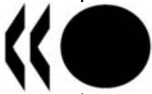

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DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

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ROUNDTABLE ON FACILITATING PRACTICES IN OLIGOPOLIES

-- Note by the United States --

This note is submitted by the Delegation of the United States to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 17-18 October 2007.

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Executive Summary

1. A "facilitating practice" is one that "makes it easier for parties to coordinate price or other behaviour in an anticompetitive way."[1]

2. The United States antitrust agencies – the Federal Trade Commission ("FTC") and the Antitrust Division of the U.S. Department of Justice ("DOJ") – analyze such practices on a case-by-case basis. Facilitating practices can, by definition, increase the incidence of horizontal coordination. That aspect is likely to be of antitrust concern. The same practices, however, may also produce efficiencies that have procompetitive effects. The agencies must balance these effects when deciding whether to bring an enforcement action.

3. Antitrust authorities need to distinguish between agreements to engage in facilitating practices and hard-core price-fixing, and to target the most severe deterrent efforts on the latter. The DOJ has sought to maintain a bright line between criminal activity – naked price-fixing – and other forms of horizontal conduct. DOJ focuses its criminal enforcement on the kinds of cases in which there is no plausible argument that defendants might have had some legitimate objective associated with their conduct. Because facilitating practices often have some plausible benefit, they are not addressed by means of criminal enforcement, although facilitating practices that are closely associated with hard-core price fixing will be of particularly high enforcement interest.

4. This submission describes specific cases in which the FTC and DOJ have assessed facilitating practices. The diverse contexts within which facilitating practices have been encountered illustrate how those practices may have different effects in different settings.

1. Introduction

5. Facilitating practices can be divided for convenience into two broad types. Some practices will facilitate agreement on the central provisions of price or output. These include things like agreements to exchange plans on future prices, or to take factory downtime. Others limit competition in collateral nonprice respects. They include restrictions on advertising or on overtime. These agreements can channel competition and thus limit the ways in which firms engage in nonprice or quality competition as a way of cheating on a price agreement. Expressed differently, one mechanism facilitates making an initial agreement on price, and the other tends to protect a price agreement that has already been reached. Regardless of its specific type, any particular facilitating agreement may produce anticompetitive effects, or efficiencies, or both.

6. The agencies assess facilitating practices in light of their individual purposes and effects. Sometimes facilitating practices may decrease competition, through such mechanisms as reducing the number of bidding variables on which the colluding firms would have to reach agreement, or helping to monitor defections from such an agreement. In other respects, however, the same practices may help to bring about beneficial efficiencies. The reduction in bidding variables may facilitate collusion, but also can help buyers to make head-to-head price comparisons, and in that respect may tend to make a market more competitive rather than less. Similarly, mechanisms to monitor defections may also tend to make prices and bidding more transparent, which under some conditions may induce greater competitive efforts by other firms. Given these complexities, the agencies must attempt to balance the procompetitive and anticompetitive effects of changes to facilitating practices that would be caused by any enforcement actions.

1. VI Areeda and Hovenkamp, *Antitrust Law*, para 1407b, at 29 (2d ed. 2003).

7. The agencies' actions have accordingly addressed facilitating practices in a number of different ways. In some cases the agencies have formally challenged facilitating practices as anticompetitive. Thus the agencies have challenged agreements to restrict comparative advertising of car prices or requiring the submission of bills only for undivided days of time. In other cases, however, the agencies have refrained from challenging facilitating practices that seemed to produce significant offsetting efficiencies. A typical case of this sort might involve restrictions on advertising that seemed reasonably calculated to prevent consumer deception or confusion. And in still other cases, the agencies affirmatively sought a remedy mandating new practices that were facilitating practices in some respects, but that appeared beneficial in other, more important ways. A case of this sort was AOL/TimeWarner, in which an FTC settlement required use of a most favoured nation clause. Such clauses can sometimes inhibit individualized negotiations, as will be discussed below, but a most favoured nation clause nonetheless appeared useful in this case as a way of preserving access to bottleneck communications networks.

8. Section 2 of this submission describes a variety of matters in which the FTC has encountered facilitating practices. These include cases challenging restraints on advertising and distribution. Section 3 discusses how the DOJ targets its criminal enforcement on hard-core cartels and then describes a civil enforcement action taken against the Airline Tariff Publishing Company, which involved both price-fixing and agreement on an information exchange mechanism that facilitated price-fixing.

2. Federal Trade Commission Cases and Policy

9. The FTC has encountered facilitating practice issues both in policy debates and in its formal enforcement of the antitrust laws. The agency's most important recent experiences have involved five situations: (1) agreed-upon elements or reference points in pricing; (2) "minimum advertised price" requirements; (3) "most favoured nation" price clauses; (4) limitations on advertising; and (5) legislated facilitating practices, such as state "post and hold" statutes in the liquor industry. These five situations will be discussed under the subheadings that follow.

