Addendum to Chapter 1, Sec. 5 [at p. 59], “The Future of Antitrust Law?”

When we wrote the text in 2017, we noted that “the basic framing of antitrust law seems open to question in a way that has not happened seriously since the triumph of economic analysis in antitrust law.” [p. 56]. Several factors prompted that comment, including the growth of the dominant internet-based platforms such as Google, Apple, Facebook, and Amazon—the GAFA—the troublesome growth in income distribution, and a renewed interest in combatting exclusionary practices. We wondered whether there would be a push to deemphasize economics in antitrust analysis and a renewed effort, not seen since the 1950s, to protect small businesses.

Four years later, it is fair to say that the trend we highlighted has become turbocharged. Lawsuits and investigations are currently pending around the world against the GAFA, and the 2020 election of Joe Biden as President is likely to accelerate those trends. On July 9, 2021, President Biden issued an executive order promoting competition in order to preserve “America’s role as the world’s leading economy.”. A number of bills are pending in the U.S. Congress that, if passed, would make the most extensive changes to antitrust law since the passage of the Clayton Act and the Federal Trade Commission Act in 1914.

There has been an outpouring of literature re-examining the classic Chicago School model of antitrust. Some, notably Jonathan B. Baker, THE ANTITRUST PARADIGM: RESTORING A COMPETITIVE ECONOMY (2019), accept the premise that antitrust law should be based on sound economic analysis but argue that current antitrust doctrine has failed to adapt in light of new economic learning over the past few decades. That economic learning includes empirical studies that suggest that market power and industrial concentration have been increasing in recent years. These critics suggest incremental changes to antitrust doctrine, such as reallocating the burden of proof in some merger matters.

Other critics, notably Tim Wu, THE CURSE OF BIGNESS: ANTITRUST IN THE NEW GILDED AGE (2018), go further and advocate broadening antitrust law to take account of other objectives such as equality of economic and political power, in addition to economic

analysis. These critics propose more far-reaching changes to antitrust doctrine, such as breaking up, or restricting vertical integration by, certain large firms with apparently enduring market power without regard to whether they have engaged in the kind of conduct that would be deemed anticompetitive under current law.

Studies of digital markets in particular by government agencies and others have expressed a shared concern as to whether the traditional tools of antitrust are up to the task of regulating the digital economy. These include a March 2019 report in the United Kingdom on Unlocking digital competition; an April 2019 report sponsored by the European Commission on competition policy for the digital era; a July 2019 report by the Stigler Center at Chicago Booth at The University of Chicago; and another July report from the Australian Competition & Consumer Commission as part of its digital platforms inquiry. Although these reports differ in many ways, all express concern about the timelines frequently associated with antitrust cases against tech firms and whether it would better to regulate these firms outside of antitrust with tools more typically associated with public-utilities regulation.

The common thread here is that antitrust is, if anything, even more important to the modern world than it was for the “old economy” of the 20th century, that laissez-faire practices yield anticompetitive outcomes without the antitrust police on the beat, and that antitrust law needs to be reinvigorated. Whether and how this activity will affect antitrust law remains to be seen. It is likely that their debate will give rise to new legal challenges with which the courts will have to wrestle, and there have been several proposals for new legislation to revise or supplement the antitrust laws. In all events, antitrust law is back in the headlines and on politicians’ minds, making possible the first serious discussion of competition policy in a Presidential campaign in a very long time.

Chapter 3: Collaboration Among Competitors

[insert before the discussion of B. Joint Ventures, on page 278]

The Supreme Court last considered the rules of the NCAA in 1984 in National Collegiate Athletic Association v. Board of Regents of the University of Oklahoma, 468 U.S. 85 (1984). In that case, the University of Oklahoma and the University of Georgia challenged restrictions imposed by the NCAA on how frequently schools could have their college football games televised. (There was a world in which Notre Dame wasn’t
on every weekend.) In a 7-2 decision, the Court ruled that the NCAA restrictions violated Section 1 of the Sherman Act. As you read the next case, have in mind the changes that have occurred in college sports and the broader society.

**National Collegiate Athletic Ass’n v. Alston**
United States Supreme Court, 2021.
___ U.S. ___.

Justice GORSUCH, delivered the opinion of the Court. In the Sherman Act, Congress tasked courts with enforcing a policy of competition on the belief that market forces “yield the best allocation” of the Nation’s resources. *National Collegiate Athletic Assn. v. Board of Regents of Univ. of Okla.*, 468 U.S. 85, 104, n. 27 (1984). The plaintiffs before us brought this lawsuit alleging that the National Collegiate Athletic Association (NCAA) and certain of its member institutions violated this policy by agreeing to restrict the compensation colleges and universities may offer the student-athletes who play for their teams. After amassing a vast record and conducting an exhaustive trial, the district court issued a 50-page opinion that cut both ways. The court refused to disturb the NCAA’s rules limiting undergraduate athletic scholarships and other compensation related to athletic performance. At the same time, the court struck down NCAA rules limiting the education-related benefits schools may offer student-athletes—such as rules that prohibit schools from offering graduate or vocational school scholarships. Before us, the student-athletes do not challenge the district court’s judgment. But the NCAA does. In essence, it seeks immunity from the normal operation of the antitrust laws and argues, in any event, that the district court should have approved all of its existing restraints. We took this case to consider those objections.

I

A

*** [In 1929], the Carnegie Foundation produced a report on college athletics that found them still “sodden with the commercial and the material and the vested interests that these forces have created.” H. Savage, The Carnegie Foundation for the Advancement of Teaching, American College Athletics Bull. 23, p. 310 (1929). Schools across the country sought to leverage sports to bring in revenue,
attract attention, boost enrollment, and raise money from alumni. The University of California’s athletic revenue was over $480,000, while Harvard’s football revenue alone came in at $429,000. Id., at 87. College football was “not a student’s game”; it was an “organized commercial enterprise” featuring athletes with “years of training,” “professional coaches,” and competitions that were “highly profitable.” Id., at viii.

The commercialism extended to the market for student-athletes. Seeking the best players, many schools actively participated in a system “under which boys are offered pecuniary and other inducements to enter a particular college.” Id., at xiv-xv. One coach estimated that a rival team “spent over $200,000 a year on players.” A. Zimbalist, Unpaid Professionals 9 (1999). In 1939, freshmen at the University of Pittsburgh went on strike because upperclassmen were reportedly earning more money. Crabb, The Amateurism Myth: A Case for a New Tradition, 28 Stan. L. & Pol’y Rev. 181, 190 (2017). In the 1940s, Hugh McElhenny, a halfback at the University of Washington, “became known as the first college player ‘ever to take a cut in salary to play pro football.’” Zimbalist 22-23. He reportedly said: “[A] wealthy guy puts big bucks under my pillow every time I score a touchdown. Hell, I can’t afford to graduate.” Id., at 211, n. 17. In 1946, a commentator offered this view: “[W]hen it comes to chicanery, double-dealing, and general undercover work behind the scenes, big-time college football is in a class by itself.” Woodward, Is College Football on the Level?, Sport, Nov. 1946, Vol. 1, No. 3, p. 35.

In 1948, the NCAA sought to do more than admonish. It adopted the “Sanity Code.” Colleges Adopt the ‘Sanity Code’ To Govern Sports, N. Y. Times, Jan. 11, 1948, p. 1, col. 1. The code reiterated the NCAA’s opposition to “promised pay in any form.” Hearings before the Subcommittee on Oversight and Investigations of the House Committee on Interstate and Foreign Commerce, 95th Congress, 2d Sess., pt. 2, p. 1094 (1978). But for the first time the code also authorized colleges and universities to pay athletes’ tuition. Ibid. And it created a new enforcement mechanism—providing for the “suspension or expulsion” of “proven offenders.” Colleges Adopt ‘Sanity Code,’ N. Y. Times, p. 1, col. 1. To some, these changes sought to substitute a consistent, above-board compensation system for the varying under-the-table schemes that had long proliferated. To others, the code marked “the beginning of the NCAA behaving as an effective cartel,” by enabling its member schools to set and enforce “rules that
limit the price they have to pay for their inputs (mainly the ‘student-athletes’).” Zimbalist 10.

The rules regarding student-athlete compensation have evolved ever since. In 1956, the NCAA expanded the scope of allowable payments to include room, board, books, fees, and “cash for incidental expenses such as laundry.” In re National Collegiate Athletic Assn. Athletic Grant-in-Aid Cap Antitrust Litig., 375 F. Supp. 3d 1058, 1063 (ND Cal. 2019) (hereinafter D.Ct.Op.). In 1974, the NCAA began permitting paid professionals in one sport to compete on an amateur basis in another. In 2014, the NCAA “announced it would allow athletic conferences to authorize their member schools to increase scholarships up to the full cost of attendance.” O’Bannon v. National Collegiate Athletic Assn., 802 F.3d 1049, 1054-1055 (CA9 2015). The 80 member schools of the “Power Five” athletic conferences—the conferences with the highest revenue in Division I—promptly voted to raise their scholarship limits to an amount that is generally several thousand dollars higher than previous limits. D.Ct.Op., at 1064.

In recent years, changes have continued. The NCAA has created the “Student Assistance Fund” and the “Academic Enhancement Fund” to “assist student-athletes in meeting financial needs,” “improve their welfare or academic support,” or “recognize academic achievement.” Id., at 1072. These funds have supplied money to student-athletes for “postgraduate scholarships” and “school supplies,” as well as “benefits that are not related to education,” such as “loss-of-value insurance premiums,” “travel expenses,” “clothing,” and “magazine subscriptions.” Id., at 1072, n. 15. In 2018, the NCAA made more than $84 million available through the Student Activities Fund and more than $48 million available through the Academic Enhancement Fund. Id., at 1072. Assistance may be provided in cash or in kind, and there is no limit to the amount any particular student-athlete may receive. Id., at 1073. Since 2015, disbursements to individual students have sometimes been tens of thousands of dollars above the full cost of attendance. Ibid.

The NCAA has also allowed payments “incidental to athletics participation,” including awards for “participation or achievement in athletics” (like “qualifying for a bowl game”) and certain “payments from outside entities” (such as for “performance in the Olympics”). Id., at 1064, 1071, 1074. The NCAA permits its member schools to award up to (but no more than) two annual “Senior Scholar Awards” of $10,000 for students to attend graduate school after their athletic eligibility expires. Id., at 1074. Finally, the NCAA allows schools to
fund travel for student-athletes' family members to attend “certain events.” Id., at 1069. ***

The NCAA's current broadcast contract for the March Madness basketball tournament is worth $1.1 billion annually. See id., at 1077, n. 20. Its television deal for the FBS conference's College Football Playoff is worth approximately $470 million per year. See id., at 1063; Bachman, ESPN Strikes Deal for College Football Playoff, Wall Street Journal, Nov. 21, 2012. Beyond these sums, the Division I conferences earn substantial revenue from regular-season games. For example, the Southeastern Conference (SEC) “made more than $409 million in revenues from television contracts alone in 2017, with its total conference revenues exceeding $650 million that year.” D.Ct.Op., at 1063. All these amounts have “increased consistently over the years.” Ibid.

Those who run this enterprise profit in a different way than the student-athletes whose activities they oversee. The president of the NCAA earns nearly $4 million per year. Commissioners of the top conferences take home between $2 to $5 million. College athletic directors average more than $1 million annually. And annual salaries for top Division I college football coaches approach $11 million, with some of their assistants making more than $2.5 million.

B

The plaintiffs are current and former student-athletes in men's Division I FBS football and men's and women's Division I basketball. They filed a class action against the NCAA and 11 Division I conferences (for simplicity's sake, we refer to the defendants collectively as the NCAA). The student-athletes challenged the “current, interconnected set of NCAA rules that limit the compensation they may receive in exchange for their athletic services.” D.Ct.Op., at 1062, 1065, n. 5. Specifically, they alleged that the NCAA's rules violate §1 of the Sherman Act, which prohibits “contract[s], combination[s], or conspirac[ies] in restraint of trade or commerce.” 15 U.S.C. §1.

After pretrial proceedings stretching years, the district court conducted a 10-day bench trial. It heard experts and lay witnesses from both sides, and received volumes of evidence and briefing, all before issuing an exhaustive decision. *** In applying the rule of reason, the district court began by observing that the NCAA enjoys “near complete dominance of, and exercise[s] monopsony power in, the relevant market”—which it defined as the market for “athletic services in men's and women's Division I basketball and FBS football, wherein
each class member participates in his or her sport-specific market.” D.Ct.Op., at 1097. The “most talented athletes are concentrated” in the “markets for Division I basketball and FBS football.” Id., at 1067. There are no “viable substitutes,” as the “NCAA’s Division I essentially is the relevant market for elite college football and basketball.” Id., at 1067, 1070. In short, the NCAA and its member schools have the “power to restrain student-athlete compensation in any way and at any time they wish, without any meaningful risk of diminishing their market dominance.” Id., at 1070.

The district court then proceeded to find that the NCAA’s compensation limits “produce significant anticompetitive effects in the relevant market.” Id., at 1067. Though member schools compete fiercely in recruiting student-athletes, the NCAA uses its monopsony power to “cap artificially the compensation offered to recruits.” Id., at 1097. In a market without the challenged restraints, the district court found, “competition among schools would increase in terms of the compensation they would offer to recruits, and student-athlete compensation would be higher as a result.” Id., at 1068. “Student-athletes would receive offers that would more closely match the value of their athletic services.” Ibid. And notably, the court observed, the NCAA “did not meaningfully dispute” any of this evidence. Id., at 1067; see also Tr. of Oral Arg. 31 (“[T]here’s no dispute that the—the no-pay-for-play rule imposes a significant restraint on a relevant antitrust market”).

The district court next considered the NCAA’s procompetitive justifications for its restraints. The NCAA suggested that its restrictions help increase output in college sports and maintain a competitive balance among teams. But the district court rejected those justifications, D.Ct.Op., at 1070, n. 12, and the NCAA does not pursue them here. The NCAA’s only remaining defense was that its rules preserve amateurism, which in turn widens consumer choice by providing a unique product—amateur college sports as distinct from professional sports. Admittedly, this asserted benefit accrues to consumers in the NCAA’s seller-side consumer market rather than to student-athletes whose compensation the NCAA fixes in its buyer-side labor market. But, the NCAA argued, the district court needed to assess its restraints in the labor market in light of their procompetitive benefits in the consumer market—and the district court agreed to do so. Id., at 1098.

Turning to that task, the court observed that the NCAA’s conception of amateurism has changed steadily over the years. The court noted that the NCAA “nowhere define[s] the nature of the
amateurism they claim consumers insist upon.” *D.Ct.Op.*, at 1070. And, given all this, the court struggled to ascertain for itself “any coherent definition” of the term, id., at 1074, noting the testimony of a former SEC commissioner that he’s “never been clear on . . . what is really meant by amateurism.” Id., at 1070-1071.

Nor did the district court find much evidence to support the NCAA’s contention that its compensation restrictions play a role in consumer demand. As the court put it, the evidence failed “to establish that the challenged compensation rules, in and of themselves, have any direct connection to consumer demand.” Id., at 1070. *** At the same time, however, the district court did find that one particular aspect of the NCAA’s compensation limits “may have some effect in preserving consumer demand.” Id., at 1082. Specifically, the court found that rules aimed at ensuring “student-athletes do not receive unlimited payments unrelated to education” could play some role in product differentiation with professional sports and thus help sustain consumer demand for college athletics. Id., at 1083.

The court next required the student-athletes to show that “substantially less restrictive alternative rules” existed that “would achieve the same procompetitive effect as the challenged set of rules.” Id., at 1104. The district court emphasized that the NCAA must have “ample latitude” to run its enterprise and that courts “may not use antitrust laws to make marginal adjustments to broadly reasonable market restraints.” Ibid. (internal quotation marks omitted). In light of these standards, the court found the student-athletes had met their burden in some respects but not others. The court rejected the student-athletes’ challenge to NCAA rules that limit athletic scholarships to the full cost of attendance and that restrict compensation and benefits unrelated to education. These may be price-fixing agreements, but the court found them to be reasonable in light of the possibility that “professional-level cash payments . . . could blur the distinction between college sports and professional sports and thereby negatively affect consumer demand.” Ibid.

The court reached a different conclusion for caps on education-related benefits—such as rules that limit scholarships for graduate or vocational school, payments for academic tutoring, or paid posteligibility internships. Id., at 1088. On no account, the court found, could such education-related benefits be “confused with a professional athlete’s salary.” Id., at 1083. If anything, they “emphasize that the recipients are students.” Ibid. Enjoining the NCAA’s restrictions on these forms of compensation alone, the court concluded, would be substantially less restrictive than the NCAA’s current rules and yet
fully capable of preserving consumer demand for college sports. Id., at 1088.

The court then entered an injunction reflecting its findings and conclusions. Nothing in the order precluded the NCAA from continuing to fix compensation and benefits unrelated to education; limits on athletic scholarships, for example, remained untouched. The court enjoined the NCAA only from limiting education-related compensation or benefits that conferences and schools may provide to student-athletes playing Division I football and basketball. App. to Pet. for Cert. in No. 20-512, p. 167a, ¶1. The court’s injunction further specified that the NCAA could continue to limit cash awards for academic achievement—but only so long as those limits are no lower than the cash awards allowed for athletic achievement (currently $5,980 annually). The court added that the NCAA and its members were free to propose a definition of compensation or benefits “related to education.” App. to Pet. for Cert. in No. 20-512, at 168a, ¶4. And the court explained that the NCAA was free to regulate how conferences and schools provide education-related compensation and benefits. Ibid. The court further emphasized that its injunction applied only to the NCAA and multi-conference agreements—thus allowing individual conferences (and the schools that constitute them) to impose tighter restrictions if they wish. Id., at 169a, ¶6. The district court’s injunction issued in March 2019, and took effect in August 2020.

Both sides appealed. The student-athletes said the district court did not go far enough; it should have enjoined all of the NCAA’s challenged compensation limits, including those “untethered to education,” like its restrictions on the size of athletic scholarships and cash awards. In re National Collegiate Athletic Assn. Athletic Grant-in-Aid Antitrust Litig., 958 F.3d 1239, 1263 (CA9 2020). The NCAA, meanwhile, argued that the district court went too far by weakening its restraints on education-related compensation and benefits. In the end, the court of appeals affirmed in full, explaining its view that “the district court struck the right balance in crafting a remedy that both prevents anticompetitive harm to Student-Athletes while serving the procompetitive purpose of preserving the popularity of college sports.” Ibid.

C

Unsatisfied with this result, the NCAA asks us to reverse to the extent the lower courts sided with the student-athletes. For their part, the student-athletes do not renew their across-the-board challenge to the NCAA’s compensation restrictions. Accordingly, we do
not pass on the rules that remain in place or the district court’s judgment upholding them. Our review is confined to those restrictions now enjoined.

Before us, as through much of the litigation below, some of the issues most frequently debated in antitrust litigation are uncontested. The parties do not challenge the district court’s definition of the relevant market. They do not contest that the NCAA enjoys monopoly (or, as it’s called on the buyer side, monopsony) control in that labor market—such that it is capable of depressing wages below competitive levels and restricting the quantity of student-athlete labor. Nor does the NCAA dispute that its member schools compete fiercely for student-athletes but remain subject to NCAA-issued-and-enforced limits on what compensation they can offer. Put simply, this suit involves admitted horizontal price fixing in a market where the defendants exercise monopoly control.

Other significant matters are taken as given here too. No one disputes that the NCAA’s restrictions in fact decrease the compensation that student-athletes receive compared to what a competitive market would yield. No one questions either that decreases in compensation also depress participation by student-athletes in the relevant labor market—so that price and quantity are both suppressed. Nor does the NCAA suggest that, to prevail, the plaintiff student-athletes must show that its restraints harm competition in the seller-side (or consumer facing) market as well as in its buyer-side (or labor) market.

Meanwhile, the student-athletes do not question that the NCAA may permissibly seek to justify its restraints in the labor market by pointing to procompetitive effects they produce in the consumer market. Some amici argue that “competition in input markets is incommensurable with competition in output markets,” and that a court should not “trade off” sacrificing a legally cognizable interest in competition in one market to better promote competition in a different one; review should instead be limited to the particular market in which antitrust plaintiffs have asserted their injury. Brief for American Antitrust Institute as Amicus Curiae 3, 11-12. But the parties before us do not pursue this line.

II

A

With all these matters taken as given, we express no views on them. Instead, we focus only on the objections the NCAA does raise.
Principally, it suggests that the lower courts erred by subjecting its compensation restrictions to a rule of reason analysis. In the NCAA’s view, the courts should have given its restrictions at most an “abbreviated deferential review,” Brief for Petitioner in No. 20-512, p. 14, or a “quick look,” Brief for Petitioners in No. 20-520, p. 18, before approving them. ***

The NCAA accepts that its members collectively enjoy monopsony power in the market for student-athlete services, such that its restraints can (and in fact do) harm competition. See D.Ct.Op., at 1067. Unlike customers who would look elsewhere when a small van company raises its prices above market levels, the district court found (and the NCAA does not here contest) that student-athletes have nowhere else to sell their labor. Even if the NCAA is a joint venture, then, it is hardly of the sort that would warrant quick-look approval for all its myriad rules and restrictions.

Nor does the NCAA’s status as a particular type of venture categorically exempt its restraints from ordinary rule of reason review. We do not doubt that some degree of coordination between competitors within sports leagues can be procompetitive. Without some agreement among rivals—on things like how many players may be on the field or the time allotted for play—the very competitions that consumers value would not be possible. See Board of Regents, 468 U.S., at 101 (quoting R. Bork, The Antitrust Paradox 278 (1978)). Accordingly, even a sports league with market power might see some agreements among its members win antitrust approval in the “twinkling of an eye.” American Needle, 560 U.S., at 203.

But this insight does not always apply. That some restraints are necessary to create or maintain a league sport does not mean all "aspects of elaborate interleague cooperation are." Id., at 199, n. 7. While a quick look will often be enough to approve the restraints “necessary to produce a game,” ibid., a fuller review may be appropriate for others.

The NCAA’s rules fixing wages for student-athletes fall on the far side of this line. Nobody questions that Division I basketball and FBS football can proceed (and have proceeded) without the education-related compensation restrictions the district court enjoined; the games go on. Instead, the parties dispute whether and to what extent those restrictions in the NCAA’s labor market yield benefits in its consumer market that can be attained using substantially less restrictive means. That dispute presents complex questions requiring more than a blink to answer.
B

Even if background antitrust principles counsel in favor of the rule of reason, the NCAA replies that a particular precedent ties our hands. The NCAA directs our attention to Board of Regents, where this Court considered the league’s rules restricting the ability of its member schools to televise football games. 468 U.S., at 94. *** Given the sensitivity of antitrust analysis to market realities—and how much has changed in this market—we think it would be particularly unwise to treat an aside in Board of Regents as more than that. ***

C

The NCAA submits that a rule of reason analysis is inappropriate for still another reason—because the NCAA and its member schools are not “commercial enterprises” and instead oversee intercollegiate athletics “as an integral part of the undergraduate experience.” The NCAA represents that it seeks to “maintain amateurism in college sports as part of serving [the] societally important non-commercial objective” of “higher education.” Id., at 3.

Here again, however, there may be less of a dispute than meets the eye. The NCAA does not contest that its restraints affect interstate trade and commerce and are thus subject to the Sherman Act. *** Nor, on the other side of the equation, does anyone contest that the status of the NCAA’s members as schools and the status of student-athletes as students may be relevant in assessing consumer demand as part of a rule of reason review.

With this much agreed it is unclear exactly what the NCAA seeks. To the extent it means to propose a sort of judicially ordained immunity from the terms of the Sherman Act for its restraints of trade—that we should overlook its restrictions because they happen to fall at the intersection of higher education, sports, and money—we cannot agree. ***

III

A

While the NCAA devotes most of its energy to resisting the rule of reason in its usual form, the league lodges some objections to the district court’s application of it as well. When describing the rule of reason, this Court has sometimes spoken of “a three-step, burden-shifting framework” as a means for “distinguish[ing] between
restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest.” American Express Co., 585 U. S., at ___ (slip op., at 9). As we have described it, “the plaintiff has the initial burden to prove that the challenged restraint has a substantial anticompetitive effect.” Ibid. Should the plaintiff carry that burden, the burden then “shifts to the defendant to show a procompetitive rationale for the restraint.” Ibid. If the defendant can make that showing, “the burden shifts back to the plaintiff to demonstrate that the procompetitive efficiencies could be reasonably achieved through less anticompetitive means.” Id., at __-___ (slip op., at 9-10). ***

In the proceedings below, the district court followed circuit precedent to apply a multistep framework closely akin to American Express’s. As its first step, the district court required the student-athletes to show that “the challenged restraints produce significant anticompetitive effects in the relevant market.” D.Ct.Op., at 1067. This was no slight burden. According to one amicus, courts have disposed of nearly all rule of reason cases in the last 45 years on the ground that the plaintiff failed to show a substantial anticompetitive effect. Brief for 65 Professors of Law, Business, Economics, and Sports Management as Amici Curiae 21, n. 9 (“Since 1977, courts decided 90% (809 of 897) on this ground”). This suit proved different. As we have seen, based on a voluminous record, the district court held that the student-athletes had shown the NCAA enjoys the power to set wages in the market for student-athletes’ labor—and that the NCAA has exercised that power in ways that have produced significant anticompetitive effects. See D.Ct.Op., at 1067. Perhaps even more notably, the NCAA “did not meaningfully dispute” this conclusion. Ibid.

Unlike so many cases, then, the district court proceeded to the second step, asking whether the NCAA could muster a procompetitive rationale for its restraints. Id., at 1070. This is where the NCAA claims error first crept in. On its account, the district court examined the challenged rules at different levels of generality. At the first step of its inquiry, the court asked whether the NCAA’s entire package of compensation restrictions has substantial anticompetitive effects collectively. Yet, at the second step, the NCAA says the district court required it to show that each of its distinct rules limiting student-athlete compensation has procompetitive benefits individually. The NCAA says this mismatch had the result of effectively—and erroneously—requiring it to prove that each rule is the least restrictive means of achieving the procompetitive purpose of differentiating college sports and preserving demand for them.
We agree with the NCAA’s premise that antitrust law does not require businesses to use anything like the least restrictive means of achieving legitimate business purposes. *** Even worse, “[r]ules that seek to embody every economic complexity and qualification may well, through the vagaries of administration, prove counter-productive, undercutting the very economic ends they seek to serve.” Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 234 (CA1 1983) (BREYER, J.). After all, even “[u]nder the best of circumstances,” applying the antitrust laws “can be difficult”—and mistaken condemnations of legitimate business arrangements “are especially costly, because they chill the very” procompetitive conduct “the antitrust laws are designed to protect.” Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 414 (2004). ***

While we agree with the NCAA’s legal premise, we cannot say the same for its factual one. Yes, at the first step of its inquiry, the district court held that the student-athletes had met their burden of showing the NCAA’s restraints collectively bear an anticompetitive effect. And, given that, yes, at step two the NCAA had to show only that those same rules collectively yield a procompetitive benefit. The trouble for the NCAA, though, is not the level of generality. It is the fact that the district court found unpersuasive much of its proffered evidence. See D.Ct.Op., at 1070-1076, 1080-1083. Recall that the court found the NCAA failed “to establish that the challenged compensation rules . . . have any direct connection to consumer demand.” Id., at 1070.

***[W]e see nothing about the district court’s analysis that offends the legal principles the NCAA invokes. The court’s judgment ultimately turned on the key question at the third step: whether the student-athletes could prove that “substantially less restrictive alternative rules” existed to achieve the same procompetitive benefits the NCAA had proven at the second step. Ibid. Of course, deficiencies in the NCAA’s proof of procompetitive benefits at the second step influenced the analysis at the third. But that is only because, however framed and at whichever step, anticompetitive restraints of trade may wind up flunking the rule of reason to the extent the evidence shows that substantially less restrictive means exist to achieve any proven procompetitive benefits.

Simply put, the district court nowhere—expressly or effectively—required the NCAA to show that its rules constituted the least restrictive means of preserving consumer demand. Rather, it was only after finding the NCAA’s restraints “patently and inexplicably stricter than is necessary” to achieve the procompetitive benefits the league had demonstrated that the district court proceeded to declare a

B

In a related critique, the NCAA contends the district court “impermissibly redefined” its “product” by rejecting its views about what amateurism requires and replacing them with its preferred conception. Brief for Petitioner in No. 20-512, at 35-36.

This argument, however, misapprehends the way a defendant’s procompetitive business justification relates to the antitrust laws. Firms deserve substantial latitude to fashion agreements that serve legitimate business interests—agreements that may include efforts aimed at introducing a new product into the marketplace. But none of that means a party can relabel a restraint as a product feature and declare it “immune from §1 scrutiny.” \textit{American Needle}, 560 U.S., at 199, n. 7. ***

The NCAA’s argument not only misapprehends the inquiry, it would require us to overturn the district court’s factual findings. While the NCAA asks us to defer to its conception of amateurism, the district court found that the NCAA had not adopted any consistent definition. Instead, the court found, the NCAA’s rules and restrictions on compensation have shifted markedly over time. The court found, too, that the NCAA adopted these restrictions without any reference to “considerations of consumer demand,” id., at 1100, and that some were “not necessary to preserve consumer demand,” id., at 1075, 1080, 1104. None of this is product redesign; it is a straightforward application of the rule of reason.

C

Finally, the NCAA attacks as “indefensible” the lower courts’ holding that substantially less restrictive alternatives exist capable of delivering the same procompetitive benefits as its current rules. Brief for Petitioner in No. 20-512, at 46. The NCAA claims, too, that the district court’s injunction threatens to “micromanage” its business. Id., at 50.

Once more, we broadly agree with the legal principles the NCAA invokes. As we have discussed, antitrust courts must give wide berth to business judgments before finding liability. Similar considerations apply when it comes to the remedy. Judges must be sensitive to the possibility that the “continuing supervision of a highly
detailed decree” could wind up impairing rather than enhancing competition. *Trinko*, 540 U.S., at 415. Costs associated with ensuring compliance with judicial decrees may exceed efficiencies gained; the decrees themselves may unintentionally suppress procompetitive innovation and even facilitate collusion. Judges must be wary, too, of the temptation to specify “the proper price, quantity, and other terms of dealing”—cognizant that they are neither economic nor industry experts. *Trinko*, 540 U.S., at 408. Judges must be open to reconsideration and modification of decrees in light of changing market realities, for “what we see may vary over time.” *California Dental*, 526 U.S., at 781. And throughout courts must have a healthy respect for the practical limits of judicial administration: “An antitrust court is unlikely to be an effective day-to-day enforcer” of a detailed decree, able to keep pace with changing market dynamics alongside a busy docket. *Trinko*, 540 U.S., at 415. Nor should any court “‘impose a duty . . . that it cannot explain or adequately and reasonably supervise.’” Ibid. In short, judges make for poor “central planners” and should never aspire to the role. Id., at 408.

Once again, though, we think the district court honored these principles. The court enjoined only restraints on education-related benefits—such as those limiting scholarships for graduate school, payments for tutoring, and the like. The court did so, moreover, only after finding that relaxing these restrictions would not blur the distinction between college and professional sports and thus impair demand—and only after finding that this course represented a significantly (not marginally) less restrictive means of achieving the same procompetitive benefits as the NCAA’s current rules.

Even with respect to education-related benefits, the district court extended the NCAA considerable leeway. As we have seen, the court provided that the NCAA could develop its own definition of benefits that relate to education and seek modification of the court’s injunction to reflect that definition. The court explained that the NCAA and its members could agree on rules regulating how conferences and schools go about providing these education-related benefits. The court said that the NCAA and its members could continue fixing education-related cash awards, too—so long as those “limits are never lower than the limit” on awards for athletic performance. D.Ct.Op., at 1104. And the court emphasized that its injunction applies only to the NCAA and multiconference agreements; individual conferences remain free to reimpose every single enjoined restraint tomorrow—or more restrictive ones still.
In the end, it turns out that the NCAA’s complaints really boil down to three principal objections.

First, the NCAA worries about the district court’s inclusion of paid posteligibility internships among the education-related benefits it approved. The NCAA fears that schools will use internships as a way of circumventing limits on payments that student-athletes may receive for athletic performance. *** The court refused to enjoin NCAA rules prohibiting its members from providing compensation or benefits unrelated to legitimate educational activities—thus leaving the league room to police phony internships. As we’ve observed, the district court also allowed the NCAA to propose (and enforce) rules defining what benefits do and do not relate to education. Accordingly, the NCAA may seek whatever limits on paid internships it thinks appropriate. And, again, the court stressed that individual conferences may restrict internships however they wish. All these features underscore the modesty of the current decree.

Second, the NCAA attacks the district court’s ruling that it may fix the aggregate limit on awards schools may give for “academic or graduation” achievement no lower than its aggregate limit on parallel athletic awards (currently $5,980 per year). D.Ct.Op., at 1104. This, the NCAA asserts, “is the very definition of a professional salary.” Brief for Petitioner in No. 20-512, at 48. The NCAA also represents that “[m]ost” of its currently permissible athletic awards are “for genuine individual or team achievement” and that “[m]ost . . . are received by only a few student-athletes each year.” Ibid. Meanwhile, the NCAA says, the district court’s decree would allow a school to pay players thousands of dollars each year for minimal achievements like maintaining a passing GPA.

The basis for this critique is unclear. The NCAA does not believe that the athletic awards it presently allows are tantamount to a professional salary. And this portion of the injunction sprang directly from the district court’s finding that the cap on athletic participation awards “is an amount that has been shown not to decrease consumer demand.” D.Ct.Op., at 1088. Indeed, there was no evidence before the district court suggesting that corresponding academic awards would impair consumer interest in any way. Again, too, the district court’s injunction affords the NCAA leeway. It leaves the NCAA free to reduce its athletic awards. And it does not ordain what criteria schools must use for their academic and graduation awards. So, once more, if the NCAA believes certain criteria are needed to ensure that academic awards are legitimately related to education, it is presently free to
propose such rules—and individual conferences may adopt even stricter ones.

Third, the NCAA contends that allowing schools to provide in-kind educational benefits will pose a problem. This relief focuses on allowing schools to offer scholarships for “graduate degrees” or “vocational school” and to pay for things like “computers” and “tutoring.” App. to Pet. for Cert. in No. 20-512, at 167a-168a, ¶2. But the NCAA fears schools might exploit this authority to give student-athletes “luxury cars” “to get to class” and “other unnecessary or inordinately valuable items” only “nominally” related to education. Brief for Petitioner in No. 20-512, at 48-49.

Again, however, this over-reads the injunction in ways we have seen and need not belabor. Under the current decree, the NCAA is free to forbid in-kind benefits unrelated to a student’s actual education; nothing stops it from enforcing a “no Lamborghini” rule. And, again, the district court invited the NCAA to specify and later enforce rules delineating which benefits it considers legitimately related to education. To the extent the NCAA believes meaningful ambiguity really exists about the scope of its authority—regarding internships, academic awards, in-kind benefits, or anything else—it has been free to seek clarification from the district court since the court issued its injunction three years ago. The NCAA remains free to do so today. To date, the NCAA has sought clarification only once—about the precise amount at which it can cap academic awards—and the question was quickly resolved. Before conjuring hypothetical concerns in this Court, we believe it best for the NCAA to present any practically important question it has in district court first.

When it comes to fashioning an antitrust remedy, we acknowledge that caution is key. Judges must resist the temptation to require that enterprises employ the least restrictive means of achieving their legitimate business objectives. Judges must be mindful, too, of their limitations—as generalists, as lawyers, and as outsiders trying to understand intricate business relationships. Judges must remain aware that markets are often more effective than the heavy hand of judicial power when it comes to enhancing consumer welfare. And judges must be open to clarifying and reconsidering their decrees in light of changing market realities. Courts reviewing complex business arrangements should, in other words, be wary about invitations to “set sail on a sea of doubt.” United States v. Addyston Pipe & Steel Co., 85 F. 271, 284 (CA6 1898) (Taft, J.). But we do not believe the district court fell prey to that temptation. Its judgment does not float on a sea of doubt but stands on firm ground—an exhaustive
factual record, a thoughtful legal analysis consistent with established antitrust principles, and a healthy dose of judicial humility.

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The judgment is Affirmed.

Justice KAVANAUGH, concurring: *** I join the Court’s excellent opinion in full. But this case involves only a narrow subset of the NCAA’s compensation rules—namely, the rules restricting the education-related benefits that student athletes may receive, such as post-eligibility scholarships at graduate or vocational schools. The rest of the NCAA’s compensation rules are not at issue here and therefore remain on the books. Those remaining compensation rules generally restrict student athletes from receiving compensation or benefits from their colleges for playing sports. And those rules have also historically restricted student athletes from receiving money from endorsement deals and the like.

I add this concurring opinion to underscore that the NCAA’s remaining compensation rules also raise serious questions under the antitrust laws. Three points warrant emphasis.

First, the Court does not address the legality of the NCAA’s remaining compensation rules. *** Second, although the Court does not weigh in on the ultimate legality of the NCAA’s remaining compensation rules, the Court’s decision establishes how any such rules should be analyzed going forward. After today’s decision, the NCAA’s remaining compensation rules should receive ordinary “rule of reason” scrutiny under the antitrust laws. *** Third, there are serious questions whether the NCAA’s remaining compensation rules can pass muster under ordinary rule of reason scrutiny. Under the rule of reason, the NCAA must supply a legally valid procompetitive justification for its remaining compensation rules. As I see it, however, the NCAA may lack such a justification.

The NCAA acknowledges that it controls the market for college athletes. The NCAA concedes that its compensation rules set the price of student athlete labor at a below-market rate. And the NCAA recognizes that student athletes currently have no meaningful ability to negotiate with the NCAA over the compensation rules.

