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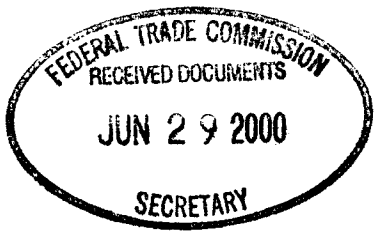

Donald S. Clark
Office of the Secretary
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: **Comments Regarding B2B Electronic Marketplaces**

Dear Mr. Clark:

On behalf of the Antitrust and Intellectual Property/E-Commerce practice groups of Keller and Heckman, LLP, we are pleased to submit these comments. Working as we do with companies and trade associations interested in the B2B marketplace and actively developing B2B initiatives, we support their initial exploration into assessing the antitrust issues of B2B marketplaces, and welcome a continuing dialogue on the issues. Because this is an emerging and dynamic technology with many uncertainties, the Federal Trade Commission (FTC) and the U.S. Department of Justice should not take action that would unnecessarily hinder normal market functioning and corrections. However, because of this very uncertainty, it may be helpful for the FTC to describe, as well as possible given the current state of knowledge, its analytical framework for addressing B2B antitrust law considerations as well as open questions and areas for future consideration.

In April 2000, the FTC and the Justice Department issued their *Antitrust Guidelines for Collaborations Among Competitors*. It provides an analytical framework for examining the organization and operation of B2B sites. In the absence of blatantly illegal conduct, such as price fixing, the competition authorities and the courts should seek to determine whether the procompetitive advantages of the collaboration outweigh any anticompetitive harm from the collaboration.

Defining the characteristics of a competitively healthy B2B site in detail would likely engender heated debate and disagreement, in no small measure because the design, structure and

format of B2B marketplaces vary widely. But, the FTC might facilitate consensus by identifying areas and issues that distinguish e-commerce and B2B sites from more traditional marketplaces.

For example, information exchange among buyers or sellers using a site may be very critical. Ownership and access to individual data is a key consideration. One can envision that a B2B site owned and operated as a joint venture by several firms would create very different antitrust concerns than one operated independently or in accordance with standard antitrust guidelines under which trade associations traditionally operate, where anonymous, aggregate data only is shared when that aggregate data will not reveal information about individual company activities. Thus, it may be inappropriate to disclose either the amount, price or cost of sales or purchases by individual companies. From a broader perspective, B2B sites should be treated as a market for analytical purposes in the same fashion that retail or transactional format is used to help define the product market in merger and general antitrust analysis.

A. General Analytical Framework

Although Internet transactions and B2B sites are based on new or emerging technology, the same fundamental analytical framework continues to apply. The essential question is: How is competition affected? In other words, the courts and enforcement officials will speculate on how the market will function with or without the particular B2B site in question and determine whether its functioning was anticompetitive based on an overall analysis. As a practical matter, enforcement officials or a private company seeking to challenge the operation of a B2B site would initially determine whether any facially illegal activity has occurred such as fixing prices or production, or allocating territories, customers, or markets. Assuming that no facially illegal activity occurred, the competition analysis might be restated as determining whether the procompetitive advantages outweigh any anticompetitive harm from the collaboration. In either case, however, the analysis is complicated by the reality that the Internet offers instant information opportunities, which can be communicated worldwide with the click of a mouse. Whether that constitutes the effective functioning of Adam Smith's perfect marketplace or collusive violations of antitrust laws remains to be seen, and will likely differ in particular cases.

The legality of B2B sites raises a potential host of competition law questions. We have grouped these into nine categories or question areas that have been derived in part from both the *Antitrust Guidelines for Collaborations Among Competitors* and prior FTC work in this area.[1/]

1. Does the B2B Internet site operate as an unadorned agreement to fix prices, curtail output, or divide markets?

[1/] David A. Balto, *Emerging Antitrust Issues in Electronic Commerce* (Nov. 12, 1999)(speech before the 1999 Antitrust Institute); Report by the FTC Staff, *Anticipating the 21st Century: Competition Policy in the New High-Tech, Global Marketplace* (May 1996).

2. Does the B2B site set standards that are anticompetitive?

3. Is the site an essential business facility?

4. Does the site create significant barriers to entry for new participants or significant barriers of entry to Internet transactions by existing competitors?

5. Does the site create anticompetitive network effects?

6. Does the site create a monopoly or a monopsony?

7. Does the site facilitate inappropriate information exchange?

8. Does the site have auction functions that operate in an anticompetitive manner?

9. From an analytical perspective, should Internet sites be treated like retail and other marketing formats that help define the product market?

A brief discussion of each point follows.

1. *Does the Internet B2B site as an unadorned agreement to fix prices, curtail output, or divide markets?*

Are the site's activities illegal *per se*? If the facts show a *per se* violation, there is no defense to finding that the antitrust laws have been violated since courts have concluded that this type of activity has no procompetitive benefits. The judicial trend, however has been to limit application of the *per se* approach and increasingly to apply a rule of reason analysis. This seems particularly appropriate in the B2B context, where certain types of marketplaces will require disclosure of prices, and the nature of the marketplace is such that information will be universally available.