2.1 Agreed elements or reference points in pricing

10. Trade associations have sometimes attempted to reduce competition among their members by encouraging them to set prices around some common references. Prices based on a trade association's relative value scales or standardized activity codes may be relatively transparent, and in that respect may encourage competition. However, in some circumstances, including the case referred to below, the Commission has challenged those practices as facilitating collusion, arguing that procompetitive benefits were outweighed by the risk of anticompetitive effects.[2]

11. In 1994, the Commission issued a complaint against the International Association of Conference Interpreters (known by its French acronym, AIIC). AIIC is a voluntary professional association of interpreters, with 2,500 members from 68 countries who perform interpretation services at multi-lingual conferences or other high-level meetings. The complaint challenged AIIC's fee schedules, work rules, and other practices that supported the underlying agreements on price. The administrative law judge upheld those charges.[3] He noted that members were paid AIIC's minimum daily rate 90 percent of the time from

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2. The Commission has successfully demonstrated that the trade associations have raised prices by using these techniques, even though in the absence of a trade association most of those industries would not have seemed susceptible to collusion, since they were not concentrated and not characterised by repeated interactions.

3. According to the administrative law judge, AIIC set minimum daily rates to be charged by members, required that all interpreters at a conference be paid the same daily rate regardless of skill or experience differences, specified the length of the working day and the number of interpreters to be hired at a conference, and required payment for travel expenses, per diem, canceled events, rest days and non-

1988 to 1991. He found that the effect of many of the other rules was to make price cutting easier to detect; thus they were facilitating practices. For example, rules requiring that travel expenses and per diem payments be stated separately on contracts would make cheating on them and on the minimum daily price easier to see. Similarly, the requirement that fees be paid on an indivisible daily basis made rates more standardized and more readily monitored by other members of the industry.[4] AIIC appealed this initial decision to the full Commission, which upheld most of these charges in 1997. However, the Commission dismissed certain charges against Association rules governing work-day length, interpreter team size, and other non-price factors the effect on competition of which were uncertain.[5]

12. In 2000, the Commission accepted a consent to settle a complaint that the Wisconsin Chiropractic Association ("WCA") had proposed the use of common external reference points in order to limit competition and raise prices among its members.[6] In 1997, the federal government and private insurance companies began accepting four new codes for chiropractic manipulations. The new procedure codes gave more detailed or precise descriptions of the particular services performed, and allowed chiropractors, like osteopathic physicians, to bill based on the number of body regions adjusted, rather than just for a single set amount. According to the complaint, shortly after the new codes were announced, the Association and its executive director conducted training seminars on the new codes. The executive director advised members that it was important for the new codes to be priced properly, and that the WCA's view was that proper pricing would be at the same level that osteopathic physicians billed for spinal manipulation services. He provided detailed data on osteopathic pricing, and encouraged chiropractors to raise their prices to those levels. After the new codes took effect, the executive director surveyed member pricing in certain localities, and reported that chiropractors in those areas had succeeded in raising reimbursement levels.[7] The consent order was designed to prevent the concerted use of the facilitating practices alleged in the complaint.

13. The Commission has also addressed relative value scales, a subject on which its views have evolved over time. "Relative value scales" are lists of assigned numerical values for various medical and surgical services, that serve to compare the value of the different services. These scales are useful in helping individual practices construct their fee schedules. They can also facilitate collusion, however. While the scales do not set actual transaction prices, competitors need to agree on only a single conversion factor in order to have identical prices across the board. The Commission issued an advisory opinion to the American Society of Internal Medicine in 1985, stating that the Society proposed a relative value scale that likely would raise anticompetitive effects.[8] With the growth of managed care, however, and the increased

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working days when the interpreter was away from his or her mandated professional address. AIIC rules also have restricted members' use of portable equipment; barred commissions to intermediaries, package fees, exclusive arrangements, moonlighting for permanently-employed interpreters, and the use of comparative advertising and trade names; required members to have a professional address and to give three months' notice before changing it; required charges for the recording of interpretation services and imposed limits on charitable work.

4. International Ass'n of Conference Interpreters, FTC Docket No. 9270 (July 31, 1996) (press release: http://www.ftc.gov/opa/1996/07/aiic-id.shtm).

5. International Ass'n of Conference Interpreters, FTC Docket No. 9270 (March 14, 1997) (press release: http://www.ftc.gov/opa/1997/03/aiic-cd.shtm).

6. Wisconsin Chiropractic Ass'n C-3943 (March 7, 2000) (Analysis to Aid Public Comment) (press release: http://www.ftc.gov/opa/2000/03/wischiro.shtm).

7. The executive director regularly provided fee surveys to the WCA's members. At times, these fee surveys reflected insufficiently aggregated data, thus effectively identifying current prices of individual chiropractic offices.