The NCAA nonetheless asserts that its compensation rules are procompetitive because those rules help define the product of college sports. Specifically, the NCAA says that colleges may decline to pay student athletes because the defining feature of college sports, according to the NCAA, is that the student athletes are not paid.
In my view, that argument is circular and unpersuasive. The NCAA couches its arguments for not paying student athletes in innocuous labels. But the labels cannot disguise the reality: The NCAA’s business model would be flatly illegal in almost any other industry in America. All of the restaurants in a region cannot come together to cut cooks’ wages on the theory that “customers prefer” to eat food from low-paid cooks. Law firms cannot conspire to cabin lawyers’ salaries in the name of providing legal services out of a “love of the law.” Hospitals cannot agree to cap nurses’ income in order to create a “purer” form of helping the sick. News organizations cannot join forces to curtail pay to reporters to preserve a “tradition” of public-minded journalism. Movie studios cannot collude to slash benefits to camera crews to kindle a “spirit of amateurism” in Hollywood.

Price-fixing labor is price-fixing labor. And price-fixing labor is ordinarily a textbook antitrust problem because it extinguishes the free market in which individuals can otherwise obtain fair compensation for their work. See, e.g., Texaco Inc. v. Dagher, 547 U.S. 1, 5 (2006). Businesses like the NCAA cannot avoid the consequences of price-fixing labor by incorporating price-fixed labor into the definition of the product. Or to put it in more doctrinal terms, a monopsony cannot launder its price-fixing of labor by calling it product definition.

The bottom line is that the NCAA and its member colleges are suppressing the pay of student athletes who collectively generate billions of dollars in revenues for colleges every year. Those enormous sums of money flow to seemingly everyone except the student athletes. College presidents, athletic directors, coaches, conference commissioners, and NCAA executives take in six- and seven-figure salaries. Colleges build lavish new facilities. But the student athletes who generate the revenues, many of whom are African American and from lower-income backgrounds, end up with little or nothing. See Brief for African American Antitrust Lawyers as Amici Curiae 13-17.

Everyone agrees that the NCAA can require student athletes to be enrolled students in good standing. But the NCAA’s business model of using unpaid student athletes to generate billions of dollars in revenue for the colleges raises serious questions under the antitrust laws. In particular, it is highly questionable whether the NCAA and its member colleges can justify not paying student athletes a fair share of the revenues on the circular theory that the defining characteristic of college sports is that the colleges do not pay student athletes. And if that asserted justification is unavailing, it is not clear how the NCAA can legally defend its remaining compensation rules.
If it turns out that some or all of the NCAA’s remaining compensation rules violate the antitrust laws, some difficult policy and practical questions would undoubtedly ensue. Among them: How would paying greater compensation to student athletes affect non-revenue-raising sports? Could student athletes in some sports but not others receive compensation? How would any compensation regime comply with Title IX? If paying student athletes requires something like a salary cap in some sports in order to preserve competitive balance, how would that cap be administered? And given that there are now about 180,000 Division I student athletes, what is a financially sustainable way of fairly compensating some or all of those student athletes?

Of course, those difficult questions could be resolved in ways other than litigation. Legislation would be one option. Or colleges and student athletes could potentially engage in collective bargaining (or seek some other negotiated agreement) to provide student athletes a fairer share of the revenues that they generate for their colleges, akin to how professional football and basketball players have negotiated for a share of league revenues. Cf. Brown v. Pro Football, Inc., 518 U.S. 231, 235-237 (1996); Wood v. National Basketball Assn., 809 F. 2d 954, 958-963 (CA2 1987) (R. Winter, J.). Regardless of how those issues ultimately would be resolved, however, the NCAA’s current compensation regime raises serious questions under the antitrust laws.

To be sure, the NCAA and its member colleges maintain important traditions that have become part of the fabric of America—game days in Tuscaloosa and South Bend; the packed gyms in Storrs and Durham; the women’s and men’s lacrosse championships on Memorial Day weekend; track and field meets in Eugene; the spring softball and baseball World Series in Oklahoma City and Omaha; the list goes on. But those traditions alone cannot justify the NCAA’s decision to build a massive money-raising enterprise on the backs of student athletes who are not fairly compensated. Nowhere else in America can businesses get away with agreeing not to pay their workers a fair market rate on the theory that their product is defined by not paying their workers a fair market rate. And under ordinary principles of antitrust law, it is not evident why college sports should be any different. The NCAA is not above the law.

NOTES AND QUESTIONS

1. The Framing of the Case. Litigants frame their cases, and courts then decide the cases presented to them by the litigants. That of course is generally true, but that point is especially important when litigants
anticipate that change in the challenged conduct may need to come incrementally if it is to come at all. And of course, the court system is just one possible place of redress, and court decisions and the outcomes that they generate may in turn shape the actions that Congress and state legislatures take. And the positions that litigants take may evolve as a case works its way through various appeals. Note here the distinction between compensation and benefits related to education and those that are not related to education. The student-athletes had challenged both sets of restrictions in the lower courts but had limited their challenge in the Supreme Court to only the restrictions on education-related benefits. Justice Kavanaugh’s concurrence emphasizes that point as well as he sets out a potential roadmap for future litigation after Alston.

2. The role of consumer demand. One of the central issues in the 1984 Board of Regents case and in Alston is the role of amateurism in college sports. The district court’s factual findings on this were detailed and nuanced. The district court rejected the contention that the NCAA’s restrictions on education-related benefits played a role in sustaining demand for college sports. The court noted that interest in the college sports in issue in the case—Division I FBS football and Division I men’s and women’s basketball—had grown even as additional funds related to education flowed to the student-athletes participating in those sports. The district court did find that rules blocking unlimited payments to these athletes might serve to keep these college sports in a separate market from their professional counterparts.

3. Per se illegality v. quick look v. the rule of reason. Note the fact that the NCAA thought that the case could be resolved in its favor under an abbreviated quick-look analysis. There is a way in which that should seem remarkable to you. A natural characterization of the NCAA here is that it was operating as a buyer-side cartel limiting the price at which it was buying labor, and you might think that would be per se illegal. As a general matter, we don’t let cartels defend their behavior by saying that there are good reasons for their otherwise forbidden behavior. What explains the posture that the NCAA was taking in the case? How would you frame the depth of the analysis that the Court seems to contemplate after Alston, especially given the idea that the Court appears to believe that the NCAA should have latitude in running its operations?

4. Immunity? Note that the NCAA argued that its restrictions should be immune from antitrust inquiry because of the “non-commercial objective” of higher education. The Supreme Court understandably and appropriately dispensed with that quickly, again, consistent with the idea that we don’t allow market participants to assert that they are in some sense “good” and therefore should be given a subsidy by allowing them to violate otherwise applicable antitrust laws. But many other jurisdictions are now addressing themselves to two of the most salient social problems of our age—environmental sustainability and extreme and growing
inequality of wealth and income—and they are considering whether and how to use competition law as one tool. Are these issues off the table for U.S. antitrust? Is that a good or bad thing?

5. Cross-market effects? A frequent criticism of the Supreme Court’s 2018 decision in *American Express* is that it forces plaintiff's to do more than just show price increases in a particular market (in that case, increases in the fees that Amex was charging to merchants): “Evidence of a price increase in one side of a two-sided transaction platform cannot by itself demonstrate an anticompetitive exercise of market power.” However one wants to characterize the institutional arrangement in *Alston*, there clearly is no transaction platform of the sort at stake in *American Express*. But the doctrinal spillover from *American Express* means that parties are sensitive to the litigation posture of multiple markets presented in a single case. Here the relevant markets are (1) the consumers of the relevant sports and (2) the schools as buyers in the labor side of the market, where the student-athletes are the suppliers. Be sure to focus on the positions the parties took on these cross-market issues in the case and how that framed how the Supreme Court addressed these issues.

6. Building back better? One university—call it Ivy U.—announces that it believes in amateur sports and that, going forward, it will provide to its student-athletes no more than cost of education and other awards like those available to non-athletes. Any problem so far? Suppose that it takes the next step and says that it will only compete against schools with similar views. OK? Suppose a group of those schools take the next step and form an organization to set the rules for the conduct of that product in competition with one another. They will make no effort to coerce other schools to offer the same arrangements. Is that all fine? Or would you say that this should be characterized as “horizontal price fixing in a market where the defendants exercise monopoly control?” If you think it’s ok, how is it different from what defendants did in *Alston*?

7. NIL. Prodded by state legislation and possible looming federal legislation, in July 2021, new NCAA interim rules on names, images and likenesses (NIL) have gone into effect. The response has been dramatic with a number of prominent college athletes likely to earn more than $1 million over the next year. How, if at all, should the NIL issue play into the path forward on high-end college athletics?

**CHAPTER 6: Mergers**

**Note on Hart-Scott-Rodino Pre-Merger Notification**

[at the end of p. 645, before 5. The State of Merger Activity and Enforcement]

On August 3, 2021, Holly Vedova, the Acting Director of the Bureau of Competition, announced on the FTC’s website that the FTC
was changing how it approached the pre-merger notification regime under the Hart-Scott-Rodino Act. The statement noted the rise in merger filings and the FTC’s limited resources to process the notifications. Because the FTC would therefore in some cases not be able to conduct full investigations of mergers in a timely manner, the FTC would notify the parties that they would be permitted close the transactions “at their own risk.” The form letter provides in pertinent part as follows:

“Please be advised that if the parties consummate this transaction before the Commission has completed its investigation, they would do so at their own risk. Any inaction by the Commission before the expiration of the waiting period should not be construed as a determination regarding the lawfulness of the transaction. Indeed, no such determination could be made unless and until the Commission completes its investigation. The parties cannot stop the investigation or avoid an enforcement action by consummating. To the contrary, and in keeping with its commitment to aggressive enforcement, the Commission may challenge transactions—before or after their consummation—that threaten to reduce competition and harm consumers, workers, and honest businesses.

“Accordingly, even if the parties consummate the above-referenced transaction, the Commission may still take further action as the public interest may require, which may include any and all available legal actions and seeking any and all appropriate remedies.”

Critics of the new policy have expressed concern that it will undermine the objectives of the Hart-Scott-Rodino Act to prevent anticompetitive mergers, instead of requiring disruptive and ineffective remedies after deals are consummated, and to give businesses and their customers, suppliers and employees valuable certainty about the lawfulness of the transactions. Critics are also concerned that the resulting uncertainty will deter procompetitive mergers.

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Note on Sprint/T-Mobile

[at the end of p. 734, after the Notes on Maverick Firms]

The wireless marketplace is a valuable case study in merger law. In August of 2011, the Justice Department sued to block the merger of AT&T, then the second-largest wireless provider, and T-Mobile, then the fourth-largest wireless provider. In that case, the Justice Department defined the market as comprised of the four national wireless services, namely, AT&T, T-Mobile, Verizon, and Sprint. In its Complaint, the Department cited the level of concentration in this market (an HHI above 3100) as well as that “the innovation that an independent T-Mobile brings to the market – as reflected in the array of industry ‘firsts’ it has introduced in the past, such as the first Android phone, Blackberry e-mail, and the Sidekick – would also be lost, depriving consumers of important benefits.” Shortly after the Department filed suit, AT&T abandoned its merger of T-Mobile.

In the wake of the Department’s action, Antitrust Division Chief Bill Baer celebrated the importance of preserving competition in wireless and T-Mobile’s role as a maverick. As he stated with regard to preserving an independent T-Mobile, “[t]his really demonstrates that competition can work. . . When you have feisty rivals whose survival depends on innovating and differentiating, they can gain market share and loosen the oligopoly. That’s exactly what T-Mobile has done.” Following this line of thinking, Baer and FCC Chair Tom Wheeler discouraged Sprint from merging with T-Mobile in 2014. After merger talks fell through, Wheeler celebrated the outcome, stating “four national wireless providers is good for American consumers. . . Sprint now has an opportunity to focus its efforts on robust competition.”

In 2018, T-Mobile and Sprint decided to merge, arguing that the consolidation would enable them to compete more effectively with the top two providers, Verizon and AT&T. The status of the merger remains unresolved as of this writing. In the spring of 2019, Federal Communications Commission Chairman Ajit Pai concluded that the

4 Gina Chon, *FCC’s Tom Wheeler Applauds Collapse of T-Mobile-Sprint Deal*, Financial Times https://www.ft.com/content/64872a46-f8c0-11e3-815f-00144feabdc0
merger was procompetitive, stating that he supported approving the transaction, citing commitments from the merging parties to deploy a wireless broadband network (using “5G” technology) that would cover 97% of the U.S. population within three years of consummating the merger. By contrast, a number of State Attorneys General sued to challenge the transaction, concluding that “[d]irect competition between Sprint and T-Mobile has led to lower prices, higher quality service, and more features for consumers [and that, if] consummated, the merger will eliminate the competition between Sprint and T-Mobile and will increase the ability of the three remaining MNOs to coordinate on pricing.” The Justice Department, however, approved the merger on the basis of the merged firms’ commitment to divest significant assets (including spectrum and their pre-paid services business) and provide wholesale support to DISH Network, which indicated its interest in using these assets to build a nationwide wireless broadband network. The State Attorneys General concluded that DISH was unlikely to emerge as an effective competitor to the three major surviving providers, rejected the settlement, and filed suit to block the merger.

After a full trial, the district court rejected the States’ challenges to the Sprint/T-Mobile merger, taking what might be described as a pragmatic—albeit unconventional—approach to merger law. The unconventional aspect of the district court’s ruling was that it concluded that the merger triggered the “structural presumption”—meaning it was facially anticompetitive—but nonetheless did not violate the Clayton Act. To reach this conclusion, the court invoked a number of practical business issues, including its conclusion that Sprint was a “weakened competitor.” The court also invoked the efficiency defense and the Justice Department-ordered remedy as reasons to uphold the merger. In short, the district court relied on a combination of factors rarely invoked—a weakened competitor

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5 https://www.cnbc.com/2019/05/20/fcc-will-not-formally-approve-t-mobile-sprint-merger-on-monday-because-it-must-still-draft-order-reuters.html


defense, an efficiency defense, and a “fix” to the merger—to uphold the merger and overcome the structurally presumption.

**United States v. AT&T, Inc.**

United States Court of Appeals, District of Columbia Circuit, 2019.

916 F.3d 1029.

[insert after discussion of the Comcast/NBC merger, on page 829]

ROGERS, Circuit Judge. On October 22, 2016, AT&T Inc. announced a proposed merger with Time Warner Inc. The government sued to enjoin this vertical merger under Section 7 of the Clayton Act, 15 U.S.C. § 18, and now appeals the denial of its request for a permanent injunction. . . . [T]he government on appeal challenges only the district court’s findings on its increased leverage theory whereby costs for Turner Broadcasting System’s content would increase after the merger, principally through threats of long-term “blackouts” during affiliate negotiations.

At trial, the government presented expert opinion on the likely anticompetitive effects of the proposed merger on the video programming and distribution industry as forecast by economic principles and a quantitative model. It also presented statements by the defendants in administrative proceedings about the anticompetitive effects of a proposed vertical merger in the industry seven years earlier. The defendants responded with an expert’s analysis of real-world data for prior vertical mergers in the industry that showed “no statistically significant effect on content prices.” The government offered no comparable analysis of data and its expert opinion and modeling predicting such increases failed to take into account Turner Broadcasting System’s post-litigation irrevocable offers of no-blackout arbitration agreements, which a government expert acknowledged would require a new model. Evidence also indicated that the industry had become dynamic in recent years with the emergence, for example, of Netflix and Hulu. In this evidentiary context, the government’s objections that the district court misunderstood and misapplied economic principles and clearly erred in rejecting the quantitative model are unpersuasive. Accordingly, we affirm.
Neither the government nor the defendants challenge application of the burden-shifting framework in United States v. Baker Hughes, 908 F.2d 981, 982-83 (D.C. Cir. 1990), for horizontal mergers that the district court applied to consider the effect of the proposed vertical merger of AT&T and Time Warner on competition. Under this framework, the government must first establish a prima facie case that the merger is likely to substantially lessen competition in the relevant market. But unlike horizontal mergers, the government cannot use a short cut to establish a presumption of anticompetitive effect through statistics about the change in market concentration, because vertical mergers produce no immediate change in the relevant market share. . . . Instead, the government must make a “fact-specific” showing that the proposed merger is “likely to be anticompetitive.” Joint Statement on the Burden of Proof at Trial at 3-4. Once the prima facie case is established, the burden shifts to the defendant to present evidence that the prima facie case “inaccurately predicts the relevant transaction’s probable effect on future competition” or to “sufficiently discredit” the evidence underlying the prima facie case, id. Upon such rebuttal, “the burden of producing additional evidence of anticompetitive effects shifts to the government, and merges with the ultimate burden of persuasion, which remains with the government at all times.

The relevant market definition is also undisputed by the government and the defendants. The district court accepted the government’s proposal that the product market is the market for multichannel video distribution. . . . The district court also accepted the government’s proposed geographic market, which included over 1,100 local multichannel video distribution markets. . . .

. . . [T]he question for this court is whether the district court’s factual findings are clearly erroneous. . . .

In Part II, we provide an overview of the video programming and distribution industry. Then, as relevant to the issues on appeal, we summarize the evidence before the district court and its findings. In Part III, we address the government’s challenges to the district court’s findings.
II.

A.

The video programming and distribution industry traditionally operates in a three-stage chain of production. Studios or networks create content. Then, programmers package content into networks and license those networks to video distributors. Finally, distributors sell bundles of networks to subscribers. For example, a studio may create a television show and sell it to Turner Broadcasting System (“Turner Broadcasting”), a programmer, which would package that television show into one of its networks, such as CNN or TNT. Turner Broadcasting would then license its networks to distributors, such as DirecTV or Comcast.

Programmers license their content to distributors through affiliate agreements, and distributors pay “affiliate fees” to programmers. Programmers and distributors engage in what are oftentimes referred to as “affiliate negotiations,” which . . . can be lengthy and complicated. If a programmer and a distributor fail to reach an agreement, then the distributor will lose the rights to display the programmer’s content to its customers. This situation, known as a “blackout” or “going dark,” is generally costly for both the programmer, which loses affiliate fee revenues, and the distributor, which risks losing subscribers. Therefore, blackouts rarely occur, and long-term blackouts are especially rare. The evidence indicated, however, that programmers and distributors often threaten blackouts as a negotiating tactic, and both may perform “go dark” analyses to estimate the potential impact of a blackout in preparation for negotiations.

The evidence before the district court also showed that the industry has been changing in recent years. Multichannel video programming distributors (“MVPDs”) . . . distribute channels to subscribers on cable or by satellite. Recently, “virtual” MVPDs have also emerged. They distribute live videos and on-demand videos to subscribers over the internet and compete with traditional MVPDs for subscribers. Virtual MVPDs, such as DirecTV Now and YouTube TV, have been gaining market share . . . .

In addition, subscription video on demand services (“SVODs”) have also emerged on the market. SVODs, such as Netflix, do not offer live video content but have large libraries of content that a viewer may access on demand. SVODs also offer low-cost subscription plans and have been gaining market share recently. Increasingly, cable
customers are “cutting the cord” and terminating MVPD service altogether. . . .

Leading SVODs are vertically integrated, which means they create content and also distribute it. Traditional MVPDs typically are not vertically integrated with programmers. In 2009, however, Comcast Corporation (“Comcast”) (a distributor and the largest cable company in the United States) announced a $30 billion merger with NBC Universal, Inc. (“NBCU”) (a content creator and programmer), whereby it would control popular video programming that included the NBC broadcast network and the cable networks of NBC Universal, Inc. The government sued to permanently enjoin the merger under Section 7, alleging that Comcast’s “majority control of highly valued video programming ... would prevent rival video-distribution companies from competing against the post-merger entity.” The district court, with the defendants’ agreement and at the government’s urging, allowed the merger to proceed subject to certain remedies for the alleged anticompetitive conduct post-merger, including remedies ordered in a related proceeding before the Federal Communications Commission (“FCC”). One remedy in the Comcast-NBCU merger was an agreement by the defendants to submit, at a distributor’s option, to “baseball style” arbitration — in which each side makes a final offer and the arbitrator chooses between them — if parties did not reach a renewal agreement. During the arbitration, the distributor would retain access to NBC content, thereby mitigating concerns that Comcast-NBCU may withhold NBC programming during negotiations in order to benefit Comcast’s distribution subscriptions. Comcast-NBCU currently operates as a “vertically integrated” programmer and distributor.

. . . . AT&T Inc. announced its plan to acquire Time Warner Inc. (“Time Warner”) as part of a $108 billion transaction. AT&T Inc. is a distribution company with two traditional MVPD products: DirecTV and U-verse. DirecTV transmits programming over satellite, while U-verse transmits programming over cable. Time Warner, by contrast, is a content creator and programmer and has three units: Warner Bros., Turner Broadcasting, and Home Box Office Programming (“HBO”). Warner Bros. creates movies, television shows, and other video programs. Turner Broadcasting packages content into various networks, such as TNT, TBS, and CNN, and licenses its networks to third-party MVPDs. HBO is a “premium” network that provides on-demand content to subscribers either directly through HBO Now or through licenses with third-party distributors. The merged firm would operate both AT&T MVPDs (DirecTV and U-verse)
and Turner Broadcasting networks (which license to other MVPDs). . .

A week after the government filed suit to stop the proposed merger, Turner Broadcasting sent letters to approximately 1,000 distributors “irrevocably offering” to engage in “baseball style” arbitration at any time within a seven-year period, subject to certain conditions not relevant here. . . . In the event of a failure to agree on renewal terms, Turner Broadcasting agreed that the distributor would have the right to continue carrying Turner networks pending arbitration, subject to the same terms and conditions in the distributor’s existing contract.

B.

The government’s increased leverage theory is that “by combining Time Warner’s programming and DirecTV’s distribution, the merger would give Time Warner increased bargaining leverage in negotiations with rival distributors, leading to higher, supracompetitive prices for millions of consumers.” Under this theory, Turner Broadcasting’s bargaining position in affiliate negotiations will change after the merger due to its relationship with AT&T because the cost of a blackout will be lower. Prior to the merger, if Turner Broadcasting failed to reach a deal with a distributor and engaged in a long-term blackout, then it would lose affiliate fees and advertising revenues. After the merger, some costs of a blackout would be offset because some customers would leave the rival distributor due to Turner Broadcasting’s blackout and a portion of those customers would switch to AT&T distributor services. The merged AT&T-Turner Broadcasting entity would earn a profit margin on these new customers. Because Turner Broadcasting would make a profit from switched customers, the cost of a long-term blackout would decrease after the merger and thereby give it increased bargaining leverage during affiliate negotiations with rival distributors sufficient to enable it to secure higher affiliate fees from distributors, which would result in higher prices for consumers.

The government also presented . . . [expert testimony] on the likely anticompetitive effect of the proposed merger. He opined, based on the economic theory of bargaining — here, the Nash bargaining theory — that Turner Broadcasting’s bargaining leverage would increase after the merger because the cost of a long-term blackout would decrease. His quantitative model predicted net price increases to consumers. Specifically, his model predicted increases in fees paid by rival distributors for Turner Broadcasting content and cost savings
for AT&T through elimination of double marginalization ("EDM"). The fee increases for rival distributors were based on the expected benefit to AT&T of a Turner Broadcasting blackout after the merger.

AT&T responded by pointing to testimony of executives’ past experience in affiliate negotiations, and presenting testimony by its experts... that critiqued the “inputs” used by [the government’s expert] in his quantitative model, opining for instance that values he used for subscriber loss rate and diversion rate were not calculated through reliable methods...

**

The district court... concluded that the government failed to present persuasive evidence that Turner Broadcasting’s bargaining leverage would “materially increase” as a result of the merger or that the merger would lead to “any raised costs” for rival distributors or consumers. It therefore did not address the... question whether any increased costs would result in a substantial lessening of competition.

III.

On appeal, the government contends that the district court (1) misapplied economic principles, (2) used internally inconsistent logic when evaluating industry evidence, and (3) clearly erred in rejecting [its expert’s] quantitative model...

(1) Application of economic principles. The government contends that in evaluating the evidence in support of its increased leverage theory, the district court erroneously discarded or otherwise misapplied two economic principles — the Nash bargaining theory and corporate-wide profit maximization.

(a) Nash bargaining theory. The Nash bargaining theory is used to analyze two-party bargaining situations, specifically where both parties are ultimately better off by reaching an agreement. John F. Nash, Jr., The Bargaining Problem, 18 Econometrica 155 (1950). The theory posits that an important factor affecting the ultimate agreement is each party’s relative loss in the event the parties fail to agree: when a party would have a greater loss from failing to reach an agreement, the other party has increased bargaining leverage. In other words, the relative loss for each party affects bargaining leverage and when a party has more bargaining leverage, that party is more likely to achieve a favorable price in the negotiation.

The district court had to determine whether the economic theory applied to the particular market by considering evidence about the “structure, history, and probable future” of the video programming
and distribution industry. . . . The district court concluded that the government presented insufficient real-world evidence to support the prediction under the Nash bargaining theory of a material increase of Turner Broadcasting’s post-merger bargaining leverage in affiliate negotiations by reason of less-costly long-term blackouts. The government’s real-world evidence consisted of statements by AT&T Inc. and DirecTV in FCC regulatory filings that vertical integration, such as in the proposed Comcast-NBCU merger, can give distributors an incentive to charge higher affiliate fees and expert opinion and a quantitative model prepared by [its expert]. The expert opinion and model were subject to deficiencies identified by AT&T’s experts, some of which [the government’s expert] conceded. By contrast, AT&T’s expert’s econometric analysis of real-world data showed that content pricing in prior vertical mergers in the industry had not increased as the Nash bargaining theory and the model predicted. Given evidence the industry was now “remarkably dynamic,” the district court credited CEO testimony about the null effect of vertical integration on affiliate negotiations.

In other words, the record shows that the district court accepted the Nash bargaining theory as an economic principle generally but rejected its specific prediction in light of the evidence that the district court credited. . . .

More concerning is the government’s contention that the district court misapplied the Nash bargaining theory in a manner that negated its acceptance of the economics of bargaining by erroneously focusing on whether long-term blackouts would actually occur after the merger, rather than on the changes in stakes of such a blackout for Turner Broadcasting. The government points to the district court’s statements . . . that “a blackout would be infeasible.” The district court also stated that “there has never been, and is likely never going to be, an actual long-term blackout of Turner [Broadcasting] content”. . . .

The question posed by the Nash bargaining theory is whether Turner Broadcasting would be more favorably positioned after the merger to assert its leverage in affiliate negotiations whereby the cost of its content would increase. Considered in isolation, the district court’s statements could be viewed as addressing the wrong question. Considered as part of the district court’s analysis of whether the stakes for Turner Broadcasting would change and if so by how much, the statements address whether the threat of long-term blackouts would be credible, as posited by the government’s increased leverage theory. The district court found that after the merger the stakes for Turner Broadcasting would change only slightly, so its threat of a long-term
blackout “will only be somewhat less incredible”. . . . [T]he district court rejected the assumption underlying the government’s theory that Turner Broadcasting would gain increased leverage from this slight change in stakes. . . .

The district court’s statements identified by the government, then, do not indicate that the district court misunderstood or misapplied the Nash bargaining theory but rather, upon considering whether in the context of a dynamic market where a similar merger had not resulted in a “statistically significant increase in content costs,” the district court concluded that the theory inaccurately predicted the post-merger increase in content costs during affiliate negotiations.

. . . The district court reasoned that because long-term blackouts are very costly and would therefore be infeasible for Turner Broadcasting even after the merger, there was insufficient evidence that “a post-merger Turner [Broadcasting] would, or even could, drive up prices by threatening distributors with long-term blackouts”. . . . [T]he district court reached a fact-specific conclusion based on real-world evidence that, contrary to the Nash bargaining theory and government expert opinion on increased content costs, the post-merger cost of a long-term blackout would not sufficiently change to enable Turner Broadcasting to secure higher affiliate fees. . . .

Not to be overlooked, the district court also credited the efficacy of Turner Broadcasting’s “irrevocable” offer of arbitration agreements with a no-blackout guarantee. It characterized the no-blackout agreements as “extra icing on a cake already frosted”. . . . [T]he district court explained that it was appropriate to consider the analysis of the Comcast-NBCU merger because the Comcast-NBCU merger was similar to the proposed merger — a vertical merger in the video programming and distribution industry. There the government had recognized, “especially in vertical mergers, that conduct remedies, such as the ones proposed [in the Comcast case], ‘can be a very useful tool to address the competitive problems while preserving competition and allowing efficiencies’ that ‘may result from the transaction.’” Like there, the district court concluded the Turner arbitration agreements would have “real-world effect.”

* * *

(b) Corporate-wide profit maximization. Still, the government maintains that the reliance on past negotiation experience indicates that the district court misunderstood, and failed to apply, the principle
of corporate-wide profit maximization by treating the principle as a question of fact, when “[t]he assumption of profit maximization is ‘crucial’ in predicting business behavior.” Appellant Br. 50 (citation omitted). This principle posits that a business with multiple divisions will seek to maximize its total profits. It was adopted as a principle of antitrust law in *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 771 (1984), holding that a parent and a wholly-owned subsidiary are not capable of conspiracy against each other under Section 1 of the Sherman Antitrust Act. Companies with multiple divisions must be viewed as a single actor, and each division will act to pursue the common interests of the whole corporation.

The . . . government’s position that the district court never accepted this economic principle overlooks that it did “accept [the expert’s] (and the Government’s) argument that generally, ‘a firm with multiple divisions will act to maximize profits across them.” And it ignores that if the merged firm was unable to exert the leverage required by the government’s increased leverage theory, then inquiring (as the district court did of [the government’s expert]) about an independent basis to conclude that the firm did have such leverage is not a rejection of the corporate-wide profit maximization principle.

The government maintains that the district court’s misapplication of the principle of corporate-wide profit maximization is evident from its statement the evidence suggests “vertically integrated corporations have previously determined that the best way to increase company wide profits is for the programming and distribution components to separately maximize their respective revenues” . . . . The district court can be viewed as conveying its understanding that Turner Broadcasting’s interest in spreading its content among distributors, not imposing long-term blackouts, would redound to the merged firm’s financial benefit, not that Turner Broadcasting would act in a manner contrary to the merged firm’s financial benefit.

. . . [T]he government . . . gives no credence to the district court’s focus on “the best way to increase company wide profits,” referring to the merged firm. AT&T, In other words, the district court was explaining that real-world evidence reflected the profit-maximization principle. . . .

* * *

Similarly, contrary to the government’s position, the district court’s findings about post-merger negotiating are not internally
inconsistent with its finding on the cost savings of the merger. The
district court found, and the government agreed, that the merger
would result in cost savings as a result of EDM. Pre-merger, both
Turner Broadcasting and AT&T earned margins over cost before their
products reached consumers: Turner Broadcasting earned a profit
margin when it licensed content to AT&T, and AT&T earned a profit
margin when it sold content to consumers. Post-merger, Turner
Broadcasting would not earn a profit margin when licensing content
to AT&T because the merged entity would eliminate that cost and . . .
pass on some of those cost savings to consumers in order to attract
additional subscribers. For there to be EDM savings, . . . the merged
firm must act on its unified interest across divisions. Thus, Turner
Broadcasting, instead of maximizing its own revenue, would license its
programming to AT&T for a lower price. . . .

(2) Inconsistent reasoning in evaluating trial testimony. The
government further maintains that the district court used internally
inconsistent reasoning when evaluating testimony from witnesses in
the industry.

At trial, third-party distributors and executives from Comcast-
NBCU and Time Warner testified about negotiations in the video
programming and distribution industry. Third-party distributors
tested about their concerns, and their reasons, that Turner
Broadcasting would gain increased bargaining leverage as a result of
the proposed merger. . . . The district court declined to credit the third-
party distributors’ testimony because “there is a threat that [third-
party distributor] testimony reflects self-interest” yet dismissed the
suggestion that testimony from the Time Warner executives should be
discounted as potentially biased due to self-interest.

The government contends this reasoning was inconsistent
because self-interest existed on both sides of the issue of whether the
proposed merger would have anticompetitive effects. Even so, the
potential for self-interest was not the only reason the district court
found third-party distributor testimony of little probative value. Much
of the third-party competitor testimony, the district court found,
“consisted of speculative concerns” and did not contain any analysis or
factual basis to support key assumptions, such as how Turner
Broadcasting’s bargaining leverage would change and how many
subscribers distributors would lose in a blackout. By contrast, the
Time Warner executives’ testimony did “not involve promises or
speculations about the employees’ future, post-merger behavior” and
instead recounted “what these executives previously experienced when
working within a vertically integrated company.” Their testimony was
uniform among all testifying witnesses and corroborated by that of a Comcast-NBCU executive — a competitor of AT&T.

(3) Rejection of [the government expert’s] quantitative model. Finally, the government contends that the district court clearly erred in rejecting [its expert’s] quantitative bargaining model.

Preliminarily, the court does not hold that quantitative evidence of price increase is required in order to prevail on a Section 7 challenge. Vertical mergers can create harms beyond higher prices for consumers, including decreased product quality and reduced innovation. Indeed, the Supreme Court upheld the Federal Trade Commission’s Section 7 challenge to Ford Motor Company’s proposed vertical merger with a major spark plug manufacturer without quantitative evidence about price increases. Ford Motor Co. v. United States, 405 U.S. 562, 567-69, 578 (1972). Here, however, the government did not present its challenge to the AT&T-Time Warner merger in terms of creating non-price related harms in the video programming and distribution industry.

. . . .The district court accepted [the government expert’s] testimony about the $352 million cost savings from the merger. But it found that insufficient evidence supported the inputs and assumptions used to estimate the annual costs increases for rival distributors . . . . Indeed, the district court found that the quantitative model . . . did not provide an adequate basis to conclude that the merger will lead to “any” raised costs for distributors or consumers, “much less consumer harms that outweigh the conceded $350 million in annual cost savings to AT&T’s customers.”

Whatever errors the district court may have made in evaluating the inputs for [the expert’s] quantitative model, the model did not take into account long-term contracts, which would constrain Turner Broadcasting’s ability to raise content prices for distributors. The district court found that the real-world effects of Turner Broadcasting’s existing contracts would be “significant” until 2021 and that it would be difficult to predict price increases farther into the future, particularly given that the industry is continually changing and experiencing increasing competition. This failure, the district court found, resulted in overestimation of how quickly the harms would occur. [The expert] acknowledged that predictions farther into the future, after the long-term contracts expire, are more difficult. Neither [the expert’s] opinion testimony nor his quantitative model considered the effect of the post-litigation offer of arbitration agreements, something he acknowledged would require a new model. And the video programming and distribution industry had experienced
“ever-increasing competitiveness” in recent years. Taken together, the government’s clear-error contention therefore fails.

* * *

Accordingly, because the district court did not abuse its discretion in denying injunctive relief, we affirm the district court’s order denying a permanent injunction of the merger.

NOTES AND QUESTIONS

1. Nash bargaining theory. Nash bargaining theory, on which the government’s case was largely based, is named after its author, Nobel laureate John Nash, and is widely accepted among economists. The idea, in a nutshell, is that parties reach agreement only when both are better off agreeing than not agreeing and that the terms on which the parties are likely to agree are driven largely by the relative costs to the parties of failing to reach a deal. If party A would be harmed more by the failure to reach agreement than party B, the terms of the deal will be relatively favorable to party B, and vice versa. In a simple buy/sell transaction regarding property for a retail store, for example, the buyer should be willing to pay (its “reservation price”) up to the cost to it of not reaching agreement; that might be the cost of buying an equivalent property from a different seller or the cost to the business of having to settle for an inferior alternative or none at all. The seller should be willing to accept (its “reservation price”) any price greater than its next best alternative, which might be the price it could get by selling the property to someone else. The difference between the parties’ reservation prices are the “gains from trade,” and the parties negotiate over how the gains from trade will be allocated. If the parties are otherwise equally skilled negotiators, the price should be midway between the parties’ reservation prices. If market circumstances cause one party’s reservation price to change, the expected transaction price will also change. The theory does not require that failure to reach agreement is a common or likely outcome, but it does require that one or both parties can credibly threaten not to reach agreement if their proposed terms are not accepted. These notions can be formalized in rigorous mathematical models.

The intuition underlying Nash bargaining theory is similar to the price theory notions that have long been fundamental to antitrust law. If S is a monopoly, the costs to the customer of not reaching agreement with S will be greater than if S has several competitors to which the customer can turn. The customer can therefore be expected to pay a higher price if S is a monopoly. Nash bargaining theory,
however, focuses on bargaining between two parties rather than on the performance of larger, multiparty markets.

2. *Vertical mergers in the past.* The government’s theory in the Comcast/NBC merger (page 800) was that rival MVPDs would be excluded as a result of the merger. The government reasoned that NBC would not forego profitable dealing with other MVPDs prior to the merger but that the merged firm would forego those profits in order to increase the size and power of the Comcast MVPD business. As explained in the note about How Vertical Mergers Can Harm Competition (pages 794-798), that is the kind of theory on which vertical mergers have been challenged in the past.

In AT&T/TW, however, the government did not argue that TW would refuse to license some or all of its content to rival distributors or that it would increase prices to above profit-maximizing levels in order to harm the rivals. Instead, it argued that the merger would make such actions less costly to the merged firm (because some of the lost sales to rivals would result in customers switching to AT&T) and would thereby increase TW’s bargaining leverage over rival distributors and enable it to charge higher prices, which would benefit both TW and AT&T. In other words, the government did not argue that the merger would give TW an incentive to sacrifice profits in order to benefit AT&T; it argued instead that the merger would enable TW to increase both its profits and AT&T’s. The court accepted the government’s theory but held that the government had failed on the facts.