2. *Does the B2B site set standards that are anticompetitive?*

Developing a functional B2B site requires that all participants use technically compatible electronic and hardware infrastructure. As existing case law make clear, there is no inherent problem with standard setting provided that the standard does not work to limit entry or create some *de facto* monopoly control. To the extent that the emerging B2B sites use generally

available software and technical interface standards that are common, open or easily accessible, the standards settings implications can be minimized from an antitrust perspective.[2/]

3. *Is the site an essential business facility?*

Under longstanding U.S. case law, if a particular facility or tool is essential to compete in a market, the owners of that essential facility are obligated to make it available on a nondiscriminatory basis. Contemporary application of this principle has included: (1) computer listing services which are essential for local real estate agents to compete in sales of residential housing, and (2) airline computer reservation systems. While the multiple listing service cases involve direct access, the computer reservation systems have tended to focus on the functioning of those systems. For example, an airline reservation system was challenged on the basis that its programing always presented one or a few airlines' flights and tended to make it awkward to see all of the available flights by airlines that were not principal sponsors of the reservation system. Because of these issues, the U.S. Department of Transportation now regulates these airline reservation systems.

4. *Does the site create significant barriers to entry for new participants or significant barriers of entry to Internet transactions by existing competitors?*

At this point, it could be argued that it is relatively easy for one or more companies to establish a website to facilitate commercial transactions. It is unlikely at the present time that the mere establishment of the B2B site, even by all of the dominant firms in a particular market, would (or should) necessarily be viewed as creating a barrier to entry. If this were demonstrated to be an effect after the operation of the site for an appropriate period, the likely remedy would be to require the site to open access or participation by excluded entities.

5. *Does the site create anticompetitive network effects?*

From an economist's perspective, the term "network effects" describes situations in which the value of the product increases as others use the same products. Network effects can be observed in an actual network such as a telephone system, or in a "virtual network," such as computer software when the software becomes more valuable as more and more people use the same software and more software becomes compatible with that widely used program. Existing examples are the Microsoft Windows operating system or Microsoft Word word-processing program.

6. *Does the site create a monopoly or a monopsony?*

[2/] For additional perspective on this issue, see the enclosed paper: Peter de la Cruz, *Standards Setting, Certification, and Product Endorsement* (1998)

Assume that the B2B site of interest consists of all the major purchases in a particular market that collectively holds 60% or more of the market. This would be the case of the GM-Ford-Chrysler site through which these companies would purchase automobile parts. Antitrust concerns will differ if there are fewer participants with higher market shares than in one where, although 60% or more of the players may participate, the market is fragmented with no truly dominant players. If the Internet site is simply a common framework through which the companies can individually purchase parts, from an antitrust perspective it is arguably no different than these companies using the same telephone network to purchase parts today. If, however, the site is used by the automobile manufacturers to jointly purchase similar parts, or engage in certain types of collective behaviors, antitrust concerns arise.

In the United States, it is not illegal for an individual company to obtain a monopoly position based on its individual, superior, competitive performance. However, collective activity to obtain a monopoly position can be a "conspiracy in restraint of trade," attempted monopolization or an unfair business practice under Sections 1 and 2 of the Sherman Act, or Section 5 of the FTC Act, respectively. At this junction, it appears that a rule of reason analysis would likely be required to demonstrate that collective buying, even in this sort of heavily concentrated marketplace, is forbidden. Case law supports buyer cooperatives on the theory that they merely enhance purchasing efficiencies and will result in lower consumer prices. Theoretically, if one can demonstrate that this purchasing collective has monopsony power, meaning the ability to obtain goods below competitive costs for extended periods of time, or if, collectively, the companies refuse to deal with suppliers outside their own online marketplace, that action could be challenged. Nonetheless, there are immense proof problems with these analyses and the time to resolve these questions may be so long that the competitive harm cannot realistically be undone. Clearly, the unconcentrated nature of the venture is a factor to consider.

A critical issue meriting separate consideration involves who holds or has access to data about site usage and orders, which leads to the following question.

7. *Does the site involve inappropriate information exchange?*

The impact of information exchanges is closely related to the monopoly and monopsony questions as well as a number of *per se* violations such as fixing price and production. But, analysis in the B2B context, tends to lead to paradoxical results. For example, price posting may be necessary to facilitate comparison shopping by buyers. But, if the sale price, amount of raw materials or parts purchased by each manufacturer is available from the B2B site, that information could be used by the participants as a guide to their own pricing and purchasing decisions, may reveal the cost and profit margins of its competitors, or otherwise be used to facilitate collusive behavior. Thus information sharing among participants at all levels in the B2B site must be carefully managed to avoid these effects while not hobbling normal competitive interplay. These concerns may be exacerbated further based on the ownership of

transactional information. In other words, if a market participant (or group of participants), trades in the marketplace and also owns the marketplace, with access to and control over the information of both its competitors and buyers or sellers in the marketplace, competitive concerns are heightened.

8. *Does the site have auction functions that operate in an anticompetitive manner?*

There is nothing inherently wrong with auctions. Arguably, Internet auction sites may reduce transaction costs and benefit consumers. But, auctions in an Internet setting may operate as collusive tools. In other words, there is a possibility that the exchange of price information or bids on line could operate to stabilize or increase prices among cooperating competitors. As a few observers have noted, in the Internet age, the dividing line between Adam Smith's perfectly informed market participants and collusion has not been defined.

