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Antitrust Developments in the Media and Entertainment Industries

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Antitrust issues continue to play a central role in the media and entertainment businesses, both in industry transactions and through litigation. The high-risk, capital-intensive nature of the media business, rapid changes in distribution technology that reward 'first-movers' and intense consumer interest in popular culture all combine to push antitrust issues to the forefront with government enforcement agencies and with private litigants.

First, in 2007, the US antitrust agencies have scrutinised a number of media and entertainment transactions. The most visible has been the proposed merger between satellite radio operators Sirius and XM, now under review by the Antitrust Division of the Department of Justice (DoJ) and the Federal Communication Commission (FCC). Google's acquisition of DoubleClick is under review by the Federal Trade Commission (FTC) and the European Commission.

Second, private antitrust litigation has followed government approval of certain acquisitions when third parties have been unsuccessful in persuading merger authorities to block transactions or impose remedies to protect their asserted interests. After a third party successfully challenged the European Commission's 2004 approval of the *Sony/BMG* recorded music joint venture, the EC retained jurisdiction over that transaction and renewed the investigation of its possible anticompetitive effects. More than three years ago, the US FTC cleared this joint venture unconditionally (indeed, without a need for a more intensive review in the framework of a second request), as so did every other antitrust authority that had jurisdiction over the joint venture. The renewed EC review highlights certain of the fundamental differences between the US and the EC antitrust regimes, including in particular the role played by third-party complainants and the procedural rights available to third parties in the EC that are not available in the US. At the same time, the private litigation fallout in the US, however, challenging the arrangements by which Comcast/Time Warner acquired Adelphia assets out of bankruptcy, swapped cable systems and dealt with programmers – after the litigants had unsuccessfully raised these concerns during the merger review process – exemplifies the risks of the US merger regime.

Third, Apple's ascension as a dominant firm in companion software (iTunes) and hardware (iPod) businesses and the steps it takes to protect its market positions continue to attract antitrust scrutiny.

Fourth, in 2007, copyright misuse defences grounded in antitrust facts and antitrust counterclaims mirroring misuse defences have continued to complicate copyright infringement actions. As the Napster litigation wound down, new actions by recorded music companies, such as the litigation seeking to enjoin and collect damages from LimeWire, have faced misuse defenses and antitrust counterclaims that change the dynamics of infringement claims.[1]

Finally, all of this has been occurring against a broader backdrop of the US Supreme Court imposing more rigorous scrutiny upon private antitrust actions[2] and unsuccessful litigation efforts by the government challenging on antitrust grounds transactions it has concluded should be blocked.[3]

The rights of third parties in the merger control process

The European Court of First Instance (CFI), in reversing in 2006 the EC's prior approval of the *Sony/BMG* recorded music joint venture, became the first European Court to reverse an EC decision that had unconditionally cleared a transaction.[4] More than two years after closing, Sony and Bertelsmann faced the prospect of having to reapply to the European Commission and comply with massive data requests in their effort to obtain approval of their joint venture. Nearly a year into that process, Sony and Bertelsmann still have not received EC approval (although they continue to operate their joint venture, and an EC decision, predicted to be favourable, is due in the early autumn). Thus, the review has stretched to almost four years, and this predicted approval may not be the end of this saga. The EC's determination could be subject to further judicial review by the CFI, should a third party, such as Impala, file another appeal.[5]

The EC procedure, where a third party appeals a determination made by a merger control authority based upon alleged substantive or procedural errors by the reviewing agency, is not available in the US. No appellate rights are available to third-party complainants in the US merger review process. Even in the context of transactions which have been resolved through a consent order, the only vehicle available to third parties is the submission of written comments to the reviewing agency during the statutory comment period. But there is no appellate right to challenge the terms of a transaction that has been cleared by an enforcement agency without conditions.

The only right left to third parties is to commence a private litigation, a process fraught with procedural and substantive obstacles. (The various lawsuits filed against Comcast and Time Warner in connection with their purchase of the Adelphia assets, discussed later, provide a recent example of such private actions.)