8. American Society of Internal Medicine, 105 F.T.C. 505 (April 19, 1985).

use of relative value scales by health care managers, the Commission has modified or set aside some orders. Such modifications have given associations more freedom to discuss relative value scales with third-party payers, governmental entities, and their own members, while also serving to caution against entering into horizontal price agreements on the basis of such scales.[9]

2.2 Minimum advertised price agreements

14. Minimum advertised price agreements (or "MAP agreements") involve the terms on which retailers are allowed to spend the cooperative advertising allowances that they receive from product manufacturers. Because MAP agreements can control the pricing strategies of a number of competing retailers, and are visible to competing manufacturers as well, they may be horizontal facilitating practices at both the retailing and manufacturing levels. After the Supreme Court's 2007 decision in *Leegin*[10], which held that purely-vertical resale price maintenance agreements could often be acceptable, as a practical matter, a MAP case without horizontal elements is unlikely to be sound.

15. Manufacturers commonly provide advertising allowances to the retailers who carry their products. The manufacturers feel that they have a right to a voice in how ads are designed, and prices advertised with their funds. They commonly specify the lowest price that can appear in such ads. The antitrust agencies have been reluctant to condemn this use of the manufacturers' own advertising budget. In 1997, the FTC issued a policy statement outlining that it would treat such MAP programs under the rule of reason in light of their possible efficiencies.[11]

16. In 2000, the Commission settled a case involving this broader use of MAP policies by the five largest distributors of pre-recorded music, who account for approximately 85% of the industry's domestic sales. The complaints alleged that these companies adopted significantly stricter MAP provisions between late 1995 and 1996. Under the new MAP policies, retailers seeking any cooperative advertising funds were required to observe the distributors' minimum advertised prices in all media advertisements, even those funded solely by the retailers. They were also required to adhere to distributors' minimum prices on all in-store signs and displays. Virtually the only way in which prices could be shown was through a small label on the product itself. The complaints alleged that by defining the covered "advertising" so broadly, the manufacturers had effectively precluded many retailers from communicating prices below MAP to their customers. The consent orders required the manufacturers to discontinue their MAP programs in their entirety for a period of seven years.[12]

17. A contemporaneous speech by FTC Commissioner Thomas Leary explained the ways in which this conduct might have facilitated horizontal agreements.[13] Imposing the broader restraints reduced price

9. Consent orders were issued in American College of Obstetricans & Gynecologists, 88 F.T.C. 955 (1976) (consent order), *modified,* 104 F.T.C. 524 (1984); American Academy of Orthopaedic Surgeons, 88 F.T.C. 968 (1976) (consent order), *modified,* 105 F.T.C. 248 (1985), *order set aside,* 119 F.T.C. 609 (1995); American College of Radiology, 89 F.T.C. 144 (1977) (consent order), *modified,* 113 F.T.C. 280 (1990); Minnesota Medical Ass'n, 90 F.T.C. 337 (1977) (consent order); and California Medical Ass'n, 93 F.T.C. 519 (1979) (consent order), *modified,* 105 F.T.C. 277 (1985), *order set aside,* 120 F.T.C. 858 (1995).

10. Leegin Creative Leather Products, Inc. v. PSKS, Inc., 127 S. Ct. 2705 (2007).

11. *See* Statement of Policy Regarding Price Restrictions in Cooperative Advertising Programs – Rescission, 6 Trade Reg. Rep. (CCH) ¶ 39,057.

12. Concerning the Market for Prerecorded Music in the United States, FTC File No. 971 0070 (C-3971 to C-3975) (May 10, 2000) (Analysis to Aid Public Comment).

13. T. Leary, *Distribution Law Developments at the Federal Trade Commission*, remarks before the Distribution and Dealer Termination Seminar (New York, June 26, 2000), http://www.ftc.gov/speeches/leary/ddtny000626.shtm.

competition among retailers, who could now no longer advertise the fact that they had discount prices. That led to higher retail prices, which led to less pressure from the retailers for the manufacturers to cut wholesale prices. Because all five manufacturers had instituted similar MAP policies simultaneously – and openly – they were able to take advantage of this reduced retailer pressure to raise their wholesale prices.

18. The CD MAP case was unusual in that the immediate effect of the facilitating practice was to lessen competition among a group of businesses, the retailers, which did not impose the practice in the first place. The Commission reportedly thought that these facts should be interpreted in light of the industry's history of interdependent behaviour at the manufacturer level.[14] Still, one should be cautious about inferring a horizontal case when the affected parties and the actors are different entities, and Commissioner Leary noted that "there may not be many cases that are as extreme as this one appeared to be . . ."[15] Nevertheless, such cases may arise.

2.3 Most-favoured-nation clauses

19. A most-favoured-nation clause is a provision in a sales contract, under which the seller agrees to give the buyer the benefit of any more favourable contract terms that it may later negotiate with some other purchaser. (The name itself is borrowed from international tariff negotiations.) Under certain narrow circumstances these clauses may tend to deter competitive price-cutting, and so may tend to facilitate the maintenance of cartel prices.