9. *Should Internet sites be treated like retail formats that help define the product market?*

We recommend that Internet sites be treated in the same fashion as other retail formats. Retail format is used to define the relevant product market within which the effect on competition of a retailer's activities should be measured.[3/] This means that the type of service offered by the retailer, such as the type and size of its stores and its product range, are important factors in defining the product market. This was true for the supermarket merger cases of the past, and it is true for the large retail buyers of today. For example, in *Staples/Office Depot* the relevant product market was defined by the court as "the sale of consumable office supplies through office supply superstores . . . ,"[4/] because the record revealed a low elasticity of demand among consumers between office supplies sold by superstores such as Staples and those sold by other retailers such as Wal-Mart. This definition is consistent with the general rule that, when determining a relevant product market, "[t]he outer boundaries of [such] market are determined by the reasonable interchangeability of use [by consumers] or the cross-elasticity of demand between the product itself and substitutes for it."[5/]

3/ This topic is discussed at length in *At a Store Near You*, which appears as attachment 6 to the April 14, 2000, filing with the FTC by Robert A. Skitol, captioned "Petition to the Federal Trade Commission on Behalf of the International Bakers Association . . . for the Issuance of Enforcement of Guidelines on Slotting Allowances in the Grocery Industry,"

4/ *Federal Trade Commission v. Staples, Inc. and Office Depot, Inc.*, 970 F. Supp. 1066, 1080 (D.D.C. 1997).

5/ *Brown Shoe v. United States*, 370 U.S. 294, 325 (1962) (footnote omitted); *Staples/Office Depot*, 970 F. Supp. at 1074, 1080.

The competition analysis should look at the effects on all market levels. Using the GM-Ford-Chrysler example, the competitive effects would be considered for the automotive parts supplier market (including the market for equipment and raw materials used to make automobiles), the automobile manufacturer market, and the retail automobile sales market. These three markets are intended to be illustrative only; other markets may be involved.

In addition to these nine broad issues, there are additional factors that an antitrust analysis should consider. These include consideration of current or historical market practices and the overall competitive profile of the industry. The real challenge is to determine what characteristics B2B sites have that distinguish them from traditional markets. The most frequently mentioned aspect is the speed of information exchanges among large groups of people. Within this context, conduct that may not have been troublesome in more traditional market settings may create anticompetitive effects in the Internet setting. On the other hand, information distribution and competitor coordination that may have been suspect in traditional markets may have a procompetitive effect in the Internet setting.

At this point it is not even clear that the B2B sites will operate as an electronic market or simply hierarchical mechanism in which transaction costs are reduced. "In essence, under a hierarchical mechanism, value chain activities are controlled and directed by management decisions either within a single firm or a cross circle interacting firms."[6/] In contrast, "when a market mechanism is at work, the flow of materials and services through the value chain is coordinated by a decentralized price system."[7/]

One theme of speculation predicts that the new B2B sites will open competition to many firms, particularly based on analysis of telecommunications systems. But, these B2B networks may serve to strengthen existing commercial relationships and lock in partners by increasing the cost of switching to a new trading partner. While this may not be initially self evident, consider that if an established electronic trading relationship is in place, those transactional costs are minimized. If a new supplier appears, particularly for a large commercial endeavor, it is likely that some type of review and investigation would be necessary to validate the propriety of changing suppliers. This review and validation of the new supplier is a form of transactional costs and could work in favor of existing suppliers.

6/ Charles Steinfield, Robert Kraut, and Alice Plummer "The Impact of Interorganizational Networks on Buyer-Seller Relationships." This paper can be found at http://www.ascusc.org/jcmc/voll/issue3/steinfld.html.

7/ *Id.*

B. Additional Antitrust Issues

While we have not endeavored to prepare a comprehensive list, there are a number of specific issues or market-context circumstances that likely merit consideration in reaching conclusions as to impact on competition.

- Is the site limited to individual seller and purchase agreements, or does it involve collective buying? Collective buying is clearly legal, but antitrust concerns may arise when the market is very concentrated or when the cooperative buying accounts for the lion's share of the market.[8/]

- Is participation available on nondiscriminatory terms using software and connection standards that are readily available when the Internet site serves as a market or purchasing vehicle?

- Are there capacity-related purchasing or selling requirements, such as requiring 10% or 90% of a company's sales or purchases in the relevant product market to be made through the site?

- Can participants float proposed, future prices in an effort to learn the reactions of their competitors?

C. Conclusion

The emergence of B2B sites raise a number of important questions. At this stage, the FTC's the best path forward may be to publically clarify the antitrust framework it will employ and perhaps the indicia of competitively healthy B2B sites. Except in those hopefully rare

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[8/] We understand that most of the B2B sites that the government has reviewed function as a marketplace for individual transactions as opposed to facilitating collective buying and selling. Source: remarks of Mary Jean Moltenbrey, Director of Civil Non-Merger Enforcement, Antitrust Division, U.S. Justice Department, before the 36th Annual Sumposium on Associations and Antitrust (May 17, 2000)(Bar Association of the District of Columbia).

instances when the B2B structure is so clearly anticompetitive that a *per se* rule should apply, a rule of reason approach seem best suited to allow for the development of these marketplaces in a manner that achieves market efficiencies without violating the antitrust laws.

