Claiming jurisdiction over foreign firms:

A review of extraterritorial legal doctrines in the competition law regimes of the United States and the European Union

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Overview

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2. Glossary
3. Traditional view of Jurisdiction
4. Evolution of the U.S. Effects Doctrine
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6. Conclusion

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1. Objectives

Objectives

- At the end of this session participants should be able to:
  - Describe how the concept of jurisdiction was traditionally understood in competition law.
  - Explain the evolution of the effects and implementation doctrines.
  - Identify the similarities and differences between the two doctrines.

2. Glossary

Glossary

- *Jurisdiction* – This is the territory or sphere of activity over which the legal authority of the State extends.

- *Territorial Principle* – This principle recognizes that an independent State can exercise jurisdiction over acts and/or persons within its territory.

Glossary

- *Extraterritoriality* - This is where a state exercises jurisdiction over acts and/or persons in a foreign territory.

- *Comity* – This is where different States will mutually recognize each other's acts and decisions out of courtesy and respect.

3. Traditional view of Jurisdiction

Detailed content:

3.1 – Jurisdiction is territorial
3.2 – Extraterritoriality – A recurring theme

3.1 Jurisdiction is territorial

- Centuries old understanding of jurisdiction was that it is necessarily territorial.

- In other words, an independent State has the legal right to address a physical presence, activity or conduct that is within its territory.

3.1 Jurisdiction is territorial

- But note the "expanded understanding" of jurisdiction emanating from the Permanent Court of International Justice's decision in *The Case of the S.S. Lotus (France v Turkey)*.

- This expanded understanding of jurisdiction is known as the "objective territoriality theory" in international law.

3.2 Extraterritoriality – A recurring theme

"While the law traditionally respected territorial borders, business in a globalized world tends to ignore such borders. This tension presents the risk that national competition laws may fail to address significant restraints of trade"

4. Evolution of the U.S. Effects Doctrine

Detailed content:

4.1 – The Sherman Act
4.2 – Early interpretation of Sherman Act Jurisdiction
4.3 – The rise of international business
4.4 – Birth of the effects doctrine
4.5 – Criticisms of the doctrine
4.6 – International opposition
4.7 – Evolution of comity
4.8 – Criticisms of comity
4.9 – Resurgence of the effects doctrine
4.10 – Evolutionary time line

4.1 The Sherman Act

- The Sherman Act (1890) is the first competition or "antitrust" legislation in the United States.

- Arguably, the Act may be seen as a legislative response to popular opinion against big business in 19th century America.

4.1 The Sherman Act

US Senator John Sherman

"The popular mind is agitated with problems that may disturb social order, and among them all none is more threatening than the inequality of condition, of wealth, and opportunity that has grown within a single generation out of the concentration of capital into vast combinations to control production and trade and to break down competition."

4. 1 The Sherman Act

- While domestic concerns certainly informed passage of the Act, there is language in it to suggest that Congress had in mind foreign commerce:

Section 1

"Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal."

4.1 The Sherman Act

Section 2

"Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony."

- Early cases under the Sherman Act demonstrate that US courts understood its jurisdictional reach in the traditional sense.

4. 2 Early interpretations of Sherman Act Jurisdiction

- The territorial application of the Act is demonstrated in:
  - **American Banana Co v United Fruit Co.** (1909)
  - **United States v Pacific & Arctic Railway & Navigation Co.** (1913)

4.2 Early interpretations of Sherman Act Jurisdiction

American Banana Co. (1909)

First case where US Supreme Court had to consider whether the Sherman Act could apply to anticompetitive foreign conduct.

Both parties were American banana companies who operated in Panamanian territory which was ruled by Costa Rica at the time.

Defendant company conspired with the Costa Rican government to drive the Plaintiff out of business in the territoriy.

The Defendant was not liable. The court said that statutes will be interpreted as applying only to the territory within the jurisdiction of the law maker, and the general words in the Sherman Act would be read with that mind.

4.2 Early interpretation of Sherman Act jurisdiction

Pacific & Arctic Railway & Navigation Co. (1913)

Case concerned a land and sea transportation route between the US and Canada which involved US and Canadian steamship and railway firms.

Canadian railway firms charged higher rates to the rivals of their US steamships partners thereby foreclosing competition along the US coastal portion of the route.

Defendants argued that the Sherman Act did not apply because a part of the route was outside US territory (the land portion in Canada).

Argument rejected. While accepting that there was no jurisdiction over foreigners operating in foreign territories, court said there was jurisdiction once they operated in US territory.

4.2 Early interpretation of Sherman Act jurisdiction

- **American Banana** may be consistent with the strict traditional view of jurisdiction under international law.

