Clarity And Confusion: FTAIA Developments In 2014

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The Foreign Trade Antitrust Improvements Act[1] has confounded practitioners and courts alike for years. This past year brought long-anticipated decisions from the Second (Lotes),[2] Seventh (Motorola Mobility II)[3] and Ninth (Hsuing)[4] Circuits regarding four important issues: (1) whether the FTAIA is substantive or jurisdictional; (2) the scope of the exclusion for conduct affecting “import commerce”; (3) the appropriate standard for the “domestic effects” test; and (4) the increasing importance of the “gives rise to a claim” test. This article summarizes these recent circuit court opinions and offers some thoughts about issues to watch going forward.

The FTAIA

The FTAIA, passed in 1982, limits the extraterritorial reach of the Sherman Act. It is structured as a set of exceptions within exceptions. After first excluding conduct that affects U.S. import trade or commerce, it provides that the Sherman Act does not apply to conduct affecting trade or commerce with foreign nations unless:

(1) such conduct has a direct, substantial, and reasonably foreseeable effect —

   a. on trade or commerce which is not trade or commerce with foreign nations, or on import trade or import commerce with foreign nations; or

   b. on export trade or export commerce with foreign nations, of a person engaged in such trade or commerce in the United States; and

(2) such effect gives rise to a claim under other provisions of U.S.C. §§ 1 to 7.

In F. Hoffman-LaRoche Ltd. v. Empagran SA,[5] the U.S. Supreme Court restated the statutory test in more easily comprehensible terms: With the exception of conduct involving U.S. import trade or import commerce, the Sherman Act does not apply to foreign conduct unless both: (1) the conduct has a “direct, substantial and reasonably foreseeable effect” on U.S. domestic or import commerce or (certain) export commerce, and (2) “such effect gives rise to a [Sherman Act] claim.”[6]
Empagran involved price-fixing claims asserted by foreign companies based on their foreign purchases. The court held that the FTAIA blocked these claims because the harm from the purchases occurred in foreign, not U.S., markets.[7] The court also rejected the argument that the “gives rise to a claim” test meant that a foreign purchaser could sue in the U.S. as long as the conduct gave rise to another party’s claim in the U.S.[8] Despite this guidance from the Supreme Court, the FTAIA has proved durably resistant to easy application, and lower courts have since issued discordant decisions touching on key aspects of the statute.

**Four Key Issues Under the FTAIA**

We begin with a summary of the key issues addressed in the 2014 appellate opinions and what appears to be the current state of the law. The cases and their implications for the future are addressed thereafter.

1. **Substantive vs. Jurisdictional Requirements**

Fortunately, one area of disagreement seems to be getting resolved: whether the FTAIA is substantive or jurisdictional, with the distinction having implications principally for the resolution of motions to dismiss. While some earlier decisions held that the FTAIA is jurisdictional,[9] since the Supreme Court’s decision in Arbaugh v. Y&H Corporation, 546 U.S. 500 (2006), courts have ruled that the FTAIA imposes a substantive merits limitation rather than a jurisdictional bar.[10] That trend continued in 2014 with the Second Circuit’s holding in Lotes and the Ninth Circuit’s holding in Hsuing, both cases reversing prior Circuit precedent.[11] One can expect future decisions to follow suit.

2. **The Import Commerce Exclusion**

There currently is a lack of consensus regarding the scope of the exclusion for conduct affecting U.S. “import commerce” — one that can be of critical importance because it exempts conduct entirely from the FTAIA’s limitations. Although the exclusion is easily applied for a U.S. company that purchases a product directly from a foreign defendant for importation into the United States,[12] the situation is less clear in situations reflecting the increasingly global supply chain.

In 2011, the Third Circuit held in Animal Science Products that the critical issue for application of the “import commerce” exclusion is whether the defendants’ alleged anti-competitive behavior was “directed at” an import, opening the door to applying the exclusion where the defendant was not the actual importer.[13] The Seventh and Ninth Circuits have taken a narrower interpretation, with the court in Hsuing observing the contrary decision of the Second Circuit in Lotes but not trying to resolve it.[14]

3. **The “Direct Effect” Requirement**

The next area of disagreement has been the appropriate test for the requirement that the foreign conduct has a “direct, substantial, and reasonably foreseeable effect” on U.S. commerce. The main issue in the recent cases has been what meaning to give the word “direct.” In LSL Biotechnologies, the Ninth Circuit held that the term has a temporal element: “an effect is ‘direct’ if it follows as an immediate consequence of the defendant’s activity,” proceeding “without deviation or interruption.”[15] That construction was reaffirmed in Hsuing.[16] However, in Minn-Chem the Seventh Circuit, sitting en banc, took a more functional approach: “the term ‘direct’ means only that ‘a reasonably proximate causal nexus’” exists between the conduct and the injury in the U.S., whether or not the effect is
“immediate.”[17] This view was reaffirmed in 2014 by the Seventh Circuit in the Motorola Mobility litigation, albeit in successive opinions that applied the test differently to the same facts.

