New York Law Journal

SERVING THE BENCH AND BAR SINCE 1888

WWW.NYLJ.COM

An ALM Publication

VOLUME 254—NO. 120

WEDNESDAY, DECEMBER 23, 2015

ANTITRUST

Expert Analysis

U.S. Brings Computerized Price-Fixing Charges

By **Elai Katz**

The U.S. Department of Justice brought criminal charges against online retailers for conspiring to fix prices by utilizing algorithm-based pricing software, among other means. The U.S. Court of Appeals for the Third Circuit ruled that a real estate owner and developer had standing to assert antitrust claims against a supermarket chain even though the developer was neither a competitor nor a customer of the defendant, because its injury from alleged interference with obtaining permits was inextricably intertwined with the harm to a rival supermarket. A district court set aside a jury verdict finding that a cable provider unlawfully tied its premium service to the rental of set-top boxes because those boxes were not available from any other source.

Other recent antitrust developments of note include the U.S. Court of Appeals for the Fifth Circuit's partial reversal of a jury verdict that a steel distribution boycott violated antitrust law and enforcement actions by U.S. antitrust agencies for failure to comply with premerger notification regulations.

Pricing Algorithm

A U.K.-based online retailer and an owner-director of the company were charged with fixing prices of posters sold over the Internet to U.S. customers, based on an alleged agreement to adopt specific computer pricing algorithms for the sale of certain posters, among other allegations. See DOJ Press Release, Dec. 4, 2015. The Department of Justice filed an indictment in the Northern District of California charging Trod Ltd (doing business as Buy 4 Less, Buy For Less and Buy-For-Less-Online) and the owner-director with fixing the prices of posters sold online through Amazon Marketplace from September 2013 through January 2014. According to the indictment, defendants and their co-conspirators used commercially available algorithm-based pricing software to price their products sold on Amazon. This software operates by collecting competitor pricing information for a specific product sold on Amazon and applies a pricing rule set by the seller.

The DOJ alleged that defendants and their co-conspirators agreed to adopt specific pricing rules for certain posters, with the goal of offering consumers the same price for the same poster. An alleged co-conspirator pleaded guilty to similar charges in this case in April 2015. The Assistant Attorney General in charge of antitrust, Bill Baer, stated, "We will not tolerate anticompetitive conduct, whether it occurs in a smoke-filled room or over the Internet using complex pricing algorithms."

> The Department of Justice filed an indictment charging Trod Ltd and the owner-director with fixing the prices of posters sold online.

Although the charges in the indictment include traditional indicia of price-fixing agreements, including allegations of conversations and communications to discuss and fix prices of agreed-upon posters, this matter raises questions about the impact of sophisticated online pricing software on competition. In the absence of an agreement to fix prices, algorithms that have the technological capacity to implement parallel pricing strategies with great speed and accuracy should fall outside the purview of §1 of the Sherman Act, like other parallel but independent conduct engaged in by human beings and addressed by the Supreme Court most recently in *Bell Atlantic v. Twombly*, 550 U.S. 544 (2007).

Antitrust Standing

Plaintiff Hanover Realty, a landowner and real estate developer, had contracted with the Wegmans supermarket chain to build a new full-service supermarket in Hanover, N.J. The contract provided that Hanover Realty would secure all of the necessary construction permits, and gave Wegmans the right to walk away from the deal should Hanover fail to obtain the permits within two years.

Defendant ShopRite is another supermarket chain with 26 locations in New Jersey, including a full-service supermarket two miles away from the proposed location of the new Wegmans. Hanover Realty asserted that ShopRite was the only full-service supermarket operating in the relevant area and that, once it learned about the proposal to open a Wegmans in town, ShopRite and its subsidiary filed numerous challenges to Hanover Realty's permit applications for the purpose of preventing the new Wegmans from opening.

Hanover Realty brought suit against ShopRite and its subsidiary, alleging that the defendants' conduct constituted attempted monopolization of the local "full-service supermarket" and the "supermarket rental space" markets in violation of §2 of the Sherman Act. The district court dismissed the claims on the grounds that Hanover Realty could not demonstrate antitrust injury and therefore did not have antitrust standing.

