Antitrust Law, Policy, and Procedure

Cases, Materials, Problems

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p. 84, append to ¶2:

The Ninth and Second Circuits recently joined the Third and Seventh Circuits in holding that the FTAIA does not limit a federal court's subject matter jurisdiction. *See United States v. Hui Hsiung*, 778 F.3d 738, 751 (9th Cir 2015); *Lotes Co. v. Hon Hai Precision Indus. Co.*, 753 F.3d 395, 405–406 (2d Cir 2014) (overruling *Filetech S.A. v. France Telecom S.A.,* 157 F.3d 922 (2d Cir. 1998), to the extent it holds that the FTAIA requirements are jurisdictional in nature).

p. 84, append to ¶2 or p. 70, end of Jurisdiction, Venue, and Service Section:

In *Daimler AG v. Bauman*, 134 S.Ct. 746 (2014), the Supreme Court held that due process does not permit the exercise of general jurisdiction in California over a German corporation based on acts committed entirely in Argentina by the corporation's Argentinian subsidiary. When the only connection to California was sizable sales by the corporation's United States subsidiary, jurisdiction was unavailable. Plaintiffs, who were Argentinian residents, alleged that the Argentinian subsidiary conspired with state security forces in violation of the Alien Tort Statute and the Torture Victims Protection Act by allegedly abducting, detaining, torturing, and killing plaintiffs or their relatives during Argentina's "Dirty War." The Court emphasized that the corporation and the corporation's U.S. subsidiary were not considered "at home" in California—neither entity was incorporated nor had its principle place of business in California. Even assuming that the U.S. subsidiary was at home in California, the Court stated that there would be no basis to subject the German Corporation to general jurisdiction in California merely on the basis that one of its subsidiaries was "at home" there. Although not an antitrust case, *Daimler* may have implications on exercising personal jurisdiction over foreign businesses in antitrust suits.

Foreign Trade Antitrust Improvements Act

p. 85, append at bottom of the page:

Recently, the Supreme Court denied certiorari to resolve an apparent circuit split between the Seventh and Ninth Circuits on the proper interpretation of the direct effects exception to the FTAIA when the two courts reached different conclusions regarding the same facts. Both cases originated from a conspiracy between Taiwanese and Korean electronics manufacturers to fix prices of LCD panels. In addition to importing panels directly into the United States, the manufacturers sold panels to foreign third parties that then integrated the panels into finished electronics and subsequently sold them in the United States. The appeals focused on the transactions encompassing the foreign third parties.

In *United States v. Hui Hsiung*, 778 F.3d 738 (9th Cir 2015), *cert. denied*, 2015 WL 1206283 (June 15, 2015), the Ninth Circuit confirmed its "directness test" initially adopted in *United States v. LSL Biotechnologies*, 379 F.3d 672 (9th Cir. 2004). The circuit found that an effect is direct if it is an "immediate consequence" of the alleged anticompetitive conduct. Further, the Ninth Circuit adopted a proximate causation standard for determining whether the direct effect "gives rise to" the plaintiff's injury. In affirming the defendant's convictions, the Ninth Circuit concluded that the domestic effects exception to the FTAIA applied:

> The constellation of events that surrounded the conspiracy leads to one conclusion—the impact on the United States market was direct and followed "as an immediate consequence" of the price fixing. To begin, the TFT–LCDs are a substantial cost component of the finished products—70—80 percent in the case of monitors and 30—40 percent for notebook computers. One of the trial witnesses explained the correlation: "[I]f the panel price goes up, then it will directly impact the monitor set price." The "price stabilization" meetings, where the price fixing initially occurred, led to direct negotiations with United States companies, both domestically and overseas, on pricing decisions. As noted before, some of the panels were imported directly into the United States. Other panels were sold overseas, often to foreign subsidiaries of American companies or to systems integrators, and then incorporated into finished products. It was well understood that substantial numbers of finished products were destined for the United States and that the practical upshot of the conspiracy would be and was increased prices to customers in the United States.
>
> There were a variety of arrangements in terms of incorporating the panels into finished products. For example, Dell had a factory in Malaysia where 100% of the products were destined for the American market. In other situations, overseas systems integrators purchased the panels for integration into finished products, often with direct oversight of TFT–LCD panel pricing by United States manufacturers. In yet other circumstances, a global product arm of a United States company purchased the panels directly from one of the co-conspirators and then sold to system integrators. It was not uncommon that the orders placed with system integrators were based on custom orders from United States customers for direct shipment to that customer. By one estimate, $23.5 billion in pricefixed panels were imported into the United States as part of finished products, such as notebook computers and computer monitors. The testimony underscored the integrated, close and direct connection between the purchase of the price-fixed panels, the United States as the destination for the products, and the ultimate inflation of prices in finished products imported to the United States. The direct connection was neither speculative nor insulated by multiple disconnected layers of transactions.

Hui Hsiung, 778 F.3d at 759–60. The court also noted that evidence supporting the import trade theory was sufficient for conviction, regardless of the domestic effects exception.

Unlike the Ninth Circuit, the Seventh Circuit's directness test, initially stated in *Minn–Chem, Inc. v. Agrium, Inc.*, 683 F.3d 845, 860 (7th Cir. 2012), requires a direct effect to have a "reasonably proximate causal nexus" to the alleged conduct. Additionally, the Seventh Circuit stated that the "give rise to" provision in the direct effects exception determines "who may bring suit" based upon the antitrust injury established by the first prong. In the recent decision of

Motorola Mobility v. AU Optronics Corp., 775 F.3d 816 (7th Cir. 2014), *cert. denied*, 2015 WL 1206313 (June 15, 2015), the Seventh Circuit concluded that the direct effects exception was not applicable:

> It was Motorola, rather than the defendants, that imported these panels into the United States, as components of the cellphones that its foreign subsidiaries manufactured abroad and sold and shipped to it. So it first must show that the defendants' price fixing of the panels that they sold abroad and that became components of cellphones also made abroad but imported by Motorola into the United States had "a direct, substantial, and reasonably foreseeable effect" on commerce within the United States. The panels—57 percent of the total—that never entered the United States neither affected domestic U.S. commerce nor gave rise to a cause of action under the Sherman Act.
>
> If the prices of the components were indeed fixed, there would be an effect on domestic U.S. commerce. And that effect would be foreseeable (because the defendants knew that Motorola's foreign subsidiaries intended to incorporate some of the panels into products that Motorola would resell in the United States), could be substantial, and might well be direct rather than "remote," the word we used in [*Minn–Chem*] to denote effects that the statutory requirement of directness excludes.
>
> The price fixers had, it is true, been selling the panels not in the United States but abroad, to foreign companies (the Motorola subsidiaries) that incorporated them into cell-phones that the foreign companies then exported to the United States for resale by the parent company, Motorola. The effect of fixing the price of a component on the price of the final product was therefore less direct than the conduct in *Minn–Chem,* where "foreign sellers allegedly created a cartel, took steps outside the United States to drive the price up of a product that is wanted in the United States, and then (after succeeding in doing so) *sold that product to U.S. customers*." *Id.* at 860 (emphasis added). But at the same time the facts of this case are not equivalent to what we said in *Minn–Chem* would *definitely* block liability under the Sherman Act: the "situation in which action in a foreign country filters through many layers and finally causes a few ripples in the United States." *Id.* In this case components were sold by their manufacturers to the foreign subsidiaries, which incorporated them into the finished product and sold the finished product to Motorola for resale in the United States. This doesn't seem like "many layers," resulting in just "a few ripples" in the United States cellphone market, though, as we'll see, the ripple effect probably was modest.

Motorola Mobility, 775 F.3d at 818–19. After assuming the first prong was satisfied, the court concluded that Motorola did not satisfy the second prong requiring the direct effect to "give rise to" the injury. Rejecting Motorola's argument that the parent company and its subsidiaries should be treated as one company, the court ultimately held that the direct purchaser doctrine barred Motorola from bringing a claim under the Sherman Act:

> What trips up Motorola's suit is the statutory requirement that the effect of

> anticompetitive conduct on domestic U.S. commerce give rise to an antitrust cause of action. 15 U.S.C. § 6a(2). The conduct increased the cost to Motorola of the cellphones that it bought from its foreign subsidiaries, but the cartel engendered price increase in the components and in the price of cellphones that incorporated them occurred entirely in foreign commerce.
>
> We have both direct purchasers—Motorola's foreign subsidiaries—from the price fixers, and two tiers of indirect purchasers: Motorola, insofar as the foreign subsidiaries passed on some or all of the increased cost of components to Motorola, and Motorola's cellphone customers, insofar as Motorola raised the resale price of its cellphones in an attempt to offload the damage to it from the price fixing to its customers. According to Motorola's damages expert, B. Douglas Bernheim, the company raised the price of its cellphones in the United States by more than the increased price charged to it by its foreign subsidiaries. We have no information about whether Motorola lost customers as a result—it may not have, if other cellphone sellers raised their prices as well. Perhaps because Motorola may actually have profited from the price fixing of the LCD panels, it has waived any claim that the price fixing affected the price that Motorola's foreign subsidiaries charged, or were told by Motorola to charge, for the cellphones that they sold their parent. . . .
>
> Whether or not Motorola was harmed indirectly, the immediate victims of the price fixing were its foreign subsidiaries, see *F. Hoffmann–La Roche Ltd. v. Empagran S.A*., supra, 542 U.S. at 173–75, 124 S.Ct. 2359, and as we said in the *Minn–Chem* case "U.S. antitrust laws are not to be used for injury to foreign customers," 683 F.3d at 858.

Id. at 819–20.

In *Lotes Co. v. Hon Hai Precision Indus. Co.*, 753 F.3d 395 (2d Cir 2014), the Second Circuit adopted the Seventh Circuit's interpretation of "direct." In comparing the two tests, the court stated:

> Indeed, *LSL's* reading of the FTAIA would violate the "cardinal principle of statutory construction" that statutes must be construed, if reasonably possible, so that "no clause, sentence, or word shall be superfluous, void, or insignificant." *TRW Inc. v. Andrews,* 534 U.S. 19, 31, 122 S.Ct. 441, 151 L.Ed.2d 339 (2001) (quoting *Duncan v. Walker,* 533 U.S. 167, 174, 121 S.Ct. 2120, 150 L.Ed.2d 251 (2001)). Reading "direct" as "immediate" would rob the separate "reasonabl[e] foreseeab[ility]" requirement of any meaningful function, since we are hard pressed to imagine any domestic effect that would be both "immediate" and "substantial" but not "reasonably foreseeable." Furthermore, we must remember that "[i]mport trade and commerce are excluded at the outset from the coverage of the FTAIA in the same way that domestic interstate commerce is excluded." *Minn–Chem,* 683 F.3d at 854; *see also* 15 U.S.C. § 6a (providing that, unless an exception applies, the Sherman Act "shall not apply to conduct involving trade or commerce (*other than import trade or import commerce*) with foreign nations"

> (emphasis added)). To demand that any domestic effect must follow as an immediate consequence of a defendant's foreign anticompetitive conduct would all but collapse the FTAIA's domestic effects exception into its separate import exclusion.
>
> Interpreting "direct" to require only a reasonably proximate causal nexus, by contrast, avoids these problems while still addressing antitrust law's classic aversion to remote injuries. Indeed, "directness" is one of the traditional formulations courts have used to talk about the common-law concept of proximate causation. . . . And courts have long applied notions of proximate causation, using the language of "directness," in determining what types of injuries the antitrust laws may properly redress. In the early twentieth century, for example, before the Supreme Court's regime-changing Commerce Clause decision in *Wickard v. Filburn,* 317 U.S. 111, 63 S.Ct. 82, 87 L.Ed. 122 (1942), courts commonly held that anticompetitive schemes whose effects on interstate commerce were merely " 'incidental,' 'indirect,' or 'remote,' " were, "under the prevailing climate, beyond Congress'[s] power to regulate, and hence outside the scope of the Sherman Act." *Mandeville Island Farms, Inc. v. Am. Crystal Sugar Co.,* 334 U.S. 219, 230, 68 S.Ct. 996, 92 L.Ed. 1328 (1948). And today, courts continue to analyze antitrust standing by considering, among other factors, the "directness or indirectness of the asserted injury," *Assoc. Gen. Contractors of Cal., Inc. v. Cal. State Council of Carpenters,* 459 U.S. 519, 540, 103 S.Ct. 897, 74 L.Ed.2d 723 (1983), using familiar principles of proximate causation, *see Blue Shield of Va. v. McCready,* 457 U.S. 465, 476–77 & n. 13, 102 S.Ct. 2540, 73 L.Ed.2d 149 (1982).

Lotes, 753 F.3d at 411–12. The court did not disregard completely concerns with proximate causation:

> Of course, proximate causation is a notoriously slippery doctrine. "In a philosophical sense, the consequences of an act go forward to eternity, and the causes of an event go back to the dawn of human events, and beyond." *CSX Transp., Inc. v. McBride,* — U.S. —, 131 S.Ct. 2630, 2642, 180 L.Ed.2d 637 (2011) (quoting W. Page Keeton et al., Prosser and Keeton on Torts § 42, at 264 (5th ed.1984)). Proximate causation is thus "shorthand for a concept: Injuries have countless causes, and not all should give rise to legal liability." *Id.* at 2637. The doctrine of proximate causation provides the legal vocabulary for drawing this line—courts ask, for example, "whether the injury that resulted was within the scope of the risk created by the defendant's [wrongful] act; whether the injury was a natural or probable consequence of the [conduct]; whether there was a superseding or intervening cause; whether the [conduct] was anything more than an antecedent event without which the harm would not have occurred." *Id.* at 2652 (Roberts, C.J., dissenting). "The proximate-cause inquiry is not easy to define, and over the years it has taken various forms; but courts have a great deal of experience applying it, and there is a wealth of precedent for them to draw upon in doing so." *Lexmark Int'l, Inc. v. Static Control Components, Inc.,* — U.S. —, 134 S.Ct. 1377, 1390, 188 L.Ed.2d 392 (2014).

> While *Minn–Chem's* "reasonably proximate causal nexus" standard incorporates all of this useful judicial experience, *LSL's* "immediate consequence" standard focuses narrowly on a single factor—the spatial and temporal separation between the defendant's conduct and the relevant effect.
>
> Herein lies the error of the decision below, which placed near-dispositive weight on the fact that USB 3.0 connectors are manufactured and assembled into finished computer products "in China" before being sold in the United States. J.A. 264. This kind of complex manufacturing process is increasingly common in our modern global economy, and antitrust law has long recognized that anticompetitive injuries can be transmitted through multi-layered supply chains. Indeed, the Supreme Court has held that claims by indirect purchasers are "consistent with the broad purposes of the federal antitrust laws: deterring anticompetitive conduct and ensuring the compensation of victims of that conduct." *California v. ARC Am. Corp*., 490 U.S. 93, 102, 109 S.Ct. 1661, 104 L.Ed.2d 86 (1989).
>
> There is nothing inherent in the nature of outsourcing or international supply chains that necessarily prevents the transmission of anticompetitive harms or renders any and all domestic effects impermissibly remote and indirect. Indeed, given the important role that American firms and consumers play in the global economy, we expect that some perpetrators will design foreign anticompetitive schemes for the very purpose of causing harmful downstream effects in the United States. Whether the causal nexus between foreign conduct and a domestic effect is sufficiently "direct" under the FTAIA in a particular case will depend on many factors, including the structure of the market and the nature of the commercial relationships at each link in the causal chain. Courts confronting claims under the FTAIA will have to consider all of the relevant facts, using all of the traditional tools courts have used to analyze questions of proximate causation.

Id. at 412–13. The court further adopted the proximate causation standard to determine whether the domestic effect "gives rise to" the plaintiff's injury:

> We thus must determine whether any domestic effect resulting from the defendants' anticompetitive conduct proximately caused Lotes's injury. We conclude that it did not. Lotes alleges that the defendants' foreign conduct had the effect of driving up the prices of consumer electronics devices incorporating USB 3.0 connectors in the United States. But those higher prices did not cause Lotes's injury of being excluded from the market for USB 3.0 connectors—that injury flowed directly from the defendant's exclusionary foreign conduct. Lotes's complaint thus seeks redress for precisely the type of "independently caused foreign injury" that *Empagran* held falls outside of Congress's intent. *Empagran*, 542 U.S. at 173.
>
> Indeed, to the extent there is any causal connection between Lotes's injury and an effect on U.S. commerce, the direction of causation runs the wrong way. Lotes

> alleges that the defendants' patent hold-up has excluded Lotes from the market, which reduces competition and raises prices, which are then passed on to U.S. consumers. Lotes's injury thus precedes any domestic effect in the causal chain. And "[a]n effect never precedes its cause." *Am. Home Prods. Corp. v. Liberty Mut. Ins. Co.*, 748 F.2d 760, 765 (2d Cir.1984).

Id. at 414.

Some commentators believe that the Supreme Court's refusal to grant certiorari to clarify the perceived circuit split weakens the credibility of the FTAIA. *See, e.g.,* Amelie Doublet, Motorola Mobility II *and the Circuit Split Over the Interpretation of the FTAIA: The Necessity for Supreme Court Review*, 83 U.S. L. W. 1683 (2015) (analyzing concerns with both tests and consequences of the circuit split). However, others are able to reconcile the two conflicting conclusions. They assert that *Motorola Mobility* and *Hui Hsiung* are actually complementary because the injuries alleged by the plaintiffs are distinguishable. *See* Hollis Salzman & Dinah Reese, *Much Ado About Injury: Making Sense Of FTAIA Circuit Split*, LAW360 (May 14, 2015, 10:11 AM EST), www.law360.com/articles/655633/much-ado-about-injury-making-sense-of-ftaia-circuit-split (emphasizing that "[i]n *Hsiung*, the redress sought was for a direct injury to U.S. commerce, while that sought in *Motorola* was for an injury that is undoubtedly indirect"). The authors believe that the cases were correctly decided, and hence there was no split in the circuits that would give rise to the Supreme Court granting certiorari. Most significantly, *Hui Hsiung* was a criminal case, in which the government must prove harm in the United States, which is ordinarily established by a showing that significant price-fixed product was imported. The government is not limited by the indirect purchaser rule or other private plaintiff limitations on standing that undermined Motorola Mobility's claim in the Ninth Circuit.

[e] The Direct Purchaser Requirement and the Problem of Passing on

p. 96, append to Note 2:

In *Lakeland Reg'l Med. Ctr. Inc. v. Astellas U.S. LLC*, 763 F.3d 1280 (11th Cir. 2014), the court held that the direct purchaser rule barred the medical center's antitrust claim because the distributors who bought the product from the defendant and then resold it to the medical center were the direct purchasers, thus the only parties who could bring a claim for damages. In its reasoning, the court reiterated the policies supporting the direct purchaser requirement:

> Although the distributors may have passed on to the Medical Center some or all of the overcharge that they paid to Astellas, the Medical Center cannot recover damages from Astellas for that overcharge because it was the second purchaser of that tied product. Indeed, to allow the Medical Center to maintain a damages claim for this particular tying arrangement would give rise to the very problems that the direct purchaser rule seeks to avoid. It would complicate the calculation of damages resulting from any overcharge by Astellas by requiring an apportionment of that overcharge throughout the Adenoscan distribution chain, between the direct purchasers (the distributors) and the indirect purchasers (like the Medical Center); it would create the possibility that both the distributors and the indirect Adenoscan purchasers like the Medical Center could recover from Astellas for the same allegedly unlawful tying arrangement; and it would discourage vigorous private-citizen enforcement of the antitrust laws by making it more difficult for the best-suited plaintiffs, the distributors, to bring an unlawful

> tying claim. *See UtiliCorp,* 497 U.S. at 208–16, 110 S.Ct. 2807. For these reasons, then, only the distributors, as the direct purchasers of Adenoscan who first paid the inflated tied price for that product, can recover damages from Astellas for that alleged overcharge resulting from Astellas's alleged tying behavior.

Lakeland Reg'l Med. Ctr., 763 F.3d at 1285–86.

[g] Antitrust Injury

p. 111, append to Note 1:

In Re Online DVD-Rental Antitrust Litig., 779 F.3d 914 (9th Cir. 2015), held that plaintiffs failed to show evidence to raise a triable issue of fact to support claim against Netflix and Walmart, alleging that absent the promotion agreement between the two companies, in which Walmart transferred its online DVD-rental subscribers to Netflix in exchange for Netflix to promote Walmart's DVD sales, Netflix would have reduced its subscription plan price. Documents entered into evidence revealed that no one, including Walmart, viewed Walmart as a competitive threat at the time the agreement was signed. The court concluded that Plaintiffs' evidence actually supported the defendants' position because Blockbuster, rather than Walmart, was a greater competitor; yet, Netflix had never lowered its plan price to $15.99 despite Blockbuster's price reduction to $14.99.

p. 112 add after note 2.

In *Gelboim v. Bank of America Corp.*, 823 F.3d 759 (2d Cir. 2016), the Second Circuit considered whether the plaintiff had suffered antitrust injury by purchasing financial instruments at interest rates that the plaintiffs themselves had negotiated. Because the negotiated interest rates relied on a standardized interest rate index as a benchmark which allegedly had been collusively set by the defendants, the court ruled that the plaintiffs had suffered antitrust injury. The court stated, "generally, when consumers, because of a conspiracy, must pay prices that no longer reflect ordinary market conditions, they suffer 'injury of the type the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful.'" *Id. at 24* (quoting *Brunswick Corp. v. Pueblo Bowl-O-Matic*, 429 U.S. 477, 489 (1977).

In *Hanover 3201 Realty, LLC v. Village Supermarkets, Inc.*, 806 F.3d 162 (3rd Cir. 2015), the court held that legal fees incurred in responding to anticompetitive sham petitioning was an antitrust injury.

