Winter 2008

E&I UPDATE

A publication of the Exemptions & Immunities Commitee of the Section of Antitrust Law, American Bar Association

IN THIS ISSUE

Message from the Editor 1

Articles

Scheme Liability Revisited: Recovering Antitrust Damages Resulting from Meritorious Patent Litigation 4
By Peter A. Barile III

Railroad Antitrust Enforcement Act Reported out of Senate Judiciary Committee 7
By M. Howard Morse

Community Pharmacy Fairness Act Reported out of House Judiciary Committee 7
By Christopher Durocher

Special Feature

E&I Case Law Update 16

MESSAGE FROM THE EDITOR

To paraphrase Mark Twain, the death of antitrust exemptions and immunities has been greatly exaggerated. Exemptions have been criticized as a matter of principle by academics, legislators and organizations such as the Antitrust Modernization Commission and the Federal Trade Commission. Antitrust purists believe that immunities, particularly industry-specific ones, undermine the guiding principles of antitrust.

Yet, here we are in 2008, and the Antitrust Section still has a committee that studies and reports on exemptions and immunities, and that committee continues to be very busy. Indeed, despite the criticism of exemptions, the courts continue to find conduct to be exempt or immune from the antitrust laws; the Supreme Court's *Credit Suisse* decision appears to expand, not limit, immunities. Similarly, while there has been some legislative activity relating to immunities, the proposed bills appear to be relatively evenly divided between adding and removing immunities.

This newsletter is further evidence that exemptions and immunities are alive, well and controversial. Peter Barile considers the application of the *Noerr-Pennington* doctrine in the apparent widening split of authority among courts considering whether non-sham petitioning activity can be part of an anticompetitive scheme. This issue also features articles on two pending bills in Congress. Christopher Durocher analyzes legislation that would create a new exemption to allow community pharmacies to collectively negotiate, while Howard Morse reviews the legislation that would lift the antitrust exemption enjoyed by railroads. In addi-

PLEASE JOIN US
for the
56th ANTITRUST LAW SPRING MEETING
March 27–29, 2008
Washington, DC

tion, contributing editors Peter Barile, Ken Carroll, Richard Fueyo, Greg Garrett and Paula Garrett Lin summarize the key exemptions and immunities cases from the second half of 2007.

There is more to come, too.

On March 10, the Committee will co-sponsor a teleconference panel discussion on antitrust enforcement in the Telecom Sector. The program, "Antitrust Enforcement in the Telecom Sector: Will the FCC, FTC, or DOJ Have Jurisdiction Over the Future," will tackle the issue of whether the FTC's common carrier exemption will prevent the FTC from regulating telecommunications, even as telecommunications companies expand their product and service lines. This program comes on the heels of a highly successful panel discussion oprganized by John T. Delacouert that considered the recent FTC v Equitable Resources case. Speakers included George Cary of Cleary, Gottlieb, Steen & Hamilton, David Wales of the FTC, Robert Young of the Pennsylvania Public Utility Commission, and William Vigdor of Vinson & Elkins.

On March 27, at the Antitrust Section Spring Meeting, the Committee will co-sponsor a program on International Air Carriers and the exemptions that they enjoy. The international air transport industry has gradually seen its industry-specific immunities chipped away, and has recently been the subject of substantial antitrust scrutiny. The panel, which includes a government enforcer, an industry lawyer, a lawyer for the trade association and a plaintiff's lawyer, will consider both industry-specific and more general immunity issues.

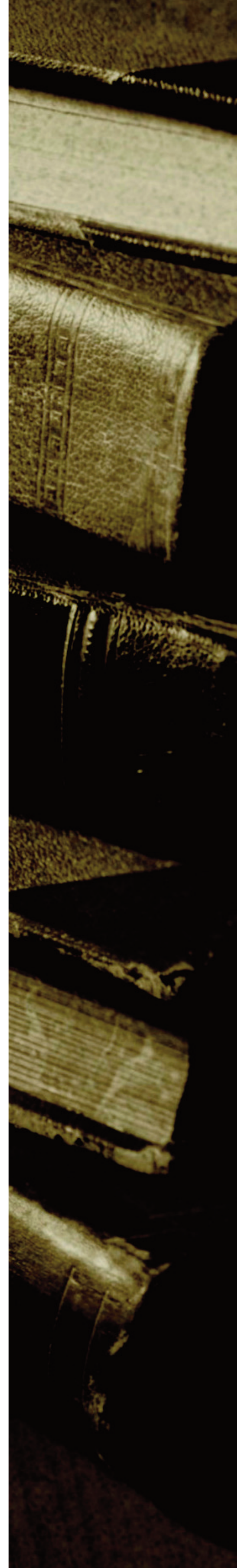
The committee has made significant strides in producing new books on key immunities that we hope will be available by the summer or fall of 2008. More projects are on the horizon, so please stay tuned.

Of course, if you want to do more than just stay tuned, please feel free to get involved. We have projects for all levels of commitment. If you would like to volunteer, please contact Howard Morse, the Committee's Chair, or any of the Vice Chairs listed below.

John Roberti

Please send all submissions for future issues to:

M. Howard Morse, Chair
Drinker Biddle & Reath LLP
1500 K St., N.W., Suite 1100
Washington, DC 200054209
howard.morse@dbr.com



Committee Leadership

Chair:

M. Howard Morse
Drinker Biddle & Reath LLP
1500 K St., N.W., Suite 1100
Washington, DC 20005-1209
(202) 842-8883
howard.morse@dbr.com

Council Representative:

Deborah A. Garza
Deputy Assistant Attorney General
950 Pennsylvania Avenue, NW,
Washington, DC 20530
Phone: 202-514-1157
deborah.garza@usdoj.gov

Vice-Chairs:

John Thomas Delacourt
Kelley Drye & Warren LLP
Washington Harbour, Suite 400
3050 K Street, NW
Washington 20007-5108
Phone: (202) 342-8525
jdelacourt@kelleydrye.com

Claudia R. Higgins
Kaye Scholer, LLP
The McPherson Building
901 Fifteenth Street, N.W., Suite 1100
Washington, DC 20005-2327
Phone: 202-682-3653
chiggins@kayescholer.com

Gregory P. Luib
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, DC 20580
(202) 326-3249
gluib@ftc.gov

John Roberti
Mayer Brown LLP
1909 K Street, NW
Washington, DC 20006-1101
tel: 202.263.3428
jroberti@mayerbrown.com

Contributing Editors

Peter Barile
Howrey LLP
1299 Pennsylvania Ave, NW
Washington, DC 20004
Phone: 202-783-0800
BarileP@howrey.com

Ken Carroll
Carrington Coleman Sloman & Blumenthal, LLP
901 Main Street, Suite 5500
Dallas, Texas 75202
(214) 855-3029
KCarroll@CCSB.com

Peggy Bayer Femenella
Federal Trade Commission
601 New Jersey Avenue, NW
Washington, DC 20580
(202) 326-3086

Richard K. Fueyo
Trenam Kemker
101 E. Kennedy Blvd., Suite 2700
Tampa, Florida 33602
(813) 227-7471
RKFueyo@trenam.com

Greg Garrett
Tydings and Rosenberg LLP
100 East Pratt Street
28th Floor
Baltimore, MD 21202
410.752.9767
ggarrett@tydingslaw.com

Paula Garrett Lin
Mayer Brown LLP
1675 Broadway
New York, NY 10019
Phone: (212) 506-2215
PLin@mayerbrown.com

Scheme Liability Revisited: Recovering Antitrust Damages Resulting from Meritorious Patent Litigation

Peter A. Barile III

Introduction

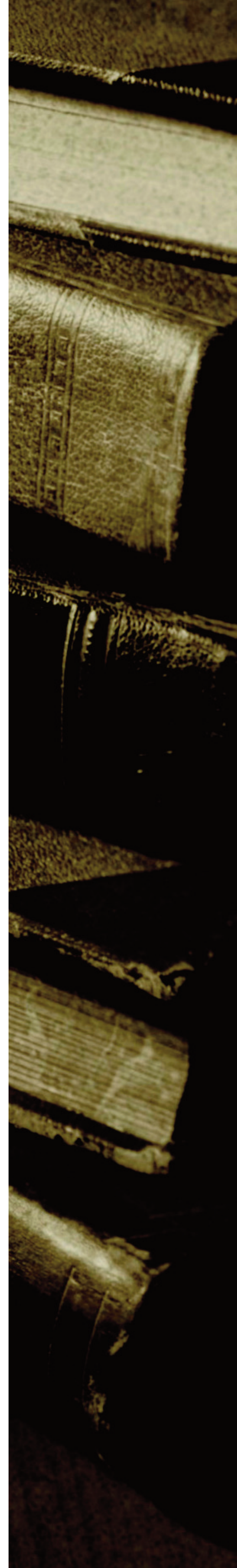
It is axiomatic that under the *Noerr-Pennington* doctrine, a necessary element of a sham litigation claim is that that the lawsuit at issue be objectively baseless. A lawsuit is objectively baseless only where "no reasonable litigant could realistically expect success on the merits."[1] Indeed, a winning case is not objectively baseless—as a matter of law.[2] Nevertheless, a recent high-profile district court case holds that antitrust plaintiffs may recover damages stemming from the defense of *meritorious* patent litigation, where that litigation is connected to a larger anticompetitive scheme. While the Federal Circuit may ultimately decide the issue,[3] for now it appears that this case, *Hynix Semiconductor Inc. v. Rambus, Inc.*,[4] may provide persuasive guidance to courts considering this issue. Thus, at least where more than a pure sham is alleged, patent holders should be aware that even a successful enforcement action could, in theory, result in their paying their opponent's (often substantial) defense expenses—times three.

The Case: An Alleged "Patent Ambush"

In *Hynix*, the Northern District of California held that the Federal Circuit would recognize liability for expenses incurred in defending non-objectively baseless lawsuits, where such lawsuits are "causally connected" to other elements of an anticompetitive scheme that violates the Sherman Act.[5] Rambus, the defendant, was alleged to have secretly prepared and obtained patents based upon information obtained in a standards-setting organization, contrary to its supposed obligations to disclose any such intellectual property to the organization.[6] When the standard was "locked in," Rambus then allegedly "ambushed" its fellow members with patent infringement suits. The organization members alleged these suits were part of a scheme to violate the antitrust laws.[7] As the patent lawsuits were never claimed to be objectively baseless in and of themselves, Rambus argued that the *Noerr-Pennington* doctrine prevented plaintiffs from recovering damages based upon the cost of the defense of the suits, even though the lawsuits allegedly were part of an overall anticompetitive scheme.[8] On this basis, Rambus moved to strike the jury demand for patent litigation defense expenses as a part of plaintiffs' claim for antitrust damages.

