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ANTITRUST

Expert Analysis

FTC Wins Merger Challenge In District Court

By **Elai Katz**

The proposed combination of two of the three major providers of estimation tools for the automotive repair and insurance industry was blocked by a district court after it ruled that the Federal Trade Commission (FTC) raised questions "so serious, substantial, difficult and doubtful" to warrant an administrative trial on the legality of the merger. The U.S. Court of Appeals for the Ninth Circuit decided that a lower court should not have dismissed claims that numerous bilateral exchange agreements between California oil companies unlawfully restrained trade because the agreements' effects on competition should have been examined in the aggregate rather than individually.

Other recent antitrust developments of note included a ruling by the U.S. Court of Appeals for the Fourth Circuit that resale price maintenance agreements between pesticide makers and their agents did not constitute concerted action for purposes of a Sherman Act §1 claim.

Acquisitions

A district court granted the FTC's request to preliminarily enjoin the closing of the proposed merger of two providers of software and database systems used by insurers and automotive repair shops to estimate repair or replacement costs for vehicles damaged in accidents. The court issued a thorough and instructive opinion after holding nine days of evidentiary hearings and legal argument on the FTC's motion.

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Although the preliminary injunction was entered merely to maintain the premerger status quo pending an administrative trial before an FTC judge, the two firms announced that they would abandon the merger, reportedly because they could not depend on the continued availability of financing for the acquisition throughout a lengthy administrative trial.

> The district court observed that it would take a new entrant several years and millions of dollars to develop and maintain a competitive database of parts and labor and a comparable software platform.

Preliminary Injunction Standard: The district court stated that under §13(b) of the FTC Act, by which Congress meant to make injunctive relief "broadly available" to the commission, the FTC need only show that there is a "reasonable probability" that the acquisition may substantially lessen competition to get an injunction. The court observed that under §13(b), showing a likelihood of success on the merits requires less than in other preliminary injunction cases, but added that the court may not simply "rubber stamp" an injunction for the FTC.

Relevant Markets and Concentration. The court accepted the FTC's claim that the combination will leave only two major players in two relevant markets: the market for the sale of software and database systems used to estimate the cost of repairing a damaged vehicle (Estimatics) and the market for systems used to determine the replacement value of vehicles in the event of total loss (total loss valuation or TLV). The court rejected the merging firms' argument that TLV systems competed with periodically updated books and other publications, such as the "Kelley Blue Book," that provide reports on the value of used vehicles, noting that most insurance companies did not consider the books to be adequate substitutes for TLV systems, which provide more detail, are based on a much broader set of data and are priced without regard to book prices. The court also discounted the competitive impact of insurers deploying their own TLV solutions, noting that these accounted for a small portion of the market.

The district court stated that the merged firm would have market shares of around 70 percent in Estimatics and 65 percent in TLV products. Such high post-merger concentration gives rise to a presumption that the merger would lessen competition, it said, but it admonished that the government's assertion of a three to two combination or a merger to "duopoly" does not settle the question. Instead, showing such a prima facie case using market concentration statistics shifts the burden to the defendants to show that the statistics are not accurate indicators of the merger's likely effect on competition or to demonstrate that procompetitive efficiencies outweigh the anticompetitive effects.

Barriers to Entry: The court rejected the merging firms' claims that the market would lack significant barriers to entry after the merger. It noted that the only recent entrants still in the market held very small shares and competed in the low end of the market. The district court observed that it would take a new entrant several years and millions of dollars to develop and maintain a competitive database of parts and labor and a comparable software platform. In addition, the court stated that the costs of converting to a new system as well as repair facilities' inclination to use the same system used by large insurance companies created strong disincentives to switching and noted that incumbents had won the vast majority of bids for long-term contracts.

The district court added that the merging parties' remedial proposals—to enable a small competitor to grow (by removing contractual restrictions and extending a license to its database) and to release exclusive rights to a third-party database—would not make entry sufficiently timely or effective.