In most cases, those who are neither consumers nor competitors of the defendant in the restrained market have difficulty demonstrating that they suffered antitrust injury. Hanover Realty conceded that it was neither a consumer nor a competitor of ShopRite in the full-service supermarket market, as it is a landowner and lessor of property and not a food retailer. Instead, Hanover Realty argued that its injuries fell within the limited exception described by the Supreme Court in *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982), for persons whose injuries are "inextricably intertwined" with the harm caused by defendants.

The Third Circuit, reversing the district court, determined that the "inextricably intertwined" exception applied to Hanover Realty's injuries and reinstated one of its claims. *Hanover 3201 Realty v. Village Supermarkets*, 806 F.3d 162 (3d Cir. Nov. 12, 2015). The appellate court reasoned that the end goal of the alleged anticompetitive conduct was to injure Wegmans, a prospective competitor. Injuring Hanover Realty, through delay tactics and inflicting high costs, "was the very means by which Defendants could get to Wegmans;

ELAI KATZ *is a partner of Cahill Gordon & Reindel.* KOMAL PATEL, *an associate at the firm, assisted in the preparation of this article.*

Hanover Realty's injury was necessary to Defendants' plan." The Third Circuit explained that had Wegmans applied for the permits itself, the costs in question would have certainly qualified as antitrust injuries; thus it "should make no difference that the parties' lease shifted these costs to Hanover Realty."

The appellate panel did, however, affirm the dismissal of Hanover Realty's claim that defendants attempted to monopolize the market for supermarket rental space. Hanover did not rely on the "inextricably intertwined" theory for this claim and instead argued that it was a direct competitor of ShopRite's subsidiary, H&H. The panel affirmed the lower court's findings that H&H's sole purpose was to manage a single ShopRite store and it did not own any other properties, such that it could not conceivably compete with Hanover Realty for more lessees.

Cable Box Tying

A district court in Oklahoma set aside a $6.3 million jury verdict awarded to cable services subscribers alleging that Cox Communications illegally tied its premium cable services to rentals of its set-top boxes. *Healy v. Cox Communications*, No. 12-CV-0481 (W.D. Okla., Nov. 12, 2015). Tying arrangements may be illegal where the seller forecloses a substantial portion of the market by exploiting its power in one market to force buyers to accept another product that they might otherwise buy from a competing seller. In granting Cox's judgement as a matter of law, the court found that the subscribers failed to offer evidence from which a jury could reasonably infer that any other supplier offered to sell set-top boxes or that Cox had prevented manufacturers from entering the market.

The court stated that the plaintiffs' theories as to how Cox prevented other manufacturers from entering the market lacked evidentiary support and required the jury to make impermissible leaps in logic. While the subscribers demonstrated that at least one manufacturer expressed a desire to enter the market, there was no evidence that Cox prevented or blocked that manufacturer from doing so. Similarly, evidence that Best Buy declined to support a third party set-top box due to its perception that cable companies would not support the product did not establish that Cox foreclosed competition.

The court noted that the subscribers' other theory, that Cox manufactured an indemnification issue to prevent Tivo from entering the market, "invites unsupported speculation" and was similarly insufficient to establish that Cox's tying arrangement foreclosed competition. For similar reasons, the court also found insufficient evidence to establish the injury element of the claim, which requires that plaintiffs suffer harm from a competition-reducing aspect of the tying arrangement.

Group Boycott

In another case involving the appeal of a jury verdict, the Fifth Circuit ruled that there was insufficient evidence of one steel manufacturer's participation in a conspiracy by steel distributors to boycott a new distributor formed by former employees. *MM Steel v. JSW Steel (USA) and Nucor Corp.*, No. 14-20267 (5th Cir. Nov. 25, 2015). The former employees alleged that as soon as they established their new steel distribution business, the incumbent distributors agreed to threaten steel manufacturers not to sell to the new firm.