[h] Standing to Sue

p. 133 add after Associated General

In *Hanover 3201 Realty, LLC v. Village Supermarkets, Inc.*, 806 F.3d 162 (3rd Cir. 2015), the Third Circuit recently considered whether antitrust standing is limited to consumers and competitors as suggested in *Associated General*. The plaintiff, Hanover Realty, a real estate developer and property owner, contracted with Wegmans for the construction of a "full-service supermarket" in Hanover, NJ. As a condition, the contract required Hanover Realty to obtain "all necessary government permits prior to beginning construction." Upon being informed of this deal, the defendants, ShopRite and its subsidiaries, allegedly commenced sham petitioning various government bodies in attempt to slow and ultimately prevent Hanover Realty from fulfilling their contractual duties, and, in turn, to impede Wegmans from placing their store in Hanover, NJ. Hanover Realty then sued ShopRite for violation of antitrust law, in relevant part, for restraining the market for full-service supermarkets. The district court dismissed the suit, finding that Hanover Realty did not have standing on the grounds that Hanover Realty "was not a consumer, competitor, or participant in the restrained markets." 806 F.3d at 166-167.

Reversing the decision below, the Third Circuit assessed the following four factors of antitrust standing:

> (1) the causal connection between the antitrust violation and the harm to the plaintiff and the intent by the defendant to cause that harm, with neither factor alone conferring standing; . . . [(2)] the directness of the injury, which addresses the concerns that liberal application of standing principles might produce speculative claims; [(3)] the existence of more direct victims of the alleged antitrust violations; and [(4)] the potential for duplicative recovery or complex apportionment of damages. *Id.* at 171.

According to the court, causation was satisfied by the allegation that the sham petitions had cost Hanover Realty thousands of dollars in legal fees. Following *McReady*, the court found directness of injury does not depend on the target of the defendants' actions. The injury to Hanover was found to be "direct" because if the Wegmans deal ultimately succeeds, Hanover Realty will have suffered an injury even though Wegmans has not. As in *McReady*, the court found that the harm to the plaintiff was "inextricably intertwined" with the intended anticompetitive harm to Wegmans because it was an "indispensable aspect of the scheme." *Id.* at 172-73.

In contrast, this was not the sort of injury which is "secondary to the anticompetitive conduct" as when a supplier loses business when competition is restrained in a downstream market. *Id.* at 173. Further, "that Wegmans is another direct victim 'does not diminish the directness of [Hanover Realty's] injury." *Id.* at 177 (quoting *In re Lower Lake Erie Iron Ore Antitrust Litigation*, 998 F.2d 1144, 1168-69 (3rd Cir. 1993)).

Finally, the court found that while the additional presence of Wegmans as a direct victim may cause some need for apportionment, it would not be "complex." The recovery of legal expenses related to the sham petitions would not need to be apportioned at all since it was entirely Hanover Realty's expense, and any damages for delay or obstruction of the lease would simply be calculated by subtracting the lost rent to Hanover Realty from Wegmans' lost profits.

In *Gelboim v. Bank of America Corp.*, 823 F.3d 759 (2d Cir. 2016) the Second Circuit provides another illuminating analysis of antitrust standing. In *Gelboim*, the defendants were a number of financial institutions responsible for setting the London Interbank Offer Rate (LIBOR). LIBOR is the average of interest rates at which those financial institutions hypothetically would lend to another financial institution. The plaintiffs were purchasers of financial instruments, the negotiated rates of which depend on LIBOR as a benchmark. The plaintiffs alleged that the defendants improperly and collusively fixed LIBOR and thereby harmed the plaintiffs.

After reversing the lower court on its finding that the plaintiffs lacked antitrust injury, the court considered what factors are relevant to an analysis of antitrust standing on remand. Similar to the Third Circuit in *Hanover Realty*, the Second Circuit considered the following four factors: (1) causation, (2) the existence of more direct victims, (3) the speculative nature of the damages plead, and (4) the potential for duplicative recovery and complex apportionment.

The court provided the following guidance for applying this balancing test. Causation is a matter of the "directness or indirectness of the asserted injury." *Id.* at 39. Special causation problems arise in the situation where a cartel controls only a small percentage of the relevant market, but their market-wide price raising effects harm consumers who have dealt with non-cartel members. The court notes that the circuits are split over the resolution of this issue. On the one side, there is no apparent difference between the harm to consumers who have dealt with the cartel and the consumer who has not. On the other hand, where the cartel controls only a small percentage of the relevant market, allowing all market consumers treble damages "would result in overkill."

The existence of more direct victims "seems to bear chiefly on whether the plaintiff is a consumer or competitor . . . but consumer status is not the end of the inquiry. The efficient enforcer criteria must be established independent of whether the plaintiff is a consumer or competitor. Implicit in the inquiry is that not every victim of an antitrust violation needs to be compensated." The court noted that directness may have diminished importance in a case such as this where both direct and remote victims will have suffered harm to the same extent and in the same way.

As for the speculative nature of damages asserted, the court writes, "highly speculative damages [are] a sign that a given plaintiff is an inefficient engine of enforcement." However, "impediments to reaching a reliable damages estimate often flow from the nature and complexity of the alleged violation." The question ultimately turns on whether the damages are necessarily "highly speculative." The court notes that there are some unusual difficulties in the instant case.

Finally, the court states that given the widespread effect of the interest-rate-standard price fix, and the countless legal actions in response worldwide, "it is wholly unclear on this record how issues of duplicate recovery and damage apportionment can be assessed."

Compare the antitrust standing inquiry to the constitutional standing required for the federal courts to exercise their authority. In *Spokeo Inc. v. Robins*, 136 S.Ct. 1540 (2016), the Supreme Court reiterated the test for federal standing. "The plaintiff must have (1) suffered an injury in fact, (2) that is fairly traceable to the challenged conduct of the defendant, and (3) that is likely to be redressed by a favorable judicial decision." *Id.* at 1547. Injury in fact, specifically, "requires a plaintiff to allege an injury that is both 'concrete *and* particularized.'" *Ibid.*

p. 134, add this note:

5. *Fisher v. Aurora Health Care*, 558 F. App'x 653 (7th Cir. 2014), held that an individual physician was not the most "efficient" plaintiff, and thus lacked standing, to bring suit alleging antitrust violations against a hospital that eliminated independent physicians from its staff to cut costs, purportedly depriving patients of medical services by independent physicians. The court concluded that insurance companies, patient-consumers, and even groups of doctors would be better plaintiffs to vindicate the claim. The court, also, noted that there is no case law supporting the contention that the antitrust laws recognize the type of injury alleged.

[3] Private Suits

[a] Jurisdiction, Venue, and Service

In *Freedom Watch, Inc. v. OPEC*, 766 F.3d 74 (D.C. Cir. 2014), the court concluded that the Plaintiff's attempts at service of process upon the defendant for an antitrust complaint by delivering a copy of the documents to the Defendant's headquarters in Vienna and by sending a copy to the headquarters by Austrian mail were invalid. However, the court remanded for the district court to reconsider whether it should authorize the Plaintiff to serve process upon the Defendant's United States general counsel. The court emphasized that the district court is not required to authorize the alternative service but should at least use its discretion under Federal Rule of Civil Procedure 4(f)(3).

III REMEDIES

[B] Award of Attorney's Fees

p. 168, append to end of section:

In *Cohlmia v. St. John Med. Ctr.*, 749 F.3d 1175 (10^{th} Cir. 2014), the medical center defendant sought attorney's fees under the Health Care Quality Improvement Act of 1986. The court awarded attorney's fees against the physician who brought antitrust claims against the medical center. The court concluded that the suit was frivolous because the physician continued suit despite indications apparent early in the litigation that the claims lacked substance.

Chapter 4 CARTELS AND OTHER JOINT CONDUCT BY COMPETITORS

I HORIZONTAL RESTRAINTS

[B] Price Fixing

[4] The Meaning and Scope of the Rule of Reason

p. 259, append this note:

12. In *Marucci Sports, L.L.C. v. Nat'l Collegiate Athletic Association*, 751 F.3d 368 (5th Cir. 2014), the Fifth Circuit affirmed dismissal of plaintiff's claim that the NCAA and the National Federation of State High School Associations illegally restrained trade by prohibiting certain non-wood baseball bats through adoption of the Bat-Ball Coefficient of Restitution Standard ("BBROC Standard"). The Fifth Circuit reasoned that "[t]he BBCOR Standard is best described as a 'rule[ ] defining the conditions of the contest' as explained in *Board of Regents,* [in which] the Supreme Court provided examples of rules or conditions that regulate athletic competitions between the NCAA's member institutions such as 'the size of the field, the number of players on a team, and the extent to which physical violence is to be encouraged or proscribed....' The liveliness of a baseball bat falls squarely within the framework of the rules and conditions described in *Board of Regents.*" *Marucci*, 751 F.3d at 376 (quoting *NCAA v. Board of Regents*).

O'BANNON V. NATIONAL COLLEGIATE ATHLETIC ASSOCIATION,
802 F.3d 1049 (9th Cir. 2015)

BYBEE, Circuit Judge:

Section 1 of the Sherman Antitrust Act of 1890, 15 U.S.C. § 1, prohibits "[e]very contract, combination ..., or conspiracy, in restraint of trade or commerce." For more than a century, the National Collegiate Athletic Association (NCAA) has prescribed rules governing the eligibility of athletes at its more than 1,000 member colleges and universities. Those rules prohibit student-athletes from being paid for the use of their names, images, and likenesses (NILs). The question presented in this momentous case is whether the NCAA's rules are subject to the antitrust laws and, if so, whether they are an unlawful restraint of trade.
After a bench trial and in a thorough opinion, the district court concluded that the NCAA's compensation rules were an unlawful restraint of trade. It then enjoined the NCAA from prohibiting its member schools from giving student-athletes scholarships up to the full cost of attendance at their respective schools and up to $5,000 per year in deferred compensation, to be held in trust for student-athletes until after they leave college. …

We conclude that the district court's decision was largely correct. Although we agree with the Supreme Court and our sister circuits that many of the NCAA's amateurism rules are likely to be procompetitive, we hold that those rules are not exempt from antitrust scrutiny; rather, they must be analyzed under the Rule of Reason. Applying the Rule of Reason, we conclude that the district court correctly identified one proper alternative to the current NCAA compensation rules—*i.e.,* allowing NCAA members to give scholarships up to the full cost of attendance—but that the district court's other remedy, allowing students to be paid cash compensation of up to $5,000 per year, was erroneous. We therefore affirm in part and reverse in part.

I

… *Fin de siècle* college football was a rough game. Serious injuries were common, and it was not unheard of for players to be killed during games. Schools were also free to hire nonstudent ringers to compete on their teams or to purchase players away from other schools. …

One of the NCAA's earliest reforms of intercollegiate sports was a requirement that the participants be amateurs. …

In 1956, the NCAA … chang[ed] its rules to permit its members, for the first time, to give student-athletes scholarships based on athletic ability. These scholarships were capped at the amount of a full "grant in aid," defined as the total cost of "tuition and fees, room and board, and required course-related books." …

In addition to its financial aid rules, the NCAA has adopted numerous other amateurism rules that limit student-athletes' compensation and their interactions with professional sports leagues. An athlete can lose his amateur status, for example, if he signs a contract with a professional team, enters a professional league's player draft, or hires an agent. And, most importantly, an athlete is prohibited—with few exceptions—from receiving *any* "pay" based on his athletic ability, whether from boosters, companies seeking endorsements, or would-be licensors of the athlete's name, image, and likeness (NIL). …

In 2008, Ed O'Bannon, a former All–American basketball player at UCLA, visited a friend's house, where his friend's son told O'Bannon that he was depicted in a college basketball video game produced by Electronic Arts (EA), a software company that produced video games based on college football and men's basketball from the late 1990s until around 2013. The friend's son turned on the video game, and O'Bannon saw an avatar of himself—a virtual player who visually resembled O'Bannon, played for UCLA, and wore O'Bannon's jersey number, 31. O'Bannon had never consented to the use of his likeness in the video game, and he had not been compensated for it.

In 2009, O'Bannon sued the NCAA and the Collegiate Licensing Company (CLC), the entity which licenses the trademarks of the NCAA and a number of its member schools for commercial use, in federal court. The gravamen of O'Bannon's complaint was that the NCAA's amateurism rules, insofar as they prevented student-athletes from being compensated for the use of their NILs, were an illegal restraint of trade under Section 1 of the Sherman Act, 15 U.S.C. § 1. …

After a fourteen-day bench trial, the district court entered judgment for the plaintiffs, concluding that the NCAA's rules prohibiting student-athletes from receiving compensation for their NILs violate Section 1 of the Sherman Act. …

IV

… Although in another context the NCAA's decision to value student-athletes' NIL at zero might be per se illegal price fixing, we are persuaded—as was the Supreme Court in *Board of Regents* and the district court here—that the appropriate rule is the Rule of Reason. As the Supreme Court observed, the NCAA "market[s] a particular brand ... [that] makes it more popular than professional sports to which it might otherwise be comparable." *Board of Regents,* 468 U.S. at 101–02. Because the "integrity of the 'product' cannot be preserved except by mutual agreement," "restraints on competition are essential if the product is to be available at all." *Id.* at 101, 102. …

[W]e follow the three-step framework of the Rule of Reason: "[1] The plaintiff bears the initial burden of showing that the restraint produces significant anticompetitive effects within a relevant market. [2] If the plaintiff meets this burden, the defendant must come forward with evidence of the restraint's procompetitive effects. [3] The plaintiff must then show that any legitimate objectives can be achieved in a substantially less restrictive manner." *Tanaka v. Univ. of S. Cal.,* 252 F.3d 1059, 1063 (9th Cir.2001) (citations and internal quotation marks omitted).

A. *Significant Anticompetitive Effects Within a Relevant Market*

…[T]he district court made the following factual findings: (1) that a cognizable "college education market" exists, wherein colleges compete for the services of athletic recruits by offering them scholarships and various amenities, such as coaching and facilities; (2) that if the NCAA's compensation rules did not exist, member schools would compete to offer recruits compensation for their NILs; and (3) that the compensation rules therefore have a significant anticompetitive effect on the college education market, in that they fix an aspect of the "price" that recruits pay to attend college (or, alternatively, an aspect of the price that schools pay to secure recruits' services). These findings have substantial support in the record.

By and large, the NCAA does not challenge the district court's findings. It does not take issue with the way that the district court defined the college education market. Nor does it appear to dispute the district court's conclusion that the compensation rules restrain the NCAA's member schools from competing with each other within that market, at least to a certain degree. Instead, … it argues that because the plaintiffs never showed that the rules reduce output in the college education market, the plaintiffs did not meet their burden of showing a significant anticompetitive effect. … [T]his argument misses the mark. Although output reductions are one common kind of anticompetitive effect in antitrust cases, a "reduction in output is not the *only* measure of anticompetitive effect." Areeda & Hovenkamp ¶ 1503b(1) (emphasis added).

The "combination[s] condemned by the [Sherman] Act" also include "price-fixing ... by purchasers" even though "the persons specially injured ... are sellers, not customers or consumers." *Mandeville Island Farms, Inc. v. Am. Crystal Sugar Co.,* 334 U.S. 219, 235 (1948). At trial, the plaintiffs demonstrated that the NCAA's compensation rules have just this kind of anticompetitive effect: they fix the price of one component of the exchange between school and recruit, thereby precluding competition among schools with respect to that component. The district court found that although consumers of NCAA football and basketball may not be harmed directly by this price-fixing, the "student-athletes themselves are harmed by the price-fixing agreement among FBS [Football Bowl Subdivision] football and Division I basketball schools." The athletes accept grants-in-aid, and no more, in exchange for their athletic performance, because the NCAA schools have agreed to value the athletes' NILs at zero, "an anticompetitive effect." This anticompetitive effect satisfied the plaintiffs' initial burden under the Rule of Reason. …

Because we agree with the district court that the compensation rules have a significant anticompetitive effect on the college education market, we proceed to consider the procompetitive justifications the NCAA proffers for those rules.

B. *Procompetitive Effects*

…[T]he NCAA offered the district court four procompetitive justifications for the compensation rules: (1) promoting amateurism, (2) promoting competitive balance among NCAA schools, (3) integrating student-athletes with their schools' academic community, and (4) increasing output in the college education market. The district court accepted the first and third and rejected the other two.

… [T]he NCAA focuses its arguments to this court entirely on the first proffered justification—the promotion of amateurism. We therefore accept the district court's factual findings that the compensation rules do not promote competitive balance, that they do not increase output in the college education market, and that they play a limited role in integrating student-athletes with their schools' academic communities, since we have been offered no meaningful argument that those findings were clearly erroneous.

The district court acknowledged that the NCAA's current rules promote amateurism, which in turn plays a role in increasing consumer demand for college sports. The NCAA does not challenge that specific determination, but it argues to us that the district court gave the amateurism justification short shrift, in two respects. First, it claims that the district court erred by focusing solely on the question of whether amateurism increases consumers' (*i.e.,* fans') demand for college sports and ignoring the fact that amateurism also increases choice for student-athletes by giving them "the only opportunity [they will] have to obtain a college education while playing competitive sports *as students.*" Second, it faults the district court for being inappropriately skeptical of the NCAA's historical commitment to amateurism. Although we might have credited the depth of the NCAA's devotion to amateurism differently, these arguments do not persuade us that the district court clearly erred.

The NCAA is correct that a restraint that broadens choices can be procompetitive. The Court in *Board of Regents* observed that the difference between college and professional sports "widen[s]" the choices "available to athletes." *Bd. of Regents,* 468 U.S. at 102. But we fail to see how the restraint at issue in this particular case—*i.e.,* the NCAA's limits on student-athlete compensation—makes college sports more attractive to recruits, or widens recruits' spectrum of choices in the sense that *Board of Regents* suggested. As the district court found, it is primarily "the opportunity to earn a higher education" that attracts athletes to college sports rather than professional sports, and that opportunity would still be available to student-athletes if they were paid some compensation in addition to their athletic scholarships. …

Indeed, if anything, loosening or abandoning the compensation rules might be the best way to "widen" recruits' range of choices; athletes might well be more likely to attend college, and stay there longer, if they knew that they were earning some amount of NIL income while they were in school. *See* Jeffrey L. Harrison & Casey C. Harrison, *The Law and Economics of the NCAA's Claim to Monopsony Rights,* 54 Antitrust Bull. 923, 948 (2009). We therefore reject the NCAA's claim that, by denying student-athletes compensation apart from scholarships, the NCAA increases the "choices" available to them.

The NCAA's second point has more force—the district court probably underestimated the NCAA's commitment to amateurism. [c.o.] But the point is ultimately irrelevant. Even if the NCAA's concept of amateurism had been perfectly coherent and consistent, the NCAA would still need to show that amateurism brings about some procompetitive *effect* in order to justify it under the antitrust laws. *See id.* at 101–02 & n. 23. The NCAA cannot fully answer the district court's finding that the compensation rules have significant anticompetitive effects simply by pointing out that it has adhered to those rules for a long time. Nevertheless, the district court found, and the record supports that there is a concrete procompetitive effect in the NCAA's commitment to amateurism: namely, that the amateur nature of collegiate sports increases their appeal to consumers. We therefore conclude that the NCAA's compensation rules serve the two procompetitive purposes identified by the district court: integrating academics with athletics, and "preserving the popularity of the NCAA's product by promoting its current understanding of amateurism."

… But, as *Board of Regents* demonstrates, not every rule adopted by the NCAA that restricts the market is necessary to preserving the "character" of college sports. We thus turn to the final inquiry—whether there are reasonable alternatives to the NCAA's current compensation restrictions.

C. *Substantially Less Restrictive Alternatives*

The third step in the Rule of Reason analysis is whether there are substantially less restrictive alternatives to the NCAA's current rules. We bear in mind that—to be viable under the Rule of Reason—an alternative must be "virtually as effective" in serving the procompetitive purposes of the NCAA's current rules, and "without significantly increased cost." ...

The district court identified two substantially less restrictive alternatives: (1) allowing NCAA member schools to give student-athletes grants-in-aid that cover the full cost of attendance; and (2) allowing member schools to pay student-athletes small amounts of deferred cash compensation for use of their NILs.[18] We hold that the district court did not clearly err in finding that raising the grant-in-aid cap would be a substantially less restrictive alternative, but that it clearly erred when it found that allowing students to be paid compensation for their NILs is virtually as effective as the NCAA's current amateur-status rule.

1. Capping the permissible amount of scholarships at the cost of attendance

The district court did not clearly err in finding that allowing NCAA member schools to award grants-in-aid up to their full cost of attendance would be a substantially less restrictive alternative to the current compensation rules. All of the evidence before the district court indicated that raising the grant-in-aid cap to the cost of attendance would have virtually no impact on amateurism … Nothing in the record, moreover, suggested that consumers of college sports would become less interested in those sports if athletes' scholarships covered their full cost of attendance, or that an increase in the grant-in-aid cap would impede the integration of student-athletes into their academic communities. …

A compensation cap set at student-athletes' full cost of attendance is a substantially less restrictive alternative means of accomplishing the NCAA's legitimate procompetitive purposes. And there is no evidence that this cap will significantly increase costs; indeed, the NCAA already permits schools to fund student-athletes' full cost of attendance. The district court's determination that the existing compensation rules violate Section 1 of the Sherman Act was correct and its injunction requiring the NCAA to permit schools to provide compensation up to the full cost of attendance was proper.

