June 28, 2007

U.S. Supreme Court Rules Investment Banks' IPO Activities Immune from Antitrust Scrutiny

On June 18, 2007, the United States Supreme Court significantly reduced the potential of antitrust liability to investment banks in the securities industry in *Credit Suisse LLC v. Billing*, 127 S.Ct. 2383. In this case, the Court held that certain activities of investment banks related to the initial public offering (IPO) syndication and marketing process and overseen by federal securities regulators were immune from antitrust laws. The Court framed the issue as whether there was a "clear repugnancy" between the securities laws at issue and antitrust laws. In answering in the affirmative, the Court found that the securities laws were "clearly incompatible" with antitrust laws, in part because of the substantial risk of injury to the securities markets should the fine distinctions between permissible and impermissible conduct be left to courts and juries. Instead, the Court found that the Securities and Exchange Commission (SEC) is the proper authority to evaluate the conduct of underwriters because courts and juries are "likely to make unusually serious mistakes in this respect."

Case Background

The Supreme Court first addressed the intersection of securities and antitrust law in a trilogy of cases decided in the 1960s and 1970s: *Silver v. New York Stock Exchange,* 373 U.S. 341 (1963), *Gordon v. New York Stock Exchange, Inc*., 422 U.S. 659 (1975), and *United States v. NASD*, 422 U.S. 694 (1975). In *Silver*, the Court ruled that plaintiffs' antitrust claims regarding group boycotts were not precluded, because the SEC lacked the authority to review the challenged transactions. The Court, however, acknowledged the possibility of a different result in cases where the SEC shared the authority to review the challenged acts. That possibility was squarely presented in *Gordon* and *NASD*. In *Gordon* the Court found that implied immunity was proper because the SEC had expansive regulatory authority over the practices at issue and had actively exercised this authority. The Court reached the same conclusion in *NASD*, despite the lack of SEC regulations dealing with the specific issue at hand, on the grounds that the SEC's pervasive regulatory regime implied the SEC's acquiescence in the conduct involved.

In the present case, the plaintiffs in *Credit Suisse* were investors who lost money after the burst of the dot-com bubble of the late 1990s and 2000. The class plaintiffs challenged the practices of investment banks, including Credit Suisse, Goldman Sachs, Lehman Brothers, Merrill Lynch, Morgan Stanley, Robertson Stephens and J.P. Morgan, surrounding the initial public offering process. Plaintiffs alleged that the underwriting banks had abused the practice of combining underwriting syndicates by agreeing amongst themselves to impose conditions that were harmful to investors. Specifically, the plaintiffs claimed that the defendants had violated

This advisory is published by Alston & Bird LLP to provide a summary of significant developments to our clients and friends. It is intended to be informational and does not constitute legal advice regarding any specific situation. This material may also be considered attorney advertising under court rules of certain jurisdictions.

Section 1 of the Sherman Act by imposing (1) "laddering" agreements (allowing investors to participate in the IPO in exchange for agreeing to purchase the issue at escalating prices in the aftermarket); (2) "tying" arrangements (allowing investors to participate in the IPO in exchange for purchasing other less attractive securities); and (3) excessive underwriting commissions. A separate suit, which was consolidated with the present one, alleged violations of Section 2(c) of the Robinson-Patman Act. The Robinson-Patman allegations involved allegations similar to those detailed above, as well as claims that the underwriter defendants favored long-term investors over "flippers" when allocating IPO shares, in violation of the commercial bribery prohibition of Section 2(c);

The United States District Court for the Southern District of New York dismissed the complaint in 2003, holding that the underwriters' alleged conduct was immune from antitrust scrutiny based on the "potential conflict" reasoning of *Gordon*. The Second Circuit Court of Appeals also looked to the "potential conflict" reasoning of *Gordon* and the "pervasive regulatory regime" reasoning of *NASD*, but reversed the district court ruling and reinstated the complaint in 2005. In so doing, the Second Circuit placed paramount importance on the lack of legislative history demonstrating Congress' intent to immunize the arrangements at issue.

The Supreme Court's Ruling

On June 18, 2007, the Court reversed the Second Circuit in a 7-1 decision. (Justice Kennedy did not participate in consideration of the case and Justice Thomas dissented.) Writing for the Court, Justice Breyer held that the underwriters' challenged conduct was immune from antitrust laws because the securities laws in this area were "clearly incompatible." The Court explained that permitting plaintiffs to bring antitrust actions such as the present one "would threaten serious harm to the efficient functioning of the securities markets." Because of the complex distinctions between activity that the SEC permits or encourages from activity that it forbids, the Court feared that courts and juries would be "likely to make unusually serious mistakes," forcing underwriters to avoid not only joint conduct that the securities laws forbid, but also conduct that the securities laws encourage. Moreover, the Court found that the "enforcement-related need for an antitrust lawsuit [was] unusually small," based upon the following facts: the SEC actively enforces its rules and regulations prohibiting the conduct at issue, investors can seek redress under the securities laws, and the SEC is required to take competitive considerations into account when creating securities policy.

Based on its concerns, the Court also rejected the position offered by the solicitor general (SG). The SG argued that the Court should remand the case to the district court to determine "whether respondents' allegations of prohibited conduct can, as a practical matter, be separated from conduct that is permitted by the regulatory scheme." Despite the SG's concern that the Court's approach would "totally preclude application of the antitrust law to underwriting syndicate behavior, even were underwriters, say, overtly to divide markets," the Court found that the risks associated with courts drawing fine lines between what is permissible and impermissible in the securities field outweighed the threat of broad antitrust immunity.

