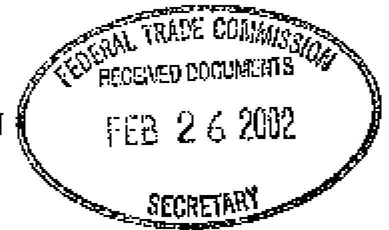
UNITED STATES OF AMERICA
BEFORE FEDERAL TRADE COMMISSION



In the Matter of POLYGRAM HOLDING, INC., a corporation, DECCA MUSIC GROUP LIMITED, a corporation, UMG RECORDINGS, INC., a corporation, and UNIVERSAL MUSIC & VIDEO DISTRIBUTION CORP., a corporation.	DOCKET NO. 9298

ORDER DENYING MOTION FOR SUMMARY DECISION

I. PROCEDURAL HISTORY

On July 30, 2001, the Commission issued a complaint charging Polygram Holding, Inc. ("Polygram"), Decca Music Group Limited, UMG Recordings, Inc., and Universal Music & Video Distribution Corp. with entering into an agreement with non-party Warner Communications Inc. ("Warner") to restrict price competition and agree to forgo advertising in violation of Section 5 of the Federal Trade Commission Act ("FTC Act") 15 U.S.C. § 45.

Respondents filed a Motion for Summary Decision ("Motion") pursuant to Commission Rule 3.24 on January 11, 2002. Complaint Counsel filed its Opposition on February 8, 2002. On

February 19, 2002, Respondents filed a Request for Leave to File Reply Memorandum and their Reply Memorandum. Respondents' motion to file a reply brief is GRANTED. For the reasons set forth below, Respondents' motion for summary decision is DENIED.

II. SUMMARY DECISION STANDARD

Commission Rule of Practice 3.24(a)(2) provides that summary decision "shall be rendered . . . if the pleadings and any depositions, answers to interrogatories, admissions on file, and affidavits show that there is no genuine issue as to any material fact and that the moving party is entitled to such decision as a matter of law." 16 C.F.R. § 3.24(a)(2). Commission Rule 3.24(a)(3) provides that once a motion for summary decision is made and adequately supported, "a party opposing the motion may not rest upon the mere allegations or denials of his pleading; his response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue of fact for trial." 16 C.F.R. § 3.24(a)(2). These provisions are virtually identical to the provisions of Fed. R. Civ. P. 56, governing summary judgment in the federal courts. *In re Hearst Corp.*, 80 F.T.C. 1011, 1014 (1972).

The mere existence of a factual dispute will not in and of itself defeat an otherwise properly supported motion for summary judgment. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986). However, "[w]here the record taken as a whole could not lead a rational trier of fact to find for the nonmoving party, there is no 'genuine issue for trial.'" *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986) (citation omitted). The party moving for summary judgment, bears the initial burden of identifying evidence that demonstrates the absence of any genuine issue of material fact. *Green v. Dalton*, 164 F.3d 671, 675 (D.C. Cir. 1999)(*citing Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986)). "Where there is conflicting

evidence about the material issues of fact, summary judgment is inappropriate." *International Assoc. Conf. Int.* 1995 FTC LEXIS 375, *1 (Nov. 29, 1995).

Once the moving party has properly supported its motion for summary judgment, the nonmoving party must "do more than simply show there is some metaphysical doubt as to the material facts." *Matsushita,* 475 U.S. at 586. The nonmoving party may not rest on mere allegations or denials of its pleading but must "come forward with 'specific facts showing that there is a genuine issue for trial.'" *Id.* at 587 (quoting Fed. R. Civ. P. 56(e)). *See also Liberty Lobby,* 477 U.S. at 256. The inferences to be drawn from the underlying facts must be viewed in the light most favorable to the party opposing the motion. *Matsushita,* 475 U.S. at 587; *International Assoc. Conf. Int.* 1995 FTC LEXIS 375, *1 (Nov. 29, 1995) (Complaint Counsel, as the non-moving party, is entitled to have the evidence viewed in the light most favorable to them and to have all factual inferences made in their favor.). Further, in antitrust cases, summary dismissal is inappropriate where there is a genuine dispute as to the material facts underlying the alleged efficiency defense. *Eastman Kodak Co. v. Image Tech. Servs.,* 504 U.S. 451, 483-86 (1992).