20. Under most ordinary circumstances, most-favoured-nation clauses are probably benign. It can make sense for buyers to seek this protection against future events, and for sellers to grant this guarantee in good faith in order to close a deal. If the market is unconcentrated and competitive, such clauses do little harm. Judge Richard Posner has described them as "standard devices by which buyers try to bargain for low prices."[16]

21. Under some circumstances, however, these clauses may be more troublesome.[17] A classic problem faced by a cartel is that its members try to cheat on it. Most-favoured-nation clauses can reduce the incentive to cheat, by increasing the costs of cheating. The low price offered on a particular contract would then become, not just a one-time occasion when the cheater could gain some incremental sales volume, but rather an occasion for across-the-board revenue losses as many of the firm's contract prices are reset.[18]

22. A number of specific circumstances would need to exist before those potential anticompetitive outcomes warrant much study, however. At a minimum, the contracts would probably have to be routinely used by most manufacturers in an industry, and by many of the customers. In addition, whether the clauses were requested or objected to by customers would be pertinent. It would also be relevant to know if there is one particularly large customer; most-favoured-nation clauses may be particularly effective in deterring

14. Id. at p.3.

15. Ibid.

16. Blue Cross & Blue Shield v. Marshfield Clinic, 65 F.3d 1406, 1415 (7th Cir. 1995).

17. For a general discussion see Jonathan Baker, *Vertical Restraints with Horisontal Consequences: Competitive Effects of "Most-Favored-Customer" Clauses*, 64 ANTITRUST L.J. 517 (1996).

18. This situation may have been present in the FTC's *Ethyl* case. There the Commission suggested that the unilateral adoption of these facilitating practices could be actionable – a proposition that the court rejected for lack of proof of actual anticompetitive effects. *See* E.I. du Pont de Nemours & Co. v. FTC, 729 F.2d 128, 140-41 (2nd Cir. 1984). The outcome might have been different had the postulated effects been shown.

discounts to smaller customers if the discount would have to be immediately offered to a much larger buyer.[19]

2.4 Limitations on advertising

23. A fourth facilitating practice reviewed by the FTC involves agreements to limit the use of truthful, no deceptive advertising. Limits on price advertising will tend to support any previous agreement that may have been made as to price. Limits on advertising nonprice factors will tend to moderate the intensity of competition in those nonprice respects, and dissuade firms from "competing away" the benefits of a price agreement.

24. In one case of this sort, the Commission issued a complaint alleging that the Arizona Automobile Dealers Association had agreed with its member dealerships to restrict non-deceptive comparative and discount advertising, and advertising concerning the terms and availability of consumer credit. The complaint challenged certain sections of the association's Standards for Advertising Motor Vehicles, which, among other things, prohibited members from advertising that prices are equal to or lower than a competitor's; that the advertiser will match or beat any price; or that the advertiser will offer compensation if it cannot do that. The complaint was settled with a consent agreement prohibiting such restrictions.[20]

25. Advertising restraints can sometimes provide offsetting consumer benefits, however, insofar as they can prevent some consumers from being confused or misled. Balancing the procompetitive and anticompetitive effects in this area can be particularly difficult. In 1993, for example, the FTC issued a complaint against the California Dental Association (CDA). The Association's 19,000 members made up 75 percent of the dentists in the state. According to the complaint, the Association's rules prohibited several valuable categories of price advertising (including advertising of across-the-board discounts for seniors or others, and statements such as "care at reasonable prices"), and useful information about the nonprice characteristics of dental services (such as "special treatment for nervous patients").[21] The Commission concluded that the Association rules improperly banned broad categories of claims, without distinguishing between the deceptive and the no deceptive. The case went to the U.S. Supreme Court on the issue of the proper application of the rule of reason; the Court remanded the case to the court of appeals.[22] That court ultimately ruled against the Commission, finding that the procompetitive benefits of the rules outweighed their anticompetitive harm,[23] and that the restrictions would prevent advertisements that would mislead consumers, and would induce dentists to provide more complete and understandable pricing information. In 2001, the Commission decided, for various reasons, not to seek further review and dismissed the complaint.

26. Agreements to restrict advertising can sometimes take variant forms, which may also raise anticompetitive issues. One such variant involves boycotts of publications that publish discount price advertising. In a case of this type, the FTC sued an association of dealers of farm equipment, several of

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19. *See* Baker, *supra,* at 521; United States v. Eli Lilly & Co., 1959 Trade Cas. (CCH) ¶ 69,536 at p. 76,152 (D. N.J. 1959) (federal government as a large buyer of pharmaceuticals).

