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Antitrust Concerns With Joint Ventures and Other Collaborations: Balancing Competitive vs. Anti-Competitive Effects

Avoiding Liability for "Naked" Agreements, Ancillary Restraints, Collusion;
Assessing the Size and Market Footprint of the JV

THURSDAY, AUGUST 24, 2017

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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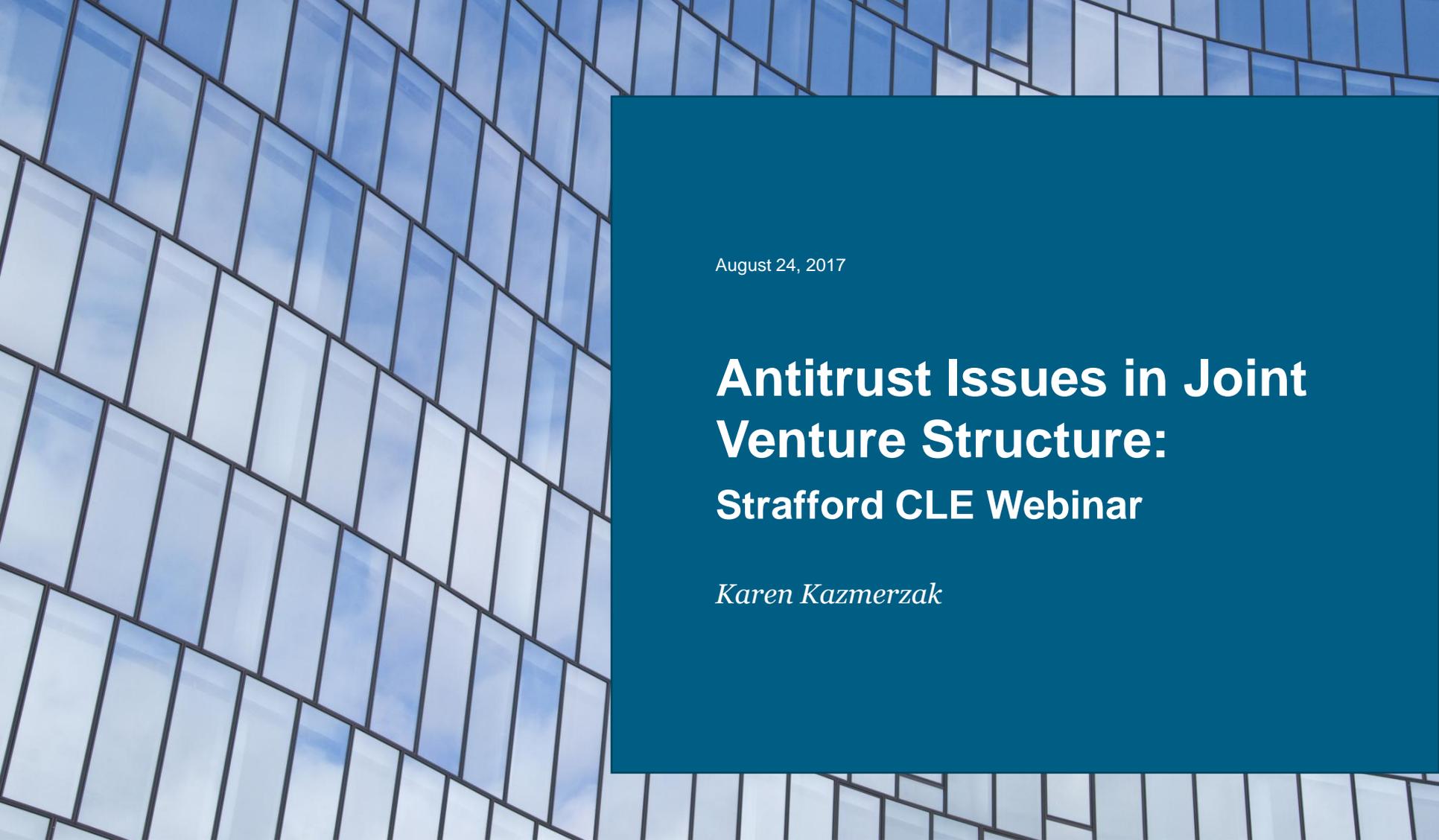
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August 24, 2017

Antitrust Issues in Joint Venture Structure: Strafford CLE Webinar

Karen Kazmerzak

SIDLEY

Introduction and Background

What is a Joint Venture?

- A joint venture (JV) can be any collaborative undertaking by which two or more entities devote their resources to pursuing a common objective.
 - Not all JVs are between competitors
 - Not all competitor collaborations are JVs
- For purposes of this presentation, it means:
 - One or more agreements, other than merger agreements
 - Between or among competitors to engage in economic activity
 - It does not need to be labeled a “joint venture” to be one
- Standards generally more permissive when arrangements do not involve competitors

Why Joint Venture?

