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OPINION

Class actions: an unbridgeable Atlantic divide

For nearly a century, the US has encouraged private actions for damages as a primary means of enforcing competition law. This idea has never caught on in Europe. Although the European Court has said that damages must be available for the civil wrong, these are awarded under national laws that view incentives to sue as a step too far.

At EU level, the consultation launched in 2005 has yet to yield any legislative proposals. The 2008 white paper proposed representative actions and opt-in collective actions where claimants first signify their interest in suing. The Commission would like to facilitate these options, but only if the result "complements, but does not replace or jeopardise, public enforcement".

Until 29 January, opt-out actions – where a lawsuit is brought on behalf of all potential claimants except those who explicitly decline to join in – were still anathema. On that day, the UK government tentatively embarked on a flirtation with the US model.

It cannot go beyond flirtation because of the many limits planned for the opt-out: restriction to claimants or their genuine representatives – not law firms, third party funders or special purpose vehicles; restriction to UK-domiciled claimants, albeit with others able to opt in; no treble or exemplary damages; no contingency fees; application of the loser-pays principle to legal costs.

A rather subtler limit when compared with the US is the exclusion from damages of any excess price that has been passed on to customers. English law confines damages to actual losses. This is reasonable enough but it would mean that the opt-out action would be futile for many business claimants – potentially its most vigorous users.

Unfettered by all these constraints, US class actions are thriving not only as a follow-on to government action but also as autonomous enforcement. They account for 90% of litigation – a total that includes all Department of Justice (DoJ) cases. According to the American Antitrust Institute, private antitrust actions now outnumber DoJ cases 25:1. In a snapshot of 40 big successful cases from 1990-2008, 15 (37.5%) were not preceded by any government action.

This is not just a privatisation of antitrust enforcement. It is also an issue of principle that those harmed by violations of federal law must be able to vindicate their federal rights. An amicus brief presented to the Supreme Court by the DoJ and the Federal Trade Commission (FTC) in January argues this with some force.

The case arose from a standard-form contract that referred all disputes between merchants and a charge card issuer to arbitration, including claims under section 1 of the Sherman Act *(American Express Co v Italian Colors Restaurant, Docket No 12-133)*.

Redress may be provided by arbitration rather than litigation, and a class arbitration is acceptable as long as all the parties agree to it. Here, however, merchants were forbidden to combine in a collective reference, so each had to incur legal costs out of all proportion to their potential recovery.

To supplant litigation, the brief argues, an arbitration agreement is only valid if it allows federal rights to be vindicated effectively. Arbitration that is bound to cost far more than the claim for damages cannot be effective.

In the absence of the incentives offered by the US litigation system, the timid UK proposal will not unleash the animal spirits of litigants or lawyers. It may be no more than a move to goad the European Commission into action. Some reflections on effective vindication of the right conferred on businesses and consumers by the European Court would be welcome.

Celia Hampton

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Standing up for US beer

The US Department of Justice (DoJ) has started legal proceedings to block Anheuser-Busch InBev’s proposed $20.1bn takeover of Mexico’s Grupo Modelo. According to the DoJ, the deal would substantially reduce competition in the market for beer in the US, with the result that consumers would pay more for beer and have less choice.

Anheuser-Busch InBev (ABI) is the world’s largest brewer. Based in Leuven, Belgium, it had revenues of approximately $39bn in 2011. Modelo is based in Mexico City and in 2011 had revenues of approximately $7bn.

In the US, ABI and Modelo control approximately 46% of annual sales between them. MillerCoors, the second largest beer firm in the US, notches up about 29% of nationwide sales. And this is a big market. Last year, Americans spent at least $80bn on beer, with ABI’s Bud Light the bestselling brand in the States and Modelo’s Corona Extra the bestselling import. Consequently, even a small increase in the price of beer could cost American consumers billions of dollars.

Prices in the US beer market are increased by strategic interaction between the largest brewers, including ABI and MillerCoors. Normally, ABI acts as the price leader, increasing prices annually in the various segments of the US beer market industry. MillerCoors and other brewers have usually joined the ABI price increases, while Modelo has not. Instead, it has priced aggressively, thereby pressurising ABI into maintaining or even lowering prices, especially in certain parts of the country. That makes Modelo a particularly important competitor in the US market and, if it disappears as a result of the takeover, strategically co-ordinated pricing will become a whole lot easier in the future.

ABI had tried to allay the DoJ’s concerns by selling Modelo’s 50% stake in Crown Imports, its US distributor, to its Crown joint venture partner Constellation Brands. As the sole distributor of Modelo’s beer, Constellation would then have control over pricing. The DoJ was unimpressed, saying it was not enough to prevent the takeover from harming consumers.

ABI responded by saying that the DoJ’s action was “inconsistent with the law, the facts and the reality of the marketplace”. The company added that it is “confident of its position” and will “vigorously contest” the DoJ’s action in court.

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State aid for Italian airports

The European Commission has opened an in-depth investigation into an Italian scheme supporting airports in Sardinia. The investigation will look into whether the scheme is in line with EU rules on state aid.