- Whereas **Pacific & Arctic Railway** may be more consistent with the objective territoriality theory that was confirmed in *Lotus* case.

4.3 The rise of international business

- Sherman Act jurisdiction was territorial, but the way that firms did business increasingly ignored territorial limitations.

- The first modern multinational enterprises (MNEs) had emerged during the latter half of the 19th century (for eg: United Fruit Co. (1899), Royal Dutch/Shell Group (1907).

4.3 The rise of international business

- The trend towards internationalization by firms was being driven in part by:
  - Increased protectionism in traditional markets in Europe.
  - Innovation in transportation and communications drove worldwide resource seeking and market seeking activities by firms.
  - Example: De Beers Mining Co's African operations.
- But increased risk of cross-border anticompetitive conduct.

4.3 The rise of international business

- Rise of international business helps to frame the evolution of Sherman Act jurisdiction.

- **United States v Aluminium Company of America et al** (the "Alcoa case") out the effects doctrine 'on the map'.

4.4 Birth of the effects doctrine

The Alcoa case (1945)

The claim against Alcoa and its Canadian subsidiary was that they conspired with foreign firms to monopolize the market for aluminum ingots in the US by eliminating import competition.

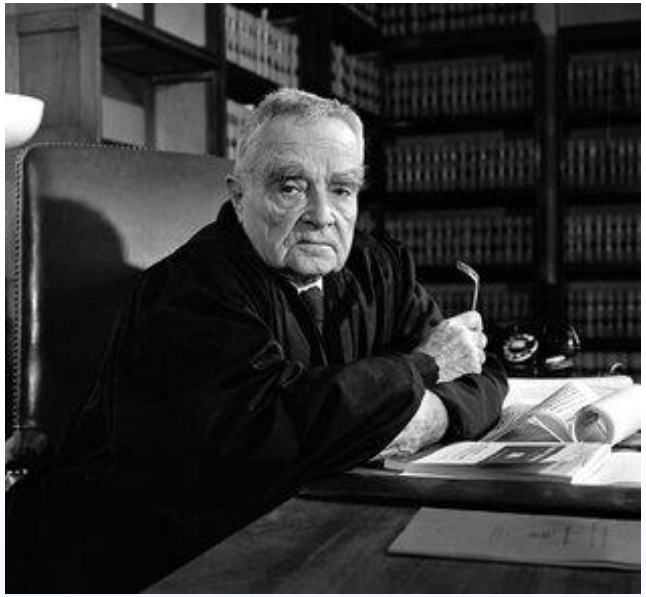
Conduct centered around 2 agreements in which Alcoa's Canadian subsidiary agreed production quotas with European firms. The quotas included exports to the United States.

The main question before the court was whether or not the Sherman Act could be applied to the agreements?

Question answered by relying on statutory interpretation – what did Congress intend when it passed the Sherman Act?

4.4 Birth of the effects doctrine

Judge Learned Hand:



"We should not impute to Congress an intent to punish all whom its courts can catch, for conduct which has no consequence within the United States…On the other hand, it is settled law…that any state may impose liabilities, even upon persons not within its allegiance, for conduct outside its borders that has consequences within its borders which the state reprehends, and these liabilities other states will ordinarily recognize."

4.4 Birth of the effects doctrine

The Alcoa case cont'd

In order to answer the question before the Court, Judge Hand formulated 2 requirements to be met: (i) that the agreement was intended to affect imports; AND (ii) that it did affect them.

The judge relied on earlier decisions such as **Pacific & Arctic Railway** in support of this formulation of the doctrine.

The first agreement was held not be a violation of the Act because it was not intended to affect US imports.

The second agreement was held to be a violation of the Act because both requirements were satisfied in relation to it.

4.5 Criticisms of the doctrine

- Arguably the effects doctrine shares some parallels with the objective territoriality theory from the *Lotus case*.

- Criticisms of the doctrine:
  - Contrary to international law
  - Somewhat vague: no precise definition of "effect"
  - Ignores the legitimate interests of other States

4.6 International opposition

- Despite the criticisms, US courts continued to use the doctrine to extend their competition law jurisdiction over foreign firms.

- US courts went so far as to issue judgments under their competition law against foreign firms to coerce compliance.

4.6 International opposition

- But there was significant international 'blow back'. In a 1978 diplomatic note the British Government stated that:

"HM Government considers that in the present state of international law there is no basis for the extension of one country's antitrust jurisdiction to activities outside of that country of the foreign national."