Impala v Commission

The chronology of the EC review in *Sony/BMG* highlights the differences between the European and American approaches. In January 2004, Sony and Bertelsmann notified the EC of their proposed joint venture. The EC "market tested" the positions taken by Sony and Bertelsmann in their merger notification, a standard EC procedure that takes the form of questionnaires sent to the merging parties' customers, suppliers and, significantly, to their competitors as well. Impala, an international trade association representing independent music producers, received that questionnaire and raised its concerns with the EC.

In the US, the antitrust agencies routinely ask the merging parties to provide contact information for their principal suppliers and customers so that they can elicit their views as to the competitive effects of a proposed transaction. The views of competitors, however, are not routinely solicited and in any event are accorded far less weight by the US agencies than by the EC.

In February 2004, the EC concluded that the Sony/BMG joint venture raised "serious doubts" as to its compatibility with EC merger law and opened formal ("Phase II") proceedings to continue its investigation. In May 2004, the EC issued a Statement of Objections, which provisionally concluded that the transaction would

strengthen a collective dominant position in recorded music and in the wholesale markets for licensing online music. From the time of the initial notification through completion of the Phase II proceedings, the EC consulted with third parties while it also conferred with Sony and Bertelsmann.

Sony and Bertelsmann filed a detailed response to the Statement of Objections, and expressed their position through a two-day oral hearing in June 2004. Their response persuaded the Commission to clear the joint venture in July 2004, unconditionally.[6] In the US, the merger control process would have ended at this point. Impala, however, appealed the EC's decision to the CFI, which reversed the EC's decision two years later in July 2006.

The American Channel v Time Warner

There is no standing to appeal FTC or DoJ approval of a transaction. An aggrieved third party must commence a separate private litigation. That action, however, cannot contest the validity of the government's determination as such or the process by which the FTC or DoJ arrived at its decision. Rather, standing to bring a private action requires pleading and proving that a plaintiff suffered antitrust injury as a result of the transaction.[7] The lawsuits brought against Comcast and Time Warner in the context of their acquisition of Adelphia highlight the differences between the EC and US review process.

In April 2005, Comcast and Time Warner, the two largest cable operators, jointly bid to acquire the assets of Adelphia, which had been the fifth largest cable operator and agreed to swap certain cable systems to consolidate their holdings in certain metropolitan areas. The America Channel, a sport and lifestyle programming network, opposed these acquisitions. It argued that neither Comcast nor Time Warner would launch or carry its channels on its cable offerings. The America Channel alleged that Comcast and Time Warner would each discriminate in favour of its own affiliated networks in which they held an equity interest, and would thereby foreclose the America Channel from distribution to nearly half of the cable homes in the US. In its comments to the FCC and to the DoJ, the America Channel argued that, as an independent, non-affiliated programmer, it already faced unlawful discrimination by cable operators. It claimed that large cable operators, like Comcast and Time Warner, favoured vertically integrated networks, and subjected independent programmers to a "gauntlet of requirements" that did not exist for affiliated programmers.

The FCC and the DoJ rejected these arguments and cleared the acquisitions. The America Channel then commenced a private action in federal court in Minnesota to enjoin the transaction, alleging multiple antitrust claims against Comcast and Time Warner.[8] In January 2007, the court dismissed the injunction claim as moot (because the acquisitions had already been completed), held that the America Channel did not have standing to sue on behalf of cable subscribers and dismissed other antitrust claims because they had not been adequately pleaded.

The America Channel then filed an amended complaint alleging, inter alia, that Comcast and Time Warner engaged in a concerted refusal to deal with it, and that the partition and swap of the Aldephia assets was an illegal market partitioning agreement. The America Channel also raised the same discrimination arguments it had raised before the FCC. In support, it alleged that only two of 114 independent networks (networks in which no merger cable operator had an equity interest) that sought carriage on Comcast's or Time Warner's cable systems network from 2003 through May 2005 had been granted carriage, and that Time Warner and Comcast had foreclosed competition by denying the other 112 requests.

