

# SHOULD UNITED STATES ANTITRUST LAW BE APPLIED TO STATE TRADING ENTERPRISES IN AGRICULTURAL TRADE?

*Anna Kingsbury\**

I.	Introduction.....	185
II.	State Trading Enterprises in International Agricultural Trade .....	186
	A. STEs Under GATT 1994.....	190
	B. STEs and Antitrust Law: STEs as Cartels.....	191
III.	Extraterritorial Application of United States Antitrust Law .....	191
	A. Extraterritorial Jurisdiction: The “Effects” Test .....	193
	B. International Comity.....	194
IV.	The New Zealand Dairy Board/Fonterra: A Case Study in the Extraterritorial Application of United States Antitrust Law .....	197
	A. The New Zealand Dairy Board .....	197
	B. Reform of the New Zealand Dairy Board: The Creation of Fonterra.....	205
V.	Antitrust Policy: Should United States Law Apply?.....	211
VI.	Conclusion .....	213

## I. INTRODUCTION

In a number of countries, State Trading Enterprises (“STEs”) control agricultural exports to the United States.<sup>1</sup> For antitrust purposes, export STEs may be characterized as cartels of producers colluding to fix prices into importing country markets. This Article considers the legal and policy issues involved in applying United States antitrust law extraterritorially to STEs. In order to analyze these issues, this article uses STEs in the New Zealand dairy industry as a case study. First, the nature of STEs and their legal status in international trade

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\* Anna Kingsbury, B.A., LL.B, MLIS, LL.M, Senior Lecturer in Law, University of Waikato, New Zealand.

1. See KAREN Z. ACKERMAN & PRAVEEN M. DIXIT, USDA, USDA AGRIC. ECON. REPORT No. 783, AN INTRODUCTION TO STATE TRADING IN AGRICULTURE 1 (1999), available at <http://www.ers.usda.gov/publications/aer783>.

law will be discussed. The Article next considers the potential liability of STEs in United States antitrust law, with particular reference to the New Zealand Dairy Board and its successor company, "Fonterra." Because these STEs could be characterized as price-fixing cartels, depending on findings of market definition and market power, United States courts would have antitrust jurisdiction, unless this jurisdiction was excluded by considerations of comity.

This Article also considers the broader issue of applying United States antitrust law to export STEs in their agricultural trade context, and the corresponding policy implications. World agricultural trade is highly distorted and characterized by protectionist practices including producer subsidies, quotas and tariffs.<sup>2</sup> The United States imposes lawful tariff rate quotas on agricultural imports. It is argued that these quotas form anticompetitive output limitations that have the effect of raising U.S. consumer prices to the level of a profit maximizing, or monopoly, price. Under this means of analysis, a price-fixing cartel could not profitably further raise United States consumer prices, and United States consumers would not gain from a successful antitrust action. More broadly, because agricultural trade is subject to high levels of protectionism in the United States, it is argued that application of United States antitrust law is not an appropriate remedy. Antitrust law may arguably become a more justifiable remedy if world agricultural trade is liberalized, or if the United States does not apply protectionist measures. However, until those preconditions are met, the application of antitrust law to export STEs in agriculture would be an unjustified exercise of United States trade power.

## II. STATE TRADING ENTERPRISES IN INTERNATIONAL AGRICULTURAL TRADE

State Trading Enterprises take a number of forms: some control imports, some control exports, and some control both. The focus of this Article is on exporting STEs which act as "single desk sellers" of agricultural products. Historically, these took the form of state marketing boards.<sup>3</sup> More recently, they are also private companies, with single desk seller status or privileges.<sup>4</sup> Modern STEs developed as marketing boards after World War I, primarily in the British Commonwealth.<sup>5</sup> The United States also operated a quasi-STE through the

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2. See ACKERMAN & DIXIT, *supra* note 1, at 4.

3. See ACKERMAN & DIXIT, *supra* note 1, at 2.

4. See *id.*

5. Michael T. Roberts, *The Unique Role of State Trading Enterprises in World Agricultural Trade: Sifting Through Rhetoric*, 6 DRAKE J. AGRIC. L. 287, 291 (2001).

Commodity Credit Corporation until 1996.<sup>6</sup> Developing countries also saw the establishment of STEs during and after World War II, with the assistance of the World Bank.<sup>7</sup>

As a matter of industrial policy, many nations maintain STEs that control exports of particular commodities.<sup>8</sup> STEs are particularly common in agriculture.<sup>9</sup> They are used by many countries that export agricultural products; they are also common in developing countries.<sup>10</sup> The stated objectives of export-controlling STEs are: maximize the returns to individual growers and producers through combined marketing and selling efforts, increase international demand, and ensure consistent quality. Typically, this is achieved through “single desk” marketing, under which the STE is granted exclusive rights to market the product internationally.<sup>11</sup>

Countries typically use export STEs to boost domestic producer prices by granting the STE monopsony power over domestic production and sole export status.<sup>12</sup> Individual producers are able to reduce risk through STE price pooling.<sup>13</sup> In addition, STEs achieve economies of scale in marketing, transportation, insurance and quality control that are not available to individual producers.<sup>14</sup> As com-

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6. *Id.* at 292; ACKERMAN & DIXIT, *supra* note 1, at 4.

7. *See* Roberts, *supra* note 5, at 292. Today, however, the World Bank is advocating reform of STEs in the interests of free trade. *See generally* MERLINDA INGCO & FRANCIS NG, DISTORTIONARY EFFECTS OF STATE TRADING IN AGRICULTURE: ISSUES FOR THE NEXT ROUND OF MULTILATERAL TRADE NEGOTIATIONS (World Bank, Policy Research Working Paper No. 1915, 1998) (showing some distortionary effects of STEs that these World Bank employees think should be addressed in trade negotiations), *available at* <http://www.econ.worldbank.org/view.php?type=5&id=758>.

8. *See, e.g.*, AUSTRALIAN WHEAT BOARD, SUMMARY (explaining the role of Australia’s STE for wheat), *at* <http://www.awb.com.au/AWBL/Launch/Site/AboutAWB/Content/AboutAWB/Summary/Summary.htm> (last visited Jan. 18, 2005).

9. *See* ACKERMAN & DIXIT, *supra* note 1, at 1.

10. *See, e.g.*, WORKING PARTY ON STATE TRADING ENTERPRISES, WTO, *New and Full Notification Pursuant to Article XVII:4(a) of the GATT 1994 and Paragraph 1 of the Understanding of the Interpretation of Article XVII – India* [hereinafter *India Notification*] G/STR/N/7/IND (Oct. 8, 2001) (showing India’s STEs as notified to the World Trade Organization; additional notifications are also available for other countries, such as Fiji, Canada, Australia, and New Zealand), *available at* <http://docsonline.wto.org>.

11. *See, e.g.*, AUSTRALIAN WHEAT BOARD, *supra* note 8 (showing the duties of Australia’s STE as exclusive manager and marketer of all Australia’s bulk wheat exports).

12. ACKERMAN & DIXIT, *supra* note 1, at 11.

13. *See* Roberts, *supra* note 5, at 299.

14. ACKERMAN & DIXIT, *supra* note 1, at 11.

modities are exported into higher value markets with tariff rate quotas, STEs also serve to ensure that producers benefit from higher prices.<sup>15</sup> Developing countries commonly use STEs to control both exports and imports, thereby stabilizing prices and ensuring a constant food supply.<sup>16</sup>

In recent years, the United States has led opposition to STEs in WTO agriculture negotiations.<sup>17</sup> The United States and other opponents of STEs, including countries within the European Union, complain that STEs have unfair competitive advantages and distort trade.<sup>18</sup> In relation to single desk sellers, specific criticisms include: lack of transparency in purchasing or selling prices, government financial backing that insulates the STE from financial risks faced by other exporters; other government subsidies and privileges afforded to STEs; monopsony control over guaranteed supplies, permitting forward contracts without commercial risks; the ability to practice price discrimination between domestic and export markets, or between different export markets; price flexibility; and the ability to insulate producers through use of a price pooling system designed to enhance producer prices.<sup>19</sup> It is argued that non-STE exporters are unfairly disadvantaged when seeking to export to developing country markets, and allocative inefficiencies may arise because production is not directly responsive to market signals.<sup>20</sup>

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15. *See id.*

16. *See, e.g., India Notification, supra* note 10, at 4.

17. *See Roberts, supra* note 5, at 292.

18. In the WTO agricultural negotiations post-Doha, the United States seeks: (i) “[t]o end exclusive export and domestic procurement rights to ensure private sector competition in markets controlled by single desk exporters;” (ii) “[t]o eliminate the use of government funds or guarantees to support or ensure the financial viability of single desk exporters;” and (iii) “[t]o establish WTO requirements for notifying acquisition costs, export pricing, and other sales information for single desk exporters.” *Hearing on the Canadian Wheat 301 Decision Before the Senate Comm. on Commerce, Sci., and Transp.*, 107th Cong. 5-7 (2002) [hereinafter *Hearing*] (statement of Ambassador Allen F. Johnson, Chief Agriculture Negotiator, Office of the U.S. Trade Rep.), available at <http://commerce.senate.gov/hearings/041902johnson.pdf>.