4.6 International opposition

- Political tensions over the extraterritorial application of US antitrust laws have also led several countries to enact "blocking statutes".
  - E.g. Protection of Trading Interests Act, 1980 (UK).
- Blocking statutes operate as a blunt constraint on the extraterritorial application of competition law by preventing cooperation between authorities.

4.7 Evolution of comity

Timberlane Lumber Co v Bank of America (1977)

Allegation that BoA's Honduran subsidiary conspired with others in Honduras to disrupt Timberlane's logging business in Honduras so as to prevent it from exporting to the US.

While accepting the effects doctrine, the Court observed that the doctrine "…by itself is incomplete because it fails to consider other nations' interests."

Court preferred what it called a "jurisdictional rule of reason" which involved the balancing of US interests vis-à-vis the interests of other States in deciding whether to apply the Sherman Act.

3 stage test to determine jurisdiction: (i) does the conduct affect the foreign commerce of the US; (ii) does it violate the Act; AND (iii) as a matter of international comity, should US jurisdiction be asserted over the conduct?

4.7 Evolution of comity

- The rationale for the 3rd stage of the Timberlane test is to determine whether or not it is appropriate for the US to *exercise* extraterritorial jurisdiction in a case to the exclusion of other states' interests.

- The court identified the types of interests to be weighed in the balancing exercise. They are:

1. The degree of conflict with foreign law or policy

4.7 Evolution of comity

2. Nationality of the parties

3. Enforcement effectiveness

4. Relative significance of the effect in the US vs. elsewhere

4.7 Evolution of comity

5. The motive for the conduct

6. Foreseeability of the effects

7. Location of the conduct or the majority of the activities

4.7 Evolution of comity

- Timberlane I's comity analysis can operate as a more finely tuned "self imposed" constraint on competition law jurisdiction than blocking statutes.

- This was demonstrated in round two of the Timberlane litigation when the US court declined to apply the Sherman Act to the conduct in Honduras.

4.7 Evolution of comity

Timberlane II (1984)

After the decision in Timberlane I the case was remanded to the district court for a decision based on the new test. District court refused jurisdiction and dismissed the case.

On the second appeal, the Court of Appeal applied the comity considerations to the same facts. Some of the facts slightly weighed in favour of asserting US jurisdiction.

Other factors such as the potential for conflict with Honduran law and the greater effect of the conduct on the Honduran economy weighed heavily against asserting US jurisdiction.

Ultimately, while the Court found that there had been an effect in a US market, the balance of considerations pointed to Honduras. This made it inappropriate to claim US jurisdiction.

4.8 Criticisms of comity

- While Timberlane's comity analysis is meant to address one of the criticisms of the classic effects doctrine, the analysis has itself been criticized:
  - Some of the factors to be balanced are inherently matters of policy, which courts are not competent to determine.

4.9 Resurgence of effects doctrine

Hartford Fire Insurance (1993)

Claim that certain London reinsurers conspired to force US primary insurers to change the terms of their policies to conform to terms preferred by those reinsurers.

Defendants conceded that there was jurisdiction under the Sherman Act, but argued that the courts should decline to exercise it based on Timberlane's comity considerations.

Supreme Court doubted the idea that comity considerations should ever require a US court to decline exercising Sherman Act jurisdiction.

Instead the real question in the case was whether or not there was a "true conflict" between British insurance law and the Sherman Act. The court found there was none and so decided that jurisdiction should be exercised over London reinsurers.

4.9 Resurgence of effects doctrine

- The overall result of **Hartford Fire** is two fold:
  - Restatement of the effects doctrine as the primary test for establishing jurisdiction; and
  - Truncating Timberlane's several comity considerations into one main consideration, i.e. whether there is a "true conflict" of laws

4.9 Resurgence of effects doctrine

- The **Hartford Fire** decision has made it more likely that jurisdiction will be exercised.

- Yet this may not necessarily lead to diplomatic tensions because:

  - Increased prevalence of competition law among states.

  - Avenues for cross border cooperation have increased.

4.10 Evolutionary time line

1890s – 1940s

Consistency between the way jurisdiction was understood under US competition law and traditional understanding of jurisdiction in international law.

1940s – 1970s

Effects doctrine developed in the context of the increasing globalization of business.

1970s – 1990s

Backlash against effects doctrine induced evolution of comity considerations as a constraint on jurisdiction.

1990s – present

Resurgence of effects doctrine.

5. Evolution of the E.U. implementation doctrine

Detailed content:

5.1 – EU competition provisions
5.2 – Commission's early view
5.3 – Transatlantic differences
5.4 – View of the courts
5.5 – Birth of the implementation doctrine
5.6 – Criticism of the doctrine
5.7 – Comparison of both effects and implementation doctrines

5.1 EU competition provisions

- Like the Sherman Act, Article 101 of the Treaty on the Functioning of the European Union (TFEU) contains broad language that may be interpreted to permit extraterritorial application:

Article 101

"…all agreements between undertakings, decisions by association of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market."