20. Arisona Automobile Dealers Ass'n, C-3497 (Feb. 25, 1994) (press release).

21. California Dental Ass'n, D-9259 (July 25, 1995) (press release: http://www.ftc.gov/opa/1995/07/cda2.shtm).

22. California Dental Assn. v. FTC, 526 U.S. 756 (1999).

23. California Dental Ass'n v. F.T.C., 224 F.3d 942 (9th Cir. 2000).

whose members had withheld their advertising from a buying guide until it agreed not to publish advertisements that included prices for new farm equipment.[24]

27. In another variant, auto dealers in a city agreed, not to reduce price advertising directly, but rather to impede consumers' ability to make price comparisons by agreeing to restrict their operating hours on weekends, so that comparison shopping became more difficult and price competition became less intense.[25]

28. In still another variant, restrictions on price advertising may be imposed, not by a private association, but by a governmental regulatory board that may in practice be dominated by members of the affected industry. The Commission has challenged such board actions when they seem to go beyond the range of discretion contemplated by the state legislature.[26] One complaint of this sort was brought against the Texas Board of Chiropractic Examiners.[27] Under Texas law, the board was the sole licensing authority for the approximately 1600 chiropractors in the state. The complaint charged the board with hindering consumers in obtaining information about chiropractors' fees, services, and products, thereby making it less likely that there would be vigorous competition within the profession. The board eventually agreed to a consent order against the practices.[28] The Commission also issued a similar complaint against the Massachusetts Board of Registration in Optometry.[29]

2.5 Government action that encourages facilitating practices

29. As the last example makes clear, facilitating practices can sometimes be imposed by the government. They may be especially troublesome when they have that origin, since actions by the government are durable, not subject to breakdown in the same way as a cartel, and are immune to many forms of legal challenge.

30. Governmental restraints on competition may serve a valid public purpose, and are generally requested on the basis of that rationale. They can also have anticompetitive effects, however, and for this reason they may be sought by association-oriented lobbying groups.

31. Facilitating practices may be imposed by a legislature through statute, or by an administrative board through regulations. The practices themselves can take a wide variety of forms. These can include restrictions on advertising, restrictions on services, minimum percentage mark-up for retailers,[30] or even authorization for competing firms to agree on prices.[31]

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24. Fastline Publications, Inc., C-3819 (May 11, 1998) (consent agreement) (press release: http://www.ftc.gov/opa/1998/05/fastline.shtm).

25. *See* Detroit Auto Dealers Ass'n, 955 F.2d 457 (6th Cir.1992).

26. Under U.S. law, governmental boards are immune from the antitrust laws if they meet the procedural requirements for "state action," but can be treated as private agreements among their members if those requirements are not met, as discussed in the following section of this submission.

27. Texas Board of Chiropractic Examiners, C-3379 (Apr. 29, 1992) (press release).

28. Texas Board of Chiropractic Examiners, 115 F.T.C. 470 (1992).

29. Massachusetts Board of Registration in Optometry, D-9195 (July 2, 1986) (press release); litigated order issued, 110 F.T.C. 549 (1988).

30. 324 Liquor Corp. v. Duffy, 479 U.S. 335 (1987).

31. Kentucky Household Goods Carriers Ass'n, D-9309 (June 22, 2005), *aff'd,* 199 Fed. Appx. 410, 2006-2 Trade Cas. (CCH) ¶ 75,384 (6th Cir. 2006).

32. To take one example, a number of states have passed "post and hold" statutes, which provide that firms selling alcoholic beverages must post their prices, and then leave them unchanged for a certain period of time.[32] On their face such statutes do not involve price fixing, since they do not authorize any horizontal agreement. They nonetheless establish a facilitating practice, since they make prices more "sticky" and less responsive to competitive circumstances.

33. Under U.S. law, facilitating practices created through statutes at the level of the state legislature are not usually open to challenge on federal antitrust grounds. Such "state action" is generally thought to be outside the intended scope of the federal antitrust statutes. However, antitrust agencies may, particularly if requested by the legislature, wish to call attention to the competitive consequences of proposed legislation.

34. An agreement on facilitating practices that would otherwise violate the antitrust laws may not be immune from antitrust scrutiny, despite the role of a subordinate state administrative agency, in two situations.[33] First, if the state agency's actions were not "clearly authorized" by the state legislature – since the necessary authority must ultimately come from one of the state's constitutional branches. Second, if the scheme is not "actively supervised" by some part of the state government, to make the conduct truly the state's own. It is not yet entirely clear at what point a facilitating practice will create "private market power" for this purpose; nor is it entirely clear whether a state regulatory board, numerically dominated by members of the regulated profession, has enough private characteristics to require active supervision.[34]

3. DOJ Criminal Enforcement

35. "Facilitating practices" must be distinguished from hard-core cartel behaviour. Cartels have been highlighted in almost all jurisdictions as the most egregious conduct inimical to competition and consumer welfare, and are subject to the most severe sanctions, including criminal prosecution, often with *per se* rules that appropriately account for their unmitigated harmfulness.

3.1 Reserving the most severe sanctions for hard-core cartels

36. Cartels merit special attention from antitrust enforcers because hard-core cartel activity is a well-defined category of collusive conduct among competitors that clearly and unambiguously eliminates competition without any prospect of offering compensating social benefits. Applying tough penalties is appropriate not just because the conduct is clearly bad, but also because there is no possibility that legitimate conduct can be mistaken for hard-core cartel conduct. Hence, tough penalties will not cause competitors to avoid socially beneficial conduct: over-deterrence is not an issue when it comes to cartels. That is not true for other types of coordinated conduct among competitors, including most facilitating practices.