19. Hugh Maginnis, *State-Trading Enterprises: Existence of Monopolies Is no Longer Justified*, 4 ECONOMIC PERSPECTIVES, May 1999, at 20-21, at <http://usinfo.state.gov/journals/ites/0599/ijee/ag-hugh.htm> (last visited Jan 18, 2005); *see generally* BRIAN PADDOCK, STATE TRADING AND INTERNATIONAL TRADE NEGOTIATIONS (Agric. and Agri-Food Can., Trade Research Series No. 1991E, 1998) (listing many of the criticisms of STEs, but also rebutting some of them), available at [http://www.agr.gc.ca/spb/radra/publications/statenego\\_e.pdf](http://www.agr.gc.ca/spb/radra/publications/statenego_e.pdf).

20. *See* Maginnis, *supra* note 19, at 21; PADDOCK, *supra* note 19, at 12; *Hearing, supra* note 18, at 2.

Supporters of STEs argue that STEs have a valuable role in agricultural policy, produce efficiencies and economies of scale for small producers who compete in trade with multinational corporations, and are not necessarily trade distorting.<sup>21</sup> It is argued that export STEs operate in international markets similar to commercial corporations; therefore, the STEs do not have unfair advantages.<sup>22</sup> Further, STE supporters assert that critics of STEs are mistaken when the critics assume that without STEs, the market would be competitive, free of distortions, and market performance would be improved.<sup>23</sup>

International agricultural markets are not level playing fields—world agricultural trade is characterized by distortions. Agricultural trade widely varies from country to country in all aspects: from subsidies,<sup>24</sup> to types of producers, to protectionist trade policies.<sup>25</sup> Exporting countries face output limitations in the shape of tariff rate quotas.<sup>26</sup> Supporters of STEs argue that without STEs, producers would be unable to compete with multinationals and would not be able to prevent these powerful countries from abusing their market power.<sup>27</sup> Moreover, in response to criticisms about transparency, STE supporters argue STEs are not necessarily less transparent than private firms; rather, supporters assert, STEs are frequently *more* transparent than private firms that are not publicly traded.<sup>28</sup> In addition, notification requirements of the GATT require a level of transparency not required of private firms, thereby disadvantaging the STEs.<sup>29</sup> In response to

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21. See PADDOCK, *supra* note 19, at 7.

22. *Id.*

23. See *id.* at 10.

24. See Elizabeth Becker, *U.S. Unilateralism Worries Trade Officials*, N.Y. TIMES, Mar. 17, 2003, at A8 (stating the United States has approved a dramatic increase in farm subsidies over the last year).

25. STEVE MCCORRISTON & DONALD MACLAREN, PERSPECTIVES ON THE STATE TRADING ISSUE IN THE WTO NEGOTIATIONS 14-15 (77th European Ass'n of Agric. Economists Seminar, Seminar No. 325, 2001) (providing an overview of research characterizing some markets in which STEs operate as imperfectly competitive), available at <http://www.ptt.fi/eaee-njf/papers/mccorriston.pdf>; see generally PADDOCK, *supra* note 19 (describing reasons why the market in which the Canadian Wheat Board operates is not perfectly competitive).

26. See PADDOCK, *supra* note 19, at 10.

27. Roberts, *supra* note 5, at 313; but see MCCORRISTON & MACLAREN, *supra* note 25, at 2 (discussing anti-competitive behavior arising from exporting countries).

28. PADDOCK, *supra* note 19, at 11-12 (“[M]any of the private firms are not publicly traded and they release even less information concerning their financial dealings than do most STEs. Moreover, given their transnational nature and the wide scope of their operations, it is by no means clear that such companies are, in fact, more transparent than exporting STEs.”) (emphasis added).

29. See *id.* at 8-9.

price discrimination concerns, STE supporters argue that price discrimination can be pro-competitive and enhance economic efficiency.<sup>30</sup>

Exporting STEs raise a number of competition concerns, and these concerns are inextricably linked to international trade law. STEs are based on cooperative structures and involve producer collaboration during marketing and selling commodities. As a single desk seller, an STE requires that buyers of its country's produce fill their supply needs solely from the STE.<sup>31</sup> As a result, individual producers are prohibited from selling direct.<sup>32</sup>

#### A. STEs Under GATT 1994

Article XVII of the GATT 1994 expressly permits the formation of STEs. The Understanding on the Interpretation of Article XVII of the GATT 1994 provides a working definition of STEs, as follows:

Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports.<sup>33</sup>

The GATT requires STEs to act in accordance with the general principles of non-discrimination.<sup>34</sup> Additional GATT STE rules cover market access,<sup>35</sup> transparency,<sup>36</sup> and prohibit quantitative restrictions.<sup>37</sup> Under Article XVII, states are required to annually report their STEs to the WTO.<sup>38</sup>

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30. *Id.* at 13 (arguing that price discrimination can improve performance by reducing inefficiencies, "can enhance competition by facilitating experimentation in pricing," and can undermine "oligopoly discipline").

31. *See* Maginnis, *supra* note 19, at 20 (stating private exporters have no choice but to buy their export supplies at a given market price [from the STE]).

32. *See id.* at 21 (stating "Producers . . . have no alternative but to sell to the single-desk exporter and take whatever price is offered.").

33. Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994, [hereinafter Article XVII Understanding], *available at* [http://www.wto.org/english/docs\\_e/legal\\_e/08-17.pdf](http://www.wto.org/english/docs_e/legal_e/08-17.pdf).

34. WTO Agreement, General Agreement on Tariffs and Trade 1994 [hereinafter GATT 1994] art. XVII, ¶ 1, Annex 1A (stating that STEs can charge different prices for sales in different markets provided this is done for commercial reasons and to meet the market conditions in the export market), *available at* [http://www.wto.org/english/docs\\_e/legal\\_e/gatt\\_47.pdf](http://www.wto.org/english/docs_e/legal_e/gatt_47.pdf).

35. GATT 1994 arts. II, ¶ 4, XVII, ¶ 4.

36. *Id.* art. XVII, ¶ 4.

37. *Id.* arts. XI, ¶ 1, XIII, ¶ 2.

38. *Id.* art. XVII, ¶ 4.

### B. *STEs and Antitrust Law: STEs as Cartels*

The criticisms of STEs previously discussed can also be framed as anti-trust issues. State Trading Enterprises can be characterized as cartels of producers, colluding to raise prices and/or limit the quantity of products delivered to importing country markets. In this respect, STEs are accused of a range of anti-competitive conduct principally arising from misuse of market power. Concerns that are expressed involve not only the classic antitrust injury to consumers argument, in the form of limitations on output and increased prices, but also a concern of injury to competitors who are seen to suffer a “disadvantage.”<sup>39</sup> Characterization of an STE as an anticompetitive cartel will depend upon the particular STE seeking to establish market power in the relevant product market. Because agricultural products from different countries are generally interchangeable, markets should be defined broadly. For example, a market should exist for “cheese” rather than separate markets for New Zealand cheese, Swiss cheese and so on. However, in *Trugman-Nash, Inc. v. New Zealand Dairy Board* (“*Trugman-Nash I*”), the district court held there was a separate market for New Zealand cheese because of the United States quota and U.S. licensing systems.<sup>40</sup>

With the issue of STE viability reframed as an antitrust issue in international trade, the analysis then focuses on extraterritorial application of the law of the importing state.<sup>41</sup> If consumers in the importing state suffer antitrust injury, this may give rise to an action in antitrust law and remedies against the STE.<sup>42</sup> This Article considers the potential application of United States antitrust law to STEs, and whether competition law remedies will be available for perceived STE injuries.

### III. EXTRATERRITORIAL APPLICATION OF UNITED STATES ANTITRUST LAW

United States antitrust laws prohibit business combinations that result in restraint of trade,<sup>43</sup> monopolization,<sup>44</sup> and anticompetitive mergers.<sup>45</sup> These anti-

39. *Hearing, supra* note 18, at 1.

40. *Trugman-Nash, Inc. v. N.Z. Dairy Bd.*, 942 F. Supp. 905, 921 (S.D.N.Y. 1996).

41. *See* RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 402 cmt. a (1987) (stating “international law recognizes links of territoriality”).

42. *See, e.g.*, U.S. DEP’T. OF JUSTICE & FTC, ANTITRUST ENFORCEMENT GUIDELINES FOR INTERNATIONAL OPERATIONS ¶ 3.1 (1995) [hereinafter GUIDELINES], *available at* <http://www.usdoj.gov/atr/public/guidelines/internat.htm> (stating that “[a]nti-competitive conduct that affects U.S. domestic or foreign commerce may violate the U.S. antitrust laws...”).

