

UNITED STATES ANTITRUST ASPECTS OF EAST–WEST COUNTERTRADE

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1. Introduction

In the typical East–West countertrade agreement, a U.S. firm agrees to export a product from the United States to a foreign country and to import a product made in that foreign country into the United States. Since such a transaction has a substantial foreseeable effect on U.S. foreign commerce, it is subject to U.S. antitrust laws under which federal courts and antitrust authorities have prescriptive jurisdiction [1]. U.S. Courts also have, at a minimum, personal jurisdiction over the American firm [2]. Regardless of the court's ability to exercise personal jurisdiction over the foreign firm, the foreign firm's conduct is subject to antitrust scrutiny, and the court may cancel the contracts in question without the foreign firm's presence as a party to the suit [3].

In recent years, the Justice Department has taken the position that the U.S. antitrust laws should not be enforced to protect foreign persons in foreign markets [4] and should not be applied to activities by U.S. firms outside the United States which have no direct or intended effect on U.S. consumers or export opportunities [5]. Under this view, if the only persons injured by countertrade activity are non-Americans outside the United States, the U.S. antitrust laws should not be applied. Until recently, this position expressed enforcement policy rather than the law. Indeed, the Supreme Court has held that foreign persons, including foreign governments, have standing to sue for violations of the U.S. antitrust laws [6]. On October 8, 1982, however, President Reagan signed Title IV of the Export Trading Company Act of 1982 [7]. This statute amends the Sherman and Federal Trade Commission Acts to apply only to activities that have a “direct, substantial, and reasonably foreseeable effect” on U.S. import commerce or on the export commerce of a

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U.S. resident [8]. Consequently, the U.S. antitrust laws no longer apply in situations where the anticompetitive effects are felt solely outside the United States.

2. Reasons for countertrade

In the typical East-West countertrade situation, the foreign firm controls access to the foreign market. The firm uses this control as leverage when bargaining with U.S. firms desiring access. Thus, the price of access becomes the agreement of the U.S. firm to commit itself to importing and marketing the foreign firm's product. Countertrade agreements often tie the volume of the foreign firm's purchases of the U.S. firm's export product to the volume of the U.S. firm's imports of the foreign product. Such provisions may enable a foreign trading company to obtain more aggressive U.S. distribution of its product or to piggy-back on the strength of a popular U.S. brand name. For example, a foreign trading company might make the following offer: "We will buy a million cases of Coca-Cola if you agree to buy and distribute our wine in the United States." Where the U.S. firm has leverage from its ability to maximize U.S. purchases of the foreign firm's product, the U.S. firm would purchase the foreign firm's product only if the foreign firm agreed to purchase or market the U.S. firm's product.

In addition to improvements in distribution and sales, there are other potential advantages of entering into countertrade agreements. For example, the parties may seek mutual economic dependence, the familiarity that results from dealing with one another, or a reduction in transaction costs. Moreover, mutual purchase commitments enable the parties to adjust sales prices to avoid foreign exchange controls and to minimize their tax liability [9].

In U.S. antitrust terminology, countertrade is best classified as "reciprocal dealing". Reciprocity has been suspect under the U.S. antitrust laws because antitrust enforcers and courts believe that the potential for negative antitrust effects is unlikely to be offset by its efficiencies. As discussed below, reciprocity perpetuates buy-sell relationships that, at least for the U.S. firm, may not be the result of the normal competitive choice made in the free market that antitrust laws are intended to protect and promote. Moreover, it has been contended that

[c]ountertrade output will in most instances tend to be sold in the Western partner's domestic market at marginal prices which, over the long-term of the countertrade agreement, will likely suppress domestic production, halt growth in domestic supply, and even cause domestic disinvestment thereby creating the possibility of a dependence on the low price commodity [10].

3. Possible anticompetitive effects

Countertrade agreements may have one or more anticompetitive effects in the United States.