III. FACTUAL ALLEGATIONS

In deciding this Respondents' motion for summary decision, evidence presented by Complaint Counsel, as the non-moving party "is to be believed and all justifiable inferences are to be drawn in its favor." *Anderson v. Liberty Lobby,* 477 U.S. 242, 255 (1986). The allegations, as stated by Complaint Counsel, follow.

This case involves a collaboration between two music companies, PolyGram and Warner Music Group ("Warner"), to produce and distribute audio and video recordings of a 1998 live

performance by the "Three Tenors" – Luciano Pavarotti, Placido Domingo, and Jose Carreras. PolyGram and Warner agreed to ban price reductions and advertising on their own earlier Three Tenors ("3T") releases – PolyGram's recording of the 3T concert in 1990, and Warner's recording of a 3T concert in 1994.

In the summer of 1990, on the eve of the final match of the World Cup soccer tournament, Carreras, Domingo, and Pavarotti performed together in Rome. PolyGram acquired from the concert promoter the right to distribute recordings of the Rome concert. This 1990 release ("3T1") became the best selling classical recording of all time.

In 1994, the Three Tenors planned a second World Cup performance in Los Angeles. Concert promoter Tibor Rudas offered to license to PolyGram the rights to the concert. When PolyGram and Rudas were unable to agree upon terms, Rudas signed a contract with Warner to distribute the 1994 Three Tenors album ("3T2"). In response to the release of 3T2, PolyGram advertised that 3T1 was the "original" Three Tenors recording – "unique and unrepeatable." PolyGram marketed 3T1 at several dollars below the price of Warner's 3T2. Three Tenors albums were both among the best-selling classical recordings in the United States in 1994, 1995, 1996, and 1997.

In 1996, Tibor Rudas discussed with Warner the next Three Tenors project, a concert in front of the Eiffel Tower for the World Cup in Paris in July 1998. Pavarotti was under exclusive contract with PolyGram. In the Spring of 1997, the Chairman of Atlantic Recording Corp. (a Warner subsidiary) asked PolyGram to allow Luciano Pavarotti to record the project for Warner. Warner and PolyGram decided to share financial and operational responsibility, profits, and losses for the 1998 Three Tenors project. For $18 million Rudas licensed to Warner worldwide

audio, video, and home television rights to the 1998 concert ("the 3T3 Rights"). Warner licensed PolyGram the 3T3 Rights outside the U.S. Warner kept the United States.

In negotiating the terms of the 1998 Three Tenors project, PolyGram and Warner discussed the scope of any covenant not to compete, and agreed in concept that, for five years, neither would release a new Three Tenors album (except as part of the collaboration). Warner stated that the non-compete should not apply to the earlier Three Tenors albums. The final Agreement, dated December 19, 1997, provides that PolyGram and Warner shall each be free to exploit its older Three Tenors albums. PolyGram and Warner worried that their new Three Tenors album would not be as original as the 1990 and '94 releases. Rudas stated that it would consist of selections not appearing on the earlier Three Tenors albums.

PolyGram and Warner representatives in March 1998, started discussing a moratorium on competition and they agreed not to discount or advertise their older Three Tenors albums in the weeks during the release of the new product. They did not want to reduce the profitability of the new Three Tenors albums.

In mid-June 1998, Tibor Rudas informed PolyGram and Warner that the repertoire for the Three Tenors concert would include several songs on 3T1 and/or 3T2. PolyGram and Warner told Rudas of their satisfaction with the repertoire.

On June 25, 1998, Tony O'Brien (Warner) and Paul Saintilan (PolyGram) discussed the moratorium. On July 2 and July 10, 1998, Saintilan provided O'Brien with letters of the terms of the moratorium, seeking Warner's assent. Soon thereafter, O'Brien notified Saintilan that the

offer was accepted, agreeing to a ten-week moratorium on all discounting and promotion of the prior 3T albums.[1]

The central, genuine issue of material fact on this motion is whether the moratorium was agreed to as part of the joint venture agreement, and was essential and necessary to it, or whether it was a separate agreement. Respondents argue that the moratorium agreement was part of the license agreement, dated December 19, 1997, which provided that the parties were required to consult and coordinate with one another regarding all marketing and promotional activities relating to the joint venture, and that on March 10, 1998, within weeks after the joint venture was created, the marketing staffs of the parties began to discuss the marketing plans, eventually resulting in the moratorium. Complaint Counsel argue that its evidence shows a separate agreement. This is an issue for determination after a trial.