The appellate court examined whether there was substantial evidence for the jury to conclude that two manufacturers joined the distributors' conspiracy to refuse to deal with the new firm. Noting that only a concerted refusal to deal is illegal, the Fifth Circuit ruled that one manufacturer decided independently not to deal with the new firm out of loyalty to its longstanding distributor, not because of the group boycott, without knowledge of any threats and before the distributors allegedly agreed to form a boycott. As to the other manufacturer, the appellate court stated that a reasonable juror could have concluded that its refusal to deal was a response to threats from distributors.

A district court in Oklahoma set aside a $6.3 million jury verdict awarded to cable services subscribers alleging that Cox Communications illegally tied its premium cable services to rentals of its set-top boxes.

Premerger Notification

The Federal Trade Commission (FTC) announced two enforcement actions involving interpretation of investment-related exemptions to premerger notification requirements. The Hart-Scott-Rodino Act (HSR Act) requires those contemplating mergers or acquisitions of voting securities or assets that meet statutory thresholds to notify the antitrust agencies and observe a waiting period before completing those transactions.

The HSR rules apply not only to mergers and acquisitions of control but also to acquisitions of minority positions valued at or above $76.3 million (the current threshold, adjusted annually). The rules exempt minority acquisitions resulting in the buyer holding not more than 10 percent of outstanding voting securities if they are made "solely for the purpose of investment."

In one matter, a complaint filed by the FTC and the Department of Justice alleged that Third Point LLC and affiliated hedge funds failed to make an HSR filing and observe the waiting period before acquiring voting securities in Yahoo! Inc. in 2011. The FTC asserted that Third Point engaged in activities that reflected an intent to acquire stock not solely for the purpose of passive investment but rather to participate in the formulation, determination or direction of the basic business decisions of Yahoo!, including communicating with potential candidates for Yahoo!'s board of directors and taking steps to assemble an alternate slate of directors. See *United States v. Third Point Offshore Fund*, 15-cv-1366 (D.D.C. Aug. 24, 2015).

In another HSR enforcement action, the FTC and DOJ asserted that Jeffries, LLC, and its parent Leucadia National Corporation, improperly relied on the institutional investor exemption when they failed to make an HSR filing before acquiring approximately 13.5 percent of the outstanding voting securities of KCG Holdings. The institutional investor exemption provides that certain institutional investors, including broker-dealers, may acquire up to 15 percent of an issuer without making a filing as long as the acquisition is solely for the purpose of investment. However, the exemption does not apply when an institutional investor acquires shares of another institutional investor of the same type. The antitrust agencies alleged that the institutional investor exemption did not apply to the acquisition because both Jeffries and KCG were broker-dealers within the meaning of the HSR rules. *United States v. Leucadia National Corp.*, 15-cv-1547 (D.D.C. Sept. 22, 2015).

The FTC majority statement in the Third Point matter emphasized that HSR violations do not depend on the likelihood of competitive harms resulting from the acquisition, noting that the HSR Act is procedural and that the investment-only exemption is narrow. In a lengthy dissent, Commissioners Joshua D. Wright (who has since left the commission) and Maureen K. Ohlhausen suggested that the antitrust agencies revisit the parameters of the investment-only exemption, including the possibility of exempting all acquisition of less than 10 percent, because those transactions are unlikely to raise competitive concerns and the agencies should avoid chilling valuable shareholder advocacy.

As Commissioners Wright and Ohlhausen noted, one of the principal concerns motivating the passage of the HSR Act (and other premerger notification laws)—providing the antitrust agencies an opportunity to review a transaction before it is too late to "unscramble the eggs"—is absent in acquisitions of 10 percent or less. Post-closing remedies should be effective in virtually any case where antitrust agencies might determine that a minority acquisition of up to 10 percent (or even 15 percent) raises substantial competitive concerns. At the same time, a clear bright-line rule would substantially reduce costs associated with evaluating and complying with HSR obligations.