Sincerely,

Peter L. de la Cruz Sheila A. Millar

Enclosure

Standards Setting, Certification, and Product Endorsement

by: Peter de la Cruz
Keller and Heckman[1]
Washington, D.C.

A noted professor of political science once described the Supreme Court's role as highly ambivalent and uncomfortably dysfunctional. He then proceeded with some elegance to describe the different forces exerted on the court and the conflicting goals that the court attempted to realize. Association standard-settings setting, certification, and endorsement activities raise the same tensions of ambivalent roles and goals. This ambivalence arises because standard-setting may promote competition by improving choice and product interchangeability. On the other hand, standards may also suppress competition or technology. Similarly, even a well-developed and acceptable standard may, over time, begin to stifle competition if it does not allow for technological and other market developments. The Supreme Court aptly summarized this in the *Allied Tube* case: [2]

> Agreement on a product standard is, after all, implicitly an agreement not to manufacture, distribute, or purchase certain types of products. Accordingly, private standard setting associations have traditionally been objects of antitrust scrutiny. When, however, private associations promulgate safety standards based on the merits of objective expert judgements and through procedures that prevent the standard setting process from being biased by members with economic interests in stifling product competition those private standards can have significant pro-competitive advantages. It is this potential for procompetitive benefits that has led most courts to apply rule-of-reason analysis to product standard-setting by private associations.

The statements in the 1988 *Allied Tube* decision echo those made two generations earlier in the *Maple Flooring* case.[3] Except when standard-setting constitutes a price fixing scheme,

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[1] This paper was prepared for presentation on February 18, 1998 at the 34th Annual Symposium on Trades Association and Antitrust Law sponsored by the Trade Association and Antitrust Law Committee of the Bar Association of the District of Columbia.

[2] *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 500 (1988)(citations omitted).

[3] *Maple Flooring Mfrs. Ass'n v. United States*, 268 U.S. 563 (1925).

courts generally evaluate standard-setting under the rule-of-reason.[4] The rule-of-reason analysis means that the courts will look at all of the circumstances in each case to determinate whether competition has been harmed.[5]

Trade association staff, members, and attorneys who counsel on these matters, face a more challenging role than the courts. In litigation, the question is evaluating the competitive effects of past action. In counseling, the task is to provide a framework under which activities will not result in antitrust or other liability claims. For the purposes of this morning's presentation, we focus on a number of pitfalls that may arise from standard-setting and related activities.

A. Basic Motivation

The importance of a reasonable justification for a standard is an important, and often overlooked, criteria. The case law is somewhat mixed as to whether a safety or public health justification is really relevant to an antitrust competition analysis.[6] However, the existence of a clear and reasonable basis for the standard can, as a practical matter, be quite influential with enforcement officials, judges, and juries. The absence of an obvious and articulated basis raises a number of questions concerning motivation and intent.

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[4] *See Allied Tube*, 486 U.S. at 500; *Consol. Metal Prods, Inc. v. Am. Petroleum Inst.*, 846 F.2d 284 (5th Cir. 1988).

[5] Justice Brandeis' description of the rule of reason is still instructive today:

> Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation or the reverse; but because knowledge of intent may help the court to interpret facts and to predict consequences. *Bd of Trade of City of Chicago v. United States*, 246 U.S. 231, 244 (1918).

[6] For an excellent summary of the case law and further discussion on this point *see,* Harry S. Gerla, *Federal Antitrust Law and Trade and Professional Association Standards and Certification*, 19 U. Dayton L. Rev. 471, 476-484 (1994).

A recent example of a well-planned standard was the subject of a May 1997 business review letter by the Justice Department's Antitrust Division. The letter expressed no objection to a proposal by the National Elevator Industry, Inc., a trade association of escalator manufacturers and installers, to try to develop an improved escalator safety standard. The socially desirable benefits of the standard were clear, and the Justice Department concluded that the standard would not be designed to disadvantage non-members nor in itself raise competitive concerns. Again, we are not arguing that a valid safety or health rationale will immunize an anticompetitive standard from antitrust attack, but a sound basis may be important when the competitive impact is unclear.

B. Standard-Setting and Price Fixing

Early cases involving standard-setting frequently focused on price impact. These cases involved activities such as collusive use of delivered prices throughout an industry, an agreed classification of buyer categories for discounting purposes, agreements on standard terms of sale, attempts to impose production quotas, or other restrictive parameters.[7]

In certain situations, the distinction between ethical criteria and price competition may disappear. For example, in 1996, the Justice Department reached a settlement with the Association of Family Practice Residency Directors. This association consists of directors of hospital residency programs. The association had an ethical rule which barred residency programs from offering individual economic incentives to attract family practice medical residence. As Anne Bingaman, then Assistant Attorney General heading the Antitrust Division stated, "professional associations must resist the impulse to use their collective power to restrict competition among their members."[8]

1. Scarce Raw Material

One older case meriting emphasis involves attempts by association members to deal with a shortage of an important raw material. In *National Macaroni Manufacturers Association v. FTC,* members of the association were faced with the shortage of the primary ingredient used to

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[7] See *C-O-Two Fire Equipment Co. v. United States*, 197 F.2d 489 (9th Cir. 1952); *Bond Crown & Cork Co. v. FTC*, 176 F. 2d 974 (4th Cir. 1959); *Fort Howard Paper Co. v. FTC*, 156 F.2d 899 (7th Cir. 1946); *Milk and Ice Cream Can Inst. v. FTC*, 152 F.2d 478 (7th Cir. 1946; *Ass'n. of Coupon Book Mfrs.*, FTC Dkt. 5532, 45 FTC 219 (1948); *Liquid Tight Paper Container Ass'n .et al.,* FTC Dkt. 4675, 40 FTC 630 (1945); and *Elec. Alloy Section of Nat'l. Elec. Mfrs. Ass'n.*, FTC Dkt. 4558, 36 FTC 336 (1943).

