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CLIENT ADVISORY

Supreme Court Clarifies Antitrust Rules Governing Joint Ventures

In its unanimous decision yesterday in *Texaco Inc.* v. *Dagher*, 547 U.S. ___ (2006), the Supreme Court made clear that a properly formed joint venture may price the products of the venture without running afoul of *per se* rules against price fixing The rule of reason applies even if the joint venture sells its products under two brands rather than one and even if there is an option to unravel the joint venture at the expiration of a fixed term of years.

BACKGROUND

The challenge arose after Texaco and Shell Oil formed a joint venture, Equilon, in which they pooled their gasoline refining and marketing assets. The creation of the joint venture had been subject to pre-merger notification under the Hart-Scott-Rodino Act, and Texaco and Shell were permitted to proceed only after modifying the joint venture pursuant to a Federal Trade Commission consent decree. Once the joint venture was formed, Texaco and Shell no longer competed with each other to produce or market gasoline. However, the output of the joint venture continued to be sold under the Texaco and Shell brands, and one person at the joint venture was responsible for setting a common price for both brands.

Plaintiffs argued that the sale of the independently branded gasoline at a common price was price fixing and a *per se* violation of the Sherman Act. Under the *per se* analysis, once a finder of fact determines that competitors have agreed to fix the prices at which each will sell a product, the agreement can be condemned without considering whether the agreement is reasonable or has any competitive benefits.

To determine whether *per se* treatment was appropriate, the Ninth Circuit applied the "ancillary restraint" doctrine and asked whether setting a single price for two brands of gasoline produced by the joint venture was "reasonably necessary to further the legitimate aims of the joint venture."[1] Although the Ninth Circuit

[1] *Dagher* v. *Saudi Refining Inc.*, 369 F.3d 1108, 1121 (9th Cir. 2004).

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recognized that the joint venture had many procompetitive effects, it concluded that it was not necessary for the joint venture to set a single price, and condemned the conduct as *per se* unlawful.

THE COURT'S DECISION

The Supreme Court rejected use of the ancillary restraints doctrine, noting that it governs only the validity of restrictions imposed by the joint venture on *non-venture* activities. The doctrine is inapplicable "where the business practice being challenged involves the core activity of the joint venture itself." Slip Op. at 6.

Instead, the Court held that as a single entity, a joint venture, like any other firm, has the discretion to set the prices of its products and that the internal pricing decisions of a legitimate joint venture should not be reviewed using the *per se* rule. Slip Op. at 4. The Court's rationale raises the further prospect that no Sherman Act §1 challenge to a joint venture's decision to set a common price for its products—whether under the per se rule or the rule of reason—can succeed. (The agreement creating a joint venture remains subject to analysis under the rule of reason.) Because plaintiffs disavowed any rule of reason challenge to the joint venture's pricing, the Court expressly declined to reach the issue. Slip Op. at 5 n.2. But by treating the pricing decision as that of a single entity "and not a pricing agreement between competing entities," Slip Op. at 4, the opinion strongly implied that the claims concerned only unilateral conduct not covered by § 1.

IMPLICATIONS

The Ninth Circuit's decision was widely viewed as anomalous, a view confirmed by the Supreme Court's unanimous reversal. Had the Ninth Circuit's decision been affirmed, the doors would have been opened to antitrust attacks on the most fundamental aspects of a joint venture's operation. The Supreme Court decision makes clear that when a joint venture prices its own products, its pricing decisions are not subject to attack as a *per se* violation of § 1.

In one interesting bit of *dicta*, the decision characterizes the Court's opinion in *State Oil Co.* v. *Khan*, 522 U. S. 3, 10-19 (1997), as "concluding that vertical price-fixing arrangements are subject to the rule of reason, not *per se* liability." Slip Op. at 3. In fact, *Khan* overruled only the Court's prior decisions holding vertical agreements setting *maximum* prices to be *per se* unlawful. 522 U.S. at 15-18 (holding such agreements must be analyzed under the rule of reason). Vertical *minimum* price fixing agreements have been treated as per se unlawful since *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U.S. 373, 409 (1911). It is not clear whether the court meant to signal the beginning of an attack on the application of the *per se* rule to vertical minimum price fixing—the last vestige of the *per se* rule in the vertical agreement context—or whether the language is simply the result of imprecise word choice.

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