37. The Department of Justice has made it clear to all that anti-cartel enforcement is its top priority, relying chiefly on two strategies. First, DOJ, which has sole responsibility for the criminal prosecution of cartels under federal law, has separated criminal from civil enforcement, permitting a large group of attorneys to focus solely on cartels. Second, the Department has declared in numerous publications,

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32. For cases challenging the validity of such statutes, *see, e.g.,* Battapaglia v. New York State Liquor Authority, 745 F.2d 166 (2nd Cir. 1984) (statute upheld); Canterbury Liquors v. Sullivan, 16 F.Supp.2d 41 (D. Mass. 1998) (statute found invalid).

33. *See* California Retail Liquor Dealers Ass'n v. Midcal Aluminum, 445 U.S. 97, 105 (1980).

34. *Cf.* Town of Hallie v. City of Eau Claire, 471 U.S. 34, 45 (1985) (explaining the characteristics of government action that ordinarily make supervision unnecessary).

speeches, and testimony, that anti-cartel enforcement is the highest priority in an explicit enforcement hierarchy.[35]

38. At the same time, DOJ carefully delimits its criminal enforcement to focus only on hard-core violations. The higher burden of proof in criminal cases (requiring proof "beyond a reasonable doubt," as opposed to the "preponderance of the evidence" standard used in United States civil law) and the narrowness of what criminal enforcement condemns (the fixing of prices, bids, output, and markets, as opposed to conduct subject to the "rule of reason" or monopolization analyses used in civil antitrust law) establish clear, predictable boundaries for business. When criminal cases focus on conduct that has no plausible business justification and that usually occurs in secret, accompanied by pre-emptive cover-ups and misrepresentation, defendants cannot reasonably argue that they failed to grasp the illegality of their actions.[36] All of these features – high burdens of proof, well-defined coverage, clear boundaries – allay the potential fears of law-abiding business persons, who can easily determine whether their own conduct will form the basis of a criminal case.

39. The particularized focus of U.S. criminal prosecution is consistent with the OECD's recommendation concerning effective action against hard-core cartels. The 1998 recommendation defines a "hard-core cartel" as "an anticompetitive agreement, anticompetitive concerted practice, or anticompetitive arrangement by competitors to fix prices, make rigged bids (collusive tenders), establish output restrictions or quotas, or share or divide markets by allocating customers, suppliers, territories, or lines of commerce." This focus is regularly underscored in DOJ speeches and press releases, and is summarized in the Antitrust Division Manual:

> In general, current Division policy is to proceed by criminal investigation and prosecution in cases involving horizontal, *per se* unlawful agreements such as price fixing, bid rigging and horizontal customer and territorial allocations . . . . There are a number of situations where, although the conduct may appear to be a *per se* violation of law, criminal investigation or prosecution may not be considered appropriate. These situations may include cases in which: (1) there is confusion in the law; (2) there are truly novel issues of law or fact presented; (3) confusion reasonably may have been caused by past prosecutorial decisions; or (4) there is clear evidence that the subjects of the investigation were not aware of, or did not appreciate, the consequences of their action.[37]

40. The decision to make anti-cartel enforcement the highest priority in the DOJ antitrust enforcement hierarchy is also a useful signal to industry. Although protection of competition in the areas of merger and non-merger civil enforcement is important, the Division gives special emphasis to cartel enforcement. This hierarchy also aligns enforcement priorities with our level of certainty about consumer harm: cartels are always harmful to consumers, whereas other types of concerted and unilateral conduct are sometimes harmful but at other times will lead to greater efficiencies that enhance consumer welfare. In

35. *E.g.,* R. Hewitt Pate, Ass't Att'y Gen., U.S. Dep't of Justice, Securing the Benefits of Global Competition, address before the Tokyo America Center 4-6 (September 10, 2004), *at* http://www.usdoj.gov/atr/public/speeches/205389.pdf; *see also* Thomas O. Barnett, Deputy Ass't Att'y Gen., U.S. Dep't of Justice, Antitrust Enforcement Priorities: A Year in Review, address before the Fall Forum of the ABA Section of Antitrust Law 2-3 (November 19, 2004), *at* http://www.usdoj.gov/atr/public/speeches/206455.pdf.

36. Cartels often use extreme measures to conceal their existence. The Division has encountered cover-ups ranging from the creation of bogus trade associations, the use of code names, and sophisticated ruses to keep general counsel in the dark, to hiding incriminating evidence in the attic of a cartel member's grandparent's home, wholesale document destruction, and witness tampering after an investigation begins.

37. Antitrust Division Manual, III.C.5.

merger and non-merger civil enforcement, antitrust enforcers need to account for the possibility of false positives, meaning the assumption of anticompetitive effects where, in fact, none exist or where the potential anticompetitive effects are outweighed by pro-consumer benefits. The Division's enforcement hierarchy helps enforcers to avoid deterring businesses from good, hard competition.

