



ANTITRUST COMPLIANCE GUIDELINES

I. POLICY

It is the policy of the SMART CARD ALLIANCE to comply fully with the antitrust laws applicable to trade association activities. In furtherance of this policy, the SMART CARD ALLIANCE has prepared these Antitrust Compliance Guidelines, pertaining to U.S. antitrust laws, and will periodically consult with legal counsel. By reviewing these Guidelines, SMART CARD ALLIANCE officers, employees, and members will be better able to identify, and thus avoid, improper activities and business practices.

Every person who is a SMART CARD ALLIANCE officer, employee, or otherwise engaged to conduct its business, shall review these Guidelines. Members participating in SMART CARD ALLIANCE events are strongly encouraged to review these Guidelines. Given the significant penalties that can result from antitrust violations (*e.g.*, criminal incarceration), everyone involved with the SMART CARD ALLIANCE has a responsibility to his or her employer, to the SMART CARD ALLIANCE, and to his or her own family to avoid antitrust violations. These Guidelines will assist you in meeting that responsibility.

II. EXECUTIVE SUMMARY: DO'S AND DON'TS

The principal function of antitrust law is to prohibit agreements and conspiracies between competitors that restrain trade. Trade associations, by their nature, involve meetings and discussions between competitors and, thus, opportunities for concerted activity. For this reason, trade association meetings are frequently the subject of regulatory scrutiny and of allegations brought in private lawsuits.

That said, antitrust law recognizes that trade associations, like the SMART CARD ALLIANCE, are of great benefit to association members, consumers, and in the public interest. Trade associations, when conducted and used properly, are procompetitive. To this end, SMART CARD ALLIANCE meetings and discussions should pertain to the following topics, subject to the advice of counsel:

- industry-wide promotion and development;
- advancing technical know-how and the improvement of productivity and efficiency;

- increasing the market acceptance of smart card technology;
- commenting or providing input on industry standards documents;
- industry standards setting, with the caveat that standards must not unreasonably exclude competition and should be reviewed by counsel;
- historical and forecast market data on a general (*i.e.*, non-specific company) basis;
- legal issues which affect, or which may affect, the whole industry;
- aggregated cost and pricing trends, with the assistance of a third party and supervision of counsel;
- the policies, laws, and pending legislation of federal and state governments, including industry lobbying efforts.

Not all agreements between competitors are unlawful. However, certain types of agreements are viewed as so pernicious to competition that they are deemed automatically, or *per se*, unlawful. Under no circumstances should SMART CARD ALLIANCE members discuss, much less agree, to engage in any of the following activities with their competitors:

- to divide-up customers, either specific customers or types of customers;
- to divide-up territories or geographical markets;
- to divide-up types of businesses, product-lines, or product markets;
- to agree on prices or terms on which to supply customers, either current or future;
- to agree on prices or terms on which to do business with suppliers;
- to agree on how and whether a competitive bid will be submitted for a particular contract or project;
- to agree on, or coordinate on, the price of a competitive bid;
- to boycott certain customers or suppliers;
- to impede the entry of a new arrival in the market.¹

The above activities should not be discussed at either formal or informal meetings at SMART CARD ALLIANCE events. If a SMART CARD ALLIANCE officer or employee is present at a meeting where a discussion implicates these activities, he or she will request that the discussion cease. Members who are present at a discussion involving these activities should also request that the

¹ These types of agreements may be lawful in very limited circumstances when an ancillary to a broader arrangement (*e.g.*, as part of a legitimate joint venture or an asset sale). Such arrangements should be reviewed by antitrust counsel.

discussion cease, and report the discussion to the SMART CARD ALLIANCE and to his or her own employer.

III. BASIC PRINCIPLES OF UNITED STATES ANTITRUST LAW

This section of the Guidelines provides you with an overview of U.S. antitrust law. The purpose is not to transform you into an antitrust lawyer, but to give you basic information so that you can better identify antitrust violations, and understand the means by which they are enforced and the consequences of a violation.

Please note, this overview is necessarily brief. Antitrust analysis is highly dependent on individual facts. Do not assume that because a company in another market was able to engage in certain conduct that you can do the same. Consult a qualified attorney experienced in antitrust issues -- and consult with the SMART CARD ALLIANCE with respect to issues that pertain to its events and programs. The risks associated with antitrust violations are too great to make a mistake.

A. The Purpose Of Antitrust Law

Over a century ago, concerned with the alarming control that businesses such as John D. Rockefeller's Standard Oil monopoly were exercising over the United States economy, Congress enacted statutes designed to ensure fair competition. Also, similar antitrust laws, have now been adopted by every state. The antitrust laws have been called the "Magna Carta" of free enterprise and are designed to prevent any competitor from unfairly gaining market power or from leveraging that power for anti-competitive purposes. The premise of the antitrust laws is that consumers benefit when there is full and fair competition.