IV. LEGAL ANALYSIS

If the potential anticompetitive impact of a challenged horizontal agreement is "obvious" or "clear," the standard for review may be abbreviated. *California Dental Assoc. v Federal Trade Commission*, 526 U.S. 756, 770 (1999) ("*CDA*"); *National College Athletic Assoc. v. Bd of Regents*, 468 U.S. 85, 109 (1984) ("*NCAA*"). If the restraint has no clear anticompetitive potential, then a more extended consideration of its market implications is required, including perhaps a "plenary market examination" of market definition and market power. *CDA*, 526 U.S. at 779.

[1] Respondents argue that they never agreed to the moratorium, and admit it only for the purpose of their motion.

Where the restraint is deemed to be anticompetitive, the next step is to consider any efficiency justification. An efficiency argument may be deemed implausible on its face where it is pretextual, or premised upon the claim that competition is unworkable or undesirable.[2]

If the efficiency argument is determined to be plausible it must be valid, and may be rejected where it is speculative or unproven,[3] where there is a less restrictive alternative,[4] where the argument sweeps too broadly,[5] or where the restraint is not an effective remedy for the competitive problem that it purports to address.[6] Where, a restraint is ancillary to a collaboration, the defendant must show that the restraint is "necessary" in order to achieve the procompetitive benefits of the collaboration. *NCAA*, 468 U.S. at 97-8; *Broadcast Music Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. at 21-3 ("*BMI*").

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[2] *Federal Trade Commission v. Indiana Federation of Dentists,* 476 U.S. 447, 463 (1986) ("*IFD*"); *NCAA,* 468 U.S. at 116-7; *National Soc'y of Professional Engineers v. United States,* 435 U.S. 679, 696 (1978) ("*NSPE*").

[3] *IFD*, 476 U.S. at 463 (1986); *Chicago Pro. Sports, Ltd. Partnership v. Nat'l Basketball Assoc.*, 961 F.2d 667, 674-76 (7th Cir. 1992).

[4] *NCAA*, 468 U.S. at 114; *Arizona v. Maricopa County Med. Soc'y,* 457 U.S. 332, 351-52 (1982); *NSPE,* 435 U.S. at 696; *Chicago Pro. Sports*, 961 F.2d at 674-76; *In re Mass. Board of Registration in Optometry*, 110 F.T.C. 549, 607-08 (June 13, 1988).

[5] *IFD*, 476 U.S. at 463; *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 649-50 (1980); *NSPE*, 435 U.S. at 696; *Mass. Board,* 110 F.T.C. at 607-08.

[6] *NCAA*, 468 at 116, 119; *Law v. NCAA*, 134 F.3d 1010, 1022-24 (10th Cir. 1998).

A. The Standard for Analyzing the Challenged Restraints

Certain categories of restraints almost always tend to raise price or reduce output; the presumptively anticompetitive effects of such agreements are "intuitively obvious."[7] Unless it is part of and essential to a joint venture, the agreement between PolyGram and Warner not to discount 3T1 and 3T2 may be a form of price fixing,[8] subject to abbreviated review.[9] The agreement between PolyGram and Warner to forgo all advertising – including truthful and non-deceptive, price-related advertising – may be also presumptively anticompetitive.[10] In *CDA*, involving limited advertising restraints in a professional services market, the Supreme Court indicated that a complete ban on truthful, non-deceptive advertising – especially in a commercial market[11] – should continue to be viewed harshly.[12] If the restraints are inherently likely to result

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[7] *CDA*, 526 U.S. at 781; *NCAA*, 468 U.S. at 110.

[8] *Catalano, Inc.*, 446 U.S. at 648 (1980) ("an agreement to eliminate discounts . . . falls squarely within the traditional *per se* rule against price fixing").

[9] *NCAA*, 468 U.S. at 100 (1984) ("[H]orizontal price fixing [is] perhaps the paradigm of an unreasonable restraint of trade.").