3. *Higher prices and injury to competition.* Is the government’s theory sound as a matter of law? The government did not try to prove that the higher prices would harm competition among MVPDs by showing, for example, that the higher prices would materially weaken AT&T’s MVPD rivals or would create a price umbrella under which AT&T could exercise market power. Can such harm be presumed? If not, is the government alleging injury to competition or just higher prices, which are not themselves enough to establish a violation of the antitrust laws? (With respect to whether high prices are themselves unlawful, see *Rambus* (Chapter 8) and *NYNEX* (Chapter 10); see also *Trinko* (Chapter 5).) Is the idea that the merger injured competition because it reduced the competitive constraints on TW by diminishing the ability of consumers to switch to unaffiliated MVPDs?

4. *Double marginalization.* Double marginalization arises when providers of complements, including vertically related firms, seek to exercise market power in the markets in which the complements are sold. As explained in Chapter 4 (pages 352-58), if the
firms do not coordinate their prices, they will in aggregate charge more than the profit-maximizing price to the detriment of both consumers and the firms themselves. The ATT&T/TW court found that the merger would enable the merged firm to coordinate the AT&T and TW prices and thus eliminate pre-merger double marginalization. Why do you suppose the parties could not have eliminated the double marginalization without a merger? Should the merging parties have the burden of proving that double marginalization could not be eliminated absent the merger in order to rely on EDM as defense?

5. Litigate or settle. DOJ passed up an opportunity to settle the AT&T/TW case on terms reportedly similar to those in the Comcast/NBC settlement. DOJ explained its view that complex conduct remedies are burdensome and often ineffective and that the better course would be to block the merger altogether, but DOJ lost and thus ended up with no remedy. Did DOJ make a mistake in choosing the litigate? Or does the outcome prove that a remedy would not have been warranted?

Merger cases almost always involve predictions about the future. There is therefore almost always some uncertainty, not just about litigation risk, but about the substantive question whether the merger will be anticompetitive. How should an enforcement agency take such substantive uncertainty into account in making enforcement decisions?

6. Never mind. On May 17, 2021, AT&T accounced that it was undoing the Time-Warner merger. The spin-off transaction is substantially more complicated than that as it also involved folding in certain assets from Discovery, but once again, Time-Warner was involved in a major merger only to have it undone at a later date. (As you may recall, amidst the internet boom, in 2000, AOL and Time-Warner merged only to undo the merger in 2009.) Does the fact that AT&T has now backed away from the Time-Warner merger cause you to change your view of any of the issues raised in the case?

NOTE ON VERTICAL MERGER GUIDELINES

In the spring of 2020, the Justice Department and the Federal Trade Commission released updated Vertical Merger Guidelines, replacing the outdated 1984 Vertical Merger Guidelines. The 1984 Guidelines, which were issued during the Reagan Administration, described little or no basis to challenge a vertical merger. In the AT&T

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9 The Guidelines can be downloaded from https://www.justice.gov/atr/page/file/1290686/download
case, the D.C. Circuit rejected the Justice Department’s challenge to the merger, but it also implicitly rejected the 1984 Guidelines. The court agreed that the Justice Departments set forth a viable theory of harm but found that the theory was not supported by the facts in that case. Notably, the court suggested that the only fundamental difference between the law applicable to horizontal mergers and that applicable to vertical mergers is that the structural presumption applies only to horizontal mergers and that, in vertical mergers, “the government must make a ‘fact-specific’ showing that the proposed merger is ‘likely to be anticompetitive.’”

The 2020 Vertical Merger Guidelines depart significantly from the 1984 Guidelines. While they note that the “agencies more often encounter problematic horizontal mergers than problematic vertical mergers,” they also state that “vertical mergers are not invariably innocuous.” The Guidelines state that they should be read in conjunction with the Horizontal Merger Guidelines and that they address only additional factors unique to vertical mergers. The Guidelines are applicable to “strictly vertical mergers,” i.e., those between firms at different stages of the same supply chain; “diagonal mergers,” i.e., those between firms at different stages of competing supply chains; and mergers of complements.

The Guidelines outline various circumstances in which a vertical merger might be regarded as anticompetitive and subject to challenge by the enforcement agencies. Harm to competition can occur in the stage closer to the final customer in which one or more of the merging firms competes, e.g., competition among retailers (the “downstream market”) or in the stage farther from the final consumer, e.g., competition among manufacturers (the “upstream market”).

The circumstances in which a vertical merger might be anticompetitive include the following, which do not exhaust the types of problematic circumstances:

- The merger might increase the ability or incentive of the merged firms to increase the costs of actual or potential future rivals of one or both of them by refusing to sell supplies to those rivals or increasing the price or reducing the quality of those supplies (“input foreclosure”). The merged firms might have the ability to foreclose rivals if doing so would cause the rivals to lose significant sales or reduce their ability to compete effectively against the merged firms, and it might have the incentive to do so if the foreclosed rivals are sufficiently important in the relevant market that the merged firm would benefit from the
reduced competition provided by those rivals.

- The merger might also increase the ability and incentive of the merged firms to require potential rivals to enter at both levels by refusing to deal with the new rivals.
- The merger might increase the ability and incentive of the merged firm to harm rivals by increasing the price or restricting the supply of complements to the rivals’ products and thereby reducing the value of those products.
- The examples above concern possible unilateral conduct by the merged firms. The Guidelines also note that a vertical merger could “enabl[e] or encourag[e] postmerger coordinated interaction among firms in the relevant market.” The merger might do so by eliminating a maverick firm that would otherwise inhibit coordination among rivals in the relevant market or by giving the merged firm access to confidential information about rivals that could be used to facilitate coordination.

The Guidelines also note that vertical mergers can create valuable merger-specific efficiencies. These include cost reductions and increased innovation attributable to the combining of complementary assets and elimination of double marginalization. (Double marginalization is discussed in the main text at pp 352-358.) In a major shift from the earlier Guidelines, the 2020 Guidelines state that merger efficiencies cannot be assumed, but instead must be proved by the merging parties.

**D. Steves and Sons and Remedies in Private Merger Cases**

[on page 843, at the end of Chapter 6]

The Supreme Court made clear more than thirty year ago that the Clayton Act authorizes divestiture in private cases “when it is appropriate under equitable principles” to protect plaintiffs from “threatened loss or damage by a violation of the antitrust laws.” California v. American Stores Co., 495 U.S. 271, 280, 285 (1990). Until this year, however, no court had ordered divestiture in a private case.

In *Steves and Sons v. JELD-WEN, Inc.*, 988 F.3d 690 (4th Cir. 2021), the Court of Appeals affirmed a district court decision ordering divestiture of assets acquired in what the court found to be an unlawful merger that had been consummated nine years earlier. The merger involved two of the three manufacturers of molded doorskins—a critical component needed to build doors. The plaintiff, Steves and
Sons, was an independent door manufacturer. The district court found that, prior to the merger, the three molded doorskin manufacturers “competed vigorously in selling doorskins to Steves and the other independent (non-integrated) door manufacturers.” *Steves and Sons, Inc. v. JELD-WEN, Inc.*, 345 F.Supp.3d 614, 631 (2018). The three manufacturers were Masonite, which had a 46% market share; JELD-WEN, 38%; and CMI, 16%.

JELD-WEN agreed to acquire CMI in 2012. Shortly thereafter, and before filing its premerger notification under the Hart-Scott-Rodino Act, JELD-WEN entered into multi-year supply agreements with Steves and other independent door manufacturers. The agreement with Steves specified the price for the doorskins; it did not, however, specify quality requirements, reimbursement terms, or other important matters. The agreement was for seven years but would automatically renew unless terminated by one of the parties.

After the agreements were entered into, JELD-WEN filed its premerger notification. The Department of Justice investigated the proposed merger, but, in the absence of any complaints from customers (who had entered into long-term supply agreements, like Steves’s), it declined to challenge it. The merger was consummated in the Fall of 2012.

The supply agreements proved to be of limited value. JELD-WEN increased the prices for Steves to almost eight percent more than that authorized under its agreement and changed its policy on reimbursing Steves for the cost of doors rendered defective by flawed doorskins. When Masonite announced in 2014 that it would not sell doorskins to independent door manufactures, Steves lost the alternative supply option it had used to put pressure on JELD-WEN when it negotiated its last agreement.

In the face of worsening supply conditions, Steves asked the Justice Department to reexamine the merger. After the Department declined to take action, Steves sued JELD-WEN in 2016, alleging that its acquisition of CMI was illegal and that it had breached the 2012 supply agreement. After a jury trial, the district court held that the acquisition of CMI violated Section 7 of the Clayton Act, ordered JELD-WEN to divest the doorskin plant it had acquired from CMI, and awarded Steves damages for breach of the supply agreement.

The Fourth Circuit Court of Appeals affirmed these aspects of the district court’s decision. The court emphasized that the merger caused the HHI of the doorskin market to increase roughly 1,200-points—six times the threshold for presumed illegality under the Merger Guidelines, 988 F.3d at 715, and that JELD-WEN did not
present any evidence to defend the merger on the merits. The court held that Steves had suffered antitrust injury because the merger denied Steves the option of a competing supplier (CMI) and because the supply agreement did not require JELD-WEN to supply high-quality products or maintain a liberal reimbursement policy and the merger reduced its competitive incentives to do so. Id. at 711.

The court also rejected JELD-WEN’s argument that Steves’ claim should be barred by the doctrine of laches because Steves waited several years to challenge the merger. 10 The court said that Steves could not have anticipated its potential loss of access to doorskins when the supply agreement was in effect and Masonite was an available alternative, id. at 717-18.

The court held that divestiture is an equitable remedy the appropriateness of which is to be assessed by consideration of the same four factors used to assess all equitable remedies: whether the plaintiff faces a threat of irreparable injury, whether there is an adequate remedy at law, the balance of hardships between the parties, and the public interest. It concluded that divestiture was appropriate in this case largely because the elimination of competition caused by the merger threatened Steves’ survival and divestiture would promote competition in the doorskin market. Id. at 719-20.

The case touches upon several important issues and raises many interesting questions, including the following:

1. The court’s discussion of the antitrust injury issue illustrates some of the ways in which a merger of suppliers can impact their customers. No doubt because it anticipated that its customers might be concerned about the merger, JELD-WEN did what many merging parties do: It entered into agreements with customers regarding post-merger conduct in order to reduce or eliminate the customers’ incentives to complain about the merger or even to provide testimony that might support a case by the government challenging the merger. From the government’s perspective, do these agreements eliminate the

10 Laches is an equitable doctrine, roughly analogous to the statute of limitations applicable to actions for damages, that “bars a plaintiff from maintaining a suit if he unreasonably delays in filing a suit and as a result harms the defendant.” Nat’l R.R. Passenger Corp. v. Morgan, 536 U.S. 101, 121 (2002). Because of its similarity to the statute of limitations, which is four years for antitrust actions, courts often begin with the presumption that equitable claims under the antitrust laws should be brought within four years of the time the cause of action accrued. E.g., Menominee Indian Tribe of Wisconsin v. United States, 614 F.3d 519, 531 (D.C. Cir. 2010).
antitrust concerns about the merger? If not, should the government challenge the merger and try to persuade the court to disregard the absence of support for the challenge by the very customers most likely to be harmed by a reduction in competition? How likely do you think the government is to win the case under those circumstances?

2. As we have seen elsewhere, many aspects of antitrust law, especially under the Sherman Act, often favor defendants because of the courts’ concern that more aggressive or ambiguous standards might be abused by opportunistic private plaintiffs whose interests are not aligned with those of the public. The court in Steves expressed no such concern. What makes this case different? Should the court have been more skeptical of Steves’ case?

3. Steves did not file suit until nearly 4 years after the merger had been consummated and JELD-WEN had made substantial investments to integrate the CMI plant into its operations. Was the court correct in rejecting JELD-WEN’s laches argument? Is there an inconsistency between the court’s holding on antitrust injury and its laches holding? Didn’t Steves know about the effect of the merger on market competition back in 2012? Is it appropriate for Steves to enter into the supply agreement and then decide, years later, whether it prefers the alternative of antitrust litigation or that it made a bad deal? (And, we should flag for you the increased importance of the laches defense. With a change of administrations in Washington D.C. and the resulting turnover at the Antitrust Division and the Federal Trade Commission, there might be an increased number of cases challenging previously consummated mergers. The pending litigation over Facebook’s purchases of Instagram and WhatsApp is an obvious example of this. While the federal enforcement agencies cannot be barred by a laches defense, the laches issue is an important defense in the lawsuit brought by many state attorneys general challenging those acquisitions.)

Chapter 7: Competition Law in the Global Economy


[insert before 3. Export Commerce, on p. 881]

From time to time, firms find themselves in the cross-hairs of conflicting national laws, with very little room to maneuver. This
might be what happened in Animal Science Prods., Inc. v. Hebei Welcome Pharm. Co. Ltd., 138 S. Ct. 1865 (2018), which involved a challenge to an alleged Chinese cartel that was fixing the price of Vitamin C that was manufactured in China and imported into the United States. On the surface, this was a relatively routine cartel case, in which a class of U.S. plaintiffs were complaining about direct sales at anticompetitively high prices. But the complication was this: the four defendant Chinese corporations asserted that the Chinese government had compelled them to become members of the Chamber of Commerce of Medicines and Health Products Importers and Exporters ("the Chamber") and that the Chamber fixed the prices the member companies had to charge, and the quantities they were permitted to sell, to U.S. customers. The Chinese sellers thus moved to dismiss the complaint on the ground that Chinese law compelled their actions—in other words, they invoked the "foreign sovereign compulsion" defense. They were backed up in this assertion by a brief amicus curiae filed by the Ministry of Commerce of the People's Republic of China; the Ministry confirmed that the Chamber was under direct government supervision and that the alleged conspiracy was in fact "a regulatory pricing regime mandated by the government of China." Id. at 1870.

The district court held that Chinese law did not excuse the companies' price-fixing, and after a trial it awarded the plaintiffs $147 million in treble damages. It also enjoined the plaintiffs from further violations of the Sherman Act. The court said that, while the Ministry's statements about Chinese law were "entitled to substantial deference," they were not "conclusive." The court noted, among other things, an earlier Chamber announcement that the manufacturers had reached a "self-regulated agreement" pursuant to which they would "voluntarily control" the quantity of exports, id., at 1871, and China's statement to the World Trade Organization that its "export administration" of Vitamin C ended in 2002. Id.

The Court of Appeals for the Second Circuit reversed. It reasoned that the case turned on whether it was impossible for the Chinese sellers to obey both Chinese and U.S. law at the same time and that determination of that question depended on "the amount of deference" owed to the Ministry's characterization of Chinese law. Id. at 1872. As to the deference question, the appeals court held that a U.S. court should not challenge "a foreign government's official representation" about its law, as long as its description of the law is "reasonable." Id.

The Supreme Court granted certiorari to review the question whether "a federal court determining foreign law ... [is] required to
treat as conclusive a submission from the foreign government describing its own law.” *Id.* at 1872. The Court answered that question in the negative. It noted that Federal Rule of Civil Procedure 44.1 entrusts the district court with the duty of ascertaining foreign law (and that this is a “question of law” for the court, not a matter of “fact”). It held in particular that “a government’s expressed view of its own law is ordinarily entitled to substantial but not conclusive weight.” *Id.* at 1875. Elaborating, it said that “the appropriate weight in each case will depend upon the circumstances; a federal court is neither bound to adopt the foreign government’s characterization nor required to ignore other relevant materials. When a foreign government makes conflicting statements … or, as here, offers an account in the context of litigation, there may be cause for caution in evaluating the foreign government’s submission.” *Id.* at 1873.

This holding will make life difficult for companies that face seemingly inconsistent rules. They will be faced with the unpalatable choice of (a) violating their home country law; (b) running the risk that, if they comply with their home country law, a U.S. court will construe it differently; (c) foregoing the U.S. market; or (d) pushing to see whether there is some flexibility in the home country law that might enable compliance with both laws. The final wrinkle is that many countries (including China) have competition laws that are, at least on paper, compatible with U.S. law. It remains to be seen whether that substantive convergence will provide some kind of relief for companies in countries that permit certain cartels or monopolies to exist.

On August 10, 2021, the Second Circuit concluded that Chinese law required the defendants in the original action to engage in price fixing and ordered the district court, under the principles of international comity, to dismiss the action with prejudice. See *Animal Science Products, Inc. v. Hebei Welcome Pharmaceutical Co.*, 13-4791-cv (2nd Cir. August 10, 2021).
Chapter 8: Intellectual Property, Technology, and Platforms

Federal Trade Commission v. Qualcomm Incorporated
969 F.3d 974.
[Insert after Notes and Questions on page 951]

CALLAHAN, Circuit Judge. This case asks us to draw the line between anticompetitive behavior, which is illegal under federal antitrust law, and hypercompetitive behavior, which is not. The Federal Trade Commission (“FTC”) contends that Qualcomm Incorporated (“Qualcomm”) violated the Sherman Act, 15 U.S.C. §§ 1, 2, by unreasonably restraining trade in, and unlawfully monopolizing, the code division multiple access (“CDMA”) and premium long-term evolution (“LTE”) cellular modem chip markets. After a ten-day bench trial, the district court agreed and ordered a permanent, worldwide injunction prohibiting several of Qualcomm’s core business practices. We granted Qualcomm’s request for a stay of the district court’s injunction pending appeal. FTC v. Qualcomm Inc., 935 F.3d 752 (9th Cir. 2019). At that time, we characterized the district court’s order and injunction as either “a trailblazing application of the antitrust laws” or “an improper excursion beyond the outer limits of the Sherman Act.” Id. at 757. We now hold that the district court went beyond the scope of the Sherman Act, and we reverse.

I

Founded in 1985, Qualcomm dubs itself “the world’s leading cellular technology company.” Over the past several decades, the company has made significant contributions to the technological innovations underlying modern cellular systems, including third-generation (“3G”) CDMA and fourth-generation (“4G”) LTE cellular standards—the standards practiced in most modern cellphones and “smartphones.” Qualcomm protects and profits from its technological innovations through its patents, which it licenses to original equipment manufacturers (“OEMs”) whose products (usually cellphones, but also smart cars and other products with cellular applications) practice one or more of Qualcomm’s patented technologies.
Qualcomm’s patents include cellular standard essential patents ("SEPs"), non-cellular SEPs, and non-SEPs. Cellular SEPs are patents on technologies that international standard-setting organizations ("SSOs") choose to include in technical standards practiced by each new generation of cellular technology. . . . Cellular SEPs are necessary to practice a particular cellular standard. Because SEP holders could prevent industry participants from implementing a standard by selectively refusing to license, SSOs require patent holders to commit to license their SEPs on fair, reasonable, and nondiscriminatory ("FRAND") terms before their patents are incorporated into standards.

. . . Rather than license its patents individually, Qualcomm generally offers its customers various "patent portfolio" options, whereby the customer/licensee pays for and receives the right to practice all three types of Qualcomm patents (SEPs, non-cellular SEPs, and non-SEPs).

Qualcomm’s patent licensing business is very profitable, representing around two-thirds of the company's value. But Qualcomm is no one-trick pony. The company also manufactures and sells cellular modem chips, the hardware that enables cellular devices to practice CDMA and premium LTE technologies and thereby communicate with each other across cellular networks. This makes Qualcomm somewhat unique in the broader cellular services industry. Companies such as Nokia, Ericsson, and Interdigital have comparable SEP portfolios but do not compete with Qualcomm in the modem chip markets. On the other hand, Qualcomm’s main competitors in the modem chip markets—companies such as MediaTek, HiSilicon, Samsung LSI, ST-Ericsson, and VIA Telecom (purchased by Intel in 2015)—do not hold or have not held comparable SEP portfolios.

Like its licensing business, Qualcomm’s modem chip business has been very successful. From 2006 to 2016, Qualcomm possessed monopoly power in the CDMA modem chip market, including over 90% of market share. From 2011 to 2016, Qualcomm possessed monopoly power in the premium LTE modem chip market, including at least 70% of market share. During these timeframes, Qualcomm leveraged its monopoly power to "charge monopoly prices on [its] modem chips." Qualcomm, 411 F. Supp. 3d at 800. Around 2015, however, Qualcomm’s dominant position in the modem chip markets began to recede, as competitors like Intel and MediaTek found ways to successfully compete. Based on projections from 2017 to 2018, Qualcomm maintains approximately a 79% share of the
CDMA modem chip market and a 64% share of the premium LTE modem chip market.

B

Qualcomm licenses its patent portfolios exclusively at the OEM level, setting the royalty rates on its CDMA and LTE patent portfolios as a percentage of the end-product sales price. This practice is not unique to Qualcomm. As the district court found, “following Qualcomm’s lead, other SEP licensors like Nokia and Ericsson have concluded that licensing only OEMs is more lucrative, and structured their practices accordingly.” OEM-level licensing allows these companies to obtain the maximum value for their patented technologies while avoiding the problem of patent exhaustion, whereby “the initial authorized [or licensed] sale of a patented item terminates all patent rights to that item.” Quanta Comput., Inc. v. LG Elecs., Inc., 553 U.S. 617, 625 (2008). Due to patent exhaustion, if Qualcomm licensed its SEPs further “upstream” in the manufacturing process to competing chip suppliers, then its patent rights would be exhausted when these rivals sold their products to OEMs. OEMs would then have little incentive to pay Qualcomm for patent licenses, as they could instead become “downstream” recipients of the already exhausted patents embodied in these rivals’ products.

Because rival chip manufacturers practice many of Qualcomm’s SEPs by necessity, Qualcomm offers these companies what it terms “CDMA ASIC Agreements,” wherein Qualcomm promises not to assert its patents in exchange for the company promising not to sell its chips to unlicensed OEMs.

Qualcomm reinforces these practices with its so-called “no license, no chips” policy, under which Qualcomm refuses to sell modem chips to OEMs that do not take licenses to practice Qualcomm’s SEPs. Otherwise, because of patent exhaustion, OEMs could decline to take licenses, arguing instead that their purchase of chips from Qualcomm extinguished Qualcomm’s patent rights with respect to any CDMA or premium LTE technologies embodied in the chips. This would not only prevent Qualcomm from obtaining the maximum value for its patents, it would result in OEMs having to pay more money (in licensing royalties) to purchase and use a competitor’s chips, which are unlicensed. Instead, Qualcomm’s practices, taken together, are “chip supplier neutral”—that is, OEMs are required to pay a per-unit licensing royalty to Qualcomm for its patent portfolios regardless of which company they choose to source their chips from.
Although Qualcomm’s licensing and modem chip businesses have made it a major player in the broader cellular technology market, the company is not an OEM. That is, Qualcomm does not manufacture and sell cellphones and other end-use products (like smart cars) that consumers purchase and use. Thus, it does not “compete”—in the antitrust sense—against OEMs like Apple and Samsung in these product markets. Instead, these OEMs are Qualcomm’s customers.

C

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Qualcomm’s competitors in the modem chip markets contend that Qualcomm’s business practices, in particular its refusal to license them, have hampered or slowed their ability to develop and retain OEM customer bases, limited their growth, delayed or prevented their entry into the market, and in some cases forced them out of the market entirely. These competitors contend that this result is not just anticompetitive, but a violation of Qualcomm’s contractual commitments to two cellular SSOs . . . to license its SEPs “to all applicants” on FRAND terms . . .

In 2011 and 2013, Qualcomm signed agreements with Apple under which Qualcomm offered Apple billions of dollars in incentive payments contingent on Apple sourcing its iPhone modem chips exclusively from Qualcomm and committing to purchase certain quantities of chips each year. Again, rivals such as Intel—as well as Apple itself, which was interested in using Intel as an alternative chip supplier—complained that Qualcomm was engaging in anticompetitive business practices designed to maintain its monopolies in the CDMA and premium LTE modem chip markets while making it impossible for rivals to compete. In 2014, Apple decided to terminate these agreements and source its modem chips from Intel for its 2016 model iPhone.

D

In January 2017, the FTC sued Qualcomm for equitable relief, alleging that Qualcomm’s interrelated policies and practices excluded competitors and harmed competition in the modem chip markets, in violation § 5(a) of the FTC Act, 15 U.S.C. § 45(a), and §§ 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1, 2. After a ten-day bench trial, the district court concluded that “Qualcomm’s licensing practices are an unreasonable restraint of trade under § 1 of the Sherman Act and exclusionary conduct under § 2 of the Sherman
Act.” The district court ordered a permanent, worldwide injunction prohibiting Qualcomm’s core business practices.

* * *

II

* * *

A

... [N]ovel business practices—especially in technology markets—should not be “conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use.” Microsoft, 253 F.3d at 91...; see also Rachel S. Tennis & Alexander Baier Schwab, Business Model Innovation and Antitrust Law, 29 Yale J. on Reg. 307, 319 (2012) (explaining how “antitrust economists, and in turn lawyers and judges, tend to treat novel products or business practices as anticompetitive” and “are likely to decide cases wrongly in rapidly changing dynamic markets,” which can have long-lasting effects particularly in technological markets, where innovation “is essential to economic growth and social welfare” and “an erroneous decision will deny large consumer benefits”). Regardless of whether the alleged antitrust violation involves concerted anticompetitive conduct under § 1 or independent anticompetitive conduct under § 2, the three- part burden-shifting test under the rule of reason is essentially the same. ... Under § 1, “the plaintiff has the initial burden to prove that the challenged restraint has a substantial anticompetitive effect that harms consumers in the relevant market”. ... “If the plaintiff carries its burden, then the burden shifts to the defendant to show a procompetitive rationale for the restraint”. ... “If the defendant makes this showing, then the burden shifts back to the plaintiff to demonstrate that the procompetitive efficiencies could be reasonably achieved through less anticompetitive means.” Likewise, “if a plaintiff successfully establishes a prima facie case under § 2 by demonstrating anticompetitive effect, then the monopolist may proffer a ‘procompetitive justification’ for its conduct.” Microsoft, 253 F.3d at 59. “If the monopolist asserts a procompetitive justification—a nonpretextual claim that its conduct is indeed a form of competition on the merits because it involves, for example, greater efficiency or enhanced consumer appeal—then the burden shifts back to the plaintiff to rebut that claim.” Id. If the plaintiff cannot rebut the monopolist’s procompetitive justification,
“then the plaintiff must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit.” Id.

The similarity of the burden-shifting tests under §§ 1 and 2 means that courts often review claims under each section simultaneously. . . . However, although the tests are largely similar, a plaintiff may not use indirect evidence to prove unlawful monopoly maintenance via anticompetitive conduct under § 2. . . .

B

A threshold step in any antitrust case is to accurately define the relevant market, which refers to “the area of effective competition.” Am. Express, 138 S. Ct. at 2285 (citation omitted). . . .

Here, the district court correctly defined the relevant markets as “the market for CDMA modem chips and the market for premium LTE modem chips.” Nevertheless, its analysis of Qualcomm’s business practices and their anticompetitive impact looked beyond these markets to the much larger market of cellular services generally. Thus, a substantial portion of the district court’s ruling considered alleged economic harms to OEMs—who are Qualcomm’s customers, not its competitors—resulting in higher prices to consumers. These harms, even if real, are not “anticompetitive” in the antitrust sense—at least not directly—because they do not involve restraints on trade or exclusionary conduct in “the area of effective competition.” Am. Express, 138 S. Ct. at 2285.

* * *

III

Accordingly, we reframe the issues to focus on the impact, if any, of Qualcomm’s practices in the area of effective competition: the markets for CDMA and premium LTE modem chips. Thus, we begin by examining the district court’s conclusion that Qualcomm has an antitrust duty to license its SEPs to its direct competitors in the modem chip markets.

* * *

A

“As the Supreme Court has repeatedly emphasized, there is ‘no duty to deal under the terms and conditions preferred by [a competitor’s] rivals[]’ Likewise, “the Sherman Act ‘does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent
discretion as to parties with whom he will deal.” Trinko, 540 U.S. at 408 (alteration in original).

The one, limited exception to this general rule that there is no antitrust duty to deal comes under the Supreme Court’s decision in Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985). There, the Court held that a company engages in prohibited, anticompetitive conduct when (1) it “unilateral[ly] terminat[es] . . . a voluntary and profitable course of dealing”; (2) “the only conceivable rationale or purpose is ‘to sacrifice short- term benefits in order to obtain higher profits in the long run from the exclusion of competition’”; and (3) the refusal to deal involves products that the defendant already sells in the existing market to other similarly situated customers. The Supreme Court later characterized the Aspen Skiing exception as “at or near the outer boundary of § 2 liability.” Trinko, 540 U.S. at 409.

The district court’s conclusion that Qualcomm’s refusal to provide exhaustive SEP licenses to rival chip suppliers meets the Aspen Skiing exception ignores critical differences between Qualcomm’s business practices and the conduct at issue in Aspen Skiing, and it ignores the Supreme Court’s subsequent warning in Trinko that the Aspen Skiing exception should be applied only in rare circumstances.

First, the district court was incorrect that “Qualcomm terminated a ‘voluntary and profitable course of dealing’” with respect to its previous practice of licensing at the chip-manufacturer level. In support of this finding, the district court cited a single piece of record evidence: an email from a Qualcomm lawyer regarding 3%-royalty-bearing licenses for modem chip suppliers. But this email was sent in 1999, seven years before Qualcomm gained monopoly power in the CDMA modem chip market. Furthermore, Qualcomm claims that it never granted exhaustive licenses to rival chip suppliers. Instead, as the 1999 email suggests, it entered into “non-exhaustive, royalty-bearing agreements with chipmakers that explicitly did not grant rights to the chipmaker’s customers.”

According to Qualcomm, it ceased this practice in response to developments in patent law’s exhaustion doctrine, which made it harder for Qualcomm to argue that it could provide “non-exhaustive” licenses in the form of royalty agreements. Nothing in the record or in the district court’s factual findings rebuts these claims. The FTC offered no evidence that, from the time Qualcomm first gained monopoly power in the modem chip market in 2006 until

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now, it ever had a practice of providing exhaustive licenses at the modem chip level rather than the OEM level.

Second, Qualcomm’s rationale for “switching” to OEM- level licensing was not “to sacrifice short-term benefits in order to obtain higher profits in the long run from the exclusion of competition,” the second element of the Aspen Skiing exception. Instead, Qualcomm responded to the change in patent-exhaustion law by choosing the path that was “far more lucrative,” both in the short term and the long term, regardless of any impacts on competition. The district court itself acknowledged that this was Qualcomm’s purpose, observing: “Following Qualcomm’s lead, other SEP licensors like Nokia and Ericsson have concluded that licensing only OEMs is more lucrative, and structured their practices accordingly.”

Finally, unlike in Aspen Skiing, the district court found no evidence that Qualcomm singles out any specific chip supplier for anticompetitive treatment in its SEP-licensing. In Aspen Skiing, the defendant refused to sell its lift tickets to a smaller, rival ski resort even as it sold the same lift tickets to any other willing buyer (including any other ski resort); moreover, this refusal was designed specifically to put the smaller, nearby rival out of business. Qualcomm applies its OEM-level licensing policy equally with respect to all competitors in the modem chip markets and declines to enforce its patents against these rivals even though they practice Qualcomm’s patents (royalty-free) . . .

As none of the required elements for the Aspen Skiing exception are present, let alone all of them, the district court erred in holding that Qualcomm is under an antitrust duty to license rival chip manufacturers. We hold that Qualcomm’s OEM-level licensing policy, however novel, is not an anticompetitive violation of the Sherman Act.

B

Conceding error in the district court’s conclusion that Qualcomm is subject to an antitrust duty to deal under Aspen Skiing, the FTC contends that this court may nevertheless hold that Qualcomm engaged in anticompetitive conduct in violation of § 2. This is so, the FTC urges, because

“Qualcomm entered into a voluntary contractual commitment to deal with its rivals as part of the SSO process, which is itself a derogation from normal market competition,” and (2) Qualcomm’s breach of this contractual commitment “satisfies traditional Section 2 standards [in that] it ‘tends to impair the
opportunities of rivals and . . . does not further competition on the merits.” We disagree.

Even if the district court is correct that Qualcomm is contractually obligated via its SSO commitments to license rival chip suppliers—a conclusion we need not and do not reach—the FTC still does not satisfactorily explain how Qualcomm’s alleged breach of this contractual commitment itself impairs the opportunities of rivals. It argues the breach “facilitat[es] Qualcomm’s collection of a surcharge from rivals’ customers.” Appellee’s Br. at 77. But this refers to a distinct business practice, licensing royalties, and alleged harm to OEMs, not rival chipmakers. In any case, Qualcomm’s royalties are “chip-supplier neutral” because Qualcomm collects them from all OEMs that license its patents, not just “rivals’ customers.” The FTC argues that Qualcomm’s breach directly impacts rivals by “otherwise deterring [their] entry and investment.” But this ignores that Qualcomm’s “CDMA ASIC Agreements” functionally act as de facto licenses (“no license, no problem”) by allowing competitors to practice Qualcomm’s SEPs (royalty-free) before selling their chips to downstream OEMs. Furthermore, in order to make out a § 2 violation, the anticompetitive harm identified must be to competition itself, not merely to competitors. The FTC identifies no such harm to competition.

The FTC’s conclusion that OEM-level licensing does not further competition on the merits is not only belied by MediaTek and Intel’s entries into the modem chip markets in the 2015–2016 timeframe, it also gives inadequate weight to Qualcomm’s reasonable, procompetitive justification that licensing at the OEM and chip-supplier levels simultaneously would require the company to engage in “multi-level licensing,” leading to inefficiencies and less profit. Qualcomm’s procompetitive justification is supported by at least two other companies—Nokia and Dolby—with similar SEP portfolios to Qualcomm’s.11 More critically, this part of the FTC’s

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1 See Br. of Amicus Curiae Nokia Technologies Oy at 18–19 (noting that “[t]here are good reasons for SEP owners to structure their licensing programs to license end-user products,” including the reduction of “transaction costs and complexities associated with negotiating and executing licenses at multiple points in the supply chain,” the avoidance of “overlapping and duplicative licensing,” “expedite[d] access to SEPs for the entire supply chain,” and “greater visibility to what products are actually licensed, for example, for auditing purposes”); Br. of Amicus Curiae Dolby Laboratories, Inc. at 28 (“Forcing SEP holders to license component suppliers would interfere with historical precedents and established practices, and produce
argument skips ahead to an examination of Qualcomm’s procompetitive justifications, failing to recognize that the burden does not shift to Qualcomm to provide such justifications unless and until the FTC meets its initial burden of proving anticompetitive harm. Because the FTC has not met its initial burden under the rule of reason framework, we are less critical of Qualcomm’s procompetitive justifications for its OEM-level licensing policy—which, in any case, appear to be reasonable and consistent with current industry practice.

* * *

Finally, we note the persuasive policy arguments of several academics and practitioners with significant experience in SSOs, FRAND, and antitrust enforcement, who have expressed caution about using the antitrust laws to remedy what are essentially contractual disputes between private parties engaged in the pursuit of technological innovation.

* * *

C

We next address the district court’s primary theory of anticompetitive harm: Qualcomm’s imposition of an “anticompetitive surcharge” on rival chip suppliers via its licensing royalty rates. According to the district court, Qualcomm’s unreasonably high royalty rates enable Qualcomm to control rivals’ prices because Qualcomm receives the royalty even when an OEM uses one of Qualcomm’s rival’s chips. Thus, the “all-in” price of any modem chip sold by one of Qualcomm’s rivals effectively includes two components: (1) the nominal chip price; and (2) Qualcomm’s royalty surcharge.

This central component of the district court’s ruling is premised on the district court’s findings that Qualcomm’s royalty rates are (1) “unreasonably high” because they are improperly based on Qualcomm’s monopoly chip market share and handset price instead of the “fair value of Qualcomm’s patents,” and (2) anticompetitive because they raise costs to OEMs, who pass the extra costs along to consumers and are forced to invest less in other handset features.

We hold that the district court’s “anticompetitive surcharge” theory fails to state a cogent theory of anticompetitive harm. . .

significant inefficiencies and lack of transparency regarding whether products in the stream of commerce are in fact licensed.”

57
First, the district court’s determination that Qualcomm’s royalty rates are “unreasonable” because they are based on handset prices misinterprets Federal Circuit law regarding “the patent rule of apportionment” and the smallest salable patent-practicing unit (“SSPPU”). The district court observed “that ‘it is generally required that royalties be based not on the entire product, but instead on the [SSPPU].’” Qualcomm, 411 F. Supp. 3d at 783.

Even if we accept that the modem chip in a cellphone is the cellphone’s SSPPU, the district court’s analysis is still fundamentally flawed. No court has held that the SSPPU concept is a per se rule for “reasonable royalty” calculations; instead, the concept is used as a tool in jury cases to minimize potential jury confusion when the jury is weighing complex expert testimony about patent damages. . . .

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A second problem with the district court’s “unreasonable royalty rate” conclusion is that it erroneously assumes that royalties are “anticompetitive”—in the antitrust sense—unless they precisely reflect a patent’s current, intrinsic value and are in line with the rates other companies charge for their own patent portfolios. Neither the district court nor the FTC provides any case law to support this proposition, which sounds in patent law, not antitrust law. . . . We decline to adopt a theory of antitrust liability that would presume anticompetitive conduct any time a company could not prove that the “fair value” of its SEP portfolios corresponds to the prices the market appears willing to pay for those SEPs in the form of licensing royalty rates.