43. 15 U.S.C. § 1 (2000).

trust provisions are enforced by federal government agencies,<sup>46</sup> states,<sup>47</sup> and private parties.<sup>48</sup> Treble damages are available.<sup>49</sup> The broad purpose of antitrust laws is to promote competition in markets, thereby promoting the interests of consumers.<sup>50</sup>

There is potential for United States antitrust laws to be applied extraterritorially to exporting STEs in other states. When STEs are characterized as cartels due to their structure and conduct, the STEs are potentially in violation of the Sherman and Clayton Acts. For example, STEs may be established with a structure that constitutes an agreement among competitors to fix prices and control output, or STEs may engage in conduct that constitutes horizontal price-fixing, which is *per se* illegal under Section One of the Sherman Act.<sup>51</sup> Other possible violations include price discrimination, such as predatory pricing, exclusionary conduct and restraints, and potential monopolization.<sup>52</sup> Antitrust liability will depend in many cases on the extent of the STE's market power, which in turn will depend on how the market is defined.<sup>53</sup> Remedies can be limited in cases of extraterritorial application of antitrust laws.<sup>54</sup> Federal courts can order relief abroad, but without a relevant treaty, enforcement is difficult.<sup>55</sup> In practice, effectiveness depends upon the presence of persons or assets in the United States. Even then effectiveness can be limited, for example, by blocking statutes.<sup>56</sup> In any antitrust action against an STE, a preliminary question will be whether United States courts have extraterritorial antitrust jurisdiction.

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44. *Id.* § 2.

45. *Id.* § 18.

46. *See generally* GUIDELINES, *supra* note 42 (showing the guidelines the Department of Justice and Federal Trade Commission use for their enforcement actions).

47. 15 U.S.C. § 15c(a)(1) (2000).

48. *Id.* § 15(a).

49. *Id.* §§ 15(a), 15c(a)(2).

50. *See generally* *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 767 (1984) (stating competition in the markets "promotes the consumer interests that the [antitrust] laws aim to foster").

51. *See id.* at 768.

52. *See* *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 223-24 (1940).

53. *See* *Brown Shoe Co. v. United States*, 370 U.S. 294, 324-25 (1962) (citing *United States v. E. I. du Pont de Nemours & Co.*, 353 U.S. 586, 593 (1957)).

54. PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION*, VOLUME IA, ¶ 275 (2d ed. 2000).

55. *Id.*

56. Protection of Trading Interests Act 1980, §§ 2(1), 5(1)-(3) (Eng.) (blocking document discovery and limiting damages recovery).

*A. Extraterritorial Jurisdiction: The “Effects” Test*

United States antitrust jurisdiction reaches foreign commerce. The Sherman Act covers restraint or monopolization of “commerce . . . with foreign nations.”<sup>57</sup> The Clayton Act also defines commerce broadly, although there are limitations on substantive provisions; for example, Section Seven of the Clayton Act applies to mergers that result in anticompetitive effects within a “section of the country.”<sup>58</sup> It is well-established that conduct occurring anywhere in the world is subject to United States antitrust laws so long as the conduct affects competition within the United States or export competition from the United States.<sup>59</sup> Courts apply an “effects test,” first articulated by Judge Hand, requiring plaintiffs show the challenged acts “were intended to affect [U.S.] imports and did affect them.”<sup>60</sup> This U.S. jurisdiction is subject to limits, however. In formulating his test, Judge Hand limited the reach of the Sherman Act “to those acts that (1) ‘significantly’ or ‘directly’ affect United States commerce, or (2) are intended to have an effect, or (3) are both intended to have and do have such an effect.”<sup>61</sup> Once a plaintiff establishes the defendant had intention to affect United States commerce, the burden shifts to the defendant, and the defendant must prove the absence of any such effects. As a result of this high burden-shifting imposed on defendants, intention alone will often support application of the Sherman Act.<sup>62</sup>

The “effects test” was incorporated by Congress into the Foreign Trade Antitrust Improvements Act (“FTAIA”) of 1982, which excludes conduct of United States exporters from Sherman Act jurisdiction “unless such conduct has a direct, substantial, and reasonably foreseeable effect” on non-foreign or import trade or commerce, or on export trade or commerce where the effect gives rise to a claim under other provisions of the Act.<sup>63</sup> The effects test has been accepted and applied by the United States Supreme Court, which declared in 1993 it “is well established by now that the Sherman Act applies to foreign conduct that was meant to produce and did in fact produce some substantial effect in the United

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57. 15 U.S.C. § 2 (2000).

58. *Id.* § 18.

59. See AREEDA & HOVENKAMP, *supra* note 54, ¶ 272c.

60. HERBERT HOVENKAMP, *FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE* 752 (2d ed. 1999).

61. AREEDA & HOVENKAMP, *supra* note 54, ¶ 272d.

62. *Id.* ¶ 272f.

63. 15 U.S.C. § 6a (2000).

States.”<sup>64</sup> The effects test has also been incorporated into the Department of Justice and Federal Trade Commission’s Joint Antitrust Enforcement Guidelines for International Operations (“Guidelines”), which take a far-reaching approach to jurisdiction. The Guidelines state that “[a]nticompetitive conduct that affects U.S. domestic or foreign commerce may violate the U.S. antitrust laws regardless of where such conduct occurs or the nationality of the parties involved.”<sup>65</sup>

In relation to import commerce, the Guidelines state, “[i]mports into the United States by definition affect the U.S. domestic market directly, and will, therefore, almost invariably satisfy the intent part of the *Hartford Fire* test.”<sup>66</sup> Whether they in fact produce the requisite substantial effects will depend on the facts of each case.”<sup>67</sup> As a result, if an STE is a cartel which targets the United States and also has an impact in the United States, it is clear the United States antitrust laws will reach it.

### B. *International Comity*

Even after the U.S. jurisdiction is established under the effects test, a court may, nonetheless, exercise its discretion not to proceed on the merits for reasons of “international comity.”<sup>68</sup> The Guidelines also consider comity in deciding whether to bring an action against a foreign party.<sup>69</sup> To understand the limitation that international comity may have on U.S. antitrust jurisdiction, the definition of international comity must be explored. The Supreme Court in *Hartford Fire* interpreted comity strictly.<sup>70</sup> However, the Ninth Circuit Court of Appeals in *Timberlane Lumber Co. v. Bank of America*,<sup>71</sup> had previously used a balancing approach and applied the factors summarized as follows:

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64. *Hartford Fire Ins. Co. v. Cal.*, 509 U.S. 764, 796 (1993). *But cf.* *Den Norske Stats Oljieselskap As v. Heeremac Vof*, 241 F.3d 420 (5th Cir. 2001) (taking a restrictive approach to jurisdiction); *Kruman v. Christie’s Int’l PLC*, 284 F.3d 384 (2d Cir. 2002) (taking a less restrictive view); *Empagran S.A. v. F. Hoffman-LaRoche, Ltd.*, 315 F.3d 338 (D.C. Cir. 2003) (taking an approach closer to the Second Circuit).

65. GUIDELINES, *supra* note 42, § 3.1.

66. GUIDELINES, *supra* note 42, § 3.11

67. *Id.*

68. *Id.* § 3.2.

69. *Id.*

70. *See Hartford Fire Ins. Co.*, 509 U.S. at 798 (contrasting their approach with the Ninth Circuit in *Timberlane Lumber Co. v. Bank of Am.*, 549 F.2d 597 (9th Cir. 1976), *aff’d* 749 F.2d 1378 (9th Cir. 1984), *cert. denied* 472 U.S. 1032 (1985)).

71. *Timberlane Lumber Co.*, 549 F.2d at 614. The Timberlane factors were applied by the Ninth Circuit Court of Appeals in *In re Insurance Antitrust Legislation*, 938 F.2d 919 (9th Cir.

- (1) the degree of conflict with foreign law or policy;
- (2) the nationality or allegiance of the parties and the locations or principal places of business or incorporation;
- (3) the extent to which enforcement by either state can be expected to achieve compliance;
- (4) the relative significance of effects on the United States as compared with those elsewhere;
- (5) the extent to which there is explicit purpose to harm or affect American commerce, and the foreseeability of such effect; and
- (6) the relative importance to the violations charged of conduct within the United States as compared with conduct abroad.<sup>72</sup>

The Third Restatement of the Foreign Relations Law of the United States, issued in 1987, also instructs courts to consider the same factors as in *Timberlane* when considering whether to exclude jurisdiction on the basis of international comity.<sup>73</sup>

The Supreme Court, in *Hartford Fire*, considered only the issue of conflict between United States and United Kingdom law, and did not address the other *Timberlane* factors.<sup>74</sup> However, in so doing it did leave open the possibility that in a proper case, a court might apply the *Timberlane* factors.<sup>75</sup> In *Hartford Fire*, the United States Supreme Court found the effects test was satisfied by the facts presented, and considered whether to decline jurisdiction on the basis of comity.<sup>76</sup> The Court concluded that under the circumstances, comity should only exclude jurisdiction where there was a clear conflict with the law of the foreign sovereign.<sup>77</sup> Although other factors had influenced the prior Ninth Circuit Court

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1991), *aff'g in part, rev'd in part, Hartford Fire Ins. Co. v. California*, 506 U.S. 814 (1993). However, the United States Supreme Court's opinion, in *In re Insurance Antitrust Litigation*, considered only the issue of conflict between U.S. and UK law, and did not address the other *Timberlane* factors.

