Cartel & Joint Conduct Review

Newsletter of the ABA Section of Antitrust Law Joint Conduct Committee

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Message from the Editors


by Joel Mitnick and Mark G. Weiss

Welcome to the Spring 2020 Edition of the *Cartel & Joint Conduct Review.* This issue covers the evolving landscape of joint conduct developments, including a high-profile interview of one of DOJ's top criminal enforcers and meaningful discussion of many antitrust hot topics including private equity and antitrust, the economics of no-poach agreements, and high-tech issues including platforms, privacy, and standardization.

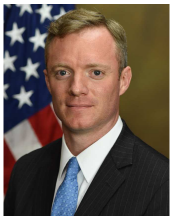
Joel Mitnick interviews Antitrust Division's Deputy Assistant Attorney General for Criminal Enforcement Richard Powers about the scope and direction of criminal prosecutions, including the Heir Location investigation, deferred prosecution agreements, and the new government procurement strike force. Kevin Goldstein and Anora Wang discuss conspiracy claims under Section 1 of the Sherman Act, as recently raised against private equity firms. Nick Dadson, Jee-Yeon Lehmann, and Samuel Weglein provide the approach of economists to analyzing vertical restraints in labor markets. Joel Mitnick and Ngoc Pham Hulbig address whether effects on data privacy are cognizable under the Sherman Act and the FTC Act. And, for a global perspective, Gabriel Araújo Souto investigates the American and European approaches to standardization and the Internet of Things.

IN THIS ISSUE

Interview with DAAG Richard Powers

by Joel Mitnick

Joel Mitnick is a partner at Cadwalader, Wickersham & Taft LLP where his practices focus on antitrust issues.



The JCC's Joel Mitnick recently caught up with the Antitrust Division's Deputy Assistant Attorney General for Criminal Enforcement. What follows is a lightly edited transcript of their discussion.

JM: Let's start with some basics. How does the Division decide when to bring an antitrust case as a criminal case, rather than as a civil case, and particularly in the context of a price-fixing case?

RP: The Division Manual, which is posted on our website, recognizes that there are some situations where the decision to proceed by criminal or civil investigation requires considerable deliberation. The Division draws very clear lines between criminal, *per se*, conduct and civil conduct. In general, the Division's policy is to proceed by criminal investigation and prosecution in cases involving horizontal, *per se*, unlawful agreement such as price-fixing, bid-rigging and customer and territorial allocations. Civil process and civil prosecution are used with respect to other suspected antitrust violations, including those that require analysis under the Rule of Reason. So, there are a number of situations where, although the conduct may appear to be a *per se* violation of law, criminal investigation and prosecution may not be appropriate. These situations may include cases where the case law is unsettled or truly novel issues of law or fact are presented.

JM: In recent memory has the Division charged an individual or entity with a criminal violation in a non-price-fixing case?

RP: We've charged a number of cases that allege *per se* criminal conduct other than price-fixing including bid-rigging and various kinds of allocation agreements. In our investigations we find that conspirators are creative and typically implement their *per se* illegal agreements using a variety of means and methods.

The Division's recent Heir Location Investigation is a great example of a customer allocation scheme without a price-fixing allegation. There, the co-conspirators agreed to allocate customers of heir location services in the United States. They agreed not to compete on an estate on which they encountered each other and to allocate the unsigned heirs to these estates once they realized both were working on the estate. The co-conspirators effectuated this agreement through the use of fee-split agreements, which were estate-specific. In essence, the co-conspirator company that was second to contact an unsigned heir to the estate agreed to end its pursuit of that estate and additional unsigned heirs to the estate in exchange for a percentage of the first or lead company's contingency fees collected from the distributions to the heirs that the company subsequently signed. Four individuals and three companies pleaded guilty in this investigation, which victimized vulnerable heirs, including the elderly.

JM: You've talked about criminal enforcement in the hard core, *per se*, context. Has the Division ever faced a criminal case where the court said that Rule of Reason was the appropriate standard of analysis?

RP: As a general matter we aren't charging Rule of Reason cases criminally. The Division Manual says we charge agreements that fall under the *per se* rule. We've litigated a number of cases where it's a common defense tactic to try to challenge the *per se* rule or to say it should be a Rule of Reason case instead. The Kemp Case (regarding heir location services that I mentioned earlier) is a great example of our team litigating this issue to an ultimately favorable ruling. There, the district court held that the Rule of Reason should apply and also dismissed the case at the trial level as being barred by the statute of limitations. The Division appealed the statute of limitations dismissal up to the 10th Circuit and the 10th Circuit reversed the dismissal and encouraged the district court to reconsider its prior ruling on Rule of Reason versus *per se* Treatment. When the case returned to the district court the judge did reconsider its prior ruling on the Division's motion and ruled in favor of the government saying the *per se* rule would apply. The defendants in that case ultimately changed their pleas to guilty.

JM: Let's shift gears to do the numbers. I believe the high -water mark in terms of annual numbers of new prosecutions was back in the 2014-2015 range at the height of the auto parts cases and financial benchmark cases. Is it correct that the Division is bringing fewer cartel cases and, if so, why?

RP: I'll get to the answer in a second but I think it's probably helpful if I provide some context for how we measure success at the Division. Stats go up, they'll come down with the nature of our work. If we as prosecutors start measuring our success by, for example, sum total of fines collected or the number of cases charged in any particular year, then we start to run the risk of turning into something akin to a company that only focuses on its stock price. Instead, what we talk about is that we are going to be a process-driven organization and, if our process is right, then the appropriate results will follow from that. We're fully committed to antitrust enforcement against cartels and collusion. These are some of the most egregious antitrust violations out there – price-fixing, bid-rigging and customer and territorial allocation. There will be times when the Division's resources are more devoted to the early investigative phases of cases. It's cyclical. And over the course of long running investigations, the stats may reflect a shift from the corporate cases to prosecuting some of the individual cases. In the last few years, as folks have transitioned off some of those investigations a lot of our energy has been devoted to the earlier phase investigations, and now we're coming back to the point where we're making decisions about whether to bring cases. And you've seen some of this with a number of charges announced in various investigations over the last few months. And I can walk through a little bit what we've been busy with.

JM: That'd be great.

RP: It's been really a mix. Late last fall we had two teams busy with trial; one trial out of our packaged seafood investigation where the team successfully litigated and tried the case against the former CEO of Bumblebee Foods and then we had another team almost at the same time in New York litigating a case against a former currency trader at JP Morgan that came out of our foreign exchange case investigation. Two hard-fought litigations that took a significant amount of time to get from indictment to trial where the Division ultimately prevailed at trial. In terms of underscoring how busy we are in developing new criminal matters, we closed fiscal year 2019 with over 100 pending grand jury investigations which is the highest total since 2010. We also opened 38 new grand jury investigations in fiscal year 2019, which is more than any year since 2009. Then moving forward, we also announced the Procurement Collusion Strike Force, which is a new initiative designed to combat antitrust crimes or related schemes in government procurement, grant and program funding. Most recently from late January to early March of this year, the Division announced charges in our long-running investigation into collusion in the generic pharmaceutical industry. We also announced a significant corporate resolution with a major generic drug manufacturer earlier this week and finally, we've also had recent success with bringing international fugitives to justice. In January, the Division announced the second-ever successfully litigated extradition on a Title 15 antitrust charge from the Air Cargo Investigation and earlier this week, we announced another successful extradition on an antitrust charge. This time it was from the Auto Parts Investigation. So, again, bringing it full circle, there is a cyclical aspect to what we do. We're not obsessed with the stats. You know, they go up, they come down. The 2014/15 timeframe was very much a high-water mark. You had a number of significant investigations hit, sort of, around the same time.

JM: One of the actions you just mentioned was the creation last November of the Procurement Collusion Strike Force which is something I was going to ask you about. So, let me turn to that. Can you tell us what that Strike Force is and what it is currently doing?

RP: Back in November we announced the Strike Force which focuses on deterring, detecting, investigating and prosecuting antitrust crimes such as bid-rigging conspiracies and related fraud schemes which undermine competition and government procurement, grant and program funding. The Strike Force is an inter-agency partnership between the Antitrust Division and thirteen initial participating U.S. Attorneys' Offices along with agents from the FBI and partner offices of Inspector General (IG). These teams are working together to conduct outreach and training for procurement officials and government contractors on antitrust risks and the procurement process. They are focused on doing this in their districts which really are spread out across the country and represent a cross-section of the American economy. The Strike Force is different from the Division's standard outreach efforts in that it harnesses the combined capacity and expertise of its members to jointly investigate and prosecute procurement-related crime. In terms of what the Strike Force has been doing since we announced back in November, we have finished all of our initial meetings and have moved forward with our outreach efforts. Since the announcement over 40 federal, state and local government agencies have reached out seeking outreach training, assistance with safeguarding their procurement processes and opportunities to work with the Strike Force on investigations. As part of the Strike Force announcement, we created a website with a reporting portal so that anyone can log on and report any types of collusion on government procurement. That website has already received numerous citizen complaints of possible illegal conduct for investigation and these have been referred out to the relevant Strike Force districts. We've already opened several grand jury investigations in connection with the Strike Force. The last thing I should mention is there's a data analytics piece to the Strike Force. The Strike Force is positioned at the center of an IG-wide effort to utilize data analytics programs across federal, state and local agencies to identify red flags of collusion in government procurement data.

JM: Let me turn to leniency. You said in a recent speech that leniency for second-in and subsequent cooperators is not exclusively focused on the order in which companies come in the door and agree to cooperate and plead guilty. Can you provide some real examples of when the Division skipped over a second-in in favor of a later-in applicant and what factors were involved?

RP: The Division's leniency policy is distinguished from others around the world in the sense that leniency is only open or available to the first to self-report so all of the subsequent companies that come in to cooperate by definition miss leniency. But they do have the opportunity to earn cooperation credit and the point we've been making for a while is that we don't base that discount on the order you come in. It's based on the value of the cooperation you provide. Embedded in that is the idea that the earlier you come in and cooperate, the better the chance there is to earn cooperation credit. You have to provide valuable cooperation; meaning if we had a four-party conspiracy if the first company comes in and gets leniency the second and third company both have an opportunity to cooperate and receive a substantial discount if they really help advance our investigation. However, the last holdout company will not usually have the opportunity to cooperate in the same way to earn credit. Now, the concept we are trying to get at is, you have to provide valuable cooperation. If you're the second in and you don't provide us much in the form of cooperation we won't give you some set amount of a discount, and it's possible that the third company in the door could provide much more valuable cooperation and thus, receive a higher discount.