Finally, even assuming that a deviation between licensing royalty rates and a patent portfolio’s “fair value” could amount to “anticompetitive harm” in the antitrust sense, the primary harms the district court identified here were to the OEMs who agreed to pay Qualcomm’s royalty rates—that is, Qualcomm’s customers, not its competitors. These harms were thus located outside the “areas of effective competition”—the markets for CDMA and premium LTE modem chips—and had no direct impact on competition in those markets. See Rambus, 522 F.3d at 464 (noting that if a practice “raises the price secured by a seller” or otherwise harms customers, “but does so without harming competition, it is beyond the antitrust laws’ reach”).
Regardless of the “reasonableness” of Qualcomm’s royalty rates, the district court erred in finding that these royalties constitute an “artificial surcharge” on rivals’ chip sales. In _Caldera, Inc. v. Microsoft Corp._, 87 F. Supp. 2d 1244 (D. Utah 1999), the primary case relied upon by the district court for its surcharging theory, Microsoft required OEMs “to pay [it] a royalty on every machine the OEM shipped regardless of whether the machine contained MS DOS or another operating system.” This resulted in OEMs having to pay two royalties instead of one for a portion of their product base unless they chose to exclusively install Microsoft’s operating system in their products. Microsoft’s policy thus had “the practical effect of exclusivity,” as it imposed a naked tax on rivals’ software even when the end-product—an individual computer installed with a non-Microsoft operating system—contained no added value from Microsoft.

Qualcomm’s licensing royalties are qualitatively different from the per-unit operating-system royalties at issue in _Caldera_. When Qualcomm licenses its SEPs to an OEM, those patent licenses have value—indeed, they are necessary to the OEM’s ability to market and sell its cellular products to consumers—regardless of whether the OEM uses Qualcomm’s modem chips or chips manufactured and sold by one of Qualcomm’s rivals. And unlike _Caldera_, where OEMs who installed non-Microsoft operating systems in some of their products were required to pay royalties for both the actual operating system and MS DOS (which was not installed), here OEMs do not pay twice for SEP licenses when they use non-Qualcomm modem chips. Thus, unlike Microsoft’s practice, Qualcomm’s practice does not have the “practical effect of exclusivity”.

In its complaint and in its briefing, the FTC suggests that Qualcomm’s royalty rates impose an anticompetitive surcharge on its rivals’ sales not for the reasons at play in _Caldera_, but rather because Qualcomm uses its licensing royalties to charge anticompetitive, ultralow prices on its own modem chips—pushing out rivals by squeezing their profit margins and preventing them from making necessary investments in research and development. But this type of “margin squeeze” was rejected as a basis for antitrust liability in _linkLine_. 555 U.S. at 451–52, 457. There, multiple digital subscriber line (“DSL”) high-speed internet service providers complained that AT&T was selling them access to AT&T’s must-have telephone lines and facilities at inflated wholesale rates and then shifting those increased profits to charge ultra-low rates for DSL.
services at retail, effectively squeezing these DSL competitors out of the market. The Court rejected the plaintiffs’ assertion of anticompetitive harm, holding that AT&T was under no antitrust duty to deal with its competitors on the wholesale level, and that the plaintiffs failed to introduce evidence of predatory pricing (that is, charging below cost) at the retail level.

Here, not only did the FTC offer no evidence that Qualcomm engaged in predatory pricing, the district court’s entire antitrust analysis is premised on the opposite proposition: that Qualcomm “charge[s] monopoly prices on modem chips.” Indeed, the district court faulted Qualcomm for lowering its prices only when other companies introduced CDMA modem chips to the market to effectively compete. We agree with Qualcomm that this is exactly the type of “garden-variety price competition that the law encourages,” and are aware of no authority holding that a monopolist may not lower its rates in response to a competitor’s entry into the market with a lower-priced product.

As with its critique of Qualcomm’s royalty rates, the district court’s analysis of Qualcomm’s “no license, no chips” policy focuses almost exclusively on alleged “anticompetitive harms” to OEMs—that is, impacts outside the relevant antitrust market. The district court labeled Qualcomm’s policy “anticompetitive conduct against OEMs” and an “anticompetitive practice[] in patent license negotiations.” But the district court failed to identify how the policy directly impacted Qualcomm’s competitors or distorted “the area of effective competition.” _Am. Express_, 138 S. Ct. at 2285.

According to the FTC, the problem with “no license, no chips” is that, under the policy, “Qualcomm will not sell chips to a cellphone [OEM] like Apple or Samsung unless the OEM agrees to a license that requires it to pay a substantial per-phone surcharge even on phones that use rivals’ chips.” But this argument is self-defeating: if the condition imposed on gaining access to Qualcomm’s chip supply applies regardless of whether the OEM chooses Qualcomm or a competitor (in fact, this appears to be the essence of Qualcomm’s policy), then the condition by definition does not distort the “area of effective competition” or impact competitors. At worst, the policy raises the “all-in” price that an OEM must pay for modem chips (chipset + licensing royalties) regardless of which
chip supplier the OEM chooses to source its chips from. As we have already discussed, whether that all-in price is reasonable or unreasonable is an issue that sounds in patent law, not antitrust law. Additionally, it involves potential harms to Qualcomm’s customers, not its competitors, and thus falls outside the relevant antitrust markets.

* * *

E

Having addressed the primary components of the district court’s antitrust ruling with respect to Qualcomm’s general business practices, we now address the district court’s more specific finding that from 2011 to 2015, Qualcomm violated both sections of the Sherman Act by signing “exclusive deals” with Apple that “foreclosed a ‘substantial share’ of the [CDMA] modem chip market.”

* * *

Qualcomm argues that its agreements with Apple were “volume discount contracts, not exclusive dealings contracts.” Unlike exclusive dealing arrangements, “volume discount contracts are legal under antitrust law . . . [b]ecause the contracts do not preclude consumers from using other . . . services.” Likewise, conditional agreements that provide “substantial discounts to customers that actually purchase[] a high percentage of their . . . requirements from” a firm are not exclusive dealing arrangements, de facto or actual, unless they “prevent[] the buyer from purchasing a given good from any other vendor.”

* * *

There is some merit in the district court’s conclusion that the Apple agreements were structured more like exclusive dealing contracts than volume discount contracts. However, we do not agree that these agreements had the actual or practical effect of substantially foreclosing competition in the CDMA modem chip market, or that injunctive relief is warranted.

During the relevant time period (2011–2015), the record suggests that the only serious competition Qualcomm faced with respect to the Apple contracts was from Intel, a company from whom Apple had considered purchasing modem chips prior to signing the 2013 agreement with Qualcomm. The district court made no finding that any other specific competitor or potential competitor was affected by either of Qualcomm’s agreements with Apple, and it is undisputed that Intel won Apple’s business the very next year, in 2014, when Apple’s engineering team unanimously recommended that the
company select Intel as an alternative supplier of modem chips. The
district court found that “Qualcomm’s exclusive deals . . . delayed
Intel’s ability to sell modem chips to Apple until September 2016.”
There is no indication in the record, however, that Intel was a viable
competitor to Qualcomm prior to 2014–2015, or that the 2013
agreement delayed Apple’s transition to Intel by any more than one
year. Given these undisputed facts, we conclude that the 2011 and
2013 agreements did not have the actual or practical effect of
substantially foreclosing competition in the CDMA modem chip
market.

* * *

We therefore REVERSE the district court’s judgment and
VACATE its injunction as well as its partial grant of summary
judgment.

NOTES AND QUESTIONS

1. Rule of reason. Was the court correct when it said that “the	hree-part burden-shifting test under the rule of reason is
essentially the same” under Section 1 and Section 2 of the Sherman
Act? Was it correct that “a plaintiff may not use indirect evidence
to prove unlawful monopoly maintenance via anticompetitive conduct
under § 2”? If so, is that a sensible rule?

2. The “no license/no chips” policy. Qualcomm’s no license/no
chip policy was the core of the FTC’s case. The court’s opinion does
not fully describe the policy or the issues it raises.

Ordinarily, when a firm sells a product that includes patented
technologies, like Qualcomm’s chips, the buyer acquires both the
product and, as a matter of law, an implied patent license. The buyer
does not need to obtain an additional or separate license to the
patented technologies in the product, and she may resell the product
to another buyer, who is also not required to obtain an additional or
separate patent license. The initial sale of the product is deemed, as a
matter of law, to “exhaust” the seller’s rights in the patents covering
technologies implemented in the product. See Quanta Comput., Inc.
charges the buyer a single price that encompasses both the product
and the implied patent license.

Patents are also often licensed in transactions that do not
involve the sale of products. The licensors in these transactions
might be technology firms, or patent assertion entities whose
business is to acquire and then license patents, that do not sell any
products; or they might be firms that both sell products and license
their patented technologies separately when they are used in other
products. Especially in the information technology industry, in which products like mobile phones can include technologies claimed by literally tens of thousands of patents, these licensing transactions commonly take place after the implementer has manufactured and sold the allegedly infringing products. At that point, if the patents are valid and infringed, the implementer has no legal right to refuse take a license.

When patents are licensed separately, the royalty or price is constrained by the often substantial likelihood that the patent would if litigated be found to be invalid or not infringed and by the parties’ estimate of the “reasonable royalty” remedy a court would order if they fail to reach agreement and the matter is litigated in a patent infringement suit. When, as in the Qualcomm case, SEPs are involved, the price is also constrained by the FRAND commitment.

Qualcomm’s no license/no chips policy is a hybrid of these two licensing methods. Qualcomm requires OEMs to agree to a separate patent license on terms specified by it in order to buy chips. If the license applied only to Qualcomm chips, the policy would be of no substantive consequence. Qualcomm could allocate the monopoly price that it would otherwise charge for the chips with an implied patent license partly to the chips and partly to the license, but the total monopoly price would remain the same.

The problem, according to the FTC, is that Qualcomm’s no license/no chips policy requires OEMs, as a condition of purchasing chips from Qualcomm, to agree to a patent license, on terms specified by it, that covers both Qualcomm’s chips and chips manufactured by Qualcomm’s competitors. Chips manufactured by Qualcomm’s competitors, like Qualcomm’s chips, use technologies claimed by Qualcomm’s patents. Because Qualcomm has a substantial monopoly in chips, OEMs are required as a practical matter to buy at least some of their chips from Qualcomm. The no license/no chips policy thus means that OEMs have to agree to license terms specified by Qualcomm for both Qualcomm chips and chips manufactured by others.

The district court found that, by using the monopoly power of its chips to insist on its desired royalties, Qualcomm is able to extract patent royalties higher than those that would have been agreed to if the patent license were negotiated separately and constrained by the risks of invalidity and non-infringement, the prospect of a “reasonable royalty” remedy in infringement litigation, and the Qualcomm’s FRAND commitment. The district court called the difference in royalty amounts a “surcharge.” The FTC argued that that surcharge increases the cost to OEMs of using chips sold by
Qualcomm’s competitors, reduces their demand for competitors’ chips, and thus serves to maintain Qualcomm’s chip monopoly.

The district court agreed with the FTC and held that the no license/no chips policy violated the Sherman Act. The court of appeals reversed the district court on that issue for three reasons.

(a) First, the court reasoned that the harm from the policy is that it allegedly results in increased license fees paid by device manufacturers, that a mere price increase is not injury to competition for antitrust purposes, and that in any event the price increase harms OEMs and the harm thus occurs outside the relevant antitrust market. Do you think the court’s reasoning is correct? Could similar reasoning have been used to find for the defendant in *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001) (en banc), on the ground that the harm there was to competing browsers and was thus outside the relevant OS market? What about a loyalty discount case in which the defendant charges customers higher prices if they deal with competitors? (Loyalty discounts are discussed at pp 617-623 in the main text.)

(b) Second, the court repeatedly said that the policy is “chip supplier neutral” and held that, even if the license fee is inflated by the policy, it does not harm competition because the same fee applies to both Qualcomm chips and rival chips. Do you think the court’s reasoning is correct? Is the policy really chip supplier neutral if, as the court found, Qualcomm offsets the high license fees by reducing the price of Qualcomm chips but provides no offset when the OEM purchased rivals’ chips? Even if Qualcomm had not offset the license fee increase, would the policy be chip supplier neutral given that the increased license fee is paid to Qualcomm but not to its competitors?

(c) Third, the court held that, to the extent that the FTC was complaining that Qualcomm reduced the prices for its chips and thus squeezed competitors’ margins, it was engaged in a lawful “margin squeeze” under *linkLine*. Do you think the court was correct? In thinking about that question, you might consider the following:

- In *linkLine*, the defendant sold inputs in the upstream market to firms with which it competed in the downstream market. Qualcomm does not sell to its competitors (chip makers) in the upstream (licensing) market, and it does not sell anything in the downstream (mobile phone) market.

- In *John Doe v. Abbott Laboratories*, 571 F.3d 930 (9th Cir. 2009), plaintiffs alleged that competing suppliers of protease inhibitors used to treat HIV were harmed because the defendant increased the price of a
complementary drug used to “boost” protease inhibitors, over which the defendant had a monopoly, but did not increase the price of its “boosted” protease inhibitor. The court held that the claim was barred by *linkLine*. In both *John Doe* and *linkLine*, the allegedly excessive price for the input or complement reflected the defendant’s market power over that product; in *Qualcomm*, by contrast, the FTC alleged that the excessive price of the patent license reflected the market power of a different product, Qualcomm’s chips.

- The rationale of *linkLine* was that the defendant could not cause more harm by selling an input at a high price than by exercising its lawful right to refuse to sell the input altogether. 555 U.S. at 450. Qualcomm, however, could not inflict the same or worse harm by refusing to license its patents to OEMs because Qualcomm was required to license its SEPs on reasonable (FRAND) terms.

3. *Business justification.* The no license/no chips policy enables Qualcomm to deal with OEMs in one transaction covering chip sales and patent licenses for chips sold by its competitors and thus to avoid the risk that OEMs might buy chips from Qualcomm and make Qualcomm sue it to collect patent royalties on its competitors’ chips. Assuming that the no license/no chips policy does harm rival chip makers and help maintain Qualcomm’s chip monopoly, do you think this transaction cost saving is sufficient to justify the policy under the Sherman Act? In thinking about this question, bear in mind that cost savings are ordinarily passed on at least in part to customers but the district court found that the no license/no chips policy results in higher prices for buyers. Consider also (i) the fact that the no license/no chips policy is unique and patent holders generally must deal with transaction costs and litigation risks when licensing their patents and (ii) the court’s concern about hostility to novel business practices, which is discussed in the next paragraph.

4. *Novel business practices.* The court repeatedly expressed the concern that antitrust law might be too quick to condemn novel business practices that disadvantage customers and competitors but are in fact valuable and efficient innovations for reasons that might not be readily apparent to the court. Does this concern seem realistic? Should the law deal with that risk by being especially skeptical of antitrust challenges to novel business practices? Might such skepticism encourage firms to devised novel business strategies to exclude rivals and then argue that antitrust law should be especially
cautious because the conduct is unfamiliar? How else might the law deal with that risk?

5. *Is the antitrust analysis different because patents are involved?* Should the antitrust analysis be different in the *Qualcomm* case from that in an ordinary case because the case involved patent licenses? If so, why and how should the analysis differ? As discussed in the main text (pp 891-892, 908-910), patents differ from tangible property because patents are nonrivalrous, they are for a limited term, and the validity and scope of patents are often uncertain. Should any of these differences affect the analysis in the *Qualcomm* case? Are there any other differences between patents and other kinds of property that should affect the analysis?

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**Ohio v. American Express Co.**

Supreme Court of the United States, 2018.


[replace the Visa decision and the lower court American Express decision at pp. 956-995]

THOMAS, J., delivered the opinion of the Court. American Express Company and American Express Travel Related Services Company (collectively, Amex) provide credit-card services to both merchants and cardholders. When a cardholder buys something from a merchant who accepts Amex credit cards, Amex processes the transaction through its network, promptly pays the merchant, and subtracts a fee. If a merchant wants to accept Amex credit cards—and attract Amex cardholders to its business—Amex requires the merchant to agree to an anti-steering contractual provision. The anti-steering provision prohibits merchants from discouraging customers from using their Amex card after they have already entered the store and are about to buy something, thereby avoiding Amex’s fee. In this case, we must decide whether Amex’s anti-steering provisions violate federal antitrust law. We conclude they do not.

I

A

Credit cards have become a primary way that consumers in the United States purchase goods and services. When a cardholder uses a credit card to buy something from a merchant, the transaction is facilitated by a credit card network. The network provides separate but interrelated services to both cardholders and merchants. For cardholders, the network extends them credit, which allows them to
make purchases without cash and to defer payment until later. Cardholders also can receive rewards based on the amount of money they spend, such as airline miles, points for travel, or cash back. For merchants, the network allows them to avoid the cost of processing transactions and offers them quick, guaranteed payment. This saves merchants the trouble and risk of extending credit to customers, and it increases the number and value of sales that they can make.

By providing these services to cardholders and merchants, credit-card companies bring these parties together, and therefore operate what economists call a “two-sided platform.” As the name implies, a two-sided platform offers different products or services to two different groups who both depend on the platform to intermediate between them. For credit cards, that interaction is a transaction. Thus, credit-card networks are a special type of two-sided platform known as a “transaction” platform. The key feature of transaction platforms is that they cannot make a sale to one side of the platform without simultaneously making a sale to the other. For example, no credit card transaction can occur unless both the merchant and the cardholder simultaneously agree to use the same credit-card network.

Two-sided platforms differ from traditional markets in important ways. Most relevant here, two-sided platforms often exhibit what economists call “indirect network effects.” Indirect network effects exist where the value of the two-sided platform to one group of participants depends on how many members of a different group participate. In other words, the value of the services that a two-sided platform provides increases as the number of participants on both sides of the platform increases. A credit card, for example, is more valuable to cardholders when more merchants accept it, and is more valuable to merchants when more cardholders use it. To ensure sufficient participation, two-sided platforms must be sensitive to the prices that they charge each side. Raising the price on side A risks losing participation on that side, which decreases the value of the platform to side B. If participants on side B leave due to this loss in value, then the platform has even less value to side A—risking a feedback loop of declining demand. Two-sided platforms therefore must take these indirect network effects into account before making a change in price on either side.

Sometimes indirect network effects require two-sided platforms to charge one side much more than the other. For two-sided platforms, “the [relative] price structure matters, and platforms must design it so as to bring both sides on board.” The optimal price might require charging the side with more elastic demand a below-cost (or
even negative) price. With credit cards, for example, networks often charge cardholders a lower fee than merchants because cardholders are more price sensitive. In fact, the network might well lose money on the cardholder side by offering rewards such as cash back, airline miles, or gift cards. The network can do this because increasing the number of cardholders increases the value of accepting the card to merchants and, thus, increases the number of merchants who accept it. Networks can then charge those merchants a fee for every transaction (typically a percentage of the purchase price). Striking the optimal balance of the prices charged on each side of the platform is essential for two-sided platforms to maximize the value of their services and to compete with their rivals.

B

Amex, Visa, MasterCard, and Discover are the four dominant participants in the credit-card market. Visa, which is by far the largest, has 45% of the market as measured by transaction volume. Amex and MasterCard trail with 26.4% and 23.3%, respectively, while Discover has just 5.3% of the market. Visa and MasterCard have significant structural advantages over Amex. Visa and MasterCard began as bank cooperatives and thus almost every bank that offers credit cards is in the Visa or MasterCard network. This makes it very likely that the average consumer carries, and the average merchant accepts, Visa or MasterCard. As a result, the vast majority of Amex cardholders have a Visa or MasterCard, but only a small number of Visa and MasterCard cardholders have an Amex. Indeed, Visa and MasterCard account for more than 432 million cards in circulation in the United States, while Amex has only 53 million. And while 3.4 million merchants at 6.4 million locations accept Amex, nearly three million more locations accept Visa, MasterCard, and Discover.

Amex competes with Visa and MasterCard by using a different business model. While Visa and MasterCard earn half of their revenue by collecting interest from their cardholders, Amex does not. Amex instead earns most of its revenue from merchant fees. Amex’s business model thus focuses on cardholder spending rather than cardholder lending. To encourage cardholder spending, Amex provides better rewards than other networks. Due to its superior rewards, Amex tends to attract cardholders who are wealthier and spend more money. Merchants place a higher value on these cardholders, and Amex uses this advantage to recruit merchants.

Amex’s business model has significantly influenced the credit-card market. To compete for the valuable cardholders that Amex attracts, both Visa and MasterCard have introduced premium cards
that, like Amex, charge merchants higher fees and offer cardholders better rewards. To maintain their lower merchant fees, Visa and MasterCard have created a sliding scale for their various cards—charging merchants less for low-reward cards and more for high-reward cards. This differs from Amex’s strategy, which is to charge merchants the same fee no matter the rewards that its card offers. Another way that Amex has influenced the credit-card market is by making banking and card-payment services available to low-income individuals, who otherwise could not qualify for a credit card and could not afford the fees that traditional banks charge. . . .

Despite these improvements, Amex’s business model sometimes causes friction with merchants. To maintain the loyalty of its cardholders, Amex must continually invest in its rewards program. But, to fund those investments, Amex must charge merchants higher fees than its rivals. Even though Amex’s investments benefit merchants by encouraging cardholders to spend more money, merchants would prefer not to pay the higher fees. One way that merchants try to avoid them, while still enticing Amex’s cardholders to shop at their stores, is by dissuading cardholders from using Amex at the point of sale. This practice is known as “steering.”

Amex has prohibited steering since the 1950s by placing anti-steering provisions in its contracts with merchants. These anti-steering provisions prohibit merchants from implying a preference for non-Amex cards; dissuading customers from using Amex cards; persuading customers to use other cards; imposing any special restrictions, conditions, disadvantages, or fees on Amex cards; or promoting other cards more than Amex. The anti-steering provisions do not, however, prevent merchants from steering customers toward debit cards, checks, or cash.

C

In October 2010, the United States and several States (collectively, plaintiffs) sued Amex, claiming that its anti-steering provisions violate §1 of the Sherman Act. After a 7-week trial, the District Court agreed that Amex’s anti-steering provisions violate §1. It found that the credit-card market should be treated as two separate markets—one for merchants and one for cardholders. Evaluating the effects on the merchant side of the market, the District Court found that Amex’s anti-steering provisions are anticompetitive because they result in higher merchant fees.

The Court of Appeals for the Second Circuit reversed. It concluded that the credit-card market is one market, not two. Evaluating the credit card market as a whole, the Second Circuit
concluded that Amex’s anti-steering provisions were not anticompetitive and did not violate §1. We granted certiorari and now affirm.

II

Section 1 of the Sherman Act prohibits “[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States.” 15 U. S. C. §1. This Court has long recognized that, “[i]n view of the common law and the law in this country” when the Sherman Act was passed, the phrase “restraint of trade” is best read to mean “undue restraint.” Standard Oil Co. of N. J. v. United States, 221 U. S. 1, 59-60 (1911). This Court’s precedents have thus understood §1 “to outlaw only unreasonable restraints.” State Oil Co. v. Khan, 522 U. S. 3, 10 (1997) (emphasis added).

Restraints can be unreasonable in one of two ways. A small group of restraints are unreasonable per se because they “‘always or almost always tend to restrict competition and decrease output.’” Business Electronics Corp. v. Sharp Electronics Corp., 485 U.S. 717, 723 (1988). Typically only “horizontal” restraints—restraints “imposed by agreement between competitors”—qualify as unreasonable per se. Id., at 730. Restraints that are not unreasonable per se are judged under the “rule of reason.” Id., at 723. The rule of reason requires courts to conduct a fact-specific assessment of “market power and market structure . . . to assess the [restraint]’s actual effect” on competition. Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 768 (1984). The goal is to “distinguish between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer’s best interest.” Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551 U. S. 877, 886 (2007).

In this case, both sides correctly acknowledge that Amex’s anti-steering provisions are vertical restraints—i.e., restraints “imposed by agreement between firms at different levels of distribution.” Business Electronics, supra, at 730. The parties also correctly acknowledge that, like nearly every other vertical restraint, the anti-steering provisions should be assessed under the rule of reason.

To determine whether a restraint violates the rule of reason, the parties agree that a three-step, burden shifting framework applies. Under this framework, the plaintiff has the initial burden to prove that the challenged restraint has a substantial anticompetitive effect that harms consumers in the relevant market. If the plaintiff carries its burden, then the burden shifts to the defendant to show a
procompetitive rationale for the restraint. If the defendant makes this showing, then the burden shifts back to the plaintiff to demonstrate that the procompetitive efficiencies could be reasonably achieved through less anticompetitive means.

Here, the parties ask us to decide whether the plaintiffs have carried their initial burden of proving that Amex’s anti-steering provisions have an anticompetitive effect. The plaintiffs can make this showing directly or indirectly. Direct evidence of anticompetitive effects would be “proof of actual detrimental effects [on competition],” FTC v. Indiana Federation of Dentists, 476 U.S. 447, 460 (1986), such as reduced output, increased prices, or decreased quality in the relevant market. Indirect evidence would be proof of market power plus some evidence that the challenged restraint harms competition.

Here, the plaintiffs rely exclusively on direct evidence to prove that Amex’s anti-steering provisions have caused anticompetitive effects in the credit-card market. To assess this evidence, we must first define the relevant market. Once defined, it becomes clear that the plaintiffs’ evidence is insufficient to carry their burden.

A

Because “[l]egal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored in antitrust law,” Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 466–467 (1992), courts usually cannot properly apply the rule of reason without an accurate definition of the relevant market. “Without a definition of [the] market there is no way to measure [the defendant’s] ability to lessen or destroy competition.” Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172, 177 (1965). Thus, the relevant market is defined as “the

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7 The plaintiffs argue that we need not define the relevant market in this case because they have offered actual evidence of adverse effects on competition—namely, increased merchant fees. We disagree. The cases that the plaintiffs cite for this proposition evaluated whether horizontal restraints had an adverse effect on competition. Given that horizontal restraints involve agreements between competitors not to compete in some way, this Court concluded that it did not need to precisely define the relevant market to conclude that these agreements were anticompetitive. Vertical restraints often pose no risk to competition unless the entity imposing them has market power, which cannot be evaluated unless the Court first defines the relevant market. See Easterbrook, Vertical Arrangements and the Rule of Reason, 53 Antitrust L. J. 135, 160 (1984) (“[T]he possibly anticompetitive manifestations of vertical arrangements can occur only if there is market power”).
area of effective competition.” Ibid. Typically this is the “arena within which significant substitution in consumption or production occurs” [citation omitted]. But courts should “combin[e]” different products or services into “a single market” when “that combination reflects commercial realities.” United States v. Grinnell Corp., 384 U.S. at 572.

As explained, credit-card networks are two-sided platforms. Due to indirect network effects, two-sided platforms cannot raise prices on one side without risking a feedback loop of declining demand. And the fact that two-sided platforms charge one side a price that is below or above cost reflects differences in the two sides’ demand elasticity, not market power or anticompetitive pricing. Price increases on one side of the platform likewise do not suggest anticompetitive effects without some evidence that they have increased the overall cost of the platform’s services. Thus, courts must include both sides of the platform—merchants and cardholders—when defining the credit-card market.

To be sure, it is not always necessary to consider both sides of a two-sided platform. A market should be treated as one sided when the impacts of indirect network effects and relative pricing in that market are minor. Newspapers that sell advertisements, for example, arguably operate a two-sided platform because the value of an advertisement increases as more people read the newspaper. But in the newspaper-advertisement market, the indirect networks effects operate in only one direction; newspaper readers are largely indifferent to the amount of advertising that a newspaper contains. Because of these weak indirect network effects, the market for newspaper advertising behaves much like a one-sided market and should be analyzed as such.

But two-sided transaction platforms, like the credit-card market, are different. These platforms facilitate a single, simultaneous transaction between participants. For credit cards, the network can sell its services only if a merchant and cardholder both simultaneously choose to use the network. Thus, whenever a credit-card network sells one transaction’s worth of card-acceptance services to a merchant it also must sell one transaction’s worth of card payment services to a cardholder. It cannot sell transaction services to either cardholders or merchants individually. To optimize sales, the network must find the balance of pricing that encourages the greatest number of matches between cardholders and merchants.

Because they cannot make a sale unless both sides of the platform simultaneously agree to use their services, two-sided transaction platforms exhibit more pronounced indirect network
effects and interconnected pricing and demand. Transaction platforms are thus better understood as “supply[ing] only one product”—transactions. [Klein, Lerner, Murphy, & Plache, *Competition in Two-Sided Markets: The Antitrust Economics of Payment Card Interchange Fees*, 73 Antitrust L. J. 571, 580 (2006)]. . . . Tellingly, credit cards determine their market share by measuring the volume of transactions they have sold.8

Evaluating both sides of a two-sided transaction platform is also necessary to accurately assess competition. Only other two-sided platforms can compete with a two-sided platform for transactions. A credit-card company that processed transactions for merchants, but that had no cardholders willing to use its card, could not compete with Amex. Only a company that had both cardholders and merchants willing to use its network could sell transactions and compete in the credit card market. Similarly, if a merchant accepts the four major credit cards, but a cardholder only uses Visa or Amex, only those two cards can compete for the particular transaction. Thus, competition cannot be accurately assessed by looking at only one side of the platform in isolation.9

For all these reasons, in two-sided transaction markets, only one market should be defined. Any other analysis would lead to “‘mistaken inferences’” of the kind that could “‘chill the very conduct the antitrust laws are designed to protect.’” *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 226 (1993). Accordingly, we will analyze the two-sided market for credit-card transactions as a whole to determine whether the plaintiffs have shown that Amex’s anti-steering provisions have anticompetitive effects.

B

The plaintiffs have not carried their burden to prove anticompetitive effects in the relevant market. The plaintiffs stake their entire case on proving that Amex’s agreements increase

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8 Contrary to the dissent’s assertion, merchant services and cardholder services are not complements. A two-sided market is different from markets for complementary products, in which both products are bought by the same buyers, who, in their buying decisions, can therefore be expected to take into account both prices. . . .

9 Non-transaction platforms, by contrast, often do compete with companies that do not operate on both sides of their platform. A newspaper that sells advertising, for example, might have to compete with a television network, even though the two do not meaningfully compete for viewers.
merchant fees. We find this argument unpersuasive. As an initial matter, the plaintiffs’ argument about merchant fees wrongly focuses on only one side of the two-sided credit-card market. As explained, the credit-card market must be defined to include both merchants and cardholders. Focusing on merchant fees alone misses the mark because the product that credit-card companies sell is transactions, not services to merchants, and the competitive effects of a restraint on transactions cannot be judged by looking at merchants alone. Evidence of a price increase on one side of a two-sided transaction platform cannot by itself demonstrate an anticompetitive exercise of market power. To demonstrate anticompetitive effects on the two-sided credit-card market as a whole, the plaintiffs must prove that Amex’s anti-steering provisions increased the cost of credit-card transactions above a competitive level, reduced the number of credit-card transactions, or otherwise stifled competition in the credit-card market. They failed to do so.

1

The plaintiffs did not offer any evidence that the price of credit-card transactions was higher than the price one would expect to find in a competitive market. As the District Court found, the plaintiffs failed to offer any reliable measure of Amex’s transaction price or profit margins. And the evidence about whether Amex charges more than its competitors was ultimately inconclusive.

Amex’s increased merchant fees reflect increases in the value of its services and the cost of its transactions, not an ability to charge above a competitive price. . . . As explained, Amex has historically charged higher merchant fees than these competitors because it delivers wealthier cardholders who spend more money. Amex’s higher merchant fees are based on a careful study of how much additional value its cardholders offer merchants. On the other side of the market, Amex uses its higher merchant fees to offer its cardholders a more robust rewards program, which is necessary to maintain cardholder loyalty and encourage the level of spending that makes Amex valuable to merchants. That Amex allocates prices between merchants and cardholders differently from Visa and MasterCard is simply not evidence that it wields market power to achieve anticompetitive ends.

In addition, the evidence that does exist cuts against the plaintiffs’ view that Amex’s anti-steering provisions are the cause of any increases in merchant fees. Visa and MasterCard’s merchant fees have continued to increase, even at merchant locations where Amex is not accepted and, thus, Amex’s anti-steering provisions do not apply. This suggests that the cause of increased merchant fees is not Amex’s
anti-steering provisions, but rather increased competition for cardholders and a corresponding marketwide adjustment in the relative price charged to merchants.

The plaintiffs did offer evidence that Amex increased the percentage of the purchase price that it charges merchants by an average of 0.09% between 2005 and 2010 and that this increase was not entirely spent on cardholder rewards. . . . [T]his evidence does not prove that Amex's anti-steering provisions gave it the power to charge anticompetitive prices. . . . This Court will “not infer competitive injury from price and output data absent some evidence that tends to prove that output was restricted or prices were above a competitive level.” Brooke Group Ltd., 509 U. S., at 237. There is no such evidence in this case. The output of credit-card transactions grew dramatically from 2008 to 2013, increasing 30%. “Where . . . output is expanding at the same time prices are increasing, rising prices are equally consistent with growing product demand.” Brooke Group Ltd., supra, at 237. And, as previously explained, the plaintiffs did not show that Amex charged more than its competitors.

The plaintiffs also failed to prove that Amex's anti-steering provisions have stifled competition among credit-card companies. To the contrary, while these agreements have been in place, the credit-card market experienced expanding output and improved quality. Amex’s business model spurred Visa and MasterCard to offer new premium card categories with higher rewards. And it has increased the availability of card services, including free banking and card-payment services for low-income customers who otherwise would not be served. Indeed, between 1970 and 2001, the percentage of households with credit cards more than quadrupled, and the proportion of households in the bottom-income quintile with credit cards grew from just 2% to over 38%.

Nor have Amex's anti-steering provisions ended competition between credit-card networks with respect to merchant fees. Instead, fierce competition between networks has constrained Amex's ability to raise these fees and has, at times, forced Amex to lower them. For instance, when Amex raised its merchant prices between 2005 and 2010, some merchants chose to leave its network. And when its remaining merchants complained, Amex stopped raising its merchant prices. In another instance in the late 1980s and early 1990s, competition forced Amex to offer lower merchant fees to “everyday
“spend” merchants—supermarkets, gas stations, pharmacies, and the like—to persuade them to accept Amex.

In addition, Amex’s competitors have exploited its higher merchant fees to their advantage. By charging lower merchant fees, Visa, MasterCard, and Discover have achieved broader merchant acceptance—approximately 3 million more locations than Amex. This broader merchant acceptance is a major advantage for these networks and a significant challenge for Amex, since consumers prefer cards that will be accepted everywhere. And to compete even further with Amex, Visa and MasterCard charge different merchant fees for different types of cards to maintain their comparatively lower merchant fees and broader acceptance. Over the long run, this competition has created a trend of declining merchant fees in the credit-card market. In fact, since the first credit card was introduced in the 1950s, merchant fees—including Amex’s merchant fees—have decreased by more than half.

Lastly, there is nothing inherently anticompetitive about Amex’s anti-steering provisions. These agreements actually stem negative externalities in the credit-card market and promote interbrand competition. When merchants steer cardholders away from Amex at the point of sale, it undermines the cardholder’s expectation of “welcome acceptance”—the promise of a frictionless transaction. A lack of welcome acceptance at one merchant makes a cardholder less likely to use Amex at all other merchants. This externality endangers the viability of the entire Amex network. And it undermines the investments that Amex has made to encourage increased cardholder spending, which discourages investments in rewards and ultimately harms both cardholders and merchants. Perhaps most importantly, anti-steering provisions do not prevent Visa, MasterCard, or Discover from competing against Amex by offering lower merchant fees or promoting their broader merchant acceptance.

In sum, the plaintiffs have not satisfied the first step of the rule of reason. They have not carried their burden of proving that Amex’s anti-steering provisions have anticompetitive effects. Amex’s business model has spurred robust interbrand competition and has increased the quality and quantity of credit-card transactions. . . . Because Amex’s anti-steering provisions do not unreasonably restrain trade, we affirm the judgment of the Court of Appeals.

It is so ordered.

BREYER, J., with whom GINSBURG, SOTOMAYOR, and KAGAN, J., join, dissenting: For more than 120 years, the American economy has prospered by charting a middle path between pure laissez-faire and
state capitalism, governed by an antitrust law dedicated to the principle that markets, not individual firms and certainly not political power, produce the optimal mixture of goods and services. By means of a strong antitrust law, the United States has sought to avoid the danger of monopoly capitalism. Long gone, we hope, are the days when the great trusts presided unfettered by competition over the American economy.

This lawsuit is emblematic of the American approach. Many governments around the world have responded to concerns about the high fees that credit-card companies often charge merchants by regulating such fees directly. The United States has not followed that approach. The Government instead filed this lawsuit, which seeks to restore market competition over credit-card merchant fees by eliminating a contractual barrier with anticompetitive effects. The majority rejects that effort. But because the challenged contractual term clearly has serious anticompetitive effects, I dissent.

I agree with the majority and the parties that this case is properly evaluated under the three-step “rule of reason” that governs many antitrust lawsuits. Under that approach, a court looks first at the agreement or restraint at issue to assess whether it has had, or is likely to have, anticompetitive effects. In doing so, the court normally asks whether the restraint may tend to impede competition and, if so, whether those who have entered into that restraint have sufficient economic or commercial power for the agreement to make a negative difference. Sometimes, but not always, a court will try to determine the appropriate market (the market that the agreement affects) and determine whether those entering into that agreement have the power to raise prices above the competitive level in that market.

It is important here to understand that in cases under §1 of the Sherman Act (unlike in cases challenging a merger under §7 of the Clayton Act, 15 U. S. C. §18), it may well be unnecessary to undertake a sometimes complex, market power inquiry: “Since the purpose [in a Sherman Act §1 case] of the inquiries into . . . market power is [simply] to determine whether an arrangement has the potential for genuine adverse effects on competition, ‘proof of actual detrimental effects, such as a reduction in output,’ can obviate the need for an inquiry into market power, which is but a ‘surrogate for detrimental effects.’” Indiana Federation of Dentists, supra, at 460–461.