72. *Timberlane Lumber Co.*, 549 F.2d at 614.

73. RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES §§ 402-03 (1987).

74. *See Hartford Fire Ins. Co.*, 509 U.S. at 815 (discussing the choice of law between the United States and foreign countries).

75. WILBUR L. FUGATE, FOREIGN COMMERCE AND THE ANTITRUST LAWS: VOLUME I 83 (5th ed. 1996).

76. 509 U.S. at 796-98.

77. *Id.* at 798.

of Appeals decision, in *In re Insurance Antitrust Litigation*, including the intent to “affect United States commerce and the substantial nature of the effect produced,”<sup>78</sup> the Supreme Court held, in *Hartford Fire*, “[t]he only substantial question in this litigation is whether ‘there is in fact a true conflict between domestic and foreign law.’”<sup>79</sup> The Court said, “[t]he fact that conduct is lawful in the state in which it took place will not, of itself, bar application of the United States anti-trust laws,’ even where the foreign state has a strong policy to permit or encourage such conduct.”<sup>80</sup> On the facts, the Court found no such clear conflict in the case.<sup>81</sup> No conflict exists “where a person subject to regulation by two states can comply with the laws of both.”<sup>82</sup>

In summary, *Hartford Fire* held that comity would only preclude exercise of U.S. jurisdiction where there is a true conflict between domestic and foreign law. However, it is significant that in *Hartford Fire*, the Supreme Court was asked to consider only one of the *Timberlane* factors—the issue of conflict.<sup>83</sup> The Court said nothing about the other factors, which leaves open the question whether these remaining factors might still be applied and prohibit the exercise of U.S. jurisdiction. In subsequent decisions, some courts have continued to use the *Timberlane* factors as an alternative or auxiliary test to the narrower *Hartford Fire* test.<sup>84</sup> An ongoing controversy exists about the scope of comity, and differing judicial approaches suggest a need for a new decision from the Supreme Court.<sup>85</sup>

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78. *Id.* (citing *In re Insurance Antitrust Litigation*, 938 F.2d 919, 934 (9th Cir. 1991)).

79. *Id.* (quoting *Société Nationale Industrielle Aérospatiale v. United States Dist. Court for S. Dist. of Iowa*, 482 U.S. 522, 555 (1987) (Blackmun, J., concurring in part and dissenting in part)).

80. *Id.* at 799 (citing RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 415 cmt. j. (1987)).

81. *See id.* (noting that because a party did not argue there was a British law requiring action prohibited by the United States, the court found no conflict between United States law and British law).

82. *Id.* (citing RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 403 cmt. e (1987)).

83. *See id.* at 798-99.

84. *FUGATE*, *supra* note 75, at 82; *see, e.g., Trugman-Nash, Inc. v. N.Z. Dairy Bd.*, 954 F. Supp. 733, 737 (S.D.N.Y. 1997) (holding that *Timberlane* factors constitute controlling law in the Second Circuit); *Metro Indus., Inc. v. Sammi Corp.*, 82 F.3d 839, 846-49 (9th Cir. 1996) (applying the *Timberlane* factors in granting jurisdiction).

85. *Compare United States v. Nippon Indus. Co.*, 109 F.3d 1, 8 (1st Cir. 1997) (describing comity as “more a matter of grace than a matter of obligation” and stating the expansion of comity had been “stunted” by *Hartford Fire*) with *Trugman-Nash, Inc.*, 954 F. Supp. at 737-38 (taking a less restrictive view, reading *Hartford Fire* more broadly and dismissing the complaint on

#### IV. THE NEW ZEALAND DAIRY BOARD/FONTERRA: A CASE STUDY IN THE EXTRATERRITORIAL APPLICATION OF UNITED STATES ANTITRUST LAW

State Trading Enterprises take a variety of forms; as a result, it is difficult to generalize about their characteristics. This Article therefore uses one important STE, the New Zealand Dairy Board, as a case study. The New Zealand Dairy Board was absorbed in 2001 into a new company (“Fonterra”) which was formed by the merger of New Zealand’s two largest dairy companies.<sup>86</sup> The events within the New Zealand dairy industry merit potential application of U.S. anti-trust laws both to the former New Zealand Dairy Board, and to the new company Fonterra.

##### A. *The New Zealand Dairy Board*

The New Zealand Dairy Board (“Dairy Board”) was one of the more important STEs on the international stage before its disappearance in 2001.<sup>87</sup> The Dairy Board was owned by cooperative dairy processing companies, which in turn were owned by farmers.<sup>88</sup> The Dairy Board operated as a single desk seller with statutory sole export powers.<sup>89</sup> The Dairy Board was responsible for all export marketing of New Zealand’s dairy produce, and the Dairy Board had power to license other exporters,<sup>90</sup> although in practice it marketed most products itself. The New Zealand Crown allocated to the Dairy Board tariff quota rights

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grounds of comity, finding an actual conflict and applying *Timberlane*); *see also* Rivendell Forest Prods., Ltd. v. Canadian Forest Prods., Ltd., 810 F. Supp. 1116, 1119-20 (D. Colo. 1993) (following *Timberlane* and dismissing on grounds of comity); AREEDA & HOVENKAMP, *supra* note 54, ¶ 273c2 (stating that *Timberlane* “invites judges to consider numerous softer considerations of comity . . .”).

86. International Union of Food, Agricultural, Hotel, Restaurant, Catering, Tobacco, and Allied Workers’ Associations (IUF), *IUF and New Zealand Dairy Workers’ Union Sign International Union Rights Agreement with Fonterra* (Apr. 8, 2002) [hereinafter *Fonterra Announcement*], available at [http://www.iuf.org.uk/cgi-bin/dbman/db.cgi?db=default&uid=default&ID=271&view\\_records=1&ww=1&en=1](http://www.iuf.org.uk/cgi-bin/dbman/db.cgi?db=default&uid=default&ID=271&view_records=1&ww=1&en=1).

87. *See State Trading Enterprises: Their Role in World Markets*, AGRIC. OUTLOOK (Econ. Research Serv., USDA), June 1997, at 11, available at <http://www.ers.usda.gov/publications/agoutlook/jun1997/ao241d.pdf>; *see also Fonterra Announcement*, *supra* note 86 (stating the New Zealand Dairy Board was the second largest STE, in terms of value of major commodities exported during 1992-94).

88. N.Z. DAIRY BD., SUBMISSION TO THE ROYAL COMMISSION ON GENETIC MODIFICATION 6 (Oct. 30, 2000) [hereinafter SUBMISSION], article on file with Drake J. Agric. L.

89. Dairy Board Act, 1961, § 14(c) (N.Z.).

90. *Id.* § 26(2).

which could be applied to designated markets such as the EU and the U.S.<sup>91</sup> Revenue earned from the imposed tariffs was returned to farmers via a pay-out system. The Dairy Board also had interests in research and development.<sup>92</sup> The Dairy Board handled thirty percent of world dairy product exports in the 1990s.<sup>93</sup> The Dairy Board did not manage domestic production (this was done by the dairy processing companies) and did not sell in the domestic market.<sup>94</sup> It had no control over New Zealand's domestic market and did not receive subsidies or other financial support from the New Zealand government.<sup>95</sup> The Dairy Board did not play a role in New Zealand imports and there were (and are) no legislative restrictions on New Zealand imports.<sup>96</sup>

The New Zealand Dairy Board was subject to considerable criticism from the United States and was often cited as an example of an STE that required WTO reform.<sup>97</sup> There is considerable doubt, however, as to whether the activities of the Board were in fact trade-distorting, or anticompetitive, in the global market. The Dairy Board controlled almost one-third of the global export market, but the Board had limited actual market power due to the availability of alternative sources of supply, such as the supply from the EU. This suggests that in most markets, the Dairy Board may in fact have been a price taker.

Karen Ackerman and Praveen Dixit have proposed a classification scheme for STEs, based on their ability to control domestic markets and external trade, which aids in the identification of STEs with the greatest potential to "distort trade."<sup>98</sup> Within this classification scheme, the New Zealand Dairy Board is classified as a "Type III STE," which does not control the domestic market but maintains quantitative controls on external trade.<sup>99</sup> According to Ackerman and

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91. *See id.*

92. SUBMISSION, *supra* note 88, at 4.

93. ACKERMAN & DIXIT, *supra* note 1, at 24.

94. Working Party on State Trading Enterprises, *New and Full Notification Pursuant to Article XVII:4(a) of the GATT 1994 and Paragraph 1 of the Understanding on the Interpretation of Article XVII – New Zealand*, at 3, G/STR/N/7/NZL (July 27, 2001) [hereinafter *New Zealand Notification*], available at <http://docsonline.wto.org>.