[8] Press release of May 28, 1996 "Justice Department moves to stop anticompetitive actions of national medical residency trade association."

make macaroni, durum wheat.[9] The association passed a resolution that millers should offer a blend of 50% durum and other wheats, and that macaroni manufacturers use the 50% blend to "maintain highest quality possible."[10] The Federal Trade Commission (FTC) ruled that the resolution was an attempt to lower the total industry demand for the scarce durum wheat and reduce price competition for the available supply.[11]

2. Restricting Terms of Trade

A somewhat more recent case involving restricted terms of trade is *Catalano v. Target Sales*.[12] In *Catalano,* local distributors of beer and alcoholic beverages agreed to change the terms of trade so that they would sell to retailers only if payment were made in advance or upon delivery. Prior to the agreement, the wholesalers had extended credit without interest up to the 30- and 42-day limits permitted by state law. In a *per curium* opinion, the Court concluded that this was simple price fixing.

A more timely example involves a professional association. In 1996, the Federal Trade Commission issued an order prohibiting the California Dental Association (CDA) from imposing restrictions on the advertising and solicitation practices of California dentists. The FTC opinion found that broad restrictions on advertising low prices and discounts was as "anticompetitive as outright price fixing" and deserved to be "treated harshly under the antitrust laws."[13]

C. Product and Technology Exclusion

Questions concerning the use of standards to exclude competing products from the marketplace have garnered significant attention over the last two decades. The trilogy of leading cases in this area consists of *American Society of Mechanical Engineers, Inc. v. Hydrolevel*

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9 *Nat'l Macaroni Mfrs. Ass'n v. FTC*, 345 F.2d 421 (7th Cir. 1965).

10 *Nat'l Macaroni Mfrs. Ass'n, et al.*, FTC Dkt. 8524, 65 FTC 583, 598-600 (1964).

11 *Id.* at 611.

12 *Catalano, Inc., v. Target Sales, Inc.*, 446 U.S. 643, 644 (1980).

13 *FTC v. California Dental Association,* FTC Dkt. 9259 (Slip copy); FTC press release, "FTC upholds charges against advertising restrictions by California Dental Association," (March 26, 1996). Available on the FTC website at http://www.ftc.gov/opa/9603/cda-cd.htm.

Corp.,[14] *Allied Tube & Conduit Corporation v. Indian Head, Inc.*,[15] and *Sessions Tank Liners, Inc. v. Joor Manufacturing, Inc.*[16] Since the cases have been well summarized in earlier papers at this Symposium and in standard reference materials, we only highlight their essential teachings here.

In *Hydrolevel,* an association which issued and interpreted a product standard was liable under the antitrust laws for the fraudulent acts of its members committed with the apparent authority of the association, even though the association never ratified, authorized, or derived any benefit. An officer of a company which made fuel cut-offs for boilers was also the vice chairman of the association's subcommittee responsible for fuel cut-off equipment standards. He fraudulently caused the subcommittee's chairman to issue, on the association's letterhead, an "unofficial" determination that a competitor's product did not comply under the applicable association standard. Under the association's rules, subcommittee chairman could issue unofficial interpretations without clearing them with the subcommittee. In applying the apparent authority theory to antitrust law for the first time, the Court stated that a rule that imposes liability on the standard-setting organization, which is best situated to prevent such violations, is consistent with congressional intent to deter such violations.[17]

In *Allied Tube,* the plaintiff was a manufacturer of plastic conduit that sued a group of manufacturers of steel conduit. The plaintiffs claimed that the steel conduit manufacturer packed a meeting of the National Fire Protection Association, whose members voted to reject a proposal to amend the association's model fire code. The amendment would have allowed the use of plastic conduit. The district court held that the challenged activity was immune under the *Noerr -Pennington* doctrine because the association was in essence a quasi-legislative arm of municipal governments that applied the model fire code. But, the Supreme Court disagreed on the grounds that the association was a purely private body and did not qualify as a government entity to which manufacturers were directing their lobbying efforts. The Court said that "the antitrust laws should not necessarily immunize what are in essence commercial activities because they have a political impact."[18]

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[14] *Am. Soc'y of Mechanical Eng'rs, Inc. v. Hydrolevel Corp.*, 456 U.S. 556 (1982)

[15] *Allied Tube,* 486 U.S. 492 (1988).

[16] *Sessions Tank Liners, Inc. v. Joor Mfg., Inc.,* 786 F.Supp. 1518 (CD Cal. 1991), rev'd on other grounds 17 F.3d 295 (9th Cir.), cert. denied, 115 S. Ct. 66 (1994).

[17] *Hydrolevel,* 456 U.S. at 573.

[18] *Allied Tube*, 486 U.S. at 507.