2. Allowing students to receive cash compensation for their NILs

In our judgment, however, the district court clearly erred in finding it a viable alterative to allow students to receive NIL cash payments untethered to their education expenses. Again, the district court identified two procompetitive purposes served by the NCAA's current rules: "preserving the popularity of the NCAA's product by promoting its current understanding of amateurism"

[18] Although the NCAA now permits schools and conferences to elect to raise their scholarship caps to the full cost of attendance, it could reverse its position on that issue at any time. The district court's injunction prohibiting the NCAA from setting a cap any lower than the cost of attendance thus remains in effect, which means that the NCAA's challenge to that portion of the injunction is not moot.

and "integrating academics and athletics." ... The question is whether the alternative of allowing students to be paid NIL compensation unrelated to their education expenses, is "virtually as effective" in preserving amateurism as *not* allowing compensation. ...

We cannot agree that a rule permitting schools to pay students pure cash compensation and a rule forbidding them from paying NIL compensation are both *equally* effective in promoting amateurism and preserving consumer demand. Both we and the district court agree that the NCAA's amateurism rule has procompetitive benefits. But in finding that paying students cash compensation would promote amateurism as effectively as not paying them, the district court ignored that not paying student-athletes is *precisely what makes them amateurs*….

Aside from the self-evident fact that paying students for their NIL rights will vitiate their amateur status as collegiate athletes, the court relied on threadbare evidence in finding that small payments of cash compensation will preserve amateurism as well the NCAA's rule forbidding such payments. Most of the evidence elicited merely indicates that paying students large compensation payments would harm consumer demand more than smaller payments would—not that small cash payments will preserve amateurism. Thus, the evidence was addressed to the wrong question. Instead of asking whether making small payments to student-athletes served the same procompetitive purposes as making no payments, the evidence before the district court went to a different question: Would the collegiate sports market be better off if the NCAA made small payments or big payments? … But there is a stark difference between finding that small payments are less harmful to the market than large payments—and finding that paying students small sums is virtually as effective in promoting amateurism as not paying them. …

The difference between offering student-athletes education-related compensation and offering them cash sums untethered to educational expenses is not minor; it is a quantum leap. Once that line is crossed, we see no basis for returning to a rule of amateurism and no defined stopping point; we have little doubt that plaintiffs will continue to challenge the arbitrary limit imposed by the district court until they have captured the full value of their NIL. At that point the NCAA will have surrendered its amateurism principles entirely and transitioned from its "particular brand of football" to minor league status. *Bd. of Regents,* 468 U.S. at 101–02. In light of that, the meager evidence in the record, and the Supreme Court's admonition that we must afford the NCAA "ample latitude" to superintend college athletics, *Bd. of Regents,* 468 U.S. at 120, we think it is clear the district court erred in concluding that small payments in deferred compensation are a substantially less restrictive alternative restraint. We thus vacate that portion of the district court's decision and the portion of its injunction requiring the NCAA to allow its member schools to pay this deferred compensation.

V

By way of summation, we wish to emphasize the limited scope of the decision we have reached and the remedy we have approved. Today, we reaffirm that NCAA regulations are subject to antitrust scrutiny and must be tested in the crucible of the Rule of Reason. When those regulations truly serve procompetitive purposes, courts should not hesitate to uphold them. But the NCAA is not above the antitrust laws, and courts cannot and must not shy away from requiring the NCAA to play by the Sherman Act's rules. In this case, the NCAA's rules have been more restrictive than necessary to maintain its tradition of amateurism in support of the college sports market. The Rule of Reason requires that the NCAA permit its schools to provide up to the cost of attendance to their student athletes. It does not require more.

We vacate the district court's judgment and permanent injunction insofar as they require the NCAA to allow its member schools to pay student-athletes up to $5,000 per year in deferred compensation. We otherwise affirm. …

NOTES AND QUESTIONS

1. The Ninth Circuit rejected the NCAA's argument "that any Section 1 challenge to its amateurism rules must fail as a matter of law because the *Board of Regents* Court held that those rules are presumptively valid." Is that a correct interpretation of *Board of Regents*. Why or why not?
2. Judge Thomas dissented regarding the majority's reversal of the district court's order that the NCAA permit up to $5,000 in deferred compensation above student-athletes' full cost of attendance. Judge Thomas reasoned that the district court's conclusion on this point was supported by sufficient evidence, including testimony from experts "that providing student-athletes with small amounts of compensation above their cost of attendance most likely would not have a significant impact on consumer interest in college sports," as well as "the fact that FBS football players are currently permitted to accept Pell grants in excess of their cost of attendance, and the fact that Division I tennis recruits are permitted to earn up to $10,000 per year in prize money from athletic events before they enroll in college." Is this evidence sufficient to uphold the district court's order or is it "threadbare," as the majority characterized it?
3. Does the amount of money already involved in college athletics undermine the NCAA's claims regarding the importance of amateurism? In his dissent, Judge Thomas noted that Division I schools had spent $5 billion on athletic facilities in the previous 15 years and that a 12-year contract for the television rights to broadcast the NCAA men's basketball championship tournament netted the NCAA over $10 billion dollars. Judge Thomas observed that "[t]he NCAA insists that this multi-billion dollar industry would be lost if the teenagers and young adults who play for these college teams earn one dollar above their cost of school attendance. That is a difficult argument to swallow." Do you agree? Why or why not?
4. From his review every rule-of-reason case between 1977 and 2009 – a total of over 700 cases applying the rule of reason – Professor Michael Carrier demonstrated "that balancing takes place in the last stage of a four-part burden-shifting approach. First, a plaintiff must show a significant anticompetitive effect, typically in the form of a price increase, output reduction, or showing of market power. Second, a defendant must offer a procompetitive justification for the restraint. Third, the plaintiff can show that the restraint is not reasonably necessary to attain the restraint's objectives or that there are alternatives less restrictive of competition. The final stage involves balancing anticompetitive and procompetitive effects." Michael A. Carrier, *How Not to Apply the Rule of Reason: The* O'Bannon *Case*, 114 MICH. L. REV. FIRST IMPRESSIONS 73, 74 (2015). Professor Carrier criticized the *O'Bannon* opinion for failing to perform the fourth step: balancing. This fourth step is necessary because a restraint of trade with high anticompetitive effects and low procompetitive justifications violates the rule of reason even if there are no less restrictive alternatives.

p. 275, append this note:

7. In *In re Southeastern Milk Antitrust Litigation*, 739 F.3d 262 (6th Cir. 2014), the Sixth Circuit held that "[u]nder a quick-look analysis, the Plaintiffs do not necessarily need to establish either product or geographic market evidence in order to defeat summary judgment." *Id*. at 275-76.

The court reasoned that "[o]nce anticompetitive behavior is shown to a court's satisfaction, even without detailed market analysis, the burden shifts to the defendant who must justify the agreement at issue on procompetitive grounds by providing some 'competitive justification' for the restraint at issue." *Id*. at 275 (citation omitted).

p.281, add new section:

[4.1] Hub-and-Spoke Conspiracies

UNITED STATES V. APPLE, INC.,
791 F.3d 290 (2d Cir. 2015)

DEBRA ANN LIVINGSTON, Circuit Judge:

Since the invention of the printing press, the distribution of books has involved a fundamentally consistent process: compose a manuscript, print and bind it into physical volumes, and then ship and sell the volumes to the public. In late 2007, Amazon.com, Inc. ("Amazon") introduced the Kindle, a portable device that carries digital copies of books, known as "ebooks." This innovation had the potential to change the centuries-old process for producing books by eliminating the need to print, bind, ship, and store them. Amazon began to popularize the new way to read, and encouraged consumers to buy the Kindle by offering desirable books—new releases and *New York Times* bestsellers—for $9.99. Publishing companies, which have traditionally stood at the center of the multi-billion dollar book-producing industry, saw Amazon's ebooks, and particularly its $9.99 pricing, as a threat to their way of doing business.

By November 2009, Apple, Inc. ("Apple") had plans to release a new tablet computer, the iPad. Executives at the company saw an opportunity to sell ebooks on the iPad by creating a virtual marketplace on the device, which came to be known as the "iBookstore." Working within a tight timeframe, Apple went directly into negotiations with six of the major publishing companies in the United States. In two months, it announced that five of those companies—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster (collectively, the "Publisher Defendants")—had agreed to sell ebooks on the iPad under arrangements whereby the publishers had the authority to set prices, and could set the prices of new releases and *New York Times* bestsellers as high as $19.99 and $14.99, respectively. Each of these agreements, by virtue of its terms, resulted in each Publisher Defendant receiving *less* per ebook sold via Apple as opposed to Amazon, even given the higher consumer prices. Just a few months after the iBookstore opened, however, every one of the Publisher Defendants had taken control over pricing from Amazon and had raised the prices on many of their ebooks, most notably new releases and bestsellers.

The United States Department of Justice ("DOJ" or "Justice Department") and 33 states and territories (collectively, "Plaintiffs") filed suit in the United States District Court for the Southern District of New York, alleging that Apple, in launching the iBookstore, had conspired with the Publisher Defendants to raise prices across the nascent ebook market. This agreement, they argued, violated § 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 *et seq.* ("Sherman Act"), and state antitrust laws. All five Publisher Defendants settled and signed consent decrees, which prohibited them, for a period, from restricting ebook retailers' ability to set prices. Then, after a three-week bench trial, the district court (Cote, *J.*) concluded that, in order to induce the Publisher Defendants to participate in the iBookstore and to avoid the necessity of itself competing with Amazon over the retail price of ebooks, Apple orchestrated a conspiracy among the Publisher Defendants to raise the price of ebooks—particularly new releases and *New York Times* bestsellers. *United States v. Apple Inc.,* 952 F.Supp.2d 638, 647 (S.D.N.Y.2013). The district court found that the agreement constituted a *per se* violation of the Sherman Act and, in the alternative, unreasonably restrained trade under the rule of reason. …

BACKGROUND

I. Factual Background

We begin not with Kindles and iPads, but with printed "trade books," which are "general interest fiction and non-fiction" books intended for a broad readership. In the United States, the six largest publishers of trade books, known in the publishing world as the "Big Six," are Hachette, HarperCollins, Macmillan, Penguin, Random House, and Simon & Schuster. Together, the Big Six publish many of the biggest names in fiction and non-fiction; during 2010, their titles accounted for over 90% of the *New York Times* bestsellers in the United States.

For decades, trade book publishers operated under a fairly consistent business model. When a new book was ready for release to the public, the publisher would sell hardcover copies to retailers at a "wholesale" price and recommend resale to consumers at a markup, known as the "list" price. After the hardcover spent enough time on the shelves—often a year—publishers would release a paperback copy at lower "list" and "wholesale" prices. In theory, devoted readers would pay the higher hardcover price to read the book when it first came out, while more casual fans would wait for the paperback.

A. Amazon's Kindle

On November 19, 2007, Amazon released the Kindle: a portable electronic device that allows consumers to purchase, download, and read ebooks. … [I]n November 2009, Amazon was responsible for 90% of all ebook sales.

Amazon followed a "wholesale" business model similar to the one used with print books: publishers recommended a digital list price and received a wholesale price for each ebook that Amazon sold. In exchange, Amazon could sell the publishers' ebooks on the Kindle and determine the retail price. At least early on, publishers tended to recommend a digital list price that was about 20% lower than the print list price to reflect the fact that, with an ebook, there is no cost for printing, storing, packaging, shipping, or returning the books.

Where Amazon departed from the publishers' traditional business model was in the sale of new releases and *New York Times* bestsellers. Rather than selling more expensive versions of these books upon initial release (as publishers encouraged by producing hardcover books before paperback copies), Amazon set the Kindle price at one, stable figure—$9.99. At this price, Amazon was selling "certain" new releases and bestsellers at a price that "roughly matched," or was slightly lower than, the wholesale price it paid to the publishers. David Naggar, a Vice President in charge of Amazon's Kindle content, described this as a "classic loss-leading strategy" designed to encourage consumers to adopt the Kindle by discounting new releases and *New York Times* bestsellers and selling other ebooks without the discount. …

B. The Publishers' Reactions

Despite the small number of ebook sales compared to the overall market for trade books, top executives in the Big Six saw Amazon's $9.99 pricing strategy as a threat to their established way of doing business. Those executives included: Hachette and Hachette Livre Chief Executive Officers ("CEOs") David Young and Arnaud Nourry; HarperCollins CEO Brian Murray; Macmillan CEO John Sargent; Penguin USA CEO David Shanks; Random House Chief Operating Officer Madeline McIntosh; and Simon & Schuster President and CEO Carolyn Reidy. In the short term, these members of the Big Six thought that Amazon's lower-priced ebooks would make it more difficult for them to sell hardcover copies of new releases, "which were often priced," as the district court noted, "at thirty dollars or more," as well as *New York Times* bestsellers. Further down the road, the publishers feared that consumers would become accustomed to the uniform $9.99 price point for these ebooks, permanently driving down the price they could charge for print versions of the books. …

Conveniently, the Big Six operated in a close-knit industry and had no qualms communicating about the need to act together. As the district court found (based on the Publisher Defendants' own testimony), "[o]n a fairly regular basis, roughly once a quarter, the CEOs of the [Big Six] held dinners in the private dining rooms of New York restaurants, without counsel or assistants present, in order to discuss the common challenges they faced." Because they "did not compete with each other on price," but over authors and agents, the publishers "felt no hesitation in freely discussing Amazon's prices with each other and their joint strategies for raising those prices." Those strategies included eliminating the discounted wholesale price for ebooks and possibly creating an alternative ebook platform. …

C. Apple's Entry into the eBook Market

Apple is one of the world's most innovative and successful technology companies. Its hardware sells worldwide and supports major software marketplaces like iTunes and the App Store. But in 2009, Apple lacked a dedicated marketplace for ebooks or a hardware device that could offer an outstanding reading experience. The pending release of the iPad, which Apple intended to announce on January 27, 2010, promised to solve that hardware deficiency.

Eddy Cue, Apple's Senior Vice President of Internet Software and Services and the director of Apple's digital content stores, saw the opportunity for an ebook marketplace on the iPad. By February 2009, Cue and two colleagues—Kevin Saul and Keith Moerer—had researched the ebook market and concluded that it was poised for rapid expansion in 2010 and beyond. …

Operating under a tight timeframe, Cue, Saul, and Moerer streamlined their efforts by focusing on the Big Six publishers. They began by arming themselves with some important information about the state of affairs within the publishing industry. In particular, they learned that the publishers feared that Amazon's pricing model could change their industry … and that the industry as a whole was in a state of turmoil. "Apple understood," as the district court put it, "that the Publishers wanted to pressure Amazon to raise the $9.99 price point for e-books, that the Publishers were searching for ways to do that, and that they were willing to coordinate their efforts to achieve that goal." ...

D. Apple's Negotiations with the Publishers

1. Initial Meetings

Apple held its first meetings with each of the Big Six between December 15 and 16 [2009]. … Cue's team … expressed Apple's belief that Amazon's $9.99 price point was not ingrained in consumers' minds, and that Apple could sell new releases and *New York Times* bestsellers for somewhere between $12.99 and $14.99. In return, Apple requested that the publishers decrease their wholesale prices so that the company could make a small profit on each sale. …

2. The Agency Model

… Cue's team … abandoned the wholesale business model for a new, agency model. Unlike a wholesale model, in an agency relationship the *publisher* sets the price that consumers will pay for each ebook. Then, rather than the retailer paying the publisher for each ebook that it sells, the publisher pays the retailer a fixed percentage of each sale. In essence, the retailer receives a commission for distributing the publisher's ebooks. Under the system Apple devised, publishers would have the freedom to set ebook prices in the iBookstore, and would keep 70% of each sale. The remaining 30% would go to Apple as a commission. ..

[A]s Cue would later describe the plan to executives at Simon & Schuster, Macmillan, and Random House, the plan "solve[d] [the] Amazon issue" by allowing the publishers to wrest control over pricing from Amazon. On January 4 and 5, Apple sent essentially identical emails to each member of the Big Six to explain its agency model proposal.

3. The "Most–Favored–Nation" Clause

Cue's thoughts on the agency model continued to evolve after the emails on January 4 and 5. Most significantly, Saul—Cue's in-house counsel—devised an alternative to explicitly requiring publishers to switch other retailers to agency. This alternative involved the use of a "most-favored nation" clause ("MFN Clause" or "MFN"). In general, an MFN Clause is a contractual provision that requires one party to give the other the best terms that it makes available to any competitor. …. [T]he MFN would require the publisher to offer any ebook in Apple's iBookstore for no more than what the same ebook was offered elsewhere, such as from Amazon.

On January 11, Apple sent each of the Big Six a proposed eBook Agency Distribution Agreement (the "Contracts"). As described in the January 4 and 5 emails, these Contracts would split the proceeds from each ebook sale between the publisher and Apple, with the publisher receiving 70%, and would set price caps on ebooks at $14.99, $12.99, and $9.99 depending on the book's hardcover price. But unlike the initial emails, the Contracts contained MFN Clauses in place of the requirement that publishers move all other retailers to an agency model. Apple then assured each member of the Big Six that it was being offered the same terms as the others.…

The MFN Clause changed the situation by making it imperative, not merely desirable, that the publishers wrest control over pricing from ebook retailers generally. Under the MFN, if Amazon stayed at a wholesale model and continued to sell ebooks at $9.99, the publishers would be forced to sell in the iBookstore, too, at that same $9.99 price point. The result would be the worst of both worlds: *lower* short-term revenue and *no* control over pricing. The publishers recognized that, as a practical matter, this meant that the MFN Clause would force them to move Amazon to an agency relationship. …

Thus, the terms of the negotiation between Apple and the publishers became clear: Apple wanted quick and successful entry into the ebook market and to eliminate retail price competition with Amazon. In exchange, it offered the publishers an opportunity "to confront Amazon as one of an organized group ... united in an effort to eradicate the $9.99 price point." Both sides needed a critical mass of publishers to achieve their goals. The MFN played a pivotal role in this *quid pro* *quo* by "stiffen[ing] the spines of the [publishers] to ensure that they would demand new terms from Amazon," and protecting Apple from retail price competition.

4. Final Negotiations

The proposed Contracts sparked intense negotiations as Cue's team raced to assemble enough publishers to announce the iBookstore by January 27. …

Correspondence from within the publishing companies also shows that Cue promoted the proposal as the "best chance for publishers to challenge the 9.99 price point," and emphasized that Apple would "not move forward with the store [unless] 5 of the 6 [major publishers] signed the agreement." As Cue said at trial, he attempted to "assure [the publishers] that they weren't going to be alone, so that [he] would take the fear awa[y] of the Amazon retribution that they were all afraid of." "The Apple team reminded the Publishers," as the district court found, "that this was a rare opportunity for them to achieve control over pricing." …

As the district court found, during the period in January during which Apple concluded its agreements with the Publisher Defendants, "Apple kept the Publisher Defendants apprised about who was in and how many were on board." The Publisher Defendants also kept in close communication. As the district court noted, "[i]n the critical negotiation period, over the three days between January 19 and 21, Murray, Reidy, Shanks, Young, and Sargent called one another 34 times, with 27 calls exchanged on January 21 alone."

By the January 27 iPad launch, five of the Big Six—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster—had agreed to participate in the iBookstore. The lone holdout, Random House, did not join because its executives believed it would fare better under a wholesale pricing model and were unwilling to make a complete switch to agency pricing. Steve Jobs announced the iBookstore as part of his presentation introducing the iPad. When asked after the presentation why someone should purchase an ebook from Apple for $14.99 as opposed to $9.99 with Amazon or Barnes & Noble, Jobs confidently replied, "[t]hat won't be the case ... the price will be the same.... [P]ublishers will actually withhold their [e]books from Amazon ... because they are not happy with the price." A day later, Jobs told his biographer the publishers' position with Amazon: "[y]ou're going to sign an agency contract or we're not going to give you the books."

E. Negotiations with Amazon

Jobs's boast proved to be prophetic. While the Publisher Defendants were signing Apple's Contracts, they were also informing Amazon that they planned on changing the terms of their agreements with it to an agency model. However, their move against Amazon began in earnest on January 28, the day after the iPad launch. That afternoon, John Sargent flew to Seattle to deliver an ultimatum on behalf of Macmillan: that Amazon would switch its ebook sales agreement with Macmillan to an agency model or suffer a seven-month delay in its receipt of Macmillan's new releases. …

The other publishers who had joined the iBookstore quickly followed Macmillan's lead. … By March 2010, Macmillan, HarperCollins, Hachette, and Simon & Schuster had completed agency agreements with Amazon. … Penguin completed its deal in June …

F. Effect on eBook Prices

As Apple and the Publisher Defendants expected, the iBookstore price caps quickly became the benchmark for ebook versions of new releases and *New York Times* bestsellers. …

The Apple price caps also had a ripple effect on the rest of the Publisher Defendants' catalogues. Recognizing that Apple's price caps were tied to the price of hardcover books, many of these publishers increased the prices of their newly released *hardcover* books to shift the ebook version into a higher price category. Furthermore, because the Publisher Defendants who switched to the agency model expected to make less money per sale than under the wholesale model, they also increased the prices on their ebooks that were *not* new releases or bestsellers to make up for the expected loss of revenue. Based on data from February 2010—just before the Publisher Defendants switched Amazon to agency pricing—to February 2011, an expert retained by the Justice Department observed that the weighted average price of the Publisher Defendants' new releases increased by 24.2%, while bestsellers increased by 40.4%, and other ebooks increased by 27.5%, for a total weighted average ebook price increase of 23.9%. Indeed, even Apple's expert agreed, noting that, over a two-year period, the Publisher Defendants increased their average prices for hardcovers, new releases, and other ebooks.

Increasing prices reduced demand for the Publisher Defendants' ebooks. …

II. Procedural History

… Hachette, HarperCollins, and Simon & Schuster agreed to settle with DOJ by signing consent decrees on the same day that the Justice Department filed its complaint. … The remaining Publisher Defendants, Penguin and Macmillan, settled in quick succession.

