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Organisation de Coopération et de Développement Economiques
Organisation for Economic Co-operation and Development

OLIS : 21-Oct-1998
Dist. : 27-Oct-1998

English text only

DIRECTORATE FOR FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS
COMMITTEE ON COMPETITION LAW AND POLICY

DAFFE/CLP/WP3/WD(98)10
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Working Party No. 3 on International Co-operation

ROUNDTABLE ON HORIZONTAL BOYCOTT AGREEMENTS

-- NOTE BY THE UNITED STATES --

This note is submitted by the United States Delegate to Working Party No. 3 FOR DISCUSSION at its forthcoming meeting on 27 October 1998.

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Hypothetical Category Number One

1. Facts: an association of retail lumber companies agrees to prevent competition from vertically integrated wholesalers by agreeing not to deal with wholesalers who sell directly to customers. *See Eastern States Retail Lumber Dealers Ass'n v. United States*, 234 U.S. 600 (1914).

2. The United States Supreme Court "has long held that certain concerted refusals to deal or group boycotts are so likely to restrict competition without any offsetting efficiency gains that they should be condemned as *per se* violations of § 1 of the Sherman Act." *Northwest Wholesale Stationers, Inc. v. Pacific Stationary and Printing Co.*, 472 U.S. 284, 290 (1985). This hypothetical is based on the facts set forth in *Eastern States Retail Lumber Dealers Ass'n v. United States*, 234 U.S. 600 (1914), in which a concerted refusal to deal was condemned as illegal *per se.*

3. The Supreme Court has cautioned, however, that not every arrangement that can be characterized as a concerted refusal to deal is anticompetitive, and that care is necessary "in defining the category of concerted refusals to deal that mandate *per se* condemnation." *Northwest Wholesale Stationers*, 472 U.S. at 294. *Per se* condemnation is appropriate only if "the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output ... or instead one designed to 'increase economic efficiency and render markets more, rather than less competitive.'" *Id*. at 289-290, *quoting Broadcast Music, Inc.* v. *Columbia Broadcasting System, Inc.*, 441 U.S. 1, 19-20 (1979). The boycott condemned in *Eastern States Retail Lumber Dealers* was an agreement among retailers collectively exercising market power, designed specifically to punish wholesalers who made sales at retail and thereby discourage such competition. There is no indication that the defendants offered any procompetitive justification for the boycott. The concerted refusal to deal in *Northwest Wholesale Stationers*, by contrast, involved the membership rules of a wholesale purchasing cooperative -- "not a form of concerted activity characteristically likely to result in predominantly anticompetitive effects." *Northwest Wholesale Stationers*, 472 U.S. at 294. Because purchasing cooperatives may serve legitimate, and procompetitive purposes, the Court applied the rule of reason.

4. The agencies accordingly would take into account any procompetitive justifications offered for a particular arrangement before concluding that *per se* condemnation is appropriate. Plausible claims that the conduct at issue enhances competition would distinguish the arrangement from the boycott condemned in *Retail Lumber Dealers* and require consideration under the rule of reason. We need only apply a rule of reason analysis (which involves balancing the agreement's anticompetitive and procompetitive effects) if there is some evidence of a valid procompetitive justification. If the agreement detailed in the hypothetical lacks, any procompetitive justification, it should be condemned as a *per se* violation. *United States v. Scuba Retailers Ass'n*, 1996-1 Trade Cas. (CCH) (S.D. Fla. May 2, 1996)*; Fair Allocation System, Inc.*, FTC File No. 971-0065 (1988) (consent).

Hypothetical Category Number Two

5. Facts: a group of cab companies which have contracts to service certain hotels form an association to certify drivers meeting quality standards set by the association. *See Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, Inc.*, 810 F.2d 869 (9th Cir. 1987).

1. Analysis of association policy against providing certification service to non-members willing to pay the full cost of certification.

6. Limiting membership in an association, even where membership brings with it some economic advantage, cannot constitute a *per se* violation of U.S. antitrust laws unless the association "possesses market power or exclusive access to an element essential to effective competition." *Northwest Wholesale Stationers*, 472 U.S. at 294. Because a hotel's patrons are free to call non-member cab companies to pick them up, even at those hotels which participate in the contracts, and generally do so for longer rides, and because hotels are free to contract with non-member cab companies, this association may not possess either of the aforementioned attributes.[1] On the other hand, if market power is present, we would consider any plausible procompetitive justification for the exclusion of non-members. The agencies would not summarily condemn the association policy as *per se* illegal. Moreover, the agencies would inquire as to the policy's procompetitive justifications.

