SUGGESTIONS FOR COMPETITOR COLLABORATION GUIDELINES

By

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Testimony Before Federal Trade Commission
Joint Venture Project Hearings
June 5, 1997

The Commission's interest in new guidelines for competitor collaborations is welcome news from my perspective as an antitrust counselor. I say this even though the Commission has already done a great deal to advance antitrust policy in this area in the last few years, and those of us who follow agency developments with some care cannot claim much inability to predict your likely mode of analysis for most kinds of collaborative activity. Nonetheless, new guidelines focused on common kinds of collaborations could be helpful to at least three audiences: first, business leaders in some industries for whom antitrust law and policy remain a bit foreign and even bizarre as applied to their markets; second, a great many members of the bar who are deeply involved in the negotiation of these collaborations but who do not live and breathe antitrust stuff on a daily basis; third, the federal district court judges who preside over private antitrust challenges, who might be forgiven for misapplication of decades-old precedents out of sync with current thinking, and who might well find this agency's 1998 guidelines in this area useful input into decision-making at the critical summary judgment stage.

Permit me to comment on two particularly difficult issues that new guidelines could usefully address. The first arises with increasing frequency in the negotiation of multi-competitor collaborations in the high-technology sector. The prospective participants may share a commitment to an existing technology along with a vision for its evolution into next-generation products for a whole range of emerging markets. All of them talk about "open standards" as part of their vision but don't necessarily interpret that idea in a common way. One of the first questions is just how open or not-so-open should be the door to participation. The problem from an antitrust standpoint is that the collaboration under consideration defies classification as either (a) conventional "industry standard-setting" for which the traditional advice is maximum openness; or (b) conventional "new product development" for which the traditional advice is in precisely the opposite direction. The venture, in fact, encompasses substantial elements of both kinds of activity.

Antitrust counselors for the parties involved will often at this point find themselves locked in vigorous debate over the "correct" advice to be given. Some will argue that the main danger of antitrust mischief is "underinclusion" -- particularly if one of the rivals being excluded has a vital interest in the emerging markets in question. Others will argue that, to the contrary, the main danger is "overinclusion" -- expanding the group to a size capable of the exercise of collective market power and also foreclosing opportunities for competitive technology development initiatives. There will in most instances be some merit in both points of view, especially in light of inevitable disagreement about facts central to the analysis. Everyone may agree that resolution of whether underinclusion or overinclusion is the greater danger depends on the ultimate effect on competition of the collaboration. That effect, however, will usually be quite unpredictable, especially since the shape and scope of the affected future markets are ill-defined at the outset of the venture.

Of course, even long after formation, and at the point of either an enforcement agency investigation or a private lawsuit, the central facts and effects of the venture will still be susceptible to great disagreement. One can imagine an enforcement agency easily determining that the parties were both justified and prudent in limiting participation in the collaboration. On the other hand, a district court judge reviewing the same venture in a suit by an excluded firm could just as easily decide the exclusion raised serious issues and, on that basis, deny summary judgment and then set a date for a jury trial. Juries of lay persons whose only understanding of antitrust doctrine will come from convoluted jury instructions based on court decisions from decades ago might be expected to sympathize with the excluded party more than with its "conspiring" rivals.

My own bias in this dilemma is to promote creative thinking on some "middle ground" between the two opposite kinds of exposure. The parties might have good reasons relating to manageability of the undertaking -- maximum efficiency and quickest time-to-market -- to limit the parties involved in the collaboration, and their interest in doing so warrants considerable deference. On the other hand, and with a view to maximizing defenses against any challenge by an excluded competitor, the parties might consider various commitments to publicize the plan, both at the outset and at key interim points. Nonparticipants could be invited to offer some input on an informal basis. The parties might also bring to the effort a "neutral" consultant, perhaps a widely respected expert in the relevant technology from academia. The parties might further commit at the outset to some form of open licensing of jointly developed intellectual property at the end of the process, recognizing that the license should be both timely and available at reasonable cost to nonparties if it is to be a featured component of the defense to any future antitrust claim.