3.1. Distortion of purchasing criteria

In a competitive economy, a buyer bases his purchasing decisions on the best available combination of low price, high quality, and service availability. In a countertrade transaction, these traditional purchasing criteria are replaced, in whole or in part, by criteria such as the foreign firm's purchasing power and the availability of substitutes for the product being offered by the U.S. firm. Thus, the U.S. firm may agree to purchase higher-priced or lower-quality goods than it would in a competitive situation. Such purchases may result in a misallocation of resources and detrimental effects for consumers. On the other hand, if the purchaser is not forced to make the purchase, the choice of higher price or lower quality may be viewed as a decision the purchaser should be free to make because the market will penalize the purchaser if the decision is economically incorrect [11].

3.2. Market foreclosure

U.S. competitors of the U.S. seller may be foreclosed from selling their higher quality products to the foreign firm as a result of the U.S. seller's countertrade agreement. Over a period of time, countertrade agreements between large U.S. firms and particular countries or state trading companies could lead to a degree of market foreclosure that approaches attempted monopolization of a particular relevant market [12]. The likelihood that a court will find attempted monopolization increases as the relevant market is defined more narrowly. Moreover, countertrade agreements may exclude U.S. competitors of the U.S. purchaser from access to the foreign seller's products.

3.3. Analyzing the anticompetitive effects of reciprocity

Countertrade may be classified as reciprocal dealing. The competitive effect of reciprocity, however, varies with the market power of the relevant firms and the extent of market foreclosure resulting from the transaction. Most cases and commentators identify three types of reciprocity: "coercive", "voluntary", and "unilateral". "Coercive" reciprocity may be exercised by either the U.S. or the foreign purchaser. The purchaser in effect threatens: "We will buy from you only if you will buy from us." The anticompetitive results of such coercive conduct may be distortion of allocative efficiency or foreclosure of U.S.

competitors. The coerced firm's purchasing decisions are based on factors other than price, quality, or service [13].

"Voluntary" reciprocity may occur because neither firm possesses sufficient market power as a purchaser to enforce its will. The reciprocal dealing then rests upon mutual convenience rather than coercion. In such circumstances, reciprocity is unlikely to involve a distortion of allocative efficiency or substantial market foreclosure [14]. On the other hand, voluntary reciprocity may involve an agreement between entities that possess substantial market power. Such situations may significantly threaten competition.

"Unilateral" reciprocity describes a firm's unilateral decision to purchase from those who purchase the goods it sells. This type of reciprocity involves neither an agreement nor any coercion. Such a practice is rarely of antitrust concern because the randomness of the purchasing decisions precludes significant distortion of the relevant market.

The antitrust cases relating to exclusive dealing provide a relevant framework for assessing the anticompetitive effects of reciprocity. In an exclusive dealing agreement the buyer agrees to purchase particular goods or services exclusively from the seller. This type of agreement often takes the form of a requirements contract in which the buyer commits itself to purchase its requirements of a particular item during a particular period from the seller. The agreement effectively excludes the supplier's competitors from the market represented by the purchaser for the relevant time period.

The U.S. Supreme Court has held that the degree of market foreclosure is a significant factor in determining the legality of exclusive dealing arrangements. In *Tampa Electric v. Nashville Coal Co.* [15], the Court stated that market foreclosure of \$128 million worth of coal covered by a utility's twenty-year requirements contract was insufficient to render the contract illegal. Although only 0.77% share of the relevant market was foreclosed, the Court did not hold that the percentage of foreclosure was insubstantial. Instead, in assessing the substantiality of the market share foreclosed, the Court stressed the need "to weigh the probable effect of the contract on the relevant area of effective competition... and the probable immediate and future effects which preemption of that share of the market might have on effective competition therein" [16]. Only after assessment of the "particularized considerations of the parties' operations" was the agreement upheld [17].

Application of the *Tampa Electric* rationale to countertrade transactions would require a detailed analysis of the affected market and the context in which the countertrade agreement was employed. In situations in which the market share foreclosed was significant, *Tampa Electric* would permit a finding that the agreement was a reasonable restraint on competition if the peculiar circumstances of the market suggested a low probability that effective competition would be lessened.

4. Precedents

4.1. U.S. law

No reported cases have dealt with the application of the U.S. antitrust laws to countertrade transactions. Moreover, the Justice Department's Antitrust Division has not instituted any cases in which trade with a nonmarket economy country was a central issue [18].