The court again dismissed the complaint on the basis that it had failed adequately to allege a conspiracy, particularly in light of the pleading standards set forth in May 2007 by the Supreme Court in *Bell Atlantic Corp. v. Twombly*.[9] The court dismissed the alleged horizontal partitioning claims as not leading to antitrust injury because the America Channel had already been denied carriage by Comcast and Time Warner prior to the Adelphia acquisition and swaps. The court also dismissed the America Channel's monopolisation claims because the America Channel had not identified a relevant geographic market within the multichannel video programming distributor market in the US but instead identified inconsistent markets. The court also noted that the America Channel had failed to identify any causal connection between the attempted monopolisation and the alleged injury.

The *Comcast/Adelphia* litigation

Interestingly, additional class actions filed against Comcast in Pennsylvania arising out of the Adelphia purchase have led to a different outcome at the pleading stage.[10] These claims were filed on behalf of cable customers in Philadelphia, Chicago and Boston. The allegations are that Comcast has acquired monopoly power in these markets through asset swaps with actual or potential competitors and that cable companies have agreed not to overbuild in each other's excessive franchise areas. Comcast argued that the plaintiffs lacked standing. Comcast argued that there was no cognizable harm to competition or the plaintiffs because the swaps of cable assets did not result in a change in the basic market structure in these three regions but only resulted in the substitution of one cable operator, with an exclusive cable franchise in a particular geographic region, for another competitor. The court rejected Comcast's argument and held that the parties to the swaps were actual or at least potential competitors in the relevant geographic regions. Importantly, the court noted that the fact that the horizontal allocation was pursuant to an asset swap did not shield the transaction from being categorised as per se unlawful for pleading purposes. Nor did the government's approval of the merger shield it from being challenged as a per se prohibition.

In contrast to the dismissal by the Minnesota court, the Pennsylvania court did not dismiss the claims relating to the acquisitions of cable systems that did not involve market allocation, claims that all parties agreed should be analyzed under the "rule of reason", even though the plaintiffs failed to define explicitly the relevant product markets. The court liberally construed the complaint in finding that the plaintiffs had sufficiently alleged the relevant geographic markets.

The Pennsylvania court initially denied Comcast's motion to dismiss prior to the Supreme Court's ruling in *Twombly*. Comcast then asked the court to reconsider its decision in light of the Supreme Court's analysis.[11] The court, however, reading *Twombly* narrowly, noted that it, "by its own terms... did not impose a heightened pleading standard"[12] and declined to change its decision.

The *Google/DoubleClick* and *Sirius/XM* transactions

These two transactions, one investigated by DoJ and the FCC (*Sirius/XM*), the other by the FTC (*Google/DoubleClick*), generated significant and organised third-party opposition. Both transactions received second requests and are still under review by the government.

Sirius and XM face opposition from public interest groups and groups representing the interests of terrestrial radio. Opponents of the transaction have argued that the combined companies would dominate the satellite radio "market". As in the 2007 *Whole Foods/Wild Oats* transaction, the antitrust argument against Sirius/XM turns on the proper definition, for antitrust purposes, of the market in which the transaction is taking place. Whole Foods and Wild Oats argued successfully that they compete in a broader market

that includes a number of large supermarket chains, while the FTC unsuccessfully opposed the merger, arguing that the competitive effects of the combination should be reviewed within a narrower "premium and natural organic food" market.[13]

Opponents of the *Sirius/XM* transaction argue that the market in which the parties compete is the satellite radio market. Sirius and XM argue that they face competition from terrestrial, high-definition and internet-based radio stations, as well as digital music players, and that this competition would constrain the combined company's ability to increase prices or decrease output.[14] Sirius and XM have also argued that the merger will provide consumers with more programming choices,[15] and have highlighted the efficiencies that the transaction would generate.