Second, if an antitrust plaintiff meets the initial burden of showing that an agreement will likely have anticompetitive effects,
normally the burden shifts to the defendant to show that the restraint in fact serves a legitimate objective.

Third, if the defendant successfully bears this burden, the antitrust plaintiff may still carry the day by showing that it is possible to meet the legitimate objective in less restrictive ways, or, perhaps by showing that the legitimate objective does not outweigh the harm that competition will suffer, i.e., that the agreement “on balance” remains unreasonable.

Like the Court of Appeals and the parties, the majority addresses only the first step of that three-step framework.

II

A

This case concerns the credit-card business. As the majority explains, that business involves the selling of two different but related card services. First, when a shopper uses a credit card to buy something from a participating merchant, the credit-card company pays the merchant the amount of money that the merchant’s customer has charged to his card and charges the merchant a fee, say 5%, for that speedy-payment service. I shall refer to that kind of transaction as a merchant-related card service. Second, the credit-card company then sends a bill to the merchant’s customer, the shopper who holds the card; and the shopper pays the card company the sum that merchant charged the shopper for the goods or services he or she bought. The cardholder also often pays the card company a fee, such as an annual fee for the card or an interest charge for delayed payment. I shall call that kind of transaction a shopper-related card service. The credit card company can earn revenue from the sale (directly or indirectly) of each of these services: (1) speedy payment for merchants, and (2) credit for shoppers. (I say “indirectly” to reflect the fact that card companies often create or use networks of banks as part of the process—but I have found nothing here suggesting that that fact makes a significant difference to my analysis.)

Sales of the two basic card services are related. A shopper can pay for a purchase with a particular credit card only if the merchant has signed up for merchant-related card services with the company that issued the credit card that the shopper wishes to use. A firm in the credit-card business is therefore unlikely to make money unless quite a few merchants agree to accept that firm’s card and quite a few shoppers agree to carry and use it. In general, the more merchants that sign up with a particular card company, the more useful that card is likely to prove to shoppers and so the more shoppers will sign up; so
too, the more shoppers that carry a particular card, the more useful that card is likely to prove to merchants (as it obviously helps them obtain the shoppers’ business) and so the more merchants will sign up. Moreover, as a rough rule of thumb (and assuming constant charges), the larger the networks of paying merchants and paying shoppers that a card firm maintains, the larger the revenues that the firm will likely receive, since more payments will be processed using its cards. Thus, it is not surprising that a card company may offer shoppers incentives (say, points redeemable for merchandise or travel) for using its card or that a firm might want merchants to accept its card exclusively.

B

This case focuses upon a practice called “steering.” American Express has historically charged higher merchant fees than its competitors. Hence, fewer merchants accept American Express’ cards than its competitors’. But, perhaps because American Express cardholders are, on average, wealthier, higher-spending, or more loyal to American Express than other cardholders, vast numbers of merchants still accept American Express cards. Those who do, however, would (in order to avoid the higher American Express fee) often prefer that their customers use a different card to charge a purchase. Thus, the merchant has a monetary incentive to “steer” the customer towards the use of a different card. A merchant might tell the customer, for example, “American Express costs us more,” or “please use Visa if you can,” or “free shipping if you use Discover.”

Steering makes a difference, because without it, the shopper does not care whether the merchant pays more to American Express than it would pay to a different card company—the shopper pays the same price either way. But if steering works, then American Express will find it more difficult to charge more than its competitors for merchant-related services, because merchants will respond by steering their customers, encouraging them to use other cards. Thus, American Express dislikes steering; the merchants like it; and the shoppers may benefit from it, whether because merchants will offer them incentives to use less expensive cards or in the form of lower retail prices overall.

In response to its competitors’ efforts to convince merchants to steer shoppers to use less expensive cards, American Express tried to stop, or at least to limit, steering by placing anti-steering provisions in most of its contracts with merchants. It called those provisions “nondiscrimination provisions.” They prohibited steering of the forms I have described above (and others as well). After placing them in its agreements, American Express found it could maintain, or even raise,
In 2010 the United States and 17 States brought this antitrust case against American Express. They claimed that the “nondiscrimination provisions” in its contracts with merchants created an unreasonable restraint of trade. (Initially Visa and MasterCard were also defendants, but they entered into consent judgments, dropping similar provisions from their contracts with merchants). After a 7-week bench trial, the District Court entered judgment for the Government, setting forth its findings of fact and conclusions of law in a 97-page opinion.

Because the majority devotes little attention to the District Court’s detailed factual findings, I will summarize some of the more significant ones here. Among other things, the District Court found that beginning in 2005 and during the next five years, American Express raised the prices it charged merchants on 20 separate occasions. In doing so, American Express did not take account of the possibility that large merchants would respond to the price increases by encouraging shoppers to use a different credit card because the nondiscrimination provisions prohibited any such steering. The District Court pointed to merchants’ testimony stating that, had it not been for those provisions, the large merchants would have responded to the price increases by encouraging customers to use other, less-expensive cards.

The District Court also found that even though American Express raised its merchant prices 20 times in this 5-year period, it did not lose the business of any large merchant. Nor did American Express increase benefits (or cut credit-card prices) to American Express cardholders in tandem with the merchant price increases. Even had there been no direct evidence of injury to competition, American Express’ ability to raise merchant prices without losing any meaningful market share, in the District Court’s view, showed that American Express possessed power in the relevant market.

The District Court also found that, in the absence of the provisions, prices to merchants would likely have been lower. It wrote that in the late 1990’s, Discover, one of American Express’ competitors, had tried to develop a business model that involved charging lower prices to merchants than the other companies charged. Discover then invited each “merchant to save money by shifting volume to Discover,” while simultaneously offering merchants additional discounts “if they
would steer customers to Discover.” The court determined that these efforts failed because of American Express’ (and the other card companies’) “nondiscrimination provisions.” These provisions, the court found, “denied merchants the ability to express a preference for Discover or to employ any other tool by which they might steer share to Discover’s lower-priced network.” Because the provisions eliminated any advantage that lower prices might produce, Discover “abandoned its low-price business model” and raised its merchant fees to match those of its competitors. This series of events, the court concluded was “emblematic of the harm done to the competitive process” by the “nondiscrimination provisions.”

The District Court added that it found no offsetting procompetitive benefit to shoppers. Indeed, it found no offsetting benefit of any kind. American Express appealed, and the U. S. Court of Appeals for the Second Circuit held in its favor. The Court of Appeals did not reject any fact found by the District Court as “clearly erroneous.” Rather, it concluded that the District Court had erred in step 1 of its rule-of-reason analysis by failing to account for what the Second Circuit called the credit-card business’s “two-sided market” (or “two-sided platform”).

III

The majority, like the Court of Appeals, reaches only step 1 in its “rule of reason” analysis. To repeat, that step consists of determining whether the challenged “nondiscrimination provisions” have had, or are likely to have, anticompetitive effects. Do those provisions tend to impede competition? And if so, does American Express, which imposed that restraint as a condition of doing business with its merchant customers, have sufficient economic or commercial power for the provision to make a negative difference?

A

Here the District Court found that the challenged provisions have had significant anticompetitive effects. In particular, it found that the provisions have limited or prevented price competition among credit-card firms for the business of merchants. That conclusion makes sense: In the provisions, American Express required the merchants to agree not to encourage customers to use American Express’ competitors’ credit cards, even cards from those competitors, such as Discover, dissenting that intended to charge the merchants lower prices. By doing so, American Express has “disrupt[ed] the normal price-setting mechanism” in the market. As a result of the provisions, the District Court found, American Express was able to raise merchant prices repeatedly without any significant loss of business, because
merchants were unable to respond to such price increases by encouraging shoppers to pay with other cards. The provisions also meant that competitors like Discover had little incentive to lower their merchant prices, because doing so did not lead to any additional market share. . . . Consumers throughout the economy paid higher retail prices as a result, and they were denied the opportunity to accept incentives that merchants might otherwise have offered to use less-expensive cards. I should think that, considering step 1 alone, there is little more that need be said.

The majority, like the Court of Appeals, says that the District Court should have looked not only at the market for the card companies’ merchant-related services but also at the market for the card companies’ shopper-related services, and that it should have combined them, treating them as a single market. But I am not aware of any support for that view in antitrust law. Indeed, this Court has held to the contrary.

In *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 610 (1953), the Court held that an antitrust court should begin its definition of a relevant market by focusing narrowly on the good or service directly affected by a challenged restraint. The Government in that case claimed that a newspaper’s advertising policy violated the Sherman Act’s “rule of reason.” . . . [The Supreme Court] explained that “every newspaper is a dual trader in separate though interdependent markets; it sells the paper’s news and advertising content to its readers; in effect that readership is in turn sold to the buyers of advertising space.” We then added:

“This case concerns solely one of those markets. The Publishing Company stands accused not of tying sales to its readers but only to buyers of general and classified space in its papers. For this reason, dominance in the advertising market, not in readership, must be decisive in gauging the legality of the Company’s unit plan.”

Here, American Express stands accused not of limiting or harming competition for shopper-related card services, but only of merchant-related card services, because the challenged contract provisions appear only in American Express’ contracts with merchants. That is why the District Court was correct in considering, at step 1, simply whether the agreement had diminished competition in merchant-related services.

***

C
... [A] discussion of market definition was legally unnecessary at step 1. That is because the District Court found strong direct evidence of anticompetitive effects flowing from the challenged restraint. As I said, this evidence included Discover's efforts to break into the credit-card business by charging lower prices for merchant-related services, only to find that the “nondiscrimination provisions,” by preventing merchants from encouraging shoppers to use Discover cards, meant that lower merchant prices did not result in any additional transactions using Discover cards. The direct evidence also included the fact that American Express raised its merchant prices 20 times in five years without losing any appreciable market share. It also included the testimony of numerous merchants that they would have steered shoppers away from American Express cards in response to merchant price increases (thereby checking the ability of American Express to raise prices) had it not been for the nondiscrimination provisions. It included the factual finding that American Express “did not even account for the possibility that [large] merchants would respond to its price increases by attempting to shift share to a competitor’s network” because the nondiscrimination provisions prohibited steering. It included the District Court’s ultimate finding of fact, not overturned by the Court of Appeals, that the challenged provisions “were integral to” American Express’ “[price] increases and thereby caused merchants to pay higher prices.”

As I explained above, this Court has stated that “[s]ince the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, proof of actual detrimental effects . . . can obviate the need for” those inquiries. That statement is fully applicable here. Doubts about the District Court’s market-definition analysis are beside the point in the face of the District Court’s findings of actual anticompetitive harm.

The majority disagrees that market definition is irrelevant. The majority explains that market definition is necessary because the nondiscrimination provisions are “vertical restraints” and “[v]ertical restraints often pose no risk to competition unless the entity imposing them has market power, which cannot be evaluated unless the Court first determines the relevant market.” Ante, at n. 7. The majority thus, in a footnote, seems categorically to exempt vertical restraints from the ordinary “rule of reason” analysis that has applied to them since the Sherman Act’s enactment in 1890. The majority’s only support for this novel exemption is Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551 U.S. 877 (2007). But Leegin held that the “rule of reason” applied to the vertical restraint at issue in that case. See id., at 898–
899. It said nothing to suggest that vertical restraints are not subject to the usual “rule of reason” analysis.

One critical point that the majority’s argument ignores is that proof of actual adverse effects on competition is, a fortiori, proof of market power. Without such power, the restraints could not have brought about the anticompetitive effects that the plaintiff proved. See Indiana Federation of Dentists, supra, at 460 (“[T]he purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition” (emphasis added)). The District Court’s findings of actual anticompetitive harm from the nondiscrimination provisions thus showed that, whatever the relevant market might be, American Express had enough power in that market to cause that harm. There is no reason to require a separate showing of market definition and market power under such circumstances. And so the majority’s extensive discussion of market definition is legally unnecessary.

D

The majority’s discussion of market definition is also wrong. . . . [T]he majority agrees with the Court of Appeals that the market for American Express’ card services is special because it is a “two-sided transaction platform.” The majority explains that credit-card firms connect two distinct groups of customers: First, merchants who accept credit cards, and second, shoppers who use the cards. The majority adds that “no credit-card transaction can occur unless both the merchant and the cardholder simultaneously agree to use to the same credit-card network.” And it explains that the credit-card market involves “indirect network effects,” by which it means that shoppers want a card that many merchants will accept and merchants want to accept those cards that many customers have and use. Ibid. From this, the majority concludes that “courts must include both sides of the platform—merchants and cardholders—when defining the credit-card market.”

1

Missing from the majority’s analysis is any explanation as to why, given the purposes that market definition serves in antitrust law, the fact that a credit-card firm can be said to operate a “two-sided transaction platform” means that its merchant-related and shopper-related services should be combined into a single market. . . . The majority defines the phrase as covering a business that “offers different products or services to two different groups who both depend on the platform to intermediate between them,” where the business “cannot make a sale to one side of the platform without simultaneously
making a sale to the other” side of the platform. I take from that
definition that there are four relevant features of such businesses on
the majority’s account: they (1) offer different products or services, (2)
to different groups of customers, (3) whom the “platform” connects, (4)
in simultaneous transactions.

What is it about businesses with those four features that the
majority thinks justifies a special market definition approach for
them? It cannot be the first two features—that the company sells
different products to different groups of customers. Companies that
sell multiple products to multiple types of customers are commonplace.

I have already explained that, ordinarily, antitrust law will not
group the two non-substitutable products together for step 1 purposes.

Neither should it normally matter whether a company sells
related, or complementary, products, i.e., products which must both be
purchased to have any function, such as ignition switches and tires, or
cameras and film. It is well established that an antitrust court in such
cases looks at the product where the attacked restraint has an
anticompetitive effect. The court does not combine the customers for
the separate, non-substitutable goods and see if “overall” the restraint
has a negative effect. . . .

The majority disputes my characterization of merchant related
and shopper related services as “complements.” See ante, n. 8 . . . I
agree that two-sided platforms—at least as some academics define
them—may be distinct from some types of complements in the respect
the majority mentions (even though the services resemble
complements because they must be used together for either to have
value). But the distinction the majority mentions has nothing to do
with the relevant question. The relevant question is whether
merchant-related and shopper-related services are substitutes, one for
the other, so that customers can respond to a price increase for one
service by switching to the other service. As I have explained, the two
types of services are not substitutes in this way. . . .

What about the last two features—that the company connects
the two groups of customers to each other, in simultaneous
transactions? That, too, is commonplace. Consider a farmers’ market.
It brings local farmers and local shoppers together, and transactions
will occur only if a farmer and a shopper simultaneously agree to
engage in one. Should courts abandon their ordinary step 1 inquiry if
several competing farmers’ markets in a city agree that only certain
kinds of farmers can participate, or if a farmers’ market charges a
higher fee than its competitors do and prohibits participating farmers
from raising their prices to cover it? Why? If farmers’ markets are
special, what about travel agents that connect airlines and passengers? What about internet retailers, who, in addition to selling their own goods, allow (for a fee) other goods producers to sell over their networks? Each of those businesses seems to meet the majority’s four-prong definition.

Apparently as its justification for applying a special market-definition rule to “two-sided transaction platforms,” the majority explains that such platforms “often exhibit” what it calls “indirect network effects.” By this, the majority means that sales of merchant-related card services and (different) shopper-related card services are interconnected, in that increased merchant-buyers mean increased shopper-buyers (the more stores in the card’s network, the more customers likely to use the card), and vice versa. But this, too, is commonplace. Consider, again, a farmers’ market. The more farmers that participate (within physical and esthetic limits), the more customers the market will likely attract, and vice versa. So too with travel agents: the more airlines whose tickets a travel agent sells, the more potential passengers will likely use that travel agent, and the more potential passengers that use the travel agent, the easier it will likely be to convince airlines to sell through the travel agent. And so forth. Nothing in antitrust law, to my knowledge, suggests that a court, when presented with an agreement that restricts competition in any one of the markets my examples suggest, should abandon traditional market-definition approaches and include in the relevant market services that are complements, not substitutes, of the restrained good.

* * *

E

Put all of those substantial problems with the majority’s reasoning aside, though. Even if the majority were right to say that market definition was relevant, and even if the majority were right to further say that the District Court should have defined the market in this case to include shopper-related services as well as merchant-related services, that still would not justify the majority in affirming the Court of Appeals. That is because, as the majority is forced to admit, the plaintiffs made the factual showing that the majority thinks is required.

Recall why it is that the majority says that market definition matters: because if the relevant market includes both merchant-related services and card-related services, then the plaintiffs had the burden to show that as a result of the nondiscrimination provisions, “the price of credit card transactions”—considering both fees charged
to merchants and rewards paid to cardholders—“was higher than the price one would expect to find in a competitive market.” . . .

The problem with this reasoning, aside from it being wrong, is that the majority admits that the plaintiffs did show this: they “offered evidence” that American Express “increased the percentage of the purchase price that it charges merchants . . . and that this increase was not entirely spent on cardholder rewards.” . . .

In the face of this problem, the majority retreats to saying that even net price increases do not matter after all, absent a showing of lower output, because if output is increasing, “rising prices are equally consistent with growing product demand.” This argument, unlike the price argument, has nothing to do with the credit-card market being a “two-sided transaction platform,” so if this is the basis for the majority’s holding, then nearly all of the opinion is dicta. The argument is also wrong. It is true as an economic matter that a firm exercises market power by restricting output in order to raise prices. But the relevant restriction of output is as compared with a hypothetical world in which the restraint was not present and prices were lower. The fact that credit-card use in general has grown over the last decade, as the majority says, says nothing about whether such use would have grown more or less without the nondiscrimination provisions. And because the relevant question is a comparison between reality and a hypothetical state of affairs, to require actual proof of reduced output is often to require the impossible—tantamount to saying that the Sherman Act does not apply at all. In any event, there are features of the credit-card market that may tend to limit the usual relationship between price and output. In particular, merchants generally spread the costs of credit-card acceptance across all their customers (whatever payment method they may use), while the benefits of card use go only to the cardholders. Thus, higher credit-card merchant fees may have only a limited effect on credit card transaction volume, even as they disrupt the marketplace by extracting anticompetitive profits.

IV

A

For the reasons I have stated, the Second Circuit was wrong to lump together the two different services sold, at step 1. But I recognize that the Court of Appeals has not yet considered whether the relationship between the two services might make a difference at steps 2 and 3. That is to say, American Express might wish to argue that the nondiscrimination provisions, while anticompetitive in respect to merchant-related services, nonetheless have an adequate offsetting
procompetitive benefit in respect to its shopper-related services. I believe that American Express should have an opportunity to ask the Court of Appeals to consider that matter. American Express might face an uphill battle. A Sherman Act §1 defendant can rarely, if ever, show that a procompetitive benefit in the market for one product offsets an anticompetitive harm in the market for another.

***

B

The majority charts a different path. Notwithstanding its purported acceptance of the three-step, burden-shifting framework I have described, the majority addresses American Express’ procompetitive justifications now, at step 1 of the analysis. And in doing so, the majority inexplicably ignores the District Court’s factual findings on the subject.

The majority reasons that the challenged nondiscrimination provisions “stem negative externalities in the credit card market and promote interbrand competition.” The “negative externality” the majority has in mind is this: If one merchant persuades a shopper not to use his American Express card at that merchant’s store, that shopper becomes less likely to use his American Express card at other merchants’ stores. The majority worries that this “endangers the viability of the entire [American Express] network,” but if so that is simply a consequence of American Express’ merchant fees being higher than a competitive market will support. . . . If American Express’ merchant fees are so high that merchants successfully induce their customers to use other cards, American Express can remedy that problem by lowering those fees or by spending more on cardholder rewards so that cardholders decline such requests. What it may not do is demand contractual protection from price competition.

In any event, the majority ignores the fact that the District Court, in addition to saying what I have just said, also rejected this argument on independent factual grounds. It explained that American Express “presented no expert testimony, financial analysis, or other direct evidence establishing that without its [nondiscrimination provisions] it will, in fact, be unable to adapt its business to a more competitive market.” It further explained that the testimony that was provided on the topic “was notably inconsistent,” with some of American Express’ witnesses saying only that invalidation of the provisions “would require American Express to adapt its current business model.” After an extensive discussion of the record, the District Court found that “American Express possesses the flexibility and expertise necessary to adapt its business model to suit a market
in which it is required to compete on both the cardholder and merchant sides of the [credit-card] platform.” The majority evidently rejects these factual findings, even though no one has challenged them as clearly erroneous.

Similarly, the majority refers to the nondiscrimination provisions as preventing “free riding” on American Express’ “investments in rewards” for cardholders. But as the District Court explained, “[p]lainly . . . investments tied to card use (such as Membership Rewards points, purchase protection, and the like) are not subject to free-riding, since the network does not incur any cost if the cardholder is successfully steered away from using his or her American Express card.” This, I should think, is an unassailable conclusion: American Express pays rewards to cardholders only for transactions in which cardholders use their American Express cards, so if a steering effort succeeds, no rewards are paid. As for concerns about free riding on American Express’ fixed expenses, including its investments in its brand, the District Court acknowledged that free-riding was in theory possible, but explained that American Express “ma[de] no effort to identify the fixed expenses to which its experts referred or to explain how they are subject to free riding.” . . . Finally, the majority reasons that the nondiscrimination provisions “do not prevent Visa, MasterCard, or Discover from competing against [American Express] by offering lower merchant fees or promoting their broader merchant acceptance.” But again, the District Court’s factual findings were to the contrary. As I laid out above, the District Court found that the nondiscrimination provisions in fact did prevent Discover from pursuing a low merchant-fee business model, by “den[y]ing merchants the ability to express a preference for Discover or to employ any other tool by which they might steer share to Discover’s lower-priced network.” The majority’s statements that the nondiscrimination provisions are procompetitive are directly contradicted by this and other factual findings.

For the reasons I have explained, the majority’s decision in this case is contrary to basic principles of antitrust law, and it ignores and contradicts the District Court’s detailed factual findings, which were based on an extensive trial record. I respectfully dissent.

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89
ADDENDUM (from the Court of Appeals Decision)

Figure 1

The basic functions of as many as five distinct actors comprising the Visa and MasterCard cooperative, open-loop systems.

<table>
<thead>
<tr>
<th>Actor</th>
<th>Cardholder Side</th>
<th>NETWORK</th>
<th>Merchant Side</th>
</tr>
</thead>
<tbody>
<tr>
<td>Function</td>
<td>Purchases goods and services from merchants.</td>
<td>Cardholder’s bank. Provides cards to cardholders, collects payment, and commonly provides cardholder rewards such as cash back or airline miles.</td>
<td>Middleman. Brings together merchants &amp; acquirers with cardholders &amp; issuers.</td>
</tr>
<tr>
<td>Examples</td>
<td>Citibank; JPMorgan Chase; Bank of America; Capital One</td>
<td>Visa; MasterCard</td>
<td>First Data Corporation; Chase Paymentech</td>
</tr>
</tbody>
</table>
Figure 2

The basic relationships and interactions between actors in the Visa and MasterCard cooperative, open-loop networks.
Figure 3

The basic functions of the three actors in the American Express proprietary, closed-loop system.

<table>
<thead>
<tr>
<th>Actor</th>
<th>Cardholder Side</th>
<th>AMERICAN EXPRESS</th>
<th>Merchant Side</th>
</tr>
</thead>
<tbody>
<tr>
<td>Function</td>
<td>Purchases goods and services from merchants.</td>
<td>Provides cards to cardholders, collects payment, and commonly provides cardholder rewards such as cash back or airline miles.</td>
<td>Middleman Brings together merchants &amp; acquirers with cardholders &amp; issuers.</td>
</tr>
<tr>
<td>Example</td>
<td>American Express</td>
<td>American Express</td>
<td>American Express</td>
</tr>
</tbody>
</table>

Figure 4

The basic relationships and interactions between the actors in the proprietary, closed-loop American Express system.

cost c
NOTES AND QUESTIONS

1. Considering two-sidedness. Try to frame the two-sided argument here. American Express assembles a pool of potential customers for merchants. That is effectively what Amex is doing in issuing cards to consumers. There is no reason that the demographics of Amex card holders should be identical to those of Visa and MasterCard. And one of the competitive tools that Amex might bring to bear in the competition between card platforms is the high quality of their consumer pool, i.e., a group of cardholders that tend to spend more at merchants. Amex then goes to a merchant to try to get it to take the Amex card. Amex notes that it charges a higher interchange fee than Visa or MasterCard, but Amex says that it needs to do that to fund the attractive benefits that it offers to build its pool of card holders. All of that seems perfectly plausible and a legitimate way to organize competition between the card platforms.

Once the customer has arrived in the store or on its website, the merchant will prefer that she use a card for which the merchant will be charged a lower fee. Amex, however, will almost certainly care what happens once an Amex cardholder walks into a merchant. Amex will contend that the fact that the merchant accepts the American Express card will be an important reason for an Amex cardholder to shop at the merchant in the first place. Amex wants to make sure that merchant who gets the benefit of advertising that they accept the Amex card—Amex customers walk into the store—also pays its fair share of the costs of building that customer pool in the first place. Amex wants to police free riding, where a merchant advertises acceptance of the Amex card, gets the benefit of having that customer in the store, but then avoids paying the costs of that by suggesting that the consumer pay with a card with a lower interchange fee (Visa or MasterCard).

Does that analysis seem right? Does that link together the behavior across both sides of the market and in doing so account for the ways that merchants might seek to avoid the costs of serving the other side of the market?

2. Relevant market. The Court held that, in a vertical case, it is necessary to define a relevant market in order to assess the competitive effects of the conduct at issue (see fn. 7). Is that correct? Suppose, for example, that some states at various times had rules prohibiting Amex from applying no-steering rules to in-state merchants and the evidence showed that, when those laws were in effect, there were more credit card transactions at lower cost to consumers and merchants in those states (1) than at other times and
(2) relative to transactions and costs in other states. Would it make sense to require proof of a market if those were the facts?

3. **Market definition.** The Court held that both cardholders and merchants should be included in a single relevant market on the ground that Amex and other credit card platforms are what the Court called “two-sided transaction platforms” that “facilitate a single, simultaneous transaction” involving both cardholders and merchants. Cases and the Merger Guidelines state that markets are defined with respect to buyers. Cardholders are not buyers of the network services purchased by merchants, so how can they be included in a market for the sale of such services?

The dissent noted that market definition entails identifying a group of products or services that buyers regard as substitutes and that therefore compete with and constrain one another. Are the substitutes for Amex from the perspective of cardholders the same as the substitutes from the perspective of merchants? Many merchants that take Visa and MasterCard do not take Amex, presumably because of the high fees charged by Amex. Would including both sides of the platform in a single market when the substitutes on one side might be different from those on the other side render the concept of a relevant market incoherent? Even if the market were defined with respect to only one side, the other side could affect the market definition. For example, assume that, if a monopolist of the hypothetical credit card market for merchants increased the merchant fee to above competitive levels, some merchants would drop the card, but not enough to themselves cause the price increase to be unprofitable. Assume further that the reduction in the number of merchants accepting the card would cause a reduction in the number of card holders and that the combination of the loss of some merchants and the reduction in the number of card holders would cause the increase in the merchant fee to be unprofitable. In that case, should it be concluded that the hypothetical market is not a market even on the merchant side? And if the price increase would be profitable after taking into account the loss of both merchants and cardholders, should it be concluded that it is a market? If feedback effects and indirect network effects can be taken into account in defining a market on one side of the platform, what is gained by trying to define a market that includes both sides?

4. **Identifying the competitors.** One way to make defining a two-sided market workable would be to ask what combination of alternatives on the two sides would, if monopolized, enable supracompetitive pricing. That way, an alternative on one side could
be included in the market even though customers on the other side would not consider it to be an alternative for their purposes. But there might be several different markets that would meet that test. For example, in the ride sharing business, one market might consist of Uber and Lyft on the rider side and Grub Hub on the driver side, while another market might consist of Uber, Lyft, and taxicabs.

The Court appears not to have had that kind of market definition in mind. It stated that “only other two-sided platforms can compete with a two-sided platform for transactions.” In United States v. Sabre Corp., 452 F.Supp.3d 97 (D. Del. 2020), a case brought by the Justice Department to block Sabre’s acquisition of Farelogix, the district court found that the two firms viewed each other as major competitors, the record reflected that competition, and their airline customers regarded them as differentiated alternatives. Nevertheless, relying on the quoted language from the American Express opinion, the court rejected the challenge to the merger on the ground that, as a matter of law, the two merging parties could not be included in the same market. The court reasoned that, while Sabre was a two-sided platform, Farelogix was not and the two firms therefore could not be included in the same market. Did the Sabre court read American Express correctly? Should it have treated the quoted language as factually inaccurate dicta or as a binding legal rule? Should it have construed that language as simply describing transactions and not as intended to describe the boundaries of the relevant market?

5. Market power. If, as the dissent says, market definition is simply an aid in assessing market power, might it have been better for the Court to ignore the market definition issue and ask directly the question whether Amex had market power? How might a court determine whether Amex had market power without defining a market?

6. Quality-adjusted prices. Does an increase in the nominal merchant fee mean that quality-adjusted prices (i.e., prices adjusted to reflect changes in the quality of the product or service) increased? Suppose the fee increase enabled Amex to increase cardholder benefits and the increased benefits increased both the number of Amex cardholders and their willingness to use the Amex card in order to obtain the benefits. If by this mechanism the increase in the merchant fee generated sales increases for the merchants sufficient for the merchants on balance to profit from the fee increase, can it be concluded that the fee increase constituted a price increase for antitrust purposes? In determining how much the merchants
benefitted from increased sales to Amex cardholders, should the court subtract sales that reflected cardholder shifting to Amex from other cards on the ground the merchants would have made those sales anyhow and they cannot be attributed to the Amex fee increase?

7. Injury to competition. The ultimate issue in the case was whether the no-steering rules unlawfully impeded Amex’s rivals. The majority said that “plaintiffs did not offer any evidence that the price of credit-card transactions was higher than the price one would expect to find in a competitive market.” Is that the correct test if the no-steering provision prevented merchants from passing on to consumers the lower fees charged by other card platforms and thus resulted in prices that were higher than they would have been without the no-steering rules?

It seems clear that the rules did harm the rivals because the rules materially reduced their ability to compete on price on the merchant side. Is that enough to find injury to competition? In thinking about this question, consider exclusive dealing agreements. Suppose firm A enters into exclusive dealing agreements with several distributors. That might harm A’s rivals because they would lose access to the distributors, but the agreements might still be legal if there are offsetting efficiencies.

Suppose A is able to show that the exclusive distributors are still better off – perhaps by being paid in money or services for their exclusivity -- even though they are unable to deal with A’s competitors. Would that be sufficient to justify the exclusivity agreements? Or is the question whether output increased in the market as a whole? Similarly, in the Amex case, would the no-steering rules be lawful if they increased Amex’s output but reduced credit card transactions overall?

The dissent suggested that there might often be no way to know whether the no-steering rules increased total output because that requires us to know what would have happened in a hypothetical world without the no-steering rules. If that is correct, how can a court decide whether the benefits of avoiding merchant free riding on the promotional efforts of Amex outweigh the harms to Amex’s rivals?

8. Two-sided price level. The Court held that harm to competition cannot be inferred from the merchant fees themselves and can be inferred from prices only if the plaintiffs proved that the defendant’s conduct elevated the platform’s two-sided price (i.e., the sum of the prices it charges to the two sides for a transaction). In the Court’s view, Amex sold a single product, transactions, and the relevant price is the two-sided price of the transactions.
The Court focused entirely on price *level* and overlooked the importance in two-sided markets of the price *structure* – the relative prices on the two sides. For example, suppose Amex increases the merchant fee and increases cardholder rewards (i.e., reduces price on the cardholder side) slightly more; in that case, the two-sided price would be slightly reduced. The cardholders might benefit from the increased rewards, and the transaction volume on American Express cards could rise as consumers choose to use those cards more frequently. But the change could nevertheless reduce economic welfare.

Merchants might benefit from additional consumer purchases stimulated by the increase in consumer rewards, but such gains would be offset (and maybe exceeded) by the increased merchant fees for all purchases on American Express cards. Moreover, some of the additional American Express transactions induced by the increased rewards might simply replace purchases that the consumer would otherwise have made using alternative payment methods equally or less costly to merchants. The change in the price structure could thus increase the merchants’ fees while generating little increase in merchant sales and might, on balance, harm merchants. In addition, if the increased rewards are worth less to consumers than the increased fees cost the merchants, both would be better off if the merchants are able to induce the cardholder to choose a different payment method by passing on to consumers part of the cost saving to the merchant resulting from the use of the alternative method. Also, if some merchants stop accepting American Express cards because of the increased fees, cardholders could be worse off from the reduced ability to use their cards even though they get increased rewards when they do use the cards. These and other problems with a two-side price test are discussed in Michael L. Katz, *Platform Economics and Antitrust Enforcement: A Little Knowledge Is a Dangerous Thing*, 28 J. ECON. & MGMT. STRATEGY 138 (2019).

9. **Efficiency and other justifications.** The majority said that the no-steering rules served the legitimate purpose of preventing free-riding on Amex’s investments in cardholder services. The idea is evidently that Amex cardholders are drawn to merchants that accept Amex cards and then, if there were no rules, the merchants might steer the cardholders to use lower-cost cards. Is that a legitimate justification or, as the dissent suggests, is it better understood as a means of insulating Amex from price competition?

Is the free-riding argument a legitimate justification if it protects Amex from a loss of goodwill; or does the justification depend on
showing that it is necessary to prevent harm to the market as a whole, taking into account the output of both Amex and competing cards?

If it is a legitimate justification, might there be less restrictive alternatives such as (i) applying the no-steering rules to only those merchants that advertise that they accept Amex cards or (ii) permitting merchants to pass lower costs of other cards on to consumers by price reductions and limiting no-steering rules to other forms of steering that might more explicitly harm the Amex brand?

With respect to the latter, is Amex telling merchants they cannot pass lower costs on to consumers any different from Gucci telling department stores that sell its handbags that they cannot charge consumers lower prices for handbags for which the stores are charged a lower wholesale price? What if Gucci can show that many consumers come to the stores because they carry Gucci handbags? If merchants were permitted to pass cost differences on to consumers, would they have any other reason to steer Amex cardholders to other cards?

10. Creating a new externality. The no-steering rules prevented retailers from charging holders of Visa, Mastercard and Discover lower prices to reflect the lower merchant fees on those cards. The rules thus restricted price competition and created something of a price umbrella for Amex so that it could charge high merchant fees. From this perspective, the rules could be seen as shifting some of Amex’s costs to holders of other cards. Moreover, if the merchant cannot require Amex cardholders to pay the higher merchant fees, it will pass its increased costs on to all customers in the form of higher merchandise prices. How should that externality affect the antitrust analysis?

11. Benefits and harms on different sides of the platform. The dissent suggested that harm on the merchant side cannot be justified by benefits on the cardholder side. It referred to case law to the effect that harm in one market cannot be justified by benefits in a different market. Should that principle apply here, or are platforms different because the harms on one side are inextricably linked to the benefits on the other side?

If effects on both sides of the market need to be considered, how should they be compared? What is the metric for weighing harm on one side against benefit on the other? If the plaintiff is able to show harm on the merchant side, should it have the burden of showing that there are no offsetting benefits on the cardholder side? Or should the defendant have the burden of proof on that issue on the ground that it is an affirmative defense, that the defendant has better access to information about the other side of the platform, or that a party should not be required to prove a negative?
12. Post-Amex case developments. Amex is an important case. Part of that has to do with the shape of the modern economy where internet and device platforms shape much of our day-to-day lives. But another part of that is the apparent breadth of the two-sided markets idea discussed in Amex and the understandable desire of potential antitrust defendants to want to use Amex to shield themselves from potential antitrust liability. You can run searches on Westlaw and Lexis just like we can and we urge you to do that, but we will highlight a couple of key cases. U.S. Airways, Inc. v. Sabre Holdings Corp., 938 F.3d 43 (2nd Cir. 2019), is an intriguing case set in the world of reservation systems for airlines, but the case is also procedurally a little awkward. The original litigation in the case occurred before the Supreme Court’s opinion in Amex, but the case came to the Second Circuit after the Supreme Court had reset the law in this area. That makes the case a difficult one for useful generalizations.

And staying in the airline reservation business, we turn to a proposed merger between Sabre and Farelogix. The U.S. government brought a challenge to the proposed merger, but that challenge was rejected in April 2020 in a lengthy opinion by Judge Leonard P. Stark of the U.S. District Court for the District of Delaware. The result in Farelogix, which is discussed briefly in Note 4 above, was seen by many as an unfortunate extension of the analysis in Amex. But after the Competition and Markets Authority of the United Kingdom blocked the merger, the parties abandoned it, and on July 20, 2020, the Third Circuit vacated the district’s court opinion. It did note that its order “should not be construed as detracting from the persuasive force of the District Court’s decision, should courts and litigants find its reasoning persuasive.”

13. But what does the Supreme Court think about the case? One final point. Sometimes you can assess the importance of a case by how often it is cited in another opinion, but in other cases, the fact that a case isn’t cited is really what is noteworthy. In Chapter 10, you will read the 2019 Supreme Court decision in Apple v. Pepper. The issue there is standing in connection with possible antitrust actions over how Apple operates the App Store for iOS devices like the iPhone and the iPad. That type of platform is a standard example of a two-sided transaction market and hence you might have expected the Supreme Court to develop its Amex jurisprudence in this important area. Yet the Supreme Court decided Apple v. Pepper without a single citation to Amex by either the majority or the dissent. Remember this note when you read Pepper.