Competitive Effects. The district court then turned to analyzing the proposed combination's likely effects on competition under coordinated effects and unilateral effects theories. It rejected the FTC's arguments that the merger was likely to lead to unilateral effects and stated that the FTC did not provide evidence showing that customers considered the remaining rival in the market a "distant third option" such that the merged firm would have the ability to raise prices without losing too many sales to a rival.

On coordinated effects, the court agreed with the defendants' argument that tacit coordination among the remaining firms was less likely in this industry because the products are differentiated, often bundled in customized packages, and mostly sold through long-term, high-value contracts with sophisticated buyers where pricing is largely not transparent. On the other hand, the court stated that these markets are mature and stable with high switching costs, and thus possibly conducive to tacit coordination in the form of customer allocation or market stabilization, even if coordination on pricing is less likely.

The court concluded that it need not ultimately decide whether the defendants or the FTC had the better argument on coordinated effects because, in the D.C. Circuit, the FTC is merely required to raise questions that are so "serious, substantial, difficult and doubtful" that they are "fair ground for thorough investigation, study, deliberation and determination by the FTC."

***FTC v. CCC Holdings Inc.,* 2009-1 CCH Trade Cases ¶76,544 (D.D.C.)**

Comment: Although the procedural posture of the merger challenge decision reported immediately above was limited to a determination of whether the closing of the proposed acquisition should be enjoined to enable the FTC to conduct an administrative trial on the merits, in fact, as is often the case in such cases, the injunction led to abandonment of the transaction. In light of these business realities, the relatively lenient burden placed upon the FTC to obtain a preliminary injunction in some courts takes on heightened significance in close cases.

The Ninth Circuit majority in 'Gilley' noted that the complaint alleged that the existence of the exchange agreements enabled a given supplier to keep gasoline out of the spot market and away from unbranded marketers with the overall effect of raising prices.

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The FTC announced the settlement of charges that the combination of two suppliers of specialty chemicals and pigments would lessen competition in violation of §7 of the Clayton Act. The commission asserted that two high performance pigments—bismuth vanadate (brilliant yellow) and indanthrone blue—constituted separate relevant markets in which the merged firm would hold shares of more than 50 percent. The FTC stated that buyers of each of these pigments could not turn to substitutes even if faced with a significant price increase because no other pigment offered the same combination of unique color and durability.

The European Commission approved the merger subject to divestitures of certain specialty chemical products.

***BASF SE,* FTC 081 0265 (April 2, 2009), available at www.ftc.gov; Mergers: Commission approves acquisition of Ciba by BASF, subject to conditions, IP/09/396 (Mar. 12, 2009), available at ec.europa.eu/competition**

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The Irish High Court vacated a decision of the Competition Authority prohibiting the merger of two food companies. The court stated that despite allegations of post-merger market shares of around 50 percent in the rashers (uncooked bacon), non-poultry cooked meats, and processed cheese markets, the retailers' countervailing buyer power would discipline price increases and should have been given more weight by the authority. The Competition Authority announced that it would appeal to the Supreme Court.

***"Competition Authority appeals to the Supreme Court on Kerry Foods decision,"* (April 7, 2009), available at www.tca.ie**

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Restraint of Trade

A wholesale purchaser of gasoline alleged that major California refiners and distributors restrained trade in violation of §1 of the Sherman Act by entering into 44 bilateral exchange agreements, which allowed the oil companies to trade product to compensate for temporary or local supply shortages. A district court noted that a prior ruling precluded the plaintiffs from asserting a broad conspiracy to limit the supply and raise the price of gasoline and dismissed the complaint for failing to allege that the exchange agreements, when considered individually, had the requisite anticompetitive effects to state a claim.

The Ninth Circuit reversed in a split decision and stated that the lower court erred by not considering the cumulative effects of the exchange agreements.

