

Client Alert

Latham & Watkins Litigation Department

***En Banc* Seventh Circuit Determines FTAIA is Not Jurisdictional and Broadly Construes "Direct" Effects**

Companies facing civil and criminal antitrust actions in the Seventh Circuit may now be scrutinized for foreign conduct that may previously have been beyond the reach of US antitrust enforcement. With its *en banc* opinion in *Minn-Chem, Inc. v. Agrium Inc.*, No. 10-1712 (7th Cir. June 27, 2011), the Seventh Circuit overruled its prior precedent and significantly expanded the extraterritorial scope of antitrust laws within its circuit. Although the Sherman Act addresses prohibitions on unlawful restraints of trade "with foreign nations," the Foreign Trade Antitrust Improvements Act (FTAIA) limits the extraterritorial reach of antitrust laws.¹ See 15 U.S.C. §§ 1-2.

The FTAIA establishes that the Sherman Act applies to foreign conduct that (1) is import commerce or (2) has a "direct, substantial, and reasonably foreseeable" effect on domestic or export commerce. Though it had previously held — consistent with a majority of other Circuits — that the FTAIA presented a jurisdictional bar, the Seventh Circuit overruled its earlier decision in *United Phosphorus, Ltd. v. Angus Chemical Co.*, 322 F.3d 942 (7th Cir. 2003), and now holds that the FTAIA sets forth a substantive element of an antitrust claim. The Seventh Circuit also adopted an expansive view of "direct" effect, such that actions forming a "reasonably proximate nexus" with a domestic injury can give rise to antitrust liability. This decision raises two potential concerns for companies subject to criminal or civil antitrust claims in the Seventh Circuit. First, if the FTAIA is construed as an element of the claim, as opposed to a jurisdictional bar, it may make it more difficult to defeat antitrust claims on a motion to dismiss. Second, the court's new "reasonably proximate nexus" standard may encourage the DOJ to try to expand its jurisdictional reach and prosecute wholly foreign conduct previously considered outside of its enforcement powers.

Background

Plaintiffs, who are purchasers of potash (potassium-rich mining elements primarily used in fertilizers), alleged that the potash industry was dominated by a small group of actors who restrained output in order to inflate global prices and thus violated Section 1 of the Sherman Act, 15 U.S.C. § 1. Plaintiffs alleged a rolling scheme where cartel members would first negotiate and agree upon prices in Brazil, India and China, then adopt those prices as benchmarks for sales in other countries,

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including the US. Between 2003 and 2008, plaintiffs alleged that potash prices increased by 600 percent, despite generally even demand.

The district court denied defendants' motion to dismiss under Fed. R. Civ. P. 12(b)(1) and the FTAIA, reasoning that plaintiffs' allegations regarding the "nexus" between the anticompetitive conduct and defendants' importation of goods were sufficient to satisfy the FTAIA's import commerce exclusion. *In re Potash Antitrust Litig.*, 667 F. Supp. 2d 907, 926-27 (N.D. Ill. 2009). Consistent with prior precedent, the district court analyzed the FTAIA as a jurisdictional question. *Id.* at 925.

On appeal, a three-judge panel of the Seventh Circuit found defendants were entitled to dismissal under either Fed. R. Civ. P. 12(b)(1) or 12(b)(6). The panel recognized that the Seventh Circuit's *en banc*'s decision in *United Phosphorus* — which held that the FTAIA's requirements are jurisdictional — could potentially be reconsidered in light of subsequent precedent, but declined to take up the issue. *Minn-Chem, Inc. v. Agrium Inc.*, 657 F.3d at 652, 658 (citing *Morrison v. Nat'l Austl. Bank*, ___ U.S. ___, 130 S. Ct. 2869 (2010) and *Arbaugh v. Y & H Corp.*, 546 U.S. 500 (2006)). The panel rejected the district court's "nexus" analysis and found the import commerce exclusion did not apply because no defendants targeted US imports through their actions. The panel adopted the Ninth Circuit's formulation that a "direct" effect "flows as an immediate consequence of the defendant's activity." *Id.* at 662 (quoting *United States v. LSL Biotechs.*, 379 F.3d 672, 680 (9th Cir. 2004)). The panel then concluded that plaintiffs' general allegations about benchmarked prices did not demonstrate a "strong enough" relationship with domestic potash sales to establish a "direct" effect. *Id.* at 662.

Seventh Circuit *En Banc* Decision

The *en banc* Seventh Circuit analyzed two issues: (1) whether the FTAIA imposes a jurisdictional limitation on a court's subject matter jurisdiction and (2) whether plaintiffs' complaint survived under the import commerce exclusion or domestic effects exception to the FTAIA. The *en banc* court resolved both questions in plaintiffs' favor.