Domestic cases on reciprocity date back to the 1930s. As one commentator noted, “[t]he general attitude toward reciprocity could be characterized as unreceptive at best and openly hostile at worst” [19]. In a 1965 merger case, the U.S. Supreme Court referred to reciprocity as “‘an irrelevant and alien factor’... intruding into the choice among competing products...” [20]. Apart from cases involving mergers, decisions declaring reciprocity in a buy-sell contract a violation of section 1 of the Sherman Act [21] (agreement unreasonably restraining trade), section 2 of the Sherman Act [22] (attempted monopolization of a relevant market), or section 5 of the Federal Trade Commission Act [23] (unfair methods of competition) have not been sustained on appeal. The Justice Department, however, has obtained a number of consent decrees in cases in which it has challenged reciprocal dealing [24]. These consent decrees include both general and detailed proscriptions designed to prevent the defendant corporations from engaging in any type of reciprocal dealing, whether consensual or “coercive”, and whether by agreement, understanding, or “unilateral” means. Furthermore, the defendants have often been required to instruct their personnel to base purchasing decisions solely upon price, quality, services, and financial responsibility, rather than considering a potential supplier's purchases from the defendant.

The Federal Trade Commission (the “FTC”) has attacked reciprocal dealing practices as an unfair method of competition under section 5 of the Federal Trade Commission Act. After initially accepting voluntary assurances of discontinuance [25], the Commission announced in 1970 that such assurances would no longer be accepted in reciprocal dealing situations, and indicated its plans to expand its reciprocity investigation program [26].

The only transnational case involving reciprocity is still in the pleadings stage. *Industria Siciliana Asfalti, Bitumi v. Exxon Research & Eng'g Co.* [27] involves a claim by an Italian refinery operator that an American oil company, Exxon, used its leverage as a purchaser of refinery capacity to coerce the plaintiff into purchasing engineering services for the construction of a refinery from Exxon rather than from another U.S. firm that submitted a lower bid. The plaintiff's initial complaint was dismissed because the allegations of coercion were inadequate [28]. An amended complaint survived a motion to dismiss by specifically alleging that the oil company had threatened to boycott

the plaintiff's refinery if the Italian refiner did not purchase Exxon engineering services [29].

In the last few years, the Antitrust Division and economists have questioned the validity of the earlier court decisions condemning reciprocal dealing practices. The latest pronouncements from the Antitrust Division have notably omitted reciprocity from the list of domestic antitrust sins [30]. Nevertheless, the courts have not overturned the existing antireciprocity decisions.

Three additional cases are relevant to the foreclosure issues discussed above. The first sheds light on the definition of a relevant market; the second and third represent attempts to define the market share deemed sufficient to justify actions involving market foreclosure and attempted monopolization.

The first case, *Dominicus American Bohio v. Gulf & Western Indus.* [31], involved the alleged monopolization by several U.S. firms of tourist facilities in the Dominican Republic. In denying the defendants' motion for summary judgment, the district court selected, as a possible relevant market, the provision of tourist facilities in one section of the Dominican Republic. Such a narrow definition of the relevant market is unusual in export cases. Nevertheless, the court's reasoning could be utilized to attack a countertrade agreement that arguably monopolizes a specific range of products in a particular country.

The second relevant case is the criminal action brought against Gulf Oil Corporation for its participation in the international uranium cartel [32]. One of the theories advanced by the Justice Department was that the cartel agreement foreclosed U.S. exporters from selling their products in foreign markets. The foreign markets accounted for approximately 30% of world uranium purchases and the individual national markets were comparatively small. Gulf pleaded *nolo contendere* to the complaint.

The countertrade agreement between Occidental Petroleum Corporation and the U.S.S.R., the subject of two International Trade Commission investigations [33], is also pertinent. Occidental agreed to sell technology and annually specified amounts of phosphate fertilizer to the Soviets, in exchange for annually specified amounts of ammonia, urea, and potash to be sold in the United States. It was projected that the Soviet ammonia imported into the United States would account for approximately 50% of all ammonia imports during the early 1980s [34]. Notwithstanding the magnitude of this market share, market foreclosure and attempted monopolization issues were not raised in the proceedings challenging the agreement.