Although treating the issue presented as one of Federal Circuit law,[9] the court viewed Federal Circuit law as inconclusive on the issue.[10] Although the Federal Circuit stated in *Atari Games Corp. v. Nintendo of America, Inc.*[11] that antitrust liability may indeed be premised upon "an overall scheme to use the patent to violate the antitrust laws," the court deemed this merely to be dicta.[12] The court also looked to *In re Independent Service Organizations Antitrust Litig.*,[13] and *Q-Parma, Inc. v. Andrew Jergens Co.*,[14] but found nothing definitive. The court then considered three approaches taken by federal circuit courts prior to the creation of the Federal Circuit: one espoused by the Tenth Circuit in *Kobe, Inc. v. Dempsey Pump Co.*,[15] that such damages are available,[16] another by the Second Circuit, not allowing such damages,[17] and a third "middle ground" approach taken by the Eighth Circuit.[18]

The court predicted that the Federal Circuit would apply the Eighth Circuit approach, which allows for litigation defense damages—but only in cases where the lawsuit at issue is "causally connected" to other anticompetitive conduct alleged to be a part of the overall scheme.[19] Applying this standard, the court held that there was a causal connection between the patent suit and the other alleged anticompetitive conduct concerning the standard-setting organization. The court reasoned that a patent ambush is "ineffective without the threat of litigation."[20] The court thus denied defendant's motion to strike plaintiffs' jury demand, allowing plaintiffs to claim litigation defense expenses as antitrust damages.[21]



A Conflict Emerges

The *Hynix* decision expands an apparent conflict among district courts about the role of non-sham patent litigation in antitrust claims. *Hynix* appears to be inconsistent with a 2006 district court opinion holding that antitrust plaintiffs "may not use litigation conduct to support a claim of an overall scheme to monopolize if they cannot prove that the litigation was a sham."[22] In *Abbott Laboratories v. Teva Pharmaceuticals USA, Inc.*,[23] the District of Delaware, like the court in *Hynix*, viewed the language in *Atari* as *dicta*. However, rather than deeming the question of scheme liability unresolved, the Delaware court concluded that the precedents of the Federal Circuit allow only two avenues by which antitrust plaintiffs could seek damages resulting from patent litigation: *Walker Process* fraud and *PRE* sham litigation. In the words of the *Abbott* court:

> If the antitrust plaintiff can prove the existence of sham litigation, the litigation conduct can be included in the mix of things alleged to violate the antitrust laws. If not, the antitrust claim can still be heard on the merits, but without the sham litigation allegations. In this way, courts avoid the risk of such mixed allegations being used as a subterfuge to avoid the stringent requirements of *Walker Process* or *Noerr* immunity.[24]

At the same time, the *Hynix* decision is quite consistent with a 2003 Eastern District of Pennsylvania case, *ID Sec. Sys. Can., Inc. v. Checkpoint Sys., Inc.*,[25] which held that evidence probative of an anticompetitive intent behind an "otherwise procompetitive and protected patent litigation" is admissible "under the overall scheme exception to the prohibition against allowing patent enforcement activities to be used as evidence of anticompetitive conduct in antitrust suits."[26] Unlike the Northern District of California and the District of Delaware, the *I.D. Security* court was guided by both *Atari* and *Kobe*, explaining that "some courts have questioned the continued viability of the overall scheme exception."[27]

Conclusion

Conflicting policy considerations drive this conflict. On the one hand, to allow antitrust plaintiffs to collect damages for expenses incurred in defending meritorious patent infringement lawsuits may serve to chill the legitimate petitioning of the courts for redress, which is precisely what the *Noerr-Pennington* doctrine seeks to avoid.[28] On the other hand, antitrust has long recognized that "acts which are in themselves legal lose that character when they become constituent elements of an unlawful scheme."[29] If otherwise protected patent lawsuits are part and parcel of a scheme to violate the antitrust laws, it arguably stands to reason that the patent holder risks his *Noerr-Pennington* protection.

At the time of the preparation of this article, the *Hynix* case was scheduled for trial. It bears watching whether there is a subsequent appeal and whether this issue, which now divides certain district courts, comes before the Federal Circuit. Likewise, it bears watching whether other trial courts adopt this permissive approach prior to the Federal Circuit (or perhaps the Supreme Court) resolving this issue definitively.

1 *See Professional Real Estate Investors v. Columbia Pictures Indus*., 508 U.S. 49, 60 (1993); *Nobelpharma AB v. Implant Innovations*, 141 F.3d 1059, 1068 (Fed. Cir. 1998).

2 *PRE*, 508 U.S. at 60.

3 *See id.* at 61 ("A winning lawsuit is by definition a reasonable effort at petitioning for redress and therefore not a sham."); *FilmTec Corp. v. Hydranautics*, 67 F.3d 931, 936 (Fed. Cir. 1995) ("Obviously, if the patentee is successful in his infringement action, his suit is not baseless, and it cannot be a sham. The converse is not true, however; just because the patentee loses, he does not lose his immunity from antitrust liability. Liability turns on whether the suit is a sham, that is, on the nature of and the underlying merits of the patentee's case.").

4 *See Nobelpharma AB v. Implant Innovations*, 141 F.3d 1059, 1068 (Fed. Cir. 1998) ("[W]hether conduct in procuring or enforcing a patent is sufficient to strip a patentee of its immunity from the antitrust laws is to be decided as a question of Federal Circuit law.").

5 2007 U.S. Dist. LEXIS 84697 (N.D. Cal. Nov. 4, 2007).

6 *Id*. at *40-41.

7 *Id*. at *44.

8 *Id*.

9 *Id*. at *46.

10 *Id*. at *14 (citing *Nobelpharma AB v. Implant Innovations*, 141 F.3d 1059, 1068 (Fed. Cir. 1998)).

11 *Id*. at *23.

12 897 F.2d 1572, 1576-77 (Fed. Cir. 1990).

13 *Hynix Semiconductor*, 2007 U.S. Dist. LEXIS 84697, at *21 (quoting *Atari*, 897 F.2d at 1576-77).

14 203 F.3d 1322, 1326 (Fed. Cir. 2000).

15 360 F.3d 1295, 1304-05 (Fed. Cir. 2004).

16 198 F.2d 416 (10th Cir. 1952).

17 *Hynix Semiconductor, 2007 U.S. Dist. Lexis 84697* at *27 (citing *Kobe, Inc. v. Dempsey Pump Co.*, 198 F.2d 416 (10th Cir. 1952)).

18 *Id*. at *26 (citing *Ansul Co. v. Uniroyal, Inc.*, 448 F.2d 872 (2d Cir. 1971)).

19 *Id*. at *35 (citing *Am. Infra-Red Radiant Co. v. Lambert Indus., Inc.*, 360 F.2d 977, 996-97 (8th Cir. 1966)).

20 *Id*. at *37.

21 *Id*. at *45.

22 *Id*. at *47.

23 *Abbott Labs. v. Teva Pharms. USA, Inc.*, 432 F. Supp. 2d 408, 430 (D. Del. 2006).

24 *Id*. at 428-29

25 249 F. Supp. 2d 622 (E.D. Pa. 2003).

26 *Id*. at 656.

27 *Id*. at 682 n.14.

28 *See City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 379 (1991).

29 *Continental Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 707 (1962).

Railroad Antitrust Enforcement Act Reported out of Senate Judiciary Committee

Bill Would Eliminate Antitrust Exemptions

M. Howard Morse

The Senate Committee on the Judiciary has approved the Railroad Antitrust Enforcement Act (S. 772). The purpose of the bill, according to the Committee, is "to remove current exemptions and subject the American freight railroad industry to all the provisions of the nation's antitrust laws." The bill would allow the Department of Justice, Federal Trade Commission, and state attorneys general to challenge mergers and anticompetitive practices and allow injured parties to bring private antitrust actions for treble damages.

As explained by the Senate Judiciary Committee, the object of the proposed legislation is "simply to remove the antitrust exemption protecting the railroad industry and allow antitrust enforcement of railroad industry practices." The Committee has concluded that "the current antitrust exemption enjoyed by the railroad industry is unwarranted due to the substantial de-regulation of the railroad industry in recent decades, and has resulted in anticompetitive behavior harming railroad customers and consumers." The Committee asserts that requiring railroads to comply with the antitrust laws will result in lower prices and more efficient, economical rail transportation of grain, coal, chemicals and other products.[1]

If enacted, the Railroad Antitrust Enforcement Act could be the first step toward implementing

continued next page

Community Pharmacy Fairness Act Reported out of House Judiciary Committee

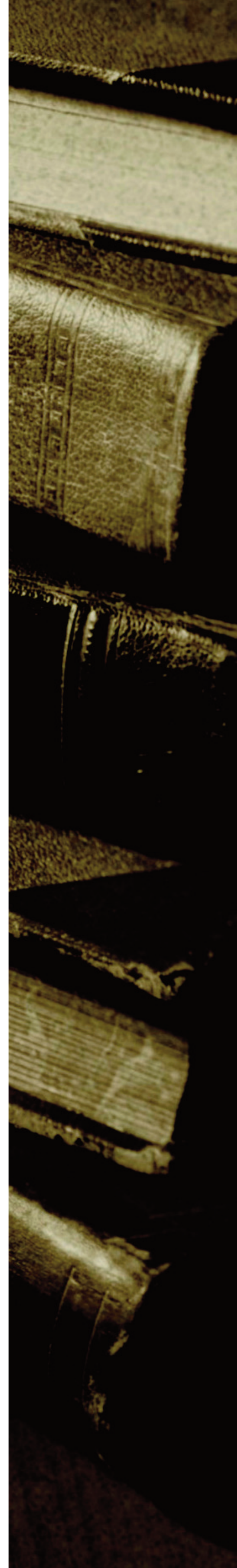
Bill Seeks Antitrust Exemption for Independent Pharmacies through Application of National Labor Relations Act

Christopher Durocher

An important piece of antitrust legislation that would provide a new antitrust exemption has taken its first step toward passage. On November 7, 2007, the House Committee on the Judiciary approved by voice vote the Community Pharmacy Fairness Act of 2007 (H.R. 971), a bill that would provide an antitrust exemption for independent pharmacies.[1] According to its supporters, the legislation would allow independent pharmacies to more effectively compete with larger pharmacies when negotiating reimbursement rates with health plans. Opponents assert that the collective bargaining permitted by H.R. 971 provides independent pharmacies disproportionate leverage and a consequent greater ability to negotiate higher reimbursement rates for prescription drugs. These higher rates would then be passed on to consumers.

H.R. 971 was introduced by Rep. Anthony Weiner (NY-D) on February 2, 2007, and has received bi-partisan support, with 179 co-sponsors. On October 18, 2007, the House Judiciary Committee's Antitrust Task Force held a hearing on H.R. 971. Representatives of the Association of Community Pharmacies Congressional Network, National Community Pharmacists Association, and the Mississippi Independent Pharmacies Association testified in favor of the legislation, while representatives of the Federal Trade Commission

continued on page 12



Railroad Antitrust Enforcement Act Reported out of Senate Judiciary Committee

continued from page 7

the Antitrust Modernization Commission's recommendation that statutory immunities be disfavored and last only for so long as necessary to satisfy a societal goal that trumps the benefit of the free market. The legislation would also implement in the railroad industry the AMC's recommendations that Congress reevaluate the filed-rate doctrine and grant the agencies full merger enforcement authority under the Clayton Act, even in industries subject to economic regulation.[2]

Opponents to the legislation argue that it is a "solution looking for a problem," premised on the assumption that a gap exists between the scope of economic regulation and the antitrust laws. They argue that rather than fill a void in current law, the legislation would "provide a dual remedy to shippers and interfere with the [Surface Transportation Board's] implementation of national transportation policy." They also note that the bill eliminates antitrust exemptions that apply to railroads, but retains those same exemptions to the extent that they apply to other parties.[3]

S. 772 was introduced by Judiciary Committee Antitrust Subcommittee Chairman Herbert Kohl (D-WI) in March 2007. It has bi-partisan support, with nine co-sponsors. The Senate Judiciary Committee voted on September 20, 2007 to report the bill, with modest changes. The Antitrust Subcommittee thereafter held a hearing, on October 3, 2007, with testimony by shippers, the railroad industry, the chairman of the Surface Transportation Board, and an academic. On December 19, 2007, the Judiciary Committee issued its report on the bill, and the bill is now pending before the full Senate.[4]

Similar legislation was introduced in the House (H.R. 1650) by Rep. Tammy Baldwin (D-WI) with 20 co-sponsors. That bill was referred to the House Judiciary Committee, and also to the Transportation and Infrastructure and Energy and Commerce Committees for consideration of provisions within their respective jurisdiction.[5]

This article provides a brief overview of the current regulatory scheme governing railroads and current antitrust framework and describes the changes that the proposed legislation would make.