Unlike the Publisher Defendants, Apple opted to take the case to trial. … On July 10, 2013, after conducting a three-week bench trial, the district court concluded that Apple had violated § 1 of the Sherman Act and various state antitrust laws. In brief, the court found that Apple "orchestrat[ed]" a conspiracy among the Publisher Defendants to "eliminate retail price competition [in the e-book market] in order to raise the retail prices of e-books." Because this conspiracy consisted of a group of competitors—the Publisher Defendants—assembled by Apple to increase prices, it constituted a "horizontal price-fixing conspiracy" and was a *per se* violation of the Sherman Act. ...

DISCUSSION

To hold a defendant liable for violating § 1 of the Sherman Act, a district court must find "a combination or some form of concerted action between at least two legally distinct economic entities" that "constituted an unreasonable restraint of trade." *Capital Imaging Assocs. v. Mohawk Valley Med. Assocs.,* 996 F.2d 537, 542 (2d Cir.1993); *see* 15 U.S.C. § 1. …

II. Apple's Liability Under § 1

This appeal requires us to address the important distinction between "horizontal" agreements to set prices, which involve coordination "between competitors at the same level of [a] market structure," and "vertical" agreements on pricing, which are created between parties "at different levels of [a] market structure." *Anderson News, L.L.C. v. Am. Media, Inc.,* 680 F.3d 162, 182 (2d Cir.2012) (internal quotation marks omitted). Under § 1 of the Sherman Act, the former are, with limited exceptions, *per se* unlawful, while the latter are unlawful only if an assessment of market effects, known as a rule-of-reason analysis, reveals that they unreasonably restrain trade. *See Leegin Creative Leather Prods., Inc. v. PSKS, Inc.,* 551 U.S. 877, 893 (2007).

Although this distinction is sharp in theory, determining the orientation of an agreement can be difficult as a matter of fact and turns on more than simply identifying whether the participants are at the same level of the market structure. For instance, courts 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."

Howard Hess Dental Labs. Inc. v. Dentsply Int'l, Inc., 602 F.3d 237, 255 (3d Cir.2010); *see also Toys "R" Us, Inc. v. FTC,* 221 F.3d 928, 932–34 (7th Cir.2000). 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." VI Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 1402c (3d ed.2010) (citing *PepsiCo, Inc. v. Coca–Cola Co.,* 315 F.3d 101 (2d Cir.2002)); *see also* Am. Bar Ass'n, *Antitrust Law Developments* 24–26 (6th ed.2007); XII Areeda & Hovenkamp, *supra,* ¶ 2004c.

Apple characterizes its Contracts with the Publisher Defendants as a series of parallel but independent vertical agreements, a characterization that forms the basis for its two primary arguments against the district court's decision. First, Apple argues that the district court impermissibly inferred its involvement in a horizontal price-fixing conspiracy from the Contracts themselves. Because (in Apple's view) the Contracts were vertical, lawful, and in Apple's independent economic interest, the mere fact that Apple agreed to the same terms with multiple publishers cannot establish that Apple consciously organized a conspiracy among the Publisher Defendants to raise consumer-facing ebook prices—even if the *effect* of its Contracts was to raise those prices. Second, Apple argues that, even if it did orchestrate a horizontal price-fixing conspiracy, its conduct should not be subject to *per se* condemnation. According to Apple, proper application of the rule of reason reveals that its conduct was not unlawful. …

A. The Conspiracy with the Publisher Defendants

Apple portrays its Contracts with the Publisher Defendants as, at worst, "unwittingly facilitat[ing]" their joint conduct. All Apple did, it claims, was attempt to enter the market on profitable terms by offering contractual provisions—an agency model, the MFN Clause, and tiered price caps—which ensured the company a small profit on each ebook sale and insulated it from retail price competition. This had the *effect* of raising prices because it created an incentive for the Publisher Defendants to demand that Amazon adopt an agency model and to seize control over consumer-facing ebook prices industry-wide. But although Apple knew that its contractual terms would entice the Publisher Defendants (who wanted to do away with Amazon's $9.99 pricing) to seek control over prices from Amazon and other ebook retailers, Apple's success in capitalizing on the Publisher Defendants' preexisting incentives, it contends, does not suggest that it joined a *conspiracy* among the Publisher Defendants to raise prices….

We disagree. At the start, Apple's benign portrayal of its Contracts with the Publisher Defendants is not persuasive—not because those Contracts themselves were independently unlawful, but because, in context, they provide strong evidence that Apple consciously orchestrated a conspiracy among the Publisher Defendants. …

Apple offered each Big Six publisher a proposed Contract that would be attractive only if the publishers acted collectively. Under Apple's proposed agency model, the publishers stood to make *less* money per sale than under their wholesale agreements with Amazon, but the Publisher Defendants were willing to stomach this loss because the model allowed them to sell new releases and bestsellers for more than $9.99. Because of the MFN Clause, however, each new release and bestseller sold in the iBookstore would cost only $9.99 as long as Amazon continued to sell ebooks at that price. So in order to receive the perceived benefit of Apple's proposed Contracts, the Publisher Defendants had to switch *Amazon* to an agency model as well—something no individual publisher had sufficient leverage to do on its own. Thus, each Publisher

Defendant would be able to accomplish the shift to agency—and therefore have an incentive to sign Apple's proposed Contracts—*only* if it acted in tandem with its competitors. *See Starr,* 592 F.3d at 324; *Flat Glass,* 385 F.3d at 360–61. By the very act of signing a Contract with Apple containing an MFN Clause, then, each of the Publisher Defendants signaled a clear commitment to move against Amazon, thereby facilitating their collective action. …

As a sophisticated negotiator, Apple was fully aware that its proposed Contracts would entice a critical mass of publishers only if these publishers perceived an opportunity collectively to shift Amazon to agency. In fact, this was the very purpose of the MFN, which Apple's Saul devised as an elegant alternative to a provision that would have explicitly *required* the publishers to adopt an agency model with other retailers. …

That the Publisher Defendants were in constant communication regarding their negotiations with both Apple and Amazon can hardly be disputed. Indeed, Apple never seriously argues that the Publisher Defendants were not acting in concert. …

Even if Apple was unaware of the extent of the Publisher Defendants' coordination when it first approached them, its subsequent communications with them as negotiations progressed show that Apple consciously played a key role in organizing their express collusion. From the outset, Cue told the publishers that Apple would launch its iBookstore only if a sufficient number of them agreed to participate and that each publisher would receive identical terms, assuring them that a critical mass of major publishers would be prepared to move against Amazon. …

Apple's involvement in the conspiracy continued even past the signing of its agency agreements. Before Sargent flew to Seattle to meet with Amazon, he told Cue. Apple stayed abreast of the Publisher Defendants' progress as they set coordinated deadlines with Amazon and shared information with one another during negotiations. …

[I]t is well established that vertical agreements, lawful in the abstract, can in context "be useful evidence for a plaintiff attempting to prove the existence of a horizontal cartel," *Leegin,* 551 U.S. at 893, particularly where multiple competitors sign vertical agreements that would be against their own interests were they acting independently, *see, e.g., Interstate Circuit v. United States,* 306 U.S. 208, 222 (1939); *Toys "R" Us,* 221 F.3d at 935–36. The MFNs in Apple's Contracts created a set of economic incentives pursuant to which the Contracts were only attractive to the Publisher Defendants to the extent they acted collectively.

… Having concluded that the district court correctly identified an agreement between Apple and the Publisher Defendants to raise consumer-facing ebook prices, we turn to Apple's … arguments that this agreement did not violate § 1 of the Sherman Act.

B. Unreasonable Restraint of Trade

… Horizontal price-fixing conspiracies traditionally have been, and remain, the "archetypal example" of a *per se* unlawful restraint on trade. *Catalano, Inc. v. Target Sales, Inc.,* 446 U.S. 643, 647 (1980). By contrast, the Supreme Court in recent years has clarified that vertical restraints—including those that restrict prices—should generally be subject to the rule of reason. *See Leegin,* 551 U.S. at 882 (holding that the rule of reason applies to vertical minimum price-fixing); *Khan,* 522 U.S. at 7 (holding that the rule of reason applies to vertical maximum price-fixing). …

1. Whether the *Per Se* Rule Applies

a. Horizontal Agreement

… [T]he Supreme Court and our Sister Circuits have held all participants in "hub-and-spoke" conspiracies liable when the objective of the conspiracy was a *per se* unreasonable restraint of trade. …

[W]hen the Supreme Court has applied the rule of reason to vertical agreements, it has explicitly distinguished situations in which a vertical player organizes a horizontal cartel. … A horizontal conspiracy can use vertical agreements to facilitate coordination without the other parties to those agreements knowing about, or agreeing to, the horizontal conspiracy's goals. For example, a cartel of manufacturers could ensure compliance with a scheme to fix prices by having every member "require its dealers to adhere to specified resale prices." VIII Areeda & Hovenkamp, *supra,* ¶ 1606b. … [W]here the vertical organizer has not only committed to vertical agreements, but has also agreed to participate in the horizontal conspiracy …, the court need not consider whether the vertical agreements restrained trade because all participants agreed to the horizontal restraint, which is "and ought to be, *per se* unlawful." *Id.*

In short, the relevant "agreement in restraint of trade" in this case is the price-fixing conspiracy identified by the district court, not Apple's vertical contracts with the Publisher Defendants. How the law might treat Apple's vertical agreements in the absence of a finding that Apple agreed to create the horizontal restraint is irrelevant. Instead, the question is whether the vertical organizer of a horizontal conspiracy designed to raise prices has agreed to a restraint that is any less anticompetitive than its co-conspirators, and can therefore escape *per se* liability. We think not.

c. Price–Fixing Conspiracy

… Apple and its amici argue that the horizontal agreement among the publishers was not actually a "price-fixing" conspiracy that deserves *per se* treatment in the first place. But it is well established that *per se* condemnation is not limited to agreements that literally set or restrict prices. Instead, any conspiracy "formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity ... is illegal per se," and the precise "machinery employed ... is immaterial." *Socony–Vacuum Oil,* 310 U.S. at 223; *see also Catalano,* 446 U.S. at 647–48 (collecting cases); XII Areeda & Hovenkamp, *supra,* ¶ 2022a, d. The conspiracy among Apple and the Publisher Defendants comfortably qualifies as a horizontal price-fixing conspiracy.

As we have already explained, the Publisher Defendants' primary objective in expressly colluding to shift the entire ebook industry to an agency model (with Apple's help) was to eliminate Amazon's $9.99 pricing for new releases and bestsellers, which the publishers believed threatened their short-term ability to sell hardcovers at higher prices and the long-term consumer perception of the price of a new book. They had grown accustomed to a business in which they rarely competed with one another on price and could, at least partially, control the price of new releases and bestsellers by releasing hardcover copies before paperbacks. Amazon, and the ebook, upset that model, and reduced prices to consumers by eliminating the need to print, store, and ship physical volumes. Its $9.99 price point for new releases and bestsellers represented a small loss on a small percentage of its sales designed to encourage consumers to adopt the new technology.

Faced with downward pressure on prices but unconvinced that withholding books from Amazon was a viable strategy, the Publisher Defendants—their coordination orchestrated by Apple—combined forces to grab control over price. Collectively, the Publisher Defendants accounted for 48.8% of ebook sales in 2010. Once organized, they had sufficient clout to demand control over pricing, in the form of agency agreements, from Amazon and other ebook distributors. This control over pricing facilitated their ultimate goal of raising ebook prices to the price caps. *See*

VIII Areeda & Hovenkamp, *supra,* ¶ 1606b ("Even when specific prices are not agreed upon, an express horizontal agreement that each manufacturer will use resale price maintenance or other distribution restraints should be illegal. Its only business function is to facilitate price coordination among manufacturers."). In other words, the Publisher Defendants took by collusion what they could not win by competition. And Apple used the publishers' frustration with Amazon's $9.99 pricing as a bargaining chip in its negotiations and structured its Contracts to coordinate their push to raise prices throughout the industry. A coordinated effort to raise prices across the relevant market was present in every chapter of this story.

This conspiracy to raise prices also had its intended effect. Immediately after the Publisher Defendants switched Amazon to an agency model, they increased the Kindle prices of 85.7% of their new releases and 96.8% of their *New York Times* bestsellers to within 1% of the Apple price caps. They also increased the prices of their other ebook offerings. Within two weeks of the move to agency, the weighted average price of the Publisher Defendants' ebooks—which accounted for just under half of all ebook sales in 2010—had increased by 18.6%, while the prices for Random House and other publishers remained relatively stable.

This sudden increase in prices reduced ebook sales by the Publisher Defendants and proved to be durable. One analysis compared two-week periods before and after the Publisher Defendants took control over pricing and found that they sold 12.9% fewer ebooks after the switch. Another expert for Plaintiffs conducted a regression analysis, which showed that, over a six-month period following the switch, the Publisher Defendants sold 14.5% fewer ebooks than they would have had the price increases not occurred. Nonetheless, ebook prices for the Publisher Defendants over those six months, controlling for other factors, remained 16.8% higher than before the switch. And even Apple's expert produced a chart showing that the Publisher Defendants' prices for new releases, bestsellers, and other offerings remained elevated a full two years after they took control over pricing.

Apple points out that, in the two years following the conspiracy, prices across the ebook market as a whole fell slightly and total output increased. However, when the agreement at issue involves price fixing, the Supreme Court has consistently held that courts need not even conduct an extensive analysis of "market power" or a "detailed market analysis" to demonstrate its anticompetitive character. *FTC v. Ind. Fed'n of Dentists,* 476 U.S. 447, 460 (1986); *see also Nat'l Soc'y of Prof'l Eng'rs v. United States,* 435 U.S. 679, 692–93 (1978). …

Moreover, Apple's evidence regarding long-term growth and prices in the ebook industry is not inconsistent with the conclusion that the price-fixing conspiracy succeeded in actually raising prices. The popularization of ebooks fundamentally altered the publishing industry by eliminating many of the marginal costs associated with selling books. When Apple launched the iBookstore just two years after Amazon introduced the Kindle, the ebook market was *already* experiencing rapid growth and falling prices, and those trends were expected to continue. The district court found that the Publisher Defendants' collective move to retake control of prices—and to eliminate Amazon's $9.99 price point for new releases and *New York Times* bestsellers—tapped the brakes on those trends, causing prices to rise across their offerings and slowing their sales growth relative to other publishers. No court can presume to know the proper price of an ebook, but the long judicial experience applying the Sherman Act has shown that "[a]ny combination which tampers with price structures ... would be directly interfering with the free play of market forces." *Socony–Vacuum Oil,* 310 U.S. at 221; *see also Arizona v. Maricopa Cnty. Med. Soc'y,* 457 U.S. 332, 346 (1982). By setting new, durable prices through collusion rather than competition, Apple and the Publisher Defendants imposed their view of proper pricing, supplanting the market's free play. This evidence, viewed in conjunction with the district court's findings as to and analysis of the conspiracy's history and purpose, is sufficient to support the conclusion that the agreement to raise ebook prices was a *per se* unlawful price-fixing conspiracy. …

NOTES AND QUESTIONS

1. Under the contracts between Apple and publishers, the publishers received less per ebook than under the traditional distribution model with Amazon. Why is this fact suspicious from an antitrust perspective? Why would publishers conspire to receive less money per ebook?
2. In dissent, Judge Jacobs argued that the per se rule did not apply and asserted that "Apple's conduct, assessed under the rule of reason on the horizontal plane of retail competition, was unambiguously and overwhelmingly pro-competitive." The judge reasoned that "Apple took steps to compete with a monopolist and open the market to more entrants, generating only minor competitive restraints in the process. Its conduct was eminently reasonable; no one has suggested a viable alternative." He concluded that "Application of the rule of reason easily absolves Apple of antitrust liability." In her opinion, Judge Livingston argued that Apple's conduct violated the rule of reason. Judge Lohier, however, declined to sign on to this part of Judge Livingston's opinion. Thus, no majority opinion exists on this issue. Which judge's approach do you think is most appropriate?
3. The *Apple* case is an example of a hub-and-spoke conspiracy. The Ninth Circuit has explained that "[a] traditional hub-and-spoke conspiracy has three elements: (1) a hub, such as a dominant purchaser; (2) spokes, such as competing manufacturers or distributors that enter into vertical agreements with the hub; and (3) the rim of the wheel, which consists of horizontal agreements among the spokes." In re Musical Instruments & Equip. Antitrust Litig., 798 F.3d 1186, 1192 (9th Cir. 2015). How are these components present in *Apple*?
4. The term "hub-and-spoke conspiracy" is relatively recent, but hub-and-spoke conspiracies are older than the Sherman Act itself. *See, e.g.*, Benjamin Klein, *The "Hub-and-Spoke" Conspiracy That Created the Standard Oil Monopoly*, 85 S. CAL. L. REV. 459 (2012).
5. Hub-and-spoke conspiracies are not limited to price fixing. Toys "R" Us (TRU) served as the hub of a hub-and-spoke conspiracy involving a group boycott. TRU pressured toy manufacturers to stop selling certain items through warehouse clubs. While each agreement between TRU and its supplier was a vertical agreement, "TRU orchestrated a horizontal agreement among its key suppliers to boycott the clubs." Toys "R" Us, Inc. v. F.T.C., 221 F.3d 928 (7th Cir. 2000). This horizontal component was necessary because "key toy manufacturers were unwilling to refuse to sell to or discriminate against the clubs unless they were assured that their competitors would do the same…" Matter of Toys R Us, Inc., 126 F.T.C. 415, 574 (1998), *aff'd* Toys "R" Us, Inc. v. F.T.C., 221 F.3d 928 (7th Cir. 2000). The Seventh Circuit noted that the TRU-orchestrated boycott "was remarkably successful in causing the 10 major toy manufacturers to reduce output of toys to the warehouse clubs, and that reduction in output protected TRU from having to lower its prices to meet the clubs' price levels." As a result, TRU was liable for a

horizontal conspiracy even though it was not in a horizontal relationship with any of its co-conspirators.

p. 283, replace the first full paragraph with the following:

Although antitrust agencies generally challenge MFN clauses under the rule of reason, not the per se rule, the Second Circuit's *United States v. Apple* opinion, 791 F.3d 290 (2d Cir. 2015), excerpted above, shows how MFN clauses can play an important part in per se violations of the Sherman Act. In that case, publishers of electronic books (ebooks) wanted to increase the price above the $9.99 per e-book that Amazon was charging. Apple wanted to enter the retail market for e-books but not at the $9.99 price point. Apple conspired with the publishers to construct an agency model that nominally gave the publishers the ability to set the resale price of ebooks – while giving Apple a 30% commission on e-book sales – but allowed Apple to set a price cap of $12.99 and $14.99 for bestsellers and electronic versions of higher-priced hardbacks. To prevent Apple from being undersold, in each of its contracts with a publisher, Apple included a most-favored-nation (MFN) clause, which gave Apple the ability to match the lowest retail price listed by any competing seller of e-books. This forced the publishers to impose the agency model on other e-book retailers, including Amazon, because if Amazon sold ebooks at a lower price than Apple then the MFN would force the publishers to charge the same low price through Apple. The arrangement succeeded in increasing the price of ebooks. The Second Circuit held that Apple committed a per se violation of Section One. Thus, although MFN clauses themselves are not inherently illegal, they can play a critical role in an overall conspiracy that is per se illegal.

[C] Proof of Agreement

[2] Conscious Parallelism and the *Interstate Circuit* Doctrine

p. 292, append this note:

3. In *In re Urethane Antitrust Litigation*, 768 F.3d 1245 (10th Cir. 2014), the Tenth Circuit affirmed a jury verdict that Dow had conspired with its competitors to fix prices for polyurethane chemical products. On appeal, Dow argued that "there was insufficient evidence that the alleged price-fixing agreement was effectively implemented." *Id*. at 1263. The Tenth Circuit rejected this contention:

> The argument rests on a purported distinction between two categories of price-fixing conspiracies: (1) those involving an agreement to set prices directly, and (2) those involving an agreement to announce price increases and try to make them stick. Conspiracies falling into the second category, Dow submits, require an evidentiary link between the price-increase announcements and subsequent prices. According to Dow, this evidentiary link is necessary because parallel price-increase announcements do not prove a conspiracy.
>
> For the sake of argument, we can assume that evidence of parallel price-increase announcements would not establish a price-fixing conspiracy. But the plaintiffs did more than show parallel announcements. The evidence included admissions by industry

insiders, collusive behavior, susceptibility of the industry to collusion, and setting of prices at a supra-competitive level.

For example, the plaintiffs presented testimony by Ms. Stephanie Barbour (Dow), who admitted that Dow had participated in a price-fixing conspiracy. Ms. Barbour directly implicated at least three Dow executives in the conspiracy: Mr. Marco Levi, Mr. David Fischer, and Mr. Peter Davies.

Another key witness for the plaintiffs was Mr. Lawrence Stern (Bayer), who recounted numerous conversations he had had with his counterparts at Dow, BASF, and Huntsman. Mr. Stern described these conversations as "inappropriate," for they pertained to future pricing and "the possibility of raising prices." …

Mr. Stern also testified that he had taken "unusual steps" to conceal his conversations with Bayer's competitors. For instance, he would use pay telephones instead of calling from his office and would use a prepaid phone card. Other times, Mr. Stern met with competitors at off-site locations, such as coffee shops or hotels. Commenting on these secretive communications, the plaintiffs' expert econometrician told the jury that "economists associate secrecy with collusion."

Testimony about a conspiracy also came from others, [including Dow's alleged co-conspirators] ...

The jury also heard from the plaintiffs' expert, Dr. John Solow, who testified about: (1) collusive conduct he had observed in the polyurethane industry, and (2) the industry's susceptibility to collusion.

Dr. Solow had observed four types of collusive conduct.

First, the defendant companies had issued "a series of ... lockstep price increase announcements," which came within weeks of each other, communicated the same or similar price increases, and were to take effect at about the same time.