4.2. U.N. guidelines

The U.N. "Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices" contains a narrowly defined prohibition of reciprocal dealing:

4. Enterprises should refrain from the following acts or behaviour in a relevant market when, through an abuse or acquisition and abuse of a dominant position of market power, they limit access to markets or otherwise unduly restrain competition, having or being likely to have adverse effects on international trade, particularly that of developing countries, and on the economic development of these countries:

...

(f) when not for ensuring the achievement of legitimate business purposes, such as quality, safety, adequate distribution or service:

...

(iv) making the supply of particular goods or services dependent upon the purchase of other goods or services from the supplier or his designee [35].

This prohibition applies only if the practice: (1) is imposed through abuse of a dominant position, (2) limits access to markets or otherwise unduly restrains competition, (3) has or is likely to have adverse effects on international trade, *and* (4) is not for the purpose of ensuring the achievement of legitimate business purposes, such as quality, safety, or adequate distribution of service.

5. Advance clearance procedures

Both the Justice Department and the FTC have procedures for granting advance clearance for contemplated business activities.

5.1. Department of Justice business review procedure

In response to a party's written request accompanied by all relevant data, the Antitrust Division may: (1) state its present enforcement intentions with respect to the proposed business conduct, (2) decline to pass on the request, or (3) take such action as it considers appropriate [36]. The Department reserves the right to bring an action after issuing a favorable business review letter [37].

Thirty days after the business review letter is issued, the letter requesting the review, the accompanying information, and the Division's letter in response are indexed in a file. This information is available to the public upon request. The party seeking the review may request nondisclosure of the information, and such requests will be honored if certain criteria justifying nondisclosure, as set forth in the regulations, are met [38].

Despite Justice Department encouragement, the business review process has been used only occasionally in connection with foreign commerce transactions. One study found only twenty-two such requests over the last ten years [39]. The Department issued eighteen positive and two negative responses, as well as two no-action responses to requests that were moot or too vague [40]. As a result of a directive issued by President Carter [41] and in order to promote exports, the Department announced in 1978 that henceforth it would respond to all export-related requests within thirty working days of receipt of all

relevant information [42]. Of course, the Department decides what information is relevant to a particular request, and the exigencies of business may not permit a firm to wait thirty days for a response. The Justice Department has not reported a noticeable increase in the use of the business review program since the 1978 statement.

In an October 1979 business review letter [43], the Justice Department stated that it had no objection to the formation of an entity designed to assist U.S. exporters and importers desiring to conduct barter trade with nations that pay with goods rather than convertible currencies. The proposed entity was designed to act as a clearinghouse through which members could dispose of bartered foreign goods among themselves. Participation was to be open to all U.S. firms and the participants were not to be restricted in their outside dealings.

5.2. FTC advisory opinions

The FTC employs a procedure which resembles the Justice Department's procedure for providing nonbonding advisory opinions. Requests for advice and supporting material are placed in the public record unless a filed confidentiality request is honored by the FTC [44].

6. Conclusion

From an antitrust perspective, the most serious problems posed by countertrade transactions are foreclosure of U.S. firms from access to foreign markets and access to foreign products sold in the United States. The following general guidelines for avoiding antitrust liability may be useful to firms contemplating or already engaging in countertrade arrangements.

(1) *Coercion*. U.S. firms should avoid exercising coercion in countertrade arrangements.

(2) *Market share*. The larger the market share held by a U.S. firm, the more circumspect the firm should be in structuring its countertrade agreements.

(3) *Product differentiation*. The perceived market power of a U.S. firm increases as the level of product differentiation between the products being bought and sold increases. Because perceived market power is often viewed as an indicator of potential market foreclosure, increased product differentiation may increase the degree of antitrust exposure.

(4) *Web of dealings*. U.S. firms holding substantial shares in relevant markets should avoid systematic, continuous barter relationships that may become permanent and thereby lead to allegations of attempted monopolization.

(5) *Nondiscriminatory access*. Barter exchanges and similar facilities which

may offer significant competitive advantages to members should be open to all qualified potential members on a nondiscriminatory basis. Reasonable fees may be charged for services rendered and access to the facility.

In sum, the lack of antitrust precedents relating to countertrade, coupled with the hostility of the antitrust laws to coercive reciprocal dealing and market foreclosure, underscore the need for firms to plan their trade arrangements carefully in order to minimize their potential antitrust liability.