JM: The Division's new policy offering deferred prosecution agreements to later-in applicants in certain circumstances is still less than a year old. Has the Division had actual experience with applicants for DPAs?

RP: It's probably helpful if I step back and talk a little bit about the circumstances when we would enter into a deferred prosecution agreement with a company. And there are some public examples going beyond this past year of when the Division did enter into deferred prosecution agreement. For example: In the LIBOR Investigation, the Division entered into the deferred prosecution agreement with several of the banks that had a Title 15 charge, and we've done several in our generic drugs investigation. But, the big change in the last year was the Division's willingness to credit compliance at the charging stage and that credit is in the form of a deferred prosecution agreement. How companies can earn that credit is by demonstrating a robust and effective compliance program. But it's important to remember that part of what we said when we made that announcement and when we talked about the circumstances under which we would enter into deferred prosecution agreement is that the credit is not exclusively based on an effective compliance program. Compliance is one of ten factors contained in the principles of federal prosecution and business organizations. We, at the Division, will do a deep dive on a company's compliance program and take account of that along with the other factors – for example – the nature and seriousness of the offense, pervasiveness of wrongdoing, cooperation, collateral consequences and all the other factors and decide what the appropriate form of disposition is. For any company that comes before the Division seeking DPA credit for a compliance program that's the general approach we're going to take. I'll also note that there's a relevant considerations section in the Division's DPAs that discusses what the Division considered when entering into these agreements and I think there what you would see is there is a discussion of, among other things, the cooperation provided by the company as well as collateral consequence issues. Those are the types of factors and things we consider when we are entering into DPAs, and I think, for companies that don't get DPAs, it is because we've done the multi-factored analysis and decided that a criminal charge in the form of either a guilty plea or an indictment was the appropriate form of disposition.

JM: Thank you. Last question. Inquiring minds are always interested in the path that led folks to senior government positions. What interests and experiences led you to be the head of the criminal section?

RP: How I got interested in antitrust is an interesting story. My mom is a journalist and has been a journalist for a long time and she covered stories involving significant bid-rigging prosecutions back in the late 90s and early 2000s. When I went to law school she actually told me: "You should look at antitrust, they actually do some interesting things" because she knew I wanted to go to the Department of Justice. I came into the Antitrust Division through the honors program, which allows students coming straight out of law school to go directly into the Department. I started in our Atlanta office and then I had the opportunity to move up to New York and work on financial market matters and spent most of my time up there working on the municipal bonds investigations and LIBOR. And that really just cemented what I love about antitrust, which is that you get to learn all of these industries you may never be exposed to. I have no background in financial services but I took the opportunity to go work on it, and I really just enjoyed it. After that, I worked pretty closely with the fraud section of the Criminal Division and made the decision to jump over. It worked out that I was able to go to the Eastern District of New York where the fraud section had a team that prosecuted healthcare fraud cases. That's where I was when this job came open and then I applied for it and went through the normal processes. So, that's my path from law school getting to where I am now. The last part I would add is: before I went to law school I spent five years on active duty in the army as an infantry officer and so I had spent most of my adult life including my time at West Point in federal service somehow. Public service has been an important part of my life and it's absolutely a privilege and honor to be a Criminal Deputy at the Antitrust Division and to continue serving.

When Private Equity Firms Face U.S. Antitrust Liability for Portfolio Company Conduct

By Kevin B. Goldstein and Anora Wang

Mr. Goldstein is an associate and Ms. Wang is an associate at Winston & Strawn LLP, where their practices focus on antitrust matters.

In multiple recent litigations, private equity (PE) firms have faced antitrust conspiracy claims under Section 1 of the Sherman Act arising—at least primarily—out of alleged anticompetitive conduct by their portfolio companies, rather than the PE firms themselves. These cases raise important questions for PE firms and their lawyers to consider as they evaluate risks from portfolio company operations and structure their investment and management relationships. This article discusses rulings from two recent cases—*In re Packaged Seafood Products Antitrust Litigation* and *In re Liquid Aluminum Sulfate Antitrust Litigation*—and the standards courts applied to determine whether a PE parent had liability based on portfolio company conduct.

It is clear that if a PE firm is actively participating in an antitrust conspiracy, then it will face liability. For example, in cartel cases, if PE partners or employees are attending cartel meetings on behalf of their firm and entering into price-fixing agreements with a portfolio company's competitor (or the competitor's parent), the PE parent can expect to be treated as any other conspirator. But what happens when the PE parent is not at the cartel meeting and is not a party to any agreement with a competitor? In cases where evidence ties only a portfolio company directly to an antitrust violation, but does not show direct participation by the PE parent, evaluating the parent's potential antitrust liability depends heavily on the details of the PE-portfolio company relationship.

In assessing the relationship between a PE firm and its portfolio company, a useful starting point is the Supreme Court cases that have laid out the fundamental principles of "corporate separateness"—that a parent corporation and its subsidiary are separate corporate forms[1]; and that the rule of corporate separateness "insulates a parent corporation from liability created by its subsidiary, notwithstanding the parent's ownership of the subsidiary."[2] As in a typical parent-subsidiary relationship, a PE firm should enjoy the presumption of corporate separateness that is only to be overcome by allegations of sufficient facts tending to show otherwise.

A claim seeking to impose antitrust liability on a PE parent for acts by its portfolio company is essentially asking the court to "pierce the corporate veil," a legal concept where entities' separate corporate forms are disregarded in limited, extreme circumstances.[3] The

[1] *Dole Food Co. v. Patrickson*, 538 U.S. 468, 474 (2003).

[2] *United States v. Bestfoods*, 524 U.S. 51, 61 (1998).

[3] Various circuit have held that the corporate veil may be pierced only in limited circumstances. *See, e.g., Doe v. Unocal Corp.*, 248 F.3d 915, 926 (9th Cir. 2001) (per curiam), *abrogated on other grounds by Daimler AG v. Bauman*, 571 U.S. 117 (2014).

federal antitrust laws, unlike some other federal statutes, do not contain statutory guidelines on when the corporate veil can be pierced, when to disregard the corporate form, or when to apply relevant state law on this issue.[4] Courts have recognized that corporate-veil-piercing is *context specific* and *purpose specific*, meaning that a pierced corporate veil in one situation might still remain intact in a different situation.[5] Therefore, it is understandably difficult for courts to articulate a generalized rule, even if only for the specific PE parent-portfolio company relationship, or only for violations of federal antitrust laws.

Without a separate framework for antitrust cases, courts have analyzed PE-portfolio relationships under the same legal frameworks used to evaluate potential parental liability in parent-subsidiary relationships in a variety of other contexts.[6] This includes asking (1) whether the portfolio company is an alter ego of the PE firm; (2) whether the portfolio company is merely an agent of the PE firm in its act violating the antitrust laws; or (3) if the challenged conduct involves individuals who hold positions in both the PE firm and the portfolio company. However, the cases demonstrate that some of these considerations are more relevant than others in the PE context.

Theories of alter ego, agency, and vicarious liability have been argued and considered in two recent district court cases, which demonstrate that courts are generally reluctant to "pierce the corporate veil" at the motion to dismiss stage, but are willing to let antitrust claims go forward against PE firms where there is at least some allegation of the PE firm's direct participation in the alleged antitrust violation.

I. Theories Recently Tested in District Courts

Two recent cases tested how district courts evaluate theories of agency and vicarious liability at the motion to dismiss stage in deciding whether a PE firm can face antitrust liability for conduct by its portfolio company. In both cases, courts denied the motions to dismiss as to those defendants that they found were sufficiently alleged to have *directly* participated in a conspiracy. Yet, in the absence of finding sufficient allegations of direct participation, one court went on to consider and reject various theories of vicarious liability, ultimately dismissing all claims against the PE parent.

In *In re Liquid Aluminum Sulfate Antitrust Litigation*, the U.S. District Court for the District of New Jersey denied a PE defendant's motion to dismiss, holding that inquiries into the plaintiff's theory of liability based on the PE firm's ownership of the portfolio company would be more appropriate for a later stage such as for summary judgment.[7] However, because the court found the alleged facts sufficient to subject the PE firm to potential liability for *direct* involvement in the alleged conspiracy, it's unclear whether the court would have let the ownership-based theory of liability survive the motion to dismiss on its own.

Then in *In re Packaged Seafood Products Antitrust Litigation*, the U.S. District Court for the Southern District of California, dealing with allegations of tuna price-fixing, considered motions to dismiss by a British PE firm, its U.S. subsidiary, and a related holding company that were invested in the Bumble Bee tuna company. There, the court found that the alleged facts failed to show two of

[4] *See e.g.*, Fair Labor Standards Act § 3(r), 29 U.S.C. § 203(r) (1976) (single-enterprise standard); ERISA § 4001(b), 29 U.S.C.A. § 1301(b)(1) (West Supp. 1981) (common control standard); Federal Tort Claims Act, 28 U.S.C. §§ 1346(b), 2672, 2674 (1976).

[5] *See e.g.*, *In re Sugar Indus. Antitrust Litig.*, 579 F.2d 13, 18-19 (1978) ("After considering all of the facts in this case, we conclude that, *at least for this purpose and in this context*, the subsidiary should be treated as the alter ego of the parent." (emphasis added)).

[6] This article generally assumes that the PE firm's ownership and control of the portfolio company is uncontested. In situations where a PE firm owns only a portion of the portfolio company or otherwise lacks control, additional considerations would apply.

