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ANTITRUST

Expert Analysis

Prohibitions on Paying College Athletes For Use of Images in Video Games

By **Elai Katz**

The U.S. Court of Appeals for the Ninth Circuit decided that rules prohibiting student-athletes from being paid for the use of their names, images and likenesses in video games did not violate antitrust law because the amateur nature of collegiate sports increases their appeal to consumers, but schools must be permitted to provide scholarships to student athletes up to the full cost of attendance. A district court ruled that patent infringement settlement agreements between a brand-name drug-maker and generic rivals were not anticompetitive without a large unjustified reverse payment.

Another district court rejected the Federal Trade Commission's challenge to a proposed combination of a domestic medical equipment sterilization company with a foreign sterilization company because the FTC failed to show that absent the merger, the foreign firm was likely to enter the U.S. market.

Other recent antitrust developments of note include the Department of Justice's decision not to challenge a merger of leading online travel booking firms and the department's continued prosecutions of auto parts cartels.

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

College Sports

The Ninth Circuit ruled that the National Collegiate Athletic Association (NCAA) may prohibit compensating student-athletes for use of their names, images, and likenesses because amateurism in college sports had concrete pro-competitive effects by increasing their appeal to consumers. The district court's solution, allowing for relatively small deferred payments to students, was not as effective an alternative to accomplish that goal and was vacated by the Ninth Circuit. *O'Bannon v. NCAA*, 2015 WL 5712106, Nos. 14-16601, 17068 (Sept. 30, 2015).

This case was brought by a group of current and former college student-athletes challenging the NCAA's rules barring students from receiving a share of the revenue generated by the sale of licenses to use their names, images, and likenesses in video games and game telecasts. In the absence of the NCAA rules, the student-athletes claimed, schools would compete to offer recruits a share of that licensing revenue.

The district court decided that the NCAA's rule violated §1 of the Sherman Act, and enjoined the NCAA from prohibiting such payments. The district court's order effectively allowed schools to give student-athletes full scholarships and deferred compensation but permitted the NCAA to cap deferred-compensation payments at $5,000 per year per athlete. The NCAA appealed. In a 2-1 decision, the Ninth Circuit vacated the latter part of the district court's ruling, allowing the NCAA to ban these payments in their entirety.

As an initial matter, the Ninth Circuit rejected the NCAA's arguments that its rules are exempt from antitrust scrutiny. The appellate court observed that Supreme Court

precedent does not hold that amateurism rules are valid as a matter of law and instead supports the application of rule of reason analysis to NCAA rules. The court affirmed the lower court's finding that the student-plaintiffs met their initial burden under the rule of reason of showing that the NCAA's compensation rules had a significant anticompetitive effect on the college education market, and that the NCAA demonstrated in response that the compensation rules served the procompetitive purposes of integrating academics with athletics and preserving amateurism. The amateur nature of collegiate sports was shown to increase their appeal and drive consumers' demand.

The appellate panel explained that under the rule of reason, a restraint with procompetitive justifications is invalid only if a substantially less restrictive alternative is "virtually as effective" in serving the procompetitive purpose. The court agreed with the first alternative identified by the district court, which required the NCAA to allow schools to grant players scholarships for attendance-related costs such as non-required books, supplies and transportation. Previous scholarships were capped at required costs like tuition and board.

The court found clearly erroneous the district court's second remedy, which permitted deferred payments up to $5,000 per year for the use of an athlete's name, image, and likeness. "Not paying student-athletes is precisely what makes them amateurs" and therefore the payment of even small sums cannot be as effective in preserving amateurism. Most of the evidence in the record compared permitting smaller payments to larger payments. However, this evidence answers the wrong question. The proper inquiry is whether making small payments to student-athletes will be as effective in preserving amateurism and consumer demand as not paying them at all. Plaintiffs had not met their burden.

The majority reasoned that the difference between payments untethered to educational expenses and non-payment "is a quantum leap" and, once the line is crossed, there is "no basis for returning to a rule of amateurism and no defined stopping point." In contrast, the dissent argued that the majority improperly dismissed testimony establishing that small amounts of compensation would not significantly impact consumer demand in college sports, and that this evidence substantially supported the district court's decision to permit compensation up to $5,000.