Thus, the antitrust laws forbid competitors from engaging in cartel-like behavior such as price fixing and forbid competitors from unfairly exercising market leverage to raise prices or exclude competition. State and federal antitrust laws accomplish this by (1) forbidding agreements among competitors that unreasonably restrain trade, (2) forbidding monopolists or potential monopolists from unfairly gaining market share or unfairly exercising market leverage, and (3) preventing mergers and acquisitions when the effect of those combinations may be to lessen competition.

B. The Enforcement Of The Antitrust Laws

Government Enforcement. The antitrust laws can be enforced by the federal or state governmental authorities. The government can seek either civil or criminal penalties against those who violate the law. Substantial fines can be assessed, and, in extreme cases, officers or employees can be sent to prison. The government may also seek injunctive relief to halt an allegedly illegal activity or to impose limits on a company's operations.

Private Enforcement. Private parties injured by reason of the antitrust laws may sue and recover triple the amount of their actual damages plus attorneys fees and costs. These suits may be brought in federal or state courts. Antitrust litigation, even when successful, is extremely time-consuming and expensive.

C. The Consequences Of A Violation

A violation may result in civil and even criminal penalties against the violator. The violation of certain antitrust laws is a felony and individual violators may be fined up to \$350,000 and sent to prison for up to three years. Companies may be fined up to \$10,000,000 and forced to disgorge any profits realized from the illegal activity. Most commonly, violators of the antitrust laws face civil lawsuits in which the injured plaintiff may recover triple the amount of their actual damages plus attorneys' fees and costs. Violators may also be subject to court-ordered injunctions, which can significantly impede the violator's business activities.

Further, the cost of defending against criminal and civil competition claims can be substantial (e.g., lawyers' fees), even if the defense is ultimately successful. For this reason, a cautious approach is advisable -- do not put yourself in situations that can later be mischaracterized as having antitrust implications.

D. Agreements that Unreasonably Restrain Trade.

In simple terms, state and federal laws prohibit any agreement that creates an unreasonable restraint of trade. A trade restraint is any interference with the usual forces of competition in the market. For example, an agreement among competitors to fix prices creates a restraint of trade because consumers will be deprived of the benefit of price competition. To prove a conspiracy in restraint of trade one must (1) prove an *agreement* between separate individuals or entities and (2) demonstrate that the agreement is *unreasonable*.

Agreement. The term "agreement" is broadly defined by the antitrust laws. An agreement does not need to be in writing or expressed. To the contrary, an informal understanding or a "knowing wink" can be an unlawful agreement. For example, assume that one of three competitors in a meeting stated, "It would be nice if prices went up tomorrow." If the competitors raised their prices the next day, they may be guilty of an agreement to fix prices despite the fact that the competitors did not appear to reach a formal agreement. Even exchanging information with a competitor about current prices or costs can be unlawful if it can be shown to have raised or stabilized prices.

Separate Entities. The requirement that there be separate entities is also important. For example, a parent and subsidiary corporation will be considered a single entity and therefore incapable of conspiracy. By contrast, two competitor corporations engaged in a joint venture remain independent entities in the eyes of the antitrust law and are thus capable of entering into an illegal conspiracy.

Unreasonable Restraint on Competition. Once an agreement among competitors is demonstrated, the next step is to prove that the agreement unreasonably restrains competition. Certain trade restraints are so injurious to competition that they are *per se* or automatically unreasonable. There is no defense to a *per se* violation of the antitrust laws. Courts will not consider the business justifications, no matter how plausible for such an agreement, and it will ignore the good motives of the involved parties. When detected, *per se* violations frequently result in guilty pleas, settlement agreements, substantial liability, and even fines or imprisonment.

The following is a list of agreements that create *per se* unreasonable trade restraints. Agreements in this limited category are absolutely prohibited by the antitrust laws.

Price Fixing. Any agreement or understanding between two or more competitors to fix prices are *per se* unlawful and prohibited. For example, it is *per se* unlawful for two competitors to agree on the prices they will charge their customers. This prohibition is broader than you might think. Price fixing includes any agreement that tends to affect prices or a material term of price. It also includes agreements to set a minimum or maximum price or that tends to stabilize prices. Significantly, in order to be unlawful, it is not even necessary that competitors reach, or even discuss, an ultimate price. Any agreement that affects prices is prohibited.

Production or Output Restrictions. Agreements between competitors that restrict production or output are *per se* unlawful and prohibited. Competitors may not agree upon production restraints and quotas.

Allocation of Customers. Agreements between competitors to allocate customers among themselves are *per se* unlawful and prohibited. This can take the form of one competitor agreeing not to take new business or to not take business from another competitor. Simply stated, competitors must independently choose their business relationships.