Notes

[1] See, generally, *Industrial Investment Development Corp. v. Mitsui*, 671 F.2d 876 (5th Cir. 1982); *Mannington Mills, Inc. v. Congoleum Corp.*, 595 F.2d 1287 (3d Cir. 1979); *Timberlane Lumber Co. v. Bank of America*, 549 F.2d 597 (9th Cir. 1976); *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945); I J. Atwood and K. Brewster, *Antitrust and American Business Abroad* 63–80 (2d. ed. 1981); Antitrust Division, U.S. Department of Justice, *Antitrust Guide for International Operations* 6-7 (1977).

[2] See, e.g., *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980).

[3] See, e.g., *United States v. National Lead Co.*, 63 F. Supp. 513 (S.D.N.Y. 1945), *aff'd*, 332 U.S. 319 (1947); *United States v. General Elec. Co.*, 82 F. Supp. 753 (D.N.J. 1949), *modified*, 115 F. Supp. 835 (D.N.J. 1952).

[4] Address by Douglas E. Rosenthal, Chief, Foreign Commerce Section, Antitrust Division, U.S. Department of Justice, before the American Society of International Law, "Subject Matter Jurisdiction in U.S. Export Trade" (Apr. 23, 1977), partially reprinted in *American Society of International Law, Proceedings of the 71st Annual Meeting* 214, 217 (1977).

[5] Antitrust Guide, *supra* note 1, at 7.

[6] *Pfizer Inc. v. Government of India*, 434 U.S. 308 (1978). See also *Joseph Muller Corp. Zurich v. Société Anonyme de Gérance et d'Armement*, 451 F.2d 727 (2d Cir. 1971), *cert. denied*, 406 U.S. 906 (1972); *Todhunter-Mitchell & Co. v. Anheuser-Busch Inc.*, 375 F. Supp. 610 (E.D. Pa.), *modified in part*, 383 F. Supp. 586 (E.D. Pa. 1974).

[7] See Pub. L. No. 97-290, 97th Cong., 2d Sess. (1982); S. Rep. No. 97-644, 97th Cong., 2d Sess. (1982); see generally Garvey, *The Foreign Trade Antitrust Improvements Act of 1981*, 14 *Law & Pol'y Int'l Bus.* 1 (1982).

[8] Export Trading Company Act of 1982, Pub. L. No. 97-290, §§402 and 403, 96 Stat. 1246-7.

[9] See Atwood & Brewster, *supra* note 1, at 355.

[10] Potter, *East-West Countertrade: Economic Injury and Dependence Under U.S. Trade Law*, 13 *Law & Pol'y Int'l Bus.* 413, 417–18 (1981).

[11] For background see, Hausman, *Reciprocal Dealing and the Antitrust Laws*, 77 *Harv. L. Rev.* 873 (1964).

[12] See, e.g., *W.E. Gore & Assoc., Inc. v. Carlisle Corp.*, 381 F. Supp. 680 (D. Del. 1974), *aff'd in part and rev'd in part*, 529 F.2d 614 (3d Cir. 1976).

[13] See *Betaseed, Inc. v. U&I, Inc.*, 1982-2 Trade Cas. ¶ 64,878 (9th Cir. 1982); L. Sullivan, *Handbook of the Law of Antitrust* §§170–71 (1977).

[14] F. Scherer, *Industrial Market Structure and Economic Performance* (2d ed. 1980).

[15] 365 U.S. 320 (1961).

[16] *Id.* at 329. The Court also noted that an exclusive dealing arrangement was a "type of contract which 'may well be of economic advantage to buyers as well as to sellers'". *Id.* at 334.

[17] *Id.* at 335. *But see Standard Oil Co. v. United States*, 337 U.S. 293, 314 (1979) (appearing to make the legality of an exclusive dealing arrangement turn almost entirely upon the percentage of the relevant market foreclosed).

[18] See Schwartz, *American Antitrust and Trading with State Controlled Economies*, 25 Antitrust Bull. 513 (1980); Address by Joel Davidow, Director, Office of Policy Planning, Antitrust Division, U.S. Department of Justice, "U.S. Antitrust, Free Trade, and Nonmarket Economies" (June 22, 1978); Atwood & Brewster, *supra* note 1, at 354-58.