A district court rejected the FTC's challenge to a proposed combination of a domestic medical equipment sterilization company with a foreign sterilization company.

Patent Settlements

Employee health benefit plans and other indirect purchasers of diabetes drugs sold under the brand name Actos brought suit alleging that settlement agreements resolving patent infringement disputes between the branded drug-maker, Takeda, and several generic drug companies, violated antitrust law. The plaintiffs alleged that generic entry should have occurred in January 2011, when the patent for the active ingredient in Actos expired. Instead, agreements settling lawsuits involving two other patents (which claimed methods of using Actos and were set to expire in 2016) did not provide for the entry of generic competition until August 2012 and, according to the complaint, delayed the availability of lower prices.

The district court dismissed the complaint for failure to articulate cognizable anticompetitive effects. *In re Actos End Payor Antitrust Litigation*, 2015 WL 5610752, No. 13-CV-9244 (RA) (S.D.N.Y. Sept. 22, 2015). The court's decision required a discerning reading of *FTC v. Actavis*, 133 S.Ct. 2223 (2013), where the Supreme Court ruled that settlement agreements between brand-name and generic drug-makers may violate antitrust law when the branded company (the patent holder) pays the generic (the alleged infringer) an "unexplained large reverse payment" to resolve the dispute, suggesting that the patent holder has serious doubts about the patent's survival.

The district court concluded that a patent settlement providing for an early generic entry date, without more, does not trigger antitrust scrutiny under *Actavis*. The court focused its inquiry on the competitive effects of the settlements, finding that the "acceleration clauses," which permitted prompt entry in

case any other generic comes to market before the agreed upon entry date, increased competition because more generics would be on the market if those clauses were triggered. The court also noted that the FTC did not challenge the settlements.

The court observed that while some settlements with non-cash terms may trigger antitrust scrutiny, such concerns are not present in the settlement agreements at issue in this case, where the key terms included generic entry before patent expiration and accelerated entry in the event another generic enters sooner. The court noted that not all settlements of patent infringement suits are illegal and that permitting these claims to proceed would have expanded the scope of *Actavis* and needlessly restricted future patent settlements.

This opinion should prove instructive not only to parties litigating "reverse payment" cases, but also to companies seeking to settle patent disputes without running afoul of antitrust law.

Sterilization Companies

The FTC sought a preliminary injunction in district court in Ohio to block the merger of Steris Corporation and Synergy Health PLC, the second and third largest medical equipment sterilization companies in the world, under the theory that the firms would have become competitors absent the merger. Steris is one of two domestic providers of gamma sterilization services, the only sterilization method currently available in the United States that is effective on high-density, high-volume equipment.

X-ray sterilization is a competitive alternative to gamma sterilization, but the method is currently not available in the United States. Synergy operates the world's only commercial X-ray sterilization facility in Switzerland. The FTC contended that Synergy was planning to introduce X-ray sterilization into the U.S. market but abandoned its efforts after the merger announcement to avoid competing with Steris's gamma facilities.

The "actual potential entrant" doctrine advanced by the FTC seeks to prevent future lessening of competition when a potential entrant (here, Synergy) merges with a firm already competing in the market (i.e., Steris). Under this doctrine, the acquisition of an "actual potential entrant" violates Section 7 of the Clayton Act if (1) the relevant market is highly concentrated; (2) the competitor "probably" would have entered the market, (3) its entry would have had pro-competitive effects, and (4) there are few other firms that can enter effectively.

> The Justice Department decided not to challenge Expedia's proposed acquisition of Orbitz despite concerns about the merger of two of the top three online travel booking providers, because the merger was not likely to substantially lessen competition.

The court stated that the FTC did not meet its burden to demonstrate that, absent the merger, "Synergy probably would have entered the U.S. contract sterilization market by building one or more x-ray facilities within a reasonable period of time." The court also noted that the "actual potential entrant" doctrine has been disfavored by the Supreme Court. *FTC v. Steris Corp.*, 2015 WL 5657294, No. 15 CV 1080 (N.D. Ohio, Sept. 24, 2015).