The Current Regulatory Framework

For more than a hundred years, under the Interstate Commerce Act of 1887, the Interstate Commerce Commission ("ICC") and later the Surface Transportation Board ("STB") has regulated the railroad industry. As explained by the Antitrust Modernization Commission, "a belief that certain industries were either 'natural' monopolies (that is, that the most efficient market structure included only one firm) or were at risk for 'excessive competition' led to government regulation of prices, costs, and entry into those industries." Technological changes and recognition of the costs and market distortion of regulation, however, have led to changes over time.[6]

Pervasive regulation of the railroad industry has been eliminated in stages. In 1976, Congress passed the Railroad Revitalization and Regulatory Reform Act ("4R Act") which reduced rate regulation.[7] Most significantly, the 1980 Staggers Rail Act limited the authority of the ICC to regulate rates where competition was not effective to protect shippers.[8] The ICC Termination Act of 1995 replaced the ICC with the STB and further deregulated the industry.[9]

Today, the STB has broad jurisdiction over interstate transportation by rail within the United States. The agency has specific statutory authority to set maximum rates, resolve railroad rate and service disputes and review railroad restructuring transactions, line sales, line construction and line abandonment. Railroads are also subject to the imposition of competitive access remedies.[10] The STB, however, is directed to exempt rail carriers, transactions and services when continued regulation is not necessary to protect shippers from the abuse of market power or to carry out transportation policy, and the STB has ex-

empted broad categories—including commodities transported in boxcars, intermodal transportation, and various agricultural commodities—that are subject to truck and other competition.[11]

At present, the STB has exclusive authority to review mergers and acquisitions, and transactions which it approves are exempt from antitrust challenge.[12] The STB must evaluate railroad mergers to determine if the "public interest in meeting significant transportation needs" outweighs any "anticompetitive effects of the transaction." The STB must "accord substantial weight" to the DOJ's views, but the DOJ's views are not binding on the STB.[13] In fact, DOJ filed comments opposing the 1996 merger of the Union Pacific Railroad and the Southern Pacific Railroad, which the STB approved. DOJ has also filed comments on other transactions recommending conditions be imposed, which were not adopted by the STB.[14] Critics note that over the last thirty years, the railroad industry has consolidated to seven large Class 1 railroads, four of which carry 90% of all freight railroad traffic.[15]

The railroad industry today is not immune from all antitrust actions, as the STB's jurisdiction over rail transportation matters does not generally displace the antitrust laws.[16] The industry does, however, have several express statutory and judicially-created immunities from antitrust law, which would be eliminated by the proposed legislation. Railroads, for example, are immune from antitrust challenge for certain transactions approved by the STB, such as leases, trackage rights, pooling arrangements, and agreements to divide traffic.[17] Railroads are also immune for rate-related agreements approved by the STB, such as agreements establishing rules governing charges that one railroad must pay to use another's equipment.[18]

The Proposed Legislation

The Railroad Antitrust Act would make a number of changes to current law to limit current antitrust immunities applicable to the railroad industry.

First, the bill would bring railroad mergers within the ambit of Section 7 of the Clayton Act and empower the antitrust enforcement agencies to sue to block acquisitions the effect of which may be substantially to lessen competition.[19] The STB would, however, continue to approve mergers and acquisitions under its "public interest" test. Thus, transactions would be subject to dual review, as are telecommunications industry transactions subject to Federal Communications Commission review.

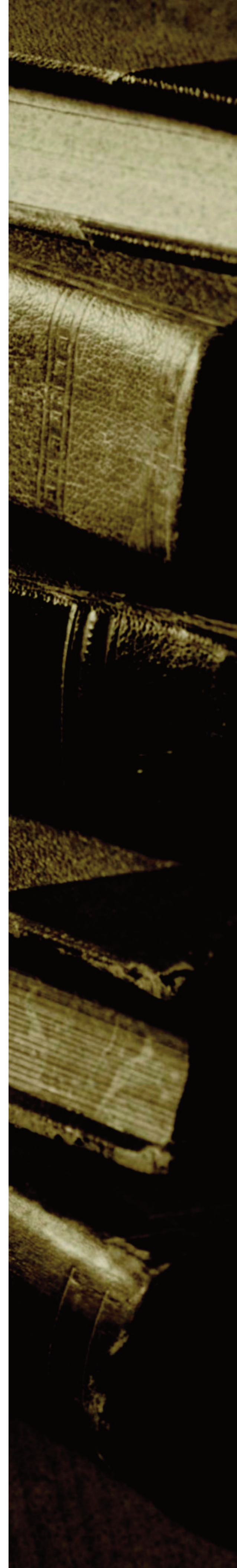
That change would be consistent with the AMC's recommendation that "even in industries subject to economic regulation, the antitrust agencies generally should have full merger enforcement authority under the Clayton Act."[20] The AMC, however, went further and recommended that Congress periodically review all instances in which a regulatory agency reviews proposed mergers or acquisitions under the agency's 'public interest' standard to determine whether in fact such regulatory review is necessary."[21] The proposed legislation leaves STB merger review in place.

The Act would eliminate the exemption from Section 16 of the Clayton Act, which currently exempts common carriers subject to STB regulation from injunctive relief in private antitrust actions. Under the bill, only non-railroad common carriers would be exempt.[22]

The Act also would remove any requirement that federal district courts defer to the primary jurisdiction of the STB in any civil antitrust action against a railroad.[23]

The Act removes any exemption from FTC jurisdiction, so that the FTC may enforce the Clayton Act and FTC Act against railroads.[24] DOJ has, however, traditionally reviewed mergers and acquisitions in transportation industries, and would be expected to continue to do so.

In addition, the Act would abolish the filed rate doctrine with respect to railroads.[25] That judicially-created doctrine, derived from the Supreme Court's 1922 decision in *Keogh v. Chicago & Northwestern Railway*, prohibits private plaintiffs from pursuing an antitrust action seeking treble damages where the plaintiff is claiming that a rate submitted to a regulator resulted from an antitrust violation. The court reasoned that



only the regulatory authority could change the rates, even if higher than they might be due to a price-fixing conspiracy.[26] The AMC recommended that Congress evaluate whether the doctrine should continue to apply where the regulatory agency no longer specifically reviews proposed rates, and noted that rail and motor carriers are generally no longer required to file rates with the STB.[27] The proposed legislation would overrule the doctrine only for the railroad industry.

Finally, the Act would eliminate exemptions from the antitrust laws for ratemaking agreements approved by the STB, STB-approved railroad agreements or combinations relating to the pooling or division of traffic and earnings.[28]

The Senate vote, on September 20, 2007, to report the bill favorably, included a number of technical amendments. The substitute also included two non-technical changes. It clarified language to make clear that the standard of review for mergers and acquisitions would not be changed by the bill. It also provides that railroad car pooling arrangements approved by the STB would continue to be exempt.[29]

The bill is intended to apply prospectively, including ongoing conduct previously immunized that continues six months after enactment of the legislation. The bill would thus give those affected by the termination of the railroad antitrust exemption six months to bring their conduct into compliance with antitrust law.[30]

The House Judiciary Committee Antitrust Task Force held a hearing to address the proposed legislation on February 25, 2008, as this newsletter was going to print. The witnesses at that hearing included different shippers but the same railroad industry representatives and academics as testified before the Senate in October.[31]

1 U.S. Senate Committee on the Judiciary, "The Railroad Antitrust Enforcement Act," Sen. Rep. 110-252, 110th Cong. 1st Sess. (Dec. 19, 2007) (hereafter *Senate Report*) at 9.

2 Antitrust Modernization Commission, *Report and Recommendations*, at 20-22 (April 2007) (hereafter *AMC Report*)

3 Testimony of G. Paul Moates, on Behalf of the Association of American Railroads, Before the Senate Committee on the Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights (Oct. 3, 2007), *available at* http://www.aar.org/PubCommon/Documents/Testimony/Moats_Testimony_on_S772.pdf.

4 *Senate Report*; Library of Congress, Thomas Report on S.772, *available at* http://thomas.loc.gov/cgi-bin/bdquery/z?d110:SN00772:@@@L&summ2=m& (last checked Jan. 30, 2008).

5 Library of Congress, Thomas Report on H.R. 1650, *available at* http://thomas.loc.gov/cgi-bin/bdquery/z?d110:HR01650:@@@L&summ2=m& (last checked Jan. 30, 2008).

6 *AMC Report* at 333.

7 Pub. L. No. 94-210, 90 Stat. 31 (1976) (codified in scattered sections of 15, 31, 45 and 49 U.S.C.).

8 Pub. L. No. 96-448, 94 Stat. 1895 (1980) (codified in scattered sections of 11, 45 and 49 U.S.C.).

9 Pub. L. No. 104-88, 109 Stat. 803 (1995).

10 49 U.S.C. §§ 10501(a), 10701 et seq., 10901, 10903, 11102.

11 49 U.S.C. § 10502; *see generally* ABA, Antitrust Law Developments (Sixth) 1463 (2007).

12 49 U.S.C. § 11321(a).

13 49 U.S.C. § 11324(d).

14 *Senate Report* at 4; *AMC Report* at 364.

15 *Senate Report* at 3.

16 H.R. Rep. No. 104-422, at 167 (1995); *Alliance Shippers v. Southern Pac. Transp. Co.*, 858 F.2d 567, 570 (9th Cir. 1988).

17 49 U.S.C. § 10706.

18 49 U.S.C. §§ 10706, 11321(a).

19 S. 772, Sec. 3.

20 *AMC Report* at 364.

21 *Id.* at 366.

22 S. 772, Sec. 2.

23 S. 772, Sec. 4.

24 S. 772, Sec. 5.

25 S. 772, Sec. 6.

26 260 U.S. 156, 162-64 (1922).

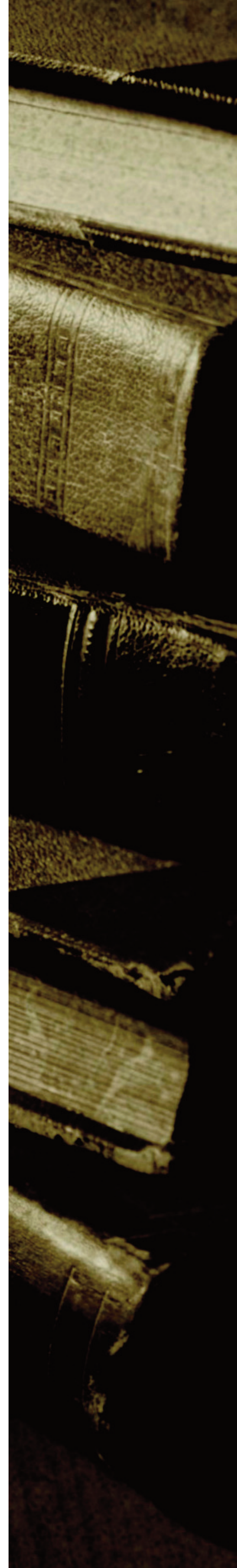
27 *AMC Report* at 362.

28 S. 772, Sec. 7. Pursuant to an amendment adopted during Judiciary Committee consideration, the Senate-reported bill would continue to exempt railroad car pooling arrangements from antitrust scrutiny.

29 *Senate Report* at 9.

30 S. 772, Sec. 8.

31 See U.S. House of Representatives Committee on the Judiciary, Antitrust Task Force "Hearing on H.R. 1650, the 'Railroad Antitrust Enforcement Act of 2007,'" *available at* http://judiciary.house.gov/oversight.aspx?ID=413.



Community Pharmacy Fairness Act Reported out of House Judiciary Committee

continued from page 7

("FTC") and Pharmaceutical Care Management Association testified in opposition. The bill is now pending before the full House.

H.R. 971 seeks to achieve its goal of making independent pharmacies more competitive by "entitling [them] to the same treatment under the antitrust laws as the treatment to which bargaining units which are recognized under the National Labor Relations Act ("NLRA") are entitled in connection with activities described in section 7 of such Act."[2] The legislation would allow independent pharmacies to collectively bargain with health plans and pharmacy benefit managers ("PBMs") [3] in the same way that labor organizations are permitted to collectively bargain with employers under the NLRA.[4] The law would exempt independent pharmacies from private actions and enforcement actions by the FTC or the Department of Justice ("DOJ") for violations of antitrust laws relating to their collective bargaining of rates.[5] Under a limitation to the exemption contained in H.R. 971, antitrust laws would still apply in situations where independent pharmacies conspired to prevent other independent pharmacies from participating in drug reimbursement programs, limit their reimbursement rates, or otherwise limit their scope of services.[6]

A sunset provision added by Rep. Weiner would limit application of the exemption to a five-year period, starting on the date of enactment. The provision also requires the Government Accountability Office to commission a study to determine the law's impact at the beginning of the fifth year after enactment.