Seventh Circuit Holds the FTAIA As An Element of An Antitrust Claim, Not a Jurisdictional Bar

Even though the majority of other circuits that have addressed the issue have applied the FTAIA as a jurisdictional bar, the *en banc* Seventh Circuit rejected the majority view and treated the FTAIA as an element of a claim. Relying on the Supreme Court's construction of securities laws in *Morrison*, the Seventh Circuit reasoned that limits on the FTAIA's extraterritorial reach describe "what conduct the law purports to regulate" and not the power of the court itself. Thus, it determined the FTAIA "sets forth an element of an antitrust claim, not a jurisdictional limit on the power of the federal courts." In so holding, the court overruled its earlier *en banc* ruling in *United Phosphorous*. In addressing the jurisdictional question, Seventh Circuit referenced the Third Circuit's recent decision in *Animal Sci. Prods., Inc. v. China Minmetals Corp.*, which overturned prior precedent and found the FTAIA did not impose a jurisdictional limitation. 654 F.3d 462 (3d Cir. 2011).

Seventh Circuit Describes the Reach of the Import Commerce and Domestic Effects Doctrines

Next, the court turned to the application of the FTAIA's import commerce and domestic effects carve-outs applied to plaintiffs' allegations.

With respect to import commerce, the court observed that “import trade and commerce are excluded at the outset” by the language of the FTAIA and thus US antitrust laws fully applied to “transactions in which a good or service is being sent directly into the United States.” To the extent the complaint alleged direct transactions between plaintiff US entities who purchased from certain defendants located outside the US, the import commerce exclusion to the FTAIA applied. After surviving this hurdle, the court turned to the extraterritorial standard in *Alcoa* and *Hartford Fire*, which limits the Sherman Act to foreign conduct “producing a substantial intended effect” in the United States. *Hartford Fire Ins. Co. v. Cal.*, 509 U.S. 764, 797 (1993). Plaintiffs’ allegations describing a cartel capable of manipulating the supply of a homogenous product in order to create a “six-fold” increase in price sufficed to overcome the *Hartford Fire* requirements. As such, the court found that those aspects of the complaint describing direct import purchases of potash from foreign entities could not be dismissed pursuant to the FTAIA.

With respect to non-import, non-domestic commerce, the court described the requirements for demonstrating that foreign conduct had a “direct, substantial, and reasonably foreseeable effect” on domestic commerce. After finding the substantiality and foreseeability elements were easily satisfied by the complaint, the court focused on what it means to have a “direct” effect. The court rejected and criticized the Ninth Circuit’s “immediate consequence” formulation that the three judge panel had applied. Instead, the *en banc* court opted for a more lenient “reasonably proximate cause” definition advocated in an *amicus* brief filed by the Department of Justice. See Brief for the United States and the Federal Trade Commission as *Amici Curiae* in Support of Neither Party on Rehearing *En Banc* (Gov’t Brief) at 21. The DOJ argued that the historical application of “directness” in antitrust actions and considerations of comity favored a reasonably proximate causation standard. In applying this standard to the complaint, the court determined that allegations that the defendants benchmarked US import sales off of cartelized prices in Brazil, India and China, combined with allegations of foreign supply restrictions that had increased prices, were sufficient for the purpose of satisfying the proximate cause standard. To the extent plaintiffs’ complaint referenced conduct of a sales agent operating entirely outside the United States, the conduct stated a claim because of its purported direct effects on domestic markets.

In sum, the Seventh Circuit read the “import commerce” exclusion and “domestic effect” exception broadly, suggesting that future litigants, including the DOJ, may be able to advance claims on conduct that would have previously been excluded under the FTAIA. Defendants in the matter have signaled their intent to appeal the decision the Supreme Court. In a motion to stay the mandate pending certiorari, defendants observed that the Seventh Circuit now split with other circuits on the definitions of import commerce and direct effects. See Defendants-Appellants’ Motion for Stay of Mandate Pending the Filing of a Petition for Certiorari at 8-10.

Client Implications

The *Minn-Chem* decision implicates procedural considerations for litigants seeking to raise FTAIA issues in civil actions. It also raises more general substantive concerns regarding the type of conduct that might now fall within the ambit of US antitrust laws.

Procedural Implications for Civil Class Actions

The court’s rejection of a jurisdictional reading of the FTAIA is a departure from the majority of other circuits that have interpreted the statute. See IB Phillip E. Areeda

and Herbert Hovenkamp, *Antitrust Law* ¶ 272i (3d ed. 2006) (noting that Congress resolved concerns regarding the broad jurisdictional scope of the Sherman Act by enacting the FTAIA). A party seeking dismissal of a complaint with Sherman Act claims in the Seventh Circuit must now move under Rule 12(b)(6), and not Rule 12(b)(1). The *Minn-Chem* court observed that this is a distinction with a difference. A motion for dismissal for lack of subject matter jurisdiction under Rule 12(b)(1) can be brought at any time and can place an evidentiary burden on plaintiffs to establish jurisdiction. This is advantageous to defendants because it allows the court to look beyond the pleadings when determining whether dismissal is appropriate. See 2 *Moore's Federal Practice – Civil* § 12.30[3]. By contrast, a defendant can only move to dismiss for failure to state a claim under 12(b)(6) before trial and, in the vast majority of cases, the sufficiency of the complaint is finalized long before that. If the FTAIA sets forth an element of an antitrust claim, as opposed to a jurisdictional bar, a court is likely to allow full discovery on the merits before deciding FTAIA issues. The *Minn-Chem* court took comfort in the fact that parties who want to use the FTAIA as a basis for dismissal “will be able to do so within these generous time limits,” but that may provide little solace to litigants who may have to engage in potentially costly discovery before being able to exclude wholly foreign conduct from the scope of an action.