Allocation of Territories. Agreements between competitors to allocate territories or geographic markets among themselves are *per se* unlawful and prohibited. Competitors must independently choose where to do business. Thus, for example, any agreement or understanding between competitors as to where they will sell their services is unlawful.

Group Boycotts. Competitors may not agree to refuse to do business with a particular supplier or customer if the purpose or effect of that agreement is to unreasonably limit competition. This could include, for example, an agreement between two or more companies not to deal with a particular supplier or distributor.

Tied Selling or Tying Arrangements. Tied selling is the practice of requiring a customer to buy one product as a condition of buying another product. For example, under certain circumstances the manufacturer of a product could not require its customers to buy spare parts or supplies as a condition of purchasing the product.

In contrast to the above list of *per se* illegal agreements, most agreements simultaneously create trade restraints while advancing legitimate business purposes. For example, two competitors may agree to jointly produce a product that neither could efficiently produce alone. Such an agreement has anti-competitive effects (the involved parties will no longer compete) and pro-competitive effects (efficiency). Where the resulting trade restraint is not a *per se* violation, antitrust law applies a balancing test called the “rule of reason” to weigh the anti-competitive restraints caused by the

agreement against its pro-competitive benefits. If, on balance, the agreement is pro-competitive, the agreement is deemed reasonable and lawful. Under this analysis, courts will consider a number of factors including the motives of the parties, all reasonable business justifications for a particular agreement, and the impact of the agreement in the product and geographic markets.

A rule or reason analysis is often complicated. There is no bright-line test for determining whether a particular agreement is, on balance, pro-competitive. This is a “gray” area of antitrust law where experts will frequently disagree. Any of the following agreements may be an antitrust violation depending on the circumstances.

Exclusive Dealing. Exclusive dealing agreements typically involve a buyer that agrees with a seller not to purchase from the seller’s competitors. For example, a manufacturer might agree to contract exclusively with one particular distributor. Such exclusive dealing agreements are generally lawful and enforceable. Exclusive dealing is an unreasonable restraint of trade only when a significant fraction of buyers or sellers are frozen out of the market by the exclusive deal. Whether any particular agreement is reasonable will depend upon a close analysis of its scope and duration in light of market conditions and the extent to which it may foreclose competition.

Reciprocal Dealing. Reciprocal dealing typically occurs where one party buys goods from another party with the understanding that the second party will buy goods from the first. Reciprocal dealing is not unlawful unless it is used coercively or anti-competitively. For example, if one party refuses to sell unless the other party reciprocates, this may constitute the type of coercion prohibited by the antitrust laws. It is more problematic when one supplies less market power and the reciprocation requirement forecloses competition.

Joint Venture. A joint venture is an integration of operations among two or more separate persons or entities in which: (1) the enterprise is under the joint control of the owners and (2) the enterprise creates significant competitive efficiencies such as permitting the development of a new technology, new product, or entry into the new market or expanded output. Legitimate joint ventures (joint ventures where resources are integrated to produce a new product or service) are generally legal. Thus, participants in a legitimate joint venture may engage in activity, such as joint setting of prices, that would normally be condemned as *per se* illegal, so long as the venture is, on balance, pro-competitive.

E. Monopolization

The antitrust laws also prohibit monopolization and attempted monopolization, which is the ability of one company to dominate a particular market or to attempt to do so. This prohibition does not require an agreement between two or more entities. Instead it applies to the unilateral conduct of any business with significant market power. Put simply, if a company has significant power in a particular product and geographic market, that company may not engage in predatory conduct for the purpose of creating or maintaining a monopoly or damaging a particular competitor.

The antitrust laws do not prohibit monopoly power by itself. Any company can legally gain monopoly power if accomplished through legitimate means such as offering superior products,

superior services, efficiency, and initiative, or by virtue of government regulation. However, a monopolist may not engage in tactics that are not designed to serve its customers but, instead, are designed to maintain, enhance, or expand its monopoly power by excluding competition or damaging a particular competitor. Examples of illegal predatory conduct include the following:

Predatory Pricing. A monopolist may not sell its products at an “unreasonably low” price for the purpose of eliminating competition. An “unreasonably low” price would include selling at below cost for the purpose of damaging or disciplining a competitor. Predatory pricing also includes selling products below cost to customers within a particular geographic area or giving away free products with the intent of damaging a competitor. Of course, cutting prices in order to increase business is the very essence of competition. Antitrust laws encourage such price competition. Thus, all below cost pricing is not prohibited.

Refusals to Deal. A monopolist may not refuse to deal with a particular supplier, customer, or competitor if the intent of that refusal is to destroy competition. For example, a company with a dominant market share may not refuse to deal with a particular distributor because that distributor also distributes for a smaller competitive manufacturer.