Supporters Cite Unfair Buying Power of Health Plans and Pharmacy Benefit Managers

In his testimony before the Antitrust Task Force, Mike James, Vice President of the Association of Community Pharmacies Congressional Network, asserted that H.R. 971 is the only way "to combat the takeover of [consumer's] health care by… huge companies whose only interest is the bottom line, not the health of patients."[7] Under current antitrust law, independent pharmacies are prohibited from collaborating to negotiate prescription drug reimbursement rates with PBMs or health plans.[8] Supporters of H.R. 971 claim that these constraints make independent pharmacies uncompetitive and ultimately will lead to pharmacy closings. Patients forced to move to mail-order programs due to pharmacy closings would lose their ability to consult local pharmacy professionals and receive personalized service.

James noted that the PBM industry controls over 95% of prescriptions filled, and that, as a result, it has disproportionate power.[9] Consequently, PBMs are able to dictate reimbursement rates without the need to engage independent pharmacies in good-faith negotiations.[10] This, according to James, means that pharmacies must accept reimbursement rates that fail to cover costs, jeopardizing pharmacy solvency.[11] In support of these claims, James noted that in 2006, due largely to low third-party reimbursement rates, 1,152 independent pharmacies were forced to close.[12] Further explaining the need for the antitrust exemption, Robert Dozier, Executive Director of the Mississippi Independent Pharmacies Association claimed, "Independent pharmacies across…the United States are a key component of the healthcare delivery system, but they are facing extinction due to the unfair business practices of the major Pharmacy Benefit Managers and Medicare Part D Plans."[13] He and the bill's other supporters see the antitrust exemption as the best way to protect the remaining independent pharmacies from the same fate.

Critics Question Wisdom of Antitrust Exemption

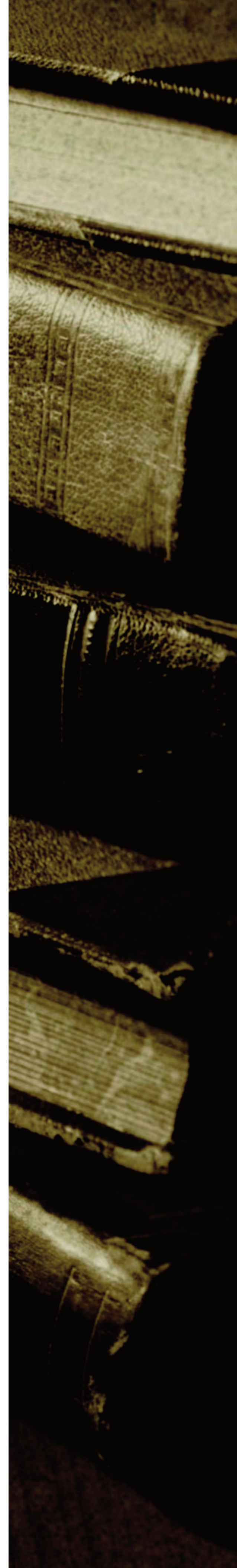
Critics of H.R. 971 claim that independent pharmacies have ample opportunity to negotiate reimbursement rates under current antitrust laws. Pharmacy service administrative organizations ("PSAOs"), which are group-purchasing networks that represent multiple independent pharmacies and provide them greater purchasing power, allow independent pharmacies to reduce administrative costs and achieve savings through

economies of scale.[14] These same PSAOs can represent pharmacies in negotiating reimbursement rates with PBMs and health plans. According to a report prepared by CRA International for the Pharmaceutical Care Management Association, the inability of PSAOs to successfully negotiate lower reimbursement rates is largely a result of "the historic willingness of individual pharmacies to defect from PSAOs or to join multiple PSAOs."[15] This has allowed PBMs to keep reimbursement rates low.

Opponents of the legislation, including the FTC, also question the wisdom of using antitrust exemptions to address perceived anticompetitive market power. David Wales, Deputy Director of the FTC's Bureau of Competition, explained that independent pharmacies are seeking relief from inequalities in bargaining power, not anticompetitive behavior.[16] Wales argued that there is no evidence that PBMs or health plans have any actual monopsonistic market power. He continued that "even if there were evidence that health plans or PBMs were able to exercise [monopsony] power over pharmacies, the Commission believes that the solution is not to authorize private competitors to use countervailing power."[17] Peter Rankin of CRA International added that the "appropriate response, instead, is to determine if there is a legitimate competitive imbalance and address the economic factors creating that imbalance."[18] Creating an antitrust exemption could stifle competition and innovation that would otherwise lead to improvements in the quality and efficiency of prescription drug delivery to consumers.[19]

Wales further noted that creating an antitrust exemption can result in unintended consequences in other markets in which the independent pharmacies operate. According to the Antitrust Modernization Commission ("AMC"), antitrust exemptions, like the one embodied in H.R. 971, "create economic benefits that flow to small, concentrated interest groups, while the costs of the exemption are widely dispersed, usually passed on to a large population of consumers through higher prices, reduced output, lower quality, and reduced innovation."[20] In the case of H.R. 971, critics fear that individual employers, patients and taxpayers would bear the burden of increased reimbursement rates if independent pharmacies were allowed to collectively bargain. According to Rankin, H.R. 971 would increase expenditures for prescription drugs by 11.8% or $29.6 billion over five years, a quarter of which would be paid by increased federal spending on Medicare Part D, the federal prescription drug coverage program.[21] Wales testified that H.R. 971 "threatens to raise prices to consumers, especially seniors, for much-needed medicine. It also threatens to increase costs to private employers who provide health care insurance to employers. All without any assurance of higher quality care."[22] As drug costs increase, employers could scale back the prescription drug benefits that they offer and patients may choose to fill fewer prescriptions. Consequently, critics contend, the consumer protection at the heart of antitrust laws and purportedly at the heart of H.R. 971's stated goal to "ensure and foster continued patient safety and quality of care" would be subverted by its very enactment.

Finally, critics question the efficacy of relying on the National Labor Relations Act's collective bargaining provision to create an antitrust exemption. The FTC considers it inappropriate for the legislation to rely on a scheme designed to address employee-employer labor negotiations.[23] In his testimony, Wales specifically cited the lack of oversight for independent pharmacy negotiations, in comparison to the National Labor Relations Board's oversight authority under the collective bargaining provision of the NLRA.[24] In response to this criticism, during the markup by the Judiciary Committee, Rep. Issa offered, and the committee approved, an amendment that would maintain the FTC's oversight responsibilities for independent pharmacies participating in collective bargaining. More fundamentally, however, critics note that the purpose of H.R. 971 is to promote the safety and quality of patient care, whereas labor laws were designed to empower employees to negotiate for higher wages and better working conditions.[25] According to the FTC, this disconnect between the goals of H.R. 971 and its method of implementation would not protect access to and quality of health care, but would "merely grant private businesses a broad immunity to present a 'united front' when negotiating prices and other terms of dealing with health plans."[26]



H.R. 971 has not been scheduled for a vote by the full House of Representatives. Senator Johnny Isakson (R-GA) introduced the Senate's companion bill, S. 885, on March 14, 2007. It has been referred to the Senate Committee on the Judiciary, which has yet to take any action on the bill.

1 H.R. 971 defines an independent pharmacy as "a pharmacy which is not owned (or operated) by a publicly traded company." H.R. 971, 110th Cong. § 2(h)(3). An amendment offered by Rep. Darrell Issa (R-CA) and approved by the committee would further limit the exemption to pharmacies with a market share of less than 10% in any Medicare Part D prescription drug plan region and less than 1% market share in the United States.

2 *Id*. at § 2(a).

3 PBMs are companies that administer drug benefit programs for employers and health insurance carriers. PBMs contract with health care providers (including pharmacies) to provide managed prescription drug benefits and to set reimbursement rates.

4 Section 7 of the National Labor Relations Act provides that "Employees shall have the right to self-organization, to form, join, or assist labor organizations, to bargain collectively through representatives of their own choosing, and to engage in other concerted activities for the purpose of collective bargaining or other mutual aid or protection, and shall also have the right to refrain from any or all such activities except to the extent that such right may be affected by an agreement requiring membership in a labor organization as a condition of employment as authorized in section 158(a)(3) of this title." 29 U.S.C. § 157.

5 H.R. 971 defines antitrust laws as those described in 15 U.S.C. §§12(a) & §45 and any similar state law. H.R. 971 §2(h)(1)

.6 H.R. 971 § 2(e).

7 *The Impact of Our Antitrust Laws on Community Pharmacies and Their Patients: Hearing on H.R. 971 Before the H. Comm. on the Judiciary*, 110th Cong. (2007) (statement of Mike James, Vice President, Association of Community Pharmacies Congressional Network).

8 *See* 15 U.S.C. § 1 *et seq.*

9 James, *supra* note 7.

10 *Id.*

11 *Id*.

12 *Id*.

13 *The Impact of Our Antitrust Laws on Community Pharmacies and Their Patients: Hearing on H.R. 971 Before the H. Comm. on the Judiciary*, 110th Cong. (2007) (statement of Robert Dozier, Executive Director, Mississippi Independent Pharmacies Association).

14 Peter J. Rankin et al., *The Cost of Independent Pharmacy Antitrust Exemptions*, 18 (May 2007) (Pharmaceutical Care Management Association); *see also The Impact of Our Antitrust Laws on Community Pharmacies and Their Patients: Hearing on H.R. 971 Before the H. Comm. on the Judiciary*, 110th Cong. (2007) (statement of Peter Rankin, Senior Associate, CRA International).

15 Rankin, *supra* note 14 at 19.

16 *The Impact of Our Antitrust Laws on Community Pharmacies and Their Patients: Hearing on H.R. 971 Before the H. Comm. on the Judiciary*, 110th Cong. 18 (2007) (statement of David Wales, Deputy Director, Federal Trade Commission).

17 *Id*. at 18.

18 James, *supra* note 7 at 4-5.

19 Wales, *supra* note 16 at 3.

20 Antitrust Modernization Commission, Report and Recommendations (April 2007) at 335, *available at* http://www.amc.gov/report_recommendations/toc.htm.

21 Rankin, *supra* note 14 at 19.

22 Wales, *supra* note 16 at 1.

23 *Id*. at 8.

24 *Id*.

25 *Id*.

26 *Id*. at 9.

American Bar Association
Section of Antitrust Law

Exemptions & Immunities,
Communications Industry, and
Computer Industry & Internet Committees

Present:

Antitrust Enforcement in the Telecom Sector: Will the FCC, FTC, or DOJ Have Jurisdiction Over Future Disputes?

Date: March 10, 2008
Time: 12:00 pm - 1:30 pm
Location: WilmerHale
1875 Pennsylvania Avenue, NW
Washington, DC

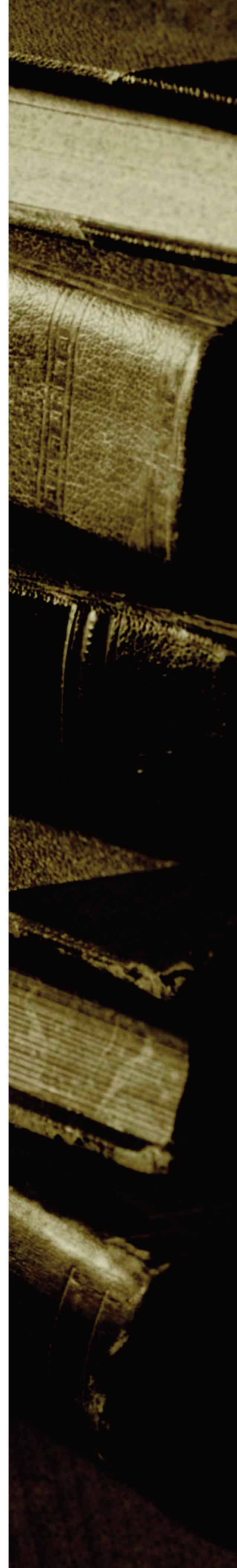
The rapid convergence of telecommunications services has necessitated not only the re-thinking of technical boundaries, but the re-thinking of traditional regulatory boundaries as well. The FCC's primary jurisdiction over highly regulated common carrier services has, in the past, limited the role of both FTC and DOJ. However, this balance may be changing. With voice, video, and data services increasingly provided in "bundles" – at least two components of which (video and data) are not classified as common carrier services, and are thus beyond the scope of the FTC Act's common carrier exemption – which agency is best situated to address competition concerns in the telecom sector? What are the limits of each agency's expertise, experience, and legal authority? Does the FCC/FTC experience in the consumer protection area provide us with useful guidance? Please join our panel of experts for a lively discussion not only of where the jurisdictional lines are currently drawn, but where they should be drawn.