Parties may now also have to litigate whether the FTAIA is a jurisdictional bar even in circuits where the issue has been long-settled. Before *Morrison* and *Arbaugh*, circuit courts consistently characterized the FTAIA's limitations as jurisdictional, consistent with the statute's legislative history. See IB Phillip E. Areeda and Herbert Hovenkamp, *Antitrust Law* ¶ 272i2 and n. 83 (3d ed. 2006) (collecting cases from the Second, Third, Seventh, Ninth, Eleventh and D.C. Circuits). After *Morrison* and *Arbaugh*, the Third and Seventh Circuits have overturned prior precedent to reclassify the FTAIA as an element of the claim. District courts have applied the same reasoning before concluding the FTAIA is not jurisdictional. For instance, in *TFT-LCD*, Judge Illston of the Northern District of California found that *Arbaugh* compelled a non-jurisdictional reading of the statute, even in the face of contrary Ninth Circuit precedent in *LSL Biotechs.*, which applied a jurisdictional reading of the FTAIA. *In re TFT-LCD (Flat Panel) Antitrust Litig.*, 882 F. Supp. 2d 953, 959 (N.D. Cal. 2011); *but see In re Cathode Ray Tube (CRT) Antitrust Litig.*, 738 F. Supp. 2d 1011, 1022-23 (N.D. Cal. 2010) (analyzing FTAIA as an issue of subject matter jurisdiction). When raising FTAIA issues, civil litigants in all circuits should be mindful that trial courts may now reject a jurisdictional reading of the FTAIA. Nevertheless, arguments in favor of a jurisdictional reading remain viable. Though the Supreme Court did not address the jurisdictional question directly in *F. Hoffman-La Roche Ltd. v. Empagran S.A.*, it did quote favorably a passage from an antitrust treatise that analyzed the FTAIA in terms of “subject matter jurisdiction.” 542 U.S. 155, 166-67 (2004) (citing Areeda and Hovenkamp, *Antitrust Law*). Given the implications to federal court dockets and the split among circuits on the issue, Supreme Court review may be appropriate to clarify the jurisdictional issue.

Broad Construction of Direct Effects

By noting that the FTAIA “applies not only to private actions, such as this one, but also to actions brought by the two federal agencies” enforcing antitrust laws, the Seventh Circuit broadcasted that its definition of direct effect had both civil and criminal implications. In its brief, the government presented the hypothetical of a conspiracy among foreign manufacturers to fix prices on inputs sold to other foreign manufacturers, who would then incorporate the input into other goods sold in the United States. Gov't Brief at 23. The government reasoned that the conspiracy to

restrain trade on those non-import inputs would proximately cause price increases for finished goods sold in domestic markets. Having succeeded in convincing the Seventh Circuit to adopt its “reasonably proximate cause” formulation, the DOJ and FTC may broaden the scope of foreign conduct subject to enforcement in the US.

Relatedly, enforcement agencies and civil plaintiffs may argue that criminal fines and civil damages awards should be larger in order to capture all injuries that were proximately caused by cartel conduct. Within the Seventh Circuit, civil plaintiffs can now argue that damages should extend to conduct that would have previously been too causally remote to give rise to liability. Likewise, enforcement agencies may be tempted to bring actions—whether civil or criminal—in the Seventh Circuit in order to gain a strategic advantage from the more favorable standard and extract more punitive outcomes.

Parties need to be mindful of the developments regarding extraterritorial enforcement of antitrust laws, particularly as the *Minn-Chem* decision suggests a departure from the long-standing view that the FTAIA is jurisdictional. Companies must also be aware that, should a suit arise based upon violations of antitrust laws abroad, the scope of the conduct at issue may expand to include actions that once appeared purely foreign in nature.

Endnotes

¹ The FTAIA states:

Sections 1 to 7 of this title [the Sherman Act] shall not apply to conduct involving trade or commerce (other than import trade or import 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 the provisions of sections 1 to 7 of this title, other than this section.

If sections 1 to 7 of this title apply to such conduct only because of the operation of paragraph (1)(B), then sections 1 to 7 of this title shall apply to such conduct only for injury to export business in the United States.

15 U.S.C. § 6a.

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