The U.S. Department of Justice has forcefully advocated for a proximate cause test, out of concern that the LSL Biotechnologies standard would cripple its enforcement efforts.[18] Although all three Circuits addressed the “direct effect” requirement, there continues to be substantial disagreement regarding the appropriate test, with the Ninth Circuit being the clear outlier.

4. The “Give Rise to a Claim” Requirement

An area of increasing importance is the requirement that the domestic effect “give rise to a claim” under the Sherman Act. On remand from the Supreme Court, the D.C. Circuit in Empagran held that the “gives rise to a claim” language requires a direct or proximate causal relationship,[19] and since then courts generally have applied that standard rather than a more lenient “but-for” standard.[20] This provides the “give rise to a claim” test real teeth, and the Second and Seventh Circuits may have signaled more aggressive application of it to use the FTAIA to dispose of Sherman Act claims based on transactions occurring in foreign markets.

We discuss in more detail below the appellate cases in 2014 that led to the continuing uncertainty over application of the FTAIA.

The Circuit Court Decisions

The Second Circuit's Decision in Lotes

In Lotes, the Second Circuit addressed both the “direct effect” and “gives rise to a claim” tests.[21] Lotes, a Taiwanese corporation, asserted Sherman Act claims alleging that members of a standards-setting organization breached their licensing commitments and precluded Lotes from participating in the U.S. market for USB 3.0 connectors, which resulted in higher prices for U.S. consumers. Defendants asserted that the FTAIA blocked Lotes’ claims.

For the “direct effect” test, the Second Circuit adopted the Seventh Circuit’s Minn-Chem standard — a “reasonably proximate causal nexus” — rather than the Ninth Circuit’s LSL Biotechnologies standard — an “immediate consequence of the defendant’s activity.”[22] But the court did not decide the case based on the “direct effect” test, as it assumed that it had been pled notwithstanding the existence of a multiparty supply chain. Instead, the court dismissed Lotes’ claims based on its failure to satisfy the “gives rise to a claim” test, because even though Lotes alleged that the defendants’ foreign conduct resulted in higher consumer prices in the United States, those prices were not the injury that Lotes allegedly suffered, which was being excluded from the market for USB 3.0 connectors.[23]

The Ninth Circuit’s Decision in Hsuing

The Ninth Circuit’s decision in Hsuing addressed the import exclusion and the “direct effect” test.[24] Hsuing and his company, AU Optronics Corp., were convicted of participating in the liquid crystal display price-fixing conspiracy. They appealed their convictions, arguing that the FTAIA barred their prosecution because the majority of price-fixed panels were sold to third parties outside the United States.

The Ninth Circuit upheld the convictions because defendants had imported some of the price-fixed panels into the U.S.[25] The court also reiterated the LSL Biotechnologies “direct effect” test that the
effect must be the “immediate consequence” of the defendant’s conduct.[26] At the same time, however, the Ninth Circuit acknowledged that the Second Circuit in Lotes had disagreed with its LSL Biotechnologies decision, but said it was “not necessary to address this disagreement because we do not rely on the direct effects exception in affirming the convictions.”[27] At the same time, the court stated that it “need not resolve whether the evidence of the defendants’ conduct was sufficiently ‘direct,’” because the LSL Biotechnologies standard clearly was met.[28] The defendants have sought en banc review and that petition is still pending.

The Seventh Circuit’s Decisions in Motorola Mobility

The most colorful case in 2014 was the Seventh Circuit’s treatment of the Motorola Mobility case, which was closely watched in light of the circuit’s prior en banc decision in Minn-Chem. The case resulted in two Seventh Circuit opinions, the second of which departed from the original decision with respect to the “direct effect” test.

Motorola, a U.S. company, asserted claims stemming from the LCD price-fixing conspiracy based on its purchases of panels that were delivered directly to Motorola facilities in the United States (“Category I”); purchases of panels by Motorola’s foreign affiliates that were delivered to the foreign affiliates’ manufacturing facilities abroad, where they were incorporated into mobile phones that were later sold in the United States (“Category II”); and purchases of panels by Motorola’s foreign affiliates that were delivered to the foreign affiliates’ manufacturing facilities abroad and incorporated into mobile phones sold outside the United States (“Category III”). The district court ruled that the Category I sales constituted “import commerce,” and so were unaffected by the FTAIA, and that the Category III sales affected only foreign commerce, so claims based on those purchases were blocked by the FTAIA. The Category II cases served as the context for the court’s discussion of the meaning of the FTAIA.