41. The DOJ usually proceeds with a criminal prosecution only where there is direct evidence of an unlawful agreement to engage in hard-core cartel conduct. In cases where a defendant does not plead guilty, the direct evidence offered most often takes the form of testimony from a cartel participant, who may be a leniency applicant, cooperating witness, or immunized co-conspirator, but can also include video- or audio-tapes or documents providing direct evidence of an unlawful agreement.

42. It is important to maintain a bright line between criminal activity – naked price-fixing – and other forms of horizontal conduct. Courts are likely to respect the enforcement agency's decision to seek significant deterrent sanctions, including incarceration, in cases where there is no plausible argument that defendants might have had some legitimate objective associated with their conduct, where the conduct is not open or routine in the industry, and where the law and enforcement policy of the agency have left no doubt as to the unlawfulness of the conduct.

3.2 Civil Enforcement Against Facilitating Practices: U.S. v. Airline Tariff Publishing Co.

43. As noted above, the DOJ usually proceeds with criminal prosecutions against hard core cartel activity when direct evidence is available. Under U.S. law, a *per se* illegal price-fixing agreement can also be inferred in the absence of direct evidence, "on the basis of conscious parallelism, when such interdependent conduct is accompanied by circumstantial evidence and plus factors such as defendants' use of facilitating practices. Information exchange is an example of a facilitating practice that can help support an inference of a price-fixing agreement."[38]

44. Courts have also discussed "a closely related but analytically distinct type of claim, also based on sec. 1 of the Sherman Act, where the violation lies in the information exchange itself – as opposed to merely using the information exchange as evidence upon which to infer a pricing agreement. This exchange of information is not illegal *per se*, but can be found unlawful under a rule of reason analysis."[39] *See U.S. v. Container Corp.*, 393 U.S. 333 (1969).

45. The Department of Justice's suit against the Airline Tariff Publishing Company (ATP)[40] is an example of a case involving horizontal conduct – price fixing and an agreement to engage in facilitating practices – where the Department determined that criminal enforcement was not appropriate. In December 1992, the Department sued eight of the largest U.S. airlines and ATP for price fixing and for operating ATP, their jointly-owned fare exchange system, in a way that facilitated collusion, in violation of §1 of the Sherman Act. ATP was a complex information exchange system among airlines that was widely and openly operated to disseminate fare information through computer reservation systems and travel agents. ATP served as a vehicle for communication and negotiation of unlawful price-fixing agreements by

38. *Todd v. Exxon Corp*., 275 F.3d 191, 192 (2d. Cir. 2001) (refusing to dismiss a complaint that alleged that 14 oil companies shared information regarding compensation to non-union managerial employees and used that information to set salaries at artificially low levels).

39. Id.

40. United States v. Airline Tariff Publishing Co., 1994-2 Trade Cas. (CCH) ¶70,687 (D.D.C. Aug. 10, 1994); see http://www.usdoj.gov/atr/cases/dir23.htm.

airlines and was operated in "a manner that unnecessarily and unreasonably allowed [the airlines] to coordinate fares."

46. Covert information exchanges that serve no purpose other than output limitation are often at the heart of criminal price-fixing conspiracies. ATP, by contrast, provided both a means for the airlines to disseminate fare information to the public and a means for the airlines to engage in essentially a private dialogue on fares. Certain features of ATP "enabled the airline defendants on many occasions to reach overt price-fixing agreements" and "facilitate[d] pervasive coordination of airline fares short of price fixing." Some of ATP's pernicious features were vestiges of the pervasive regulatory system that had been dismantled when civil aviation was deregulated in the 1980s. In these circumstances the Department determined that civil rather than criminal enforcement was appropriate.[41]

47. The Division's civil complaint targeted two kinds of conduct. First, the defendant airlines had engaged in various combinations and conspiracies with other airline defendants, which included agreements, understandings, and concerted actions to fix prices by increasing fares, eliminating discounted fares, and setting fare restrictions for tickets purchased for domestic air travel. These actions were *per se* violations of §1 the Sherman Act. The defendants used ATP's computerized fare exchange system to (1) exchange proposals and negotiate fare changes, (2) trade fare changes in certain markets in exchange for fare changes in other markets, and (3) exchange mutual assurances concerning the level, scope, and timing of fare changes.

48. Second, the airline defendants and ATP had conspired and reached an agreement to create, maintain, operate, and participate in the ATP fare exchange system. The defendants designed and operated the system in a way that unnecessarily facilitated coordinated interaction among them so that they could (1) communicate more effectively with one another about future fare increases, restrictions, and elimination of discounted fares, (2) establish links between proposed fare changes in one or more city-pair markets and proposed changes in other city-pair markets, (3) monitor each other's changes, including changes in fares not available for sale, and (4) reduce uncertainty about each other's pricing intentions. The second cause of action challenged the agreement to engage in the facilitating practice – apart from any agreement on price or output – as a violation of §1 of the Sherman Act, under a rule-of-reason analysis.