[7] *City of Greensboro v. Am. Sec., LLC* (*In re Liquid Aluminum Sulfate Antitrust Litig.*), 2018 U.S. Dist. LEXIS 16577, *38, 2018 WL 658691.

the PE entities' direct involvement in the alleged price-fixing conspiracy. The court went on to reject the plaintiffs' "alter ego theory"— that attempted, among other things, to impute acts of the portfolio company to the PE investors—for failure to allege an "unity of interest." The court also rejected the plaintiffs' "agency theory"[8] and "vicarious liability theory" (involving dual officers) when the plaintiffs failed to overcome a presumption that "the directors are wearing their 'subsidiary hats' and not their 'parent hats' when acting for the subsidiary."[9]

A. In re Liquid Aluminum Sulfate Antitrust Litigation (D.N.J. 2018)

In *Liquid Aluminum Sulfate*, a PE firm that owned entities running a water chemical business, and two individuals working for the PE firm as managing directors, among others, were named as defendants in antitrust litigation concerning alleged collusion to allocate customers and/or fix the price of a water treatment chemical, liquid aluminum sulfate, known as "Alum." The PE firm and its two managing directors (the "PE defendants") filed motions to dismiss in the district court, which the court denied on February 1, 2018. In 2019, the PE firm agreed to pay $13 million to settle the antitrust claims against it.[10]

In their motions to dismiss, the PE defendants argued that their "mere ownership" of the portfolio company was "insufficient to subject them to liability" for the portfolio company's alleged antitrust violation.[11] The court rejected this argument with minimal discussion, citing two reasons. First, the court found that the complaint allegations included "numerous specific examples" that, if found to be true, could make the PE defendants liable for having directly participated in the alleged conspiracy.[12] Second, which is important for its implications, was that "[s]uch an argument seems to be more appropriate for the summary judgment phase of the case and not the motion to dismiss phase."[13]

There, the allegations pertaining to the PE firm's direct involvement included that the PE defendants (1) reviewed and authorized significant Alum bids, (2) oversaw the portfolio company's announced intent to increase prices in the market, (3) required that all bids by the portfolio company over a certain amount be approved by the PE firm, where the approved price was determined by whether the portfolio company was "predestined to win" or submitting an intentionally losing "throw-away" bid, and (4) requested monthly reports in order to monitor the conspiracy.[14]

As the *Liquid Aluminum Sulfate* case shows, when a court considers plaintiffs' allegations of the PE firm's direct involvement in the conspiracy sufficient to move the case to a next phase, it may opt to preserve the plaintiffs' ownership-based theory of liability as well without detailed analysis of when to disregard the basic rule of corporate separateness.

B. In Re Packaged Seafood Products Antitrust Litigation (S.D. Cal. 2020)

In *Packaged Seafood Products*, three PE-related entities—a British PE firm, its subsidiary U.S. PE firm, and a related Cayman Islands holding company that ultimately held the assets of the portfolio company Bumble Bee, a packaged seafood manufacturer—among others, were named as defendants in litigation alleging a conspiracy to fix prices of packaged seafood throughout the United States.

The claims went through two rounds of motion to dismiss briefing and rulings.

In the first ruling, on September 5, 2018 (the "2018 order"), the court denied a motion to dismiss as to one of

[8] *In re Packaged Seafood Prods. Antitrust Litig.*, No. 3:15-md-02670-JLS-MDD (S.D. Cal. Jan. 28, 2020) (ECF No. 2270) (order granting defendants' motion to dismiss), at 15.

[9] *Id.* at 16 ((*citing Bestfoods*, 524 U.S. 51 (1998)).

[10] *In re Liquid Aluminum Sulfate Antitrust Litigation*, No. 2:16-md-02687-JLL-JAD (D.N.J. May 13, 2019) (ECF No. 1293) (order granting preliminary approval of proposed settlement).

[11] *In re Liquid Aluminum Sulfate Antitrust Litig.*, at *38-39.

[12] *Id.* at *32.

[13] *Id.* at *38.

[14] *Id.* at *31-32.

the three PE defendants (the U.S. entity), but dismissed the parent British entity and the Cayman Islands holding company.[15] The court's partial denial of the motion to dismiss was based on its finding that the complaint "plausibly demonstrates [the U.S. PE entity] directly participated in the ongoing conspiracy."[16] By contrast, the court found insufficient allegations that the British or Cayman Islands defendants directly participated in the alleged conspiracy or that the U.S. PE entity or portfolio company were alter egos of them.[17]

Subsequently, the plaintiffs amended their complaints against the British PE firm and the Cayman Islands holding company, and the two defendants again filed a joint motion to dismiss for lack of personal jurisdiction and for failure to state a claim. The court granted the defendants' motion on January 28, 2020 (the "2020 Order").[18] In the 2020 Order, the court's analysis addressed claims based on theories of "*agency*" and "*vicarious liability*."

The following summarizes the court's relevant analysis from both the 2018 Order and 2020 Order.

1. <u>*Alter Ego Liability Theory*</u>

As addressed in the 2018 Order, the plaintiffs initially relied on an alter ego theory to support both their arguments for antitrust claims and for exercise of personal jurisdiction over the British PE firm and the Cayman Islands holding company. Because the court considered the parties' alter ego arguments on both issues to be "co-extensive," it addressed the theory at length in its analysis of personal jurisdiction, and then largely incorporated that same discussion for its analysis of the antitrust claims.[19]

In its discussion of personal jurisdiction, the district court laid out the Ninth Circuit's alter ego test to exercise jurisdiction on a parent by imputing the subsidiary's contacts with the forum:

> To satisfy the alter ego exception, the plaintiff must demonstrate "(1) that there is such unity of interest and ownership that the separate personalities [of the two entities] no longer exist and (2) that failure to disregard [their separate identities] would result in fraud or injustice."

2018 Order at 1143 (*citing Unocal*, 248 F.3d at 926 (alterations in original).

As between the British PE firm and the portfolio company, the defendants first argued that, as a threshold matter, alter ego liability was foreclosed because the former did not directly own the latter. The court responded that actual/direct ownership is not a prerequisite for an alter ego theory, as "equitable ownership might be sufficient in some contexts."[20]

In analyzing whether a PE firm has "equitable ownership"

[15] *In re Packaged Seafood Prods. Antitrust Litig.*, 338 F. Supp. 3d 1118, 1186 (S.D. Cal. Sep. 5, 2018) [hereinafter, 2018 Order].

[16] *Id.* at 1180. Here, the court cited allegations that included (1) the U.S. PE firm was subject to an ongoing DOJ inquiry where the portfolio company had already pled guilty to price fixing; (2) the PE firm had knowledge of the market dynamics that should have caused it to "diagnose why prices remained elevated despite decreasing demand and increasing supply; (3) a telephone conversation involving a dual officer of the British PE firm and its subsidiary U.S. firm that discussed non-public price list information; and (4) emails between dual officers of the British PE firm and its subsidiary U.S. firm discussing actions to show public support of price increase. *Id.* at 1180-82.

[17] *See id.* at 1155, 1174. While some allegations implicating the U.S. PE entity might also have implicated the British or Cayman Islands entities, the court found that the plaintiffs had "impermissibly engaged in group pleading without differentiating between who was employed by what entity" and deemed the allegations insufficient as to those two entities. *Id.* at 1184.

[18] *In re Packaged Seafood Prods. Antitrust Litig.*, No. 3:15-md-02670-JLS-MDD (S.D. Cal. Jan. 28, 2020) (ECF No. 2270) (order granting defendants' motion to dismiss) [hereinafter, 2020 Order].

[19] 2018 Order, 338 F. Supp. 3d 1174.

[20] *Id.* at 1149 (*citing* In re Schwarzkopf, 626 F.3d 1032, 1038 (9th Cir. 2010)).

of a portfolio company that was separated by several layers of controlling entities, the court cited precedent that owning no shares was not dispositive if sufficient facts existed to demonstrate that one "acted as owner" of the other;[21] and that equitable ownership existed where "business activities are effectively controlled by its managing agent and attorney-in- fact."[22] The court found that the British PE firm had equitable ownership of the portfolio company, considering facts showing (1) the British PE firm exercised control and directed the investment of the fund that ultimately owned the portfolio company; (2) the British PE firm executives themselves seemed to think they owned the portfolio company; and (3) the portfolio company, in its criminal plea agreement with the Department of Justice, included the British PE firm as a "parent company."[23]

After having satisfied itself that the British PE firm had sufficient equitable ownership of the portfolio company, the court then moved on to analyze their "unity of interest" under the alter ego test. Following the Ninth Circuit precedents *Doe v. Unocal Corp* and *Ranza v. Nike, Inc.*, the court stated that "[t]he unity of interest element requires 'a showing that the parent controls the subsidiary to such a degree as to render the latter the mere instrumentality of the former."[24] Focusing on "control,"[25] the court turned to the cases as cited in *Unocal* to guide its inquiry.

Specifically, the court cited situations as sufficient to show unity of interest and appropriate for corporate veil piercing where: (1) the parent uses its subsidiary as a "marketing conduit" and tries to shield liability arising from the subsidiary's activities;[26] (2) the parent directs every facet of the subsidiary from broad policy decisions to routine matters of day-to-day operations.[27] Conversely, merely showing the following would be *insufficient* to show an unity of interest:

> (1) involvement in its subsidiaries' acquisitions, divestments and capital expenditures; (2) formulation of general business policies and strategies applicable to its subsidiaries, including specialization in particular areas of commerce; (3) provision of loans and other types of financing to subsidiaries; (4) maintenance of overlapping directors and officers with its subsidiaries; and (5) alleged undercapitalization of its subsidiaries.

2018 Order, at 25 (citing *Unocal*, 248 F.3d at 927).

Applying these principles to the relationship the British PE firm and the portfolio company, the court found that the plaintiffs' evidence fell short of alleging a unity of interest, because (1) merely receiving information and providing input on business decisions did not reach the level of active involvement to overcome the observance of corporate formalities;[28] (2) the fact that the British PE firm placed directors on the portfolio company's board, by itself, is not dispositive;[29] and (3) the facts pertaining to the British PE firm's placement of a large debt on the portfolio company (e.g., increasing debt-to-capital ratio from 60% to 90%) did not reach the level of pervasive undercapitalization required to demonstrate unity of

[21] *Id.* at 1150 (*discussing* Tatung Co. v. Shu Tze Hsu, 217 F. Supp. 3d 1138, 1178 (C.D. Cal. 2016)).

[22] *Id.* (*discussing* Troyk v. Farmers Grp., Inc., 171 Cal. App. 4th 1305, 1343 (Ct. App. 2009)), *as cited in Schwarzkopf*, 626 F.3d 1032, 1039 (9th Cir. 2010)).

[23] With regard to the last fact, the court reasoned that even if the term "parent companies" were not defined, it indicated at least "some modicum of control" of the portfolio company by the PE firm. *See id.*

[24] *Id.* at 1145 (*citing* Ranza v. Nike, Inc., 793 F.3d 1059, 1073 (9th Cir. 2015) (*quoting Unocal*, 248 F.3d at 926).