The last of our trilogy is *Sessions Tank Liners, Inc. v. Joor Manufacturing, Inc.*[19] In *Sessions Tank Liners,* plaintiff was in the business of lining storage tanks and competed with the defendant who manufactured and sold tanks. A subcommittee of the Western Fire Chiefs Association added a provision to the Uniform Fire Code which, in effect, prohibited the use of plaintiff's tank lining service. This prohibition was based entirely on the testimony of the defendant's president. The association did not seek any input from the plaintiff or any other person prior to adopting the standards. Also, some of the statements made by the defendant's president were false and intended to mislead the subcommittee into adopting a standard that would injure its competitor.

The district court, apparently acting consistently with the Supreme Court's direction in *Allied Tube,* found the conduct to be anticompetitive and an antitrust violation. The Ninth Circuit did not address the anticompetitive aspect of the claim, but reversed solely on the grounds that the conduct was immune under *Noerr Pennington.* The Ninth Circuit justified its decision on the grounds that "the only anticompetitive injuries that *Sessions* complains of are the direct result of governmental action. . . ." [20]

C. Standards-setting Guidelines

Hydrolevel, Allied Tube, Session Tank Liners, and other cases emphasize the seriousness and detail with which associations must approach standards making. Some guidelines that might be derived from standards-setting cases include:

- Do not develop or use standards as a means of fixing prices, boycotting suppliers, or otherwise restricting competition.

- Provide adequate notice of standard development to all potentially affected parties and provide an opportunity to participate in the development or revision of the standard.

- Develop performance rather than specification standards whenever possible, that is, focus on the performance to be achieved as opposed to product design or composition.

- Avoid discriminating against any participant in the standards development program or against any person or firm potentially affected by the standard.

- Allow periodic review and update when necessary.

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19 *Sessions,* 786 F.Supp. 1518 (CD Cal. 1991).

20 *Sessions,* 17 F.3d at 301.

- Carefully control how compliance or noncompliance with the standard is determined and how any such determination is publicized. Carefully handle any interpretations of the standards, and limit the persons authorized to make such interpretations.

- Establish and follow procedures that provide adequate notice to potentially affected persons as well as the opportunity for them to participate in and seek review of an interpretation.

- Ensure that there are no agreements to adhere to standards once they are established. Participating parties should have the freedom to follow checklist standard as they see fit.

D. The limits of procedural safeguards

While the case law provides abundant guidance on some points, it may be potentially misleading on the importance of procedural safeguards. In addition, the applicability of the *Noerr-Pennington* doctrine to conduct by companies who are individuals that attempt to influence standards making organizations is unsettled.

In particular in the *Hydrolevel* case, and to a somewhat lesser extent *Allied Tube* and *Sessions,* the absence of adequate procedural safeguards may appear controlling. However, the existence or application of some procedural safeguards, in and of itself, will not end the antitrust analysis. As the Supreme Court stated in *Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Company:*[21]

> The absence of procedural safeguards can in no sense determine the antitrust analysis. If the challenged concerted activity of members would amount to a *per se* violation of the § 1 of the Sherman Act, no amount or procedural protection would save it. If the challenged action would not amount to a violation of § 1, no lack of procedural protections would convert it into a *per se* violation because the antitrust laws do not themselves impose on joint ventures a requirement of process.

Given this pronouncement, why bother with procedural safeguards at all? As a practical matter, the development and adherence to strong procedural safeguards will, in fact, provide real protection for the association and its law-abiding members. In other words, should a company or companies abuse the association's process through fraud or false representations, the procedural safeguards may serve as practical and financial protection from liability.

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[21] *Northwest Wholesale Stationers, Inc. v. Pac. Stationery and Printing Co.*, 472 U.S. 284, 293 (1985).

E. *Noerr-Pennington* Immunity

The *Noerr-Pennington* doctrine, in simplified terms, states that the antitrust laws are not applicable to legitimate group action intended to influence legislative, executive branch, or administrative decision making.[22] From a practical perspective, the model electric code at issue in *Allied Tube* and the Uniform Fire Code at issue in *Sessions Tank Liners* had identical effect. Some commentators have argued that the difference is one of pleading. In the *Allied Tube* case the complaint focused on the effect of the standards making organization's action while in *Sessions Tank Liner* the complaint focused on the effect from government action.[23] While this analysis may be technically accurate, prospectively, this is not a line that companies and their counselors can draw when determining how to approach or manage standards activity. Thus, conservative judgement would recommend that companies treat private standards setting organizations as private standards-setting organizations meaning that their activities before the association would not be immune under *Noerr-Pennington.*

F. Certification

Certification is the process by which a product, service, individual, or institution is evaluated against pre-existing standards and criteria. If the appropriate criteria or standards are met, the individual or company is typically granted the right to use a particular mark or designation to demonstrate compliance with the standard. Certification activities by trade and professional associations may involve programs on product certification, professional credentialing, or academic accreditation. Certification programs are often companions to standard-setting, in which the criteria for certification of a product, individual or institution are established. Product certification provides consumers with information regarding the quality of a product, especially where the information to be communicated is technical or not easily verifiable by the consumer. Similarly, the certification of individuals can demonstrate the achievement of established criteria involving education and professional experience or qualification.