The Ninth Circuit majority noted that the complaint alleged that the existence of the exchange agreements enabled a given supplier to keep gasoline out of the spot market and away from unbranded marketers with the overall effect of raising prices. The appellate court rejected the defendants' argument that plaintiffs' economic theory was unsound and stated that such analysis was not appropriate at the motion to dismiss stage notwithstanding the Supreme Court's 2007 *Twombly* decision.

The dissent read the complaint to assert that the bilateral agreements made it easier for the gasoline suppliers to coordinate their activity but did not in themselves have an anticompetitive effect.

***Gilley v. Atlantic Richfield Co.,* No. 06-56059, 2009 U.S. App. LEXIS 7161 (April 3, 2009)**

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Resale Price Maintenance

Pest control service providers alleged that pesticide manufacturers engaged in vertical price fixing or resale price maintenance in violation of §1 of the Sherman Act by agreeing with their distributors to set minimum resale prices for termiticide products. The Fourth Circuit affirmed the grant of summary judgment for defendants on the grounds that the distributors acted as the manufacturers' agents. The appellate court relied on the U.S. Supreme Court's 1926 *General Electric* decision holding that a manufacturer may lawfully set minimum prices at which its genuine agents may resell its products and rejected the plaintiffs' argument that this rule was implicitly overruled by the 2007 *Leegin* opinion, where the Court decided that resale price maintenance agreements were no longer unlawful per se.

The Fourth Circuit explained that the existence of a bona fide principal-agent relationship precludes assertion of an antitrust agreement, the first element of any restraint of trade claim under §1 of the Sherman Act. The court noted that the pesticide makers retained title as well as other indicia of ownership in the termiticide products, such as bearing the risk of loss. The appellate panel observed that absent the agency exception, home sellers could not tell a real estate agent the price at which they wanted to sell their home without violating the Sherman Act.

***Valuepest.com of Charlotte, Inc. v. Bayer Corp.,* 2009-1 CCH Trade Cases ¶76,547**

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Relevant Market

A provider of immigration services alleged that a rival attempted to monopolize the market by hiring away one of the plaintiff's key employees. A district court dismissed the claims on summary judgment and stated that the plaintiff failed to present evidence in support of the relevant submarket it sought to define. The court rejected the proposed relevant market—business-related immigration services provided by single-source providers to larger multinational corporations—and noted that the plaintiff did not bring forth any evidence showing the extent to which customers might turn to providers of limited immigration services if one-stop global immigration services providers were to raise their prices significantly.

Turning to the broader market asserted by plaintiff—immigration services—the court stated that the plaintiff offered no evidence that the defendants possessed monopoly power while the defendants identified many competitors in the provision of immigration services to large corporations.

The court also denied the plaintiff's request for discovery under Federal Rule of Civil Procedure 56(f) and observed that, having refused to reveal evidence it should have in its possession regarding the market in which it operated, the plaintiff could not insist that its competitor disclose its own competitively sensitive information. The court noted that, in some circumstances, summary judgment may be granted prior to discovery.

***Emigra Group LLC v. Fragomen, Del Rey, Bernsen & Loewy, LLP,* 07 Civ. 10688, 2009 U.S. Dist. LEXIS 27568 (S.D.N.Y. March 31, 2009)**

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Abuse of Dominance

The European Court of Justice affirmed the European Commission's decision that an Internet service provider abused its dominant position in the French market for residential high-speed Internet access by charging predatory prices as part of a strategy to "pre-empt" the market and restrict entry by competing providers. The court stated that under European Community law, the commission was not required to prove that the defendant had a realistic chance of recouping its losses for charging below-cost prices when the commission has presented evidence of pricing below average total costs and an intention to eliminate competition.

***France Télécom SA v. Commission,* C-202/07 (April 2, 2009), available at curia.europa.eu**

Comment: Unlike the law in Europe, predation claims in the U.S. require proof of likelihood of recoupment of the dominant firm's investment in below-cost prices, as the U.S. Supreme Court ruled in the 1993 *Brooke Group* decision, and reaffirmed in the 2007 *Weyerhaeuser* opinion.