[25] For a more extensive discussion on courts' analysis of "control" in the joint conduct context, see generally James Keyte & Kenneth Schwartz, Private Equity and Antitrust: A New Landscape, ANTITRUST (Fall 2016) 21 (differentiating having "legal control" as evidenced in economic interest and voting rights and having actual con- trol through requirement of approval for certain actions and sitting on board).

[26] 2018 Order,at 1145 (*citing Unocal*, 248 F.3d at 926 (*quoting* United States v. Toyota Motor Corp., 561 F. Supp. 354, 359 (C.D. Cal. 1983)).

[27] *Id.* (*citing Unocal*, 248 F.3d at 926–27 (*quoting Rollins Burdick Hunter of S. Cal., Inc. v. Alexander & Alexander Servs., Inc.*, 206 Cal. App. 3d 1, 11 (Ct. App. 1988)).

[28] *Id.* at 1153.

[29] *Id.* at 1154.

interest.[30] Having concluded that the plaintiffs did not allege "unity of interest," the court ruled that the plaintiffs' "alter ego" theory failed for jurisdiction as well as liability.

2. *Agency and Vicarious Liability Theories*

In the 2020 order, the *Packaged Seafood Products* court addressed the British PE firm's and the Cayman Islands company's motion to dismiss claims in the amended complaint alleging liability under theories of "agency" and "vicarious liability."[31] While the plaintiffs made another attempt to allege *direct* participation in the conspiracy by the PE firm and the holding company, the court found no new plausible allegations on this ground.

In their remaining theories, the plaintiffs argued that the British PE firm should be liable because (1) the U.S. PE firm subsidiary was merely an agent of the British PE firm, and (2) employees of the U.S. subsidiary involved in the alleged anticompetitive acts also held positions at the British PE parent ("dual officers").[32] The court's analysis focused significantly on the allegations related to dual officers.

The court began its agency analysis under federal common law principles of agency,[33] and looked to the general test set out in the Restatement of Agency:[34] However, focusing on the allegations related to dual officers, the court further framed its analysis under the Supreme Court's hold in *United States v. Bestfoods*, which established that "when alleging liability for a parent corporation based on the actions of an employee of both the subsidiary and the parent corporation, the party alleging liability must plead facts showing that the employee was acting within his or her capacity as an employee of the parent corporation and not the subsidiary."[35] "Otherwise, courts 'generally presume that the directors are wearing their 'subsidiary hats' and not their 'parent hats' when acting for the subsidiary.'"[36]

Relying upon this *Bestfoods* presumption, the court went on to find that, although the complaint contained allegations of anticompetitive acts undertaken by certain dual officers of both the British PE firm and its subsidiary U.S. PE entity, plaintiffs had failed to plead sufficient facts that those employees were acting on behalf of the parent British PE firm and not the subsidiary.[37] The court also gave particular weight to the defendants' contention that the dual officers were acting in their capacity as employees of the U.S. PE entity because it was consistent with the overall corporate function of that U.S. entity, which had been tasked by the parent with oversight of the Bumble Bee portfolio company.

Thus, the court rejected the plaintiffs' theories of agency, as well as vicarious liability, when they failed to provide extra facts to overcome the presumption that the individual was acting in the subsidiary capacity.

II. CONCLUSION

There is no separate statutory rule for courts to assess whether the relationship between a PE firm and a portfolio company justifies imposing liability on the PE firm for alleged antitrust violations by the portfolio company. However, all analyses start from the same presumption of respecting the corporate forms as they exist separately, and attaching liability on the parent only in limited and extreme cases, where "piercing the corporate veil" is warranted. In conducting this analysis,

[30] *Id.*

[31] The plaintiffs also made a futile attempt to raise a "representative service doctrine" that the court summarily addressed as a non-viable theory for imposing liabil- ity. *See* 2020 Order, at 17 ("The Court has been unable to find, and Plaintiffs have failed to provide, a single case in which any court has found liability for a parent corporation based on the representative services doctrine.").

[32] *Id.* at 7-9.

[33] *Id.* at 15. The parties did not dispute that federal common law was applicable.

[34] "[A] plaintiff must demonstrate: (1) a manifestation by the principal that the agent shall act for him; (2) that the agent has accepted the undertaking; and (3) that there is an understanding between the parties that the principal is to be in control of the undertaking." *Id.* (*citing* Restatement (Third) of Agency,§ 1.01).

[35] *Id.* at 16 (*discussing Bestfoods*, 524 U.S. 51, 69-70 (1998)).

[36] *Id.*

[37] *Id.*

courts make fact-intensive inquiries of the relation between a PE firm and portfolio companies in order to arrive at a context specific and purpose specific decision on the appropriateness of attaching antitrust liability.

PE firms should be aware that, if their portfolio companies are drawn into antitrust litigation, they themselves as parents could well be drawn in with them. Although courts are reluctant to pierce the corporate veil, where there is some evidence of the PE parent's direct participation in the alleged conspiracy—even if relatively minor evidence—courts have been willing to allow claims to go past the motion to dismiss stage against the PE parent.

PE parents can give themselves some protection by focusing managerial responsibility with those employees that have a formal executive or director role in the portfolio company, rather than allowing information to flow freely up to the PE level and to employees of the parent that have no official role in the portfolio company. PE parents, like any corporate parent, can also protect themselves and their investment through having a robust antitrust compliance program. In the case of PE firms in particular, investing in thorough antitrust-focused diligence on the front-end—before acquiring the target—can catch existing risks before they become the PE firm's liability.

Vertical Relationships, Horizontal Effects? The Evolving Debate on Vertical Labor-Market Restraints

by Nick Dadson, Jee-Yeon Lehmann, and Samuel Weglein

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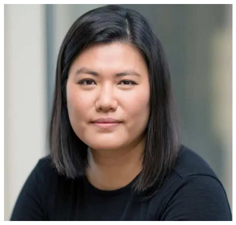

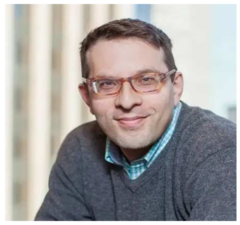

The 2016 joint Department of Justice ("DOJ") and Federal Trade Commission ("FTC") Antitrust Guidance for Human Resource Professionals and various statements of interest filed by the DOJ in no-poach litigation matters in 2019[2] make clear that that "naked" no-poach agreements—those that are not reasonably ancillary to legitimate collaborations or joint ventures—between horizontal competitors for labor are *per se* illegal.[3]

However, there has been a growing debate over the appropriate treatment of labor-market restraints between parties with vertical elements: (1) no-poach clauses in the franchise context; and (2) non-compete agreements between an employer and an employee. In this article, we explore the nature of these two types of agreements and discuss the evolving debate on their potential competitive effects and factors impacting the proper legal standard for their evaluation.

I. Franchise No-Poach Agreements

"No-poach" agreements in the franchise context are clauses in franchise contracts that restrict franchisees from soliciting and/or hiring employees from other franchisees within the same system. According to estimates in 2016, nearly 60% of the major franchises across a variety of industries—such as fast-food restaurants, automotive services, cleaning services, and tax preparation services—included such "no-poach" clauses in their standard franchise contracts.[4] Since 2017, such franchise no-poach agreements have been the subject of antitrust scrutiny by government enforcers and private litigants, most notably by the State of Washington's attorney general (AG). According to the Washington AG's office, it has negotiated for the removal of no-poach clauses at over 100 franchises nationwide since starting its investigations in early 2018.[5]

Amid the flurry of class actions and enforcement activities against franchisors for the use of no-poach provisions in their contracts, there has been a growing debate over the appropriate antitrust standard under which to evaluate

1 The authors thank Noah Kessler for his excellent research assistance.

2 *See*, *e.g.*, Statement of Interest of the United States, In Re: Railway Industry Employee No-Poach Antitrust Litigation, No. 2:18-MC-00798 (W.D. Pa. Feb. 8, 2019), ECF No. 158; *see also* Statement of Interest of the United States, Danielle Seaman v. Duke University, et al., No. 1:15-cv-462 (M.D.N.C. Mar. 7, 2019), ECF No. 325.

3 Dep't of Justice Antitrust Div. and Fed. Trade Comm'n, Antitrust Guidance for Human Resource Professionals 3 (Oct. 2016), https://www.justice.gov/atr/file/903511/download.

4 Alan B. Krueger and Orley Ashenfelter, *Theory and Evidence on Employer Collusion in the Franchise Sector*, 4 (NBER Working Paper No. 24831, 2018), https://www.nber.org/papers/w24831.

5 Washington State Office of the Attorney General, AG Ferguson's Initiative to End No-Poach Clauses Nationwide Reaches 100 Corporate Chains (Oct. 7, 2019), https://www.atg.wa.gov/news/news-releases/ag-ferguson-s-initiative-end-no-poach-clauses-nationwide-reaches-100-corporate.

these franchise no-poach agreements. In early 2019, the DOJ sought to bring clarity by filing a statement of interest in several pending antitrust cases against franchisors. In its statement, the DOJ pointed to the vertical relationship between the franchisor and franchisees as a basis for subjecting most no-poach clauses in franchise contracts to a full rule of reason analysis.[6] In response, the Washington State AG's office filed its own amicus brief advocating for a presumptive *per se* treatment of no-poach clauses in horizontal franchise agreements with corporate-owned stores,[7] and broadly contending that a franchisor bears a "heavy burden" to demonstrate that the no-poach provision is ancillary and reasonably necessary to the operation of the franchise system.[8]

At the motion-to-dismiss stage, courts have differed in their view of no-poach provisions in franchise contracts. Some courts have found that the provisions and facts alleged do not warrant *per se* analysis,[9] while others have found that the plaintiff's alleged facts provided sufficient grounds for a quick-look analysis.[10] Still others have declined to decide which standard is applicable in the early stages of the litigation.[11]

The current debate highlights two key issues that are relevant to determining which antitrust standard is applicable to assessing franchise no-poach provisions. The first issue is whether and to what extent franchisors and franchisees constitute a single economic entity (or whether, in the alternative, they are horizontal competitors). The second issue is whether there are salient procompetitive benefits from no-poach agreements in the franchise system.

Independence of Franchisors and Franchisees?

