ANTITRUST COMPLIANCE GUIDE

FOR THE

MANAGED FUNDS ASSOCIATION

"People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices."

Adam Smith, The Wealth of Nations, Book I, Chapter X, p. 82

I. Introduction

This Guide is designed to assist the members of the Managed Funds Association ("MFA") in understanding and complying with our nation's antitrust laws. Although the Guide sets forth general antitrust principles and rules, it is not intended to make you an expert on antitrust law; rather, its purpose is to enable you to recognize and avoid potential antitrust concerns and to seek assistance from legal counsel when appropriate.

II. The Antitrust Enforcement System

A. The Antitrust Laws and Enforcement Authorities

The purpose of the antitrust laws is to preserve and promote free and fair competition in the marketplace. In this way, the most able competitors will prosper and consumers will have the widest range of choices at the lowest possible costs.

The principal federal agencies charged with enforcement of the antitrust laws are the Antitrust Division of the Department of Justice and the Federal Trade Commission. They can enforce the antitrust laws through civil proceedings, or, in certain cases, the Antitrust Division may bring a criminal enforcement action against a person or company that violates the antitrust laws. In addition to the federal enforcement agencies, private parties may bring suit for injuries resulting from violations of federal antitrust laws. Moreover, State Attorneys General are empowered to bring suit on behalf of their citizens for violations of certain federal antitrust laws.

It is MFA's policy to comply fully with federal and state antitrust laws and to cooperate with government investigators seeking information in connection with their investigatory responsibilities. At the same time, each member of MFA is entitled to representation by its own counsel in any such investigation. If a government investigator contacts a member, serves a subpoena or otherwise makes a request for information from a member in connection with an MFA matter, the member should immediately (and before responding) notify its own legal counsel by telephone. The member should also immediately notify Mark Epley, Executive Vice President and General Counsel of MFA.

B. Consequences of Antitrust Violations

In addition to the fact that antitrust compliance is good public policy, there are several other compelling reasons for strictly observing the requirements of the antitrust laws. Failure to heed the rules described in this Guide may result in:

(1) Criminal Prosecution. Some antitrust violations are felonies, for which a corporation can be fined the greatest of three alternatives:

- $100,000,000,
- twice the gain derived from the crime, or
- twice the loss caused to the victims of the crime.

An individual (including an employee, officer or director) who authorizes or participates in a criminal antitrust violation may be imprisoned for up to ten years for each offense and may be fined the greater of

- $1,000,000,
- twice the gain received, or

- twice the loss caused to victims.

(2) Treble Damage Actions. Public and private parties may bring civil actions against defendants, alleging that the defendants' actions constituted antitrust violations that harmed the plaintiffs. A party injured by an antitrust violation is entitled to recover three times the amount of its damages, plus its court costs and the fees of its lawyers. An antitrust defendant's potential liability may thus reach astronomical proportions, particularly in class actions brought against it on behalf of a group of allegedly injured parties.

(3) Injunctions. If a court finds that an association, company, or individual violated the antitrust laws, that defendant will be ordered to stop the offending conduct. In some cases, the defendant may also have to take corrective action to restore competition in the marketplace, such as reinstatement of terminated customers.

(4) Costly Litigation. The costs of antitrust litigation to a defendant can be staggering, both in dollars and in harm to the reputation of a company, a trade group, or an individual. Antitrust litigation is notoriously expensive and often requires that executives and managers divert their attention from productive pursuits to responding to subpoenas and depositions and otherwise participating in the defense of a case.

In some instances, the Federal Trade Commission or the Department of Justice may enter into a consent agreement with the party that allegedly was violating the antitrust laws. These agreements can impose formidable conditions on the settling party. For example, in *in re National Association of Music Merchants, Inc.*, 74 Fed. Reg. 56, 12867 (FTC 2009), the FTC alleged that a trade group facilitated price fixing and retail price maintenance among its members. The trade group signed a consent agreement in which it agreed to institute comprehensive antitrust procedures. The order expires in twenty years.

C. Key Antitrust Principles

In considering whether activities may violate the antitrust laws, it is useful to keep two important concepts in mind:

(1) Agreements. Although the antitrust laws generally require a finding of an agreement, direct proof of an agreement is not needed in order to prove a violation. Any understanding – whether written or oral, express or implied – may constitute an agreement. Courts may infer an agreement from circumstantial evidence and from conduct many businesspeople may regard as completely innocent. As a consequence, extreme care should be taken in all contacts with competitors.

(2) "*Per Se*" Violations. As a general principle, only those joint or concerted activities that unreasonably restrain trade are violations of the antitrust laws. However, certain kinds of conduct are considered so inherently anticompetitive that they are said to be per se illegal. This means that these activities are automatically unlawful – no defense or justification may be offered. It is especially important to be able to recognize and avoid these per se violations, such as price fixing, as discussed below. The Department of Justice may bring criminal enforcement actions against persons who engage in such activities.

D. Trade Associations and Relationships with Competitors

(1) Trade Associations and Industry Groups Generally. Although trade associations and industry groups provide many important and valuable services, they

may also create antitrust dangers for their member companies. Because these groups provide an opportunity for competitors to get together, often in a relaxed and informal atmosphere, they may serve to foster unlawful understandings or agreements regarding price, production levels, customers, suppliers and the like.