The same rule-of-reason approach applied to analyzing standards applies to certification. For example, in July 1997 the Justice Department approved a proposal by the Post-Tensioning Institute (PTI) that would require all of its manufacturer members to comply with standards governing the way they reinforce concrete using high strength steel wires. At a construction

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[22] The doctrine derives its name from the first two Supreme Court cases in which was articulated. *E. R.R.. Presidents Conference v. Noerr Motor Freight, Inc.,* 365 U.S. 127 (1961); *United Mine Workers of Am. v. Pennington,* 381 U.S. 657 (1965).

[23] Richard S. Taffet, *Antitrust and Trade Associations* at 100-101, Section of Antitrust Law, American Bar Association (1996).

site, high strength steel wires are stressed to a predetermined force by hydraulic jacks at one end and are locked off at both ends by anchoring devices. The steel wires are encased in a sheathing that prevents the wire from bonding with the concrete and allows the wire to move during the tensioning process and even after the concrete is set.

PTI's goal was to improve the reputation of unbonded post tensioning systems and promote their utilization over competing systems or materials. The program was voluntary and open to non-members. While PTI administered the program, it was executed by an organization independent of PTI and its members.

The Justice Department concluded that the association's certification program was acceptable because it would not exclude other companies from competing for construction contacts or unreasonably restrict competition. Indeed, it may have procompetitive effects if it results in improved quality and reputation of the post-tensioning system that the association promotes. In antitrust parlance, the Department stated that "the proposal would not appear to have the effect of facilitating price collusion or reducing output."[24]

In contrast, programs that result in boycotting competitors or fixing prices have been held unlawful.[25] Several cases involving accreditation have involved challenges to the criteria underlying an accreditation decision. Thus, it is important that the underlying standard or criteria be reasonable. In one case, the court held that a decision not to re-accredit a school was not arbitrary or unreasonable when viewed against the organization's accreditation criteria.[26]

Accreditation practices of the American Bar Association have been the subject of several antitrust suits. In *Paralegal Institute v. ABA*, accreditation criteria were found to be reasonable and not a restraint of trade.[27] A dispute with a law school resulted in a U.S. Justice Department investigation into the ABA's accreditation guidelines. The investigation led to a consent decree which imposed detailed reforms on the ABA's accreditation process, including such matters as

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[24] Letter of July 30, 1997 from Joel I. Klein, acting Assistant Attorney General to Douglas F. Rhorman (July 30, 1997).

[25] *See Radiant Burner, Inc. v. Peoples Gas Light & Coke Co*, 364 U.S. 656 (1961) (holding that alleged arbitrary denial of certification stated an antitrust cause of action); *Nat'l Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679 (1982) (holding that rule prohibiting competitive bidding had effect of stabilizing prices).

[26] *Medical Inst. of Minnesota v. Nat'l Ass'n of Trade and Technical Schs.*, 817 F.2d 1310 (8th Cir. 1987); *See also, Transp. Careers, Inc. v. Nat'l Home Study Counsel,* 646 F. Supp 1474 (D.Ind. 1986).

[27] *Paralegal Inst., Inc. v. Am. Bar Ass'n.*, 475 F. Supp. 1123, 1131 (S.D. N.Y.), *affm'd*, 662 F.2d 575 (1980).

accreditation committee membership criteria and the manner in which law schools may appeal the ABA's unfavorable decisions.[28]

In summary, some guidelines for certification include the following points.

- Criteria for certification should be objective and established after consulting potentially affected parties;
- Representations made with respect to testing procedures must be truthful and not misleading;
- Certification should not be limited to a pass/fail, but should involve grading systems so as to convey which of the criteria have been met and permit the applicant to rectify performance deemed sub-standard.
- Applicants denied certification should be afforded minimum due process, including written notice together with the reasons for the denial and an opportunity to present its case in writing or at a hearing. The ultimate decision on an appeal should be made by a body composed of individuals or firms other than those rendering the initial decision.
- Membership in the organization should not be a condition of participating in the certification program.
- Participation in the certification program should be voluntary.
- Fees charged to participate must be reasonably related to the direct and indirect costs of the program.

G. Quality Statements and Product Liability Issues

In addition to the antitrust issues that accompany certification program development, associations must be sensitive to other product liability considerations. Nearly 30 years ago, two seminal cases concluded that certifying organizations could be held liable for damages if they were negligent in approving the product and if people foreseeably relying on that certification could be harmed.[29] A more recent case held at the International Association of Plumbing and

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[28] *United States v. Am. Bar Ass'n,* 60 FR 39421 (August 2, 1995) (proposed final judgement and competitive impact statement).

[29] *Hempstead v. Gen. Fire Extinguisher Corp.,* 269 F.Supp 109 (D. Del. 1967); *Hanberry v. Hearst Corp.*, 276 Cal. App. 2d 680 (1969).

Mechanical Officials (IAPMO) held at the association could be liable if it failed to comply with its duty of care to delist substandard pipe.[30] In all of these cases, the courts held that the organization owed a duty of care to consumers and be held liable if lapses in the certification processes resulted in injury.