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The ride-hailing companies Uber and Lyft have generated an enormous amount of attention; and their entry into local transportation markets has raised some tricky legal questions, especially in labor law and antitrust. We are still at early days in litigation over those issues; but as you read the next three case, you should have a few questions firmly in mind. First, what would the antitrust issues look like if Uber was just a corporation that hired drivers as Uber’s employees? That arrangement would almost certainly trigger the application of any number of local, state or federal labor and employment laws, but that isn’t our issue here. Our focus is on the antitrust issues that arrangement might give rise to. Second, try a different configuration of “Uber.” Uber enters a local transportation market and requires all of its independent drivers in that market to agree to charge prices for their services specified by Uber. Uber isn’t a driver, but it is the company organizing the drivers. And in this version, the drivers are not employees of Uber but instead are treated under applicable labor and employment law as independent contractors. What antitrust issues might that arrangement pose? Try a third configuration. Uber calls itself a platform—whatever that is exactly—and says that it matches drivers with passengers. Again, the drivers remain as independent contractors. Consider a couple flavors of the third hypo. Suppose Uber just matches drivers and passengers who then separately negotiate a price for a ride. Uber gets paid for the matching service. Alternatively, suppose Uber provides a platform service that both matches drivers and passengers and informs them of the price for their transaction, which Uber determines by using the vast amount of data available to it to match supply and demand in the local market.

As you read the next three cases, consider your answers to the above questions. What is Uber exactly, and how does that matter for antitrust?

**Meyer v. Kalanick**


174 F.Supp.3d 817.

JED S. RAKOFF, UNITED STATES DISTRICT JUDGE: On December 16, 2015, plaintiff Spencer Meyer, on behalf of himself and those similarly situated, filed this putative antitrust class action lawsuit against defendant Travis Kalanick, CEO and co-founder of Uber Technologies, Inc. (“Uber”). Mr. Meyer’s First Amended
Complaint, filed on January 29, 2016, alleged that Mr. Kalanick had orchestrated and facilitated an illegal price-fixing conspiracy in violation of Section 1 of the federal Sherman Antitrust Act, 15 U.S.C. § 1, and the New York State Donnelly Act, New York General Business Law § 340. Plaintiff claimed, in essence, that Mr. Kalanick, while disclaiming that he was running a transportation company, had conspired with Uber drivers to use Uber's pricing algorithm to set the prices charged to Uber riders, thereby restricting price competition among drivers to the detriment of Uber riders, such as plaintiff Meyer.

On February 8, 2016, defendant Kalanick moved to dismiss the Amended Complaint. Plaintiff opposed on February 18, 2016; defendant replied on February 25, 2016; and oral argument was held on March 9, 2016. Having considered all of the parties’ submissions and arguments, the Court hereby denies defendant’s motion to dismiss.

In ruling on a motion to dismiss, the Court accepts as true the factual allegations in the complaint and draws all reasonable inferences in favor of the plaintiff. *** In the antitrust context, stating a claim under Section 1 of the Sherman Act “requires a complaint with enough factual matter (taken as true) to suggest that an agreement was made. Asking for plausible grounds to infer an agreement does not impose a probability requirement at the pleading stage; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement.” Bell Atl. Corp. v. Twombly, 550 U.S. 544, 556 (2007).

The relevant allegations of the Amended Complaint are as follows. Uber, founded in 2009, is a technology company that produces an application for smartphone devices (“the Uber App”) that matches riders with drivers (called “driver-partners”). Uber states that it is not a transportation company and does not employ drivers. Defendant Kalanick, in addition to being the co-founder and CEO of Uber, is a driver who has used the Uber app. Plaintiff Meyer is a resident of Connecticut, who has used Uber car services in New York.

Through the Uber App, users can request private drivers to pick them up and drive them to their desired location. Uber facilitates payment of the fare by charging the user’s credit card or other payment information on file. Uber collects a percentage of the fare as a software licensing fee and remits the remainder to the driver. Drivers using the Uber app do not compete on price, and cannot negotiate fares with drivers for rides. Instead, drivers charge the fares set by the Uber algorithm. Though Uber claims to allow drivers to depart downward from the fare set by the algorithm, there is no practical mechanism by
which drivers can do so. Uber’s “surge pricing” model, designed by Mr. Kalanick, permits fares to rise up to ten times the standard fare during times of high demand. Plaintiff alleges that the drivers have a “common motive to conspire” because adhering to Uber’s pricing algorithm can yield supra-competitive prices, and that if the drivers were acting independently instead of in concert, “some significant portion” would not agree to follow the Uber pricing algorithm.

Plaintiff further claims that the drivers “have had many opportunities to meet and enforce their commitment to the unlawful agreement.” Plaintiff alleges that Uber holds meetings with potential drivers when Mr. Kalanick and his subordinates decide to offer Uber App services in a new geographic location. Uber also organizes events for its drivers to get together, such as a picnic in September 2015 in Oregon with over 150 drivers and their families in attendance, and other “partner appreciation” events in places including New York City. Uber provides drivers with information regarding upcoming events likely to create high demand for transportation and informs the drivers what their increased earnings might have been if they had logged on to the Uber App during busy periods. Moreover, plaintiff alleges, in September 2014 drivers using the Uber App in New York City colluded with one another to negotiate the reinstitution of higher fares for riders using Uber-BLACK and UberSUV services (certain Uber car service “experiences”). Mr. Kalanick, as Uber’s CEO, directed or ratified negotiations between Uber and these drivers, and Uber ultimately agreed to raise fares.

As to market definition, plaintiff alleges that Uber competes in the “relatively new mobile app-generated ride-share service market,” of which Uber has an approximately 80% market share. Uber’s chief competitor in this market, Lyft, has only a 20% market share, and a third competitor, Sidecar, left the market at the end of 2015. Although, plaintiff contends, neither taxis nor traditional cars for hire are reasonable substitutes for mobile app-generated ride-share service, Uber’s own experts have suggested that in certain cities in the U.S., Uber captures 50% to 70% of business customers in the combined market of taxis, cars for hire, and mobile-app generated ride-share services.

Plaintiff claims to sue on behalf of the following class: “all persons in the United States who, on one or more occasions, have used the Uber App to obtain rides from uber driver-partners and paid fares for their rides set by the Uber pricing algorithm,” with certain exclusions, such as Mr. Kalanick. Plaintiff also identifies a “subclass” of riders who have paid fares based on surge pricing. Plaintiff alleges
that he and the putative class have suffered antitrust injury because, were it not for Mr. Kalanick’s conspiracy to fix the fares charged by Uber drivers, drivers would have competed on price and Uber’s fares would have been “substantially lower.” Plaintiff also contends that Mr. Kalanick’s design has reduced output and that, as “independent studies have shown,” the effect of surge pricing is to lower demand so that prices remain artificially high. Based on these allegations, plaintiff claims that Mr. Kalanick has violated the Sherman Act, 15 U.S.C. § 1, and the Donnelly Act, New York General Business Law § 340.

In the instant case, the Court finds that plaintiff has adequately pled both a horizontal and a vertical conspiracy. As to the horizontal conspiracy, plaintiff alleges that Uber drivers agree to participate in a conspiracy among themselves when they assent to the terms of Uber’s written agreement (the “Driver Terms”) and accept riders using the Uber App. In doing so, plaintiff indicates, drivers agree to collect fares through the Uber App, which sets fares for all Uber drivers according to the Uber pricing algorithm. In plaintiff’s view, Uber drivers forgo competition in which they would otherwise have engaged because they “are guaranteed that other Uber drivers will not undercut them on price.” Without the assurance that all drivers will charge the price set by Uber, plaintiff contends, adopting Uber’s pricing algorithm would often not be in an individual driver’s best interest, since not competing with other Uber drivers on price may result in lost business opportunities. The capacity to generate “supra-competitive prices” through agreement to the Uber pricing algorithm thus provides, according to plaintiff, a “common motive to conspire” on the part of Uber drivers. Plaintiff also draws on its allegations about meetings among Uber drivers and the “September 2014 conspiracy,” in which Uber agreed to reinstitute higher fares after negotiations with drivers, to bolster its claim of a horizontal conspiracy. In plaintiff’s view, defendant Kalanick is liable as the organizer of the price-fixing conspiracy, and as an Uber driver himself.

Defendant Kalanick argues, however, that the drivers’ agreement to Uber’s Driver Terms evinces no horizontal agreement among drivers themselves, as distinct from vertical agreements between each driver and Uber. According to Mr. Kalanick, drivers’ individual decisions to enter into contractual arrangements with Uber constitute mere independent action that is insufficient to support plaintiff’s claim of a conspiracy. Defendant asserts that the most “natural” explanation for drivers’ conduct is that each driver “independently decided it was in his or her best interest to enter a vertical agreement with Uber,” and doing so could be in a driver’s best
interest because, for example, Uber matches riders with drivers and processes payment. In defendant’s view, the fact that “a condition of [the agreement with Uber] was that the driver-partner agree to use Uber’s pricing algorithm” does not diminish the independence of drivers’ decisions. See id. at 13. It follows, defendant contends, that such vertical arrangements do not support a horizontal conspiracy claim.

The Court, however, is not persuaded to dismiss plaintiff’s horizontal conspiracy claim. In *Interstate Circuit v. United States*, 306 U.S. 208 (1939), the Supreme Court held that competing movie distributors had unlawfully restrained trade when they each agreed to a theater operator’s terms, including price restrictions, as indicated in a letter addressed to all the distributors. For an illegal conspiracy to exist, the Supreme Court stated:

> It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it.... Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act.

*Interstate Circuit*, 306 U.S. at 226-27. Much more recently, the Second Circuit stated:

> [C]ourts have long recognized the existence of “hub-and-spoke” conspiracies in which an entity at one level of the market structure, the “hub,” coordinates an agreement among competitors at a different level, the “spokes.” These arrangements consist of both vertical agreements between the hub and each spoke and a horizontal agreement among the spokes to adhere to the [hub’s] terms, often because the spokes would not have gone along with [the vertical agreements] except on the understanding that the other [spokes] were agreeing to the same thing.

*United States v. Apple, Inc.*, 791 F.3d 290, 314 (2d Cir.2015), (internal citation and quotation marks omitted);

In this case, plaintiff has alleged that drivers agree with Uber to charge certain fares with the clear understanding that all other Uber drivers are agreeing to charge the same fares. These agreements are organized and facilitated by defendant Kalanick, who as at least
an occasional Uber driver, is also a member of the horizontal conspiracy.

On a motion to dismiss, the Court is required to draw all reasonable inferences in plaintiff’s favor. Given this standard, the Court finds that plaintiffs have plausibly alleged a conspiracy in which drivers sign up for Uber precisely “on the understanding that the other [drivers] were agreeing to the same” pricing algorithm, and in which drivers’ agreements with Uber would “be against their own interests were they acting independently.” Apple, 791 F.3d at 314, 320. Further, drivers’ ability to benefit from reduced price competition with other drivers by agreeing to Uber’s Driver Terms plausibly constitutes “a common motive to conspire.” Apex Oil Co. v. DiMauro, 822 F.2d 246, 254 (2d Cir. 1987). The fact that drivers may also, in signing up for Uber, seek to benefit from other services that Uber provides, such as connecting riders to drivers and processing payment, is not to the contrary. Of course, whether plaintiff’s allegations are in fact accurate is a different matter, to be left to the fact-finding process.

The Court’s conclusion that plaintiff has alleged a plausible horizontal conspiracy is bolstered by plaintiff’s other allegations concerning agreement among drivers. Plaintiff, as noted supra, contends that Uber organizes events for drivers to get together, and, more importantly, that Mr. Kalanick agreed to raise fares following drivers’ efforts to negotiate higher rates in September 2014. While it is true that these allegations about agreements among drivers reaching even beyond acceptance of Uber’s Driver Terms are not extensive, nonetheless, they provide additional support for a horizontal conspiracy, and plaintiff need not present a direct, “smoking gun” evidence of a conspiracy, particularly at the pleading stage. Mayor & City Council of Baltimore, Md. v. Citigroup, Inc., 709 F.3d 129, 136 (2d Cir. 2013).

More basically, it is well to remember that a Sherman Act conspiracy is but one form of conspiracy, a concept that is as ancient as it is broad. It is fundamental to the law of conspiracy that the agreements that form the essence of the misconduct are not to be judged by technical niceties but by practical realities. Sophisticated conspirators often reach their agreements as much by the wink and the nod as by explicit agreement, and the implicit agreement may be far more potent, and sinister, just by virtue of being implicit. *** In the instant case, Uber’s digitally decentralized nature does not prevent the App from constituting a “marketplace” through which Mr. Kalanick organized a horizontal conspiracy among drivers.
Defendant argues, however, that plaintiff’s alleged conspiracy is “wildly implausible” and “physically impossible,” since it involves agreement “among hundreds of thousands of independent transportation providers all across the United States.” Yet as plaintiff’s counsel pointed out at oral argument, the capacity to orchestrate such an agreement is the “genius” of Mr. Kalanick and his company, which, through the magic of smartphone technology, can invite hundreds of thousands of drivers in far-flung locations to agree to Uber’s terms. The advancement of technological means for the orchestration of large-scale price-fixing conspiracies need not leave antitrust law behind. The fact that Uber goes to such lengths to portray itself—one might even say disguise itself—as the mere purveyor of an “app” cannot shield it from the consequences of its operating as much more.

Recent jurisprudence on vertical resale price maintenance agreements does not, as defendant would have it, undermine plaintiff’s claim of an illegal horizontal agreement. In Leegin, the Supreme Court held that resale price maintenance agreements—e.g., a retailer’s agreement with a manufacturer not to discount the manufacturer’s goods beneath a certain price—are to be judged by the rule of reason, unlike horizontal agreements to fix prices, which are per se illegal. See Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551 U.S. 877, 886 (2007). The Court cited various “procompetitive justifications for a manufacturer’s use of resale price maintenance,” and concluded that although this practice may also have anticompetitive effects, the rule of reason is the best approach to distinguishing resale price maintenance agreements that violate the antitrust laws from those that do not.

Here, unlike in Leegin, Uber is not selling anything to drivers that is then resold to riders. Moreover, the justifications for rule of reason treatment of resale price maintenance agreements offered in Leegin are not directly applicable to the instant case. In particular, the Court’s attention has not been drawn to concerns about free-riding Uber drivers, or to efforts that Uber drivers could make to promote the App that will be under-provided if Uber does not set a pricing algorithm. See Leegin, 551 U.S. at 890-91. While Mr. Kalanick asserts that Uber’s pricing algorithm facilitates its market entry as a new brand, this observation—which is fairly conclusory—does not rule out a horizontal conspiracy among Uber drivers, facilitated by Mr. Kalanick both as Uber’s CEO and as a driver himself. The Court therefore finds that plaintiff has adequately pleaded a horizontal antitrust conspiracy under Section 1 of the Sherman Act.
As to plaintiff’s claim of a vertical conspiracy, a threshold question is whether plaintiff has alleged a vertical conspiracy in the Amended Complaint, which defendant denies. Although plaintiff’s allegations of a vertical conspiracy are much more sparse than his contentions about a horizontal conspiracy, the Court finds that the Amended Complaint adequately pleads a vertical conspiracy between each driver and Mr. Kalanick. In particular, plaintiff alleges that “[a]ll of the independent driver-partners have agreed to charge the fares set by Uber’s pricing algorithm,” and that Mr. Kalanick designed this business model. The Amended Complaint also includes several allegations that would be pertinent to a rule of reason, vertical price-fixing theory. Under the Sherman Act count, plaintiff states that the “unlawful arrangement consists of a series of agreements between Kalanick and each of the Uber driver-partners, as well as a conscious commitment among the Uber driver-partners to the common scheme of adopting the Uber pricing algorithm...” Plaintiff claims that Mr. Kalanick is per se liable as organizer of the conspiracy and as an occasional Uber driver, and then states that “[i]n the alternative, Kalanick is also liable under Section 1 of the Sherman Act under a ‘quick look’ or ‘rule of reason’ analysis.” In the Court’s view, these allegations of legal theory, when coupled with the allegations of pertinent facts, are sufficient to plead a vertical conspiracy theory.

The question, then, is whether this theory is plausible under a “rule of reason” analysis. Under this analysis, “plaintiff bears the initial burden of showing that the challenged action has had an actual adverse effect on competition as a whole in the relevant market.” Capital Imaging Associates, P.C. v. Mohawk Valley Med. Associates, Inc., 996 F.2d 537, 543 (2d Cir. 1993). “To survive a Rule 12(b)(6) motion to dismiss, an alleged product market must bear a rational relation to the methodology courts prescribe to define a market for antitrust purposes—analysis of the interchangeability of use or the cross-elasticity of demand, and it must be plausible.” Todd v. Exxon Corp., 275 F.3d 191, 200 (2d Cir. 2001) (internal citation and quotation marks omitted).

As to market definition, plaintiff defines the relevant market as the “mobile app-generated ride-share service market.” Plaintiff alleges that Uber has an approximately 80% market share in the United States in this market; Uber’s chief competitor Lyft has nearly a 20% market share; and a third competitor, Sidecar, left the market at the end of 2015. Plaintiff then explains that traditional taxi service is not a reasonable substitute for Uber, since, for example, rides generated by a mobile app can be arranged at the push of a button and tracked on riders’ mobile phones; riders need not carry cash or a credit
card, or, upon arrival, spend time paying for the ride; and riders can rate drivers and see some information on them before entering the vehicle. Indeed, plaintiff claims, Uber has itself stated that it does not view taxis as ride-sharing competition.

Plaintiff also alleges that traditional cars for hire are not reasonable substitutes, since they generally need to be scheduled in advance for prearranged locations. Id. ¶ 106. However, plaintiff nevertheless contends that “Uber has obtained a significant share of business in the combined markets of taxis, cars for hire, and mobile-app generated ride-share services,” and that Uber’s own experts have suggested that in some U.S. cities, Uber has 50% to 70% of business customers “among all types of rides,” which seems to refer to these combined markets.

Defendant contests plaintiff’s proposed market definition, arguing that plaintiff provides inadequate justification for the exclusion not just of taxis and car services, but also of public transit such as subways and buses, personal vehicle use, and walking. In defendant’s view, “[e]ach of these alternatives is a clear substitute for the services provided by driver-partners.”

One could argue this either way (and defendant’s attorneys are encouraged to hereinafter walk from their offices to the courthouse to put their theory to the test). But for present purposes, plaintiff has provided plausible explanations for its proposed market definition, and the accuracy of these explanations may be tested through discovery and, if necessary, trial. “Market definition is a deeply fact-intensive inquiry [and] courts [therefore] hesitate to grant motions to dismiss for failure to plead a relevant product market.” Chapman v. New York State Div. for Youth, 546 F.3d 230, 238 (2d Cir. 2008). Plaintiff’s allegation that Uber—an industry member—recognizes that it does not compete with taxis also deserves consideration. The Court finds that plaintiff has pleaded a plausible relevant product market.

The Court further finds that plaintiff has adequately pleaded adverse effects in the relevant market. Specifically, plaintiff pleads that “Kalanick’s actions have further restrained competition by decreasing output,”; “Uber’s market position has already helped force Sidecar out of the marketplace”; “Uber’s dominant position and considerable name recognition has also made it difficult for potential competitors to enter the marketplace” . ¶ 103.

Defendant counters that Uber provides many pro-competitive benefits, see Def. Reply Br. at 9, and also disputes the conclusions that plaintiff purports to draw from the cited studies. See Def. Letter.
Defendant’s counter-assertions, while certainly well worth a fact-finder’s consideration, do not persuade the Court to grant a motion to dismiss. The Court hence determines that plaintiff has plausibly pleaded adverse effects in the relevant market. Consequently, the Court finds that plaintiff has presented a plausible claim of a vertical conspiracy under Section 1 of the Sherman Act. *** For these reasons, the Court denies defendant Kalanick’s motion to dismiss. ***

Philadelphia Taxi Ass’n, Inc. v. Uber Technologies, Inc.
886 F.3d 332.

RENDELL, Circuit Judge: Philadelphia taxicab drivers, aggrieved by the influx of taxis hailed at the touch of an app on one’s phone, brought this antitrust action to protest the entry of Appellee Uber Technologies, Inc. (“Uber”) into the Philadelphia taxicab market. The Philadelphia Taxi Association (“PTA”), along with 80 individual taxicab companies (collectively, “Appellants”), appeal the District Court’s dismissal of their Second Amended Complaint (“SAC”) alleging one count of attempted monopolization under Section 2 of the Sherman Act, 15 U.S.C. § 2, and seeking injunctive relief and treble damages under Section 4 of the Clayton Act, 15 U.S.C. § 15.

Appellants urge us to reverse the District Court’s Order, contending that Uber violated the antitrust laws because its entry into the Philadelphia taxicab market was illegal, predatory, and led to a sharp drop in the value of taxicab medallions as well as a loss of profits. They contend that this is evidence that Uber’s operation in Philadelphia was anticompetitive and caused them to suffer an antitrust injury. However, the conduct they allege falls short of the conduct that would constitute an attempted monopoly in contravention of the antitrust laws. Thus, we will affirm the District Court’s dismissal of the SAC for failure to state a claim for attempted monopolization and failure to state an antitrust injury.

I. Background & Procedural History

From March of 2005 to October of 2014, taxicabs operating in Philadelphia were required to have a medallion and a certificate of public convenience, issued by the Philadelphia Parking Authority (“PPA”). Medallions are property, and are often pledged as collateral to borrow funds to finance the purchase of the cab or to “upgrade and improve the operations of taxicabs.” 53 Pa. C.S.A. § 5712(a). Once
medallion-holders comply with the obligatory standards for taxicabs, they may obtain a certificate of public convenience. Those standards, which provide for safety and uniformity among taxicabs, require vehicles to be insured and in proper condition, and mandate that drivers are paid the prevailing minimum wage, are proficient in English, and have the appropriate drivers’ licenses.

As alleged in the SAC, when the medallion system was mandated in Philadelphia in 2005, a medallion was worth only $65,000. In October of 2014, there were approximately 500 taxicab companies in Philadelphia. Together, 7,000 drivers held 1610 medallions, each valued at an average of $545,000.

Appellants are 80 of those 500 companies, which collectively hold 240 of the 1610 medallions, as well as PTA, which was incorporated to advance the legal interests of its members—the 80 individual medallion taxicab companies.

Uber began operating in Philadelphia in October of 2014 without securing medallions or certificates of public convenience for its vehicles. While a potential rider can avail himself of a medallion taxicab by calling a dispatcher or hailing an available cab, to use Uber, he can download the Uber application onto his mobile phone and request that the vehicle come to his location, wherever he is. Passengers enter payment information, which is retained by Uber and automatically processed at the end of each ride. Uber does not own or assume legal responsibility for the vehicles or their operation, nor does it hire the drivers as its employees. Uber did not pay fines to the PPA or comply with its regulations when it first entered the Philadelphia taxi market, as is otherwise required for medallion taxicabs. Appellants maintain that this rendered Uber’s operation illegal, and enabled the company to cut operating costs considerably.

In October of 2016, the Pennsylvania state legislature passed a law approving Uber’s operation in Philadelphia, under the authority of the PPA. The law, which went into effect in November of 2016, allows the PPA to regulate both medallion taxicab companies and Transportation Network Companies (“TNCs”)—a classification that includes Uber and other vehicle-for-hire companies that operate through digital apps—in Philadelphia. TNCs must now obtain licenses to operate and comply with certain requirements, including insurance obligations and safety standards for drivers and vehicles. The law also exempts TNCs from disclosing the number of drivers or vehicles operating in the city, and allows TNCs to set their own fares, unlike medallion taxicab companies, which comply with established rates,
minimum wages, and have a limited number of vehicles and medallions operating at once in Philadelphia.

Before this law passed, in Uber’s first two years in Philadelphia, nearly 1200 medallion taxi drivers left their respective companies and began to drive for Uber. In those two years, there were 1700 Uber drivers and vehicles operating in Philadelphia, serving over 700,000 riders, for more than one million trips. Simultaneously, medallion taxi rides reduced by about 30 percent, and thus Appellants experienced a 30 percent decrease in earnings. The value of each medallion dropped significantly, to approximately $80,000 in November of 2016. Fifteen percent of medallions have been confiscated by the lenders due to default by drivers.

The PTA and 75 individual taxicab companies filed a Complaint, alleging three counts: attempted monopolization under Section 2 of the Sherman Act, tortious interference with contract under Pennsylvania law, and unfair competition under Pennsylvania law. Uber moved to dismiss the Complaint.

Appellants, the PTA and now 80 individual taxicab companies, then filed an Amended Complaint, alleging the same three counts. Uber moved to dismiss the Amended Complaint. The District Court granted the dismissal, without prejudice. The District Court noted that Plaintiffs alleged merely harm to their business after Uber entered the Philadelphia taxicab market, and that Plaintiffs pointed to Uber’s supposed illegal participation in the taxicab market as evidence of attempted monopolization. However, the District Court concluded that these harms are “not the type of injuries that antitrust laws were intended to prevent, and thus do not establish antitrust standing.” Phila. Taxi Ass’n, Inc. v. Uber Techs., Inc., 218 F. Supp. 3d 389, 392 (E.D. Pa. 2016). The Court also dismissed the state law claims, for failure to plead the proper elements of an unfair competition or a tortious interference claim.

Appellants then filed the SAC, alleging one count of attempted monopolization under Section 2 of the Sherman Act and seeking treble damages under Section 4 of the Clayton Act. Uber responded with a Motion to Dismiss, which the District Court granted, with prejudice. The District Court held that Appellants, in spite of multiple opportunities for amendment, had pled no antitrust injury sufficient for antitrust standing, and were unlikely to cure the lack of standing with any amendments to the SAC. The Court also held that the PTA could not satisfy the requirements for associational standing because the association’s members lacked standing to sue on their own.***

III. Discussion
*** If the challenged conduct has an effect on “prices, quantity or quality of goods or services,” Mathews v. Lancaster Gen. Hosp., 87 F.3d 624, 641 (3d Cir. 1996), we will find a violation of antitrust laws only when that effect harms the market, and thereby harms the consumer.

Anticompetitive conduct is the hallmark of an antitrust claim. An allegation of anticompetitive conduct is necessary both to: (1) state a claim for attempted monopolization; and (2) aver that a private plaintiff has suffered an antitrust injury. Appellants’ SAC, however, is deficient in averring conduct that is, in fact, anticompetitive.

While our caselaw is unresolved regarding which to address first—an antitrust violation or an antitrust injury—we need not resolve that here, because Appellants’ claim fails on both counts. We begin by discussing how Appellants’ allegations in the SAC fall short of demonstrating anticompetitive conduct, and thus fail to state a claim for attempted monopolization, and then discuss how in the alternative, Appellants fail to allege antitrust injury to have antitrust standing. For both reasons, we affirm the judgment of the District Court dismissing the SAC with prejudice.

A. Attempted Monopolization

To prevail on a claim under Sherman Act Section 2 for attempted monopolization, a plaintiff must prove: “(1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power.” Mylan Pharm. Inc. v. Warner Chilcott Pub. Ltd. Co., 838 F.3d 421, 433 (3d Cir. 2016) (quoting Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 317 (3d Cir. 2007). *** Liability hinges on whether valid business reasons, as part of the ordinary competitive process, can explain the defendant’s actions that resulted in a dangerous probability of achieving monopoly power. See Avaya Inc., RP v. Telecom Labs, Inc., 838 F.3d 354, 393 (3d Cir. 2016).

In the SAC, Appellants allege that Uber: (1) flooded the market with non-medallion taxicabs, entered the market illegally without purchasing medallions, operated at a lower cost by failing to comply with statutory requirements and regulations, and lured away drivers from Individual Plaintiffs, which allegedly impaired the competitive market for medallion taxicabs; (2) knew of PPA’s regulatory jurisdiction over vehicles for hire, purposefully ignored or avoided the regulations and rulings of the Court of Common Pleas, and thereby excluded rivals from competing in the taxicab market; and (3) is dangerously close to achieving monopoly power with its market share and by operating in an unfair playing field with the “financial ability”
to be the only market player and to destroy competitors' business. SAC ¶ 83. Appellants also complain that the new legislation authorizing the TNCs’ operation would facilitate the creation of an illegal monopoly.

We find that the SAC fails to plausibly allege any of the three elements of an attempted monopolization claim.

1. Anticompetitive Conduct

Allegations of purportedly anticompetitive conduct are meritless if those acts would cause no deleterious effect on competition. This is where the SAC falters: Appellants set forth a litany of ways in which Uber’s entry into the market has harmed Appellants’ business and their investment in medallions; yet none of the allegations demonstrate a harmful effect on competition.

To determine whether conduct is anticompetitive, “courts must look to the monopolist’s conduct taken as a whole rather than considering each aspect in isolation.” LePage’s Inc. v. 3M, 324 F.3d 141, 162 (3d Cir. 2003) (en banc).

Here, Appellants claim that Uber inundated the Philadelphia taxicab market illegally with their non-medallion vehicles. They contend that Uber’s entry into the market was predatory because it failed to comply with statutory and regulatory requirements, failed to purchase medallions, failed to pay drivers a minimum wage, and failed to obtain the proper insurance, among other actions. All of these actions, Appellants assert, enabled Uber to operate at a significantly lower cost than the medallion companies, and thereby acquire a stronghold in the Philadelphia taxicab market.

Appellants also maintain that Uber “flooded” the Philadelphia taxicab market by improperly luring drivers away from medallion companies, including Individual Plaintiffs. Appellants cite Uber’s practice of sending representatives to 30th Street Station and the Philadelphia International Airport, where medallion taxicab drivers often congregate, to disseminate information about its services and to recruit potential drivers. They argue that Uber promised new drivers financial inducements, such as reimbursements for the cost of gasoline, as an incentive to leave their medallion companies and instead drive for Uber.

Considering the averments regarding Uber’s conduct in their totality, Uber’s elimination of medallion taxicab competition did not constitute anticompetitive conduct violative of the antitrust laws.

First, inundating the Philadelphia taxicab market with Uber vehicles, even if it served to eliminate competitors, was not anticompetitive. Rather, this bolstered competition by offering
customers lower prices, more available taxicabs, and a high-tech alternative to the customary method of hailing taxicabs and paying for rides. It is well established that lower prices, as long as they are not predatory, benefit consumers—“regardless of how those prices are set.” *Atl. Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990). “Cutting prices in order to increase business often is the very essence of competition.” *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 592 (1986). Thus, lost business alone cannot be deemed a consequence of “anticompetitive” acts by the defendant. See *Atl. Richfield*, 495 U.S. at 337.

Second, Uber’s ability to operate at a lower cost is not anticompetitive. Running a business with greater economic efficiency is to be encouraged, because that often translates to enhanced competition among market players, better products, and lower prices for consumers. Even if Uber were able to cut costs by allegedly violating PPA regulations, Appellants cannot use the antitrust laws to hold Uber liable for these violations absent proof of anticompetitive conduct. Even unlawful conduct is “of no concern to the antitrust laws” unless it produces an anticompetitive effect. *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 487 (1977).

Finally, hiring rivals may be anticompetitive, but only in certain cases. For example, if rival employees were hired in an attempt to exclude competitors from the market for some basis other than efficiency or merit, such as to acquire monopoly power or to merely deny the employees to the rival, this could violate the antitrust laws if injurious to the rival and to competition at large.

However, Appellants acknowledge that the nearly 1200 medallion taxicab drivers that Uber recruited did not remain idle, but rather they drove for Uber. In sum, what Appellants allege does not give rise to an inference of anticompetitive or exclusionary conduct and suggests, if anything, that Uber’s ability to attract these drivers was due to its cost efficiency and competitive advantage.

Thus, the SAC is devoid of allegations of truly anticompetitive conduct.

2. Specific Intent to Monopolize

Appellants allege specific intent to monopolize from Uber’s knowledge that the PPA maintained regulatory authority over vehicles-for-hire, and its choice to avoid regulation by being a TNC that neither owned vehicles nor employed drivers. They also point to Uber’s alleged willful disregard of the rulings of the Court of Common
Pleas. Appellants’ claim, in essence, is that Uber’s knowledge that their operation was illegal reveals a specific intent to monopolize.

“[I]n a traditional § 2 claim, a plaintiff would have to point to specific, egregious conduct that evinced a predatory motivation and a specific intent to monopolize.” *Avaya*, 838 F.3d at 406 (citing *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456 (1993)). ***

While Uber’s alleged conduct might have formed the basis of a regulatory violation, its knowledge of existing regulations alone cannot reasonably be said to demonstrate specific intent to monopolize. Further, Uber’s choice to distinguish itself from other vehicles-for-hire, eschewing medallions in favor of independent drivers who operate their own cars at will, can instead be reasonably viewed as “predominantly motivated by legitimate business aims.” *Times Picayune Publ’g Co. v. United States*, 345 U.S. 594, 627 (1953). Appellants have not averred any other motive. The allegations suggest that these business choices allowed Uber to operate more efficiently, and to offer a service that consumers find attractive, thus enabling it to acquire a share of the Philadelphia taxicab market.

Thus, Uber’s alleged competitive strategy of creating a vehicle-for-hire business model, presumably to acquire customers, does not reflect specific intent to monopolize. Accordingly, Appellants have failed to allege specific intent on Uber’s part.

3. Dangerous Probability of Achieving Monopoly Power

We held in *Broadcom Corp. v. Qualcomm Inc.* that because the dangerous probability standard is a complex and “fact-intensive” inquiry, courts “typically should not resolve this question at the pleading stage ‘unless it is clear on the face of the complaint that the “dangerous probability” standard cannot be met as a matter of law.’” 501 F.3d at 318-19 (quoting *Brader v. Allegheny Gen. Hosp.*, 64 F.3d 869, 877 (3d Cir. 1995)).

We may consider factors such as “significant market share coupled with anticompetitive practices, barriers to entry, the strength of competition, the probable development of the industry, and the elasticity of consumer demand” to determine whether dangerous probability was alleged in the pleadings. Id. Entry barriers include “regulatory requirements, high capital costs, or technological obstacles[] that prevent new competition from entering a market.” Id. at 307 (citations omitted). “No single factor is dispositive.” Id. at 318.

Appellants argue that Uber has a dangerous probability of achieving monopoly power because it has pushed numerous competitors out of the market. As discussed, however, the SAC fails to
allege anticompetitive practices by Uber. Nor does the SAC mention Uber’s market share; it merely suggests that Uber and medallion taxicabs had similar numbers of vehicles operating in Philadelphia as of October 2016. This allegation falls short of indicating Uber’s market share in the context of all the competitors in the Philadelphia taxicab market, such as other TNCs.

Similarly, the SAC makes no allegation of current barriers to entry or weak competition from other market participants. Appellants make the bold allegation that Uber holds the power to raise barriers to entry in the market, without any factual support. In fact, the SAC alleges that Uber was readily able to enter the Philadelphia market. *** Surely other competitors, such as Lyft, are able to enter without difficulty, as well.

Nor does the SAC describe any potentially harmful industry developments. It only vaguely claims that Uber may be able to drive out competition and raise entry barriers. Appellants assert in the SAC that once Uber becomes the dominant competitor, it would be able to charge higher prices, and consumers who do not own smartphones would be deprived of the ability to hail taxis on the street. Absent any allegations of a dangerous probability of achieving monopoly power, this argument fails. And, as counsel for Uber stated at oral argument, if Uber raised its prices, this would encourage other rivals to enter the market and charge lower prices, battling Uber through price competition.

Because the elements of attempted monopolization are often interdependent, proof of one element may provide “permissible inferences” of other elements. Broadcom, 501 F.3d at 318 (quoting Barr Labs., Inc. v. Abbott Labs., 978 F.2d 98, 112 (3d Cir. 1992)). Even so, none of the other elements of attempted monopolization allow us to infer a dangerous probability that Uber will achieve monopoly power. Acknowledging Broadcom’s reticence to resolve the dangerous probability question at the pleadings stage, we nevertheless find that the SAC does not allege any of the relevant factors to prove that Uber had a dangerous probability of achieving monopoly power.

In sum, Appellants have failed to set forth a plausible claim of attempted monopolization under Section 2 of the Sherman Act, as a matter of law. ***

V. Conclusion

Appellants may have been better off, financially, if Uber had not entered the Philadelphia taxicab market. However, Appellants have no right to exclude competitors from the taxicab market, even if

If medallion taxicabs could prevent TNCs from entering the Philadelphia market, and if incumbents could prevent new entrants or new technologies from competing because they fear loss of profits, then “economic progress might grind to a halt.” Id. at 596-97. “Instead of taxis we might have horse and buggies; instead of the telephone, the telegraph; instead of computers, slide rules.” Id. at 597.

Absent any allegations of anticompetitive conduct, Appellants fail to allege any of the elements for a claim for attempted monopolization under Section 2 of the Sherman Act and fail to allege antitrust standing.

For the foregoing reasons, the judgment of the District Court is AFFIRMED.

Chamber of Commerce of the United States of America v. City of Seattle
890 F.3d 769.

M. SMITH, Circuit Judge: On December 14, 2015, the Seattle City Council enacted into law Ordinance 124968, an Ordinance Relating to Taxicab, Transportation Network Company, and For-Hire Vehicle Drivers (Ordinance). The Ordinance was the first municipal ordinance of its kind in the United States, and authorizes a collective-bargaining process between “driver coordinators”—like Uber Technologies (Uber), Lyft, Inc. (Lyft), and Eastside for Hire, Inc. (Eastside)—and independent contractors who work as for-hire drivers. The Ordinance permits independent-contractor drivers, represented by an entity denominated an “exclusive driver representative,” and driver coordinators to agree on the “nature and amount of payments to be made by, or withheld from, the driver coordinator to or by the drivers.” Seattle, Wash., Municipal Code § 6.310.735(H)(1). This provision of the Ordinance is the crux of this case.