95. *Id.*

96. ACKERMAN & DIXIT, *supra* note 1, at 24-25.

97. *See, e.g.*, STAFF OF HOUSE COMM. ON AGRIC., 105TH CONG., AGRICULTURAL TRADE EXPANSION DELEGATION NEW ZEALAND-AUSTRALIA REPORT (1998), available at <http://agriculture.house.gov/105/ausnz.htm>.

98. ACKERMAN & DIXIT, *supra* note 1, at 17-18.

99. *Id.* at 21, 24. The authors actually describe a Type III STE as an STE that "competes with private firms to procure and sell domestic production in the home market, but maintains quan-

Dixit, Type III STEs “have the potential to moderately distort trade, but the actual extent of distortion would depend on factors such as the extent of international market power, the range of exclusive privileges available to the firm, the policy objectives of the STE and the importance (share) of external trade in domestic consumption and production.”<sup>100</sup> Exporting STEs which also have control over the domestic market have more power to distort trade, but this in turn will be influenced by other factors such as share of the international market.<sup>101</sup>

The Dairy Board was not only criticized by United States trade interests, but it was also the defendant in U.S. litigation, in the case of *Trugman-Nash, Inc. v. New Zealand Dairy Board* (“*Trugman-Nash I*”).<sup>102</sup> This suit was brought by holders of import licenses for cheese in the United States, alleging, *inter alia*, antitrust violations of Sections One and Two of the Sherman Act.<sup>103</sup> The Dairy Board had created a subsidiary, Western Dairy, which pursuant to United States Department of Agriculture regulations, had been designated as the “preferred” importer of New Zealand cheese.<sup>104</sup> As a result, American importers such as plaintiffs could purchase New Zealand cheese only from Western Dairy.<sup>105</sup> Plaintiffs complained that as importers, they had “no alternative but to procure New Zealand dairy produce, including cheese, from the monolithic export cartel created by the [Dairy] Board, its Directors, and co-conspirators.”<sup>106</sup> The complaint was that plaintiffs could not “deal directly and individually with New Zealand dairy farmers or cooperatives, in an effort . . . to pay a lower price for the cheese plaintiffs then resell in the American market.”<sup>107</sup> In summary, the plaintiffs claimed the formation of the cooperatives into a cartel resulted in higher prices for U.S. importers.

The Dairy Board moved to dismiss the claims on two grounds: lack of jurisdiction and failure to state claims upon which relief could be granted.<sup>108</sup> The jurisdictional arguments were “founded primarily upon the manner in which the New Zealand Dairy Board Act of 1961 [“Dairy Board Act”], . . . created and

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titative controls on external trade.” *Id.* at 17. This was not the case with the Dairy Board, as it played no role in New Zealand domestic markets. Nevertheless, it is classified as a Type III STE.

100. *Id.* at 17-18.

101. *See generally id.* at 18.

102. *Trugman-Nash, Inc. v. N. Z. Dairy Bd.*, 942 F. Supp. 905 (S.D.N.Y. 1996).

103. *Id.* at 909.

104. *Id.* at 911.

105. *Id.*

106. *Id.* at 912 (citation omitted).

107. *Id.*

108. *Id.* at 909.

governs the conduct of the NZDB.”<sup>109</sup> The Dairy Board asserted the following doctrines applied to the jurisdictional analysis: act of state, foreign sovereign compulsion, and international comity.<sup>110</sup>

The *Trugman-Nash* I court held that the applicability of all three doctrines depended on the answer to the same question: “whether New Zealand law compels defendants to conduct their affairs in the manner described,” which plaintiffs alleged violated the Sherman Act.<sup>111</sup> If New Zealand law did not so compel the defendants, then the defendants could comply with laws of both countries, and there would be no basis for antitrust immunity.<sup>112</sup> The court’s opinion did not find any language in the Dairy Board Act mandating the Dairy Boards’ pricing and selling structure.<sup>113</sup> The court said “[t]he [Dairy Board] Act created the Board; defines the Board’s ‘general functions’ in language that is general indeed; commands the Board, in comparable language, to ‘comply with the general trade policy of the Government of New Zealand,’ an unsurprising directive for the Parliament to include.”<sup>114</sup> The Dairy Board Act does not require that all export produce be marketed by or through the Dairy Board.<sup>115</sup> Parliament’s policy was to maximize New Zealand’s dairy product income, “but the statute falls well short of compelling any particular commercial arrangements to carry that policy out.”<sup>116</sup> The most that could be said was “that the New Zealand Parliament established a statutory scheme conferring comprehensive powers” upon the Board and the Board’s conduct was “perfectly consistent with New Zealand law and policy.”<sup>117</sup> The doctrines of international comity (on a narrow construction of *Hartford Fire*) and foreign sovereign compulsion did not therefore apply.<sup>118</sup> The act of state doctrine did not apply either, because the complaint was not about an official act of a foreign sovereign performed within its own territory.<sup>119</sup> The plaintiffs did not challenge the validity of the New Zealand Dairy Board Act.<sup>120</sup> They challenged the conduct of the Board pursuant to the powers

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109. *Id.*

110. *Id.*

111. *Id.*

112. *See id.*

113. *Id.* at 912.

114. *Id.*

115. *Id.*

116. *Id.*

117. *Id.* at 912-13.

118. *See id.* at 913.

119. *Id.*

120. *Id.*

under the statute.<sup>121</sup> The court therefore rejected the defendant's argument that these doctrines, viewed separately or together, excluded jurisdiction.<sup>122</sup>

The New Zealand Dairy Board also moved to dismiss the action for failure to state a claim, resulting in the court's assessment of whether the complaint stated a claim upon which relief could be granted under the Sherman Act.<sup>123</sup> Plaintiff's complaint alleged the Dairy Board and its co-conspirators—New Zealand dairy producers and their fifteen cooperative dairy companies—had created an “export cartel.”<sup>124</sup> It alleged the cartel members had collectively refused to supply dairy produce, including cheese, to U.S. importers in a free and competitive market, and the effect was the inflation of export prices on New Zealand produce.<sup>125</sup> Thus, they “alleged a price-fixing cartel which is unlawful *per se*...”<sup>126</sup> The court first considered whether there was a sufficient plurality of conspirators as required by Section One of the Sherman Act and considered authority on whether cooperatives or trade associations could be considered single enterprises for the purposes of antitrust analysis.<sup>127</sup> The court utilized the analysis set out in *Mt. Pleasant v. Associated Electric Cooperative, Inc.*<sup>128</sup> As a result, the court concluded that “the requisite plurality of [Section One] conspirators does not exist in this case unless the [fifteen] New Zealand dairy cooperatives or the dairy farmers who make up those cooperatives pursued ‘diverse interests,’ as that phrase is defined in *Mt. Pleasant*.”<sup>129</sup> The *Mt. Pleasant* court defined “diverse interests” as those “interests ‘which tend to show that any two of the defendants are, or have been, actual or potential conspirators, . . . or, at the very least, interests which are sufficiently divergent so that a reasonable juror could conclude that the entities have not always worked together for a common cause.’”<sup>130</sup> This issue could not be resolved on a motion to dismiss.<sup>131</sup>

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121. *Id.* (by allowing this the court was following *Hartford Fire*, but the court failed to discuss the *Timberlane* factors in its opinion).

122. *Id.* at 913, 914.

123. *Id.* at 915.

124. *Id.* at 916.

125. *Id.*

126. *Id.*

127. *Id.* at 916-17.

128. *Id.* at 917-19 (construing *Mt. Pleasant v. Associated Elec. Coop.*, 838 F.2d 268 (8th Cir. 1988)).

129. *Id.* at 919.

130. *Id.* (quoting *Mt. Pleasant*, 838 F.2d at 276).

131. *Id.*

Plaintiffs also alleged conspiracy to monopolize in violation of Section Two of the Sherman Act.<sup>132</sup> The court held that:

[t]he offense of monopoly under [Section Two] of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.<sup>133</sup>

The plaintiffs contended that the defendants, along with their co-conspirators, created an export cartel with “the intent ‘of monopolizing the market for the importation, distribution, and sale in the United States of New Zealand cheese.’”<sup>134</sup> The plaintiffs argued that competitors in the market were holders of USDA-granted quota licenses for the importation of New Zealand cheese and for this purpose “no other products are interchangeable for New Zealand cheese.”<sup>135</sup> The court accepted that New Zealand cheese imported into the United States qualified as the “relevant market” for the Sherman Act Section Two analysis.<sup>136</sup> “For the quota-licensed New Zealand cheese importer, desirous of deriving maximum profit from its license, New Zealand cheese is no more interchangeable with other cheeses than were non-Kodak parts for servicers of Kodak equipment.”<sup>137</sup> The court agreed with defendants stating, “the licensed New Zealand cheese importers’ non-interchangeable New Zealand cheese market [was] a creation of American law,” but said “that [did] not prevent an identifiable market from being a market.”<sup>138</sup> The court concluded the complaint “sufficiently allege[d] the existence of the relevant market, and conduct by defendants that not only could achieve monopoly power in that market, but in fact ha[d] done so.”<sup>139</sup> The claims, therefore, survived defendants’ motion to dismiss.