- Lower costs
- Obtain economies of scale
- Increase production capacity
- Pool research and development resources
- Commercialize new products
- Facilitate entry into new markets

Pre-formation Considerations

- Composition
 - Relationship between the JV parties
 - Structure of JV
 - Membership model adopted by JV
 - Purpose of JV
 - Other ways to achieve same objective of JV

- Strategic decisions
 - Pricing and output decisions
 - Territories
 - Customers

- Anticipated customer reaction

Joint Venture Membership Models

- Closed
 - Membership generally determined at formation
 - Additional membership typically not contemplated
 - E.g.: Production, marketing and distribution, research and development, fully-integrated
- Limited
 - Members can be added after formation
 - But highly restrictive policies constraining number of members
 - E.g.: Purchasing, distribution
- Open
 - Open to all market participants that meet stated qualifications
 - E.g.: Standard-setting organizations, networks

JVs Come in a Number of Forms

- Co-venturers compete with each other outside the JV
- Co-venturers compete with the JV
- Joint activity often not performed through entities
 - Joint development arrangements
 - Joint marketing and promotion
 - Joint purchasing
- Standard-setting organizations
- Trade association data collection and dissemination
- Benchmarking
- Distribution by vertically integrated firms
 - Where a manufacturer sells through independent distributors and through own distribution arm
 - Where a component manufacturer sells to independent downstream firms and transfers in internal manufacturing operations

Primary Antitrust Laws Governing JVs

- Sherman Act § 1
- Sherman Act § 2
- FTC Act § 5
- Clayton Act §§ 7 and 7A
- Clayton Act § 8

Agency Guidance on JVs

- Antitrust Guidelines for Collaborations Among Competitors
- Statements of Antitrust Enforcement Policy in Health Care
- Accountable Care Organization Guidelines
- Antitrust Guidelines for the Licensing of Intellectual Property
- Other agency guidance
 - DOJ: <https://www.justice.gov/atr/business-review-letters-and-request-letters>
 - FTC: <https://www.ftc.gov/tips-advice/competition-guidance/competition-advisory-opinions>

Antitrust Concerns with Joint Ventures

Strafford Webinar 8/24/17

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Antitrust Issues in JV Structure



- Is the JV a single entity?
 - No structural issues
- Is the restraint a core restraint?
 - No structural issues
- Is the restraint an ancillary restraint?
 - Balancing test
- Is the restraint a collateral restraint?
 - Potentially problematic, could be *per se* unlawful
- Caveats
- Exclusion of competitors

Is the JV a Single Entity?



- If the JV is a single entity, then there are no issues in terms of problematic agreements or restraints; unless the JV exercises or facilitates the exercise of market power, it is lawful
- *American Needle, Inc. v. NFL*, 560 U.S. 183 (2010)
 - JV functions that are controlled by the JV through its ownership of the assets necessary to supply those functions are single-entity functions. Benjamin Klein, *Single Entity Analysis of Joint Ventures After American Needle*
- *Cf. Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210 (D.C. Cir. 1986) (nationwide network of moving companies not a single entity)

Is the Restraint a Core Restraint?



- A restraint (a) involving the JV's products or services and (b) necessary to produce those very products or services (e.g., setting JV prices) is a core restraint
 - A core restraint is either not an antitrust restraint within Section 1, is effectively *per se* lawful, or only to a very limited extent subject to the Rule of Reason. R of R analysis would likely focus on whether the formation of the JV was itself problematic. *Texaco Inc. v. Dagher*, 547 U.S. 1 (2006)
 - JV restraint regarding purchase of inputs

Is the Restraint an Ancillary Restraint?



- An ancillary restraint promotes the procompetitive attributes and competitive success of a legitimate collaboration
 - *E.g.*, agreement by parent not to compete directly with JV
- If a restraint is ancillary, then the burden arguably should be on a plaintiff to prove a less-restrictive alternative that furthers the same legitimate objectives
 - *Cf.* Collaboration Guidelines § 3.2 (restraint must be reasonably related to efficiency-enhancing integration and reasonably necessary to achieve pro-competitive benefits)

Is the Restraint a Collateral Restraint?



- Collateral restraint – e.g., a non-compete between JV parents. *Yamaha Motor Co. v. FTC*, 657 F.2d 971 (8th Cir. 1981)
- Collateral restraints involving competitors are likely condemned under some sort of “quick look.” *Polygram Holding, Inc. v. FTC*, 416 F.3d 29 (D.C. Cir. 2005)
 - Cf. agreement by parent(s) not to compete with JV itself – ancillary restraint – Rule of Reason

Is the Restraint a Collateral Restraint? (Continued)



- At the extremes, such restraints may render the JV a “sham” and may be *per se* unlawful “naked” restraints
 - *U.S. v. Topco Associates, Inc.*, 405 U.S. 596 (1972)
- Recent development: FTC investigation of CDK Global / Reynolds & Reynolds



- *The Medical Center at Elizabeth Place, LLC v. Atrium Health System*, 817 F.3d 934 (6th Cir. 2016)
 - Careful structure defeated by thin “intent” evidence
 - Anomalous decision?