While the government is still reviewing the *Sirius/XM* merger, Wall Street seems to believe that the merger will receive approval. Interestingly, when a federal court ruled in favor of Whole Foods, shares of XM jumped, and when an appellate court refused to delay that decision, XM shares rose again.

Google faces opposition from large, organised competitors, such as Microsoft and AT&T, who oppose Google's acquisition of DoubleClick on antitrust grounds. Public interest groups also oppose the transaction on privacy rights grounds. Google and DoubleClick are not horizontal competitors; they are present in different segments of the online search advertising business. One antitrust issue that has been reported is the risk of anti-competitive effects in the respective markets where Google and DoubleClick are potential competitors: were it not for this transaction Google might innovate and enter DoubleClick's segment, or its presence as a potential entrant could have a restraining effect on DoubleClick's conduct. Whether such a theory is viable under these facts remains to be seen.

The *Apple iPod/iTunes* antitrust litigation

Apple's iTunes online music store is now by far the world's largest online music store, accounting for approximately 80 per cent of all lawful online music sales in the US. Indeed, it is the third-largest overall music retailer in the US, trailing Wal Mart and Best Buy.[16]

At the same time, Apple's iPod sales represent approximately 90 per cent of the digital music player sales in the US. This parallel success in both the software and hardware segments is at least to some degree the result of the lack of interoperability between the iPod and other online music stores. Consumers who have purchased online music from iTunes must have an iPod if they want to play that music on a digital music player, and consumers who purchase music from online stores other than iTunes cannot upload this music on an iPod.

This lack of interoperability has been challenged by European antitrust and consumer protection agencies, primarily in France and Scandinavia, and is the subject of putative class action litigation in the US. At the pleading stage, two California courts have denied Apple's motions to dismiss claims of an illegal tie between iTunes and iPods as well as a monopolization claim.[17] Plaintiffs alleged that Apple possesses, through its iTunes/iPod franchise, monopoly power in the markets for the sale of digital music online and portable hard drive digital music players. Apple's primary factual defence is that music downloaded from iTunes can be played on numerous computers that are not manufactured by Apple, and that the iPod is capable of playing music from CDs as well as music downloaded from iTunes. Further, Apple argues that is proprietary digital rights management software is necessary, and appropriate, to protect copyrighted content.

If proven, certain of plaintiffs' monopolisation claims may be problematic for Apple. Plaintiffs alleged that Apple took steps to foreclose RealNetworks, which competes with iTunes in the sale of online music through the RealNetworks music store, from providing music that could be played on the iPod. Allegedly, RealNetworks had successfully engineered a software program allowing the music sold on its RealNetwork music store to be played on the iPod. In 2004, RealNetworks publicly stated that songs sold through its online RealNetworks music store would now be playable on the iPod, thereby allowing iPod owners to purchase online music from an online store that competes with iTunes. Apple then allegedly modified its software to prevent music downloads from RealNetworks to iPods. Discovery in these litigations is ongoing. Apple's success and commanding market position will continue to attract antitrust attention.

The antitrust "defence" to copyright infringement

The US antitrust laws recognize that competitors may appropriately need to collaborate through joint ventures to achieve efficiencies that each could not attain on its own. Further, the Noerr-Pennington doctrine also allows for coordinated efforts by competitors, often through trade associations, to influence the legislative, administrative and adjudicatory processes. The government, however, commonly scrutinises joint ventures and trade association activities to ensure, among other things, that they do not facilitate 'spillover' effects that result in anti-competitive exchanges of information or concerted refusals to deal. Joint venture partners and trade associations commonly set appropriate guidelines and firewalls necessary to ensure that the joint venture and trade association efforts would withstand scrutiny in the event of government investigations or private actions.