The analysis in *Trugman-Nash I* is open to criticism. First, it is clear New Zealand cheese would not form a separate market if the market were not so tightly regulated, as other cheese is reasonably interchangeable in use with New

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132. *Id.* at 920.

133. *Id.* (quoting *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 481 (1992) (citing and quoting *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966))).

134. *Id.* (citation omitted).

135. *Id.* (citation omitted).

136. *Id.* at 921.

137. *Id.* (discussing *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 482 (1992)).

138. *Id.*

139. *Id.*

Zealand cheese.<sup>140</sup> The plaintiffs' import licenses only have value because the United States government limits imports. Thus, if there is in fact a separate market for New Zealand cheese, it is solely a creation of the United States government. In addition, it is arguable that even in a regulated market, license holders can substitute non-New Zealand cheese for New Zealand cheese by applying for licenses to buy non-New Zealand cheese. These licenses would then be reasonably interchangeable with licenses for New Zealand cheese; therefore, it is inaccurate to identify a separate market for New Zealand cheese.

Second, the United States government has imposed an output limitation in the form of a tariff rate quota.<sup>141</sup> Arguably, it is this output—not the conduct of the New Zealand Dairy Board—which is actually reducing competition.<sup>142</sup> The quota limits output and thereby raises consumer prices to the profit-maximizing, or monopoly price, level.<sup>143</sup> The alleged price-fixing activities of the Dairy Board could not, therefore, continue to raise prices profitably. United States consumers would only be presented with lower prices if both the alleged price-fixing and the output limitations were removed. Therefore, it is not logical to impose liability on the Dairy Board under United States law for an uncompetitive market situation that is in fact created by United States government policy. As a matter of industrial and trade policy, the United States has decided to impose a quota to protect its farmers, and in doing so, has raised costs to United States consumers. In this sense, the conflict here is not only between the New Zealand government's industrial policy and United States antitrust law, but also between United States industrial and trade policy and United States antitrust law.

However, the *Trugman-Nash* I opinion was not the end of the story, even though the substantive antitrust law holdings were not revisited. On a motion for reargument, the court in *Trugman-Nash* II subsequently issued a new opinion, taking a different view on jurisdiction and the doctrines of act of state, foreign sovereign compulsion, and international comity.<sup>144</sup> In the new opinion, the court reconsidered the statutory scheme, particularly Section 17(1A) of the Dairy Board Act of 1961, which required that any person wishing to export dairy produce from New Zealand apply to the Dairy Board for permission.<sup>145</sup> The section

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140. Cf. *United States v. E. I. du Pont de Nemours & Co.*, 351 U.S. 377, 394-95 (1956) (rejecting the government's contention that the market should be narrowly defined to show du Pont had created a monopoly).

141. *Trugman-Nash, Inc.*, 942 F. Supp. at 921.

142. See *id.* (implying that markets come into being as a result of governmental action).

143. See *id.*

144. *Trugman-Nash, Inc. v. N.Z. Dairy Bd.*, 954 F. Supp. 733, 736 (S.D.N.Y. 1997).

145. *Id.*

provided that the Dairy Board may grant or refuse a particular export application, after “having had regard” to considerations in Section 17(1A)(a)-(c), as follows:

- (a) The extent to which the markets are in states that do not impose quantitative restrictions on the importation of dairy produce; and
- (b) The extent to which the export of the produce to the markets might result in a direct or indirect reduction of the overall returns to the New Zealand dairy industry; and
- (c) Any other relevant guidelines for the time being established by the Board for the purposes of this section and published by the Board.<sup>146</sup>

The court held that, in its earlier opinion, it had “overlooked” Section 17(1A)(a), and that the provision was relevant “because the United States, through its own statutory import quota system, imposes ‘quantitative restrictions on the importation of dairy produce.’”<sup>147</sup> The defendants argued that if individual New Zealand dairy producers were granted export licenses, the effect would be to “introduce price competition to an undifferentiated market where only a fixed quantity could be sold.”<sup>148</sup> This would decrease returns to the New Zealand dairy industry, a result the Dairy Board Act mandated the Dairy Board to avoid. The court held that the Dairy Board Act mandated “Board disapproval of sales price competition among New Zealand dairy producers in respect of exports to nations like the United States that restrict import quantities.”<sup>149</sup> There was therefore an “actual and material conflict between American antitrust law and New Zealand law in respect of the marketing of dairy export produce [and] that conflict [was] sufficient to entitle defendants to invoke the doctrines of act of state, foreign sovereign compulsion, and international comity.”<sup>150</sup> As a second ground for granting defendant’s motion for reargument, the court concluded it had also overlooked the *Timberlane* factors, and these factors were controlling in the Second Circuit.<sup>151</sup>

The *Trugman-Nash II* case therefore raises important questions of extra-territorial application of United States antitrust law to STEs. The case suggests substantive antitrust liability for export STEs is at least possible, if not probable. Export STEs are based on the concept of joint action by producers in order to

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146. *Id.*

147. *Id.*

148. *Id.*

149. *Id.*

150. *Id.*

151. *Id.* at 737.

maximize prices. Such an arrangement can be characterized as a classic per se price fixing agreement. Jurisdiction is also likely to be available under the effects test, as it is likely such conduct will be held to have a direct, substantial, and reasonably foreseeable effect on United States consumers.<sup>152</sup> Exercise of jurisdiction is also possible under *Hartford Fire* if there is no clear conflict between the law in the STE country of origin and United States law.<sup>153</sup> Exercise of jurisdiction may also depend on the application of the *Timberlane* factors.<sup>154</sup> For STEs to avoid extraterritorial application of U.S. antitrust law, it will be essential that their structure and conduct is clearly *mandated* by domestic law and not merely *permitted*. State Trading Enterprises must recognize that, to avoid exercise of jurisdiction, it will be necessary to show a clear conflict of laws.

#### B. Reform of the New Zealand Dairy Board: The Creation of Fonterra

In recent years, pressure for STE reform has led many countries to deregulate and restructure their marketing boards. One approach has been to convert marketing boards into producer-owned companies, some of which have retained their single desk seller status.

The New Zealand Dairy Board is an example of an STE that has undergone restructuring. In October 2001, the New Zealand Dairy Board was absorbed into a new company ("Fonterra"), formed by the merger of New Zealand's two largest dairy companies.<sup>155</sup> Legislation exempted the merger from antitrust scrutiny by New Zealand's competition agency, the Commerce Commission.<sup>156</sup> Thirteen thousand New Zealand dairy farmer suppliers cooperatively own Fonterra.<sup>157</sup>

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152. See, e.g., *Occidental Petroleum Corp. v. Buttes Gas & Oil Co.*, 331 F. Supp. 92, 102 (C.D. Cal. 1971) (differentiating the type of effect necessary for U.S. jurisdiction pursuant to the Sherman Act, as compared to the type of effect necessary to show a violation of the Sherman Act, explaining while a direct and substantial effect is necessary for a Sherman Act violation, *any effect* that is not both insubstantial and indirect will support federal jurisdiction).

153. See *Hartford Fire Ins. Co. v. Cal.*, 509 U.S. 764, 798 (1993).

154. *Timberlane Lumber Co. v. Bank of Am.*, 549 F.2d 597, 614-15 (9th Cir. 1976).

155. See FONTERRA, FACTS & FIGURES [hereinafter FACTS], at <http://www.fonterra.com/content/aboutfonterra/factsandfigures/default.jsp> (last visited Jan. 26, 2005); FONTERRA, SELECT COMMITTEE SUBMISSION ¶ 1.6 [hereinafter COMMITTEE], available at [http://www.fonterra.com/content/unmanaged/merger\\_archive/select\\_committee/default.jsp](http://www.fonterra.com/content/unmanaged/merger_archive/select_committee/default.jsp) (both describing the company and the history of its formation).

156. See Dairy Industry Restructuring Act, 2001, § 7 (N.Z.).

157. FONTERRA, OUR STRUCTURE, at <http://www.fonterra.com/content/aboutfonterra/ourstructure/default.jsp> (last visited Jan. 26, 2005).

Shareholders represent ninety-five percent of New Zealand's dairy farmers and are spread throughout New Zealand.<sup>158</sup> Fonterra is New Zealand's largest company; it generates twenty percent of New Zealand's export receipts and seven percent of its gross domestic product.<sup>159</sup> One of the top ten dairy companies in the world, Fonterra is the leading exporter of dairy products and is responsible for one-third of international dairy trade.<sup>160</sup>

Fonterra replaced the New Zealand Dairy Board, but Fonterra did not retain the Dairy Board's single export seller status.<sup>161</sup> However, quota export rights to designated markets, including the United States, were allocated to Fonterra.<sup>162</sup> Fonterra thus has the license to export to the European Communities and Canada until 2007, to export cheddar cheese and low-fat cheese to the United States until the end of 2008, to export NSPF cheese and other American-type cheeses until the end of 2009, and to export all dairy products to Japan until 2010,<sup>163</sup> meaning that Fonterra is the sole exporter to those countries. Therefore, although Fonterra is not an STE on the traditional marketing board model, it retains STE status, as defined by the GATT 1994, as a non-governmental enterprise with special statutory rights in the exercise of which it may "influence...the level or direction of imports or exports."<sup>164</sup>

Fonterra is therefore an interesting example of a new form of STE. It is no longer a state marketing board, and it is no longer a single desk seller. Nevertheless, it is a cooperatively owned private company whose shareholders constitute ninety-five percent of New Zealand dairy producers. It was formed by a merger of the two largest dairy companies, was exempted from antitrust scrutiny and retains licenses to sell into designated markets, including the United States.