In Motorola I,[29] in an unsolicited opinion on the merits in the context of an petition for interlocutory review, Judge Richard Posner affirmed the entry of partial summary judgment against Motorola, on three grounds: (1) the indirect sales of LCD panels in the United States, through their incorporation in cell phones, did not satisfy the FTAIA requirement that the U.S. injury be “direct”; (2) the allegedly inflated price charged by the foreign seller to the foreign subsidiary of Motorola did not create an effect that was cognizable under the Sherman Act; and (3) from a policy standpoint, adoption of Motorola’s proposed theory of liability would dramatically increase the exposure of international sales transactions to the Sherman Act, a result that the Supreme Court had cautioned against in Empagran.

Motorola, supported by agencies of the U.S. government and opposed by amicus curiae including a number of foreign governments, sought en banc review. In response, the court vacated its opinion and, this time after briefing and argument, issued a new opinion that similarly affirmed summary judgment against Motorola.

In Motorola II,[30] the court again quickly concluded that the Category I purchases satisfied the FTAIA (defendants’ products were sent to Motorola in the United States), but that the Category III purchases did not (the products never entered the United States).[31] For the Category II purchases, the court assumed the “direct effect” test was satisfied.[32] It departed from its analysis in Motorola Mobility I, in which it said as a matter of statutory interpretation that a “direct effect” on U.S. commerce could not follow from the importation of a finished product containing a price-fixed component even one step away from its direct sale. Instead, the panel returned to the en banc decision in Minn-Chem, which said that an effect in the United States cannot be “direct” as a matter of law if the price-fixing “‘filters through many layers and finally causes a few ripples in the United States.’”[33]
Noting that there had been only one intermediate sale prior to importation of the finished product, the court explained that the effect on Motorola “might well be direct rather than ‘remote,’ the term we used in Minn-Chem, Inc. v. Agrium, Inc.”[34] Characterizing the effect on U.S. prices as “less direct” than it was in Minn-Chem, the court nonetheless declined to presume that the minimal “direct effect” could not be shown.[35]

That left the “gives rise to a claim” requirement. Judge Posner concluded that the Category II purchases did not satisfy it because the original purchasers of the price-fixed components were Motorola’s foreign subsidiaries: “Whether or not Motorola was harmed indirectly, the immediate victims of the price fixing were its foreign subsidiaries ... and as we said in the Minn-Chem case, ‘U.S. antitrust laws are not be used for injury to foreign customers.’”[36]

Noting that the foreign subsidiaries have remedies under local law, the court characterized their U.S. parent’s efforts to litigate their dispute in U.S. courts, where remedies and enforcement was presumably stricter, as impermissible “forum shopping.” The opinion also cited the “related flaw” that Motorola’s U.S. parent was an indirect purchaser of the price-fixed goods, and thus did not have standing under Illinois Brick[37] to bring Sherman Act claims.[38] The court rejected Motorola’s effort to take advantage of Illinois Brick’s “owner or control” exception,[39] finding that exception unavailing for foreign subsidiaries of U.S. corporations, and reasoning that the transactions still occurred in foreign commerce.[40]

Finally, the court acknowledged the desire of amicus United States that any decision adverse to Motorola not adversely impact criminal prosecutions by being based on the categorical rule announced in Motorola I, that an indirect sale to a U.S. customer can never give rise to a “direct” effect on U.S. commerce. While perhaps resulting in a more workable and sensible framework, this aspect of Motorola II served to underscore the extent to which construction of the FTAIA was at least as much a matter of policy than of pure construction of statutory terms.

On Jan. 12, 2015, the court issued an amended opinion that made additional points why Motorola could not assert claims on behalf of its overseas subsidiaries, and reiterating that those companies can pursue remedies under local laws. At the same time, the court issued a separate order denying Motorola’s petition for en banc review, and Motorola has already indicated that it will seek Supreme Court review.

Looking Ahead

These four decisions suggest some developing consensus, but there also is a lack of agreement on some important issues.