Second, Dr. Solow noticed "a widespread pattern of communication" among the top executives of the defendant companies. Dr. Solow was struck not only by the frequency and secrecy of these communications but also by their timing, for the contacts frequently occurred within days of a lockstep price-increase announcement. This proximity suggested that the price-increase announcements had been coordinated.

Third, Dr. Solow detected a "price over volume strategy," where the companies would stick to their list prices even if it meant walking away from opportunities to earn business or make sales at lower, but still profitable, prices. In Dr. Solow's view, these actions would not take place in a competitive market and the companies were acting contrary to their interests.

> Fourth, the defendant companies monitored one another to prevent cheating and to discipline any supplier that was found cheating.
>
> Dr. Solow also testified that the polyurethane industry was "ripe for collusion" based on six features:
>
> > 1. Sales of polyurethane products were "concentrated in the hands of only a handful of firms" during the conspiracy period;
> >
> > 2. the market had high barriers to entry;
> >
> > 3. polyurethane products are homogenous;
> >
> > 4. there were no close product substitutes available to customers;
> >
> > 5. there was excess capacity for MDI, TDI, and polyether polyols during the conspiracy period, meaning that the companies could "produce more output than the customers actually want[ed] to buy," putting a "strong downward pressure on prices;" and
> >
> > 6. the industry has several trade associations, which provided "an opportunity to engage in price fixing behavior."
>
> … The evidence, viewed favorably to the plaintiffs, goes beyond parallel announcements of price increases.

Id. at 1264-65.

The Tenth Circuit also affirmed the jury's award of over $400 million in damages, which were trebled to over $1.2 billion.

[3] Surviving a Motion to Dismiss

p. 306, append these notes:

5. After having its decision to deny the defendants' motion to dismiss affirmed by the Seventh Circuit, the district court in *In re Text Messaging Antitrust Litigation* granted the defendants' motion for summary judgment. 46 F. Supp. 3d 788 (N.D. Ill. 2014). The Seventh Circuit again affirmed. 782 F.3d 867 (7th Cir. 2015). The opinion is excerpted below.

6. In *Evergreen Partnering Group, Inc. v. Pactiv Corp.*, 720 F.3d 33 (1st Cir. 2013), the First Circuit vacated a district court's dismissal of a claim by Evergreen Partnering Group that its rivals had conspired to boycott its recycled polystyrene packaging by "withholding positive information about the success of Evergreen's earlier recycling programs, promoting a sham competitor, and disseminating false information to the

public about the cost-effectiveness of Evergreen's closed-loop recycling method." *Id*. at 40. After rejecting the need to evaluate the sufficiency of Evergreen's evidence at the dismissal stage, the First Circuit characterized the "slow influx of unreasonably high pleading requirements at the earliest stages of antitrust litigation" as a misinterpretation of *Twombly*. Because *Twombly* "'does not impose a probability requirement at the pleading stage,'" the First Circuit opined that courts at the pleading stage should not decide "which inferences are more plausible than other competing inferences, since those questions are properly left to the factfinder." *Id*. at 45 (quoting *Twombly*).

7. In *SD3, LLC v. Black & Decker (U.S.) Inc.*, 801 F.3d 412 (4th Cir. 2015), the Fourth Circuit reversed the district court's dismissal of plaintiff's group boycott claim. Plaintiff SawStop claimed that several major table-saw manufacturers conspired to boycott SawStop's safety technology. The Fourth Circuit cautioned against misreading *Twombly* as a probability standard, explaining that "[w]hen a court confuses probability and plausibility, it inevitably begins weighing the competing inferences that can be drawn from the complaint." The court concluded that the plaintiff sufficiently alleged a plausible agreement among the defendants to engage in a group boycott because the complaint told a detailed story, including alleging "the particular time, place, and manner in which the boycott initially formed," naming "at least six specific individuals who took part in forming the boycott," and "explain[ing] how the manufacturers implemented the boycott."

[4] Surviving a Motion for Summary Judgment

p. 346, append this note and the following case excerpt:

6. In *Hyland v. HomeServices of Am., Inc.*, 771 F.3d 310 (6th Cir. 2014), a group of home sellers brought class action litigation that characterized the 6% commission rate charged by real estate firms as price fixing in violation of Section One of the Sherman Act. The Sixth Circuit noted that the "court has set out the following considerations, sometimes referred to as 'plus factors,' in determining when circumstantial evidence amounts to a finding of concerted action: 1) whether defendants' actions, if taken independently, would be contrary to their economic interests; 2) product uniformity; 3) whether the defendants have been uniform in their actions; 4) whether the defendants have exchanged or have had the opportunity to exchange information relative to the alleged conspiracy; and 5) whether the defendants have a common motive to conspire or have engaged in a large number of communications." *Id*. at 320. The Sixth Circuit affirmed summary judgment for the defendants because, although the plaintiff presented "a good deal of circumstantial evidence that supports its theory of collusion," the plaintiff did not "counter[] the conclusion reached by the district court that the conduct at issue was also consistent with permissible competition and therefore does not support an inference of antitrust conspiracy." *Id*. at 322. If the evidence is susceptible to two different reasonable interpretations, should the plaintiff be able to present its case to the jury? Why or why not?

7. In *In re Chocolate Confectionary Antitrust Litigation*, 801 F.3d 383 (3d Cir. 2015), the Sixth Circuit affirmed the district court's grant of summary judgment to defendants accused of fixing prices of chocolate products. The Sixth Circuit noted that in a concentrated market, firms may maintain supracompetitive prices through interdependent decision-making, without any agreement, if they each "independently conclude that the industry as a whole would be better off by raising prices." Applying these insights to the alleged facts, the court concluded that "[e]vidence of a disconnected foreign conspiracy, limited possession of advance pricing information, mere opportunities to conspire without suspect meetings or conversations about pricing, conduct that is consistent with pre-conspiracy conduct, and a weak showing of pretext do not support a reasonable inference of a conspiracy."

8. In *Dairy Farmers of America, Inc. Cheese Antitrust Litigation*, 801 F.3d 758 (7th Cir. 2015), the Seventh Circuit affirmed the district court's grant of summary judgment to defendants accused of conspiring to manipulate the price of certain milk futures on the Chicago Mercantile Exchange. Defendants had met regularly for various business purposes and had discussed "market conditions and forecasts." The Seventh Circuit concluded that the evidence of agreement among defendants was ambiguous because the communications at issue "could be understood as a part of a legitimate business relationship as readily as they could be understood as a part of a conspiracy." Finding the evidence of conspiracy ambiguous, the court, citing *Twombly*, looked for any evidence tending to exclude the possibility that the defendants were pursuing independent interests though their interactions. The court found that the parallel conduct cited by plaintiffs was not enough to exclude the possibility that one of the defendant's (Schreiber) was pursuing its own interests in restoring certain price spreads. The Seventh Circuit therefore concluded that plaintiffs had failed to raise an issue of material fact as to conspiracy and upheld the district court's grant of summary judgment to defendants.

IN RE TEXT MESSAGING ANTITRUST LITIGATION

782 F.3d 867 (7th Cir. 2015)

Posner, Circuit Judge.

This class action antitrust suit is before us for the second time. More than four years ago we granted the defendants' petition to take an interlocutory appeal (see 28 U.S.C. § 1292(b)) from the district judge's refusal to dismiss the complaint for failure to state a claim. But we upheld the judge's ruling. *In re Text Messaging Antitrust Litigation,* 630 F.3d 622 (7th Cir.2010). Three years of discovery ensued, culminating in the district judge's grant of the defendants' motion for summary judgment, followed by entry of final judgment dismissing the suit, precipitating this appeal by the plaintiffs.

The suit is on behalf of customers of text messaging—the sending of brief electronic messages between two or more mobile phones or other devices, over telephone systems (usually wireless systems), mobile communications systems, or the Internet. (The most common method of text messaging today is to type the message into a cellphone, which transmits it instantaneously over a telephone or other communications network to a similar device.) Text messaging is thus an alternative both to email and to telephone calls. The principal defendants are four wireless network providers—AT & T, Verizon, Sprint, and T–Mobile—and a trade association, The Wireless Association, to which those companies belong. The suit claims that the defendants, in violation of section 1 of the Sherman Act, 15 U.S.C. §§ 1 *et seq.,* conspired with each other to increase one kind of price for text messaging service—price per use (PPU), each "use" being a message, separately priced. This was the original method of pricing text messaging; we'll see that it has largely given way to other methods, but it still has some customers and they are the plaintiffs and the members of the plaintiff class.

The defendants' unsuccessful motion to dismiss the complaint—the motion the denial of which we reviewed and upheld in the first appeal—invoked *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544 (2007), which requires a complaint to pass a test of "plausibility" in order to avoid dismissal. The reason for this requirement is to spare defendants the burden of a costly defense against charges likely to prove in the end to have no merit. We decided that the plaintiffs' second amended complaint passed the test … [W]e pointed to the small number of leading firms in the text messaging market, which would facilitate concealment of an agreement to fix prices; to the alleged exchanges of price information, orchestrated by the firms' trade association; to the seeming anomaly of a price increase in the face of falling costs; and to the allegation of a sudden simplification of pricing structures followed very quickly by uniform price increases.

With dismissal of the complaint refused and the suit thus alive in the district court, the focus of the lawsuit changed to pretrial discovery by the plaintiffs, which in turn focused on the alleged price exchange through the trade association and the sudden change in pricing structure followed by uniform price increases. Other factors mentioned in our first opinion—the small number of firms, and price increases in the face of falling costs—were conceded to be present but could not be thought dispositive. It is true that if a small number of competitors dominates a market, they will find it safer and easier to fix prices than if there are many competitors of more or less equal size. For the fewer the conspirators, the lower the cost of negotiation and the likelihood of defection; and provided that the fringe of competitive firms is unable to expand output sufficiently to drive the price back down to the competitive level, the leading firms can fix prices without worrying about competition from the fringe. But the other side of this coin is that the fewer the firms, the easier it is for them to engage in "follow the leader" pricing ("conscious parallelism," as lawyers call it, "tacit collusion" as economists prefer to call it)—which means coordinating their pricing without an actual agreement to do so. As for the apparent anomaly of competitors' raising prices in the face of falling costs, that is indeed evidence that they are not competing in the sense of trying to take sales from each other. However, this may be not because they've agreed not to compete but because all of them have determined independently that they may be better off with a higher price. That higher price, moreover—the consequence of parallel but independent decisions to raise prices—may generate even greater profits (compared to competitive pricing) if costs are falling, provided that consumers do not have attractive alternatives.

Important too is the condition of entry. If few firms can or want to enter the relevant market, a higher price generating higher profits will not be undone by the output of new entrants. Indeed, prospective entrants may be deterred from entering by realization that their entry might lead simply to a drastic fall in prices that would deny them the profits from having entered. And that drastic fall could well be the result of parallel but independent pricing decisions by the incumbent firms, rather than of agreement.

The challenge to the plaintiffs in discovery was thus to find evidence that the defendants had colluded expressly—that is, had explicitly agreed to raise prices—rather than tacitly ("follow the leader" or "consciously parallel" pricing). The focus of the plaintiffs' discovery was on the information exchange orchestrated by the trade association, the change in the defendants' pricing structures and the defendants' ensuing price hikes, and the possible existence of the smoking gun—and let's begin there, for the plaintiffs think they have found it, and they have made it the centerpiece—indeed, virtually the entirety—of their argument.

Their supposed smoking gun is a pair of emails from an executive of T–Mobile named Adrian Hurditch to another executive of the firm, Lisa Roddy. Hurditch was not a senior executive but he was involved in the pricing of T–Mobile's products, including its text messaging service. The first of the two emails to Roddy, sent in May 2008, said "Gotta tell you but my gut says raising messaging pricing again is nothing more than a price gouge on consumers. I would guess that consumer advocates groups are going to come after us at some point. It's not like we've had an increase in the cost to carry message to justify this or a drop in our subscription SOC rates? I know the other guys are doing it but that doesn't mean we have to follow." ("SOC" is an acronym for "system on a chip," a common component of cellphones.) The second email, sent in September 2008 in the wake of a congressional investigation of alleged price gouging by the defendants, said that "at the end of the day we know there is no higher cost associated with messaging. The move [the latest price increase by T–Mobile] was colusive [*sic*] and opportunistic." The misspelled "collusive" is the heart of the plaintiffs' case.

It is apparent from the emails that Hurditch disagreed with his firm's policy of raising the price of its text messaging service. (The price increase, however, was limited to the PPU segment of the service; we'll see that this is an important qualification.) But that is all that is apparent. In emphasizing the word "col[l]usive"—and in arguing in their opening brief that "Hurditch's statement that the price increases were collusive is thus dispositive. Hurditch's statement is a party admission and a co-conspirator statement"—the plaintiffs' counsel demonstrate a failure to understand the fundamental distinction between express and tacit collusion. Express collusion violates antitrust law; tacit collusion does not. There is nothing to suggest that Hurditch was referring to (or accusing his company of) express collusion. In fact the first email rather clearly refers to tacit collusion; for if Hurditch had thought that his company had agreed with its competitors to raise prices he wouldn't have said "I know the other guys are doing it but *that doesn't mean we have to follow* " (emphasis added). They would have to follow, or at least they would be under great pressure to follow, if they had agreed to follow.

As for the word "opportunistic" in the second email, this is a reference to the remark in the first email that T–Mobile and its competitors were seizing an opportunity to gouge consumers—and in a highly concentrated market, seizing such an opportunity need not imply express collusion. …

Nothing in any of Hurditch's emails suggests that he believed there was a conspiracy among the carriers. There isn't even evidence that he had ever communicated on any subject with any employee of any of the other defendants. The reference to "the other guys" was not to employees of any of them but to the defendants themselves—the companies, whose PPU prices were public knowledge.

The plaintiffs make much of the fact that Hurditch asked Roddy to delete several emails in the chain that culminated in the "colusive" email. But that is consistent with his not wanting to be detected by his superiors criticizing their management of the company. The plaintiffs argue that, no, the reason for the deletion was to destroy emails that would have shown that T–Mobile was conspiring with the other carriers. If this were true, the plaintiffs would be entitled to have a jury instructed that it could consider the deletion of the emails to be evidence (not conclusive of course) of the defendants' (or at least of T–Mobile's) guilt. But remember that there is no evidence that Hurditch was involved in, or had heard about, any conspiracy, and there is as we've just seen an equally plausible reason for the deletion of the emails in question. There's nothing unusual about sending an intemperate email, regretting sending it, and asking the recipient to delete it. And abusing one's corporate superiors—readily discernible even in Hurditch's emails that were not deleted—is beyond intemperate; it is career-endangering, often career-ending. Hurditch and Roddy acknowledged in their depositions that at least one of the deleted emails had criticized T–Mobile's senior management in "emotional" terms. Furthermore, if T–Mobile destroyed emails that would have revealed a conspiracy with its competitors, why didn't it destroy the "smoking gun" email—the "colusive" email? …

The plaintiffs point out that the existence of express collusion can sometimes be inferred from circumstantial evidence, and they claim that they produced such evidence, along with Hurditch's emails, which they term direct evidence of such collusion—which, as we know, they are not. Circumstantial evidence of such collusion might be a decline in the market shares of the leading firms in a market, for their agreeing among themselves to charge a high fixed price might have caused fringe firms and new entrants to increase output and thus take sales from the leading firms. Circumstantial evidence might be inflexibility of the market leaders' market shares over time, suggesting a possible agreement among them not to alter prices, since such an alteration would tend to cause market shares to change. Or one might see a surge in nonprice competition, a form of competition outside the scope of the cartel agreement and therefore a possible substitute for price competition. Other evidence of express collusion might be a high elasticity of demand (meaning that a small change in price would cause a substantial change in quantity demanded), for this might indicate that the sellers had agreed not to cut prices even though it would be to the advantage of each individual seller to do so until the market price fell to a level at which the added quantity sold did not offset the price decrease.

The problem is that these phenomena are consistent with tacit as well as express collusion; their absence would tend to negate both, but their presence would not point unerringly to express collusion. And anyway these aren't the types of circumstantial evidence on which the plaintiffs rely. Rather they argue that had any one of the four carriers not raised its price, the others would have experienced costly consumer "churn" (the trade's term for losing customers to a competitor), and therefore all four dared raise their prices only because they had agreed to act in concert. For that would minimize churn—PPU customers would have no place to turn for a lower price. There is, however, a six-fold weakness to this suggested evidence of express collusion:

First, a rational profit-maximizing seller does not care about the number of customers it has but about its total revenues relative to its total costs. If the seller loses a third of its customers because it has doubled its price, it's ahead of the game because twice two-thirds is greater than one (4/3 > 3/3).

Second, in any case of tacit collusion the colluders risk churn, because no one would have committed to adhere to the collusive price. And yet tacit collusion appears to be common, each tacit colluder reckoning that in all likelihood the others will see the advantages of hanging together rather than hanging separately.

Third, the four defendants in this case did not move in lockstep. For months on end there were price differences in their services. For example, during most of the entire period at issue (2005 to 2008) T–Mobile's PPU was 5 cents below Sprint's. To eliminate all risk of churn the defendants would have had to agree to raise their prices simultaneously, and they did not.

Fourth, while there was some churn, this does not imply that each defendant had decided to raise its price so high as to drive away droves of customers had the other defendants not followed suit. … One reason is that, as noted earlier, while 5 cents can make a large percentage difference in this market, it is such a small absolute amount of money that it may make no difference to most consumers, especially when a nickel or a dime or 20 cents is multiplied by a very small number of monthly messages. More important, as a customer's monthly messaging increases, and also the price per message (as was happening during this period), the alternative of a text messaging bundle plan becomes more attractive. …

Fifth, the period during which the carriers were raising their prices was also the period in which text messaging caught on with the consuming public and surged in volume. Many PPU customers would have found that they were text messaging more, and the more one text messages the more attractive the alternative of a bundle plan. The defendants *wanted* their PPU customers to switch to bundles …

And sixth, if the carriers were going to agree to fix prices, they wouldn't have fixed their PPU prices; why risk suit or prosecution for fixing such prices when the PPU market was generating such a slight—and shrinking—part of the carriers' overall revenues? The possible gains would be more than offset by the inevitable legal risks. Furthermore, since an agreement to fix prices in the PPU market would have left the carriers free to cut prices on the bulk of their business (for they are not accused of fixing bundle prices), the slight gains from fixing PPU prices would be negated by increased competition in the carriers' other markets. …

It remains to consider the claim that the trade association of which the defendants were members, The Wireless Association (it has a confusing acronym—CTIA, reflecting the original name of the association, which was Cellular Telephone Industries Association), and a component of the association called the Wireless Internet Caucus of CTIA, were forums in which officers of the defendants met and conspired to raise PPU prices. Officers of some of the defendants attended meetings both of the association and of its caucus, but representatives of companies not alleged to be part of the conspiracy frequently were present at these meetings, and one of the plaintiffs' expert witnesses admitted that in the presence of non-conspirators "the probability of collusion would go away." Still, opportunities for senior leaders of the defendants to meet privately in these officers' retreats abounded. And an executive of one of the defendants (AT & T) told the president of the association that "we all try not to surprise each other" and "if any of us are about to do something major we all tend to give the group a heads up"—"plus we all learn valuable info from each other." This evidence would be more compelling if the immediate sequel to any of these meetings had been a simultaneous or near-simultaneous price increase by the defendants. Instead there were substantial lags. And as there is no evidence of what information was exchanged at these meetings, there is no basis for an inference that they were using the meetings to plot prices increases. …

The plaintiffs have presented circumstantial evidence consistent with an inference of collusion, but that evidence is equally consistent with independent parallel behavior.

We hope this opinion will help lawyers understand the risks of invoking "collusion" without being precise about what they mean. Tacit collusion, also known as conscious parallelism, does not violate section 1 of the Sherman Act. Collusion is illegal only when based on agreement. Agreement can be proved by circumstantial evidence, and the plaintiffs were permitted to conduct and did conduct full pretrial discovery of such evidence. Yet their search failed to find sufficient evidence of express collusion to make a prima facie case. The district court had therefore no alternative to granting summary judgment in favor of the defendants.

Affirmed.

NOTES AND QUESTIONS

1. Given this Seventh Circuit decision affirming summary judgment for the defendants, was the Seventh Circuit correct to deny the defendants' earlier motion to dismiss? Why or why not?

2. Judge Posner wrote that the use of the word "collusion" could refer to either express collusion (which violates antitrust law) or tacit collusion (which is legal). He noted that the plaintiffs' circumstantial evidence was "consistent with an inference of collusion" but was "equally consistent with independent parallel behavior." Does that create a genuine issue of material fact? Should the plaintiffs have been able to present their case to a jury? Why or why not?

VALSPAR CORP. V. E.I. DU PONT DE NEMOURS & CO.
873 F.3d 185 (3d Cir. 2017)

HARDIMAN, Circuit Judge

This appeal involves an alleged conspiracy to fix prices in the titanium dioxide industry in violation of Section 1 of the Sherman Act. Appellant Valspar, a purchaser of titanium dioxide, claimed Appellee DuPont conspired with other titanium dioxide suppliers to fix prices. Valspar argued that the price-fixing agreement was made manifest primarily by thirty-one parallel price increase announcements issued by the suppliers. DuPont countered that the parallel pricing was not the product of an agreement, but rather the natural consequence of the marketplace. Specifically, DuPont posited that because the market for titanium dioxide is an oligopoly, the price movement was caused by “conscious parallelism”—an economic theory that explains oligopolists will naturally follow a competitor's price increase in the hopes that each firm's profits will increase. The District Court agreed with DuPont and granted its motion for summary judgment. We will affirm.

The facts of this case were essentially undisputed in the District Court. The parties agree that the market for titanium dioxide is an oligopoly. Titanium dioxide is a commodity-like product with no substitutes, the market is dominated by a handful of firms, and there are substantial barriers to entry.