The scheme in question is aimed at improving air services between Sardinia and the European and Italian mainland, particularly outside peak holiday periods. The way it works is that funds are given to airport operators who choose airlines meeting certain annual targets: they must provide a given frequency of service and reach a given volume of passengers on "strategic" routes. In turn, these airlines are paid by the airports. The airlines will be selected via tender.

Italy set the scheme out in a regional law dated 2010 and implementing acts have been adopted. The airports of Alghero, Cagliari and Olbia have already received advance payments through loans granted by the financial branch of the Sardinian region. And these airports have, in turn, paid air carriers, including Ryanair, for some of their services. No tender has been carried out for the selection of airlines.

Italy notified the scheme to the Commission in November 2011, saying that it was planned to come into effect in 2012 and 2013.

The Commission has taken the preliminary view that the scheme has already been implemented, in breach of the standstill obligation in article 107 of the treaty on the functioning of the European Union. Article 107 requires member states to get Commission approval before implementing state aid projects.

In addition, although Italy contends that the compensation paid under this scheme is intended to remunerate airports for the discharge of a public service obligation, the Commission doubts whether this arrangement meets the criteria of EU rules on services of general economic interest. It is looking, in particular, at whether it meets the criteria on a clear definition of the public service remit and the selection of the service at the least cost.

The Commission also doubts whether the measure in favour of air carriers complies with the specific state aid rules for the aviation sector.

Italy has been invited to respond to the Commission's position and comments may also be submitted by other member states and any interested third parties.

The investigation takes place against the background of the Commission's ongoing review of its 2005 guidelines on state aid to airlines and airports, and several investigations in the air transport sector in various member states, including another investigation involving Alghero airport.

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Telefónica and Portugal Telecom fined

The European Commission has fined Telefónica and Portugal Telecom for agreeing to an illegal non-compete contract clause.

The two companies had agreed not to compete with each other for business across the Iberian peninsula, with Telefónica keeping out of Portugal and Portugal Telecom keeping out of Spain.

Telefónica has been fined €66.9m and Portugal Telecom €12.3m. Their agreement was in breach of article 101 of the treaty on the functioning of the European Union which prohibits anticompetitive agreements.

In 2010, Telefónica bought the Brazilian mobile operator Vivo, which was until then jointly owned by both Telefónica and Portugal Telecom. The companies inserted a clause in this contract indicating that they would not compete with each other in Spain and Portugal as from the end of September 2010.

The parties terminated the non-compete agreement in early February 2011, after the Commission opened antitrust proceedings.

Although non-compete agreements are regarded as among the most serious breaches of competition rules, in setting the level of fines, the Commission took into account the relatively short duration of the infringement and the fact that the illegal agreement was not kept secret by the parties.

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OFT reports on personal bank accounts

Following a review of personal current accounts in the UK, the Office of Fair Trading (OFT) says that major changes in this market are still needed.

“Personal current accounts are critical to the efficient functioning of the UK economy, said OFT chief executive, Clive Maxwell. “Despite some improvements, this market is still not serving consumers as well as it should.”

The personal current account market in the UK is worth £9bn. The OFT’s review is part of its ongoing programme of work on retail banking and follows its 2008 market study, which found that the market for personal current accounts was not working well for consumers. At that time, it was difficult for customers to work out how much their account was costing them and there were particular concerns about unarranged overdraft charges.

Although customers have saved an estimated £928m a year from a fall in unauthorised overdraft charges over the last five years, other concerns remain: the major banks have increased their share of the market, entry by new competitors remains infrequent and consumers still only rarely switch to an alternative provider.

Overdraft charging structures remain too complex, according to the OFT review. And it is still hard to compare the costs of current accounts. “Customers still find it difficult to assess which account offers the best deal and lack confidence that they can switch accounts easily,” said Clive Maxwell. “This prevents them from driving effective competition between providers.”

The review finds that, overall, there is a lack of competition and low levels of innovation. Combined with customer apathy in the face of unclear costs and not much variety in the types of current accounts on offer, the picture is of a market that is not working well.

But the OFT is not recommending a reference to the Competition Commission. The review makes a series of recommendations, including further measures to make costs more transparent and switching banks easier. And over the coming months, some major changes for banks will occur, such as the sale of branches from both Lloyds Banking Group and the Royal Bank of Scotland.

The regulator plans to revisit the personal current account market by 2015.

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OPINION

Under the spotlight

A recent FTC data report reveals that oil and pharmaceutical mergers attract a lot of attention when it comes to antitrust scrutiny

*by Mike Cowie and Michael Weiner**

On 4 January this year, the US Federal Trade Commission (FTC) issued a data report on its horizontal merger investigation and enforcement record over the past 15 years. The report shows, sector-by-sector, the level of market concentration triggering FTC action, as well as the impact of other antitrust enforcement such as the presence of hot documents (see further below) and the presence of strong customer complaints.

One major feature of the report is that oil sector and pharmaceutical sector mergers stand out for antitrust scrutiny. Another important lesson is that counsel should focus even more on managing document creation and customer communications.