Evaluation of the first issue requires assessing the nature of the business relationships that exist within the franchise system and the alignment of economic interests between franchisor and franchisee. Economists often describe the franchising business model as a "contractual alternative to vertical integration."[12] The franchisor-franchisee relationship can thus be seen as a vertical one in which the franchisor supplies various inputs—tangible and intangible—to the franchisee, which, in turn, supplies a product or service to customers in a local area. To harness the benefits that vertical integration provides without resorting to vertical integration, franchise contracts often contain a set of vertical restraints, including input purchase requirements, resale price controls, and output quotas.[13]

Economic studies on franchising indicate that the franchisor and the franchisees have a strong shared interest in creating a brand that is known for its uniformly high-quality product. Competition within the brand can hinder the brand's ability to achieve these objectives and to compete effectively against other brands, so franchisors may impose contractual terms that limit intra-brand competition and instead foster inter-brand competition. For example, franchisors often place restrictions on their franchisees' pricing to ensure that franchisees do not engage in a "race to the bottom" which may diminish the quality of the product or service, and hence, the value of the brand.[14] Similarly, many franchisors offer some form of territorial restrictions or require the franchisees to purchase certain inputs exclusively from the franchisor or from a franchisor-designated exclusive supplier.[15] Although these restrictions "limit the franchisee's ability to behave opportunistically" and "reduce the franchisee's independence and limit his [or her] capacity to personalize his [or her] business,"[16] the franchisees recognize the benefit that these vertical controls can have on the entire brand, and therefore, their ability to compete with other franchise systems.

[6] *See, e.g.*, Corrected Statement of Interest of the United States of America at 11, Stigar v. Dough Dough, Inc., et al., No. 2:18-cv-00244 (E.D. Wash. Mar. 8, 2019), ECF No. 34 ("The franchise relationship is in many respects a vertical one because the franchisor and the franchisee normally conduct business at different levels of the market structure. Restraints imposed by agreement between the two are usually vertical and thus assessed under the rule of reason.").

[7] Amicus Curiae Brief by the Attorney General of Washington at 7, Stigar v. Dough Dough, Inc., et al., No. 2:18-cv-00244 (E.D. Wash. Mar. 11, 2019), ECF No. 36.

[8] *Id.* at 9.

[9] *Ogden v. Little Caesars Enters., Inc. et al.*, 393 F. Supp. 3d 622, 633 (E.D. Mich. 2019).

[10] *Deslandes v. McDonald's USA LLC et al.*, 2018 WL 3105955, *8 (N.D. Ill. June 25, 2018).

[11] *Butler v. Jimmy John's Franchise, LLC*, 331 F.Supp.3d 786, 797 (S.D. Ill. 2018) (describing the evidence pled by the plaintiff as likely supporting a quick look analysis, but allowing the *per se* standard would be appropriate if "Herculean independence" among franchises were shown and "the rule of reason may rear its head" if "Jimmy John's carries its burden under the quick look approach").

[12] Roger D. Blair and Francine Lafontaine, The Economics of Franchising 19 (New York: Cambridge University Press, 2010).

[13] *Id.* at 82.

[14] Franchise agreements may also include some form of an assigned geography within which the franchisee may operate its franchise, and may require the franchisee to acquire certain inputs exclusively from the franchisor or from a franchisor-designated exclusive supplier.

[15] Francine Lafontaine and Margaret Slade, *Franchising and Exclusive Distribution: Adaptation and Antitrust*, in The Oxford Handbook of International Antitrust Economics, Vol. 2 (Roger D. Blair and D. Daniel Sokol, eds., New York: Oxford University Press, 2015).

[16] Blair and Lafontaine, *supra* note 12, at 125.

While most enforcement agencies and private litigants recognize some level of alignment in the economic interests of franchisors and franchisees, some have pointed to the existence of franchisor-owned stores as evidence that the no-poach clauses are not purely vertical restraints with cognizable benefits to competition. Plaintiffs also underscore that even given some alignment of economic interests, it is important to assess whether the individual franchisees have distinct *hiring* interests. The debate on the proper standard will depend on whether plaintiffs can adequately plead hub-and-spoke conspiracies. Specifically, does the provision constitute more of a vertical agreement between the spokes (franchisees) and the hub (the franchisor), or it is more of a horizontal agreement among individual franchisees or stores along the rim of the wheel? To the extent that they are enforced, the impact on the mobility of employees from vertical agreements between the franchisor and each franchisee in the system, and from horizontal agreements among the franchisees themselves, may be observationally similar. However, given that there are differences in the motivations underlying vertical and naked horizontal agreements, and in the incentives problems that each type of agreement is seeking to resolve, their economic effects will likely vary as well.

Potential Procompetitive Benefits of No-Poach Clauses?

The second key issue in determining the applicable antitrust standard for assessing franchise no-poach provisions is whether the no-poach clause is reasonably necessary to the efficient operation of the franchise system, or whether such an agreement serves no other purpose than suppressing workers' wages. Franchisors argue that there are clear procompetitive effects from placing limits on soliciting and hiring of workers between franchisees. Franchisees make investments in training their employees, and this training can lead to higher quality products and services. Because training enhances the value of the brand, the franchisor has a strong interest in ensuring that franchisees provide the optimal level of training and investment in their personnel. No-poach clauses can incentivize these investments by increasing retention, preventing franchisees from free-riding on others' investments, and decreasing service disruptions. All of these benefits accrue to the franchise brand, and, in turn, to the individual franchisees, which may benefit employees in the long run. Thus, even if no-poach clauses can be shown to have a horizontal element, the potential for these procompetitive benefits can provide support for a rule of reason analysis.

Plaintiffs, however, question whether the no-poach clauses are ancillary to and reasonably necessary to the operation of the franchise system and to promoting inter-brand competition. They point to the existence of successful franchise systems without such clauses and some franchisors' own statements about the lack of enforcement of no-poach clauses as evidence that such agreements cannot be justified using the ancillary-restraint exception.

If the joint economic interests of the franchisor and the franchisees can be demonstrated and the potential for strong procompetitive benefits of no-poach clauses can be shown, the court may find sufficient support to analyze these agreements in a rule of reason framework.

In a rule of reason analysis, potential procompetitive benefits of franchise no-poach clauses must be weighed against potential anticompetitive harm of reduction in wages. The balance of these two effects will likely depend on the specific nature of the no-poach provision and the relevant labor market for the employees covered by the no-poach provision. Depending on the type of employee covered by the no-poach provision, there will likely be differences in the cost and the nature of the personnel investment, and the value of that investment inside and outside the specific franchise system. These differences will affect a franchisee's incentive to invest in its employees in the absence of a no-poach provision, as well as the extent to which market forces—for example, competition from other franchise systems and other types of jobs—will discipline any potential negative wage effects of such provisions.

Even when conducting the balancing exercise of weighing potential procompetitive benefits against their potential anticompetitive harm, some argue that labor market restraints are distinct from other restraints in the franchise system—for example, pricing restrictions. When a franchisor imposes pricing terms on its franchisees, the potential anticompetitive effect is felt in the downstream product market. But so is the procompetitive effect—the consumer benefits from the experience of uniform product pricing, quality, and service that can result from product pricing restrictions. However, the potential procompetitive effect of no-poach clauses may be more cognizable in the product market than in the labor market where the potential anticompetitive effect may be present. In the product market, consumers can benefit from greater incentive to provide the optimal level of training, which may lead to better customer services, higher quality products, and robust inter-brand competition. However, the no-poach clauses, by limiting a worker's mobility, may negatively affect his or her ability to negotiate for higher wages. Hence, the *per se* proponents argue that the consumer welfare standard does not (or ought not) recognize any procompetitive effects from franchise no-poach agreements.

II. Non-Compete Agreements

Another form of a labor-market restraint with a vertical element that has drawn increased scrutiny from antitrust enforcers in recent years has been the non-compete agreement. This is a restrictive covenant between an employer and an employee that restricts the employee, upon leaving the employer, from taking a job at a competing firm or starting a competing business. These agreements usually stipulate a specific length of time and the industry and/or geographic scope for the non-compete restriction. According to a recent study, roughly 20% of labor participants in the United States were subject to non-compete agreements in 2014.[17]

While non-compete agreements are legally enforceable in most states, an increasing number of states are adopting or considering rules that will place strict limits on their temporal, industry, and geographical scope and restrict their use with low-wage workers. Although non-compete agreements have rarely been the subject of antitrust litigation, some scholars argue that they may be seen to violate antitrust law if they are used to enhance or exploit a firm's market power.[18] Two key antitrust issues are relevant for the analysis of non-compete agreements.[19] The first is whether an agreement between employer and employee effectively restricts competition between horizontal competitors. The second is whether important procompetitive benefits can be derived from non-compete agreements.

[17] Evan Starr, J.J. Prescott, and Norman Bishara, *Non-competes in the U.S. Labor Force* 15 (Univ. of Mich. Law & Econ Research Paper No. 18-013, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2625714.

[18] Alan B. Krueger and Eric A. Posner, *A Proposal for Protecting Low-Income Workers from Monopsony and Collusion* 9 (2018), https://www.hamiltonproject.org/assets/files/protecting_low_income_workers_from_monopsony_collusion_krueger_posner_pp.pdf.

[19] Non-compete agreements are enforced in most state courts. There is an ongoing debate between the worker's freedom to contract against potential bargaining power imbalances and negative externalities. In this article, we focus on potential antitrust issues that may be associated with non-compete agreements.

Do Non-Compete Agreements Effectively Restrict Horizontal Competition?

The first issue requires an examination of the employee's likely options for employment and/or business ventures after the employee's departure. If in the absence of a non-compete agreement, the employee would have started a competing firm on her own, some might argue that the agreement could be viewed, in a sense, as a horizontal agreement among *future* competitors to limit the level of competition. In reality, however, not all non-compete agreements restrict employees' ability to start their own firms upon departure, and in many industries, departing employees do not pose a likely threat as new firm entrants.

Alternatively, some might argue that a non-compete agreement could be viewed be as a vertical agreement between a supplier (the employee) and a downstream producer (the employer). Viewed this way, the non-compete agreement might be characterized as a kind of exclusive supply agreement that forecloses competitors from accessing talent. The frequent use of such agreements could discourage competitors from entering the market because of the concern that they may be unable to hire a sufficient amount of quality labor. The wide use of non-compete agreements may make it difficult for current or prospective rival firms to successfully compete against a more established, larger firm. Whether and the extent to which these agreements have such effects is an empirical question, and will depend on industry and occupation characteristics and the size of the relevant labor pool.

