IN RE SULFURIC ACID ANTITRUST LITIGATION: REAFFIRMING THE PRINCIPLES OF BMI AND POLK

Ismael T. Salam
Student Fellow
Institute for Consumer Antitrust Studies

I. INTRODUCTION

On December 27 2012, the Court of Appeals for the Seventh Circuit decided a case that had trudged along for nine years involving sulfuric acid producers and distributors in Canada and the United States. The issue was whether certain agreements designed to restrict production of sulfuric acid constituted price fixing and were illegal per se or were subject to the rule of reason. The case presented novel issues of involuntary production and potential antidumping exposure, which the court had not seen or heard before. The originality of the issues supported the court’s ultimate ruling that the per se illegal rule should be reserved for cases “in which experience has convinced the judiciary that a particular type of business practice has no (or trivial) redeeming benefit.”

II. PRICE FIXING UNDER THE PER SE RULE AND THE RULE OF REASON

Section 1 of the Sherman Act prohibits agreements, including conspiracies, whose anticompetitive effects on trade outweigh their procompetitive benefits. Certain agreements, however, are so likely to be anticompetitive and so unlikely to have procompetitive benefits that they are deemed illegal “per se.” These per se illegal agreements are not afforded a case-by-case

---

1 In re Sulfuric Acid Antitrust Litigation, Nos. 12-1109, 12-1224, slip op. at 13 (7th Cir. Dec. 27, 2012); see Thomas Demitrack, United States: Federal Appeals Court Reaffirms Flexible Legal Standard For Restraints In Competitor Collaborations, JONES DAY (Feb. 15, 2013), http://www.mondaq.com/unitedstates/x/216268/Antitrust+Competition/Federal+Appeals+Court+Reaffirms+Flexible+Legal+Standard+For+Restraints+In+Competitor+Collaborations (discussing case).
2 In re Sulfuric Acid Antitrust Litigation, at 13.
3 Id.
4 See 15 U.S.C. § 1 (2010) (“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.”).
inquiry into their net effect on competition as provided by the rule of reason.\textsuperscript{5} Included in this per se group are conspiracies to fix or stabilize prices.\textsuperscript{6}

Deciding that an agreement is not illegal per se can be outcome determinative. Under the rule of reason, defendants have a greater opportunity to refute the anticompetitive effects and offer a procompetitive justification, whereas no such opportunity exists if the conduct is illegal per se. Nevertheless, if a defendant violates a per se violation of the Sherman Act, the conduct is likely to be prosecuted criminally. If found guilty, a criminal fine of twice the defendant’s gain or the victim’s loss may be imposed, and individuals may be imprisoned for up to 10 years.\textsuperscript{7}

III. THE INVESTIGATION

In 1999 the U.S. Department of Justice (“DOJ”) and the Canadian Competition Bureau launched investigations into illegal price-fixing and collusive activities in the sulfuric acid sector.\textsuperscript{8} Several companies were of interest, including the Canadian based mining firms, Norfalco, LLC, Noranda, Inc., and Falconbridge, Ltd.\textsuperscript{9} Noranda and Falconbridge, which is controlled by Noranda,\textsuperscript{10} produce about 5 percent of North America’s 40 million tonnes of sulfuric acid\textsuperscript{11} each year and they are two of Canada’s biggest base metal miners.\textsuperscript{12} The concern

\textsuperscript{7} 15 U.S.C. § 3571(d).
\textsuperscript{10} Paul Waldie, Lawsuit Names Firms, GLOBE AND MAIL (May 7, 2003), http://www.globemedia.com/story/gam/20030507/RNORA.
\textsuperscript{11} Sulfuric acid is a component in the manufacture of many products, including rubber, plastics, high-octane gasoline, organic products, paints, pigments, processing metals, explosives, paper, detergents, batteries, and a wide variety of specialty chemicals. Kenneth B. Moll, supra note 10. However, the most prominent use of sulfuric acid is in the manufacture of fertilizers. Id.
was that the Canadian firms had colluded with U.S. companies by having the U.S. companies shut down their production of sulfuric acid in exchange for distributing the Canadian firms’ sulfuric acid, seemingly in an effort to maintain prices.\textsuperscript{13}

The DOJ requested the Royal Canadian Mounted Police to search the business premises of the Canadian firms and seize thousands of documents.\textsuperscript{14} After the documents were seized, a legal battle ensued wherein the DOJ attempted to have the documents handed over by the Canadian government.\textsuperscript{15} The Canadian companies were adamant that their documents not be turned over, because they did not want to be dragged into the U.S. judicial system.\textsuperscript{16}