A systematic review of merger investigations

The FTC Bureau of Economics prepared the report using FTC staff memoranda written at the time of each merger investigation. The FTC practice on merger investigations is that the Bureau of Competition (consisting of attorneys) and the Bureau of Economics (consisting of economists) prepare separate written recommendations on each merger investigation. These staff memoranda are non-public and confidential. Typically, they contain detailed factual descriptions of the industry structure and other marketplace conditions.

In preparing the report, the Bureau of Economics reviewed all staff memoranda from second request investigations over a 15-year period and focused on horizontal merger investigations. They excluded merger investigations based on potential competition, vertical theories, or buyer power. The Bureau of Economics categorised each market based on several variables: market concentration (as measured by the Herfindahl-Hirschman Index or “HHI”); the number of significant competitors; the presence of hot documents; the presence of customer complaints; and entry conditions.

Market share standards vary by industry

The report leaves little doubt that oil is the most antitrust-sensitive industry by far. The FTC data on second-request investigations by market concentration show that 71% of oil sector second-request investigations involved markets with HHIs below 2,400. The next closest sector was grocery, at 11%. For all sectors other than oil, the rate was just 2%.

Indeed, over the past 15 years, the FTC challenged mergers in 90 markets with HHI levels below 2,000. The oil sector accounted for 100% of these. No other industry experienced an FTC merger challenge at these concentration levels. The FTC will investigate and challenge oil sector mergers with relatively low market shares.

The report shows that the FTC has not been investigating or challenging pharmaceutical sector mergers at relatively low market shares. However, when the FTC does investigate mergers in the pharmaceutical sector, it almost always brings an enforcement action. Roughly 98% of second-request investigations in the pharmaceutical field result in some enforcement action, compared to 75% for all other sectors. Even when it comes to oil, second-request investigations lead to enforcement actions at a rate of about 75%. Once the FTC initiates an investigation, pharmaceutical sector mergers are extremely likely to be challenged.

Significant competitors

In addition to tracking HHI for each investigated market, the FTC report assesses the number of significant competitors. A competitor is “significant” if it is a “close rival” (when the theory of potential harm is unilateral market power) or if it is needed for inclusion in a collusive group (when the theory of potential harm is collusion).

The report shows a significant difference in outcomes when the merger can be characterised as 5-to-4 or fewer competitors (eg 4-to-3 or 3-to-2). The FTC challenged mergers characterised as 6-to-5 at a rate of 35%. The enforcement rate jumped to 64% for mergers characterised as 5-to-4 and to 77% for 3-to-2 mergers. These results emphasise the need for counsel to assess whether the FTC is likely to view a competitor as significant, as well as the need for effective advocacy regarding competitor significance.

The “significant competitor” data also highlights the need for industry-specific advice. For example, the report shows that 100% of the enforcement actions in the pharmaceutical sector involved 5-to-4 or fewer competitors. The FTC closed all investigations of mergers with 6-to-5 or more competitors. Of the merger investigations of 5-to-4 or less, the FTC brought challenges 98% of the time. The message for the pharmaceutical sector is that 6-to-5 mergers get cleared and mergers with any fewer competitors are very likely to be challenged.

Hot documents may be fatal

The FTC report also provides evidence on the impact of hot documents. The FTC defines “hot documents" as those in which the parties predict the merger will lead to an adverse price or non-price effect (for example, a capacity restriction). The presence of hot documents, so defined, is relatively infrequent – the FTC uncovers hot documents in just about 10% of the investigations. When they do arise, however, hot documents may doom the transaction. The FTC brought enforcement actions in 89% of the investigations in which hot documents were present.

This is an area where counsel can make a huge difference. The FTC defined hot documents so as to exclude ordinary course of business documents such as strategic or marketing plans. For instance, a marketing plan describing the merging parties as close rivals is not treated as a hot document for the purposes of this report. Rather, the report focuses on documents analysing the likely impact of the merger. These typically come from the board, senior management, business development personnel, bankers, or others closely involved in the negotiation or approval of the merger. Counsel should provide early education and ongoing oversight of the deal team communications.

Strong customer complaints may also be fatal

A similar picture emerges with respect to the data on "strong customer complaints" – defined as a credible customer concern that a significant anticompetitive effect would result. The FTC brought enforcement actions in 97% of the mergers involving strong customer complaints.

Counsel may face challenges to assess in advance how customers are likely to view the merger. There may be practical and legal impediments to obtaining customer views before reaching an agreement and making a public announcement. Having a post-announcement customer communications plan could be critical. Customer views may be shaped based on what they hear about the deal's impact on product offerings, pricing, personnel, synergy plans and other matters.

Establishing ease of entry may be an uphill battle

Under the merger guidelines, ease of entry may trump high market shares. The report bears this out. It shows that the FTC has closed several high market share investigations (25 markets with HHIs over 3,000) where entry was easy.

Ease of entry is a valuable card to play but it is hard to get. The report shows that the FTC found entry easy in just about 17% of the investigated markets. This indicates that the FTC is sceptical of entry arguments and that counsel should be prepared not only with carefully prepared entry arguments, but also with additional good non-entry related arguments in order to win clearance for a high market share deal.

REFERENCES

http://www.ftc.gov/os/2013/01/130104horizontalmergerreport.pdf

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