This concern has been heightened in the music industry (and among other content providers) in the context of the industry's strategy of attempting to shut down illegal peer-to-peer networks such as Napster, Kazaa, Grokster, Baidu and, more recently, LimeWire. In these cases, the copyright owners, either individually or through trade associations such as the Recorded Industry Association of America or the International Federation of the Phonographic Industry, sued to enjoin copyright violations. In response, it has become routine for the alleged infringer to assert a copyright misuse affirmative defence based on antitrust theories and often an antitrust counterclaim mirroring the misuse allegations. For example, Hummer Winblad, a co-defendant with Napster in the *In re Napster Copyright Litigation* that had provided financing to the file sharing service, alleged that "[the music companies] and their co-conspirators … contracted, combined, and conspired with the intent to unreasonably restrain trade in the market for the online distribution of recorded music, and to unreasonably restrain, thwart and eliminate competition in the related and interdependent market for the financing of online recorded music distribution ventures."[18] Similar claims were asserted in the Kazaa and Grokster litigations, and are now being asserted by LimeWire. These claims slow down and complicate the copyright infringement litigation, give some added leverage to the infringer, and place on the copyright owners the significant burden of full blown antitrust conspiracy discovery, not only of joint ventures and trade association activities but all communications among competitors that infringers may attempt to 'spin' into a conspiracy theory.

* * *

The high profile of the media industry and the high-risks of the business itself assure that it will continue to be a target of antitrust scrutiny by suppliers, customers and competitors as well as by the government.

Notes

1 See *Arista Records LLC et al v Lime Wire LLC et al* (SDNY).

2 See *Bell Atlantic Corp v Twombly*, 127 S Ct 1955 (21 May 2007).

3 See *Federal Trade Commission v Whole Foods Market Inc*, 2007 WL 2377000 (DDC, 16 August 2007)

4 See *Independent Music Publishers and Labels Association (Impala) v European Commission*, Case T-464/04 (European Court of First Instance, 13 July 2006).

5 Under EC merger control law, third parties considered to have a "sufficient interest" in the Commission's procedure include customers, suppliers, competitors, members of the administration or management organs of the merging parties or recognized workers' representatives of the parties (See DG Competition Best Practices on the conduct of EC merger control proceedings, paragraph 34).

6 See *Sony/BMG*, case no. Comp/M3333, Commission Decision C(2004) 2815 (July 19, 2004).

7 To obtain an injunction or a temporary restraining order to stop the consummation of a proposed merger, a third party must demonstrate a likelihood of success on the merits in proving a violation and threatened or irreparable harm. See *American Telnet, Inc v GTE Corp*, 1999 US Dist LEXIS 5781, at 9 (ND Tex 1999) ("Section 16 of the Clayton Act requires a showing of irreparable harm to obtain a preliminary injunction.").

8 See *America Channel, LLC v Time Warner Cable, Inc*, No 06-2175, 2007 WL 142173, 2007 WL 1892227 (D Minn).

9 127 S Ct 1955 (21 May 2007).

10 See *Glaberson v Comcast Corp*, No. 03-6604, 2006 WL 3762028 (ED Pa, 19 Dec 2006);

11 See *Behrend v Comcast Corp*, Nos. 03-6604, 07-218, 07-219, 2007 WL 2221415 (ED Pa, 31 July 2007).

12 Idem, *5.

13 See *Federal Trade Commission v Whole Foods Market Inc*, 2007 WL 2377000 (DDC, 16 August 2007)

14 Reply filed with FCC 8/27/2007.

15 Reply filed with FCC 8/27/2007.

16 See 'Apple's iTunes Was 3rd Biggest Music Retailer by Units Sold in 1Q' (AP, 24 June 2007) available at http://biz.yahoo.com/ap/070624/music_sales.html?.v=1.

17 See *Slattery v Apple Computer, Inc*, WL 2204981 (ND Cal) and *Tucker v Apple Computer, Inc*, 493 F Supp 2d 1090 (ND Cal). The cases were consolidated on 19 March 2007.

18 See *In re Napster, Inc Copyright Litigation, UMG Recordings Inc, et al v Hummer Winblad Ventures Partners, et al*, 479 F3d 1078 9th Cir (Cal), 14 March 2007.

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