PANELISTS: **John Rogovin** – Partner, WilmerHale (former General Counsel, FCC)
Maureen Ohlhausen – Director, Office of Policy Planning, FTC
J. Bruce McDonald – Partner, Jones Day (former DAAG, Antitrust Div., DOJ)
Jim Kohlenberger – Exec. Dir., Voice on the Net ("VON") Coalition

MODERATOR: **Martin Stern** – Partner, K&L Gates

To RSVP, please e-mail Pamela Greenstein at Pamela.Greenstein@wilmerhale.com. A dial-in number for the program will be sent to you in advance at the e-mail address provided. If you have any questions, please contact Diane Odom at (312) 988-5702 (odomd@staff.abanet.org).

Recordings of this Brown Bag will be posted on the Section's Web site in the Members Only area and will downloadable in MP3 format, free of charge, at http://www.abanet.org/antitrust/at-bb/bb-audio.shtml



E&I CASE LAW UPDATE

Implied Immunities

***In re Short Sale Antitrust Litigation*, No. 06 Civ. 2859 (VM), 2007 U.S. Dist. LEXIS 94116 (S.D.N.Y. Dec. 20, 2007)**.

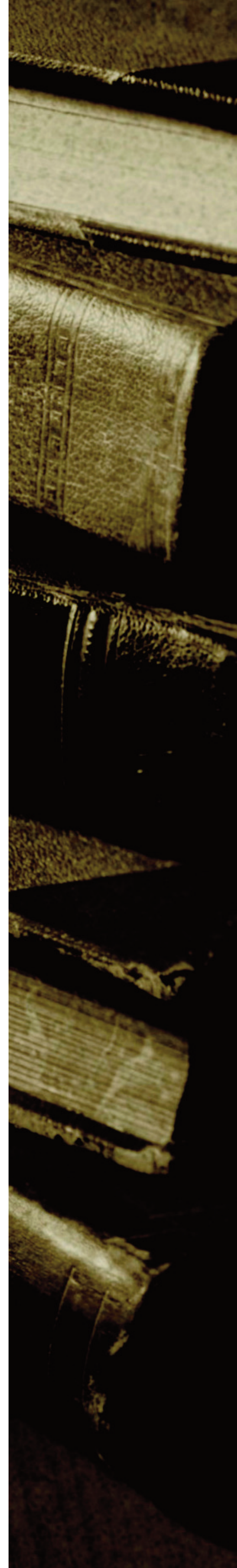
Applying the Supreme Court's recent decision in *Credit Suisse Securities (USA) LLC v. Billing*, 127 S. Ct. 2383 (2007), Southern District Judge Victor Marrero has dismissed a Sherman Act § 1 class action against participants in the short sale securities market. Plaintiffs (short sellers of securities) alleged that defendants (most of the major broker-dealers in the industry) conspired to fix prices or fees in connection with "hard-to-borrow" securities, and also conspired for fees to be charged even when the seller's broker never actually located or delivered the shorted or "borrowed" securities to the purchaser's broker. Judge Marrero, applying the four-part test articulated in *Billing*, found plaintiffs' antitrust claims to be "clearly incompatible" with the securities laws governing short sales and, therefore, held that those securities laws impliedly preclude application of the antitrust laws to the conduct in question. Neither the SEC nor the DOJ weighed in on the implied preclusion issue, as they did in *Billing*.

The court began its opinion with a primer on short selling: Short Seller tells his or her broker to sell shares Seller doesn't own (in the expectation shares in the subject stock can later be purchased for less than the price he or she is getting in this "short sale"). At least theoretically, Short Seller "borrows" the shares to complete this original sale from his or her broker who, in turn, may use its own holdings or locate and acquire them elsewhere. Later, Short Seller purchases shares of the same stock in the market to "cover" the short sale – i.e., repay or replenish the "borrowed" stock used in the short sale. In addition, Short Seller must pay a daily fee for the stock borrowed on his or her behalf to complete the original short sale. "Hard-to-borrow" stocks – stocks in short supply, for example – command higher fees. Short Seller's profit, if any, comes from the net proceeds of the short sale minus the cost of acquiring replacement shares later and the fees incurred in "borrowing" the stock needed to complete the original short sale.

Plaintiffs alleged that the defendant broker-dealers violated Section 1 by, among other things, (1) agreeing to fix the fees charged on "hard-to-borrow" stocks and colluding to classify particular stocks as "hard-to-borrow," and (2) agreeing in some cases essentially to mimic short sales and borrowings by failing to actually locate and deliver any borrowed stock, instead simply keeping a list of "IOUs" among the brokers, but nevertheless charging Sellers the full borrowing fees.

Defendants moved to dismiss on a variety of grounds, but the only one addressed by the court was implied preclusion under *Billing*, which the parties had covered in fairly short supplemental briefs. In a nutshell, defendants argued that the SEC had adopted Regulation SHO specifically to govern the short sale market, creating an active regulatory regime to which Sherman Act claims were clearly repugnant.

Judge Marrero applied the four criteria articulated by the Supreme Court in *Billing* for determining whether antitrust claims are "clearly incompatible" with the securities laws and therefore are impliedly precluded in a given context: (1) whether possible conflict between the securities and antitrust laws would affect "practices that lie squarely within an area of financial market activity that the securities law seeks to regulate"; (2) whether regulatory authority exists under the securities laws to supervise the activities in question; (3) whether the responsible regulatory entities actively exercise that



authority; and (4) whether there is a risk of conflicting guidance, requirements, duties, and standards if both the securities laws and antitrust laws were applied to the conduct in question.

Noting that short selling provides the securities markets with needed market liquidity and pricing efficiency, the court quickly determined that the "short sale securities market lies squarely within an area of financial market activity that the securities laws seek to regulate," satisfying the first *Billing* factor. Given Regulation SHO, the court similarly had little difficulty finding that factors two and three (authority to regulate and actual regulation by the SEC and others) also were met. To be fair, however, plaintiffs rightly argued that, unlike the situation in *Billing*, the SEC had never specifically sought to regulate the "borrowing fees" charged by brokers in short sales, much less agreements among brokers to fix such fees – a logical gap the court didn't directly address. (Indeed, plaintiffs' argument on this score came close to that mounted by the Solicitor General in *Billing*, on which the Supreme court declined to express a view, that implied preclusion surely would not extend to things like, say, overt market division.)

Although the court then invoked language from *Billing*—referencing concerns about "a serious legal line-drawing problem"—its analysis of the fourth factor seemed the most difficult. It may be true that antitrust claims for brokers' failures to deliver borrowed securities (the second general focus of Plaintiffs' claims) might conflict with Regulation SHO's treatment of "FTDs" (failures to deliver). But it is more difficult to argue that an actual price- or fee-fixing conspiracy among brokers, such as Plaintiffs putatively alleged, would conflict with any SEC regulation of the short sale market. As in *Billing*, however, the court found serious potential conflict not so much in the allegedly wrongful conduct itself as in the evidence and attendant conduct that would be used to prove an antitrust violation. The court noted that brokers in the business of effecting short sales for their clients had many legitimate reasons to communicate regularly about that market – for example, in specific instances, to locate and borrow securities to complete a transaction, and more generally, to evaluate which securities truly are "hard-to-borrow." Evidence of such communications may be portrayed by the defendants as necessary to the operation of the market, but might be painted by Plaintiffs (or taken by a jury) as evidence of collusion or the opportunity for same. So, as in *Billing*, Judge Marrero found that allowing plaintiffs' antitrust claims to go forward "would likely chill a broad range of activities that the securities laws permit and encourage," and thereby improperly inhibit beneficial conduct in the short sale market. (The court did not invoke the argument, persuasive in *Billing*, that allowing the antitrust claims to proceed would in effect countenance an end run around Congress's efforts in the PSLRA and elsewhere to rein in spurious securities actions.)

Judge Marrero, therefore, dismissed plaintiffs' antitrust claims with prejudice.

[Thanks to Ken Carroll]

The Noerr-Pennington *Doctrine*

Love Terminal Partners, L.P. v. City of Dallas, et al., No. 3:06-CV-1279-D, 2007 U.S. Dist. Lexis 80736 (N.D. Tex. Oct. 31, 2007).

A federal district court in Dallas in October dismissed antitrust claims against the cities of Dallas and Ft. Worth, American and Southwest Airlines, and others, in connection with the compromise agreement they forged to enable direct (and, eventually, non-stop) service from Dallas Love Field to destinations throughout the United States. The court reached its decision primarily on the basis of *Noerr* immunity because, although that agreement embodied a number of what otherwise would have been

per se violations, it was aimed at securing Congress's modification of the infamous "Wright Amendment" that limited flights at Love, and was fashioned in response to congressional invitation; what's more, the accord and its agreed restraints were explicitly made subject to congressional approval (which was obtained in the Wright Amendment Reform Act of 2006), and, by its express terms, would have been null and void had such approval not been achieved. The result, therefore, is hardly surprising.

*****

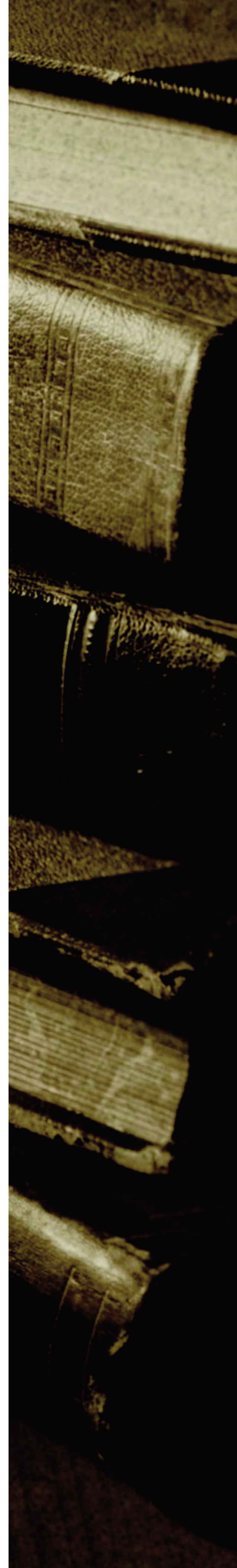
The factual background of this dispute is both long and arcane. But it must be endured to give meaning to the court's decision.

DFW International Airport opened in 1974 on the plains just north of Dallas and Ft. Worth. Before that, commercial air service to and from Dallas had been via its "in-town" airport, Love Field. When upstart Southwest Airlines proposed to re-initiate interstate service from Love in 1979, Speaker of the House Jim Wright (of Ft. Worth) stepped in to protect DFW by securing statutory restrictions on scheduled commercial flights into and out of Love. The "Wright Amendment" prohibited non-stop or even "through-ticketed" direct service by large jets between Love Field and points outside the State of Texas and the states adjoining it. In the years that followed, the Wright Amendment became more and more of a burr under the saddle of Dallas consumers and air travelers throughout the country. They regarded it as needlessly insulating DFW and the airlines that flew into and out of it (principally, American) from long-haul competition by Southwest and Love, and as effectively fostering monopolies in two submarkets, with American servicing 85% of the air travel (mostly long-haul) at DFW, and Southwest servicing 95% of the air travel (mostly short-haul) at Love. Consequently, a number of efforts were made over the years to repeal or at least chip away at the Amendment.