The Supreme Court's decision also implicitly rejected the lower courts' interpretations of *Gordon* and *NASD*. Whereas both the district court and the Second Circuit viewed these cases as stating two alternative possibilities for antitrust immunity, the Court explained that, together, these cases exemplify four factors that courts should consider in determining whether certain laws

are repugnant to antitrust laws. The Court held that three factors should be treated as critical: (1) the existence of regulatory authority under the securities law to supervise the activities in question; (2) evidence that the responsible regulatory entities exercise that authority; and (3) a resulting risk that the securities and antitrust laws, if both applicable, would produce conflicting guidance, requirements, duties, privileges, or standards of conduct. The Court also held that courts should consider a fourth factor: (4) whether the possible conflict affects practices that lie squarely within an area of financial market activity that securities law seeks to regulate. The Court held that all four factors were present in the *Credit Suisse* case, leading to immunity from antitrust liability.

Justice Stevens concurred with the majority's judgment. According to Stevens, the alleged conduct of the defendants did not violate antitrust laws. "To suggest that an underwriting syndicate can restrain trade . . . by manipulating the terms of IPOs is frivolous." Justice Thomas filed a dissenting opinion on the grounds that the securities laws "contain broad savings clauses that preserve rights and remedies existing outside of the securities laws."

Conclusion and Implications

Credit Suisse will significantly reduce the legal risks to investment banks since many antitrust suits involving regulated securities activities will be precluded. Additionally, *Credit Suisse* could significantly broaden the field of antitrust preclusion in other heavily regulated industries. The Court, citing *Verizon Communications, Inc. v. Trinko*, 540 U.S. 398 (2004), another recent antitrust case involving telecommunications, explicitly acknowledged that the need for antitrust enforcement is lessened in heavily regulated industries. While it remains to be seen whether the Court's four-factor test will be applied outside of the securities context, these four factors could pave the way to reduced antitrust liability in a number of industries. Moreover, as noted critically by Justice Stevens in his concurring opinion, this is the second case in less than a month in which the Court's decision to lessen or restrict antitrust plaintiffs from pursuing antitrust claims was explicitly based on concern over the potential burdens and costs to antitrust defendants in defending such claims.[1] *Credit Suisse*, therefore, is consistent with the trend in recent years for the Supreme Court to narrow the scope of antitrust liability. Regardless of its ultimate significance, however, at the very least *Credit Suisse* has drastically curtailed investors' ability, "to dress what is essentially a securities complaint in antitrust clothing."

1 The other case referred to is *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, where the Court articulated a heightened pleading standard for antitrust suits. For an advisory of this decision, *see* Alston & Bird Antitrust/Litigation Advisory: U.S. Supreme Court Uses Antitrust Case to Ease Standard for Dismissing Baseless Civil Claims.

If you have any questions or would like additional information, please contact your Alston & Bird attorney or any one of the following.

Members of Alston & Bird's Antitrust Group

Randall L. Allen
404.881.7196
randall.allen@alston.com

William Barron
212.210.9500
william.barron@alston.com

Debra D. Bernstein
404.881.4476
debra.bernstein@alston.com

Adam J. Biegel
404.881.4692
adam.biegel@alston.com

Teresa T. Bonder
404.881.7369
teresa.bonder@alston.com

Kristine McAlister Brown
404.881.7584
kristy.brown@alston.com

Mark Calloway
704.444.1089
mark.calloway@alston.com

Naeemah Clark
212.210.1266
naeemah.clark@alston.com

Rebecca B. Crawford
404.881.4824
rebecca.crawford@alston.com

Stephanie B. Driggers
404.881.7163
stephanie.driggers@alston.com

Rodney J. Ganske
404.881.4996
rod.ganske@alston.com

Kevin E. Grady
404.881.7164
kevin.grady@alston.com

H. Stephen Harris, Jr.
404.881.7197
steve.harris@alston.com

Sean C. Hyatt
404.881.4968
sean.hyatt@alston.com

William H. Jordan
404.881.7850
bill.jordan@alston.com

Alan Kanzer
212.210.9480
alan.kanzer@alston.com

Michael P. Kenny
404.881.7179
mike.kenny@alston.com

Peter Kontio
404.881.7172
peter.kontio@alston.com

Gregory B. Mauldin
404.881.4823
greg.mauldin@alston.com

Mark A. McCarty
404.881.7861
mark.mccarty@alston.com

Heather Munday
404.881.7932
heather.munday@alston.com

Matthew D. Richardson
404.881.4478
matt.richardson@alston.com

Suzanne Smith
404.881.7959
suzanne.smith@alston.com

Thomas Walker
704.444.1055
thomas.walker@alston.com

Kenneth G. Weigel
202.756.3431
ken.weigel@alston.com

Valarie C. Williams
404.881.7631
valarie.williams@alston.com

If you would like to receive future Antitrust Advisories electronically, please forward your contact information including e-mail address to ***antitrust.advisory@alston.com****. Be sure to put "****subscribe****" in the subject line.*

ALSTON+BIRD LLP

www.alston.com

ATLANTA
One Atlantic Center
1201 West Peachtree Street
Atlanta, GA 30309-3424
404.881.7000

CHARLOTTE
Bank of America Plaza
101 South Tryon Street
Suite 4000
Charlotte, NC 28280-4000
704.444.1000

NEW YORK
90 Park Avenue
New York, NY 10016-1387
212.210.9400

RESEARCH TRIANGLE
3201 Beechleaf Court
Suite 600
Raleigh, NC 27604-1062
919.862.2200

WASHINGTON, DC
The Atlantic Building
950 F Street, NW
Washington, DC 20004-1404
202.756.3300

www.alston.com

© Alston & Bird LLP 2007