In May 2003, a hearing was held by the Court of Appeal for Ontario\textsuperscript{17} and it was discovered that an unnamed Noranda executive convinced American sulfuric acid producers in the 1980’s to close three manufacturing plants, fix prices, and exchange customer-lists.\textsuperscript{18} In exchange for the American companies’ cooperation, the executive agreed to pay the American companies a commission for selling Noranda sulfuric acid to product manufacturers in the United States.\textsuperscript{19} The Canadian court ordered the documents to be turned over and stated that “based on the edited information, reasonable grounds exist to believe that the \{companies\} have engaged in conduct that offends the Sherman Act.”\textsuperscript{20} However, after further review of the

\textsuperscript{12} See NORFALCO, SULFURIC ACID HANDBOOK 1 (Apr. 2007) (“NorFalco is North America’s largest merchant marketer of sulfuric acid, responsible for the marketing and distribution of over 2.3 million tons of sulfuric acid per year.”) available at http://www.norfalco.com/EN/ProductsServices/Documents/NorFalco_H2SO4TechBrochure.pdf.
\textsuperscript{13} SCOTT, supra note 9.
\textsuperscript{15} Kenneth B. Moll, supra note 10.
\textsuperscript{17} Information about the Court of Appeal for Ontario can be found at http://www.ontariocourts.on.ca/coa/en/.
\textsuperscript{18} Kenneth B. Moll, supra note 10.
\textsuperscript{19} Id.
\textsuperscript{20} Waldie, supra note 11.
documents, the DOJ and the Canadian Competition Bureau decided not to pursue any action against the companies.\(^{21}\)

That same month it was reported in the press that U.S. acid producers and chemical companies, who purchased the Canadian acid to manufacture various products, were conducting their own investigations into illegal price fixing and collusive activities.\(^{22}\) Among those buyers was Ohio Chemical Services, which filed a class action lawsuit in federal court along with other purchasers of sulfuric acid (“Plaintiffs”).\(^{23}\)

**IV. THE DISTRICT COURT’S RULING**

The Plaintiffs claimed that Noranda and Falconbridge, the Canadian manufacturers, DuPont, and the other U.S. manufactures of sulfuric acid (“Defendants”) violated Section 1 of the Sherman Act.\(^{24}\) The Plaintiffs argued that Defendants, horizontal competitors, colluded to close plants and reduce the output of sulfuric acid to balance supply and stabilize prices.\(^{25}\)

Plaintiffs claimed that Defendants’ conduct was a per se violation of Section 1, whereas Defendants argued that the rule of reason applies.\(^{26}\) The original trial judge denied summary judgment for the Defendants, but refused to decide which rule applies.\(^{27}\) That judge then retired and the case was reassigned to Chief Judge Holderman. The Defendants were unsure of what defense to prepare, because of the lack of guidance by the prior judge. They asked the Judge Holderman to decide whether the rule of reason or the per se rule applies. Judge Holderman


\(^{23}\) Plaintiffs’ Brief, *In re Sulfuric Acid*, No. 12-1109 (7th Cir. December 27, 2012).

\(^{24}\) *Id.* at 5–56.

\(^{25}\) *Id.* at 1.

\(^{26}\) *Id.* at 1–5.

\(^{27}\) *In re Sulfuric Acid Antitrust Litigation*, Nos. 12-1109, 12-1224, slip op. at 4–5 (7th Cir. Dec. 27, 2012).
ruled without written opinion that the rule of reason applies. Rather than going to trial under the rule of reason, Plaintiffs agreed to have judgment entered against them and sought appellate review in the Seventh Circuit.

III. THE APPEAL

The appellate court affirmed the district court’s ruling in an important opinion by Judge Posner. The court reviewed the circumstances surrounding the challenged conduct. The Canadian firms encountered a problem with storing their sulfuric acid. While not principally engaged in the production of sulfuric acid, the Canadian firms were required by their government to convert the byproduct of their mining operations—sulfuric dioxide—into sulfuric acid to prevent the sulfuric dioxide from generating acid rain. The Canadian market for selling the sulfuric acid is quite limited and the cost of storing it high. Due to increased Canadian regulations, the Canadian companies were forced to build a larger plant to covert more byproduct into sulfuric acid.