One creative effort took shape in the late 1990s, when Legend Airlines sought to exploit a loophole in the Wright Amendment by using smaller jets, whose seating capacity fell below Wright's constraints, to provide interstate service into and out of Love. That effort was scuttled in short order by a multifaceted attack from American Airlines and Ft. Worth. But a separate six-gate terminal had been built to handle Legend's proposed operations, and that provides the setting for the dispute that gave rise to this lawsuit.

Plaintiffs in this case acquired the former Legend terminal, or the rights to it. They proposed to bring a new airline competitor into Love Field, operating from that terminal. But, as the saying goes, timing is everything, and it did not favor plaintiffs here.

At about that same time in 2005, bills were introduced in Congress seeking the outright repeal of the Wright Amendment. If that effort had succeeded, plaintiffs' strategy might have paid off handsomely. But the immediate result of the repeal efforts was simply to ignite a smoldering war between the Cities of Dallas and Ft. Worth, Southwest and American, and their respective partisans in Congress and elsewhere. Tiring of the squabble, in early 2006, several members of Congress suggested that Dallas and Ft. Worth work together to forge a compromise – a "local solution" – that could be presented to Congress for approval and implementation. So, the two cities, along with the DFW airport authority, American, and Southwest, hammered out a joint strategy that, if it pleased no one, at least gained grudging acceptance from all. The agreement, finalized on July 11, 2006, provided for immediate repeal of Wright's "no-direct-service" restrictions and allowed through-ticketing of direct flights between Love and all other destinations in the U.S., as long as the flight made an intermediate stop in Texas or one of several other contiguous or nearby states. Non-stop long-haul service, however, would be delayed for another 8 years. Significant restraints were imposed on Love's capacity, with the agreement calling for the reduction of available gates there from 32 to 20 – including the demoli-



tion of the former Legend terminal held by plaintiffs. The 20 surviving gates were allocated by agreement – 16 to Southwest, 2 to American, 2 to another competitor – and the Southwest and American gate leases were extended to 2028. Southwest effectively promised not to invade American's turf at DFW: it agreed to give up one of its allocated gates at Love for each gate it opened at DFW. The agreement, in sum, (a) embodied express market divisions and agreements not to compete between horizontal competitors, (b) further entrenched the American and Southwest submarket monopolies, and (c) created significant barriers to competition by potential new entrants. Absent some sort of immunity, that agreement clearly was per se illegal (as a leaked internal DOJ memo apparently concluded).

Meanwhile, when plaintiffs neared the deal that would have put a new airline into their terminal in early summer, 2006, Dallas's mayor publicly cautioned against such an arrangement, given the impending agreement among the defendants here, and their intent to seek congressional endorsement of their accord. Plaintiffs' airline suitor, predictably, walked away. So, plaintiffs filed suit, alleging violations of Sherman Act Sections 1 and 2, as well as certain state law claims.

In the fall of 2006, not long after the defendants reached their agreement, Congress enacted the Wright Amendment Reform Act of 2006. The Reform Act expressly directs the accomplishment of a number of the elements of the agreement – such as the reduction of gates at Love Field from 32 to 20 – and explicitly requires the City of Dallas and the FAA to oversee operations at Love in accordance with "the contract dated July 11, 2006." Congress rejected requests to include an express exemption from the antitrust laws for the participants in the agreement, but it also declined an antitrust "savings clause" proposed in the House. More than one member of Congress observed that the overall result was an implicit grant of immunity, and even noted that it meant the death knell for this very lawsuit.

*****

For all the twists and turns of the factual setting, the legal analysis here was relatively simple, straightforward, and predictable.

The district court dismissed the case under FRCP 12(b)(6). Citing *Bayou Fleet Inc. v. Alexander*, 234 F.3d 852 (5th Cir. 2000), the court recognized that *Noerr* and most of the other arguments raised by defendants were affirmative defenses – i.e., that *Noerr* provided immunity from liability, but not from suit. Nevertheless, it held that 12(b)(6) dismissal is appropriate even on the basis of a defense, such as *Noerr*, if that defense "appears clearly on the face of the pleadings" and the documents attached to those pleadings (including, here, the agreement among the defendants and certain public statements in connection with it). The court had little difficulty deciding that, in this case, the *Noerr* defense did appear clearly in the pleadings.

First, the court acknowledged that even if the defendants' conduct, intentions, and agreement were anticompetitive, the "essence" of the *Noerr* doctrine was insulation from antitrust liability for efforts to secure government action, even where the result sought was anticompetitive and the efforts to achieve it were motivated by anticompetitive intent. It found that both the agreement and the related public statements here indisputedly demonstrated that the agreement and the efforts leading to it were dedicated to seeking congressional action – repeal or modification of the Wright Amendment – that the core of the defendants' actions in fact had been invited by Congress, and that the ultimate agreement was expressly made subject to congressional approval.

So, it dismissed any suggestion that the sham exception applied here. Further, the court noted the Supreme Court's rejection in *Omni* of a "conspiracy exception" to *Noerr*, and therefore found that *Noerr*'s protections extended to all the defendants. Finally, the court held that all the defendants' public statements and conduct leading to and in connection with the agreement, like the agreement itself

and the direct communications with Congress, were in aid of their overall goal of successfully petitioning the government.

With respect to the defendants' conduct in effectuating the agreement, the court articulated yet another basis for dismissal. The court ruled that "the Reform Act plainly and unambiguously incorporates all the rights and obligations of the Contract," and in fact "compels defendants to implement the terms of the Contract." Consequently, citing the Second Circuit's decision in *Alpha Lyracom Space Comm'ns, Inc. v. Comm'ns Satellite Corp.*, 946 F.2d 168 (2d Cir. 1991), the court held that the more specific directives of the Reform Act effectively embody an exception to the more general provisions of the Sherman Act, such that no antitrust liability can flow from the defendants' conduct done pursuant to the Reform Act.

The court closed its opinion by declining to exercise supplemental jurisdiction over plaintiffs' state-law claims. In addition, it found it unnecessary even to address defendants' arguments that some or all of their conduct also was immunized by the state action doctrine and by the Local Government Antitrust Act of 1984.

[Thanks to Ken Carroll]

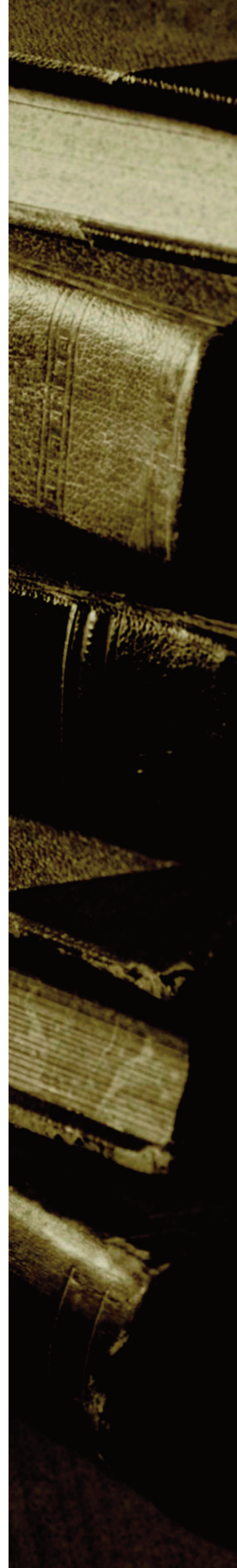
Louisiana Wholesale Drug Co., Inc., v. Aventis Pharmaceuticals, Inc., No. 07 Civ. 7343, 2008 U.S. Dist. LEXIS 3611 (S.D.N.Y. Jan. 18, 2008).

The district court in the Southern District of New York recently denied a Rule 12(b)(6) motion to dismiss the Section 2 claim of a generic drug manufacturer made against a brand-name manufacturer for filing what it alleged was a "sham" citizen petition designed to delay FDA approval of plaintiff's ANDA and thus extend and maintain the brand-name manufacturer's monopoly.

Plaintiff alleged that Aventis filed a sham citizen petition "on the eve" of final approval, one year after the generic manufacturers of leflunomide submitted their ANDAs to the FDA. *Id.* at *5-6. Defendants sought dismissal, maintaining that the petition was not a sham, but rather was legitimate petitioning activity pursuant to FDA regulations immunized under the *Noerr-Pennington* doctrine. *Id.* at *3. The court stated the Twombly standard thus: "While detailed factual allegations are not needed, they must be enough to raise a right to relief above the speculative level on the assumption that all of the complaint's allegations are true to survive a Rule 12(b)(6) motion to dismiss." *Id.* at *7-8 (citing *Bell Atlantic Co. v. Twombly*, 127 S. Ct. 1955, 1964 (2007)).

Observing that a "valid attempt to procure government action, even when initiated to attain a competitive advantage, is protected," the court explained that "*Noerr-Pennington* immunity is not absolute; for instance, it does not protect the filing of sham litigation" *Id.* at *10. Thus, according to the court, "Aventis's petition must have had no reasonable chance of success and must have been directed at harming the generic manufacturers' interests in some manner distinct from preventing any potential improper labeling of the generic leflunomide." *Id.* at *13. Plaintiff alleged that Aventis "sought to block the approval of the generic ANDAs not because of the health concerns, but solely to delay and impede approval of generics so as to maintain its monopoly over the branded leflunomide market." *Id.* at *14.

Quoting an FDA letter rejecting Aventis' citizen petition as "unfounded," the court held that at the motion to dismiss stage, it could not be established that the defendants were entitled to *Noerr-Pennington* immunity. *Id.* at *16 & n.2. As stated by the court: "The complaint and limited administrative record produced thus far demonstrates that there are triable issues of fact concerning the reasonability and viability of Aventis's Citizen Petition . . . . [I]f Louisiana Wholesale can establish that Aventis never intended or could reasonably expect to affect FDA labeling policy with respect to the five



ANDAs, and filed the Petition solely to delay or impede the approval of generics, *Noerr-Pennington* immunity will be unavailable. Upon this record, Louisiana Wholesale's claim is entitled to proceed." *Id.* at *17.

The court denied defendants' Rule 12(b)(6) motion on antitrust injury and standing grounds as well.

[Thanks to Peter Barile]

***Estrada v. City of San Luis*, No. CV-07-1071, 2007 WL 4025215 (D. Ariz. Nov. 15, 2007).**

The District of Arizona in November applied the *Noerr-Pennington* doctrine outside the federal antitrust context to dismiss claims for negligence, intentional interference, intentional infliction of emotional distress, invasion of privacy, false light, and defamation, among other state law claims.

In May 1998, plaintiffs, former Chiefs in the City Fire Department, terminated one of the defendants from his job in the City's fire department. That defendant subsequently was elected to the City Council. Upon being elected, the defendant allegedly instructed his co-defendant (who had a contract with the City to provide ambulance services) to file a complaint with the City falsely accusing plaintiffs of violating the terms of the contract. The filing of the complaint was to be a quid pro quo for the City's-renewal of the co-defendant's contract, over which the new Councilman had authority. In response to the letter, the City began a "results-oriented" investigation that ultimately led to plaintiffs' terminations.

Plaintiffs alleged that the letter was tortious, but defendants moved to dismiss on *Noerr-Pennington* grounds. Citing a line of cases applying *Noerr* outside the federal antitrust context, the court applied *Noerr* to plaintiff's state law claims. The court held the filing of the letter, despite being allegedly false, to not fall within the sham exception, under *Omni*, as the petitioning conduct was directed to the legislative, as opposed to the judicial branch.