[19] Allison, *The Antitrust Implications of Barter*, 58 Chi. Kent L. Rev. 89, 91 (1981).

[20] *FTC v. Consolidated Foods Corp.*, 380 U.S. 592, 594 (1965) (citation omitted).

[21] 15 U.S.C. §1 (1976).

[22] 15 U.S.C. §2 (1976).

[23] 15 U.S.C. §45 (1976).

[24] See citations collected in ABA Section of Antitrust Law, *Antitrust Law Developments* 29, n. 187 (1975).

[25] See *id.* at 30, n. 188.

[26] *Federal Trade Commission to Change its Approach in Reciprocity Matters*, Antitrust & Trade Reg. Rep. (BNA) No. 478, at A-3 (1970).

[27] 1977-1 Trade Cas. ¶ 61,256 (S.D.N.Y. 1977).

[28] *Id.* at 70, 778-83.

[29] 1977-2 Trade Cas. ¶ 61,636, at 72,621 (S.D.N.Y. 1977).

[30] See, e.g., 1982 Justice Department Merger Guidelines, Trade Reg. Rep. (CCH) No. 546 (released June 14, 1982); 47 Fed. Reg. 28,493 (June 30, 1982). For background see Japan Society Conference Report, "Should Economic Analysis Alone Dictate Enforcement of Competition Laws in the United States?" (Feb. 18, 1982) (Public Affairs Series No. 19); P. Areeda and D. Turner, 5 *Antitrust Law* 164-202 (1980).

[31] 473 F. Supp. 680 (S.D.N.Y. 1979).

[32] *United States v. Gulf Oil Corp.*, Crim. No. 78-123 (W.D. Pa. Filed May 9, 1978).

[33] Anhydrous Ammonia from the USSR, 44 Fed. Reg. 61,269 (1979) (Investigation No. TA-406-5, USITC Pub. No. 1006) (determination of market disruption); Anhydrous Ammonia from the USSR, 45 Fed. Reg. 27,570 (1980) (Investigation TA-406-6, USITC Pub. No. 1051) (determination of no market disruption).

[34] See *Certain Tariff and Trade Bills: Hearings Before the Subcomm. on Trade of the House Comm. on Ways and Means*, 96th Cong., 2d Sess., 606, 612 (1980) (Statement of L.L. Jaquier, Executive Vice President, W.R. Grace & Co.).

[35] Section D(4) (f) (iv), U.N. Doc. TD/RBP/CONF/10 (1980) (footnote omitted), reprinted in 19 *Int'l Legal Mats.* 813, 818-19 (1980). For background see Benson, *The U.N. Code on Restrictive Business Practices: An Antitrust Code is Born*, 30 *Am. U.L. Rev.* 1031 (1980).

[36] The procedure may be found in 28 C.F.R. §50.6 (1981); 2 Trade Reg. Rep. (CCH) ¶ 8559.

[37] See, e.g., *United States v. Grinnell Corp.*, 30 F.R.D. 358, 363 (D.R.I. 1962).

[38] *Comegys, Business Reviews by the Antitrust Division*, The Conference Board Record (March 1974) at 22.

[39] Davidow, *U.S. Antitrust and Doing Business Abroad: Recent Trends and Developments*, 5 *N.C. J. Int'l L. & Com. Reg.* 23, 31 (1980).

[40] *Id.*

[41] Statement on United States Export Policy, 14 *Weekly Comp. Pres. Doc.* 1631, 1634 (Sept. 26, 1978).

[42] U.S. Department of Justice, Press Release (Dec. 6, 1978), reprinted in 2 Trade Reg. Rep. ¶8559, at 14,031-3.

[42] U.S. Department of Justice, Press Release (Oct. 2, 1979).

[44] 16 C.F.R. §§1.1-1.4 (1982); 3 Trade Reg. Rep. (CCH) ¶ 9801.01-.04. See *Golden Grain Macaroni Co.*, [1979-73 Transfer Binder] Trade Reg. Rep. (CCH) ¶ 19,521, at 21,587 (FTC 1971) (suit filed after favorable advisory opinion issued).