At the time of its establishment, Fonterra had market power in the New Zealand markets for dairy products and for milk supplied by farmers.<sup>165</sup> In re-

158. *Id.*

159. FONTERRA, ABOUT NEW ZEALAND, at

<http://www.fonterra.com/content/dairyingnz/aboutnz/default.jsp> (last visited Jan. 26, 2005).

160. FACTS, *supra* note 155.

161. Tony Wharton, *The New Zealand Dairy Industry Merger*, THE STATE OF NEW ZEALAND AGRICULTURE AND FORESTRY 2001 (N.Z. Ministry of Agric. and Forestry), available at <http://www.maf.govt.nz/mafnet/rural-nz/statistics-and-forecasts/sonzaf/2001/2001-01.htm>.

162. See *Dairy Production and Trade Developments*, DAIRY: WORLD MARKET AND TRADE (Foreign Agric. Serv., USDA), Dec. 2001, available at <http://www.fas.usda.gov/dlp/circular/2001/01-12Dairy/dairyprd.html>; see also Wharton, *supra* note 161.

163. Dairy Industry Restructuring Act, 2001, § 24 (N.Z.).

164. Article XVII Understanding, *supra* note 33.

165. *Dairy Production and Trade Developments*, *supra* note 162.

sponse to competition concerns, the legislative package approving the merger required divestiture of some assets within twelve months to improve competition in the domestic dairy products markets<sup>166</sup> and also contained provisions for the protection of farmer suppliers and shareholders.<sup>167</sup> Fonterra nevertheless plays a direct role in New Zealand domestic markets beyond that which was played by the former Dairy Board. Under the Ackerman and Dixit classification scheme, this arguably means Fonterra has more power to distort trade than did the Dairy Board.<sup>168</sup>

The New Zealand government's enactment of legislation allowing a merger to establish Fonterra as a monopoly was a clear application of industrial policy, and a prioritizing of industrial policy over antitrust concerns. The government sought to create a national champion exporter to compete with other large dairy companies internationally. The effect on domestic markets was a lesser consideration.<sup>169</sup> In a submission to the Parliamentary Select Committee considering the merger legislation, Fonterra Co-operative group stated that:

Together, the government of New Zealand and the industry have agreed to a new partnership which:

- a. maintains and strengthens competition in New Zealand consumer markets;
- b. strengthens a world class international marketer of New Zealand [d]airy products;
- c. removes huge costs and inefficiencies;

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166. Dairy Industry Restructuring Act, 2001, § 9 (N.Z.).

167. *Id.* at Schedule 1 (provisions required for the new co-op constitution).

168. See ACKERMAN & DIXIT, *supra* note 1, at 17-19. The category into which Fonterra would fall under the Ackerman and Dixit classification is arguable, depending on how the exclusive rights to sell into designated markets are characterized, as well as an assessment of the degree of market power domestically. Fonterra could be classed as either a Type III or a Type IV STE.

169. See FONTERRA, SHAREHOLDER QUESTIONS AND ANSWERS ¶ 1.2(3) [hereinafter QUESTIONS] ("The dairy industry exists primarily to participate in international markets. As New Zealand's economic well being is dependent on the industry remaining a dominant player in international markets, the industry's structure must be designed to provide it with the best chance to prosper in those markets. The domestic market is but a part of the picture."), *at* [http://www.fonterra.com/content/unmanaged/merger\\_archive/news/news\\_cd03.jsp](http://www.fonterra.com/content/unmanaged/merger_archive/news/news_cd03.jsp) (last visited Jan. 26, 2005); see also The Honorable Jim Sutton, Minister of Agriculture, Dairy Industry Restructuring Bill First Reading (June 26, 2001) ("The Bill provides for regulatory and structural reform of the dairy industry, to increase the industry's responsiveness to international markets and to stimulate investment and innovation."), *available at* <http://www.beehive.govt.nz/ViewDocument.cfm?DocumentID=11018>.

- d. maintains New Zealand ownership;
- e. retains farmer control through the co-operative; [and]
- f. ensures New Zealanders, and not foreign customers, will take the benefits of those gains.<sup>170</sup>

The policy was to reform the New Zealand Dairy Board to create an internationally-competitive exporting company, large enough to achieve economies of scale and with the goal of maximizing returns to New Zealand producers and to New Zealand as a nation.<sup>171</sup> Fonterra was to be a national champion, explicitly seeking to maximize returns at the expense of foreign consumers.

The restructuring of the New Zealand Dairy Board into Fonterra provides an example of STE-reform and a case study in the potential extraterritorial application of United States antitrust law to a non-governmental enterprise with STE status. It is also an example of one government's industrial policy goal of creating an exporting company as national champion, and government's exempting the merger from antitrust laws.

The merger and creation of Fonterra was authorized by the Dairy Industry Restructuring Act of 2001.<sup>172</sup> In relation to United States antitrust law, this raises two questions. First, would the merger itself be subject to United States antitrust jurisdiction under the effects test, and second, would it escape jurisdiction under the doctrine of international comity? The merger was granted immunity from New Zealand competition law, but is still subject to scrutiny in other jurisdictions. Here, the merger itself was arguably anticompetitive, and in violation of either Section One of the Sherman Act or Section Seven of the Clayton Act.<sup>173</sup> The merger arguably produced a company with monopsony power in the domestic market for milk from producers, and market power in the supply of milk to consumers. A United States antitrust plaintiff could argue, after *Trugman-Nash*, that the licensing system in the United States creates United States

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170. COMMITTEE, *supra* note 155, at ¶ 1.8.

171. See QUESTIONS, *supra* note 169, at ¶ 1.2(3) (stating that “[t]he dairy industry exists primarily to participate in international markets” and New Zealand’s “economic well being is dependent on the industry remaining a dominant player in international markets”).

172. See Dairy Industry Restructuring Act, 2001, §4 (N.Z.).

173. See WILBUR L. FUGATE, FOREIGN COMMERCE AND THE ANTITRUST LAWS: VOLUME II, 161-62, 166 (5th ed. 1996) (discussing the jurisdictional restrictions of the Clayton Act, which stipulate the requisite effect to be “in any line of commerce or in any activity affecting commerce in any section of the country”. In relation to the section of the country requirement, Fugate concludes “imports certainly qualify, and exports probably do.”).

markets for New Zealand dairy products such as cheese, and that in allowing the merger, the New Zealand government allowed the creation of a monopoly in those United States markets, which is contrary to United States merger law. A plaintiff might also argue that the merger will allow Fonterra to subsidize its exports by raising prices in the domestic market and thereby engage in predatory pricing in the United States market,<sup>174</sup> or that the merger creates a dairy company with market power in the global market for dairy products, and the company can use such market power to raise prices and reduce output into the United States.

In reply, Fonterra would argue that U.S. courts do not have jurisdiction under the effects test and under the doctrines of act of state, foreign sovereign compulsion, and international comity. Under the effects test and the Guidelines, conduct must have a “direct, substantial, and reasonably foreseeable effect” on non-foreign or import trade or commerce.<sup>175</sup>

The doctrine of international comity requires analysis under *Hartford Fire* and *Timberlane*. Under *Hartford Fire*, a court will consider “whether ‘there is in fact a true conflict between domestic and foreign law.’”<sup>176</sup> The merger was authorized and exempted from antitrust scrutiny by the Dairy Industry Restructuring Act of 2001 (“Restructuring Act”).<sup>177</sup> However, from the language of the Restructuring Act, it did not *compel* the dairy cooperatives to merge. One stated purpose of the Restructuring Act was to “allow an amalgamation,” and the effect of the authorization granted was to *permit* the merger, not to *compel* it.<sup>178</sup> The other *Timberlane* factors<sup>179</sup> might tend to favor the merger, however, as it is a New Zealand merger forming a New Zealand company, the principal effects would be felt in New Zealand. However, it is not clear what weight these factors

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174. See, e.g., *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588-90 (1986). However, in such a predatory pricing case it would be difficult to prove harm to United States consumers and to prove ability to recoup lost profits plus interest.

175. 15 U.S.C. § 6a (2000).

176. *Hartford Fire Ins. Co.*, 509 U.S. at 798 (1993) (quoting *Société Nationale Industrielle Aérospatiale v. United States Dist. Court for the S. Dist. of Iowa*, 482 U.S. 522, 555 (1987) (Blackmun, J., concurring in part and dissenting in part)).