Synergy began developing a plan to enter the U.S. X-ray sterilization market in April 2013. To justify the substantial costs and risks of this plan, the board would require significant revenue commitments from customers. However, according to the court, the evidence showed that not a single customer was willing to provide such a commitment. Customers stated that there was no significant benefit to X-ray sterilization that would justify the substantial transition costs and expressed concern that should one of Synergy's facilities experience a problem there would be no readily available domestic alternative.

The court also noted that after inputting more accurate figures, the business model reflected a risky investment with low returns and produced metrics that were unlikely to obtain board approval. The court determined that Synergy's board, which had exclusive authority to approve large capital expenditures, would not have approved the plan to move forward with the U.S. X-ray project and the project would have ended regardless of the proposed merger.

The court found the timing of Synergy's decision to be highly persuasive. Synergy continued to work on

its plan for four months after the October 2014 merger announcement. The court observed that such efforts were "not a sham to convince the FTC that Synergy wanted to enter the market" but instead demonstrated legitimate efforts by Synergy employees who wanted the project to succeed. Further, Synergy had publicly disclosed plans to build two X-ray facilities shortly after the merger announcement, demonstrating that it did not view the proposed merger as an impediment to its plan.

The court reasoned that if the proposed merger was the reason Synergy abandoned its plans to enter the U.S. market, Synergy would have stopped working on the project when it entered merger negotiations or immediately after the deal was announced rather than in February 2015. In addition, Synergy would not have cancelled the project right after the FTC expressed concerns over the merger, "as Synergy had to know that doing so would only have solidified the FTC's position."

The court determined that the failure to obtain customer commitments and the inability to lower capital costs were detrimental to Synergy's plans and the most significant reasons for terminating its project. Absent the merger, these obstacles would still prevent Synergy from entering the U.S. market. The court concluded that the proposed merger had "no effect whatsoever" on Synergy's plans. In early October the FTC stated it would not appeal the district court's decision and agreed to withdraw the matter from administrative adjudication.

Even though the FTC's challenge was unsuccessful in this case, practitioners should consider potential competition issues when evaluating antitrust risk in mergers.

Online Travel Merger

The Justice Department decided not to challenge Expedia's proposed acquisition of Orbitz despite concerns about the merger of two of the top three online travel booking providers, because the merger was not likely to substantially lessen competition. (See DOJ Press Release, September 16, 2015.) Since Expedia had purchased another major player in the industry, Travelocity, just three weeks prior to announcing the Orbitz deal, the Justice Department investigated concerns that the merger would result in only two competitors, Expedia and Priceline, controlling 95 percent of the online travel booking market.

After a six month investigation, the Justice Department found no evidence that the merger is likely to result in higher charges for consumers or the companies that list their services with online travel websites. The investigation found that the commissions Expedia charges to airline, car rental companies and hotels are not likely to increase post-merger because many companies either do not list with Orbitz or receive only a small source of bookings from Orbitz listings and, as a result, Orbitz has not had significant impact on Expedia's commission charges in recent years. Additionally, the Justice Department observed that the online travel booking market is "rapidly evolving" and introducing new participants. Notably, both Google and TripAdvisor had introduced new online booking services within the past 18 months.

Auto Parts Conspiracy

In the latest charges arising from allegations of widespread bid rigging in a number of auto parts markets, three Japanese executives were indicted for conspiring to rig bids and fix the prices of automotive body sealing products sold to auto manufacturers. (See DOJ Press Release, October 8, 2015.) Automotive body sealing products keep out rain, wind and noises and include trunk lids and door-side weather-stripping among other products.

The Department of Justice stated that the price-fixed products were sold to Japan-based auto makers for installation in vehicles manufactured and sold in the United States. According to the charges, the three executives instructed their subordinates to communicate with those at other companies to allocate sales, rig bids and fix prices of body sealing products. The indictment also alleges that two of the executives encouraged employees to destroy evidence of the conspiracy. Thus far, 58 individuals and 37 companies have been charged with participating in various auto parts conspiracies and have agreed to pay more than $2.6 billion in criminal fines.

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