[10] *Mass. Board*, 110 F.T.C. 549 (1988). The fact that the moratorium on price and advertising competition was to last only ten weeks may be irrelevant. *Chicago Pro. Sports Ltd.*, 961 F.2d at 674.

[11] *CDA*, 526 U.S. at 773 n.10 ("'It would be unrealistic to view the practice of professions as interchangeable with other business activities, and automatically to apply to the professions antitrust concepts which originated in other areas.'") (*quoting Goldfarb v. Virginia State Bar*, 421 U.S. 773, 788-89 n.17 (1975)).

[12] *CDA*, 526 U.S. at 773 ("the restrictions at issue here are very far from a total ban on price or discount advertising").

in anticompetitive effects, market definition is not a necessary element of the analysis.[13] Here, factual inquiry is required to determine whether the restraints are presumptively anticompetitive.[14]

B. Plausible Efficiency Argument

Respondents assert that if the party defending a restraint identifies an economically plausible procompetitive justification, then the challenged agreement must be reviewed under the fullest rule of reason.

The *CDA* decision does not support Respondents' thesis. In *CDA*, the Supreme Court considered restrictions on certain non-verifiable advertising claims adopted by an association of dentists. The association claimed that the restrictions were designed to avoid false and deceptive claims in a market characterized by "striking disparities between the information available to the professional and the patient." *CDA*, 526 U.S. at 771. The Court ordered a more detailed consideration of "empirical evidence of procompetitive effects" in the context of a "quick look" analysis. *Id.* at 775 n.12.[15] The Court ordered an abbreviated analysis of the proffered efficiency

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[13] *Law v. NCAA*, 134 F.3d 1010, 1020 (10th Cir. 1998) ("[W]here a practice has obvious anticompetitive effects – as does price-fixing – there is no need to prove that the defendant possesses market power.").

[14] *See* Expert Report of Dr. Stephen Stockum ¶ 11 (opining that in absence of efficiency justification, price and advertising restraints adopted by PolyGram are likely to have anticompetitive effects). In reaching these conclusions, Dr. Stockum relies upon economic theory and empirical research. *See* Complaint Counsel's Statement of Material Facts ¶ 63 and articles cited therein.

[15] *CDA*, 526 U.S. at 779-81 ("Saying here that the Court of Appeals's conclusion at least required a more extended examination of the factual underpinnings than it received is not, of course, necessarily to call for the fullest market analysis . . . . What is required, rather, is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint.").

justifications without an examination of market definition, market power, or actual anticompetitive effects. If the Three Tenors moratorium price restrictions and advertising bans are *prima facie* anticompetitive, the burden shifts to the Respondents to advance a plausible and valid efficiency justification. *Id.* at 769-70.

Respondents also argue that, since they have plausible efficiency justifications, a rule of reason analysis requires that Complaint Counsel prove anticompetitive effects and that, because Complaint Counsel disclaim reliance on a rule of reason analysis, judgment in their favor must be entered. Complaint Counsel, however, dispute and want to disprove at trial the "plausibility" of PolyGram's proffered efficiency justifications at trial as pretextual, and legally insufficient. Respondents' efficiency justification defense raises a factual issue for trial.

C. Restraints Adopted "In the Context of" a Joint Venture

Respondents argue that, if their efficiency justification is "related to" or "adopted in the context of" a joint venture, the restraint cannot be condemned as *per se* unlawful, but rather must be subjected to the fullest rule of reason review. Horizontal restraints will not escape condemnation solely because they arise in the general context of a joint venture. Rather, the restraint must have been "necessary" or "essential" to enable the efficiency-enhancing integration that renders the joint venture procompetitive.[16] Respondents argue that the moratorium was an

[16]Although language in *CDA*, 526 U.S. at 778, would seem to indicate that a defendant need only prove that a restraint was "plausibly related to a venture's procompetitive effects," other cases have required a stricter standard. *E.g.*, *BMI*, 441 U.S. at 23 (declining to apply *per se* analysis to ancillary price restraint where "the agreement on price [was] necessary to market the product"); *NCAA*, 468 U.S. at 101 (noting that the "critical" fact warranting more in-depth rule of reason review, as opposed to *per se* condemnation, of the challenged restraint was that the "case involve[d] an industry in which horizontal restraints are essential if the product is to be available at all"); *Maricopa*, 457 U.S. at 352-53 (maximum fee schedule established by physicians found
(continued...)

important part of their marketing plans for the new album. This argument, although vague, raises factual disputes which would prevent summary judgment.