To be sure, a non-compete agreement is different from many exclusive supply agreements. Consider the following typical Sherman Act Section 2 exclusive supply case. A large manufacturer of widgets, fearing the competition posed by a new entrant, requires that its supplier of rose petals (a necessary input into producing widgets) become an exclusive supplier. The supplier may be pressured into becoming an exclusive supplier, because if it does not agree, it may lose its most important customer. In this typical fact pattern, the exclusive supply agreement is contemporaneous to the restriction: the supplier is strong-armed into agreeing to supply rose petals to the incumbent, but not to the new entrant, and the impact on competition may be felt immediately.

A non-compete agreement, by contrast, is not a contemporaneous commitment to supply labor exclusively; it is sequential. In a non-compete agreement, the worker agrees to a *future* restraint. As long as the worker remains at Firm X, the agreement does not pose any restraint. It is only when the worker leaves Firm X that he or she will be unable to supply labor to Firm Y, but usually for a limited period of time.

The non-contemporaneous nature of the non-compete agreement, as well as limitations on the restrictions' applicable length of time, will likely lead to different impacts on competition and foreclosure effects, if any. However, to the extent that non-compete agreements effectively deter employees from quitting, they may pose some level of contemporaneous restraint on the supply of labor.

Potential Procompetitive Effects of Non-Compete Agreements?

The second issue—particularly relevant if non-compete agreements are to be viewed as vertical restraints—involves the assessment of potential procompetitive effects of such agreements. They have often been used by employers as a means of protecting their own investments in employees' human capital, and protecting their intangible assets, such as trade secrets. These investments may take the form of sharing confidential business information, providing access to customer lists, or training. In the absence of non-compete agreements, employers may be less likely to make such investments. That is, without contractual provisions restricting the free appropriation of such investments by the employee and competing firms upon that employee's departure, the employer may have less incentive to train workers and to invest in developing the careers of its employees. In other words, non-compete agreements can optimize employers' incentives to invest in their workers, which can lead to great labor demand and productivity, and in turn, higher wages.

However, skeptics argue that, in reality, the human capital investment and asset protection rationale for the enforceability of non-compete agreements are at best applicable to only a small portion of the workforce. First, to the extent that these agreements create additional incentives for investment in human capital and intangible assets, the benefits of these agreements may only be "marginal" to the incentives that already exist given the labor market frictions that "often prevent employees from switching jobs."[20] Second, some commentators point to the fact that employers provide general human capital training (i.e., training that would be valuable outside a specific firm) even in the absence of non-compete agreements.[21] To the extent that workers are aware of non-compete clauses in their employment contracts prior to starting their jobs, they may be able to negotiate for better contractual terms in exchange for the restraint on their mobility. However, the ability to negotiate over non-compete agreements is dependent on knowledge of their existence and the relative bargaining power of workers and employers.

Ultimately, the balance of the potential procompetitive and anticompetitive effects of non-compete agreements will depend on the nature and scope of the agreement and the type of the worker and industry.

III. Conclusion

Amidst growing concerns about increased industry concentration, wage stagnation, and rising inequality, the spotlight on labor-market restraints and the debate over how to analyze them continues to grow. While recent litigation and statements from enforcement agencies make clear that no-poach agreements between horizontal competitors for labor that are not ancillary or reasonably necessary to legitimate collaboration are *per se* illegal, there is ongoing and evolving debate over the appropriate treatment of labor-market restraints with vertical elements. Key issues in the debate center on whether the *prima facie* vertical nature of no-poach clauses in franchise contracts and the non-compete agreements reflect the reality of the relationships that exist between the parties to the agreement. They also center on the strength of cognizable procompetitive effects that can result from these restraints, and whether those effects can be realized in the same market in which potential anticompetitive effects are alleged.

20 Eric A. Posner, *The Antitrust Challenge to Covenants Not to Compete in Employment Contracts* 14 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3453433.

21 *Id.*

Competition and Consumer Privacy

by Joel Mitnick and Ngoc Pham Hulbig

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Introduction

Antitrust enforcers globally are concerned about whether large digital platforms have amassed and abused market power. The concerns are sometimes expressed in the context of traditional antitrust language, including whether certain mergers are anticompetitive or certain conduct is exclusionary or raises rivals costs. But increasingly, the enforcement community is asking whether data privacy is being compromised. Privacy concerns traditionally were the subject of consumer protection/privacy statutes, not competition statutes. The current focus raises the question of whether privacy is a proper subject of U.S. and international competition law.

A Debate Within The Agencies

There is increased discussion about privacy as a dimension of antitrust enforcement and interest in what tech companies are doing with the data they acquire. At the FTC, Commissioner Rebecca Slaughter posits that acquisitions by big tech platforms, *e.g.* – Google, Apple, Facebook, Amazon ("GAFA"), may reduce privacy protections offered by GAFA rivals and therefore may reduce competition to protect consumer data.[1] The DOJ signaled last year that the Antitrust Department will be "reviewing whether and how market-leading online platforms have achieved market power and are engaging in practices that have reduced competition, stifled innovation, *or otherwise harmed consumers*."[2] And last fall, New York Attorney General Letitia James announced a major multi-jurisdiction state AG task force investigating possible anticompetitive practices by Facebook, citing "concern[s] that Facebook may have put consumer data at risk."[3] The discussion is similarly robust in Europe, where agencies like Germany's Federal Cartel Office have taken action, suing Facebook for abuse of dominance, Europe's equivalent of Section 2 of the Sherman Act, for certain of Facebook's consumer targeting advertising practices.

FTC Commissioner Noah Phillips delivered a thoughtful speech before Stanford Law School's Center for Internet

[1] Rebecca Kelly Slaughter, Commissioner, Federal Trade Commission, Remarks at FTC Hearing #12: *The FTC's Approach to Consumer Privacy* (Apr. 10, 2019), https://www.ftc.gov/public-statements/2019/04/remarks-commissioner-rebecca-kelly-slaughter-ftc-hearing-12-ftcs-approach.

[2] *Justice Department Reviewing the Practices of Market-Leading Online Platforms*. Department of Justice (July 23, 2019) (emphasis added), https://www.justice.gov/opa/pr/justice-department-reviewing-practices-market-leading-online-platforms.

[3] Press Release, Letitia James, New York State Attorney General, *Attorney General James Gives Update On Facebook Antitrust Investigation*, (Oct. 22, 2019), https://ag.ny.gov/press-release/2019/attorney-general-james-gives-update-facebook-antitrust-investigation.

and Society in which he rejected calls for extending antitrust jurisprudence to reach privacy-related injuries.[4] Phillips shared, "[p]rivacy can be evaluated as a qualitative parameter of competition, like any number of non-price dimensions of output; but competition law is not designed to protect privacy. Put to the task, it will fail; and both competition and privacy will suffer."[5] Perhaps one reason why certain U.S. enforcers are reaching for antitrust tools to fix perceived privacy harms is that there *is* no omnibus federal consumer data privacy statute as exists in many other countries. California's recently enacted privacy statute may establish a national floor but falls short of national law. In the absence of federal legislation on privacy, enforcers and litigants may be left to force the round peg of privacy into the square hole of antitrust.[6]

Precedent

There is no modern case law squarely addressing the question of whether harm to privacy rights may be cognizable under the antitrust laws. However, there are some useful guideposts. In *FTC v. Raladam*,[7] the Supreme Court held that the FTC's jurisdiction over "unfair methods of competition" did not extend to cases alleging deception, reasoning that antitrust laws did not reach consumer protection injuries.[8] In response, Congress seven years later augmented the FTC's jurisdiction with the power to regulate "unfair or deceptive acts and practices."[9]

More recently, the Commission considered privacy implications explicitly when evaluating Google's 2007 proposed acquisition of DoubleClick, but did not decide to rule on that issue. The Commission stated, "[b]ecause the evidence did not support the theories of potential competitive harm, there was no basis on which to seek to impose conditions on this merger. We want to be clear, however, that we will closely watch these markets and, should Google engage in unlawful tying or other anticompetitive conduct, the Commission intends to act quickly."[10]

In a dissenting statement in Google/DoubleClick, Commissioner Pamela Jones Harbour noted, "[w]hile this transaction sparked great interest in privacy issues and created momentum for a meaningful discussion, it would be short-sighted to focus on the behavior of a single company (in a merger context) when the issue is relevant to so many other firms as well."[11] In considering theories that might make privacy "cognizable" under the antitrust laws, she went on to note, "[o]ne could argue, for example, that if network effects lead to a reduction in the number of search competitors, consumers will suffer from a diversity of choice among search engines, which will reduce the incentives of search firms to compete based on privacy protections or related non -price dimensions."[12]

Some Issues About The Nature Of Privacy In Competition

Too many policymaker speeches conflate "big data" with "data privacy." Big data is generally understood to be the accumulation of large storehouses of consumer or industry data. To the firm that accumulates it, the data is an asset. The bigger the data set, generally the more valuable the asset. By contrast, data privacy refers to the protections afforded to individuals and organizations that generate such data.

Data, like any other asset, may be wielded in a competitive or anticompetitive manner. Under various theories of Section 1 of the Sherman Act, *e.g.*- tying or boycott, or Section 2, *e.g.* –

4 Noah Joshua Phillips, Commissioner, Federal Trade Commission, Remarks at Stanford Law School's Center for Internet and Society: *Should We Block This Merger? Some Thoughts on Converging Antitrust and Privacy* (Jan. 30, 2020), https://www.ftc.gov/system/files/documents/public_statements/1565039/phillips_-_stanford_speech_10-30-20.pdf.

5 *Id.* at 3.

6 Joel Mitnick and Monica Martin, *The Competition-Privacy Collision*, Global Competition Review USA (Dec. 13, 2019), https://globalcompetitionreview.com/article/usa/1212095/the-competition-privacy-collision.

7 283 U.S. 643 (1931).

8 *Id.*

9 15 USC §45(a).

10 Statement of the Federal Trade Commission, In the matter of Google/DoubleClick, FTC File No. 071- 0170 (Dec. 20, 2007), https://www.ftc.gov/system/files/documents/ public_statements/418081/071220googledc-commstmt.pdf.