[Thanks to Peter Barile]

Noerr-Pennington *and The State Action Doctrine*

***Sanders v. Brown*, 504 F.3d 903 (9th Cir. 2007).**

The Ninth Circuit is the latest Circuit Court of Appeal to evaluate the Tobacco Litigation Master Settlement Agreement ("MSA"). The court followed the lead of the Sixth Circuit, holding that the Sherman Act does not preempt the MSA. The court further held that the tobacco companies are entitled to immunity under *Noerr*, and that the State of California is entitled to state action immunity.

In 1998, a majority of the states and territories settled their lawsuits against the four dominant tobacco companies by entering into the MSA, which generally provides that each of the four major manufacturers ("OPMs") must make an annual payment, directly related to the manufacturer's market share, to the settling states. Manufacturers who chose to join the MSA subsequently ("SPMs") need not make any payment to the states, so long as each SPM's market share remains at or below the greater of its 1998 market share or 125% of its 1997 market share. The plaintiff alleged that, in order to ensure that California received the maximum payout under the MSA, the state enacted the

Qualifying Act, providing that any manufacturer that did not participate in the MSA ("NPM") would be required to pay into escrow an amount equal to the amount that the NPM would be required to pay if the NPM were a party to the MSA. California also enacted the Contraband Amendment, prohibiting a tobacco company from selling cigarettes in the state, unless the manufacturer complies with the MSA or the Qualifying Act.

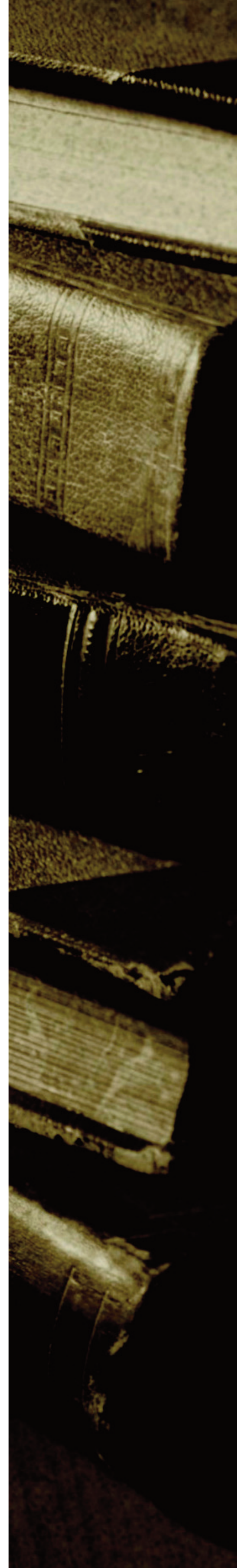
The plaintiff, a smoker, alleged that this scheme created a cartel, permitting participating tobacco companies to raise their prices without fear of losing market share because increases in market share are penalized by the MSA and implementing statutes. Therefore, when one tobacco company raises its price, all others follow suit in order to maintain their relative market shares. These effects allegedly create a horizontal output-restriction cartel. The plaintiff argued that the scheme was preempted by the Sherman Act, that the defendant tobacco companies illegally fixed cigarette prices, evidenced by the parallel price increases, and that California had violated the Sherman Act.

Relying on *Fisher v. City of Berkley*, the court first held that the Sherman Act did not preempt California's implementation of the MSA, because the Qualifying Act and the Contraband Amendment did not "mandate or authorize conduct that in all cases violates the federal antitrust law." The court recognized that the statutes pressure the NPMs to charge higher prices than they otherwise might, as those manufacturers must factor in the amounts required under the MSA or the implementing statutes. This effect, however, did not force the NPMs to peg their prices to those companies participating in the MSA, nor did it bar market entry.

The plaintiff also argued that the tobacco defendants used the MSA and implementing statutes to create a price-fixing cartel. The court held that, under *Noerr*, the tobacco defendants were immune for the violations alleged by the plaintiff. The court recognized that the Supreme Court has never held that a settlement agreement could constitute petitioning activity protected by *Noerr*. Nonetheless, the court found that the "act of negotiating a settlement with a state undoubtedly is a form of speech directed at a government entity." Further, the court observed that imposing liability on a person for negotiating a settlement would discourage settlements, and that the state attorneys general, as executive officers, have the authority to restrain trade so long as the restraint is not preempted by the Sherman Act.

The plaintiff further argued that, based on *Cantor v. Detroit Edison Co.*, even if the companies are entitled to antitrust immunity for negotiating the settlement, they were not entitled to immunity for increasing prices after the MSA. The court disagreed, stating that the lower courts have narrowly interpreted *Cantor*. Further, the court held that private parties are immune from antitrust liability for "injuries that result 'directly' from valid government action taken on the petitioner's behalf." Thus, because the plaintiff's injury—supra-competitive cigarette prices—was caused directly by the operation of the MSA and enabling statutes, the cigarette manufacturers were immune under *Noerr*. The court did note, however, that the manufacturers would not be immune if they created an output cartel subsequent to the MSA.

The plaintiff also sought relief against the State of California, asking that the court issue an injunction prohibiting the enforcement of the MSA and the implementing statutes. The state argued that its entry into the MSA and enactment of the implementing statutes were immune based on *Parker v. Brown*. The court found that a court-approved settlement negotiated by a state attorney general, such as the MSA, is "state action" under *Parker*. The court then stated that there was confusion in Supreme Court precedent concerning whether the two-pronged test *Midcal* test should be applied to the MSA scheme, or whether the test was irrelevant because the state as sovereign is always immune from antitrust liability. The court ultimately held that the state's sovereign acts are always immune from antitrust liability, and therefore no *Midcal* analysis is necessary.



Finally, the court addressed the argument that the MSA is a hybrid restraint. Relying wholly on its previous holding—that the MSA does not delegate power to private parties to fix prices—the court found that the MSA could not be classified as a hybrid restraint.

The Ninth Circuit's decision further exacerbates the split among the Circuits concerning the propriety of the MSA and the proper method of analyzing anticompetitive state legislation. The court noted that its decision conflicts with decisions from the Second and Third Circuits.

[Thanks to Greg Garrett]

Mercatus Group LLC v. Lake Forest Hospital, No. 07 C 2042, 2007 U.S. Dist. LEXIS 84920, (N.D. Ill. Nov. 15, 2007).

In *Mercatus Group*, the district court considered motions to dismiss a complaint brought by Mercatus, a developer and manager of physician centers that compete with hospitals in the delivery of diagnostic imaging services, against defendants Lake Forest Hospital ("LFH"), the Village of Lake Bluff, Illinois ("Village"), and certain individuals who were trustees of the Village. Among a number other claims, Mercatus alleged that through its conduct in connection with zoning permit hearings and otherwise, LFH sought to monopolize the diagnostic medical imaging market in eastern Lake County, Illinois and exclude Mercatus from that market in violation of §§ 1 and 2 of the Sherman Act. *Mercatus Group*, 2007 U.S. Dist. LEXIS 84920, at *1-*2. In an opinion that relied largely on analysis under the *Noerr-Pennington* and *Parker* doctrines, the district court, inter alia, declined to dismiss the antitrust claims in their entirety. *Id* at *3.

Mercatus alleged that it began plans to build a physician center in Lake Bluff, three miles away from LFH, and that zoning ordinances automatically permitted the property it sought to develop to be used for this purpose, subject only to site plan approval from the Village. *Id.* Initially, the Village did not raise the need for any special permits. *Id*. at *3. However, after one of the Village trustees who also was a physician at LFH informed Mercatus that he would oppose the physician center, the Village notified Mercatus that a special use permit was needed, requiring approval of the Village board of trustees (the "Village Board"). *Id.* at *4. Mercatus alleged that although the Village Board initially granted the requisite permission, LFH intervened by misrepresenting information about the proposed development to the Village Board and others, and engaging in so-called "non-petitioning" conduct such as intimidating physicians to back out of commitments to work for Mercatus, causing the Village Board to deny upon reconsideration special use permission. *Id.* at *5-*6.

As to the antitrust claims, the court, construing the allegations in a light most favorable to Mercatus, held, inter alia, that (i) LFH's efforts to petition the Village Board members to change their votes occurred in a setting that was arguably adjudicatory in nature, and therefore not barred by the *Noerr-Pennington* doctrine on a motion to dismiss; (ii) Mercatus could not claim that LFH's petitioning conduct fell within the "sham" exception to *Noerr-Pennington* immunity; and (iii) LFH could not avail itself of state action immunity on the motion to dismiss. *Id.* at *11-*44.

LFH argued that its conduct in petitioning the Village Board regarding Mercatus' permit application was not a violation of the Sherman Act under the *Noerr-Pennington* doctrine, which recognizes that "those who petition government for redress are generally immune from antitrust liability." *Id.* at *12 (quoting *Professional Real Estate Investors, Inc. v. Columbia Pictures Indus*., 508 U.S. 49, 56 (1993)). The court rejected this argument and refused to dismiss antitrust claims based on these allegations, holding instead that because the Village Board arguably acted in an adjudicatory capacity instead of a

legislative capacity, any misrepresentations by LFH would not necessarily be immunized under *Noerr-Pennington*.

In reaching this conclusion, the court observed that although *Noerr-Pennington* immunity exists in certain circumstances even if the petitioning at issue involved misrepresentations, the doctrine holds that misrepresentations in the adjudicatory (and not legislative) context are not immunized. *Id.*, at *15 (citing *Metro Cable Co. v. CATV of Rockford, Inc.*, 516 F.2d 220, 226-28 (7th Cir. 1975) and *California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508, 513, 516 (1972)). The court then found that, like the proceedings at issue in *Kottle v. Northwest Kidney Centers*, 146 F.3d 1056 (9th Cir. 1998), the Village Board proceedings bore many indicia of an actual adjudicatory proceeding:

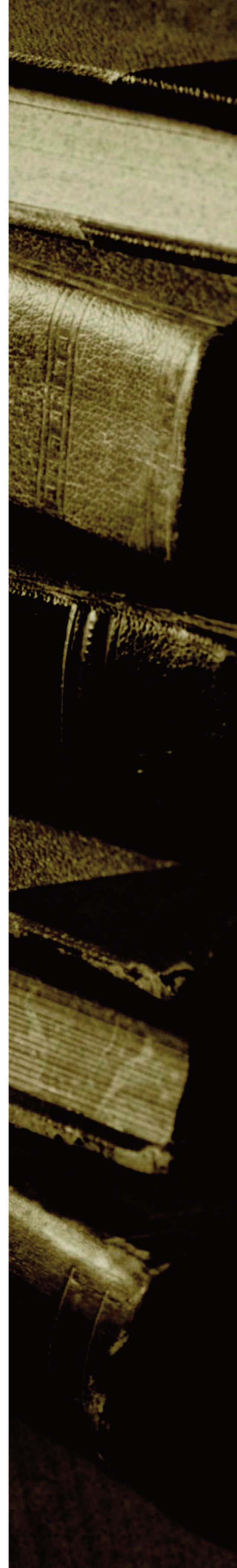
"[P]ursuant to Village ordinance, the site plan applicant first submits specified materials to the [Village's Architectural Board of Review ("ABR")] for its review. The ABR conducts a public hearing during which any interested party may present evidence. The ABR makes a decision and the ordinance then provides for review of the ABR's decision by the Village Board, which must notify the applicant in writing of the time, date and location of the Board meeting at which the site plan is to be reviewed by the Board. The favorable vote of two-thirds of the Trustees is required to reject the ABR's decision and either approve a site plan disapproved by the ABR or vice versa. Further, the Board cannot deny any site plan unless it issues a resolution that includes findings of fact detailing the specific standards under 10-1-9(E) with which the site plan fails to conform. Moreover, the court notes that Mercatus alleges that counsel was present at the Board meetings."

Id. at *21-*22. Based on these allegations, the court found that "it is plausible that the Village Board was acting in an adjudicatory capacity instead of a legislative capacity." *Id.* at *22-*23.