Respondents argue that parties to a joint venture are not obligated to compete directly with their venture. Where two firms have a cooperative relationship there may be competitive gains from forbidding them to cooperate in ways that yield no economies but simply limit competition.[17]

The issue is whether each of the respondents would have entered into the joint venture without assurance by the other that it would not discount or advertise its own earlier Three Tenors album during the introduction of the joint Three Tenors album in 1998 as agreed in the moratorium. *Polk Bros., Inc. v. Forest City Enterprises, Inc.*, 776 F.2d 185, 190 (7th Cir. 1985). If so, the moratorium was separate from and not ancillary to the joint venture.

D. Ancillary Restraints

If PolyGram and Warner decided it was unnecessary to bring their earlier Three Tenors albums, 3T1 and 3T2, into the venture in order to create 3T3, that choice probably precludes the

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[16](...continued)
unlawful where it was unnecessary; schedule set by insurers was a workable alternative); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 227 (D.C. Cir. 1986) (restraints adopted by joint venture were upheld given that they were "reasonably necessary to the business it is authorized to conduct"); *General Leaseways, Inc. v. National Truck Leasing System*, 744 F.2d 588, 594-95 (7th Cir. 1984) (market division agreement among truck leasing companies judged illegal as it was not necessary to the venture).

[17] *General Leaseways*, 744 F.2d at 594.

parties from coordinating the price and advertising for these non-venture products.[18] Although the facts are in dispute, it appears that Warner licensed its competitor PolyGram to distribute 3T3 outside of the United States, and may have later exacted a promise that PolyGram would not compete with Warner inside of the United States. If the challenged moratorium was not ancillary to the joint venture agreement and restricted price and advertising competition on non-venture products, it would exceed the scope of the parties' integration and could be condemned as a matter of law.[19]

E. Efficiency Justifications

If the joint venture agreement was in place before discussions of the moratorium commenced, it would not justify the challenged restraints.[20] If the restraints here are not essential to the joint venture, this case involves presumptively anticompetitive restraints, and Respondents

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[18] *United States of Am. v. Visa U.S.A. Inc.*, 163 F. Supp. 2d 322, 405-06 (S.D.N.Y. 2001) (agreement prohibiting members of Visa and MasterCard networks from offering a third competing product – American Express or Discover card – judged illegal); *In re Brunswick Corp.*, 94 F.T.C. 1174, 1275-77 (1979) (agreement restricting venturer's sale of pre-existing, non-venture product judged *per se* illegal), *aff'd as modified sub nom. Yamaha Motor Co. v. FTC*, 657 F.2d 971, 984 (8th Cir. 1981).

[19] The cases in which restraints were upheld involved restraints on joint venture assets. *BMI*, 441 U.S. 1, 24 (restraint solely concerned pricing of blanket license that was product of the joint venture; participants were free to separately license and price their individual works); *Rothery*, 792 F.2d 210, 214 (restrictions concerned venturers' use of joint venture assets); *Polk Bros.*, 776 F.2d at 189 (restraint applicable to sales from jointly constructed facility; venturers remained free to increase output from separately operated facilities).

[20] *Blackburn v. Sweeney*, 53 F.3d 825, 827 (7th Cir. 1995) (allocation of territories was not ancillary to agreement to dissolve law partnership where restraint was adopted after the termination of the partnership); *Polk Bros.*, 776 F.2d at 189 ("A court must ask whether an agreement promoted enterprise and productivity at the time it was adopted.").

would have the burden of coming forward with a valid efficiency justification. Respondents must show how the moratorium was necessary and how it benefitted consumers and competition

Respondents advance four arguments in support of the agreement not to compete. All relate to the marketing (not production) of 3T3. Some arguments raise factual issues which preclude summary judgment.