Sometimes suggestions along these lines are met with hostility from parties who regard them as gratuitous meddling by lawyers insufficiently sensitive to the business imperatives involved. And, in some cases, this hostility may be warranted. My belief, however, is that suggestions along these lines do make sense for those collaborations where an excluded party's future gripe may not appear totally frivolous to a reviewing agency or court and where the facts governing assessment of the gripe are both unclear at the outset of the activity and hotly disputed at the later fact-finding point. I would accordingly urge some thoughtful input about middle-ground steps of this sort in new agency collaboration guidelines.

My second issue for your consideration involves the dilemma presented by highly concentrated but "distressed" industries characterized by declining demand, excess capacity, high fixed costs, marginal if any profitability, and strong disincentives to further investment even to maintain assets now committed to the business. A merger between leading firms in an industry of this sort would face rough sledding when scrutinized under today's Merger Guidelines: the HHIs would be way off the chart; the reviewing agency would be quick to see significant risk of coordinated-interaction effects; an entry story would be out of the question; and, while the parties would have a strong showing of expected efficiencies in the form of reduced variable as well as fixed costs, the 1997 revision to the efficiencies section of the Merger Guidelines suggests low prospects of clearance on this basis.

But now consider the proposition of the same leading firms in this same industry fashioning a production joint venture between them: excess capacity is eliminated through a consolidation of production facilities and other upstream operations while taking care to preserve downstream competition in the sale of what becomes consolidated but lower-cost output. I suggest to you that this is a form of competitor collaboration that antitrust policy should encourage in today's environment. There is in fact solid precedent for clearing such ventures -- the Alcan/Arco and GM/Toyota ventures of the mid-1980s come to mind -- and I do not doubt that today's FTC would be receptive to straightforward arguments on their behalf.

There is nonetheless a real "perception" problem in this area, exacerbated by reactions I've heard from several quarters to the new efficiencies section to the Merger Guidelines. The perception problem is two-fold. First, despite expectations (generated by the Commission's hearings of a year and a half ago) of a broader role for efficiency considerations in merger enforcement policy, the new section is seen as a reinforcement of longstanding barriers to justifying a merger on this ground. Second, despite critical differences between a full-scale merger between major competitors and a joint venture between the same firms, the business community is skeptical that the agencies would be any more willing to accept an efficiency showing in support of the one than they would in support of the other. The skepticism may be quite unwarranted but is nonetheless evident in comments one hears from both thoughtful members of the business community and their legal advisors.

There is an easy solution to this problem. The agencies could include in new competitor collaboration guidelines some clarification of how they approach efficiency effects in the context of production joint ventures or similar undertakings that do not eliminate downstream competition. A collaboration entailing "partial" integration may well present competitive risks, but they will often be of a character and magnitude warranting less antitrust concern than those presented by a full-scale merger between the same parties. Conversely, such a venture may well promise substantial efficiencies of a character and magnitude likely to enhance the ability and incentive of both parties to compete in the affected downstream market in the years ahead. Indeed, there could be a greater likelihood that resulting efficiencies ultimately benefit downstream consumers than would be the case if one party acquired the totality of the other.

In this context, the agencies can readily accept a broader array of efficiencies, and afford more generous treatment to them as offsetting competitive risks, than might be appropriate in the review of a full-scale merger. This is a rather simple notion that is implicit in agency actions of various sorts in recent years. It would now be highly desirable to make it explicit and elaborate upon it in new guidelines addressing the particular kind of joint venture I have described.

The agencies discuss efficiencies as a factor in rule-of-reason assessments of some forms of competitor collaborations in both the intellectual property guidelines and the latest version of the health care enforcement policy statements. I would urge similarly generous but also more concrete and detailed treatment of this subject in guidelines addressing production joint ventures in distressed-industry circumstances. A serious and extended effort of this kind would help to achieve what is to date the unachieved or largely unachieved objective of the National Cooperative Research and Production Act, as enacted in 1993. The explicit Congressional intent was to reduce risk and uncertainty confronting production joint ventures by ensuring application of the rule-of-reason standard to them. The next most useful step in that direction is some meaningful clarification of the efficiency side of the rule-of-reason standard as applied to these kinds of undertakings.