the maximum penalty for corporations to a $100 million fine.

24. In 1970, the DOJ released a list of nine types of intellectual property licensing practices that the DOJ believed to be *per se* unlawful. These became known as "the nine no-no's." Willard K. Tom and Joshua A. Newberg, *Antitrust and Intellectual Property: From Separate Spheres to Unified Field*, 66 Antitrust L.J. 167, 225 (1997). Today, at least eight of these practices are generally analyzed under the rule of reason and are likely to be regarded as lawful under many circumstances. *Id*.

25. In 1995, the DOJ and the FTC jointly published Antitrust Guidelines for the Licensing of Intellectual Property (4 Trade Reg. Rep. (CCH) (Apr. 6, 1995)). These Guidelines replaced the intellectual property provisions of the DOJ's 1988 Antitrust Enforcement Guidelines for International Operations (4 Trade Reg. Rep. (CCH) ¶13,109, at 20,589-20 (Nov. 10, 1988)). The 1995 Guidelines echoed "the policy of the preceding administrations that patent licensing is generally procompetitive, that the policy objectives underlying both the antitrust laws and the patent laws are complementary, and that most transactions involving patents should be examined under the rule of reason." Alan J. Weinschel, *Antitrust-Intellectual Property Handbook* 1:23 (2000).

26. Recent decisions of the Federal Circuit have demonstrated a growing tendency to protect the rights of patentees by limiting the availability of antitrust remedies. *See* Robert Pitofsky, *Challenges of the New Economy: Issues at the Intersection of Antitrust and Intellectual Property, Remarks Before the American Antitrust Institute Conference: An Agenda for Antitrust in the 21st Century*, National Press Club (Jun. 15, 2000). These decisions, in particular *In re Indep. Serv. Orgs.*

*Antitrust Litg. (Xerox)*, 203 F.3d 1322 (Fed. Cir. 2000), have drawn fierce criticism from antitrust scholars, including former FTC chairman Pitofsky, who commented that *Xerox* and other relevant cases "have upset [the] traditional balance [between antitrust and intellectual property] in a way that has disturbing implications for the future of antitrust in high-technology industries." *Id*.

27. *See generally* Ky P. Ewing, Jr., *Current Trends in State Antitrust Enforcement: Overview of State Antitrust Law*, 56 Antitrust L.J. 103 (1987) (discussing the increased role of states in antitrust enforcement, following the 1976 enactment of the Hart-Scott-Rodino Act and concurrent federal funding, which encouraged states to take a more active approach in protecting competition).

28. Antitrust Enforcement Guidelines for International Operations were issued by the DOJ and the FTC in April of 1995, and were "intended to provide antitrust guidance to businesses engaged in international operations on questions that relate specifically to the [agencies'] international enforcement policy." Dep't of Justice and FTC, *Antitrust Enforcement Guidelines for International Operations* (1995), 4 Trade Reg. Rep. (CCH) 13,107. The 1995 Guidelines replaced a 1988 version that was issued by the DOJ. While the 1988 Guidelines echoed the Reagan administration's philosophy of minimal government intervention, the 1995 Guidelines, which were issued while President Clinton was in power, expanded the scope of international conduct that the agencies might challenge. They also offer more comprehensive guidance on various aspects of international antitrust enforcement, including principles of reciprocity and comity.

29. In *Hoffmann-La Roche, Ltd. v. Empagran S.A*, 542 U.S. 255 (2004), foreign and domestic vitamin purchasers alleged that they were injured by a price-fixing conspiracy between a number of U.S. and non-U.S. companies. The Supreme Court held that the foreign plaintiffs' claims were banned by the Foreign Trade Antitrust Improvements Act (15 U.S.C. § 6a ) ("FTAIA"). Resolving a circuit split, the Court held that the FTAIA precludes foreign plaintiffs from bringing Sherman Act claims in the U.S., where the injuries to these plaintiffs are "independent of any adverse domestic effect." *Id*. at 164.

30. While U.S. antitrust policy concentrates on maximizing output and consumer surplus, the European Union's competition policy often focuses on promoting "business rivalry" (*i.e.,* protecting competitors). Daniel J. Gifford and Robert T. Kudrle, *Rhetoric and Reality in the Merger Standards of the United States, Canada, and the European Union*, 72 Antitrust L.J. 423, 424 (2005). For example, the antitrust enforcement arm of the European Commission has often treated merger-related efficiencies negatively when it has believed that they can harm competitors. *Id*. at 458.

31. In *LePage's, Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003), the Third Circuit held that the use of exclusive dealing and bundled rebates by a manufacturer, a monopolist that held 90% of the market for transparent tape, injured its competitor in violation of § 2 of the Sherman Act. The Third Circuit's focus on the injury to a competitor, as opposed to consumer harm, is similar to the approach in recent European Commission decisions. *See*, *e.g.*, CFI Judgment of 30 September 2003, Case T-203/01, *Michelin v. Commission*; CFI Judgment of 17 December 2003, Case T-219/99, *British Airways v. Commission*.

32. The Tunney Act (Antitrust Procedures and Penalties Act, 15 U.S.C. § 16) provides mandatory procedures that the DOJ must follow when it proposes to settle a civil antitrust suit by entering into a consent decree. Under the Act, the DOJ must provide the general public with an opportunity to comment on the proposed settlement and the court must find the settlement to be in the public interest.

33. Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 U.S.C. § 18a), and regulations promulgated thereunder. Among other things (and to oversimplify), the Act requires a company that seeks to purchase stock or assets of another company to file notification forms with both the DOJ and the FTC. After filing, the company must refrain from closing for at least 30 days. During the 30-day period, the agencies can determine whether to investigate further and seek additional information, which further extends the waiting period until 30 days after substantial compliance with the request for information.