Acting on behalf of its members Uber, Lyft, and Eastside, Plaintiff-Appellant the Chamber of Commerce of the United States of America, together with Plaintiff-Appellant Rasier, LLC, a subsidiary of Uber (collectively, the Chamber), sued Defendants-Appellees the City of Seattle, the Seattle Department of Finance and Administrative
Services (the Department), and the Department’s Director, Fred Podesta (collectively, the City), challenging the Ordinance on federal antitrust and labor law grounds. First, the Chamber asserts that the Ordinance violates, and is preempted by, section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1, because the Ordinance sanctions price-fixing of ride-referral service fees by private cartels of independent-contractor drivers. Second, the Chamber claims that the Ordinance is preempted by the National Labor Relations Act (NLRA), 29 U.S.C. §§ 151-169, under Machinists and Garmon preemption.

The district court dismissed the case, holding that the state-action immunity doctrine exempts the Ordinance from preemption by the Sherman Act, and that the NLRA does not preempt the Ordinance. The Chamber appealed both holdings.

We have jurisdiction over this appeal pursuant to 28 U.S.C. § 1291. We reverse the district court’s dismissal of the Chamber’s federal antitrust claims, and remand the federal antitrust claims to the district court for further proceedings. We also affirm the district court’s dismissal of the Chamber’s NLRA preemption claims.

FACTUAL AND PROCEDURAL BACKGROUND

A. Ride-Referral Companies

Eastside is the largest dispatcher of taxicab and for-hire vehicles in the Pacific Northwest. Eastside provides licensed taxicab and for-hire vehicle drivers with dispatch, advertising, payment processing, and other administrative services, in exchange for a weekly fee, payable by drivers to Eastside. Relying on advertising and a preexisting client base, Eastside generates transportation requests from passengers, who call, text-message, or email Eastside to request a ride. Eastside then refers ride requests to drivers through a mobile data terminal. If a passenger uses a credit card to pay a driver, Eastside processes the transaction and remits the payment to the driver. The drivers who pay for Eastside’s services are independent contractors—Eastside does not dictate how the drivers operate their transportation businesses. For example, some drivers own licensed vehicles, whereas others lease them.

Uber and Lyft, founded in 2009 and 2012, respectively, have ushered ride-referral services into the digital age. Uber and Lyft have developed proprietary smartphone applications (apps) that enable an online platform, or digital marketplace, for ride-referral services, often referred to as “ridesharing” services. After downloading the Uber or Lyft app onto their smartphones, riders request rides through the app, which transmits ride requests to available drivers nearby. Drivers are
free to accept or ignore a ride request. If a driver accepts a ride request, he or she is matched electronically with the rider, and then proceeds to the rider's location and fulfills the ride request. If a driver ignores a ride request, the digital platform transmits the request to another nearby driver. Drivers may cancel a ride request, even after initially accepting it, at any point prior to the commencement of the ride. Riders, too, may decide whether or not to accept a ride from any of the drivers contacted through the app. After a ride is completed, riders pay drivers via the Uber or Lyft app, using a payment method, such as a credit card, placed on file with Uber or Lyft.

Uber and Lyft's business models have facilitated the rise of the so-called “gig economy.” In order to receive ride requests through the apps, drivers contract with, and pay a technology licensing fee to, Uber or Lyft. These licensing fees are a percentage of riders' paid fares: Uber and Lyft subtract their technology licensing fees from riders' payments, and remit the remainder to drivers. Drivers' contractual agreements with either Uber or Lyft are not exclusive—in fact, many drivers use several ridesharing apps and even operate multiple apps simultaneously. Drivers may use the Uber and Lyft apps for however long and whenever they wish, if they wish to use them at all.

B. The Ordinance

On December 14, 2015, the Seattle City Council adopted Ordinance 124968. The stated purpose of the Ordinance is to “allow[] taxicab, transportation network company, and for-hire vehicle drivers (‘for-hire drivers’) to modify specific agreements collectively with the entities that hire, direct, arrange, or manage their work,” in order to “better ensure that [for-hire drivers] can perform their services in a safe, reliable, stable, cost-effective, and economically viable manner.” Seattle, Wash., Ordinance 124968, pmbl.

The Ordinance requires “driver coordinators” to bargain collectively with for-hire drivers. Id. § 1(I). A “driver coordinator” is defined as “an entity that hires, contracts with, or partners with for-hire drivers for the purpose of assisting them with, or facilitating them in, providing for-hire services to the public.” Seattle, Wash., Municipal Code § 6.310.110. The Ordinance applies only to drivers who contract with a driver coordinator “other than in the context of an employer-employee relationship”—in other words, the Ordinance applies only to independent contractors. Id. § 6.310.735(D).

The collective-bargaining process begins with the election of a “qualified driver representative,” or QDR. Id. §§ 6.310.110, 6.310.735(C). An entity seeking to represent for-hire drivers operating within Seattle first submits a request to the Director of Finance and
Administrative Services (the Director) for approval to be a QDR. Id. § 6.310.735(C). Once approved by the City, the QDR must notify the driver coordinator of its intent to represent the driver coordinator’s for-hire drivers. Id. § 6.310.735(C)(2).

Upon receiving proper notice from the QDR, the driver coordinator must provide the QDR with the names, addresses, email addresses, and phone numbers of all “qualifying drivers.” Id. § 6.310.735(D). This disclosure requirement applies only to driver coordinators that have “hired, contracted with, partnered with, or maintained a contractual relationship or partnership with, 50 or more for-hire drivers in the 30 days prior to the commencement date” set by the Director. Id.

The QDR then contacts the qualifying drivers to solicit their interest in being represented by the QDR. Id. § 6.310.735(E). Within 120 days of receiving the qualifying drivers’ contact information, the QDR submits to the Director statements of interest from qualifying drivers indicating that they wish to be represented by the QDR in collective-bargaining negotiations with the driver coordinator. Id. § 6.310.735(F)(1). If a majority of qualifying drivers consent to representation by the QDR, the Director certifies the QDR as the “exclusive driver representative” (EDR) for all for-hire drivers for that particular driver coordinator. Id. § 6.310.735(F)(2).

Once the Director certifies the EDR, the driver coordinator and the EDR shall meet and negotiate in good faith certain subjects to be specified in rules or regulations promulgated by the Director including, but not limited to, best practices regarding vehicle equipment standards; safe driving practices; the manner in which the driver coordinator will conduct criminal background checks of all prospective drivers; the nature and amount of payments to be made by, or withheld from, the driver coordinator to or by the drivers; minimum hours of work, conditions of work, and applicable rules. Id. § 6.310.735(H)(1) (emphasis added).

If an agreement is reached, the driver coordinator and the EDR submit the written agreement to the Director. Id. § 6.310.735(H)(2). The Director reviews the agreement for compliance with the Ordinance and Chapter 6.310 of the Seattle Municipal Code, which governs taxicabs and for-hire vehicles. Id. In conducting this review, the Director is to “ensure that the substance of the agreement promotes the provision of safe, reliable, and economical for-hire transportation services and otherwise advance[s] the public policy goals set forth in Chapter 6.310 and in the [Ordinance].” Id.
The Director’s review is not limited to the parties’ submissions or the terms of the proposed agreement. Id. Rather, the Director may gather and consider additional evidence, conduct public hearings, and request information from the EDR and the driver coordinator. Id.

The agreement becomes final and binding on all parties if the Director finds the agreement compliant. Id. § 6.310.735(H)(2)(a). The agreement does not take effect until the Director makes such an affirmative determination. Id. § 6.310.735(H)(2)(c). If the Director finds the agreement noncompliant, the Director remands it to the parties with a written explanation of the agreement’s failures, and may offer recommendations for remedying the agreement’s inadequacies. Id. § 6.310.735(H)(2)(b).

If the driver coordinator and the EDR do not reach an agreement, “either party must submit to interest arbitration upon the request of the other,” in accordance with the procedures and criteria specified in the Ordinance. Id. § 6.310.735(I). The interest arbitrator must propose an agreement compliant with Chapter 6.310 and in line with the City’s public policy goals. Id. § 6.310.735(I)(2). The term of an agreement proposed by the interest arbitrator may not exceed two years. Id.

The interest arbitrator submits the proposed agreement to the Director, who reviews the agreement for compliance with the Ordinance and Chapter 6.310, in the same manner the Director reviews an agreement proposed by the parties. Id. § 6.310.735(I)(3).

The parties may discuss additional terms and propose amendments to an approved agreement. Id. § 6.310.735(J). The parties must submit any proposed amendments to the Director for approval. Id. The Director has the authority to withdraw approval of an agreement during its term, if the Director finds that the agreement no longer complies with the Ordinance or furthers the City’s public policy goals. Id. § 6.310.735(J)(1). ***

ANALYSIS

I. State-Action Immunity Does Not Protect the Ordinance from Preemption by Section 1 of the Sherman Act.

We turn first to the Chamber’s federal antitrust claims, and hold that the Ordinance does not meet the requirements for state-action immunity.

A. Preemption

In determining whether the Sherman Act preempts a state or local law pursuant to the Supremacy Clause, we apply the principles

A state or local law, “when considered in the abstract, may be condemned under the antitrust laws,” and thus preempted, “only if it mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.” *Id.* at 661. “Such condemnation will follow under [section] 1 of the Sherman Act when the conduct contemplated by the statute is in all cases a per se violation.” *Id.* However, “[i]f the activity addressed by the statute does not fall into that category, and therefore must be analyzed under the rule of reason, the statute cannot be condemned in the abstract.” *Id.* Unlike the categorical analysis under the per se rule of illegality, “[a]nalysis under the rule of reason requires an examination of the circumstances underlying a particular economic practice, and therefore does not lend itself to a conclusion that a statute is facially inconsistent with federal antitrust laws.” *Id.* In short, the Ordinance may be preempted facially by federal antitrust law if it authorizes a per se violation of section 1 of the Sherman Act, but not if it must be analyzed under the rule of reason.

***

Here, the district court assumed, without deciding, “that collusion between independent economic actors to set the prices they will accept for their services in the market is a per se antitrust violation.” On appeal, the City acknowledges that it “did not challenge the Chamber’s contention that collective negotiations regarding topics such as payments to drivers could, absent Parker immunity, constitute per se antitrust violations.” Because the district court dismissed the Chamber’s federal antitrust claims solely on the basis of state-action immunity, we limit our analysis to that issue. We accept, without reaching the merits of the question, that the Ordinance authorizes a per se antitrust violation. The parties may address on remand which mode of antitrust analysis—the per se rule of illegality or the rule of reason—applies.

B. The Requirements for State-Action Immunity

The state-action immunity doctrine derives from *Parker v. Brown*, 317 U.S. 341 (1943). In *Parker*, the Supreme Court held that “because ‘nothing in the language of the Sherman Act ... or in its history’ suggested that Congress intended to restrict the sovereign capacity of the States to regulate their economies, the Act should not
be read to bar States from imposing market restraints ‘as an act of

State-action immunity is the exception rather than the rule. *** The Supreme Court uses a two-part test, sometimes referred to as the *Midcal* test, to “determin[e] whether the anticompetitive acts of private parties are entitled to immunity.” Id. First, “the challenged restraint [must] be one clearly articulated and affirmatively expressed as state policy,” and second, “the policy [must] be actively supervised by the State.” Id. (quoting *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, **445 U.S. 97, 105** (1980)).

“Because municipalities and other political subdivisions are not themselves sovereign, state-action immunity under *Parker* does not apply to them directly.” Id. As such, “immunity will only attach to the activities of local governmental entities if they are undertaken pursuant to a ‘clearly articulated and affirmatively expressed’ state policy to displace competition.” Id. at 226, (quoting *Cmty. Commc’ns Co. v. Boulder*, **455 U.S. 40, 52** (1982)). Local governmental entities, “unlike private parties, . . . are not subject to the ‘active state supervision requirement’ because they have less of an incentive to pursue their own self-interest under the guise of implementing state policies.” Id. (quoting *Town of Hallie v. City of Eau Claire*, **471 U.S. 34, 46-47** (1985)). “Where state or municipal regulation by a private party is involved, however, active state supervision must be shown, even where a clearly articulated state policy exists.” *Hallie*, **471 U.S. at 46 n.10**.

i. The Clear-Articulation Test

We conclude that the anticompetitive restraint challenged in this case fails the first prong of the *Midcal* test. The State of Washington has not “clearly articulated and affirmatively expressed” a state policy authorizing private parties to price-fix the fees for-hire drivers pay to companies like Uber or Lyft in exchange for ride-referral services.

The clear-articulation test is met “if the anticompetitive effect was the ‘foreseeable result’ of what the State authorized.” *Phoebe Putney*, **568 U.S. at 226-27** (quoting *Hallie*, **471 U.S. at 42**). “[T]o pass the “clear articulation” test,’ a state legislature need not ‘expressly state in a statute or its legislative history that the legislature intends
for the delegated action to have anticompetitive effects.” Id. at 226 (alteration in original) (quoting Hallie, 471 U.S. at 43). ***

Our inquiry with respect to the clear-articulation test is a precise one. “[T]he relevant question is whether the regulatory structure which has been adopted by the state has specifically authorized the conduct alleged to violate the Sherman Act.” Cost Mgmt. Servs., Inc. v. Wash. Nat. Gas Co., 99 F.3d 937, 942 (9th Cir. 1996) (emphasis added). The state’s authorization must be plain and clear: The relevant statutory provisions must “plainly show that the [state] legislature contemplated the sort of activity that is challenged,” which occurs where they “confer ‘express authority to take action that foreseeably will result in anticompetitive effects.’” Hass v. Or. State Bar, 883 F.2d 1453, 1457 (9th Cir. 1989) (first emphasis added) (quoting Hallie, 471 U.S. at 43-44). The state, in its sovereign capacity, must “clearly intend[] to displace competition in a particular field with a regulatory structure ... in the relevant market.” S. Motor Carriers Rate Conference, Inc. v. United States, 471 U.S. 48, 64 (1985).

Once we determine that there is express state authorization, we then turn to the concept of foreseeability, which “is to be used in deciding the reach of antitrust immunity that stems from an already authorized monopoly, price regulation, or other disruption in economic competition.” Shames, 626 F.3d at 1084 (second emphasis added). A foreseeable result cannot circumvent the requirement that there be express authorization in the first place: “[A] foreseeable result cannot create state authorization itself,” but must itself stem from express authorization, which is “the necessary predicate for the Supreme Court’s foreseeability test.” Id. (quoting Columbia Steel Casting Co. v. Portland Gen. Elec. Co., 111 F.3d 1427, 1444 (9th Cir. 1996)). We must be careful not to “appl[y] the concept of ‘foreseeability’ from [the] clear-articulation test too loosely.” Phoebe Putney, 568 U.S. at 229.

Applying these principles to the Ordinance, we conclude that the clear-articulation requirement has not been satisfied. The state statutes relied upon by the City Council in enacting the Ordinance—Revised Code of Washington sections 46.72.001, 46.72.160, 81.72.200, and 81.72.210—do not “plainly show” that the Washington legislature “contemplated” allowing for-hire drivers to price-fix their compensation. Nor is such an anticompetitive result foreseeable.

We examine the state statutes in turn. First, Revised Code of Washington section 46.72.001 provides:

The legislature finds and declares that privately operated for hire transportation service is a vital part of the transportation system within the state. Consequently, the safety, reliability,
and stability of privately operated for hire transportation services are matters of statewide importance. The regulation of privately operated for hire transportation services is thus an essential governmental function. Therefore, it is the intent of the legislature to permit political subdivisions of the state to regulate for hire transportation services without liability under federal antitrust laws.

That the Washington state legislature “inten[ded] ... to permit political subdivisions of the state to regulate for hire transportation services without liability under federal antitrust laws,” id., is insufficient to bring the Ordinance within the protective ambit of state-action immunity. We are mindful of the Supreme Court’s instruction that “a State may not confer antitrust immunity on private persons by fiat,” Ticor Title, 504 U.S. at 633, and that a “State may not validate a municipality’s anticompetitive conduct simply by declaring it to be lawful,” Hallie, 471 U.S. at 39. Rather, it must first meet the Midcal requirements: A state “may displace competition with active state supervision [only] if the displacement is both intended by the State and implemented in its specific details.” Ticor Title, 504 U.S. at 633. We may not “defer[] to private pricefixing arrangements under the general auspices of state law,” but instead must ensure that the “precondition[s] for immunity from federal law,” such as “[a]ctual state involvement,” are met. Id. After all, “[i]mmunity is conferred out of respect for ongoing regulation by the State, not out of respect for the economics of price restraint.” Id.

The plain language of the statute centers on the provision of “privately operated for hire transportation services,” Wash. Rev. Code § 46.72.001, not the contractual payment arrangements between for-hire drivers and driver coordinators for use of the latter’s smartphone apps or ride-referral services. Although driver coordinators like Uber and Lyft contract with providers of transportation services, they do not fulfill the requests for transportation services—the drivers do. Nothing in the statute evinces a clearly articulated state policy to displace competition in the market for ride-referral service fees charged by companies like Uber, Lyft, and Eastside. In other words, although the statute addresses the provision of transportation services, it is silent on the issue of compensation contracts between for-hire drivers and driver coordinators. To read into the plain text of the statute implicit state authorization and intent to displace competition with respect to for-hire drivers’ compensation would be to apply the clear-articulation test “too loosely.” Phoebe Putney, 568 U.S. at 229. ***
The regulation of rates in one area—i.e., the regulation of rates charged to passengers for transportation services—does not confer the shield of state-action immunity onto anticompetitive conduct in a related market—i.e., price-fixing the fees for-hire drivers pay to Uber and Lyft in order to use their digital platforms.

In cases in which the Supreme Court found the clear-articulation test to be satisfied, the initial state authorization clearly contemplated and plainly encompassed the challenged anticompetitive conduct. *** Tellingly, Uber and Lyft did not exist when the Washington statutes were enacted. The very concept of digital ridesharing services was probably well beyond the imaginations of lawmakers two to three decades ago, much less foreseeable. But the fact that technology has advanced leaps and bounds beyond the contemplation of the state legislature is not, on its own, the dispositive factor in our holding today. Digital platforms like Uber and Lyft have become “highly interconnected with modern economic and social life,” Fields v. Twitter, Inc., 881 F.3d 739, 749 (9th Cir. 2018), and present novel challenges and contexts for regulation. Nevertheless, it is not our role to make policy judgments properly left to the Washington state legislature. Instead, we must tread carefully in the area of state-action immunity, lest “a broad interpretation of the doctrine ... inadvertently extend immunity to anticompetitive activity which the states did not intend to sanction,” or “a broad application of the doctrine ... impede states’ freedom by threatening to hold them accountable for private activity they do not condone ‘whenever they enter the realm of economic regulation.’” Cost Mgmt. Servs., 99 F.3d at 941 (quoting Ticor Title, 504 U.S. at 635-36).

Applying governing law, we hold that the clear-articulation requirement for state-action immunity is not satisfied in this case.

ii. The Active-Supervision Requirement

We next hold that the Ordinance does not meet the active-supervision requirement for Parker immunity.

“The active supervision requirement demands ... ‘that state officials have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy.’” N.C. State Bd. of Dental Examiners v. FTC, ___ U.S. ___ (2015) (quoting Patrick v. Burget, 486 U.S. 94, 101 (1988)). Because “[e]ntities purporting to act under state authority might diverge from the State’s considered definition of the public good” and “[t]he resulting asymmetry between a state policy and its implementation can invite private self-dealing,” the active-supervision requirement
“seeks to avoid this harm by requiring the State to review and approve interstitial policies made by the entity claiming immunity.” Id.

As a threshold matter, we first clarify that the active-supervision requirement applies to this case. It is settled law that “active state supervision is not a prerequisite to exemption from the antitrust laws where the actor is a municipality rather than a private party.” Hallie, 471 U.S. at 47. However, where, as here, “state or municipal regulation by a private party is involved, . . . active state supervision must be shown, even where a clearly articulated state policy exists.” Id. at 46n.10 (citing Southern Motor Carriers, 471 U.S. at 62).

Southern Motor Carriers is illustrative. *** Likewise here, private parties—for-hire drivers and driver coordinators—are permitted to set rates collectively and submit them to the Director for approval. Accordingly, the active-supervision requirement applies.

The involvement of private parties in municipal regulation renders this case ineligible for the municipality exception outlined in Hallie: “Hallie explained that ‘[w]here the actor is a municipality, there is little or no danger that it is involved in a private price-fixing arrangement. The only real danger is that it will seek to further purely parochial public interests at the expense of more overriding state goals.’” Dental Examiners, 135 S.Ct. at 1112 (alteration in original) (quoting Hallie, 471 U.S. at 47). In contrast, this case presents a scenario in which the City authorizes collective price-fixing by private parties, which the Director evaluates and ratifies. The amount of discretion the Ordinance confers upon private actors is far from trivial.

Having decided that the active-supervision requirement applies to this case, we turn to examine whether it is met. Clearly, it is not. It is undisputed that the State of Washington plays no role in supervising or enforcing the terms of the City’s Ordinance.

The City cites no controlling authority to support its argument that the Supreme Court uses the word “State” simply “as shorthand for the State and all its agents, including municipalities.” The Supreme Court has stated repeatedly that active supervision must be “by the State itself.” Midcal, 445 U.S. at 105:

We take it as a given that the Supreme Court means what it states. In Hallie, the Supreme Court stated that “[w]here state or municipal regulation by a private party is involved, however, active state supervision must be shown.” 471 U.S. at 46 n.10. In the first clause, the Supreme Court used “state or municipal,” thus drawing a disjunctive difference between the two words. In the second clause, it used only “state.” It is highly improbable that the Supreme Court chose to distinguish between states and municipalities in the
Moreover, the City’s interpretation of the Supreme Court’s use of “State” collapses the specific distinction the Supreme Court has drawn between cities, which are not sovereign entities, and states, which are. Sovereign capacity matters. Indeed, the very origins of *Parker* immunity stem from respect for the states’ sovereign capacity to regulate their economies. *Phoebe Putney*, 568 U.S. at 224. A “substate governmental entity” is simply not equivalent to a state: “Because municipalities and other political subdivisions are not themselves sovereign, state-action immunity under *Parker* does not apply to them directly.” *Phoebe Putney*, 568 U.S. at 225. Unlike a state, a municipality may invoke the protective cloak of *Parker* immunity under “the narrow exception *Hallie* identified” not because it is sovereign, but because there is “little or no danger that it is involved in a private price-fixing arrangement”; the fact that “municipalities are electorally accountable and lack the kind of private incentives characteristic of active participants in the market”; and the “substantially reduc[ed] ... risk that [a municipality] would pursue private interests while regulating any single field.” *Dental Examiners*, 135 S.Ct. at 1112-13 (quoting *Hallie*, 471 U.S. at 47). All of the reasons justifying the *Hallie* exception are eviscerated by the involvement of private parties in this case.

In concluding that the active-supervision requirement is not satisfied in this case, we do not disturb *Hallie*’s well-settled rule that municipal actors need not meet the active-supervision requirement. See *Hallie*, 471 U.S. at 47. Rather, following *Hallie*, we hold that in this case, in which private actors exercise substantial discretion in setting the terms of municipal regulation, “active state supervision must be shown.” Id. at 46 n.10. Because the distinction between states and municipalities is of crucial importance for purposes of state-action immunity, we reject the City’s invitation to treat the two entities interchangeably.

II. The Ordinance Is Not Preempted by the National Labor Relations Act.

We next hold that the Ordinance is not preempted by the NLRA under either *Machinists* or *Garmon* preemption. ***

CONCLUSION

For the foregoing reasons, we reverse the district court’s dismissal of the Chamber’s federal antitrust claims, and remand the federal antitrust claims to the district court for further proceedings.
We also affirm the district court’s dismissal of the Chamber’s NLRA preemption claims.***

NOTES AND QUESTIONS

1. Understanding Uber and Lyft as a business. The Third Circuit dismissed the Section 2 claims in the Philadelphia Taxi Ass’n case pretty quickly. The court said Uber was an entrant adding new competition to the local transportation market and antitrust law generally favors new entry. That said, Uber and Lyft have both lost substantial amounts of money in building up their new services and of course the pandemic has exacerbated their business problems. What facts would you need to have to make an assessment of whether Uber and Lyft have been engaging in predatory pricing? Is it enough to show that they lost money for an extended period of time? Should that fact, if established, be enough to show a predatory intent? And how should we think about recoupment in these markets?

2. Understanding contracts and corporate form. Return to the questions that we posed before the three cases that you just read. What explains how Uber and Lyft are organized? Suppose that Uber and Lyft are organized to avoid having drivers characterized as employees? How should all of that matter for how we see the antitrust issues that may be raised in these situations? Should a court rely on the parties’ characterization of their relationship in the operative documents, or should it make an independent assessment of the economic substance of the relationship?

3. Antitrust and localism. City of Seattle puts in play how choices by local governments matter for possible antitrust liability. Why should federal antitrust law play any role here at all? It is easy to see that the home state might not internalize harms to consumers in other states that result from actions by the home state and that we therefore cannot rely on state or local officials to make good decisions when those decisions have effects in other states. But is antitrust law the best tool to address that problem? Moreover, the situation in City of Seattle is mainly local. If Seattle doesn’t want robust competition in local transportation markets, why is that a federal concern and why should federal antitrust law somehow supply an answer?
European Commission – Press Release

Antitrust: Commission fines Google €4.34 billion for illegal practices regarding Android mobile devices to strengthen dominance of Google’s search engine

Brussels, 18 July 2018

[insert after the discussion of Google/Shopping, at the bottom of p. 1049]

The European Commission has fined Google €4.34 billion for breaching EU antitrust rules. Since 2011, Google has imposed illegal restrictions on Android device manufacturers and mobile network operators to cement its dominant position in general internet search.

Google must now bring the conduct effectively to an end within 90 days or face penalty payments of up to 5% of the average daily worldwide turnover of Alphabet, Google’s parent company.

Commissioner Margrethe Vestager, in charge of competition policy, said: “Today, mobile internet makes up more than half of global internet traffic. It has changed the lives of millions of Europeans. Our case is about three types of restrictions that Google has imposed on Android device manufacturers and network operators to ensure that traffic on Android devices goes to the Google search engine. In this way, Google has used Android as a vehicle to cement the dominance of its search engine. These practices have denied rivals the chance to innovate and compete on the merits. They have denied European consumers the benefits of effective competition in the important mobile sphere. This is illegal under EU antitrust rules.”

In particular, Google:

- has required manufacturers to pre-install the Google Search app and browser app (Chrome), as a condition for licensing Google’s app store (the Play Store);
- made payments to certain large manufacturers and mobile network operators on condition that they exclusively pre-installed the Google Search app on their devices; and
- has prevented manufacturers wishing to pre-install Google apps from selling even a single smart mobile device running on alternative versions of Android that were not approved by Google (so-called “Android forks”).

**Google's strategy and the scope of the Commission investigation**
Google obtains the vast majority of its revenues via its flagship product, the Google search engine. The company understood early on that the shift from desktop PCs to mobile internet, which started in the mid-2000s, would be a fundamental change for Google Search. So, Google developed a strategy to anticipate the effects of this shift, and to make sure that users would continue to use Google Search also on their mobile devices.

In 2005, Google bought the original developer of the Android mobile operating system and has continued to develop Android ever since. Today, about 80% of smart mobile devices in Europe, and worldwide, run on Android.

When Google develops a new version of Android it publishes the source code online. This in principle allows third parties to download and modify this code to create Android forks. The openly accessible Android source code covers basic features of a smart mobile operating system but not Google’s proprietary Android apps and services. Device manufacturers who wish to obtain Google’s proprietary Android apps and services need to enter into contracts with Google, as part of which Google imposes a number of restrictions. Google also entered into contracts and applied some of these restrictions to certain large mobile network operators, who can also determine which apps and services are installed on devices sold to end users.

The Commission decision concerns three specific types of contractual restrictions that Google has imposed on device manufacturers and mobile network operators. These have enabled Google to use Android as a vehicle to cement the dominance of its search engine. In other words, the Commission decision does not question the open source model or the Android operating system as such.

**Google’s dominance**

The Commission decision concludes that Google is dominant in the markets for general internet search services, licensable smart mobile operating systems and app stores for the Android mobile operating system.

**General search services**

Google is dominant in the national markets for general internet search throughout the European Economic Area (EEA), i.e. in all 31 EEA Member States. Google has shares of more than 90% in most EEA Member States. There are high barriers to enter these
markets. This has also been concluded in the Google Shopping decision of June 2017.

Smart mobile operating systems available for licence

Android is a licensable smart mobile operating system. This means that third party manufacturers of smart mobile devices can license and run Android on their devices.

Through its control over Android, Google is dominant in the worldwide market (excluding China) for licensable smart mobile operating systems, with a market share of more than 95%. There are high barriers to entry in part due to network effects: the more users use a smart mobile operating system, the more developers write apps for that system – which in turn attracts more users. Furthermore, significant resources are required to develop a successful licensable smart mobile operating system.

As a licensable operating system, Android is different from operating systems exclusively used by vertically integrated developers (like Apple iOS or Blackberry). Those are not part of the same market because they are not available for licence by third party device manufacturers.

Nevertheless, the Commission investigated to what extent competition for end users (downstream), in particular between Apple and Android devices, could indirectly constrain Google’s market power for the licensing of Android to device manufacturers (upstream). The Commission found that this competition does not sufficiently constrain Google upstream for a number of reasons, including:

- end user purchasing decisions are influenced by a variety of factors (such as hardware features or device brand), which are independent from the mobile operating system;
- Apple devices are typically priced higher than Android devices and may therefore not be accessible to a large part of the Android device user base;
- Android device users face switching costs when switching to Apple devices, such as losing their apps, data and contacts, and having to learn how to use a new operating system; and
- even if end users were to switch from Android to Apple devices, this would have limited impact on Google’s core business. That's because Google Search is set as the default search engine on Apple devices and Apple users are therefore likely to continue using Google Search for their queries.
App stores for the Android mobile operating system

Google is dominant in the worldwide market (excluding China) for app stores for the Android mobile operating system. Google’s app store, the Play Store, accounts for more than 90% of apps downloaded on Android devices. This market is also characterised by high barriers to entry. For similar reasons to those already listed above, Google’s app store dominance is not constrained by Apple’s App Store, which is only available on iOS devices.

Breach of EU antitrust rules

Market dominance is, as such, not illegal under EU antitrust rules. However, dominant companies have a special responsibility not to abuse their powerful market position by restricting competition, either in the market where they are dominant or in separate markets.

Google has engaged in three separate types of practices, which all had the aim of cementing Google’s dominant position in general internet search.

1) Illegal tying of Google’s search and browser apps

Google offers its mobile apps and services to device manufacturers as a bundle, which includes the Google Play Store, the Google Search app and the Google Chrome browser. Google’s licensing conditions make it impossible for manufacturers to pre-install some apps but not others.

As part of the Commission investigation, device manufacturers confirmed that the Play Store is a “must-have” app, as users expect to find it pre-installed on their devices (not least because they cannot lawfully download it themselves).

The Commission decision has concluded that Google has engaged in two instances of illegal tying:

- First, the tying of the Google Search app. As a result, Google has ensured that its Google Search app is pre-installed on practically all Android devices sold in the EEA. Search apps represent an important entry point for search queries on mobile devices. The Commission has found this tying conduct to be illegal as of 2011, which is the date Google became dominant in the market for app stores for the Android mobile operating system.

- Second, the tying of the Google Chrome browser. As a result, Google has ensured that its mobile browser is pre-installed on practically all Android devices sold in the EEA.
Browsers also represent an important entry point for search queries on mobile devices and Google Search is the default search engine on Google Chrome. The Commission found this tying conduct to be illegal as of 2012, which is the date from which Google has included the Chrome browser in its app bundle.

Pre-installation can create a *status quo* bias. Users who find search and browser apps pre-installed on their devices are likely to stick to these apps. For example, the Commission has found evidence that the Google Search app is consistently used more on Android devices, where it is pre-installed, than on Windows Mobile devices, where users must download it. This also shows that users do not download competing apps in numbers that can offset the significant commercial advantage derived through pre-installation. For example, in 2016:

- on **Android** devices (with Google Search and Chrome pre-installed) more than 95% of all search queries were made via Google Search; and

- on **Windows Mobile** devices (Google Search and Chrome are not pre-installed) less than 25% of all search queries were made via Google Search. More than 75% of search queries happened on Microsoft’s Bing search engine, which is pre-installed on Windows Mobile devices.

Google’s practice has therefore reduced the incentives of manufacturers to pre-install competing search and browser apps, as well as the incentives of users to download such apps. This reduced the ability of rivals to compete effectively with Google.

The Commission also assessed in detail Google’s arguments that the tying of the Google Search app and Chrome browser were necessary, in particular to allow Google to monetise its investment in Android, and concluded that these arguments were not well founded. Google achieves billions of dollars in annual revenues with the Google Play Store alone, it collects a lot of data that is valuable to Google’s search and advertising business from Android devices, and it would still have benefitted from a significant stream of revenue from search advertising without the restrictions.

2) *Illegal payments conditional on exclusive pre-installation of Google Search*

Google granted significant financial incentives to some of the largest device manufacturers as well as mobile network operators on
condition that they exclusively pre-installed Google Search across their entire portfolio of Android devices. This harmed competition by significantly reducing their incentives to pre-install competing search apps.

The Commission’s investigation showed that a rival search engine would have been unable to compensate a device manufacturer or mobile network operator for the loss of the revenue share payments from Google and still make profits. That is because, even if the rival search engine was pre-installed on only some devices, they would have to compensate the device manufacturer or mobile network operator for a loss of revenue share from Google across all devices.

In line with the recent EU court ruling in Intel, the Commission has considered, amongst other factors, the conditions under which the incentives were granted, their amount, the share of the market covered by these agreements and their duration.

On this basis, the Commission found Google’s conduct to be illegal between 2011 and 2014. In 2013 (after the Commission started to look into this issue), Google started to gradually lift the requirement. The illegal practice effectively ceased as of 2014.

The Commission also assessed in detail Google’s arguments that the granting of financial incentives for exclusive pre-installation of Google Search across the entire portfolio of Android devices was necessary. In this regard, the Commission dismissed Google’s claim that payments based on exclusivity were necessary to convince device manufacturers and mobile network operators to produce devices for the Android ecosystem.

3) Illegal obstruction of development and distribution of competing Android operating systems

Google has prevented device manufacturers from using any alternative version of Android that was not approved by Google (Android forks). In order to be able to pre-install on their devices Google’s proprietary apps, including the Play Store and Google Search, manufacturers had to commit not to develop or sell even a single device running on an Android fork. The Commission found that this conduct was abusive as of 2011, which is the date Google became dominant in the market for app stores for the Android mobile operating system.

This practice reduced the opportunity for devices running on Android forks to be developed and sold. For example, the Commission has found evidence that Google’s conduct prevented a number of large manufacturers from developing and selling devices based on Amazon’s Android fork called “Fire OS”.

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135
In doing so, Google has also closed off an important channel for competitors to introduce apps and services, in particular general search services, which could be pre-installed on Android forks. Therefore, Google’s conduct has had a direct impact on users, denying them access to further innovation and smart mobile devices based on alternative versions of the Android operating system. In other words, as a result of this practice, it was Google – and not users, app developers and the market – that effectively determined which operating systems could prosper.

The Commission also assessed in detail Google’s arguments that these restrictions were necessary to prevent a “fragmentation” of the Android ecosystem, and concluded that these were not well founded. First, Google could have ensured that Android devices using Google proprietary apps and services were compliant with Google’s technical requirements, without preventing the emergence of Android forks. Second, Google did not provide any credible evidence that Android forks would be affected by technical failures or fail to support apps.

The effects of Google’s illegal practices

The Commission decision concludes that these three types of abuse form part of an overall strategy by Google to cement its dominance in general internet search, at a time when the importance of mobile internet was growing significantly.
First, Google's practices have denied rival search engines the possibility to compete on the merits. The tying practices ensured the pre-installation of Google's search engine and browser on practically all Google Android devices and the exclusivity payments strongly reduced the incentive to pre-install competing search engines. Google also obstructed the development of Android forks, which could have provided a platform for rival search engines to gain traffic. Google's strategy has also prevented rival search engines from collecting more data from smart mobile devices, including search and mobile location data, which helped Google to cement its dominance as a search engine.

Furthermore, Google’s practices also harmed competition and further innovation in the wider mobile space, beyond just internet search. That’s because they prevented other mobile browsers from competing effectively with the pre-installed Google Chrome browser. Finally, Google obstructed the development of Android forks, which could have provided a platform also for other app developers to thrive.

Consequences of the decision

The Commission’s fine of €4,342,865,000 takes account of the duration and gravity of the infringement. In accordance with the Commission’s 2006 Guidelines on fines (see press release and MEMO), the fine has been calculated on the basis of the value of Google’s revenue from search advertising services on Android devices in the EEA.

The Commission decision requires Google to bring its illegal conduct to an end in an effective manner within 90 days of the decision.

At a minimum, Google has to stop and to not re-engage in any of the three types of practices. The decision also requires Google to refrain from any measure that has the same or an equivalent object or effect as these practices.

The decision does not prevent Google from putting in place a reasonable, fair and objective system to ensure the correct functioning of Android devices using Google proprietary apps and services, without however affecting device manufacturers’ freedom to produce devices based on Android forks.

It is Google’s sole responsibility to ensure compliance with the Commission decision. The Commission will monitor Google’s compliance closely and Google is under an obligation to keep the Commission informed of how it will comply with its obligations.