11 Dissenting Statement of Commissioner Pamela Jones Harbour, In the matter of Google/DoubleClick, FTC File No. 071-0170, (Dec. 20, 2007). https://www.ftc.gov/sites/default/files/documents/ public_statements/statement-matter-google/doubleclick/071220harbour_0.pdf.

12 *Id.* at 10, n. 25.

exclusionary conduct, or Section 7 of the Clayton Act, *e.g.* – elimination of nascent competition through merger, antitrust law is plainly equipped to address anticompetitive uses of or restrictions on data as an asset class. But, none of those abuses relate to privacy.

There is, however, a lively debate about whether companies today are actually offering privacy protections on their platforms as a dimension of competition and, if so, whether consumers actually value the privacy protections that are being offered.[13] Some enforcers, such as Commissioner Phillips, are skeptical that consumers even value privacy protections as a dimension of competition.[14] But, for example, if one of the GAFA platforms proposed an acquisition of a rival that distinguished itself by offering substantially greater privacy protections for its customers' data than does the GAFA platform, why shouldn't the potential loss of that privacy competition be a valid subject of inquiry under Section 7? Indeed, DOJ has indicated it is "especially vigilant" in reviewing platform mergers both for exclusionary effects on rivals and for the potential of extracting more consumer data from customers.[15] Similarly, if platform rivals entered into a conspiracy to end ruinous competition by adding expensive privacy technologies to their platforms, why shouldn't consumers be able to sue for the value of the lost privacy protections?[16] Moreover, how should courts balance pro-privacy actions by dominant platforms that restrict access by third-party competitors to its customers' data against the harm to competition posed by the lack of access?[17]

Conclusion

Despite a lively debate, the reach of antitrust law in the area of privacy remains unclear. Congressional action on privacy legislation would offer welcome clarity and relief. Meanwhile, jurisprudential hurdles, albeit possibly low ones, may have to be overcome before courts will accept the application of the Sherman and Clayton Acts to remedy privacy injuries.

[13] *See* Phillips, *supra* note 4, at 13.

[14] *Id.*

[15] Tony Romm, *DOJ issues new warning to big tech: Data and privacy could be competition concerns*, WASH. POST (Nov. 8, 2019), https://www.washingtonpost.com/technology/2019/11/08/ doj-issues-latest-warning-big-tech-data-privacy-could-be-competition-concerns/.

[16] Of course, developing an economic theory of how to quantify such harm is a topic for some other article.

[17] *See, e.g.,* Jack Karsten, *Pursuing a harms-based approach to privacy and antitrust regulation*, BROOKINGS TECHTANK (Mar. 27, 2019), https://www.brookings.edu/blog/techtank/2019/03/27/pursuing-a-harms-based-approach-to-privacy-and-antitrust-regulation/; Becky Chao, *The Role of Antitrust Law When Mergers Threaten Consumer Privacy*, NEW AMERICA WEEKLY (Feb. 28, 2019), https://www.newamerica.org/weekly/edition-238/antitrust-merger-consumers-privacy/.

Antitrust Authorities and the Standardization of Internet of Things: An Analysis of Possible Approaches under U.S & EU Antitrust Law

by Gabriel Araújo Souto

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I. Introduction

In a globalized economy, standards are more important than ever. Particularly in hi-tech markets, standards, when properly developed, play a positive role in promoting the efficient distribution of new technologies in a manner that is most beneficial to the consumer and the economy in general.[1] Nevertheless, the lack of interoperability[2] across Internet of Things (IoT) platforms results in fragmentation, higher development costs, greater risks for suppliers and users, and limits on the scope of market opportunities.[3] Therefore, investing in the development of a protocol or an architectural framework for IoT that is attractive for companies and industries to apply in their business can be very costly. Given the operational importance of IoT solutions to companies, they are expected to take a shared-risk approach, forming coalitions and joint-ventures while retaining control over their operations.[4]

Cooperation and coordination efforts can improve interoperability and increase the market acceptance of innovative solutions. By establishing standard-setting policies that are transparent and effective, these organizations enable competition and facilitate product innovation. Moreover, a plural engagement results in an easy process of standard adoption for companies to make. Multilateral and accessible Organizations, like International Telecommunication Union (ITU), could facilitate early-adoption of IoT, reduce the possibility of private litigation, and mitigate an eventual imposition of standards by a dominant company with an established market power.[5]

Companies compete in the market to set these standards, which can lead to standard wars.[6] The economic advantages of a settled technical standard for interoperability purposes are so large that competition between standards is not sustainable.[7] Even if a period of competition between standards could lead to the development of better standards, both the parallel experimentation with different standards and the uncertainty about the future standard could lead to wasteful investments and slow down the innovation on the market for complementary products and services, damaging the implementation of IoT products.[8]

1 *See* Carl Shapiro & Hal R. Varian, *Information Rules: A strategic guide to the network economy*, Harvard Business School Press 229-230 (1999) (explaining that standards generate greater value for users by promoting interoperability).

2 Interoperability means that heterogeneous devices and protocols need to be able to inter-work with each other. This is challenging due to a large number of different platforms used in IoT systems. *See* John Palfrey and Urs Gasser, *Interop: The Promise and Perils of Highly Interconnected Systems*, Jackson, TN: Basic Books 5 (2012) (stating that in information technology, interoperability refers to the ability to transfer and render useful data and other information across systems, applications and components).

3 IEEE IoT, *Towards a definition of the Internet of Things (IoT)*, IEEE Internet Initiative 1 34 (May 13, 2016), https://iot.ieee.org/images/files/pdf/IEEE_IoT_Towards_Definition_Internet_of_Things_Issue1_14MAY15.pdf

4 John Hagedoorn, *Understanding the rationale of strategic technology partnering-interorganizational modes of cooperation and sectoral differences*, 14 Strategic Management Journal 5 371–385 (1993).

5 *See* Shapiro & Varian, *supra* note 1, at 237 (stating that history proves that the establishment of a consensus policy on the adoption of a standard is critical to launching new technologies).

6 *See id.*, *supra* note 1, at 261 (defining standard wars as the struggle of two new incompatible technologies to become a de facto standard).

7 Wolfgang Kerber & Heike Schweitzer, *Interoperability in the Digital Economy*, 8 JIPITEC 43 (2017), https://www.jipitec.eu/issues/jipitec-8-1-2017/4531/JIPITEC_8_1_2017_Kerber_Schweitzer.pdf.

8 *Id.*, at 232 (stating that the extension of competition between standard technologies can result in incompatibilities and be blockaded by an owner of IPR that may delay the adoption and usefulness of it).

Considering those potential problems, firms may agree on a new single standard through negotiations moderated by standard-setting organizations (SSOs). SSOs can enforce continuous debates, improvements, unification, quick adoption, and openness of a standard-setting process.[9]

Therefore, the development of interoperability strategies needs open collaborations and open standards to facilitate interoperability in IoT and provide a path of coordinated technological evolution by a SSO.[10] For that reason, the choice of the best protocol to be standardized could be done by choosing the most efficient in a long-term analysis through IoT testing,[11] and after defining the best technology, the SSO must enforce a fair, reasonable and non-discriminatory (FRAND) commitment to license the IPR between all members. This would enable a shared and interoperable framework that is essential to an efficient implementation of the IoT technology in every market.

II. Analysis of IoT Standardization Under Competition Law

Antitrust authorities must be aware of standard-setting because legally a standard constitutes an agreement between companies, which raises traditional concerns regarding collusion.[12] Though a standardization agreement is not capable of producing restrictive effects on competition in the absence of a company's market power, certain behaviors of SSOs can directly lead to a restrictive effect on competition which can be identified as anti-competitive practices. For example, the inclusion of a company in a standard can change the market value of technology as the holder of an essential patent can acquire an incremental degree of market power which he would not possess in the absence of a standard.[13] This happens when a switch to a different standard produces significant costs and companies get locked into the standard previously set, developing a barrier to entry. As a result, potentially competing technologies are excluded from the market. To identify possible approaches for the IoT standardization, it is important to analyze the anticompetitive effects of standardization agreements with a focus on the United States (U.S.) and European Union (EU) jurisdictions, which will be divided into (A) barrier to entry; (B) refusal to deal and (C) exclusionary conduct.

A. Barrier to Entry

There are relevant legal frameworks set to prevent barriers to entry. For example, the European Commission (EC) Guidelines on horizontal cooperation agreements[14] point out that where participation in standard-setting is unrestricted; the procedure for adopting the standard is transparent; with no obligation to comply and accessible on FRAND terms will normally not restrict competition within the meaning of Article 101(1) of the Treaty on the Functioning of the European Union (TFEU). The Court of Justice of the European Union (CJEU) has confirmed that the EC is right to apply these assessment criteria if a standard restricts competition. For example, in *EMC Development AB v European Commission*,[15] EC ruled that standard-setting will normally not restrict competition if it guarantees openness, transparency, non-binding obligations to comply with the standard and accessibility with reasonable and non-discriminatory terms. Also, the Federal Trade Commission (FTC) has provided some guidance in evaluating the legality of standardization programs under the U.S. antitrust laws.[16] This guidance suggests that standards should be voluntary; groups should

[9] Joseph Farrell & Timothy Simcoe, *Four Paths to Compatibility*, The Oxford Handbook of the Digital Economy 41 (2012), www.oxfordhandbooks.com/view/10.1093/oxfordhb/9780195397840.001.0001/oxfordhb-9780195397840-e-2.

[10] *Id.,* at 238 (explaining that openness is a fundamental principle to approach consensus on the standard-setting process and to promote its credibility).

[11] *See* Benny Sand, *IoT Testing – The Big Challenge Why, What & How*, Qualitest (2018), https://www.qualitestgroup.com/white-papers/iot-testing-the-big-challenge/ (stating that the key to successful implementation of an IoT standard is the test of concurrent protocols that best support a chosen and established framework).

[12] *See* U.S. Dep't of Justice & Fed. Trade Comm'n, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* 33-56 (2007), https://www.ftc.gov/sites/default/files/documents/reports/antitrust-enforcement-and-intellectual-property-rights-promoting-innovation-and-competition-report.s.department-justice-and-federal-trade-commission/p040101promotinginnovationandcompetitionrpt0704.pdf (highlighting the key antitrust concerns raised by SSO participation and provides questions that a company should consider as it navigates through the standard-selection process).

[13] Ruben Schellingerhout, *Standard-setting from a competition law perspective*, 1 European Commission Competition Policy Newsletter 4 (2011), http://ec.europa.eu/competition/publications/cpn/2011_1_1_en.pdf.