Valspar, a large-scale purchaser of titanium dioxide, alleges that a group of titanium dioxide suppliers conspired to increase prices. It claims that the conspiracy began when DuPont—the largest American supplier—joined the Titanium Dioxide Manufacturers Association (TDMA) in 2002, when the association opened participation to non-European companies. Shortly after joining the TDMA, DuPont announced a price increase. Within two weeks, DuPont's price increase was matched by Millennium, Kronos, and Huntsman (other TDMA members and members of the alleged conspiracy). This began what Valspar alleged to be the “Conspiracy Period”—twelve years during which the alleged conspirators announced price increases 31 times….

Oligopolies pose a special problem under § 1 because rational, independent actions taken by oligopolists can be nearly indistinguishable from horizontal price fixing. This problem is the result of “interdependence,” which occurs because “any rational decision [in an oligopoly] must take into account the anticipated reaction of the other firms.” In re Flat Glass Antitrust Litig., 385 F.3d 350, 359 (3d Cir. 2004) (alteration omitted) (quoting Philip E. Areeda & Herbert Hovenkamp, Antitrust Law 207 (2d ed. 2000)). In a market with many firms, “the effects of any single firm's price and output decisions ‘would be so diffused among its numerous competitors that they would not be aware of any change.’ ” Id. (quoting Areeda & Hovenkamp, supra, at 206). The opposite is true in an oligopoly, where any price movement “will have a noticeable impact on the market and on its rivals.” Id. (quoting Areeda & Hovenkamp, supra, at 206); see also In re Text Messaging Antitrust Litig., 782 F.3d 867, 875 (7th Cir. 2015) (oligopolists “watch each other like hawks”).

This “oligopolistic rationality” can cause supracompetitive prices because it discourages price reductions while encouraging price increases. A firm is unlikely to lower its price in an effort to win market share because its competitors will quickly learn of that reduction and match it, causing the first mover's profits to decline and a subsequent decline in the overall profits of the industry. Flat Glass, 385 F.3d at 359. Similarly, if a firm announces a price increase, other market participants will know that “if they do not increase their prices to [the first-mover's] level, [the first-mover] may be forced to reduce its price to their level. Because each of the other firms know this, each will consider whether it is better off when all are charging the old price or [the new one]. They will obviously choose [the new price] when they believe that it will maximize industry profits.” Id. (quoting Areeda & Hovenkamp, supra, at 207–08).

The Supreme Court has explained that this behavior does not violate antitrust laws. See Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 227, 113 S.Ct. 2578, 125 L.Ed.2d 168 (1993). Even though such interdependence or “conscious parallelism” harms consumers just as a monopoly does, it is beyond the reach of antitrust laws for two reasons. First, some courts and scholars theorize "that interdependent behavior is not an 'agreement' within the term's meaning under the Sherman Act." Flat Glass, 385 F.3d at 360 (citing Donald F. Turner, The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal, 75 Harv. L. Rev. 655, 663–65 (1962)). And second, "it is close to impossible to devise a judicially enforceable remedy for 'interdependent' pricing." Clamp-All Corp. v. Cast Iron Soil Pipe Inst., 851 F.2d 478, 484 (1st Cir. 1988) (Breyer, J.). The problem is this: "How does one order a firm to set its prices without regard to the likely reactions of its competitors?"

"When faced with whether a plaintiff has offered sufficient proof of an agreement to preclude summary judgment, a court must generally apply the same summary judgment standards that apply in other contexts." Flat Glass, 385 F.3d at 357…. However, we have recognized there is "an important distinction" to this general standard in antitrust cases. Flat Glass, 385 F.3d at 357. "[A]ntitrust law limits the range of permissible inferences from ambiguous evidence in a § 1 case." Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 588, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986). Specifically, "conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy." The reason for this more rigorous standard is that mistaken inferences are especially costly in antitrust cases, since they could penalize desirable competitive behavior and "chill the very conduct the antitrust laws are designed to protect."

With those principles informing our analysis, this Court has developed specialized evidentiary standards at summary judgment in antitrust cases in general and in oligopoly cases in particular. Our analysis often begins with evidence of parallel price movements. See Chocolate, 801 F.3d at 397. In non-oligopolistic markets, "[p]arallel behavior among competitors is especially probative of price fixing because it is the sine qua non of a price fixing conspiracy." Southway Theatres, Inc. v. Ga. Theatre Co., 672 F.2d 485, 501 (5th Cir. Unit B 1982). But in an oligopolistic market, parallel behavior "can be a necessary fact of life," In re Baby Food Antitrust Litig., 166 F.3d 112, 122 (3d Cir. 1999), and "[a]ccordingly, evidence of conscious parallelism cannot alone create a reasonable inference of a conspiracy," Chocolate, 801 F.3d at 398. Therefore, to prove an oligopolistic conspiracy with proof of parallel behavior, that evidence "must go beyond mere interdependence" and "be so unusual that in the absence of an advance agreement, no reasonable firm would have engaged in it." Baby Food, 166 F.3d at 135.

Because proof of parallel behavior will rarely itself create an inference of conspiracy, a plaintiff will often need to "show that certain plus factors are present" in order "[t]o move the ball across the goal line." Chocolate, 801 F.3d at 398–99. "Plus factors are proxies for direct evidence because they tend to ensure that courts punish concerted action—an actual agreement." Id. (internal formatting and citations omitted). "Although we have not identified an exhaustive list of plus factors, they may include (1) evidence that the defendant had a motive to enter into a price fixing conspiracy; (2) evidence that the defendant acted contrary to its interests; and (3) evidence implying a traditional conspiracy." Id. at 398.

While normally all three plus factors are weighed together, in the case of oligopolies the first two factors are deemphasized because they "largely restate the phenomenon of interdependence." *Flat Glass*, 385 F.3d at 360. Put another way, "[e]vidence of a motive to conspire means the market is conducive to price fixing, and evidence of actions against self-interest means there is evidence of behavior inconsistent with a competitive market." Chocolate, 801 F.3d at 398. Since those qualities are intrinsic to oligopolies, we instead focus on the third plus factor: "evidence implying a traditional conspiracy." To meet this factor, we require "proof that the defendants got together and exchanged assurances of common action or otherwise adopted a common plan even though no meetings, conversations, or exchanged documents are shown."….

Valspar bases its case primarily on the 31 parallel price increase announcements issued by the competitors during the alleged conspiracy, arguing that it is "inconceivable" that, on 31 occasions, the competitors "conduct[ed] independent analyses ... [and] nearly simultaneously arrived at identical price increase amounts to be implemented on exactly the same day."

Valspar's argument fails for two reasons. First, its characterization of the suppliers' price announcements neglects the theory of conscious parallelism and flies in the face of our doctrine that in an oligopoly "any rational decision must take into account the anticipated reaction of the other ... firms." Baby Food, 166 F.3d at 122 (emphasis added) (citations omitted).5 Thus, DuPont does not claim that the competitors' numerous parallel price increases were discrete events—nor could it do so with a straight face. But it doesn't need to. The theory of interdependence recognizes that price movement in an oligopoly will be just that: interdependent. And that phenomenon frequently will lead to successive price increases, because oligopolists may "conclude that the industry as a whole would be better off by raising prices." Chocolate, 801 F.3d at 397.6

Second, Valspar does not engage this Court's demanding rule that in order to raise an inference of conspiracy on this point, it was required to show that the suppliers' parallel pricing went "beyond mere interdependence [and was] so unusual that in the absence of advance agreement, no reasonable firm would have engaged in it." Baby Food, 166 F.3d at 135. Valspar never cites this important controlling precedent, nor does it attempt to show how it might be met.

Apart from Valspar's failure to carry its burden, DuPont demonstrates that "market realities ... clearly controvert [Valspar's] contention" that these announcements are evidence of a conspiracy. Id. at 131. First, supply contracts in the titanium dioxide industry contained price-protection clauses requiring a notice period to customers before a price increase, meaning that if a supplier failed to match a competitor's announcement, it was foregoing the possibility of negotiating a price increase during that period. These industry-wide contractual provisions made the benefit of matching a price increase announcement high and the risk minimal: if a competitor later undercut that price in an effort to take market share, the supplier could refrain from implementing the price increase or even respond by lowering its price. Second, DuPont demonstrated that the market for titanium dioxide remained competitive despite the frequent price increase announcements. Indeed, Valspar employees testified that it was "very common" to negotiate away a supplier's attempt to increase price, DuPont Br. 6, and said that "[o]ften ... an aggressive supplier would be interested in achieving more volume and would come in and offer a [lower] price," id. at 9. Across all suppliers' attempted price increases, Valspar was able to avoid that increase (or even negotiate a decrease) one-third of the time. Thus, Valspar's characterization of this evidence is controverted by market realities; "aggressive" and "common" price competition between firms is inconsistent with the idea that those same firms have conspired not to compete on price.

Valspar also advances the related argument that the flurry of price announcements reflects a drastic change from pre-conspiracy behavior in the titanium dioxide market. A change in industry practices must be "radical" or "abrupt" to "create an inference of a conspiracy." Chocolate, 801 F.3d at 410 (citation omitted). Valspar claims to have met this standard because there were only three parallel price increase announcements before the alleged conspiracy period (as compared to the thirty-one during the conspiracy period).

We disagree. In Chocolate, the plaintiffs advanced a similar argument, relying on an increased frequency in parallel pricing activity from pre-conspiracy behavior. There, we explained that "the focus of the Plaintiffs' argument is unduly narrow" because "[h]istorically, parallel pricing in the U.S. chocolate market has not been at all uncommon." Chocolate, 801 F.3d at 410. Here too, public parallel price increase announcements are "consistent with how this industry has historically operated." Valspar, 152 F.Supp.3d at 252 (quoting Chocolate, 801 F.3d at 410). Similarly, when other courts have found a radical or abrupt change to indicate conspiracy, that change has generally been more than just an uptick in frequency of a pre-established industry practice. See Toys "R" Us, Inc. v. FTC, 221 F.3d 928, 935 (7th Cir. 2000) (group of toy distributors unanimously stopped dealing with warehouse clubs after years of that being an industry norm). That logic rings particularly true in this context because "it is generally unremarkable for the pendulum in oligopolistic markets to swing from less to more interdependent and cooperative." Chocolate, 801 F.3d at 410 (citing Areeda & Hovenkamp, supra, at 229).

Having found that the pattern of parallel price increases does not raise an inference of conspiracy, we next turn to Valspar's argument that the plus factors evidence a conspiracy. As explained above, this Court has developed a specialized rule that in oligopolistic markets, " 'the first two factors largely restate the phenomenon of interdependence,' ... [which] leaves traditional non-economic evidence of a conspiracy as the most important plus factor." Chocolate, 801 F.3d at 398 (citation omitted). Tellingly, Valspar ignores this important point and instead emphasizes why the first two plus factors are met. Valspar's "victory ... is a hollow one," however, having succeeded in showing interdependence but not conspiracy. Id. at 400.

The first factor relates to motive to enter a conspiracy, i.e., that "the market is conducive to price fixing." Id. at 398. There is little doubt that this highly concentrated market for a commodity-like product with no viable substitutes and substantial barriers to entry was conducive to price fixing.

The second plus factor looks for evidence of action against self-interest, i.e., "evidence that the market behaved in a noncompetitive manner." Flat Glass, 385 F.3d at 361 (citation omitted). Valspar presents evidence that there was "a 16% overcharge" and that "price increases were not correlated to supply-and-demand principles." While true, this is largely irrelevant because it ignores the fact that "firms in a concentrated market may maintain their prices at supracompetitive levels, or even raise them to those levels, without engaging in any overt concerted action." ….

We finally reach Valspar's evidence under our third plus factor: traditional conspiracy evidence, where we look for "proof that the defendants got together and exchanged assurances of common action or otherwise adopted a common plan even though no meetings, conversations, or exchanged documents are shown."10 Flat Glass, 385 F.3d at 361 (citation omitted). We approach the third plus factor as this Court did in Chocolate, first considering individual groups of evidence to see whether any raise an inference of conspiracy, before evaluating all of the proof in context. See 801 F.3d at 403–12. Here, we agree with the District Court that Valspar failed to raise an inference of conspiracy. Each strand of evidence is weaker than similar evidence in cases where this Court has affirmed summary judgment in favor of companies that operate in an oligopolistic market.

First, Valspar shows that DuPont and the other competitors took part in a data sharing program offered by the Titanium Dioxide Manufacturers Association. As part of this program (the Global Statistics Program, or GSP) the competitors provided production, inventory, and sales-volume data (but never price data) to the TDMA, which then aggregated, anonymized, and redistributed the data.

Without citing any precedent to show why this type of information sharing was illegal, Valspar argues that the GSP allowed each conspirator to calculate its own market share and thus deduce whether it was getting its fair share of the conspiracy's profits. This argument suffers from the loaded question fallacy. Instead of setting out to prove: "Does the GSP show that a conspiracy existed?," Valspar attempts to answer: "How did the GSP further the conspiracy?" This approach cannot satisfy Valspar's burden. "[A] litigant may not proceed by first assuming a conspiracy and then explaining the evidence accordingly." Blomkest Fertilizer, Inc. v. Potash Corp. of Saskatchewan, 203 F.3d 1028, 1033 (8th Cir. 2000)….

Relatedly, Valspar claims that the alleged conspirators "used the TDMA meetings to communicate their pricing plans, coordinate price increases, and confirm that each competitor would follow the leader on price increases." Valspar Br. 50. Valspar's argument essentially begins and ends with opportunity: the TDMA meetings brought the competitors together, so one should assume that they used the meetings to conspire. But as the District Court noted, "[t]here is no evidence that there was any discussion of prices during these meetings and certainly no evidence of an agreement."…

Next, Valspar suggests that the competitors used industry consultants as conduits to funnel information. For example, Valspar points to an e-mail from a Kronos employee to a consultant noting that the employee had heard rumors of an impending Huntsman price increase, but thought it "sound[ed] weird" and wanted to know if the consultant could "confirm anything from [his] lofty position." Valspar Br. 20.

This sort of inquiry to a consultant is not probative of conspiracy. We have explained that "it makes common sense to obtain as much information as possible of the pricing policies and marketing strategies of one's competitors." Baby Food, 166 F.3d at 126. In fact, this type of inquiry undermines the existence of a conspiracy because conspirators would have no need to ask consultants about the specifics of their own conspiracy….

Valspar also emphasizes a selection of internal e-mails sent by the various competitors. For example, a DuPont e-mail advocated for a price modification "[o]nly if you are not undercutting a Kronos price increase!" Valspar Br. 9. A Millennium e-mail said: "We should have this extra [market] share—customers have been and want to buy this from us. Competitors will let us have this." Id. at 8. And a Cristal e-mail stated that "all major global players have been very disciplined with pricing implementation up to this point." Id. at 10.

These e-mails are helpful to Valspar, but only superficially. They may raise some suspicion insofar as they indicate that something anticompetitive is afoot. But as we have explained, oligopolistic conscious parallelism is by nature anticompetitive and also legal. See Chocolate, 801 F.3d at 397. Essentially, these e-mails show that the competitors were aware of the phenomenon of conscious parallelism and implemented pricing strategies in response to it. It makes sense that each firm would implement such strategies, since conscious parallelism allows firms in an oligopoly to "in effect share monopoly power" and maintain "prices at a profit-maximizing, supracompetitive level." Brooke Group, 509 U.S. at 227, 113 S.Ct. 2578….

For the reasons stated, we will affirm the judgment of the District Court.

STENGEL, Chief District Judge, dissenting….

The majority's ruling creates an unworkable burden, not supported by our precedent, for plaintiffs seeking to prove a Sherman Act price-fixing case with circumstantial evidence.

Second, it affirms a decision where a district judge weighed and compartmentalized evidence, a task better suited for juries—not judges….

This Court favors a sliding scale approach to determine the types of inferences allowed to be drawn from circumstantial evidence in antitrust cases. According to our Circuit's precedent, and that of the Supreme Court's, the range of inferences that may be drawn from circumstantial evidence depends upon "the plausibility of the plaintiffs' theory and the dangers associated with such inferences." Chocolate, 801 F.3d at 396 (quoting In re Flat Glass Antitrust Litig., 385 F.3d 350, 357 (3d Cir. 2004)). In cases where an antitrust plaintiff's economic theory of liability "makes no economic sense," and drawing inferences in the plaintiff's favor would deter healthy competition, the plaintiff must produce "more persuasive evidence" to bolster its claim. Id. On the other hand, when a plaintiff's theory makes economic sense, courts draw more liberal inferences in favor of the plaintiff. Valspar presented an economic theory that makes perfect economic sense, yet the District Court and majority did not draw any inferences in Valspar's favor….

It is true that conscious parallelism alone cannot create an inference of conspiracy. The majority has taken this to mean that any evidence of conscious parallelism is therefore incapable of raising an inference of conspiracy. This is incorrect. Parallel pricing is a necessary requirement of any § 1 price-fixing claim, and simply because parallel pricing alone cannot preclude summary judgment does not mean that courts ignore evidence of it. Indeed, our precedent has repeatedly warned against overlooking this important factor in these types of cases, especially where the plaintiff's economic theory—as it does here—makes perfect economic sense.2

The sheer number of parallel price increase announcements in this case—31 to be exact—is unprecedented….

This amount of parallel price increase announcements, in a relatively short time period, commands attention…. Here, there is evidence that many of the manufacturers' price increase announcements were made within hours, days, or weeks of each other. For example, in one instance, DuPont announced a price increase at 11:00 a.m., Tronox matched it seven hours later, and Kronos matched it eight hours later. The next day, Millennium and Huntsman announced identical price increases. In another instance, all five TiO2 manufacturers made the same price increase announcement within a four-day period. This close timing creates a strong inference of conspiracy….

The sheer amount of parallel conduct in this case, coupled with the plausibility of Valspar's economic theory, should inform our analysis of the plus factors. Flat Glass, 385 F.3d at 358 ("[A]n agreement among oligopolists to fix prices at a supracompetitive level ... makes perfect economic sense" and therefore "more liberal inferences from the evidence should be permitted than in Matsushita because the attendant dangers from drawing inferences recognized in Matsushita are not present"); id. at n.8 ("*Matsushita* itself said little about proof requirements in a case where underlying structural evidence indicates that the offense is quite plausible" (quoting Herbert Hovenkamp, The Rationalization of Antitrust, 116 HARV. L. REV. 917, 925–26 (2003))). It did not. The majority paid very little mind to these distinctions—especially the plausibility of Valspar's economic theory.

The majority's formulation of the summary judgment standard in this case, coupled with its dismissive treatment of unprecedented parallel-conduct evidence, creates too high a hurdle for plaintiffs attempting to prove a price-fixing conspiracy using circumstantial evidence. The limitations in antitrust cases announced in Matsushita, and that we followed in Chocolate, were never meant to require something more than circumstantial evidence of an agreement to preclude summary judgment. Nor did they impose some "special" burden….

Traditional conspiracy evidence is often the most important "plus factor" in a case like this one. Chocolate, 801 F.3d at 401. Traditional conspiracy evidence is evidence that "the defendants got together and exchanged assurances of common action or otherwise adopted a common plan even though no meetings, conversations, or exchanged documents are shown."

… Valspar presented various forms of traditional conspiracy evidence. For example, Valspar presented a Millennium email stating "we have competition on board for the Oct 1 price increase announcement." Having "competition on board" for a price increase announcement certainly conveys that the suppliers somehow got together and exchanged assurances of "common action," i.e., to announce the same prices. The same goes for the suppliers' emails about the "collective needs" of the industry14 and getting everyone "on the bus" or, put another way, "on their horses."

Today's decision could easily be read to require direct evidence of an agreement in an oligopoly/antitrust case despite the fact that neither our prior jurisprudence (nor the Supreme Court's) has ever required such evidence….

I am not sure how this circumstantial evidence could be stronger. It unequivocally shows that one alleged conspirator's (Millenium's) CEO met with another alleged conspirator's (Huntsman's) President days before a parallel price increase announcement. This meeting occurred at the same time an email was written stating that TiO2 "competition" was "on board" with a particular price increase announcement. Even more persuasive, there is evidence that all the TiO2 suppliers discussed "improv[ing] pricing" at an industry conference in 2005 and that in 2002 DuPont and Kronos announced an identical price increase just days after Jim Fisher met with these two "competitors."

A jury should be allowed to determine whether Fisher's meetings with both Kronos and DuPont—days before a parallel price increase announcement—were suspect. A jury should be allowed to determine whether an email that "competition" is "on board" for a price increase announcement was concerted action, particularly when this email was written one day after Huntsman's President personally met with Millennium's CEO….

I am certainly mindful of the theory of interdependence and the presence of an oligopoly. With that said, from the very start, Valspar presented a theory that makes perfect economic sense. It supported this theory with strong evidence of parallel conduct in the form of 31 (an unprecedented amount) of parallel price increase announcements. Recognizing conscious parallelism to be insufficient on its own to survive summary judgment, Valspar also presented viable evidence in support of the plus factors: (i) price signaling, (ii) exchanges of confidential information, (iii) relatively static market shares, (iv) intercompany sales of TiO2 at below market price, (v) abrupt departure from pre-conspiracy conduct, and (vi) a market susceptible to conspiracy. Although the TiO2 market is an oligopoly, Valspar also presented evidence that did not simply restate interdependence: non-price acts against self-interest. Finally, it presented traditional conspiracy evidence. Viewed together, and not compartmentalized, all this evidence was more than sufficient to preclude summary judgment.

For these reasons, I respectfully dissent.