49. The ATP case involved "cheap talk" – communication that does not commit firms to a course of action -- such as announcing a future price increase but leaving open the option to rescind or revise it before it takes effect.[42] If the terms of agreement are complex (*e.g.*, specifying prices in numerous markets) but there is a common desire to reach agreement, cheap talk can help firms reach a collusive equilibrium. ATP was a joint venture owned by the major airlines. ATP collected fare information from the airlines and distributed it daily to all the airlines and to the major computer reservation systems (CRSs) that serve travel agents. This arrangement was an efficient instrument for cheap talk:

> Airlines are charged a fee for each change, so that changes are not absolutely costless, but the fees for any change are very small relative to the revenues involved. Since ATP updates all CRSs once a day, airlines can quickly observe and respond to each other's fares using this system, with (at most) a one day lag. Since any significant price movement can be quickly matched by competitors, the potential benefits from cheating on any collusive price are usually small relative to the advantages of maintaining a high

41. U.S. v. Mercury PCS II, L.L.C. (http://www.usdoj.gov/atr/cases/indx87.htm) is another example of a civil enforcement action against horisontal conduct – use of coded bids by rivals in a Federal Communications Commission auction of wireless spectrum as part of an agreement not to bid against each other.

42. Joseph Farrell and Matthew Rabin, "Cheap Talk," 10 *Journal of Economic Perspectives* 103 (Summer 1996).

price.[43]

For example, to eliminate an unwanted discount fare, an airline could tell ATP that the fare would terminate next Tuesday. If the other airlines did the same with their competing discount fares, all the changes would take effect as announced. If some airlines failed to respond, the last date of availability (Last Ticket Date, or LTD) could be moved to a later date to give the laggards more time, or the changes could be withdrawn. Because a proposed fare increase would not take effect until the airline could observe whether it was matched, there was minimal risk that it would lose a sale to a lower-priced rival before a price consensus was reached. Airlines could also use a First Ticket Date (FTD) to signal when they wanted a new fare to take effect, and they could impose "punishment fares" effective immediately, with an LTD signalling an offer to remove it if the offending airline were to change its behaviour.

50. In more complex (and more typical) examples, airlines had differing pricing strategies, depending on market concentration and hub locations, and the "cheap talk" negotiations occurred simultaneously over numerous markets. One alleged instance, in September 1989, started with a proposal by an airline to eliminate discount one-way fares (known as "junk" fares in the industry) in hundreds of city-pair markets:

> Several airlines communicated their agreement to this proposal by also filing to eliminate the fares altogether, but one dissenting airline proposed instead to increase the junk fares by ten dollars each way. One of the airlines supporting the first proposal expressed its dissatisfaction with this counterproposal by briefly lowering the junk fares by ten dollars each way in the markets very important to the dissenting airline, using a [LTD] only a few days away. However, when some of the other airlines began to match the counterproposal to increase fares by ten dollars (instead of eliminate them), the punishing airline withdrew the lower fares immediately (before the [LTD] on the fares) and also filed to increase fares by ten dollars. At that point, another airline proposed yet a third alternative -- to increase the junk fares by twenty dollars each way. Throughout the negotiation process, the airlines continuously altered [FTDs] of the proposed increases, and kept scorecards of which airlines were supporting which proposal, with what [FTD], until they had reached a consensus. Eventually, all the airlines agreed to the third proposal, and the twenty dollar increase went into effect. (One airline estimated that the increase would generate an additional $7 million/month for that airline alone.)[44]

3.3 Remedies in U.S. v. ATP

51. *ATP* was ultimately resolved by a federal court consent decree. The decree was crafted to ensure that the airline defendants did not continue to use the ATP fare dissemination system or any similar mechanism in a manner that unnecessarily facilitated fare coordination or that enabled them to reach specific price-fixing agreements. It prohibited the airline defendants from disseminating FTDs or using designating mechanisms to signal links between fares, and substantially restricted their use of LTDs. The Final Judgment also prohibited other conduct that would allow the airline defendants to communicate without market risk their pricing intentions or signal competitors that fare actions in different markets were

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43. William Gillespie, "Cheap Talk, Price Announcement, and Collusive Coordination," EAG 95-3, Discussion Paper, Economic Analysis Group, Antitrust Division, U.S. Department of Justice (9/25/95). See also Severin Borenstein, "Rapid Price Communication and Coordination: The Airline Tariff Publishing Case (1994)," Chapter 13 in John E. Kwoka, Jr. and Lawrence J. White (eds.), *The Antitrust Revolution: Economics, Competition, and Policy*, 3rd ed. (1999).

44. U.S. v. ATP, United States' Response to Public Comments, April 8, 1993, p. 17, quoted in Gillespie, *op. cit.*, p. 11.

linked. The Final Judgment did not prevent the airline defendants from disseminating their currently available fares through ATP to CRSs for consumer booking and ticketing, from advertising current fare information to consumers, or from offering for sale fares for which travel could only begin in the future, for example, offering fares in the summer that applied to winter travel to warmer locations. Neither did it regulate the independent pricing decisions of an airline, whether or not those prices were a response to, or evoked a response from, other airlines.