1. Profit maximization

Respondents' assertion that the moratorium would assist PolyGram and Warner "to recoup" their investment does not appear to be a procompetitive (*i.e.*, pro-consumer) justification for the moratorium. "'We do it because it's more profitable' is not a defense" under the FTC Act.[21]

2. Consumer confusion

Respondents argue that the moratorium on discounting and promotion of older Three Tenors albums helped eliminate the risk that some consumers would confuse the various Three Tenors albums and not purchase the new album that they intended to buy. Analogous challenges were dismissed by the Supreme Court, with the observation that the argument amounts to "nothing less than a frontal assault on the basic policy of the Sherman Act."[22] Further, there is no

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[21] *Chicago Pro. Sports Ltd. Partnership v. NBA*, 754 F. Supp. 1336, 1359 (N.D. Ill. 1991), *aff'd*, 961 F.2d 667 (7th Cir. 1992). *See also Law v. NCAA*, 134 F.3d at 1023; *Delaware & Hudson Railway Co. v. Consolidated Rail Corp.*, 902 F.2d 174, 178 (2d Cir. 1990); *FTC v. Superior Court Trial Lawyers Assoc.*, 493 U.S. 411, 422 (1990).

[22] *IFD*, 476 U.S. at 463 (rejecting claim that providing X rays to insurance companies will necessarily lead then to make unwise and dangerous choices); *NSPE*, 435 U.S. at 694 (rejecting claim that competitive bidding will necessarily lead to inferior engineering work).

evidence in the summary judgment record that consumers were in fact confused in selecting among the various Three Tenors albums.

Respondents assert that if earlier Three Tenors albums had been discounted, then music retailers may have positioned these products prominently in their stores, resulting in a "cluttered selling proposition." There is a fact dispute as to whether music retailers display their products in a manner that would not confuse their customers. Further, a less restrictive remedy might have been to make the packaging for 3T3 more distinct. A seller is not permitted to make its product appear unique by suppressing competing products.[23]

3. Marketing strategy

Respondents next assert that the moratorium "reflected a commercially sound marketing strategy," similar to the strategy that would be adopted if a single firm owned all three Three Tenors albums in 1998. This defense relies upon disputed facts. There is evidence, however, that the moratorium was not necessary and that a sound and effective marketing strategy for the 1998 Three Tenors album might have been developed that did not depend upon reduced competition from the earlier Three Tenors albums.[24] In 1994, Warner successfully launched 3T2 without restricting PolyGram's marketing activity in support of 3T1.

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[23] *NCAA*, 468 U.S. at 116-17.

[24] *Cf. NCAA*, 468 U.S. at 114 (efficiency justification rejected on the basis of factual finding that "NCAA football could be marketed just as effectively without the television plan").

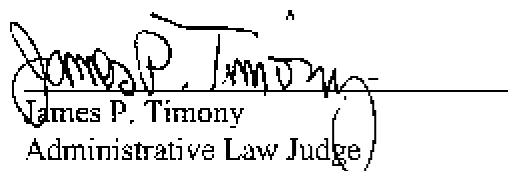
4. Free riding

Respondents' free riding defense raises factual questions that must be addressed at trial.[25] At least some of the costs of any free riding might have been mitigated by a joint advertising arrangement.[26] PolyGram and Warner apparently agreed to share the 3T3 advertising costs incurred during the moratorium period and "when payment is possible, free-riding is not a problem because the 'ride' is not free." *Chicago Pro. Sports*, 961 F.2d at 675.

Finally, there appear to be less restrictive alternatives for the free riding concern. According to PolyGram's expert witness, the danger that advertising for 3T3 may have benefitted the older Three Tenors albums arose principally because 3T3 was not sufficiently different from 3T1 and 3T2. PolyGram could have made 3T3 more distinct through a more distinct repertoire or by other means.

The motion for summary decision is DENIED. Counsel shall confer and file by February 28, 2002, any additional stipulated material facts as to which there is no dispute.

ORDERED:



James P. Timony
Administrative Law Judge

Date: February 26, 2002

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[25] Respondents argue that Complaint Counsel's expert conceded the plausibility of proffered efficiency justifications. Dr. Stockum's testimony acknowledged that it is "plausible" that advertising for 3T3 may lead some consumers to purchase 3T1 or 3T2. This alone is insufficient to establish a meritorious free rider defense.

[26] H. Hovenkamp, *Federal Antitrust Policy: The Law of Competition and Its Practice* at 203 § 5.2b3 (2d ed. 1999) (where firms that benefit from advertising pay a proportionate share of the costs of advertising, free rider concerns are ameliorated).