Exclusion of Competitors



- Buying cooperative – Rule of Reason. *Northwest Wholesale Stationers v. Pacific Stationery & Printing*, 472 U.S. 284 (1985)
- Denial of access can nevertheless be condemned. See, e.g., *Realcomp II Ltd. v. FTC*, 635 F.3d 815 (6th Cir. 2011)

IP and JVs



- Patent pools
- Standard-setting organizations
- Network JVs



- *U.S. Philips Corp. v. ITC*, 424 F.3d 1179 (Fed. Cir. 2005); *Princo Corp. v. ITC*, 616 F.3d 1318 (Fed. Cir. 2010)
- Offering of a package license
 - Essential patents
 - Non-essential patents
- Suppression of a patented technology
- *Cf. Broadcast Music v. CBS*, 441 U.S. 1 (1979) (JV to provide blanket copyright licenses)



- *Addamax Corp. v. Open Software Foundation*, 888 F. Supp. 274, 280-81 (D. Mass. 1995) (treating standard-setting organization as a joint venture for antitrust purposes)
- Rule of Reason analysis
 - *National Association of Review Appraisers v. Appraisal Foundation*, 64 F.3d 1130, 1133-34 (8th Cir. 1995)
 - *Broadcom Corp. v. Qualcomm Inc.*, 501 F.3d 297, 309 (3d Cir. 2007) (“private standard setting . . . need not, in fact, violate antitrust law” because of its procompetitive effects)



- Networks – network effects
 - Positive feedback due to demand-side scale-economies; the larger the network, the more valuable it is to buyers/users of network products and services
 - Cooperation may be essential to ensure functions, but may facilitate market power (creation of entry barriers; denial of access to rivals)
 - Rule of Reason generally applied (bank / credit card network cases)
 - Large networks may be subject to Sherman Act § 2

Special Statutory Protections



- National Cooperative Research Act of 1984 (“NCRA”) and National Cooperative Research and Production Act of 1993 (“NCRPA”), codified together at 15 U.S.C. § § 4301-06
- R&D and production JVs (and, after 2004), voluntary standards development organizations
 - Rule of Reason treatment (would likely get anyway)
 - Notification to Agencies → no treble damages (JV and parents)



- Limitations
 - Use of existing facilities not for production of new product/technology
 - Exclusions: marketing / distribution to party other than parent; certain information exchanges; allocating a market with a competitor
 - U.S. nexus

Questions?



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What Information is Permissible to Share Among Co-Venturers?

Two Broad Families of Issues Relating to Information Sharing

- Pre-merger Conduct

- Ongoing Conduct

Main Legal Principles in US Relating to Ongoing Conduct

- Information exchange as discussed here is subject to rule of reason treatment
- Certain content is riskier than other content
 - Price information is riskier than cost and other non-price information
 - Detailed information is riskier than aggregated information
 - Multiplicity of sources
 - Granularity of content
 - Future information is riskier than stale information

Noteworthy Court Decisions

- Maple Flooring Manufacturers' Association v. United States, 268 U.S. 563 (1925)
- Cement Manufacturers' Protective Association v. United States, 268 U.S. 588 (1925)
- United States v. Container Corporation of America, 393 U.S. 333 (1969)
- United States v. U.S. Gypsum Company, 438 U.S. 422 (1978)
- National Society of Professional Engineers v. United States, 435 U.S. 679 (1978)
- Todd v. Exxon Corp., 275 F.3d 191 (2d Cir. 2001)

Agency Guidance

- Competitor Collaboration Guidelines § 3.31(b)
 - “[T]he sharing of information related to a market in which the venture operates or in which the participants are actual or potential competitors may increase the likelihood of collusion on matters such as price, output or other competitively sensitive variables”
- Health Care Statement 6: Provider Participation in Exchanges of Price and Cost Information Safety Zone
 - Independent third-party manages the information exchange
 - Data collected at least 3 months old
 - At least 5 firms reporting and no one firm represents more the 25% of statistic
 - Sufficiently aggregated

Agency Enforcement Actions

- PepsiCo, Inc., FTC File No. 0910133 (2010)
 - Memorialize protocol for handling restricted information
 - Adopt defensive measures (e.g., limit employees, restrict access with IT safeguards)
 - Require confidentiality agreements
 - Train employees on antitrust compliance best practices
 - Monitor compliance

- Decisions & Orders, Sigma Corp.(C-4347) and McWane (C-9351) (FTC 2012)
 - Data exchanged must relate to transactions that are at least 6 months old
 - Data with respect to price, output, and cost for any 3 competitors must not represent more than 60% of dollar or unit sales
 - Communications among competitors may only take place at official meetings relating to the exchange on topics identified on a written agenda prepared in advance of meeting and in the presence of antitrust counsel
 - Industry statistics gathered through the exchange must be made publicly available

Biography



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Karen Kazmerzak, a former Federal Trade Commission attorney, has a broad practice counseling clients regarding antitrust matters involved in mergers and acquisitions and concerning antitrust issues in licensing, distribution, pricing, and competitor collaborations.

Karen represents clients seeking merger clearance from the FTC and the U.S. Department of Justice, and clients that are third-party market participants subpoenaed by the government or that oppose an acquisition. Karen also works closely with co-counsel and economists around the world to develop the best global strategy for clients' advocacy across several jurisdictions, including in the United States.