Product endorsements must be approached carefully. In addition to all of the antitrust and product liability issues, associations must be sensitive to the perceptions which such endorsements create. One current example of these difficulties involves a decision by the American Medical Association (AMA) to enter into an endorsement agreement with Sunbeam Corporation. Sunbeam's Home Health Business includes heating pads, blood pressure monitors, thermometers, air cleaners, and similar products. Sunbeam viewed the AMA endorsement as encouraging consumers to "choose and use our products." Sunbeam also agreed to include AMA information sheets with select Sunbeam products for a five-year period.

The endorsement agreement and AMA insert programs were first publicized on August 12 and 13, 1997. By August 21, the AMA had issued a statement attempting to revise its agreement with Sunbeam. The AMA concluded that its "decision to approve the Sunbeam agreement in the form adopted was an error. As a result, our credibility was called into question." The AMA then decided not to make any product endorsements in the healthcare field and asked Sunbeam to release it from participating in this program on an exclusive basis. AMA also determined that it would accept no money from Sunbeam, other than to recover the costs for including health information in the products.

Sunbeam believed that it had a contract with the AMA and that it would be difficult to re-negotiate with these preconditions. By early September, Sunbeam had filed an action in the federal district court in Chicago seeking to enforce the terms of the five-year agreement, under which the AMA seal would appear on certain Sunbeam products. By mid-September, the Board of Trustees and the American Medial Association announced a reorganization of its top management team. The AMA concluded that there was a systematic breakdown of the AMA's procedures designed to ensure arrangements with other organizations are consistent with AMA policy, and that significant new initiatives are reviewed by the Board of Trustees for their approval prior to implementation. This led to the departure of the AMA's Chief Operating Officer and two other top officers.[31]

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[30] *FNS Mortgage Serv. Corp. v. Pac. Gen. Group, Inc.*, 24 Cal. App. 4th 1564 (1994).

[31] The information on Sunbeam/AMA in this paper was derived from press releases and other materials obtained at the following websites: www.prcentral.com/prlsunbeam, http://europe.cnnfn.com/hot stories/companies/9708/21/intv_dunlap; http://europe.cnnfn.com/hot stories/companies/9709/08/sunbeam/; http://medicine.wustl.edu/@wumsama/amapage.htm; http://www.pcma.org/usae_930.htm; and

And, if this wasn't enough, on December 3, 1997 the Center for Science in the Public Interest (CSPI) asked that an Ethics Task Force be convened by the AMA to investigate whether the association's endorsement of Proctor and Gamble's olestra product is "part of a deal that would have yielded $800,000 to the AMA."[32]

H. Legislative Developments

Trade and professional associations may find themselves named as defendants in lawsuits because they provided information to their members or other associations about the quality or performance of products. Some members of Congress have concluded that the cost of litigation has had a "substantial chilling effect" on the ability and willingness of trade and professional associations to disseminate valuable information.

In response, Sen. Mitch McConnell (R-KY) introduced the *Trade and Professional Association Free Flow of Information Act of 1997* (S.1135) The bill was introduced in August 1997. A similar House bill (H.R. 1542) was introduced by Rep. Sonny Bono (R-CA) in May 1997. The purpose of these bills is to "promote the free flow of goods and services and lessen burdens on interstate commerce by ensuring the free flow of information concerning product defects, quality, or performance among trade and professional associations and their members."

The bills, which have very similar provisions, would remove associations from civil liability for harm caused by the dissemination of information to their members concerning the quality of a product. They also limit those instances when such information may be obtained by a plaintiff through a subpoena. Finally, the bills create a qualified association-member privilege for confidential communications between an association and a member. However, the bills are not drafted to shield associations from fraud or knowingly false statements or statements made with a "reckless indifference to their truth or falsity." Section 3 of the House Bill states:

> (a) IN GENERAL --
>
> (1) IN GENERAL — Except as provided in subsection (b), a trade or professional association shall not be subject to civil liability relating to harm caused by the provision of information described in paragraph (2) by the trade or professional association to a member of the trade or professional association.

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http://www5.yahoo.com/headlines/970920/businessstories/sunbeam_1.html

[32] "Olestra is a noncaloric fat substitute." This PSI press release can be located at http://www.cspinet.org/new/amaoles.htm.

(2) INFORMATION — The information described in this paragraph is information relating to a product concerning --
(A) the quality of the product;
(B) the performance of the product; or
(C) any defect of the product.

(3) APPLICABILITY — This subsection applies with respect to civil liability under Federal or State law.

(b) EXCEPTION FOR LIABILITY — Subsection (a) shall not apply with respect to harm caused by an act of a trade or professional association that a court determines, on the basis of clear and convincing evidence, to have been caused by the trade or professional association by the provision of information described in subsection (a)(2) that the trade or professional association —
(1) knew to be false; or
(2) provided a reckless indifference to the truth or falsity of that information.

According to recent reports, the House bill has 24 cosponsors, including five Democrats and 19 Republicans. Sen. McConnell's bill is currently cosponsored by Sen. Jesse Helms (R-NC) and Sen. Tim Hutchinson (R-AR). At this point it is unclear whether the bills will rally further support, but it is worth keeping an eye on their progress.

I. Conclusion

Standards-setting, certification and endorsement activities may be an important and necessary undertaking for many associations. While this presentation has focused on all of the difficulties that these activities can create, the vast amount of standards making and certification activities are not the subject of litigation and dispute. To remain in the unreported category, association staff, members, and counsel must recognize the close degree of attention and continuing effort that a sound program entails.