1. **What is the scope of the import commerce exclusion?**

One issue to watch in 2015 is whether courts will come to apply a broad construction of the import commerce exclusion. As noted above, in Animal Science Products, the Third Circuit held that the issue is not whether the defendant was the physical importer, but whether the defendant’s conduct was “directed at” an import; in other words, whether “the defendants’ conduct target[ed] import goods or services.”[41] In Motorola Mobility, the analysis was straightforward. The Seventh Circuit said that the exception applied to Motorola’s Category I purchases, but it did not need to consider whether it applied to the Category II purchases because the goods were imported into the U.S. after being sold to Motorola’s overseas subsidiaries.
Hsuing gave the Ninth Circuit an opportunity to address the issue because some of the price-fixed goods were imported directly into the U.S. but some were not. Despite acknowledging that it has not “defined ‘import trade’ for purposes of the FTAIA,”[42] the Ninth Circuit expressly decided not to do so: “We need not determine the outer bounds of import trade by considering whether commerce directed at, but not consummated within, an import market is also outside the scope of the FTAIA’s import provisions because at least a portion of the transactions here involves the heartland situation of the direct importation of foreign goods into the United States.”[43]

Thus far, then, there appears to be a lack of uniformity in how the circuits will apply the import commerce exception if the defendant was not the physical importer, a potentially critical issue in connection with imported products having a global supply chain.

2. What standard will be applied for the “direct, substantial, and reasonably foreseeable” test?

The 2014 decisions underscore that disagreements persist regarding what it means for a U.S. injury to be “direct” for purposes of the domestic effects requirement. In Lotes, the Second Circuit, following the Seventh Circuit’s Minn-Chem decision, construed the statutory test to mean that the defendant’s conduct must have a “reasonably proximate causal nexus” with an effect on U.S. commerce. In doing so, the Second Circuit disagreed with the Ninth Circuit’s LSL Biotechnologies decision, which held that the FTAIA permits a Sherman Act claim to proceed only if the effect is an “‘immediate consequence of the defendant’s ... activity,’” proceeding “‘without deviation or interruption.’”[44]

Shortly after the Second Circuit issued its decision in Lotes, the Ninth Circuit in Hsuing recognized the Second Circuit’s disagreement with LSL Biotechnologies test and declined to address it.[45] The Seventh Circuit’s Motorola Mobility II decision does not settle the matter, as it assumed for purposes of a motion to dismiss that a “direct” effect — while perhaps unlikely — had been shown.[46] The Second Circuit in Lotes, likewise, assumed without too much difficulty that a “direct” U.S. effect could be shown based upon an alleged price increase in the upstream foreign supply chain.[47] Notably, the effect of Motorola Mobility II and Lotes may be that, in a case involving foreign cartel activity, it will be more difficult to prevail on a motion to dismiss on grounds that a “direct effect” was not adequately pled.

3. Will the “gives rise to a claim” requirement overtake the “direct effect” requirement?

With the Seventh and Second Circuits seemingly adopting a lower bar for satisfaction of the “direct effect” requirement at the pleading stage, the fact that both courts resolved cases in defendants’ favor under the “gives rise to a claim” test may be significant. Lotes will probably remain a bit sui generis in its facts, but Motorola Mobility II raises some basic questions about the application of the FTAIA to cases where the direct purchasers of price-fixed components are foreign companies.

Judge Posner took a categorical approach to these transactions, concluding without much need for an explanation that a foreign company that buys a cartel-inflated component abroad for incorporation into a U.S.-bound finished product has not made a purchase affecting U.S. commerce or subject to the Sherman Act.[48] The fact that Motorola-U.S. owned and claimed to control that foreign company was irrelevant; ownership would not confer a right to sue on the foreign affiliate’s behalf, and in any event would not change the “foreign” nature of the injury.[49]

It may seem that the Seventh Circuit’s “foreign commerce” ground for decision is just a subset of the indirect purchaser doctrine of Illinois Brick, and indeed that limitation is described as a “related flaw” in
Motorola Mobility’s argument. [50] Illinois Brick (which was not even cited in Motorola Mobility I) seems to appear in Motorola Mobility II to limit arguments by plaintiffs that a parent company that owns or controls a direct-purchasing subsidiary might be deemed to be the direct purchaser. [51] Judge Posner again takes a categorical approach to the issue, limiting the “owner or control” exception to exclude claims by U.S. parent companies based on purchases by their subsidiaries in foreign markets. [52] If a bright line is to be drawn based on the situs of the buyer and the seller, it is not clear what situation would survive the second prong of the FTAIA where a price-fixed component (or product) is not sold to a U.S. customer.