The Canadians sought to dispose the sulfuric acid in the larger U.S. market and contacted potential distributors, including those named as defendants. The existing U.S. sulfuric acid producers produced sulfuric acid at higher costs and sold it to chemical companies for use in manufacturing other goods, such as paper and paint. In exchange for the U.S. companies curtailing their production, the Canadians would sell sulfuric acid cheaply enough to make distribution more profitable than production for U.S. companies, in what were referred to as

28 Id.
29 Id.
31 In re Sulfuric Acid Antitrust Litigation, Nos. 12-1109, 12-1224, slip op. at 5–6 (7th Cir. Dec. 27, 2012).
32 Id. at 7.
33 Id.
34 Id. at 6–7.
“shutdown agreements”. Several U.S. producers were even scared that if they did not agree to distribute the Canadian acid, then the Canadian distribution network eventually would undercut the U.S. producer pricing, driving them out of the market. The Canadian companies also granted their new distributors certain exclusive territories in the U.S.

The issue before the Court of Appeals was whether the shutdown agreements and exclusive territorial grants are the sort of practices that “fall within the scope of the per se rule against price fixing, or fall outside of it . . . [and are] governed by the rule of reason.” The Plaintiffs argued that the per se rule applies, because the agreements reduced total sales of acid in the U.S., raised the market price, and created supracompetitive profits by not allowing the distributors to compete with each other. The court, however, found that this was not the only plausible interpretation of the shutdown agreements and grants.

The court reasoned that the Canadians had both an opportunity for profit and bearing of risks by selling the acid in the U.S. market. The Canadians might profit by directly selling their acid, but were presented with the risk that their profit would be hindered by the U.S. firms producing their own acid. If the U.S. companies continued production, then the supply would greatly exceed demand, and the costs of converting the byproduct and transporting the acid would not be outweighed by the profits from selling the acid. Furthermore, the Canadian firms risked being subject to antidumping lawsuits if they decided to sell at a loss, and the court was not certain the Canadian companies would be able to successfully defend by proving that selling

35 Id. at 8.
36 In re Sulfuric Acid Antitrust Litigation, Nos. 12-1109, 12-1224, slip op. at 7 (7th Cir. Dec. 27, 2012).
37 Id.
38 Id. at 5.
39 Id. at 8.
40 Id.
41 Id.
42 Id.
43 Id. at 9.
at a loss was more profitable than closing down mining operations or building new storage facilities.\(^{44}\) Moreover, insisting that a distributor agree not to sell a competing line of goods is not per se illegal, and the court saw no distinction where the distributor previously manufactured competing goods.\(^{45}\)

The court did call the shutdown agreements price fixing,\(^{46}\) but a kind that is not illegal per se. Relying on *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*\(^{47}\) and *Polk Bros., Inc. v. Forest City Enterprises, Inc.*\(^{48}\) the court found that price fixing between competitors or agreements that restrict competition may not be per se illegal if the challenged practices also promoted “enterprise and productivity.”\(^{49}\) The Plaintiffs argued that *BMI* and *Polk* should be limited to beneficial business endeavors that create a new product, and that no new product had been created here—only the replacement of one’s sulfuric acid for another.\(^{50}\) The court disagreed and stated the shutdown agreements could be said to have created a new product—Canadian smelter acid in the U.S. market.\(^{51}\)

Plaintiffs contended that this case was not novel, but merely a repeat of *United States v. Socony Vacuum Oil Co.*,\(^{52}\) where large oil refiners paid small refiners for their supply of oil with the intention of holding it off the market to raise prices.\(^{53}\) The court distinguished this case based on the aim of the companies. In *Socony-Vacuum* the only objective was to raise prices, whereas the objective of the Defendants was to “facilitate entry into the U.S. market, which would lower

---

\(^{44}\) See id. at 9–10 (citing HARVEY KAYE & CHRISTOPHER A. DUNN, INTERNATIONAL TRADE PRACTICE §§ 15:1, 19:2 (2012)).
\(^{45}\) Id. at 11.
\(^{46}\) Id.
\(^{47}\) 441 U.S. 1, 24 (1979).
\(^{48}\) 776 F.2d 185, 189 (7th Cir. 1985).
\(^{49}\) In re Sulfuric Acid Antitrust Litigation, Nos. 12-1109, 12-1224, slip op. at 11 (7th Cir. Dec. 27, 2012).
\(^{50}\) Id. at 12.
\(^{51}\) Id.
\(^{52}\) 310 U.S. 150 (1940).
\(^{53}\) In re Sulfuric Acid Antitrust Litigation, Nos. 12-1109, 12-1224, slip op. at 14 (7th Cir. Dec. 27, 2012).
prices and prevent the shutdown of Canadian smelting operations, which would have reduced output and raised the price of acid in the United States.”