[5] Intra-Enterprise Conspiracy

p. 355, append this note:

5. In *Medical Center at Elizabeth Place, LLC v. Atrium Health System*, 817 F.3d 934 (6th Cir. 2016), a group of formerly independent hospitals formed a "hospital network" through a joint operating agreement that merged some of their healthcare functions. The Sixth Circuit reversed the district court's decision that the network constituted a single entity that, pursuant to the *Copperweld* Doctrine, could not violate Section One. The Sixth Circuit noted that the record "demonstrate[d] that defendant hospitals compete with each other for physicians and patients, with each defendant hospital continuing to market certain hospital services to the public." The hospitals also continued to make independent decisions regarding staffing and medical strategies. The court reversed the district court's grant of summary judgment because a genuine issue of material fact existed as to whether the hospitals' joint venture constituted a single entity or concerted action.

Chapter 5 **VERTICAL RESTRICTIONS**

ANTI-STEERING RULES
OHIO V. AMERICAN EXPRESS CO.
138 S.Ct. 2274 (2018)

JUSTICE THOMAS delivered the opinion of the Court.[1]

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 antisteering contractual provision. The antisteering 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 antisteering provisions violate federal antitrust law. We conclude they do not.

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 inter-related 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. See Evans & Schmalensee, Markets With Two-Sided Platforms, 1 Issues in Competition L. & Pol'y 667 (2008); Evans & Noel, Defining Antitrust Markets When Firms Operate Two-Sided Platforms, 2005 Colum. Bus. L. Rev. 667, 668; Filistrucchi, Geradin, Van Damme, & Affeldt, Market Definition in Two-Sided Markets: Theory and Practice, 10 J. Competition L. & Econ. 293, 296 (2014). 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

[1] [joined by Chief Justice Roberts and Justices Kennedy, Alito, and Gorsuch.]

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. 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.

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.'… 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.

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…. 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 card- holder 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…. In sum, Amex's business model has stimulated competitive innovations in the credit-card market, increasing the volume of transactions and improving the quality of the services.

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 antisteering provisions in its contracts with merchants. These antisteering 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 antisteering provisions do not, however, prevent merchants from steering customers toward debit cards, checks, or cash.

In October 2010, the United States and several States (collectively, plaintiffs) sued Amex, claiming that its antisteering provisions violate §1 of the Sherman Act…. After a 7-week trial, the District Court agreed that Amex's antisteering 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 antisteering provisions are anticompetitive because they result in higher merchant fees.

The Court of Appeals for the Second Circuit reversed. United States v. American Express Co., 838 F. 3d 179, 184 (2016). 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 antisteering provisions were not anticompetitive and did not violate §1…. This Court's precedents have … understood §1 "to outlaw only unreasonable restraints."

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. Restraints that are not unreasonable per se are judged under the "rule of reason." 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….

In this case, both sides correctly acknowledge that Amex's antisteering provisions are vertical restraints—i.e., restraints "imposed by agreement between firms at different levels of distribution." 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. See 1 J. Kalinowski, Antitrust Laws and Trade Regulation §12.02[1] (2d ed. 2017) (Kalinowski); P. Areeda & H. Hovenkamp, Fundamentals of Antitrust Law §15.02[B] (4th ed. 2017) (Areeda & Hovenkamp) 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 antisteering 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 antisteering 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.

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….[2] [T]he relevant market is defined as "the area of effective competition." Typically this is the "arena within which significant substitution in consumption or production occurs." Areeda & Hovenkamp §5.02; accord, 2 Kalinowski §24.02[1] But courts should "combin[e]" different products or services into "a single market" when "that combination reflects commercial realities."

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. See Times-Picayune Publishing Co. v. United States, 345 U. S. 594, 610 (1953).

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

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[2]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. See Indiana Federation of Dentists, supra, at 460–461; Catalano, supra, at 648–649. But vertical restraints are different. See Arizona v. Maricopa County Medical Soc., 457 U. S. 332, 348, n. 18 (1982); Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551 U. S. 877, 888 (2007). 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 id., at 898 (noting that a vertical restraint "may not be a serious concern unless the relevant entity has market power"); 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").

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.

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 "suppl[ying] only one product"—transactions.[3]

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…. Only a company that had both cardholders and merchants willing to use its network could sell transactions and compete in the credit-card market.

For all these reasons, "[i]n 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."… 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 antisteering provisions have anticompetitive effects.

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 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 antisteering 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.

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.

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…. 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….

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

[3]Contrary to the dissent's assertion, merchant services and cardholder services are not complements. *See* Filistrucchi 297 ("[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").

increase was not entirely spent on cardholder rewards. The plaintiffs believe that this evidence shows that the price of Amex's transactions increased.

Even assuming the plaintiffs are correct, this evidence does not prove that Amex's antisteering provisions gave it the power to charge anticompetitive prices. "Market power is the ability to raise price profitably by restricting output." Areeda & Hovenkamp §5.01 (emphasis added); accord, Kodak, 504 U. S., at 464; Business Electronics, 485 U. S., at 723. 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." 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 antisteering 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%.....

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…. 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 antisteering 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. Cf. Leegin, 551 U. S., at 890–891 (recognizing that vertical restraints can prevent retailers from free riding and thus increase the availability of "tangible or intangible services or promotional efforts" that enhance competition and consumer welfare). Perhaps most importantly, antisteering 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 antisteering provisions have anticompetitive effects.…

Justice Breyer, dissenting.[4]

For more than 120 years, the American economy has prospered by charting a middle path between pure lassez-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." 1 P. Areeda & H. Hovenkamp, Antitrust Law ¶100b, p. 4 (4th ed. 2013) (Areeda & Hovenkamp). 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. See GAO, Credit and Debit Cards: Federal Entities Are Taking Actions to Limit Their Interchange Fees, but Additional Revenue Collection Cost Savings May Exist 31–35 (GAO–08–558, 2008). 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. See ibid.

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, (quoting 7 P. Areeda, Antitrust Law ¶1511, p. 429 (3d ed. 1986)).

Second (as treatise writers summarize the case law), 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." 7 Areeda & Hovenkamp ¶1504b, at 415; see California Dental Assn. v. FTC, 526 U. S. 756, 771 (1999); id., at 788 (BREYER, J., dissenting).

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. 7 Areeda & Hovenkamp ¶1507a, at 442.

[4]Joined by Justices Ginsburg, Sotomayor, and Kagan.

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

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….

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 antisteering provisions in most of its contracts with merchants…. After placing them in its agreements, American Express found it could maintain, or even raise, its higher merchant prices without losing too many transactions to other firms….

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.

The District Court added that it found no offsetting pro-competitive benefit to shoppers. Indeed, it found no offsetting benefit of any kind....

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, 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. The provisions thereby "suppress[ed] [American Express'] . . . competitors' incentives to offer lower prices . . . resulting in higher profit-maximizing prices across the network services market." 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." See ibid. In support of that argument, the Government pointed out, and the District Court had held, that the newspaper dominated the market for the sales of newspapers to readers in New Orleans, where it was the sole morning daily newspaper. But this Court reversed. We 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." Ibid.

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....

Once a court has identified the good or service directly restrained, as Times-Picayune Publishing Co. requires, it will sometimes add to the relevant market what economists call "substitutes": other goods or services that are reasonably substitutable for that good or service.... The reason that substitutes are included in the relevant market is that they restrain a firm's ability to profitably raise prices, because customers will switch to the substitutes rather than pay the higher prices. See 2B Areeda & Hovenkamp ¶561, at 378.

But while the market includes substitutes, it does not include what economists call complements: goods or services that are used together with the restrained product, but that cannot be substituted for that product.... An example of complements is gasoline and tires. A driver needs both gasoline and tires to drive, but they are not substitutes for each other, and so the sale price of tires does not check the ability of a gasoline firm (say a gasoline monopolist) to raise the price of gasoline above competitive levels. As a treatise on the subject states: "Grouping complementary goods into the same market" is "economic nonsense," and would "undermin[e] the rationale for the policy against monopolization or collusion in the first place." 2B Areeda & Hovenkamp ¶565a, at 431.

Here, the relationship between merchant-related card services and shopper-related card services is primarily that of complements, not substitutes…... Thus, unless there is something unusual about this case—a possibility I discuss below—there is no justification for treating shopper-related services and merchant-related services as if they were part of a single market, at least not at step 1 of the "rule of reason."

Regardless, 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. [T]his 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 credit 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. Indiana Federation of Dentists, 476 U. S., at 460–461 (internal quotation marks omitted)….

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." 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. 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….. 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….

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 phrase "two-sided transaction platform" is not one of antitrust art—I can find no case from this Court using those words. 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. Ante, at 2. 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. A firm might mine for gold, which it refines and sells both to dentists in the form of fillings and to investors in the form of ingots. Or, a firm might drill for both oil and natural gas. Or a firm might make both ignition switches inserted into auto bodies and tires used for cars. I have already explained that, ordinarily, antitrust law will not group the two nonsubstitutable 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, nonsubstitutable goods and see if "overall" the restraint has a negative effect. See 2B Areeda & Hovenkamp ¶565a…..

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.

To justify special treatment for "two-sided transaction platforms," the majority relies on the Court's decision in United States v. Grinnell Corp., 384 U. S. 563, 571–572 (1966). In Grinnell, the Court treated as a single market several different "central station services," including burglar alarm services and fire alarm services. It did so even though, for consumers, "burglar alarm services are not interchangeable with fire alarm services." But that is because, for producers, the services were indeed interchangeable: A company that offered one could easily offer the other, because they all involve "a single basic service—the protection of property through use of a central service station." . Thus, the "commercial realit[y]" that the Grinnell Court relied on, ibid., was that the services being grouped were what economists call "producer substitutes." See 2B Areeda & Hovenkamp ¶561, at 378. And the law is clear that "two products produced interchangeably from the same production facilities are presumptively in the same market," even if they are not "close substitutes for each other on the demand side." That is because a firm that produces one such product can, in response to a price increase in the other, easily shift its production and thereby limit its competitor's power to impose the higher price.

Unlike the various types of central station services at issue in Grinnell Corp., however, the shopper-related and merchant-related services that American Express provides are not "producer substitutes" any more than they are traditional substitutes. For producers as for consumers, the services are instead complements. Credit card companies must sell them together for them to be useful. As a result, the credit-card companies cannot respond to, say, merchant-related price increases by shifting production away from shopper-related services to merchant-related services…. Thus, our precedent provides no support for the majority's special approach to defining markets involving "two-sided transaction platforms."…

[T]he academic articles the majority cites do not support the majority's flat rule that firms operating "two-sided transaction platforms" should always be treated as part of a single market for all antitrust purposes. Rather, the academics explain that for market-definition purposes, "[i]n some cases, the fact that a business can be thought of as two-sided may be irrelevant," including because "nothing in the analysis of the practices [at issue] really hinges on the linkages between the demands of participating groups." "In other cases, the fact that a business is two-sided will prove important both by identifying the real dimensions of competition and focusing on sources of constraints." That flexible approach, however, is precisely the one the District Court followed in this case, by considering the effects of "[t]he two-sided nature of the . . . card industry" throughout its analysis.

Neither the majority nor the academic articles it cites offer any explanation for why the features of a "two-sided transaction platform" justify always treating it as a single antitrust market, rather than accounting for its economic features in other ways, as the District Court did. The article that the majority repeatedly quotes as saying that " '[i]n two-sided transaction markets, only one market should be defined,', justifies that conclusion only for purposes of assessing the effects of a merger. In such a case, the article explains, "[e]veryone would probably agree that a payment card company such as American Express is either in the relevant market on both sides or on neither side . . . . The analysis of a merger between two payment card platforms should thus consider . . . both sides of the market." In a merger case this makes sense, but is also meaningless, because, whether there is one market or two, a reviewing court will consider both sides, because it must examine the effects of the merger in each affected market and submarket. See Brown Shoe Co., 370 U. S., at 325.

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." This mirrors the Court of Appeals' holding that the Government had to show that the "nondiscrimination provisions" had "made all [American Express] customers on both sides of the platform—i.e., both merchants and cardholders—worse off overall."

The problem with this reasoning, aside from it being wrong, is that the majority admits that the plaintiffs did show this: they "offer[ed] 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." Indeed, the plaintiffs did not merely "offer evidence" of this—they persuaded the District Court, which made an unchallenged factual finding that the merchant price increases that resulted from the nondiscrimination provisions "were not wholly offset by additional rewards expenditures or otherwise passed through to cardholders, and resulted in a higher net price."

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.'… 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.

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.

… I would not now hold that an agreement such as the one before us can never be justified by procompetitive benefits of some kind. But the Court of Appeals would properly consider procompetitive justifications not at step 1, but at steps 2 and 3 of the "rule of reason" inquiry. American Express would need to show just how this particular anticompetitive merchant-related agreement has procompetitive benefits in the shopper-related market. In doing so, American Express would need to overcome the District Court's factual findings that the agreement had no such effects.

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," ibid., 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."… 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." The majority does not even acknowledge, much less reject, these factual findings, despite coming to the contrary conclusion.

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[ying] 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.

NOTES AND QUESTIONS

1. Note that the 3-step burden-shifting framework for antitrust cases under the rule of reason is verbally approved by all members of the Court. The differences between the majority and the dissent go to how much the plaintiff must show in step one.

2. One of the unusual things about the majority opinion, as Justice Breyer noted repeatedly in his dissent, is that the majority paid very little attention to the district court record, ignoring several fact findings to the effect that the anti-steering rule was unreasonably exclusionary and resulted in higher prices, not merely for credit card transactions, but even for merchandise. These costs would be shared by all customers, no matter which card they used or even if they used cash. Should an appellate court, including the Supreme Court, have a duty either to rely on relevant lower court fact findings or else explicitly rejected them as not supported by the record? Significantly, while the Supreme

Court majority ignored many fact findings it never suggested that future appellate courts are free to ignore fact findings. Where does that leave them?

3. At one point Justice Breyer suggests that the case should be remanded so that American Express could show offsetting benefits, as step 2 of the rule of reason requires. What would those benefits be? And what kinds of facts would AmEx need to show to establish them? As Justice Breyer quoted the district court, 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."

4. The majority assumes that the harms on the merchant side of the market, where the challenged restraint occurred, were offset against benefits on the other side of the market. Indeed, that was the rationale for its inclusion of both sides in the same market. That might be the case when the only issue is distribution of revenue; for example, high advertising revenue might offset low magazine subscription prices, or vice-versa. But this case involved an exclusionary practice, which requires very different analysis. On a typical transaction the AmEx merchant acceptance fee is approximately 50% greater than the fee charged by competing general purpose credit cards. Suppose, for example, that on a purchase of a good AmEx's merchant fee was $30, but $20 for Visa, a representative rival. This $10 difference creates bargaining room for the merchant and the card holder to strike a mutually beneficial deal. Suppose, for example, that the merchant offers the customer a $6 discount for using Visa, which would make the customer $6 better off for that particular transaction and the merchant $4 better off. Both would benefit if the customer used the Visa card, and the customer would do it if the value it placed on AmEx's perks was less than the $6 price discount.

   The anti-steering provision prevents this transaction from occurring, however. As a result, the customer stays with the AmEx card and experiences a $6 loss, and the merchant also loses $4. So, far from being a situation where value goes up on one side and down on the other, it goes down on *both* the merchant side and the cardholder side of the platform. Further, the competing platform, Visa, is also worse off because it was denied the opportunity to offer a lower cost substitute transaction. The only entity that is better off is AmEx – not the dealing partners on one or the other side of the platform, but the owner of the platform itself. It is better off in part because the AmEx card holder did not place much value on the AmEx perks. The AmEx card holders most likely to switch are those that would benefit most from using a different card.

   To be sure, other AmEx card holders would decline the merchant's offer to switch, because for them the value of the perks might be as high as the merchant's acceptance fee, or at least as high as that portion of the fee that the merchant offered them for switching. As the district court found, "…even if a merchant is inclined to steer away from American Express, the cardholder would still have the freedom to use an Amex card if the cardholder decides the rewards offered by American Express are of greater value than the discount…." Card holders whose behavior was actually changed by the antisteering rule were worse off as a result of the rule, thus creating lost value on both sides of the platform.

The only factor that might make this situation welfare positive would be if keeping the transaction was necessary to making AmEx's business model viable. And if so, does that provide a benefit to competition in excess of costs? For example, AmEx might argue that it needs a certain minimum transaction volume coupled with higher prices in order to be profitable. But that query does not depend on whether there is one market or two. Indeed, it does not even depend on the existence of a platform, but only on the existence of scale economies and examination of the welfare effects of Amex's keeping both its volume and its margins high. These are core issues in industrial organization, such as economics of scale in processing transactions on the platform, and the number of transactions that the platform needs to maintain profitability. See Erik N. Hovenkamp, Platform Antitrust, ___ J. Corp. L. __ (2019), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3121481.

5. What does the majority mean when it concludes that the anti-steering provision is procompetitive because it induces "welcome acceptance" of the AmEx card. Isn't this simply saying that customers should not be informed that an alternative transaction is cheaper? If a customer is about to purchase Brand A and a merchant says "Brand B is equally good but cheaper," that certainly diminishes "welcome acceptance" of Brand A, but isn't that what competition is all about?

   The majority states that the anti-steering rule is intended to control for an "externality," and likens the case to *Leegin*, printed at the beginning of this chapter. That decision observed that a manufacturer might use resale price maintenance in order to control free riding. Did the majority assume that someone could receive the AmEx card perks simply by owning the card? If that were the case, free riding would be possible: someone could acquire the card in order to obtain the perks, but then use a less costly card to make actual purchases. As the dissent pointed out, however, one received AmEx perks only by actually *using* the AmEx card. As a result the customer paid the full costs of substituting to a different card and steering simply provided the customer with the information that it needed to decide which between the two alternatives – a higher priced product but AmEx's perks, or a lower priced product but with the presumably fewer perks -- could provide. There is no free riding.
6. The dissent characterized the relationship between the merchant side and the card holder side of the transaction as "complements," noting that grouping complements, such as automobiles and tires, into the same market is "economic nonsense." The majority disagreed in a footnote, stating that they were not complements because they were not "bought by the same buyers." The two sides were clearly complements, but they were complements in production rather than in use. Complements in production are goods that are produced together, although they may or may not be consumed together. Examples are beef and cowhide, oil and natural gas, or voice communications and texting. Many goods, such as a truck and an SUV are partial complements in production – they go through the same production process until the very end, when they are outfitted differently. Cardholder and merchant transactions across a credit card platform are

virtually perfect complements in production, more like beef and cowhide, because each credit card purchase is simultaneously accompanied by an equal merchant transaction.

7. The majority concludes that the fact that the output of credit card transactions grew 30% belies any idea that the price increases restricted output. This is an example of the static market fallacy, or simply assuming that everything else in a market remained unchanged during the relevant time period. The static market fallacy is relatively common, and it caustions that we must compare the effect of a restraint, not against actual output, bur rather against output in a but for world in which the restraint was absent.
8. One common concern about health care costs is that they are so high because patients are indifferent to prices. First, they are paid indirectly by insurers. Second, most patients do not even pay the insurance premium. Rather it is paid by either an employer or a government agency. As a result, the patient pays only a small portion of the medical bill and is inclined to spend too much. Doesn't the *AmEx* antisteering rule operate in the same way, making cardholders indifferent to merchant costs and thus diminishing the consumer incentive to reduce them.
9. The majority's definition of a single "relevant market" for the two sides of a platform is highly controversial and undermines a fundamental principle of neoclassical economics that is more than a century old – that is, that an economic "market" consists of goods that compete with one another. Was that definition necessary to the Court's analysis? The dissent clearly thought not. Isn't it possible to assess offsetting benefits even if they are found to occur within a different market? The majority does narrow the scope of its holding, concluding that it does not apply to all platforms but only those that "facilitate a single, simultaneous transaction" between the two sides. It then gives magazine or newspaper advertising as an example of a two-sided platform that does not meet this test. Although advertising revenue comes in one side and subscriptions on the other, there is not a simultaneous one-to-one relationship between them.

   It is also important to limit the market definition holding to true "platforms." Consider Netflix, for example. Netflix actually purchases a nonexclusive license to a movie or other program, and then sells the right to watch that program to the subscriber. As a result the requirement of a simultaneous transaction between seller and buyer is not met. Likewise, for most transactions Amazon actually purchases goods and then resells them to customers on its website. In these cases there is not a two-sided market at all, but only Amazon as seller and the purchaser as buyer.

   Is Realtor.com a two-sided market? Google Search or Bing? Match.com? Facebook? Spotify or Pandora? Uber or Lyft? AirBnB? How about the market for Apps on Google Play for Android devices, or the App Store for Apple devices? What about healthcare networks, where insureds pay monthly premiums on one side and providers are compensated for individual services on the other?
10. What about the majority's new rule that assessing market power directly in a vertical case requires a market definition, even though it does not in a vertical case.

Chapter 6 MONOPOLY STRUCTURE, POWER, AND CONDUCT

II THE MODERN MONOPOLIZATION OFFENSE: POWER

[A] Market Power, Barriers to Entry, and the Relevant Market

p. 657, append this note:

6. In *Lenox MacLaren Surgical Corp. v. Medtronic, Inc.*, 762 F.3d 1114 (10th Cir. 2014), the Tenth Circuit affirmed a district court's denial of summary judgment to a Section 2 defendant (Medtronic) accused of monopolizing the market for surgical bone mills – medical devices used in spinal-fusion surgery. The defendant argued that the market should include hand tools such as scalpels and scissors, which would render the defendant's market share too small to constitute a monopoly. The Tenth Circuit concluded that "[t]he differing definitions create a fact question on the product market, precluding summary judgment. For three reasons, a fact-finder could reasonably conclude that the relevant product market includes bone mills but excludes hand tools: (1) [the plaintiff] presented expert testimony that substantial price changes would not lead surgeons to switch from bone mills to hand tools; (2) a substantial price difference exists between hand tools and bone mills; and (3) Medtronic's market literature identifies its competition as other companies' bone mills, not hand tools."