If Google fails to ensure compliance with the Commission decision, it would be liable for non-compliance payments of up to 5% of
the average daily worldwide turnover of Alphabet, Google’s parent company. The Commission would have to determine such non-compliance in a separate decision, with any payment backdated to when the non-compliance started.

Finally, Google is also liable to face civil actions for damages that can be brought before the courts of the Member States by any person or business affected by its anti-competitive behaviour. The new EU Antitrust Damages Directive makes it easier for victims of anti-competitive practices to obtain damages.

Other Google cases

In June 2017, the Commission fined Google €2.42 billion for abusing its dominance as a search engine by giving an illegal advantage to Google’s own comparison shopping service. The Commission is currently actively monitoring Google’s compliance with that decision.

The Commission also continues to investigate restrictions that Google has placed on the ability of certain third party websites to display search advertisements from Google’s competitors (the AdSense case). In July 2016, the Commission came to the preliminary conclusion that Google has abused its dominant position in a case concerning AdSense.

Background

Today’s decision is addressed to Google LLC (previously Google Inc.) and Alphabet Inc., Google’s parent company. The Commission opened proceedings concerning Google’s conduct as regards the Android operating system and applications in April 2015 and sent a Statement of Objections to Google in April 2016.

Article 102 of the Treaty on the Functioning of the European Union (TFEU) and Article 54 of the EEA Agreement prohibit abuse of a dominant position.

More information on this investigation is available on the Commission’s competition website, in the public case register under the case number 40099.

NOTES AND QUESTIONS

1. In the beginning. Be sure to step back and consider the posture that Google was in when it decided to move into the smartphone operating system market by buying Android in mid-2005. In 2007, based on worldwide sales, Nokia’s Symbian operating system had 63.5% of the market; Microsoft Windows Mobile, 12%; and RIM’s
Blackberry, 9.6%. Apple introduced the iPhone in January 2007 to rave reviews, but you couldn’t buy it until later that year. Microsoft was not in the handset market but instead was trying to replicate the strategy it had used to enormous success in the PC market. That meant selling software for a fee and getting handset markets to adopt it. We know, after the fact of course, that the iPhone would transform the smartphone market. Apple, as it had with the Macintosh, was vertically integrated: Apple hardware combined with Apple software and both of those were available only through Apple. What strategy would you have advised Google to try? Vertically integrate? Charge a fee for the smartphone OS software as Microsoft was doing? How would you describe Google’s strategy and why did they adopt it?

2. Consumers speak. What do you make of the fact that the combination of the introduction of the iPhone and then Android-based smartphones completely displaced the positions of the preexisting sophisticated phone makers? Said, again, Nokia, Microsoft and RIM were pushed to the side by Apple and the ecosystem that Google created. Did that happen through anti-competitive behavior? If so, when did that anti-competitive behavior begin?

3. Defining markets. The EC excluded Apple from the relevant market because it defined the market in issue as that for licensable smartphone OSs and Apple doesn’t license iOS separately. Is that the right approach? Might competition between the iPhone and Android phones constrain Google’s ability to increase prices to firms licensing Android?

4. Dominance and contractual practices. The EC might concede that Google’s entry into smartphones was procompetitive. The actual Android decision—and recall, as this supplement went to press we have available only the press release set out above—focused on how Google behaved once it achieved a dominant position in the market for licensable smartphone OSs. The Google Play store had become dominant, and the EC found that Google was tying various search software to Google Play. Given the EC decision, how should Google have changed its practices once it had achieved a dominant position in the market? Should Google have revisited its decision to not charge a fee for licensing Android? Should it do so now? If Google had (or now does) move to charging a fee, how would that change competition in the smartphone OS market and the search market? In that regard, it is worth noting that Google is reported to pay Apple a substantial amount of money to get its search software preinstalled on the iPhone.

5. The choice screen. The EC ruling required Google to implement a remedy, and on August 2, 2019, Google announced that it would be
incorporating a choice screen into Android. The simple version of that idea is that a user of a new Android phone would be presented with a list of search engines the first time the user went to run a search. The user could then designate any one of the listed search engines as the default search engine going forward. (This should sound very much like the browser choice screen that was implemented in Europe to settle the browser case brought by the Commission against Microsoft.) The idea behind the choice screen is simple enough, though the next question is how to populate the list of presented search engines and choose a sequence for the listing. Exactly how that was done has changed during the last two years, moving from an auction model to one in which different search engines are listed for free. As to the possible efficacy of this type of remedy, visit statcounter.com and run a few searches on Europe and the United States to see what search engines get used on mobile devices.

Additional European Developments

1. **Google AdSense fine.** On March 20, 2019, the European Commission issued its third fine against Google, this time in the amount of €1.49 billion for what the commission found to be abusive practices in online advertising. The core of the violation was Google's contracting practices in connection with its AdSense product. In 2006, Google had inserted certain exclusivity clauses in its contracts for search advertising. While those clauses evolved over time, Google continued to use contracts to limit the ability of firms to compete with Google's advertising product.

2. **Amazon investigation.** On July 17, 2019, the European Commission announced that it had opened an investigation into Amazon:

   The European Commission has opened a formal antitrust investigation to assess whether Amazon’s use of sensitive data from independent retailers who sell on its marketplace is in breach of EU competition rules.

   Commissioner Margrethe Vestager, in charge of competition policy, said: “European consumers are increasingly shopping online. E-commerce has boosted retail competition and brought more choice and better prices. We need to ensure that large online platforms don’t eliminate these benefits through anti-competitive behaviour. I have therefore decided to take a very close look at Amazon’s business practices and its dual role as marketplace and retailer, to assess its compliance with EU competition rules.”
Amazon has a dual role as a platform: (i) it sells products on its website as a retailer; and (ii) it provides a marketplace where independent sellers can sell products directly to consumers.

When providing a marketplace for independent sellers, Amazon continuously collects data about the activity on its platform. Based on the Commission’s preliminary fact-finding, Amazon appears to use competitively sensitive information – about marketplace sellers, their products and transactions on the marketplace.

As part of its in-depth investigation the Commission will look into:

- the standard agreements between Amazon and marketplace sellers, which allow Amazon’s retail business to analyse and use third party seller data. In particular, the Commission will focus on whether and how the use of accumulated marketplace seller data by Amazon as a retailer affects competition.
- the role of data in the selection of the winners of the “Buy Box” and the impact of Amazon’s potential use of competitively sensitive marketplace seller information on that selection. The “Buy Box” is displayed prominently on Amazon and allows customers to add items from a specific retailer directly into their shopping carts. Winning the “Buy Box” seems key for marketplace sellers as a vast majority of transactions are done through it.

If proven, the practices under investigation may breach EU competition rules on anticompetitive agreements between companies (Article 101 of the Treaty on the Functioning of the European Union (TFEU)) and/or on the abuse of a dominant position (Articles 102 TFEU).

The Commission will now carry out its in-depth investigation as a matter of priority. The opening of a formal investigation does not prejudge its outcome.

3. Apple investigations. On June 16, 2020, the European Commission announced that it had opened two investigations into Apple’s practices. One related to how Apple runs the App Store. The Commission had received two complaints regarding the App Store rules, one from Spotify on March 11, 2019 and the second from an unnamed e-book and audiobook distributor on March 5, 2020. Based on those complaints, the Commission is investigating Apple’s requirement that app developers use Apple’s in-app purchase system
for sales within an app (including a 30% royalty rate to Apple for subscription fees). The Commission is also looking at allegations that Apple restricts the ability of app providers to inform customers from within the app of ways of purchasing books and more outside of the app.

The second investigation is looking at claims that Apple is limiting competition in payments markets in restricting access to functionality on iOS devices. The technology in question is the built-in near field communication (NFC) technology that makes possible tap-and-go payments at stores. The Commission is concerned about the possibility that in restricting access to that technology to the benefit of Apple Pay Apple is distorting competition in the digital wallets market.

Chapter 10: Institutional Framework

**Apple Inc. v. Pepper**

Supreme Court of the United States, 2019.

U.S. _, 139 S.Ct. 1514.

[replace Kansas v. Utilicorp United, Inc. at pp. 1181-1192]

Justice KAVANAUGH delivered the opinion of the Court: In 2007, Apple started selling iPhones. The next year, Apple launched the retail App Store, an electronic store where iPhone owners can purchase iPhone applications from Apple. Those “apps” enable iPhone owners to send messages, take photos, watch videos, buy clothes, order food, arrange transportation, purchase concert tickets, donate to charities, and the list goes on. “There’s an app for that” has become part of the 21st-century American lexicon.

In this case, however, several consumers contend that Apple charges too much for apps. The consumers argue, in particular, that Apple has monopolized the retail market for the sale of apps and has unlawfully used its monopolistic power to charge consumers higher-than-competitive prices.

A claim that a monopolistic retailer (here, Apple) has used its monopoly to overcharge consumers is a classic antitrust claim. But Apple asserts that the consumer-plaintiffs in this case may not sue Apple because they supposedly were not “direct purchasers” from Apple under our decision in *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 745-746 (1977). We disagree. The plaintiffs purchased apps directly from Apple and therefore are direct purchasers under *Illinois Brick*. At this early pleadings stage of the litigation, we do not assess the
merits of the plaintiffs’ antitrust claims against Apple, nor do we consider any other defenses Apple might have. We merely hold that the Illinois Brick direct-purchaser rule does not bar these plaintiffs from suing Apple under the antitrust laws. We affirm the judgment of the U.S. Court of Appeals for the Ninth Circuit.

In 2007, Apple began selling iPhones. In July 2008, Apple started the App Store. The App Store now contains about 2 million apps that iPhone owners can download. By contract and through technological limitations, the App Store is the only place where iPhone owners may lawfully buy apps.

For the most part, Apple does not itself create apps. Rather, independent app developers create apps. Those independent app developers then contract with Apple to make the apps available to iPhone owners in the App Store.

Through the App Store, Apple sells the apps directly to iPhone owners. To sell an app in the App Store, app developers must pay Apple a $99 annual membership fee. Apple requires that the retail sales price end in $0.99, but otherwise allows the app developers to set the retail price. Apple keeps 30 percent of the sales price, no matter what the sales price might be. In other words, Apple pockets a 30 percent commission on every app sale.

In 2011, four iPhone owners sued Apple. They allege that Apple has unlawfully monopolized “the iPhone apps aftermarket.” App. to Pet. for Cert. 53a. The plaintiffs allege that, via the App Store, Apple locks iPhone owners “into buying apps only from Apple and paying Apple’s 30% fee, even if the iPhone owners wish ‘to buy apps elsewhere or pay less.’” Id., at 45a. According to the complaint, that 30 percent commission is “pure profit” for Apple and, in a competitive environment with other retailers, “Apple would be under considerable pressure to substantially lower its 30% profit margin.” Id., at 54a-55a. The plaintiffs allege that in a competitive market, they would be able to “choose between Apple’s high-priced App Store and less costly alternatives.” Id., at 55a. And they allege that they have “paid more for their iPhone apps than they would have paid in a competitive market.” Id., at 53a.

Apple moved to dismiss the complaint, arguing that the iPhone owners were not direct purchasers from Apple and therefore may not sue. In Illinois Brick, this Court held that direct purchasers may sue antitrust violators, but also ruled that indirect purchasers may not sue. The District Court agreed with Apple and dismissed the complaint. According to the District Court, the iPhone owners were not
direct purchasers from Apple because the app developers, not Apple, set the consumers’ purchase price.

The Ninth Circuit reversed. The Ninth Circuit concluded that the iPhone owners were direct purchasers under Illinois Brick because the iPhone owners purchased apps directly from Apple. According to the Ninth Circuit, Illinois Brick means that a consumer may not sue an alleged monopolist who is two or more steps removed from the consumer in a vertical distribution chain. See In re Apple iPhone Antitrust Litig., 846 F. 3d 313, 323 (2017). Here, however, the consumers purchased directly from Apple, the alleged monopolist. Therefore, the Ninth Circuit held that the iPhone owners could sue Apple for allegedly monopolizing the sale of iPhone apps and charging higher-than-competitive prices. Id., at 324. We granted certiorari. 585 U.S. ___ (2018).

II

A

The plaintiffs’ allegations boil down to one straightforward claim: that Apple exercises monopoly power in the retail market for the sale of apps and has unlawfully used its monopoly power to force iPhone owners to pay Apple higher-than-competitive prices for apps. According to the plaintiffs, when iPhone owners want to purchase an app, they have only two options: (1) buy the app from Apple’s App Store at a higher-than-competitive price or (2) do not buy the app at all. Any iPhone owners who are dissatisfied with the selection of apps available in the App Store or with the price of the apps available in the App Store are out of luck, or so the plaintiffs allege.

The sole question presented at this early stage of the case is whether these consumers are proper plaintiffs for this kind of antitrust suit—in particular, our precedents ask, whether the consumers were “direct purchasers” from Apple. Illinois Brick, 431 U.S. at 745-746. It is undisputed that the iPhone owners bought the apps directly from Apple. Therefore, under Illinois Brick, the iPhone owners were direct purchasers who may sue Apple for alleged monopolization.

That straightforward conclusion follows from the text of the antitrust laws and from our precedents.

First is text: Section 2 of the Sherman Act makes it unlawful for any person to “monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations.” 26 Stat. 209, 15 U.S.C. § 2. Section 4 of the Clayton Act in turn provides that “any person who shall be injured in his business or
property by reason of anything forbidden in the antitrust laws may sue... the defendant... and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney’s fee.” 38 Stat. 731, 15 U.S.C. § 15(a) (emphasis added). The broad text of § 4—“any person” who has been “injured” by an antitrust violator may sue—readily covers consumers who purchase goods or services at higher-than-competitive prices from an allegedly monopolistic retailer.

Second is precedent: Applying § 4, we have consistently stated that “the immediate buyers from the alleged antitrust violators” may maintain a suit against the antitrust violators. Kansas v. UtiliCorp United Inc., 497 U.S. 199, 207 (1990); see also Illinois Brick, 431 U.S. at 745-746. At the same time, incorporating principles of proximate cause into § 4, we have ruled that indirect purchasers who are two or more steps removed from the violator in a distribution chain may not sue. Our decision in Illinois Brick established a bright-line rule that authorizes suits by direct purchasers but bars suits by indirect purchasers. Ibid., at 746.

The facts of Illinois Brick illustrate the rule. Illinois Brick Company manufactured and distributed concrete blocks. Illinois Brick sold the blocks primarily to masonry contractors, and those contractors in turn sold masonry structures to general contractors. Those general contractors in turn sold their services for larger construction projects to the State of Illinois, the ultimate consumer of the blocks.

The consumer State of Illinois sued the manufacturer Illinois Brick. The State alleged that Illinois Brick had engaged in a conspiracy to fix the price of concrete blocks. According to the complaint, the State paid more for the concrete blocks than it would have paid absent the pricefixing conspiracy. The monopoly overcharge allegedly flowed all the way down the distribution chain to the ultimate consumer, who was the State of Illinois.

This Court ruled that the State could not bring an antitrust action against Illinois Brick, the alleged violator, because the State had not purchased concrete blocks directly from Illinois Brick. The proper plaintiff to bring that claim against Illinois Brick, the Court stated, would be an entity that had purchased directly from Illinois Brick. Ibid.

The bright-line rule of Illinois Brick, as articulated in that case and as we reiterated in UtiliCorp, means that indirect purchasers who are two or more steps removed from the antitrust violator in a distribution chain may not sue. By contrast, direct purchasers—that
is, those who are “the immediate buyers from the alleged antitrust violators”—may sue. *UtiliCorp*, 497 U.S. at 207.

For example, if manufacturer A sells to retailer B, and retailer B sells to consumer C, then C may not sue A. But B may sue A if A is an antitrust violator. And C may sue B if B is an antitrust violator. That is the straightforward rule of *Illinois Brick*. See *Loeb Industries, Inc. v. Sumitomo Corp.*, 306 F.3d 469, 481-482 (C.A.7 2002) (Wood, J).

In this case, unlike in *Illinois Brick*, the iPhone owners are not consumers at the bottom of a vertical distribution chain who are attempting to sue manufacturers at the top of the chain. There is no intermediary in the distribution chain between Apple and the consumer. The iPhone owners purchase apps directly from the retailer Apple, who is the alleged antitrust violator. The iPhone owners pay the alleged overcharge directly to Apple. The absence of an intermediary is dispositive. Under *Illinois Brick*, the iPhone owners are direct purchasers from Apple and are proper plaintiffs to maintain this antitrust suit.

B

All of that seems simple enough. But Apple argues strenuously against that seemingly simple conclusion, and we address its arguments carefully. For this kind of retailer case, Apple’s theory is that *Illinois Brick* allows consumers to sue only the party who sets the retail price, whether or not that party sells the good or service directly to the complaining party. Apple says that its theory accords with the economics of the transaction. Here, Apple argues that the app developers, not Apple, set the retail price charged to consumers, which according to Apple means that the consumers may not sue Apple.

We see three main problems with Apple’s “who sets the price” theory.

First, Apple’s theory contradicts statutory text and precedent. As we explained above, the text of § 4 broadly affords injured parties a right to sue under the antitrust laws. And our precedent in *Illinois Brick* established a bright-line rule where direct purchasers such as the consumers here may sue antitrust violators from whom they purchased a good or service. *Illinois Brick*, as we read the opinion, was not based on an economic theory about who set the price. Rather, *Illinois Brick* sought to ensure an effective and efficient litigation scheme in antitrust cases. To do so, the Court drew a bright line that allowed direct purchasers to sue but barred indirect purchasers from suing. When there is no intermediary between the purchaser and the antitrust violator, the purchaser may sue. *** Apple’s theory would
require us to rewrite the rationale of *Illinois Brick* and to gut the longstanding bright-line rule.

To the extent that *Illinois Brick* leaves any ambiguity about whether a direct purchaser may sue an antitrust violator, we should resolve that ambiguity in the direction of the statutory text. And under the text, direct purchasers from monopolistic retailers are proper plaintiffs to sue those retailers.

*Second,* in addition to deviating from statutory text and precedent, Apple’s proposed rule is not persuasive economically or legally. Apple’s effort to transform *Illinois Brick* from a direct-purchaser rule to a “who sets the price” rule would draw an arbitrary and unprincipled line among retailers based on retailers’ financial arrangements with their manufacturers or suppliers.

In the retail context, the price charged by a retailer to a consumer is often a result (at least in part) of the price charged by the manufacturer or supplier to the retailer, or of negotiations between the manufacturer or supplier and the retailer. Those agreements between manufacturer or supplier and retailer may take myriad forms, including for example a markup pricing model or a commission pricing model. In a traditional markup pricing model, a hypothetical monopolistic retailer might pay $6 to the manufacturer and then sell the product for $10, keeping $4 for itself. In a commission pricing model, the retailer might pay nothing to the manufacturer; agree with the manufacturer that the retailer will sell the product for $10 and keep 40 percent of the sales price; and then sell the product for $10, send $6 back to the manufacturer, and keep $4. In those two different pricing scenarios, everything turns out to be economically the same for the manufacturer, retailer, and consumer.

Yet Apple’s proposed rule would allow a consumer to sue the monopolistic retailer in the former situation but not the latter. In other words, under Apple’s rule a consumer could sue a monopolistic retailer when the retailer set the retail price by marking up the price it had paid the manufacturer or supplier for the good or service. But a consumer could not sue a monopolistic retailer when the manufacturer or supplier set the retail price and the retailer took a commission on each sale.

Apple’s line-drawing does not make a lot of sense, other than as a way to gerrymander Apple out of this and similar lawsuits. In particular, we fail to see why the form of the upstream arrangement between the manufacturer or supplier and the retailer should determine whether a monopolistic retailer can be sued by a downstream consumer who has purchased a good or service directly
from the retailer and has paid a higher-than-competitive price because of the retailer’s unlawful monopolistic conduct. As the Court of Appeals aptly stated, “the distinction between a markup and a commission is immaterial.” 846 F. 3d at 324. *** If a retailer has engaged in unlawful monopolistic conduct that has caused consumers to pay higher-than-competitive prices, it does not matter how the retailer structured its relationship with an upstream manufacturer or supplier—whether, for example, the retailer employed a markup or kept a commission.

To be sure, if the monopolistic retailer’s conduct has not caused the consumer to pay a higher-than-competitive price, then the plaintiff’s damages will be zero. Here, for example, if the competitive commission rate were 10 percent rather than 30 percent but Apple could prove that app developers in a 10 percent commission system would always set a higher price such that consumers would pay the same retail price regardless of whether Apple’s commission was 10 percent or 30 percent, then the consumers’ damages would presumably be zero. But we cannot assume in all cases—as Apple would necessarily have us do—that a monopolistic retailer who keeps a commission does not ever cause the consumer to pay a higher-than-competitive price. We find no persuasive legal or economic basis for such a blanket assertion.

In short, we do not understand the relevance of the upstream market structure in deciding whether a downstream consumer may sue a monopolistic retailer. Apple’s rule would elevate form (what is the precise arrangement between manufacturers or suppliers and retailers?) over substance (is the consumer paying a higher price because of the monopolistic retailer’s actions?). If the retailer’s unlawful monopolistic conduct caused a consumer to pay the retailer a higher-than-competitive price, the consumer is entitled to sue the retailer under the antitrust laws.

Third, if accepted, Apple’s theory would provide a roadmap for monopolistic retailers to structure transactions with manufacturers or suppliers so as to evade antitrust claims by consumers and thereby thwart effective antitrust enforcement.

Consider a traditional supplier-retailer relationship, in which the retailer purchases a product from the supplier and sells the product with a markup to consumers. Under Apple’s proposed rule, a retailer, instead of buying the product from the supplier, could arrange to sell the product for the supplier without purchasing it from the supplier. In other words, rather than paying the supplier a certain price for the product and then marking up the price to sell the product
to consumers, the retailer could collect the price of the product from consumers and remit only a fraction of that price to the supplier.

That restructuring would allow a monopolistic retailer to insulate itself from antitrust suits by consumers, even in situations where a monopolistic retailer is using its monopoly to charge higher-than-competitive prices to consumers. We decline to green-light monopolistic retailers to exploit their market position in that way. We refuse to rubber-stamp such a blatant evasion of statutory text and judicial precedent.

In sum, Apple’s theory would disregard statutory text and precedent, create an unprincipled and economically senseless distinction among monopolistic retailers, and furnish monopolistic retailers with a how-to guide for evasion of the antitrust laws.

C

In arguing that the Court should transform the direct-purchaser rule into a “who sets the price” rule, Apple insists that the three reasons that the Court identified in Illinois Brick for adopting the direct-purchaser rule apply to this case—even though the consumers here (unlike in Illinois Brick) were direct purchasers from the alleged monopolist. The Illinois Brick Court listed three reasons for barring indirect-purchaser suits: (1) facilitating more effective enforcement of antitrust laws; (2) avoiding complicated damages calculations; and (3) eliminating duplicative damages against antitrust defendants.

As we said in UtiliCorp, however, the bright-line rule of Illinois Brick means that there is no reason to ask whether the rationales of Illinois Brick “apply with equal force” in every individual case. 497 U.S. at 216. We should not engage in “an unwarranted and counterproductive exercise to litigate a series of exceptions.” Id., at 217.

But even if we engage with this argument, we conclude that the three Illinois Brick rationales—whether considered individually or together—cut strongly in the plaintiffs’ favor here, not Apple’s.

First, Apple argues that barring the iPhone owners from suing Apple will better promote effective enforcement of the antitrust laws. Apple posits that allowing only the upstream app developers—and not the downstream consumers—to sue Apple would mean more effective enforcement of the antitrust laws. We do not agree. Leaving consumers at the mercy of monopolistic retailers simply because upstream suppliers could also sue the retailers makes little sense and would
directly contradict the longstanding goal of effective private enforcement and consumer protection in antitrust cases.

Second, Apple warns that calculating the damages in successful consumer antitrust suits against monopolistic retailers might be complicated. It is true that it may be hard to determine what the retailer would have charged in a competitive market. Expert testimony will often be necessary. But that is hardly unusual in antitrust cases. \textit{Illinois Brick} is not a get-out-of-court-free card for monopolistic retailers to play any time that a damages calculation might be complicated. \textit{Illinois Brick} surely did not wipe out consumer antitrust suits against monopolistic retailers from whom the consumers purchased goods or services at higher-than-competitive prices. Moreover, the damages calculation may be just as complicated in a retailer markup case as it is in a retailer commission case. Yet Apple apparently accepts consumers suing monopolistic retailers in a retailer markup case. If Apple accepts that kind of suit, then Apple should also accept consumers suing monopolistic retailers in a retailer commission case.

Third, Apple claims that allowing consumers to sue will result in “conflicting claims to a common fund—the amount of the alleged overcharge.” \textit{Illinois Brick}, 431 U.S. at 737. Apple is incorrect. This is not a case where multiple parties at different levels of a distribution chain are trying to all recover the same passed-through overcharge initially levied by the manufacturer at the top of the chain. If the iPhone owners prevail, they will be entitled to the \textit{full amount} of the unlawful overcharge that they paid to Apple. The overcharge has not been passed on by anyone to anyone. Unlike in \textit{Illinois Brick}, there will be no need to “trace the effect of the overcharge through each step in the distribution chain.” 431 U.S. at 741.

It is true that Apple’s alleged anticompetitive conduct may leave Apple subject to multiple suits by different plaintiffs. But \textit{Illinois Brick} did not purport to bar multiple liability that is unrelated to passing an overcharge down a chain of distribution. *** Multiple suits are not atypical when the intermediary in a distribution chain is a bottleneck monopolist or monopsonist (or both) between the manufacturer on the one end and the consumer on the other end. A retailer who is both a monopolist and a monopsonist may be liable to different classes of plaintiffs—both to downstream consumers and to upstream suppliers—when the retailer’s unlawful conduct affects both the downstream and upstream markets.

Here, some downstream iPhone consumers have sued Apple on a monopoly theory. And it could be that some upstream app developers
will also sue Apple on a monopsony theory. In this instance, the two suits would rely on fundamentally different theories of harm and would not assert dueling claims to a “common fund,” as that term was used in *Illinois Brick*. The consumers seek damages based on the difference between the price they paid and the competitive price. The app developers would seek lost profits that they could have earned in a competitive retail market. *Illinois Brick* does not bar either category of suit.

In short, the three *Illinois Brick* rationales do not persuade us to remake *Illinois Brick* and to bar direct-purchaser suits against monopolistic retailers who employ commissions rather than markups. The plaintiffs seek to hold retailers to account if the retailers engage in unlawful anticompetitive conduct that harms consumers who purchase from those retailers. That is why we have antitrust law.

***

*** The consumers here purchased apps directly from Apple, and they allege that Apple used its monopoly power over the retail apps market to charge higher-than-competitive prices. Our decision in *Illinois Brick* does not bar the consumers from suing Apple for Apple’s allegedly monopolistic conduct. We affirm the judgment of the U.S. Court of Appeals for the Ninth Circuit.

*It is so ordered.*

Justice GORSUCH, with whom THE CHIEF JUSTICE, Justice THOMAS, and Justice ALITO join, dissenting: More than 40 years ago, in *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), this Court held that an antitrust plaintiff can’t sue a defendant for overcharging someone else who might (or might not) have passed on all (or some) of the overcharge to him. *Illinois Brick* held that these convoluted “pass on” theories of damages violate traditional principles of proximate causation and that the right plaintiff to bring suit is the one on whom the overcharge immediately and surely fell. Yet today the Court lets a pass-on case proceed. It does so by recasting *Illinois Brick* as a rule forbidding only suits where the plaintiff does not contract directly with the defendant. This replaces a rule of proximate cause and economic reality with an easily manipulated and formalistic rule of contractual privity. That’s not how antitrust law is supposed to work, and it’s an uncharitable way of treating a precedent which—whatever its flaws—is far more sensible than the rule the Court installs in its place.

II
*** The lawsuit before us depends on just the sort of pass-on theory that *Illinois Brick* forbids. The plaintiffs bought apps from third-party app developers (or manufacturers) in Apple’s retail Internet App Store, at prices set by the developers. The lawsuit alleges that Apple is a monopolist retailer and that the 30% commission it charges developers for the right to sell through its platform represents an anticompetitive price. The problem is that the 30% commission falls initially on the developers. So if the commission is in fact a monopolistic overcharge, the developers are the parties who are directly injured by it. Plaintiffs can be injured only if the developers are able and choose to pass on the overcharge to them in the form of higher app prices that the developers alone control. Plaintiffs admitted as much in the district court, where they described their theory of injury this way: “[I]f Apple tells the developer ... we’re going to take this 30 percent commission ... what’s the developer going to do? The developer is going to increase its price to cover Apple’s... demanded profit.” App. 143.

Because this is exactly the kind of “pass-on theory” *Illinois Brick* rejected, it should come as no surprise that the concerns animating that decision are also implicated. Like other pass-on theories, plaintiffs’ theory will necessitate a complex inquiry into how Apple’s conduct affected third-party pricing decisions. And it will raise difficult questions about apportionment of damages between app developers and their customers, along with the risk of duplicative damages awards. If anything, plaintiffs’ claims present these difficulties even more starkly than did the claims at issue in *Illinois Brick*.

Consider first the question of causation. To determine if Apple’s conduct damaged plaintiffs at all (and if so, the magnitude of their damages), a court will first have to explore whether and to what extent each individual app developer was able—and then opted—to pass on the 30% commission to its consumers in the form of higher app prices. Sorting this out, if it can be done at all, will entail wrestling with “complicated theories” about “how the relevant market variables would have behaved had there been no overcharge.” *Illinois Brick*, 431 U.S. at 741-743. Will the court hear testimony to determine the market power of each app developer, how each set its prices, and what it might have charged consumers for apps if Apple’s commission had been lower? Will the court also consider expert testimony analyzing how market factors might have influenced developers’ capacity and willingness to pass on Apple’s alleged monopoly overcharge? And will the court then somehow extrapolate its findings to all of the tens of
thousands of developers who sold apps through the App Store at different prices and times over the course of years?

This causation inquiry will be complicated further by Apple’s requirement that all app prices end in $0.99. As plaintiffs acknowledge, this rule has caused prices for the “vast majority” of apps to “cluster” at exactly $0.99. Brief for Respondents 44. And a developer charging $0.99 for its app can’t raise its price by just enough to recover the 30-cent commission. Instead, if the developer wants to pass on the commission to consumers, it has to more than double its price to $1.99 (doubling the commission in the process), which could significantly affect its sales. In short, because Apple’s 99-cent rule creates a strong disincentive for developers to raise their prices, it makes plaintiffs’ pass-on theory of injury even harder to prove. Yet the court will have to consider all of this when determining what damages, if any, plaintiffs suffered as a result of Apple’s allegedly excessive 30% commission.

Plaintiffs’ claims will also necessitate “massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge,” including both consumers and app developers. *Illinois Brick*, 431 U.S. at 737. If, as plaintiffs contend, Apple’s 30% commission is a monopolistic overcharge, then the app developers have a claim against Apple to recover whatever portion of the commission they did not pass on to consumers. *** So courts will have to divvy up the commissions Apple collected between the developers and the consumers. To do that, they’ll have to figure out which party bore what portion of the overcharge in every purchase. And if the developers bring suit separately from the consumers, Apple might be at risk of duplicative damages awards totaling more than the full amount it collected in commissions. To avoid that possibility, it may turn out that the developers are necessary parties who will have to be joined in the plaintiffs’ lawsuit. See Fed. Rule Civ. Proc. 19(a)(1)(B).

III

The United States and its antitrust regulators agree with all of this, so how does the Court reach such a different conclusion? Seizing on *Illinois Brick*’s use of the shorthand phrase “direct purchasers” to describe the parties immediately injured by the monopoly overcharge in that case, the Court (re)characterizes *Illinois Brick* as a rule that anyone who purchases goods directly from an alleged antitrust violator can sue, while anyone who doesn’t, can’t. Under this revisionist version of *Illinois Brick*, the dispositive question becomes whether an
“intermediary in the distribution chain” stands between the plaintiff and the defendant. And because the plaintiff app purchasers in this case happen to have purchased apps directly from Apple, the Court reasons, they may sue.

This exalts form over substance. Instead of focusing on the traditional proximate cause question where the alleged overcharge is first (and thus surely) felt, the Court’s test turns on who happens to be in privity of contract with whom. *** To evade the Court’s test, all Apple must do is amend its contracts. Instead of collecting payments for apps sold in the App Store and remitting the balance (less its commission) to developers, Apple can simply specify that consumers’ payments will flow the other way: directly to the developers, who will then remit commissions to Apple. No antitrust reason exists to treat these contractual arrangements differently, and doing so will only induce firms to abandon their preferred—and presumably more efficient—distribution arrangements in favor of less efficient ones, all so they might avoid an arbitrary legal rule.

Nor does Illinois Brick come close to endorsing such a blind formalism. Yes, as the Court notes, the plaintiff in Illinois Brick did contract directly with an intermediary rather than with the putative antitrust violator. But Illinois Brick’s rejection of pass-on claims, and its explanation of the difficulties those claims present, had nothing to do with privity of contract. Instead and as we have seen, its rule and reasoning grew from the “general tendency of the law ... not to go beyond” the party that first felt the sting of the alleged overcharge, and from the complications that can arise when courts attempt to discern whether and to what degree damages were passed on to others. The Court today risks replacing a cogent rule about proximate cause with a pointless and easily evaded imposter. We do not usually read our own precedents so uncharitably.

Maybe the Court proceeds as it does today because it just disagrees with Illinois Brick. After all, the Court not only displaces a sensible rule in favor of a senseless one; it also proceeds to question each of Illinois Brick’s rationales—doubting that those directly injured are always the best plaintiffs to bring suit, that calculating damages for pass-on plaintiffs will often be unduly complicated, and that conflicting claims to a common fund justify limiting who may sue. Court even tells us that any “ambiguity” about the permissibility of pass-on damages should be resolved “in the direction of the statutory text,” ignoring that Illinois Brick followed the well-trodden path of construing the statutory text in light of background common law principles of proximate cause. Last but not least, the Court suggests
that the traditional understanding of *Illinois Brick* leads to “arbitrary and unprincipled” results. It asks us to consider two hypothetical scenarios that, it says, prove the point. The first is a “markup” scenario in which a monopolistic retailer buys a product from a manufacturer for $6 and then decides to sell the product to a consumer for $10, applying a supracompetitive $4 markup. The second is a “commission” scenario in which a manufacturer directs a monopolistic retailer to sell the manufacturer’s product to a consumer for $10 and the retailer keeps a supracompetitive 40% commission, sending $6 back to the manufacturer. The two scenarios are economically the same, the Court asserts, and forbidding recovery in the second for lack of proximate cause makes no sense.

But there is nothing arbitrary or unprincipled about *Illinois Brick*’s rule or results. The notion that the causal chain must stop somewhere is an ancient and venerable one. As with most any rule of proximate cause, reasonable people can debate whether *Illinois Brick* drew exactly the right line in cutting off claims where it did. But the line it drew is intelligible, principled, administrable, and far more reasonable than the Court’s artificial rule of contractual privity. Nor do the Court’s hypotheticals come close to proving otherwise. In the first scenario, the markup falls initially on the consumer, so there’s no doubt that the retailer’s anticompetitive conduct proximately caused the consumer’s injury. Meanwhile, in the second scenario the commission falls initially on the manufacturer, and the consumer won’t feel the pain unless the manufacturer can and does recoup some or all of the elevated commission by raising its own prices. In that situation, the manufacturer is the directly injured party, and the difficulty of disaggregating damages between those directly and indirectly harmed means that the consumer can’t establish proximate cause under traditional principles.

*** Without any invitation or reason to revisit our precedent, and with so many grounds for caution, I would have thought the proper course today would have been to afford *Illinois Brick* full effect, not to begin whittling it away to a bare formalism. I respectfully dissent.

NOTES AND QUESTIONS

1. *What’s the deal?* Be sure to sketch out the differences between how the majority thinks the Apple App Store works and how the dissent sees that. Do consumers buy the apps directly from Apple, or do they buy them from the app developers? Are there sales that all? Is the software licensed rather than sold? How do those arrangements affect how the case should
be understood? And does the procedural posture of this case matter for how the Court should understand that?

2. Where are the platforms? Always pay attention to what you don’t see in an opinion and here what you do not see is any discussion of two-sided markets or platforms. Given that these issues loomed large in the Supreme Court’s 2018 decision in *American Express*, what accounts for the absence of those issues here? Would the Court have understood the case differently if it had been much more explicit in thinking about the app store as a two-sided market with Apple acting as an intermediary between iOS developers and iOS users? Does the analysis here meant that the Court is backing away from the aggressive approach it took to two-sided markets in *American Express*? Or are there important differences between *Amex* and *Pepper* such that it was sensible for direct economic analysis to loom so large in *Amex* and yet be largely absent in *Pepper*?

3. What is left of *Illinois Brick*? Justice Gorsuch seems to think that the majority is undercutting *Illinois Brick*. *Illinois Brick* concerned a cartel in the upstream market and the question whether the resale buyers in the downstream market could recover damages. The heart of the case was about the difficulty of calculating damages in situations where we have many layers (say a manufacturer, a retailer and an ultimate consumer). Is the situation in *Pepper* different from that case? Do we think damages calculations are easier in platforms? Harder? Is Justice Gorsuch right to believe that, if the Court is willing to embrace mixed damages calculations in this context, it should be willing to do so more generally and directly overrule *Illinois Brick*? *Pepper* involved a transaction platform that sells distribution services to buyers (app developers and consumers) on both sides of the platform and is accused of illegally monopolizing the distribution market. Is *Illinois Brick* even relevant to *Pepper*?