The court was not persuaded by the language in *Socony-Vacuum* that “any combination which tampers with price structures is engaged in unlawful activity.” Judge Posner noted the age of the 1940 opinion. Since then, certain agreements involving price structures have been found not to be per se illegal, such as resale price maintenance.

Similarly, the court did not find the exclusive territorial grants a per se violation. The court saw the grants as a means of compensating the U.S. companies for changing over their business model from production and distribution of acid, generally, to distribution solely of Canadian acid. While such grants can reduce competition at the distributor level, they also increase competition at the producer level, and may have done so in this case.

V. CONCLUSION

Some may criticize the court for having further chipped away at the per se rule. Whereas *BMI* and *Polk* may have suggested that a finding of a new product bring introduced into the market is required to subject conduct that is otherwise per se illegal to the rule of reason, critics may claim that now alleged violators need only plausibly show that the challenged practice when

---

54 Id.
55 310 U.S. at 221.
56 *In re Sulfuric Acid Antitrust Litigation*, at 14 (citing Leegin Creative Leather Products, Inc. v. PSKS, Inc. 551 U.S. 877, 894 (2007)).
57 Id.
58 Id. The court also addressed the issue of a joint venture created solely for the elimination of competition, but found that the joint venture had a legitimate purpose. The joint venture enabled the Canadians access to DuPont’s distribution network and may have allowed DuPont to sell the Canadian acid in conjunction with its other chemicals, providing a one-stop-shop. *See Robert Brown, Sulfuric Acid Market Faces Turbulence As Noranda DuPont Entity Moves Ahead*, ICIS (July 5, 1999) (quoting Kim Ross, President of Noranda DuPont, “In the past, it was very difficult to respond to a customer who said 'I would like to deal with you directly, to supply my plants all over North America’, because we had multiple channels,” he says. “Now we're able to respond when somebody comes to us and says, 'Can you address my needs in multiple locations? That's what we're set up to do.'”). Kim Ross, the president of the joint venture, described the partnership as unique because the two sources of acid provided “more levers to address customer requirements.” Id.
adopted could reasonably have been believed to promote enterprise and productivity—a
significantly lower bar.\textsuperscript{59}

However, the court has done nothing more than reaffirm principles set forth in \textit{BMI} and
subsequent case law: A cursory examination into the underlying circumstances, such as whether
there is promotion of enterprise and productivity, may reveal whether challenged conduct is of
the classic type of price fixing prohibited by the Sherman Act or if the conduct presents
sufficient procompetitive results, which should be subject to the rule of reason. Moreover, the
novel issues of involuntary production of the acid and potential antidumping exposure presented
a case the like of which had not been subjugated to the per se rule. Per se theory of liability is
reserved for those instances where particular business practice has no redeeming benefit and
where the court is familiar with the consequences of the illegal conduct.\textsuperscript{60}

Nevertheless, conduct that is not per se illegal is does not mean it is lawful.\textsuperscript{61} The
Defendants conduct would have been reviewed under the rule of reason and could have been
found to be violating the Sherman Act. The Plaintiffs opted not to go to trial under the rule of
reason, and Judge Posner criticized that decision. The oral argument suggested that the Plaintiffs
thought far more work would be necessary to prove up their claim under the rule of reason, such
as establishing market share.\textsuperscript{62} While that may be true if the defendant creates a triable issue of
justification for their conduct, the work is “probably less than they think.”\textsuperscript{63} If a plaintiff proves
that defendants agreed to raise prices or restrict output, then he has made a prima facie case that
the defendants’ behavior is unreasonable. Such a prima facie case does not require proof of

\textsuperscript{59} See Demitrack, \textit{supra} note 1.
\textsuperscript{60} Illinois State Bar Association, \textit{In re: Sulfuric Acid Antitrust Litigation} (summarizing the case),
\textsuperscript{61} Demitrack, \textit{supra} note 1.
\textsuperscript{62} \textit{In re} Sulfuric Acid Antitrust Litigation, Nos. 12-1109, 12-1224, slip op. at 3–4 (7th Cir. Dec. 27, 2012).
\textsuperscript{63} \textit{Id.} at 4.
market share. However, if the defendants create a triable issue of justification for their conduct, then the plaintiffs then would have to rebut this justification under the rule of reason. Because the Plaintiffs decided not to pursue recourse under the rule of reason, the case was dismissed.

64 Demitrack, supra note 1.