Because the government or private plaintiffs may prove such agreements with circumstantial evidence, it is particularly important that all MFA members exercise great caution in the informal conversations that occur naturally outside of formal meetings.

You should also bear in mind that industry group activities, by their nature, are the result of concerted action by competitors. The antitrust laws have no special provisions that permit any particular activities just because they are conducted under the auspices of a trade association or industry group. Should a court or antitrust agency find that the activities of the group restrain trade, the member companies and individuals may also be subjected to liability, along with the group itself. As a consequence, MFA plans and initiatives will be reviewed in advance by counsel.

(2) Price-Fixing Agreements. Agreements among competitors to fix the prices to be charged for their products or services are automatically unlawful, and may subject the participants to both criminal and civil sanctions. This is true regardless of whether the prices fixed are reasonable or whether minimum or maximum prices are established. Similarly, it makes no difference that the agreement does not specify prices precisely – mere agreement among competitors to stabilize prices is unlawful. Other examples of potentially unlawful price fixing among competitors include:

- An agreement to limit production or sales;
- An agreement to adopt a new formula for computing prices;
- An understanding on price ceilings, price ranges, list prices or discounts;
- An agreement on elements of price or conditions of sale, such as credit terms or delivery terms;
- An understanding to verify prices or exchange current or future price information.

(3) Customer and Market Allocation. In most instances, it is automatically unlawful for competitors to agree that they will not compete for business. Examples of such prohibited arrangements between competitors include:

- An agreement dividing specific customers;
- An understanding that they will not sell into each other's geographic territory;
- An agreement dividing product lines.

(4) Group Boycotts and Collective Refusals to Deal. An agreement among competitors not to buy from or sell to specified third parties may constitute an automatic violation of the antitrust laws. Examples of prohibited conduct include:

- An understanding not to sell to price discounters;
- A joint decision by competing sellers of a product not to purchase from a supplier unless that supplier ceases dealing with a competing seller;

- An agreement among competitors not to sell to a customer unless the customer agrees not to deal with a specified supplier.

Particular care should be exercised when participating in industry self-regulation programs, for concerted action taken against non-members or non-complying members can result in an illegal group boycott.

(5) Information Exchanges. The exchange of sensitive business information among competitors can create serious antitrust concerns. In particular, trading data that directly or indirectly conveys present or future price, cost or production information may support allegations of price fixing. Consequently, all exchanges of sensitive business information with actual or potential competitors either directly or through trade groups, are to be avoided unless approved in advance by counsel.

(6) Group Purchasing. The procompetitive potential of group buying organizations has been frequently recognized by the antitrust agencies. These activities may reduce costs by creating more efficient purchasing and permitting purchasers, particularly smaller ones, to buy at prices they could not obtain on their own. Accordingly, these arrangements have generally received favorable treatment under the antitrust laws. In some instances, however, anticompetitive effects may result. Parties should exercise caution whenever the members of the buying group account for a large portion (over 35%) of the total sales of a product or service, or the product purchased accounts for a large proportion (more than 20%) of the total cost of the products or services being produced and sold by the members.

E. Trade Associations and Government Petitions

MFA serves a very important role by acting as liaison between industry members and the Executive Branch, Congress, and the federal regulatory agencies, as well as state legislatures and state regulatory agencies. In performing this function, MFA members join together, under the auspices of the association, to discuss issues of concern to the industry and the government sector and to prepare, adopt, and present positions for action by government agencies. The antitrust laws grant immunity to competitors acting jointly to seek to influence the government, even if the effect of their lobbying is the enactment of a law that harms other businesses. The "Noerr-Pennington doctrine" is an antitrust principle established by the Supreme Court in a pair of cases, which held that under the First Amendment it cannot be a violation of the federal antitrust laws for competitors to lobby the government to change the law in a way that would reduce competition. To ensure that this immunity applies, discussions about proposed MFA action towards the government should occur only within the context of MFA meetings. Furthermore, should an MFA committee or group identify practices that it believes should be addressed by the government, and should those practices raise antitrust issues, MFA's General Counsel should be consulted.

III. Responsibility of Members of the MFA

Adam Smith's famously stated that "people of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices." The FTC recently said that:

The Federal Trade Commission does not take nearly so jaundiced a view toward trade association activities. The Commission is aware that trade associations can serve numerous valuable and pro-competitive functions, such as expanding the market in which its members sell; educating association members, the public, and government officials; conducting market research; establishing inter-operability standards; and otherwise helping firms to function more efficiently.

At the same time, it is imperative that trade association meetings not serve as a forum for rivals to disseminate or exchange competitively-sensitive information, particularly where such information is highly detailed, disaggregated, and forward-looking. The risk is two-fold. First, a discussion of prices, output, or strategy may mutate into a conspiracy to restrict competition. Second, and even in the absence of an explicit agreement on future conduct, an information exchange may facilitate coordination among rivals that harms competition. In light of the long recognized risk of antitrust liability, a well-counseled trade association will ensure that its activities are appropriately monitored and supervised.

In re National Association of Music Merchants, Inc, supra., *Analysis of Consent Order to Aid Public Comment*, at 2.

As independent businesses, members of MFA must assume individual responsibility for compliance with the antitrust laws. This Antitrust Compliance Guide is intended to assist MFA members in meeting their obligations in this area. Each member should study it carefully. MFA expects its members to adhere to these guidelines in the context of MFA activities.