5.2 Commission's early view

- The Commission initially took the view that Article 101 permitted extraterritorial application in a manner similar to the effects doctrine:

"Article 85 [predecessor to Article 101]…applies to restrictive practices which MAY AFFECT trade between Member States even if the undertakings and associations which are parties to the restricted practices are established or have their headquarters outside the Community, and even if the restrictive practices in question also affect markets outside the EEC." (Commission, 1985)

5.3 Transatlantic differences

- Yet it was several European states who had voiced the most opposition to the effects doctrine (for eg: the United Kingdom).

- But these European states also had to respond to the threats posed to their common economic interests by globalization.

5.4 – View of the courts

- Notwithstanding the Commission's preference for an effects based approach, the Courts declined to adopt that view.

- Instead, the judges developed other legal approaches such as the "single economic entity doctrine" and the "implementation doctrine".

5.4 View of the courts

The "Dyestuffs" case (1972)

ICI, manufacturer of dyes, was found to have engaged in a concerted practice with other producers to simultaneously increase the prices of a wide range of dyes by the same % amount on 3 occasions.

ICI's registered office was in England but it had subsidiaries in the Common Market. Evidence that London HQ ordered subsidiaries to increase the prices.

ICI challenged jurisdiction of Commission. Commission's argument was two fold: (i) ICI acted within the Common Market; and (ii) Alternatively, ICI's conduct had effects in the Common Market.

Court ruled that ICI carried out concerted practice directly within the Common Market through its subsidiary. Therefore Commission had jurisdiction over ICI.

5.4 View of the courts

- Arguably, it was open to the Court in Dyestuffs to apply the effects doctrine.

- However, jurisdiction was justified on the basis that the company and its subsidiary formed a single economic entity in the Common Market.

5.4 View of the courts

- A possible reason for this approach is that it allowed the Court to avoid the tension between Member States' opposition to the effects doctrine and the need to address cross border conduct:
    - Jurisdiction can be asserted once foreign firms establish subsidiaries in EU territories.

5.5 Birth of implementation doctrine

The "Wood Pulp" case (1972)

Wood pulp producers, all outside of the European Community, engaged in concerted practice on the prices charged to customers in the Community.

Commission claimed jurisdiction on the basis that the conduct affected prices charged in the Community. Producers argued that this was not compatible with international law.

The Court upheld jurisdiction against the producers. It drew a distinction between the formation of anti-competitive conduct and its implementation within the Community.

Concerted practice on pricing had been implemented in the Community when the producers sold directly to Community purchasers at the agreed prices.

5.6 Criticisms of the doctrine

- Note the Wood Pulp Court's distinction between "formation" of anti-competitive conduct and its "implementation" in the Community.
  - It did not define "implementation"
- But in the later case of **Gencor v Commission** (1999), the court explained that "implementation" only requires sales within the Community.

5.6 Criticisms of the doctrine

- Arguably, Dyestuffs is more consistent with the territoriality principle than Wood Pulp:
  - Notably, at no point did the Wood Pulp court identify any physical activity committed by the producers on Community territory.

5.7 Comparison of both doctrines

Similarities

- *No requirement for offending firm(s) to be physically present in affected territory.*
- *Also no requirement for any part of the conduct to have occurred in the affected territory.*
- *Requirement for causal connection between the conduct and economic repercussions.*

Differences

- *Conceptually, the effects doctrine is wider than the implementation doctrine.*
- *This means that in practice the effects doctrine can be applied to some conduct (e.g. concerted refusal to deal) whereas the implementation doctrine may not.*

6. Conclusion

Detailed content:

6.1 – Relevance to the Caribbean
6.2 – Concluding remarks

6.1 Relevance to the Caribbean

CSME

> RTC competition provisions (Chapter 8).

> CCJ must apply international law (Article 217).

Member States

> Presumption against extraterritoriality.

> No or little precedent for extraterritorial application of domestic laws.

6.2 Concluding remarks

- Arguably, the doctrines evolved as competition law responses to risks posed to national economic interests by globalization.

- In this regard, both doctrines involve a fundamental untethering of competition law from strictly territorial notions of jurisdiction.

6.2 Concluding remarks

- Yet, another view, is that these doctrines are the legal manifestations of the power and/or influence of certain States in the global political economy.

- On this view, perhaps SIDs will be better served by pursuing other avenues to address cross border anticompetitive conduct (eg cooperation agreements).


Thank you