177. Dairy Industry Restructuring Act, 2001, § 7 (N.Z.).

178. Dairy Industry Restructuring Act, 2001, § 4 (N.Z.).

179. *Timberlane Lumber Co.*, 549 F.2d at 614-15 (setting out the additional factors to be used in analyzing the effects of a merger as: the nationality or allegiance of the parties and the locations or principal places of business or corporations, the extent to which enforcement by either state can be expected to achieve compliance, the relative significance of effects on the United States as compared with those elsewhere, the extent to which there is explicit purpose to harm or affect American commerce, the foreseeability of such effect, and the relative importance of violations charged of United States conduct as compared with conduct abroad).

would carry in a court as compared to the factor of conflict between the antitrust laws/policies of the two countries. Therefore, if the merger that created a monopoly was itself challenged under Section One of the Sherman Act or Section Seven of the Clayton Act, a court would exclude jurisdiction on grounds of international comity, only if it gave the comity defense a broad interpretation, using the *Timberlane* factors.<sup>180</sup>

The second question is whether United States antitrust jurisdiction extends over Fonterra's price-fixing. In relation to conduct such as the "price-fixing" alleged in *Trugman-Nash I*, the Dairy Industry Restructuring Act clearly grants export licenses to designated markets for "initial periods" and license continuations at reduced amounts.<sup>181</sup> The statute also provides that export rights vest or revert to the Crown, and the Governor-General has power to allocate new licenses by Order in Council made on the recommendation of the Minister.<sup>182</sup> However, if United States customers of Fonterra were to allege cartelization as in *Trugman-Nash I*, the comity defense is likely to apply. There is a strong case that Fonterra is compelled to operate as a single desk seller under the statute. Unlike the Dairy Board, Fonterra has no power to license other exporters. It is an exclusive licensee from the Crown. Thus, although customers are prevented from dealing directly with producers, with "effects" on U.S. consumers, there is in fact a true conflict between U.S. antitrust law and New Zealand law. Further, the statute prohibits transfer, sub-license or other disposal of an initial license in respect of a designated market.<sup>183</sup> In addition, the *Timberlane* factors would favor Fonterra as they favored the Dairy Board in *Trugman-Nash*. Comity is therefore likely to apply.

If an antitrust action were to succeed against the merger or price-fixing, a United States court has broad discretion in relation to remedies and could order divestiture of assets, enjoin conduct, and order damages including treble damages and seize assets in the United States.<sup>184</sup>

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180. See *Hartford Fire Ins. Co.*, 509 U.S. 799 (1993) (stating that lawful conduct in foreign state in which it took place will not, of itself, bar application of United States antitrust laws on the grounds of comity, even though foreign state has strong policy to permit or encourage such conduct).

181. Dairy Industry Restructuring Act, 2001, §§ 24-25 (N.Z.).

182. *Id.* § 26.

183. *Id.* §§ 28-29.

184. See generally FUGATE, *supra* note 75, at 306-33 (discussing jurisdictional questions for relief in foreign trade antitrust cases).

## V. ANTITRUST POLICY: SHOULD UNITED STATES LAW APPLY?

United States antitrust jurisdiction should be excluded in the case of the New Zealand dairy industry. In a broader sense, U.S. antitrust law is not a useful tool for remedying the imperfections in international agricultural markets as they are currently configured. The purpose of antitrust law is to promote competition in markets for the benefit of consumers.<sup>185</sup> Where private power has been substituted for competition, antitrust law intervenes to restore competition.<sup>186</sup> Intervention is therefore only justified where a market would be competitive, or at least more competitive, but for the merger or restraint. World agricultural trade simply does not offer a counterfactual competitive market. Rather, world agricultural trade is characterized by protectionism, subsidies and tariff rate quota.<sup>187</sup> Agricultural export STEs are a response to the distorted character of world agricultural trade.<sup>188</sup> They are used by agricultural exporting nations like New Zealand, and by many developing countries, to improve returns to producers in a protectionist marketplace and thereby attempt to make the playing field a little more level.<sup>189</sup>

The United States uses both subsidies and quotas to protect its domestic producers from competition.<sup>190</sup> In so doing, it chooses to place the interests of its producers above the interests of its consumers, and by limiting output, imposes higher prices on its consumers. The New Zealand case illustrates this point. There exists an output limitation for New Zealand dairy produce in the United States markets, but this output limitation is a creation of United States policy, and it is this output limitation that raises prices to consumers. New Zealand, by contrast, does not subsidize its producers, and sets no import quotas.<sup>191</sup> New Zealand has restructured the dairy industry so that Fonterra operates as an STE only in markets distorted by tariff rate quota, such as the United States market. In this trade context, the United States antitrust laws are the wrong remedy for imperfec-

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185. William J. Kolasky, Using Competition Policy to Promote International Competitiveness, Address Before the American Chamber of Commerce, Seoul, Republic of Korea (Nov. 14, 2002), available at <http://www.usdoj.gov/atr/public/speeches/200485.pdf>.

186. See *id.*

187. See STAFF OF HOUSE COMM. ON AGRIC., *supra* note 97.

188. See PADDOCK, *supra* note 19, at 7.

189. ACKERMAN & DIXIT, *supra* note 1, at 11.

190. See Allen N. Rae, The U.S. Farm Bill 2002: A View from New Zealand, Presented at the AARES 5th Annual Symposium (Sep. 19, 2002), available at [http://econ.massey.ac.nz/caps/UNE\\_Farm\\_Bill.pdf](http://econ.massey.ac.nz/caps/UNE_Farm_Bill.pdf).

191. *New Zealand Notification*, *supra* note 94, at 3-4.

tions in competition. The right remedy is dismantling the tariff rate quota, and this remedy will be achieved, if at all, through trade negotiations rather than through antitrust suits.

Nevertheless, plaintiffs may bring antitrust suits against STEs in United States courts.<sup>192</sup> In such cases, courts should take a broad approach to comity, and apply all of the *Timberlane* factors rather than focusing only on the narrow issue of conflict. *Hartford Fire* does not preclude such an approach.<sup>193</sup> This relatively broad approach to comity seems to allow some scope for the contextual considerations that are an essential element in any assessment of STE antitrust liability, and the result should be exclusion of jurisdiction in such circumstances. If courts do not apply comity, then, at a minimum, STE conduct should not be subject to per se rules, but should be subject to rule of reason analysis that takes into account quota output limitations and other protectionist measures.<sup>194</sup> Application of comity is, however, a better approach.

The author's view is not that extraterritorial antitrust law should never be used to protect consumers in agricultural trade. On the contrary, in the event that agricultural trade is substantially liberalized and STEs with market power are effectively cartelizing a market, antitrust law is available and should be used. United States antitrust law is a useful tool in circumstances where there exists a clear counterfactual competitive market, without quota or similar restrictions, and where United States consumers suffer antitrust injury. However, such actions against STEs are likely to be rare under liberalized trade conditions. Without quota restrictions, courts can be expected to define agricultural product markets more broadly. (For example, the relevant market will be "cheese" rather than "New Zealand cheese"). In markets broadly defined, there will be few STEs with sufficient market power to operate as effective cartels.

There are current proposals to negotiate a multilateral competition law agreement within the World Trade Organization.<sup>195</sup> Such a multilateral agreement formed in a trade context has the potential to be a more balanced instrument

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192. See, e.g., *Hartford Fire Ins. Co.*, 509 U.S. at 794-99 (1993) (refusing to dismiss the suit and allowing application of the Sherman Act).

193. See *id.*

194. See generally Roberts, *supra* note 5, at 311-14 (finding that when addressing policy considerations of STEs, various rules, accommodations and options are needed to adequately address STEs).

195. WORLD TRADE ORGANIZATION, TRADE AND COMPETITION POLICY: WORKING GROUP SET UP BY SINGAPORE MINISTERIAL, at [http://www.wto.org/english/thewto\\_e/minist\\_e/min01\\_e/brief\\_e/brief13\\_e.htm](http://www.wto.org/english/thewto_e/minist_e/min01_e/brief_e/brief13_e.htm) (last visited Jan. 26, 2005).

for resolving disputes over STEs rather than extraterritorial application of United States law.<sup>196</sup> However, to be credible, any such agreement would need to recognize the political and economic context in which international agricultural trade takes place and the concerns of agricultural exporting nations and developing countries in relation to agricultural trade.

## VI. CONCLUSION

United States antitrust law has potential application to export STEs in agricultural trade, as shown by this Article's case study of the former New Zealand Dairy Board and its replacement, Fonterra. A United States court would have jurisdiction over export STEs in situations where there are effects on United States markets, and where the comity doctrine does not apply. At a normative level, in the context of the highly imperfect markets that exist in agricultural trade, antitrust law should only be applied in situations where there exists a clear counterfactual competitive market, free of quota or similar restrictions. At present, protectionist trade measures are the principal barrier to competition in agricultural trade. The comity doctrine should therefore be interpreted broadly in these cases. However, once trade law, or at least United States trade practice, is reformed, antitrust law may well have a useful role to play in promoting competition in agricultural markets.

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196. *See, e.g., id.* (explaining the Group's consideration of many policies and concepts to develop a mutually supported policy).