Leveraging. Leveraging is the practice of using monopoly power in one market to monopolize or attempt to monopolize another market. For example, a monopolist may not use its market power in one geographic area, even if lawfully acquired, to force concessions from suppliers regarding a different geographic area where it faces competition.

F. Price Discrimination

Under the Robinson Patman Act, it may be unlawful to consistently favor one customer, by offering favorable pricing or preferential sales terms, over a competing customer. Additionally, it may be unlawful to demand a discriminatory price from a supplier. This is a complicated, and often counter-intuitive, area of antitrust law. If you believe that your business arrangements implicate price discrimination, consult with a qualified attorney.

G. Mergers and Consolidation.

Antitrust laws also provide a remedy to attack a business’s growing market power even before there is proof that the business is engaged in anti-competitive conduct. These laws prohibit any merger or acquisition which may substantially lessen competition in any relevant geographic market.

The competitive concern in any merger is whether the resulting entity will itself be so powerful that it can exercise power by imposing anti-competitive prices or terms without fear of losing significant market share. Alternatively, the concern is whether the merger leaves the market so concentrated that the small number of firms remaining in the market place will be able to expressly or tacitly collude on prices or terms. The following section describes the basics of how to determine whether a business has market power or if a market is too concentrated.

H. Determining Market Power.

Except in the case of conspirators engaging in *per se* anti-competitive actions such as price fixing, every potential antitrust claim involves an analysis of the market. This is usually done through the testimony of expert witnesses. The first step in this analysis is to determine the relevant product and geographic markets. The relevant product market includes all goods and services that compete directly or are otherwise valid substitutes. The relevant geographic market is the area of “effective competition” in which a purchaser can find alternative sources.

Once the relevant product and geographic markets are defined, the next step is to establish that the alleged restraint has an adverse effect in that market. This is usually accomplished by showing market power. Market power is defined as the ability to raise price without fear of competitive reprisal. In other words, market power exists whenever a competitor can raise prices above the levels it could charge in a competitive market. Implicit within the definition of market power is either lack of competition or the ability to exclude competition. The main obstacles to the achievement of market power include the readiness of a firm’s customers to take their business elsewhere, or the presence of numerous rivals who can and will expand their business to satisfy buyers repelled by the price increase.

The existence of market power is usually established by market share. Conventionally, a 50-55% market share is the benchmark for the existence of market power. However, in certain cases, a smaller market share may be enough. The question is whether the firm exercising market power has the ability to exclude competition or to raise prices above competitive levels.

I. Exemptions.

Even where all of these elements are proven, the conduct in question may not be unlawful. There are many types of industries or business activities that enjoy partial or complete protection from the antitrust laws. The most commonly applied exemptions include:

State Action Exemption. The courts have ruled that anticompetitive conduct by public and private entities may be exempt from the antitrust laws if it is required or compelled by state law. Generally, the conduct must be part of a clearly articulated and affirmatively expressed program by the state legislature to replace competition with regulation and the anticompetitive effects must have been clearly foreseeable. Also, if the activity is that of a private person, as opposed to a state or local government agency, the conduct must be actively supervised by a governmental regulatory agency acting pursuant to state law.

Solicitation of Government Action. The First Amendment to the United States Constitution protects the rights of companies to petition the government. Thus, it is not a violation of the antitrust laws for competitors to jointly lobby the government, even if the result these competitors seek is anti-competitive. Thus, railroads can legally lobby for laws that restrict the operation of truckers without violating the antitrust laws. Competitors are also permitted to engage in joint litigation activity without violating the antitrust laws. The exception is when the litigation is a “sham” designed to for no legitimate purpose other than to impose burdens upon rivals.

The Business of Insurance. Under the McCarran-Ferguson exemption, the business of insurance is exempt from the antitrust laws to the extent it is regulated by state law. The exemption is designed to protect the regulation of the insurance by the states. The exemption does not extend to all activities of insurers, but only to those activities that involve or are directly related to the spreading and underwriting of policyholder risk by insurers. Activities of insurers that are not part of that risk sharing function will be subject to antitrust review. The exemption also does not protect any “boycott” whereby two or more insurers agree to withhold business from a group of service providers or policyholders or where two or more insurers use collective leverage to extract concessions from policyholders or service providers.

IV. CONCLUSION

The SMART CARD ALLIANCE is committed to antitrust compliance. We hope that these Guidelines will assist SMART CARD ALLIANCE officers, employees, and members in identifying activities and business practices that may have antitrust implications. We emphasize, again, that these Guidelines are necessarily brief. They do not describe, in any comprehensive fashion, the full-range of antitrust laws and regulations applicable to SMART CARD ALLIANCE events and activities, or those of its members. If you have any questions, please contact your employer’s counsel. For compliance questions concerning the SMART CARD ALLIANCE, please feel free to contact:

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