[14] European Commission, *Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements*, Official Journal of the European Union (Jan. 14, 2011), https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52011XC0114(04)&from=EN.

[15] *EMC Development AB v European Commission*, 189 Judgment of the Fifth Chamber of General Court 203 (2010), http://curia.europa.eu/juris/liste.jsf?language=en&num=T-432/05.

[16] *See, e.g.*, U.S. Dep't of Justice & Federal Trade Comm'n, *Antitrust Guidelines for the Licensing of Intellectual Property* § 3.2 (1995), http://www.justice.gov/atr/public/guidelines/0558.htm (enforcing a regulatory approach on technology and innovation markets where IP licensing may affect competition).

not exclude competition and should be fully open to membership and transparent. Moreover, the Brazilian antitrust authority (CADE) presents an excellent guideline[17] about SSOs limit of performance to avoid any competition infringement by recommending the non-disclosure of sensitive data of competitors, the non-elaboration of tables, even if suggestive of prices and commercial conditions in which products and services will be provided, and the anonymization of competitor's data during the process of standard-setting.

The EC Guidelines provide a good legal framework reference by enforcing that there must be clarity concerning the possible new adopters of the standard. New adapters must be able to make an informed decision when endorsing the protocol. their Moreover, a system where potentially relevant Intellectual Property Rights (IPR) are disclosed up-front may increase the likelihood of effective access being granted to the standard, since it allows the participants to distinguish technologies covered by IPR and enables the participants to analyze potential effects on the final price of adoption on their products. Thus, the EC Guidelines recognize the potential benefits of *ex ante* disclosures as having the potential to generate strong pro-competitive benefits by allowing comparison on quality and price. This position is also enforced by the U.S. Department of Justice that recognizes *ex ante* IPR disclosure policies as compliant with the U.S. antitrust law framework.[18]

Therefore, in order to ensure effective access to the standard, the IPR policy enforced by SSOs must propose a FRAND commitment, that is, members of SSOs wishing to have their IPR included in the standard must provide an irrevocable commitment in writing to at least offer to license their essential IPR to all third parties on fair, reasonable and non-discriminatory terms. This type of commitment is designed to prevent IPR holders from creating barriers for a standard to be implemented. The IPR disclosure obligation is also a solution for patent ambush because it avoids the standard to be blocked at a later stage by an IPR holder that is unwilling to license on reasonable terms or not at all. For this reason, there is an important pro-competition rationale behind requiring the disclosure of patents and patent applications before a standard is set.[19]

B. Refusal to Deal

Regarding refusal to deal, particularly important is the distinction between horizontal and vertical interoperability. Horizontal interoperability denotes the interoperability of competing products, services or platforms while vertical interoperability refers to the interoperability of a product, service or platform with complementary products and services. Thus, the degree to which complementary products can be shared across different platforms, and complementary products of one platform can be accessed from rival platforms characterizes the horizontal openness of a platform.[20]

On the horizontal market, interoperability requirements can prevent market tipping, since network effects will no longer work in favor of the strongest player alone but will be market-wide.[21] Therefore, a refusal to interconnect with a horizontal competitor could qualify as an abuse of dominant position and consequently justify the imposition of interoperability duties as a competition law remedy as done in the *Aspen Skiing* case.[22] Under EU antitrust law, the

[17] CADE, *Guia para programas de compliance*, Gabinete da Presidência do Cade 34-36 (2016), www.cade.gov.br/acesso-a-informacao/publicacoes-institucionais/guias_do_Cade/guia-compliance-versao-oficial.pdf.

[18] *See* Hill B. Wellford, *Antitrust Issues in Standard Setting*, 2d Annual Seminar on IT Standardization and Intellectual Property 1 (Mar. 29, 2007), https://www.justice.gov/atr/speech/antitrust-issues-standard-setting (stating that IPR disclosure policies permit licensing of intellectual property before a standard is set that enables SDO members to consider patent licensing costs).

[19] Ruben Schellingerhout, *supra* note 13, at 7.

[20] Wolfgang Kerber & Heike Schweitzer, *supra* note 7, at 41.

[21] *Id.*, at 51.

[22] *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985).

refusal to interconnect horizontally has not yet been found to constitute an abuse. The fact that a dominant firm benefits from network effects does not qualify as an abuse of dominant position, nor does the risk of market tipping change this legal appraisal.

Thus, a dominant firm may have incentives to foreclose competition in adjacent markets by impeding interoperability with third party complementary products or services.[23] In order to protect competition and follow-on-innovation on such adjacent markets, mandating vertical interoperability may be economically justified by an analysis of essential facilities doctrine.[24] For example, a refusal to grant access to interface information has been qualified as an abuse of dominance in the *Microsoft* case where, according to the EC, Microsoft's refusal to disclose the relevant interface information to competitors constituted an abuse of its dominant position on the market for client PC operating systems.[25] However, a non-interoperability policy of a dominant company should not be considered abusive if effective methods are available to competitors to achieve interoperability.[26]

C. Exclusionary Conduct

Standards can be used as a tool to promote the exclusion of competitors from the market. One of the most prominent practices of exclusionary conduct in the standardization system is the patent ambush which is when a company first hides the fact that it holds essential IPR over the standard being developed and then starts claiming it once the standard has been agreed and other companies are locked into using it.

Consumer welfare and competitiveness are harmed by patent ambush, which also frustrates the aims of standard-setting organizations.[27] During the standard-setting process, multiple technologies may compete to be the chosen standard, however, as a result of the patent ambush, essential information of the technologies is intentionally hidden since disclosure of information only occurs once industry adhere to the standard, thereby increasing switching costs and providing the IPR owner to charge a monopoly price.

The EC's investigation in the *Rambus* case,[28] when the company asserted its patents against all standard-compliant memory chips, showed the potential restrictive effects on competition resulting from non-disclosure of relevant IPR. The EC took the view initially that Rambus could only claim royalties for the use of its patents from manufacturers complying with the industry standard at a certain level due to non-disclosure of the existence of patents and patent applications which were later claimed to be relevant to the adopted standard.[29]

In this sense, in 2003, the FTC alleged that the Union Oil Company of California (Unocal) monopolized the market for the manufacture of a specific type of gasoline and subverted California's regulatory standard-setting process by misrepresenting that certain research was non-proprietary while pursuing patents on the same technology.[30] Also, in U.S. *Rambus* case,[31] the FTC determined that Rambus had unlawfully obtained monopoly power through claiming patents adopted as the relevant standards by SSOs. However, the D.C. Circuit decided that the FTC failed to satisfy the exclusionary conduct element under Section 2 of the Sherman Act and therefore Rambus' development of market power was an insufficient evidence that the SSO would have

[23] John M. Newman, *Anticompetitive Product Design in the New Economy*, 39 Florida State University Law Review 1 (2012), https://ir.law.fsu.edu/cgi/viewcontent.cgi?article=1028&context=lr.

[24] Wolfgang Kerber & Heike Schweitzer, *supra* note 7, at 52.

[25] *Case COMP/C-3/37.792, Microsoft Corp., Comm'n Decision*, 2007 O.J. (L 32) 23 (Mar. 24, 2004), http://www.europa.eu.int/comm/competition/antitrust/cases/decisions/37792/en.pdf.

[26] Wolfgang Kerber & Heike Schweitzer, *supra* note 7, at 55.

[27] *Federal Trade Commission v. Qualcomm, Inc.*, No. 17-CV-00220-LHK (N.D. Cal. Nov. 06, 2018).

[28] *Case COMP/38.636, Rambus Comm'n Decision*, (summary at 2010 O.J. (C 30) 17), (Dec. 9, 2009), http://ec.europa.eu/competition/antitrust/cases/decisions/38636/en.pdf.

[29] Ruben Schellingerhout, *supra* note 13, at 4.

[30] *Union Oil Co. of Cal. (Unocal),* 140 F.T.C. 123 (2005).

[31] *Rambus*, Inc. v. F.T.C., 522 F.3d 456, 469 (D.C. Cir. 2008), cert. denied, 129 S. Ct. 1318 (2009).

selected an alternative standard or demanded a favorable licensing commitment.

Furthermore, cases like N-Data's[32] (about a violation of Section 5 of the FTC Act by failing to honor a licensing commitment when N-Data acquired patents from National Semiconductor that had been incorporated into a widely adopted standard), Dell's[33] (related to an infringement under Section 5 of the FTC Act when the company failed to disclose while participating in a standard-setting process and then attempted to enforce patent rights after the standard was adopted) and Qualcomm's[34] (about anticompetitive conducts when a false commitment relied by a SSO to license its technology on certain terms was made on a standard-setting process highlight the potential consequences of failing to disclose ownership of patents and/or pending patent applications when the SSO requires disclosure of such information) make a panorama that enforces a duty to search for patents that must be disclosed.

III. Conclusion

Whereas EU and U.S. antitrust laws and enforcers acknowledge that standard-setting is generally procompetitive,[35] standard organizations must cooperate to reduce the risk of fragmentation, duplication and conflicting standards in the IoT field.[36] Furthermore, the creation of guidelines by EU and U.S. antitrust authorities[37] that delimits an environment of legal certainty to companies to implement the standard-setting process compliant with their competition law becomes an indispensable effort for the development and prosperity of IoT standards.

32 *Negotiated Data Solutions LLC (N-Data),* No. C-4234 (F.T.C. Sept. 22, 2008).

33 *Dell Computer Corp.,* 121 F.T.C. 616 (1996).

34 *Qualcomm Inc. v. Broadcom Corp.,* 548 F.3d 1004, 1019-22 (Fed. Cir. 2008).

35 *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 500-01 (1988). *See also*, Standards Development Organization Advancement (SDO) Act of 2004, *Pub. L. No. 108-237*, 118 Stat. 661 (2004) (codified as amended at 15 U.S.C. §§ 4301–4305 (2006) (explaining that private standard-setting conduct shall not be deemed illegal *per se* and insulating such conduct from treble damages).

36 Urs Gasser, *Interoperability in the digital ecosystem*, Research Publication No. 2015-13 GSR discussion paper 13-15 (Jul. 6, 2015), http://ssrn.com/abstract=2639210.

37 *See* CADE*, supra* note 17, at 34-36 (providing recommendations for competitors and SSOs on standard-setting processes).

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