4. How will courts treat the FTAIA for claims brought under Illinois Brick-repealer statutes?

That brings us to a final issue, not discussed in the four appellate decisions, that is worth watching: Does the FTAIA apply to state analogues to the Sherman Act? The issue is of most importance in states with Illinois-Brick repealer statutes that allow indirect purchasers to sue for damages. It is of great interest and concern not only to defendants and the class action bar, but also to companies that opt out of class actions in favor of pursuing damages recoveries on their own through negotiation or, where required, litigation. There is no clear answer yet. Some courts have found that congressional intent in passing the FTAIA would be impermissibly frustrated if state law were permitted to regulate foreign commerce more extensively than the Sherman Act, but other courts have hesitated to so find. [53]

If the FTAIA does apply to limit state antitrust law claims, it is possible that either or both of the “direct effect” and “gives rise to a claim” requirements would block otherwise viable actions. On the other hand, if the FTAIA does not apply to claims brought under state antitrust law, companies that purchase from overseas intermediaries, as well as downstream purchases and consumers, may be able to bring indirect purchaser claims — even though the FTAIA would preclude a U.S. company that acquired price-fixed products from its foreign subsidiary from bringing a direct purchaser claim under the Sherman Act, at least according to the Seventh Circuit. As more opt outs press indirect purchaser claims and defendants assert that the FTAIA blocks them, we are likely to see more decisions squarely addressing the issue.

Conclusion

2014 was an important year in the evolution of the 33-year-old FTAIA, but not one that put to rest important questions that have been roiling the courts for decades.

Especially in the area of international cartel activity, only the easy cases involving U.S. direct purchasers of foreign products at prices inflated by cartel activity can be said to meet with settled law. Where conduct involving the importation of finished products containing price-fixed components is concerned, open questions like these remain: whether claims will be subject to the FTAIA at all; if so, the extent to which the claims will be limited by the statutory requirements that an effect on U.S. commerce be “direct” and “give rise to a claim” under the Sherman Act; whether the indirect purchaser doctrine will be applied in connection with intra-corporate situations involving foreign entities; and whether state antitrust laws will be construed to be limited by the FTAIA or the principles it embodies. It seems improbable that additional appellate decisions will resolve the full range of inconsistencies, and all likely would benefit if the Supreme Court were to supplement the guidance it provided in Empagran.

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[4] United States v. Hui Hsuing, 758 F.3d 1074 (9th Cir. 2014), petition for reh’g & reh’g en banc pending.


[6] Id. at 161-62.

[7] Id. at 163-69.

[8] Id. at 173-74.


[12] E.g., Minn-Chem, 683 F.3d at 855 (“transactions between the plaintiff purchasers and the defendant cartel members are the import commerce of the United States”) (emphasis in original).


[14] 758 F.3d at 1094 n.8.


[16] 758 F.3d at 1094.

[17] 683 F.3d at 847.


[20] See Lotes, 753 F.3d at 414 (citing In re Dynamic Random Access Memory (DRAM) Antitrust Litig., 546 F.3d 981, 987 (9th Cir. 2008), and In re Monosodium Glutamate Antitrust Litig., 477 F.3d 535, 538 (8th Cir. 2007)).


[22] Id. at 409-13.

[23] Id. at 413-15.


[25] Id. at 1091-92.

[26] Id. at 1094.

[27] Id.

[28] Id.

[29] 746 F.3d 842 (7th Cir. 2014), vacated & reh’g granted by 2014 U.S. App. LEXIS 12704 (7th Cir. July 1, 2014).


[31] Id. at *4-*9.

[32] The court concluded, as it had in Motorola Mobility I, that the “substantial” and “foreseeable” prongs of the domestic effects test might be satisfied so summary judgment was inappropriate. For example, if a price-fixed component was included in cell phones assembled overseas and sold to Motorola in the U.S. “there would be an effect on U.S. commerce,” which “could be substantial.” Id. at *9. Similarly, the court found the requirement that the effect be “foreseeable” was satisfied “because the defendants knew that finished products sold in the United States would incorporate price-fixed components sold abroad.” Id.

[33] Id. at *10 (quoting Minn-Chem, 683 F.3d at 860).

[34] Id. at *9.

[35] Id.

[36] Id. at *11-*12, (quoting Minn-Chem, 683 F.3d at 858).


[39] 431 U.S. at 736 n.16.


[41] 654 F.3d at 462.

[42] 758 F.3d at 1090.

[43] Id. at 1090 n.7. At least one district court, however, has construed Hsiung to have incorporated the Third Circuit’s rule that conduct motivated by an intent to affect U.S. import commerce can satisfy the statutory requirement. See In re: TFT-LCD (Flat Panel) Antitrust Litig., 2014 U.S. Dist. LEXIS 132228, at *63 (N.D. Cal. Sept. 18, 2014).

[44] Lotes, 753 F.3d at 410-11 (citations omitted).

[45] Hsuing, 758 F.3d at 1087-88.


[47] Lotes, 753 F.3d at 412-13.


[50] Id. at *14.