2. Analysis of an association rule barring foreigners from membership.

7. While the arbitrariness of such a rule does not radically alter the application of the *per se* rule to this hypothetical, it could affect a rule of reason analysis. Applying rule of reason analysis requires a more fact-intensive inquiry than is possible within the parameters of this hypothetical. For instance, we would need to know the percentage of drivers foreclosed from servicing the hotel contracts as a result of the no-foreigner rule.

8. If competition from outside the association were sufficient to prevent the exercise of market power, the rule would not cause competitive harm. If instead competition from outside the association were insufficient to check an exercise of market power and the rule significantly limited the number of drivers available to service the hotel contracts, it could enable the non-foreign drivers to charge more. The procompetitive benefit of such a rule is not readily apparent. Although the association might reasonably claim that the hotels want to ensure that the cab drivers they recommend speak English or are legal residents of the United States, those criteria could be met through less restrictive means than a "no foreigner" rule. If it could be shown that the rule limited the number of available drivers to a competitively significant extent, this rule would fail the rule of reason test.

3. Analysis of rule that no driver could join before spending five years as an employee of a member cab company.

9. As in the above hypothetical, this rule would be analyzed under the rule of reason. As with that hypothetical, the association's rule only presents a potential competitive problem to the extent that the hotels use association membership as a contracting criteria and the five-year limitation restricts the number of available drivers to a competitively significant degree. If the agencies found that the rule limited the number of available drivers to a competitively significant extent, the agencies would inquire whether the rule is a reasonable means of achieving a legitimate goal, that is whether a safe-driving record or adequate knowledge of city routes would be less restrictive alternatives of achieving the goal.

Hypothetical Category Number Three

1. Additional Facts: contract cab companies' liability insurers increase their premiums because of risks associated with their hotel business and companies collectively refuse to deal with any hotel that does not either reimburse each of its cab companies for the premium increase or reduce its coverage requirements.

10. Whether characterized as price-fixing or a group boycott designed to reduce output and increase price, this agreement constitutes a *per se* violation of the U.S. antitrust laws. *See FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990).

2. Additional Facts: hotels, which can be held liable for accidents by contract cabs, seek to minimize their insurance premiums by requiring cab companies to file prompt, detailed post-accident reports. Companies collectively refuse to submit the required reports.

11. While the practice described here is arguably *per se* illegal, it is very similar to the conduct which led the FTC to file suit against the Indiana Federation of Dentists.[2] First, we would determine whether this agreement directly limits some form of competition that would have existed absent the agreement. In this hypothetical, absent the agreement, the member companies would have competed with respect to cooperating with the hotels' cost-containment efforts. Even if not a *per se* violation of the antitrust laws, this agreement clearly presents a competitive problem. The agencies would likely oppose such an agreement, without conducting a full-blown rule of reason analysis, unless the association could present and substantiate a procompetitive justification for the agreement.

3. Additional Facts: when one association member has a contract with a hotel, no other member may seek the hotel's business during the term of that contract or discuss with the hotel whether it might seek the business after the contract has expired.

12. This is seriously anticompetitive conduct, but it is not clear it fits any of the traditional categories that have been held to be *per se* illegal under U.S. law. Perhaps the agencies would want to consider the degree to which a prohibition against solicitation during the life of the contract equated to an all-out ban on solicitation. We likely would challenge the conduct either as a *per se* violation or under a truncated rule of reason (*FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 450 (1986)).

4. Additional Facts: No association member may offer telephone pick-up service except through the hotels with which it has a contract.

13. The fact that the two companies here belong to an association which might engage in other procompetitive conduct is irrelevant to the agencies' analysis of this agreement, which we would view as a *per se* illegal agreement not to compete. *See Palmer v. BRG of Georgia*, 498 U.S. 46 (1990)(*per curiam)*(finding territorial allocation *per se* illegal); *United States v. Cadillac Overall Supply Co.*, 568 F.2d 1078 (5th Cir.) *cert. denied*, 437 U.S. 903 (1978)(finding customer allocation *per se* illegal).

NOTES

1. If actually faced with this situation, the agencies would engage in additional factual inquiry to determine whether certification was necessary for effective competition. One factual issue not addressed by the hypothetical is the extent to which hotels rely on certification in awarding contracts to cab drivers and companies. Hotels may also be able to negate any potential competitive harm if they contract with companies and drivers for set rates.

2. The Commission found that the Federation's policy of requiring its members to withhold x rays from dental insurers for use in benefits determinations constituted an unreasonable restraint of trade in violation of Section 5 of the Federal Trade Commission Act. *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 450 (1986). While the Supreme Court refused to apply the *per se* boycott rule to the Federation's activities, it did condemn the practice without applying a full blown rule of reason analysis, noting that in the absence of "some countervailing procompetitive virtue -- . . . -- such an agreement limiting consumer choice . . . cannot be sustained under the Rule of Reason." *Id*. at 459.