The court rejected arguments by Mercatus that *Noerr-Pennington* immunity also should not apply because LFH's conduct fell within the general "sham exception" to the doctrine, which does not extend immunity to situations in which persons use the government process, as opposed to the outcome of that process, to directly harm or harass another party. *Id.* at *25-*30. The court applied the two-pronged test set forth in *Professional Real Estate Investors*, which requires, for the sham exception to apply, that the efforts (i) are objectively baseless, and (ii) conceal an attempt to interfere with a competitors' business relationships through the use of the governmental process as an anticompetitive weapon. *Id.* at *26 (citing *Professional Real Estate Investors*, 508 U.S. at 60-61). It rejected Mercatus' claim that LFH's conduct fell within the sham exception because the plaintiff failed to allege facts showing that LFH was not genuinely attempting to obtain legitimate government action in its favor. *Id.* at *30.

After declining to dismiss at least some of LFH's alleged "non-petitioning" conduct on antitrust standing grounds, *id.* at *30-*35, the district court also held that LFH could not avail itself of immunity from suit under the *Parker* doctrine, pursuant to which actions of a state to restrain trade are immune from the antitrust laws. *Id.* at *36. First, the court observed that municipalities such as the Village of Lake Bluff, like states, are entitled to immunity under the antitrust laws pursuant to the *Parker* doctrine, so long as they are "acting pursuant to a 'clearly articulated and affirmatively expressed' state policy to displace competition." *Id.* at *37 (quoting *Fuchs v. Rural Elec. Convenience Co-op. Inc.*, 858 F.2d 1210, 1214 (7th Cir. 1988)). Here, the Village was entitled to antitrust immunity because it found that displacement of competition was the foreseeable result of an Illinois statute that permitted municipalities to "classify, regulate and restrict the location of trades and industries and the location of buildings designed for specified industrial, business, residential, and other uses" and "prohibit uses, buildings, or structures incompatible with the character of such districts." *Id.* (quoting 65 ILCS 5/11-13-1(4)).

The court then noted that this immunity can extend to private parties under circumstances where the private party demonstrates that (i) the state clearly authorized its conduct, and (ii) the state su-



pervised the allegedly anticompetitive policy. *Id.* at *39 (citing *Fuchs*, 858 F.2d at 1215). After noting that the parties did not address this two-part test, the district court rejected LFH's argument, under cases such as *Michigan Paytel Joint Venture v. City of Detroit*, 287 F.3d 527, 538 (6th Cir. 2002) and *Zimomra v. Alamo Rent-A-Car, Inc.*, 111 F.3d 1495, 1500-01 (10th Cir. 1997), that the Village was the "effective decisionmaker" in denying Mercatus the requisite development and site plan approvals, thereby also entitling LFH to state action immunity. *Id.*, at *39-*41. The court concluded it was inappropriate to dismiss on the ground of state action immunity because "it is plausible that Mercatus could demonstrate that LFH was the effective decisionmaker." *Id.* at *44.

[Thanks to Paula Garrett Lin]

Justice v. Town of Cicero, No. 06 C 1108, 2007 WL 2973851 (N.D. Ill. Oct. 10, 2007).

In *Justice v. Town of Cicero*, the Town of Cicero, Illinois moved to dismiss a complaint filed by two plaintiffs against the Town and a number of its employees, alleging civil rights violations pursuant to 42 U.S.C. § 1983 arising out of the execution of a search warrant, as well as an antitrust violation brought by plaintiff John Justice based on the Town's water department rates and billing practices. The district court granted the motion to dismiss the complaint in its entirety. *Id.*at *9.

In support of his antitrust claim, Justice contended that the Town (i) had a monopoly over the water supply; (ii) charged minimum fees on two water meters and a late fee of approximately 33 percent; and (iii) tied extra meters, minimum usage charges, usurious late charges, and sewer charges to the basic supply of water. *Id.* at *7. Justice did not identify which provisions of the antitrust laws the Town had violated. *Id.* The district court held that these allegations failed to meet the minimum pleading standards of Federal Rule of Civil Procedure 8(a)(2). *Id.*

In dismissing the antitrust claim, the court, citing to *Parker v. Brown*, 317 U.S. 341, 350-51 (1943), noted that the *Parker* doctrine exempts states, acting through their legislatures, from antitrust liability arising from anticompetitive conduct. *Id.* at *7. It then observed that under the *Parker* doctrine, local governments were beyond the reach of the antitrust laws so long as they can demonstrate that their anticompetitive activities are authorized by the state "'pursuant to state policy to displace competition with regulation or monopoly public service.'" *Id.* at *7 (quoting *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 39 (1985)).

In this case, the court found sufficient basis upon which to apply the *Parker* doctrine. First, the Illinois legislature granted local governments such as the Town of Cicero the authority to build and operate their own waterworks and to fix and collect water rates as deemed necessary or expedient. *Id.* (citing 65 ILCS 5/11-125-3). Second, the Illinois legislature had codified the *Parker* state action exemption for local governments. *Id.* (citing 50 ILCS 35/1). The district court concluded that due to these statutory provisions, the plaintiff's assertions failed to state any antitrust violation against the Town of Cicero:

> Plaintiff's bare assertions are belied by both 65 ILCS 5/11-125-3, which expressly grants local governments the power to "make all needful rules and regulations concerning the use of water supplied by the waterworks of the city or village" and to fix and collect such water rates "as the corporate authorities may deem necessary or expedient," and 50 ILCS 35/1, which exempts local governments from federal antitrust laws "to the extent that their activities are either (1) expressly or by necessary implication authorized by Illinois law or (2) within traditional areas of local government activity. *Id.* at *8.

[Thanks to Paula Garrett Lin]

The State Action Doctrine

Mobile County Water, Sewer, and Fire Protection Auth. v. Mobile Area Water and Sewer Sys., 2007 WL 3208587 (S.D. Ala. Oct 29, 2007).

The Southern District of Alabama denied plaintiff's application for a TRO, due to the likelihood of success of the affirmative defense of state action immunity. Plaintiff, a water service provider sued defendant, a water and sewer service provider dominant in the sewer service market in the area, for tying its water service to its sewer service, thereby allegedly freezing plaintiff out of the water service market. The court held that a state statute, which authorized the defendant to "combine" water and sewer operations, represented a clearly articulated policy, the foreseeable result of which was that companies would tie water services to sewer services and thus foreclose competing water providers from the marketplace. Accordingly, the court held that the state action immunity doctrine would bar plaintiff's claims and so denied its request for relief.

[Thanks to Peter Barile]

The Filed Rate Doctrine

Wah Chang v. Duke Energy Trading and Marketing, No. 05-55367, 2007 U.S. App. LEXIS 26797 (9th Cir. Nov. 20, 2007).

Continuing a long line of cases in which antitrust claims arising from the 2000-2001 California energy crisis have been dismissed on filed rate grounds, the Ninth Circuit affirmed the dismissal of a retail electricity purchaser's antitrust claims under the filed rate doctrine.

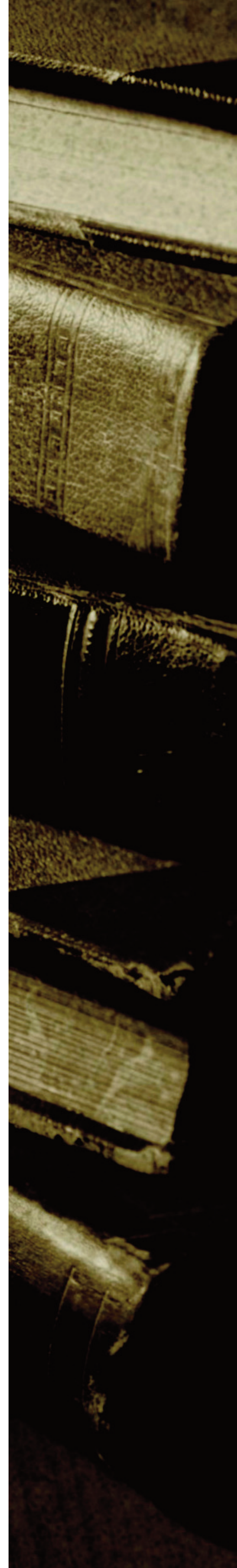
Plaintiff alleged it purchased electricity for its plant in Oregon at retail from PacifiCorp, a purchaser of electricity in the wholesale spot market. By contract, plaintiff's rates were indexed to the wholesale spot market price at the California-Oregon border, such that the price increases in the wholesale market caused by defendant energy companies' alleged anticompetitive market manipulation were passed on to plaintiff.

The court described the filed rate doctrine to be "a form of deference and preemption, which precludes interference with the rate setting authority of an administrative agency, like FERC." *Id.* at *5-*6. The court further explained that the "filed rate doctrine's fortification against direct attack is impenetrable," when it comes to FERC-established rates. *Id.* at *7. As "the rates in question were, as a matter of law, a result of tariffs approved by" FERC, the court held by a 2-1 majority that the filed rate doctrine shielded defendants from any antitrust liability. *Id.* at *4.

Disagreeing with this fundamental assumption of the majority, Judge Pregerson would have reversed due to the fact that the increased rates paid by plaintiff actually were set by contract and were not a result of any FERC filed rates—rates that were not challenged by plaintiff. Framing the question presented as "whether the filed rate doctrine bars the claims of retail electricity consumers who do not directly challenge FERC's established rates," Judge Pregerson questioned whether FERC would have jurisdiction over plaintiff's claims and by extension the applicability of the filed rate defense. *Id.* at *16-*17.

The strong dissent may portend an en banc consideration of the case.

[Thanks to Peter Barile]



E&J Gallo Winery v. Encana Corp., 503 F.3d 1027 (9th Cir. 2007).

The Ninth Circuit in September affirmed the decision of the United States District Court for the Eastern District of California, holding that E&J Gallo Winery ("E&J") could pursue its state and federal claims against Encana Corporation for alleged manipulation of the natural gas market. The court held that the filed rate, or *Keogh*, doctrine did not bar E&J's suit.

E&J entered into a contract with Encana, an energy trader, to purchase natural gas for use at E&J's wineries and glass plant. Although the contract did not specify how the parties would calculate the price of natural gas, in practice, the price was pegged to indices reported in two trade publications. The indices represent compilations of reported sales prices, which are informally reported to the publications by the traders themselves. After an investigation, the Federal Energy Regulatory Commission ("FERC") found that, in some instances, the information used as the basis for the indices was misreported. E&J alleged that Encana agreed with its competitors to manipulate the indices by setting an inflated basis price for natural gas, to misreport information to the publications, and to engage in sham trades to artificially inflate the reported demand for natural gas.

Since the mid-1990s, the natural gas market has been substantially deregulated. For wholesale sales, FERC's authority to set rates has been limited to those sales preceded by a sale to a pipeline, local distribution company, or retail customer. Further, FERC has issued blanket certificates permitting sales of natural gas to all persons except interstate pipelines, thus suspending the rate-filing requirements for such sales.

Encana moved for summary judgment, arguing that the filed rate doctrine precluded E&J from recovering under any theory. The court first held that, to the extent that Congress authorized FERC to set rates for natural gas, and to the extent that FERC exercised its authority to do so, the use of those rates cannot serve as a basis for a lawsuit under the federal antitrust laws, nor can those rates support a state law claim. The court also stated that the filed rate doctrine can apply to market-based rates under appropriate circumstances, so long as the regulator "continues to engage in regulatory activity." Because FERC continues to maintain oversight of the natural gas market, the court found that the filed rate doctrine continues to apply in the natural gas market, even though FERC's regulation was executed "with a light hand." Relying on this holding, the court found that E&J could not pursue an action based on its retail purchases of natural gas, because the market-based wholesale rates are subject to FERC's jurisdiction, and FERC's blanket certificates are insufficient to remove the rates from the coverage of the filed rate doctrine.

E&J could, however, recover under its theory that the indices were manipulated in violation of the Sherman Act. First, the court noted that not all the transactions comprising the indices were subject to FERC's jurisdiction. Next, the court held that to the extent the indices consist of transactions beyond FERC's jurisdiction, the filed rate doctrine is inapplicable to manipulation of the indices. E&J was precluded, however, from challenging the indices to the extent that they are made up of transactions subject to FERC's authority.

[Thanks to Greg Garrett]