[B] The Geographic Market

p. 668, append this note:

5. In *It's My Party, Inc. v. Live Nation, Inc.*, 811 F.3d 676 (4th Cir. 2016), the Fourth Circuit rejected a local concert promoter's attempt to define the promotion market as national, which would have made the defendant – a promoter with a nationwide network – appear to have significant market power. The court reasoned that the market was local, in part, because the demand for concerts is local and advertising is local, which means that "market dynamics favor promoters familiar with local media outlets and the local audience." Consequently, the court held that the relevant market was concert promotion in the Washington–Baltimore area. The court also rejected the plaintiff's attempt to define the venue market in an artificially narrow manner – "'major amphitheaters' [with] large outdoor spaces suitable only for popular artists, while excluding clubs, arenas, stadiums, and other venues" – that made the plaintiff and the defendant the only two participants in the market. The court observed that the plaintiff's "approach is akin to defining a market to include tennis players who have won more than three Olympic gold medals and finding that only Venus and Serena Williams fit the bill."

III THE MODERN MONOPOLIZATION OFFENSE: CONDUCT

[A] Innovation and Exclusion

p. 682, append this paragraph to the end of note 5:

In *New York ex rel. Schneiderman v. Actavis PLC*, 787 F.3d 638 (2d Cir. 2015), the Second Circuit explained that "neither product withdrawal nor product improvement alone is anticompetitive. But under *Berkey Photo,* when a monopolist *combines* product withdrawal with some other conduct, the overall effect of which is to coerce consumers rather than persuade them on the merits, and to impede competition, its actions are anticompetitive under the Sherman Act." *Id*. (emphasis in original) (citations omitted). Under this articulation of the law, did the courts reach the correct results in *Berkey Photo*, *California Computer*, and *C.R. Bard?*

[D] Vertical Integration, Refusals to Deal and Exclusionary Contracting

[1] The Monopolist's Refusal to Deal and the Essential Facility Doctrine

p. 785, append this note:

8. In *In re Adderall XR Antitrust Litigation*, 754 F.3d 128 (2d Cir. 2014), the Second Circuit affirmed dismissal of drug wholesalers' claims that a pharmaceutical company (Shire) violated Section Two by breaching contracts to supply its rivals with an unbranded version of a drug that the rivals would have resold to the wholesalers for less than the wholesalers had to pay for the branded version. The contracts were settlement agreements to resolve patent litigation. The wholesaler-plaintiffs claimed that the contracts created a "duty to deal" under antitrust law. The Second Circuit distinguished *Aspen Skiing* because "Shire did not terminate any prior course of dealing—let alone a 'presumably profitable' one that had, as in *Aspen Skiing,* 'originated in a competitive market and had persisted for several years.'" *In re Adderall*, 754 F.3d at 135 (quoting *Aspen Skiing*). The court explained:

> This is not a case where the alleged monopolist sought to "terminate a prior (voluntary) course of dealing with a competitor," *In re Elevator Antitrust Litig.,* 502 F.3d at 53 (citing *Trinko,* 540 U.S. at 409), under circumstances that evince an intent willfully to acquire or maintain monopoly power, *Trinko,* 540 U.S. at 407. The mere existence of a contractual duty to supply goods does not by itself give rise to an antitrust "duty to deal."

In re Adderall, 754 F.3d at 135.

[2] Exclusionary Contracting by the Monopolist

p. 808, append this note:

4. In *Kolon Industries Inc. v. E.I. DuPont de Nemours & Co.*, 748 F.3d 160 (4th Cir. 2014), Kolon claimed that DuPont had illegally monopolized the market for para-aramid – a synthetic fiber used in body armor, tires, and fiber optic cables, among other uses – by using exclusive supply agreements. The district court granted summary judgment to DuPont, in part because DuPont had exclusive supply agreements with only 21 of approximately 1,000 potential customers. The Fourth Circuit affirmed, explaining that:

> [the district] court rejected Kolon's argument that DuPont's twenty-one supply arrangements substantially foreclosed the entire relevant market by blocking Kolon from

> crossing a "critical bridge" to "high volume" customers. On appeal, Kolon again stresses its "critical bridge" theory. … Pointing to evidence that DuPont perceived Kolon's market entry as a threat, Kolon argues that DuPont "strategically entered into supply agreements with high-volume customers in the key commercially sustainable entry segments ... that Kolon sought to enter." Kolon submits that despite the relatively low number and short duration of DuPont's supply agreements, these agreements "choked off the 'critical bridge' to Kolon's entry into the U.S. market" because they foreclosed Kolon's access to the most important high-volume customers. …
>
> While we acknowledge that a singular emphasis on the percentage of *customers* foreclosed cannot resolve the inquiry (as foreclosure of a few important customers could substantially foreclose access to a market), we agree with the district court that Kolon failed to show what "proportionate volume of commerce" in the entire relevant market was foreclosed by DuPont's supply agreements. [citations omitted] Likewise, although Kolon's "critical bridge" theory is certainly plausible, the evidence does not support its application here.
>
> Unlike the plaintiffs in *Dentsply* and *LePage's,* Kolon offered no evidence that access to the foreclosed customers (or even to the identified market segments) was necessary to achieve scale in the broader U.S. para-aramid market. And even if we assume the significance of those customers and market segments, Kolon does not dispute that DuPont had supply agreements with fewer than half of its identified "key" customers within those segments.
>
> Meanwhile, DuPont persuasively distinguishes *Dentsply* and *LePage's* based on the fact that the defendants in those "critical bridge" cases foreclosed the plaintiffs' access to distribution networks rather than end-customers. We are not convinced that, as Kolon contends, this is "a distinction without a difference." As the district court observed, unlike with Dentsply's and 3M's agreements that foreclosed access to distribution networks shown to be necessary to reach many end-customers, "the record presents no reason to think that Kolon could not sell to other customers occupying the same segment of the para-aramid market ... as customers that have supply agreements with DuPont."
>
> In sum, we conclude that neither the probable nor the actual effect of DuPont's supply agreements was to "foreclose competition in a substantial share of the line of commerce affected." *Tampa Elec.,* 365 U.S. at 327. Accordingly, those agreements do not violate the willful maintenance prong of our § 2 monopolization inquiry. Because Kolon failed to raise a genuine issue of material fact as to either prong, summary judgment was appropriate on its monopolization claim.

Kolon Indus., 748 F.3d at 176-77.

p. 824, insert prior to Notes and Questions:

PHILADELPHIA TAXI ASSN. V. UBER TECHNOLOGIES, INC.
886 F.3d 332 (3d Cir. 2018), pet. for cert. filed, Jn. 25, 2018

Before: AMBRO, KRAUSE, and RENDELL, Circuit Judges

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.[5] 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

[5]We are aware that the issue of whether drivers can be classified as employees or independent contractors is the subject of ongoing litigation. See, e.g., Razak v. Uber Techs., Inc., No. 16-cv-573, 2017 WL 4052417 (E.D. Pa. Sept. 13, 2017).

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 taxicab 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.

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….

II. Standard of Review

We accept as true the factual allegations in the complaint, and draw all reasonable inferences in the plaintiff's favor. W. Penn Allegheny Health Sys., Inc. v. UPMC, 627 F.3d 85, 91 (3d Cir. 2010).

III. Discussion

Competition is at the heart of the antitrust laws; it is only anticompetitive conduct, or "a competition-reducing aspect or effect of the defendant's behavior," that antitrust laws seek to curtail. Atl. Richfield Co. v. USA Petroleum Co., 495 U.S. 328, 344, 110 S.Ct. 1884, 109 L.Ed.2d 333 (1990). "[I]t is inimical to the antitrust laws to award damages for losses stemming from continued competition." Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 109–10, 107 S.Ct. 484, 93 L.Ed.2d 427 (1986) (alternations and internal quotation marks omitted). This comports with the principle underlying antitrust laws: to protect competition, not competitors. See Brown Shoe Co. v. United States, 370 U.S. 294, 320, 82 S.Ct. 1502, 8 L.Ed.2d 510 (1962).

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. … 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)). Moreover, to survive a motion to dismiss under Rule 12(b)(6), the claim must be "plausible on its face," allowing us to "draw the reasonable inference that the defendant is liable for the misconduct alleged." Ashcroft v. Iqbal, 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009) (quoting Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570, 127 S.Ct. 1955, 167 L.Ed.2d 929 (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.

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. 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….

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,[6] benefit consumers—"regardless of how those prices are set." Atl. Richfield, 495 U.S. at 340, 110 S.Ct. 1884. "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, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986). Thus, lost business alone cannot be deemed a consequence of "anticompetitive" acts by the defendant. See Atl. Richfield, 495 U.S. at 337, 110 S.Ct. 1884.

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. …

Some courts have inferred specific intent from anticompetitive or exclusionary conduct, Advo, Inc. v. Philadelphia Newspapers, Inc., 51 F.3d 1191, 1199 (3d Cir. 1995), for instance, when business conduct is "not related to any apparent efficiency." Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 608 n.39 (1985) (quoting R. Bork, The Antitrust Paradox 157 (1978); see also 4 Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law ¶ 805d, (4th ed. 2017) (discussing how some courts "would find for the plaintiff only if the defendant's acts were not motivated by 'reasonable' or 'legitimate' business purposes").

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

[6] To allege predatory pricing, a plaintiff must first demonstrate that prices are set below costs, and that the competitor had a dangerous probability of recouping those lost profits after it had driven other competitors out of the market. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222, 224 (1993). Appellants have not alleged predatory pricing in this case.

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, 73 S.Ct. 872, 97 L.Ed. 1277 (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. "[E]asy entry—particularly historical evidence of entry—is even more significant in the attempt case than in monopolization cases generally." Areeda & Hovenkamp, ¶ 807a.[7] 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,

[7]Areeda and Hovenkamp explain that in an attempt case, when "the defendant is not yet a monopolist," market prices are more competitive. ¶ 807g. On the other hand, "[i]n a monopolization case the defendant is already a dominant firm and the market already presumably exhibits monopoly prices that have not been effectively disciplined by new entry." Id. Thus, easy entry into the market is indicative that the market lacks barriers to entry that may otherwise protect a dominant firm's monopoly power. Id.

this would encourage other rivals to enter the market and charge lower prices, battling Uber through price competition….

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.

III. Antitrust Standing

Alternatively, Appellants' antitrust claim fails for lack of antitrust standing, which is a threshold requirement in any antitrust case. Rooted in prudential principles, antitrust standing is distinct from Article III standing, which is rooted in the Constitution. Ethypharm S.A. Fr. v. Abbott Labs., 707 F.3d 223, 232 (3d Cir. 2013).7 While "[h]arm to the antitrust plaintiff is sufficient to satisfy the constitutional standing requirement of injury in fact," courts must also consider "whether the plaintiff is a proper party to bring a private antitrust action." Associated Gen. Contractors of Cal., Inc. v. Cal. State Council of Carpenters, 459 U.S. 519, 535 n.31, 103 S.Ct. 897, 74 L.Ed.2d 723 (1983); see also Areeda & Hovenkamp, ¶ 335.

Of the requirements for antitrust standing, antitrust injury is "a necessary but insufficient condition," and is the only requirement in dispute here…. In Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., the Supreme Court rejected the notion that antitrust injury could be alleged by a private plaintiff averring that it would have fared better without the defendant's alleged conduct. 429 U.S. 477. Rather, the plaintiff must prove the existence of an antitrust injury, which is an "injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful."… The injury must "reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation."…

Compensating plaintiffs injured by the effects of truly anticompetitive conduct serves the purpose of antitrust laws, namely, to foster competition. Thus, the antitrust injury requirement ensures that damages are only awarded for losses that "correspond[ ] to the rationale for finding a violation of the antitrust laws in the first place." Atl. Richfield, 495 U.S. at 342; Areeda & Hovenkamp, ¶ 337a.

Appellants decry Uber's entry into Philadelphia as a campaign to inflict economic harm and to cause Appellants to lose their market share. They argue that all vehicles-for-hire legally operating in Philadelphia, and the riding public, have been harmed by Uber's allegedly illegal presence in Philadelphia between October of 2014 and October of 2016, when TNCs were officially permitted to operate. Appellants allege that they experienced financial harm and a reduced market share through fewer drivers, medallion cabs sitting idle, a decline in ridership, and loss of medallion value. The effect of the decrease in earnings, Appellants argue, is that taxicab companies are nearing default on their medallions and are close to being driven out of business.

Appellants allege their own injury, namely, financial hardship. Tellingly, they fail to aver an antitrust injury, such as a negative impact on consumers or to competition in general, let alone any link between this impact and the harms Appellants have suffered.9 Perhaps this is because Appellants cannot do so. According to Appellants' own pleadings, Uber's entry into the Philadelphia market, regardless of its legality, increased the number of vehicles-for-hire available to consumers and product differentiation in the market, thereby increasing competition.

The facts of *Brunswick* illustrate this point. There, a bowling equipment manufacturer acquired several failing bowling alleys that had defaulted ontheir equipment payments. Three active bowling alleys brought an antitrust claim against the manufacturer, arguing that if the alleys had been allowed to fail, former patrons would have frequented plaintiffs' alleys, increasing plaintiffs' profits and market share.

The Supreme Court held that even if the acquisition was unlawful because it provided the manufacturer with monopoly power, the plaintiffs failed to prove that there were anticompetitive effects of that acquisition in order to establish an antitrust injury. Plaintiffs sought to recover lost profits from bolstered competition—the manufacturer's keeping the defaulting alleys in business. Id. The presence of more bowling alleys resulted in more competition, and thus the Supreme Court held that plaintiffs had not sustained an antitrust injury.

Similarly here, Appellants urge the application of antitrust laws for the express opposite purpose of antitrust laws: to compensate for their loss of profits due to increased competition from Uber. However, harm to Appellants' business does not equal harm to competition. "Conduct that merely harms competitors, ... while not harming the competitive process itself, is not anticompetitive." Broadcom, 501 F.3d at 308. Were we to award Appellants antitrust damages to compensate for their financial injuries, we would condemn vigorous competition, rather than encourage it. See Travelers Ins. Co. v. Blue Cross of W. Pa., 481 F.2d 80, 84 (3d Cir. 1973).

Without demonstrating a harmful effect on price, such as predatory or monopoly pricing, Appellants instead argue that Uber's ability to operate at a lower cost caused Appellants economic harm and caused Appellants to lose their market share. But Appellants never argue that the lower cost—evidence of increased competition—failed to result in lower prices for consumers. "A plaintiff who wants ... less competition or higher prices, that would injure consumers, does not suffer antitrust injury." U.S. Gypsum Co. v. Ind. Gas Co., 350 F.3d 623, 627 (7th Cir. 2003).

Nor do Appellants aver a negative effect on the availability of taxicab services. Appellants themselves admit that Uber's 1700 vehicles took over 700,000 riders on more than one million trips in its first two years in Philadelphia, while the number of medallion cabs allegedly decreased by at least 15 percent, or roughly 240 vehicles, from its peak of 1610. Thus, the SAC alleges an increase in the availability of vehicles-for-hire for Philadelphia passengers.

Appellants also insist that Uber's alleged illegal presence in Philadelphia caused an antitrust violation. They attempt to circumvent the antitrust injury requirement by focusing on how Uber's purportedly illegal operation enabled it to cut costs and increase its market share. But again, the Supreme Court has squarely rejected illegal conduct as a basis for antitrust injury. A competitor's illegal presence in a market is not a per se antitrust violation, and any resulting injury is alone insufficient for a private plaintiff to state an antitrust injury. Atl. Richfield, 495 U.S. at 334, 110 S.Ct. 1884 (quoting Brunswick, 429 U.S. at 489, 97 S.Ct. 690).

Finally, Appellants do not cite any case in support of the contention that Uber's violation of state regulations, even if that gave Uber a competitive advantage, renders its operation in violation of antitrust laws. Even if we were to find Uber's operation in Philadelphia unlawful in its first two years, we would do so under PPA regulations, and not under antitrust laws. Ultimately, Uber's presence in the market, as alleged, created more competition for medallion taxicabs, not less, and thus Uber's so-called "predation"—operating without medallions or certificates of public convenience—does not give rise to an antitrust injury.

In sum, we affirm the dismissal of the SAC for the additional reason that it fails to assert an antitrust injury….

V. Conclusion

….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.

Chapter 7 MERGERS AND ACQUISITIONS

INTRODUCTION

I. VERTICAL INTEGRATION THROUGH MERGER

COMPLAINT: UNITED STATES OF AMERICA V. AT&T, INC., DIRECTV GROUP HOLDINGS, LLC, AND TIME WARNER INC.

(Filed November 20, 2017)

First, the merger would result in higher prices for consumers of traditional subscription television because it would give the merged company the power to raise the prices that competing video distributors pay to it for Time Warner's popular TV networks for no reason other than that those networks would now be owned by AT&T/DirecTV. Time Warner's networks are some of the most valuable in the country. . . . Nonetheless, there is currently a limit to what video distributors will agree to pay Time Warner for its Turner networks. If, in negotiations, Time Warner seeks too high a price for the Turner TV networks, the video distributor across the table may walk away. Without a deal, Time Warner loses monthly payments from the video distributor and advertising revenue—and gains nothing in return. This merger, if allowed, would change that. After the merger, if the merged company raised prices of the Turner networks to the video distributor and no deal were reached, resulting in a blackout of such networks, the merged company would still lose monthly payments and advertising revenue from the video distributor with whom it could not reach a deal, but, importantly, it would now get an offsetting benefit. Because the video distributor walking away from a deal with the merged company would lose access to Turner's popular programming, some of the video distributor's valuable customers would be dissatisfied and switch to a competing video distributor. Some of those departing customers would sign up with AT&T/DirecTV, bringing with them significant new profits for the merged company. . . .

Second, the merger would enable the merged company to impede disruptive competition from online video distributors . . . AT&T/DirecTV perceives online video distribution as an attack on its business that could, in its own words, "deteriorate[] the value of the bundle." Accordingly, AT&T/DirecTV intends to "work to make [online video services] less attractive." AT&T/DirecTV executives have concluded that the "runway" for the decline of traditional pay-TV "may be longer than some think given the economics of the space," and that it is "upon us to utilize our assets to extend that runway." This merger would give the merged firm key, valuable assets, empowering it to do just that. . . . After the merger, the merged firm would likely use Turner's important programming to hinder these online video distributors—for example, the merged firm would have the incentive and ability to charge more for Turner's popular networks and take other actions to impede entrants that might otherwise threaten the merged firm's high profit, big-bundle, traditional pay-TV model. The merger would also make oligopolistic coordination more likely. For example, the merger would align the structures of the two largest traditional video distributors, who would have the incentive and ability to coordinate to impede competition from innovative online rivals and result in higher prices. . . .

INDUSTRY BACKGROUND

Popular television shows like *The Big Bang Theory* generally travel through three layers of production and distribution: A studio like Warner Bros. creates the show; a programmer like Turner or a broadcaster like CBS purchases the right to include the show on one of its networks; and a video distributor like AT&T/DirecTV or Comcast purchases the right to include the network in one or more packages that it sells to customers. . . .

Programmers make money by licensing their networks to video distributors and by selling air time for advertisements shown on their networks. Accordingly, programmers generally seek to have their networks carried by many video distributors. They typically reach multi-year agreements under which video distributors pay programmers monthly, per-subscriber license or "affiliate" fees for a bundle of networks owned by the programmer. Programmers' arms-length negotiations with video distributors involve a give and take based on the relative bargaining leverage of the parties, which is informed by the options available to each party in the event a deal is not reached. Video distributors make money by receiving monthly subscriber fees from their customers and need to carry popular programming to attract those customers. So programmers with popular networks that carry hit shows and live sports have more bargaining leverage with video distributors than do programmers with less popular networks. Programmers also gain revenue through advertising, the price of which is typically based on the number of consumers watching their networks. . . .

ANTICOMPETITIVE EFFECTS

. . . In the event an MVPD or virtual MVPD does not carry a group of popular networks, most customers who leave that distributor in response to that blackout will look elsewhere for a comparable video distributor that still offers those networks. Because AT&T/DirecTV has an MVPD that it offers throughout the United States, it stands to gain a significant number of new customers in the event a rival MVPD or virtual MVPD is foreclosed from carrying certain popular networks that the merged company continues to carry—i.e., a blackout.

Accordingly, were this merger to go forward, the merged company could "more credibly threaten to withhold" Turner's popular programming—including the hit shows and live sporting events carried by TNT, TBS, and Cartoon Network—as leverage in its negotiations with MVPDs and virtual MVPDs. . . . In fact, MVPDs have done studies to determine the subscriber loss that would occur if they did not have the popular networks Time Warner owns. Unsurprisingly, given the popularity of Turner's networks—which carry hit shows and important live sports events—these studies confirm that the anticipated subscriber loss rate is likely to be significant. In addition, because the merged company would know beforehand that the rival MVPD would soon lack Turner programming, the merged company would be in a particularly strong position, as a result of the merger, to target the rival MVPD's customers with advertisements and telephone calls urging them to subscribe to AT&T/DirecTV's television offerings

The merged company's bargaining leverage as a seller of programming would thus increase, and not through the offering of lower prices or a superior product or service offering, but directly because of this proposed merger. Competing MVPDs and virtual MVPDs would thus recognize that it will make financial sense to pay the merged firm a higher price for Turner networks than it would prior to the merger, rather than risk losing valuable customers. And the merged company would know that it can extract higher rates for Turner's networks because, if no deal were reached, the merged firm would capture a significant number of the customers who would depart the competing MVPD or virtual MVPD's service, and it would have an improved chance to sign up new customers since one rival would lack Turner's highly popular programming. . . .

In addition, the merger would likely give the merged firm the incentive and ability to use its control of HBO to substantially lessen competition. Due to its strong brand and consumer recognition and demand, MVPDs (including AT&T/DirecTV) today use HBO as a tool to entice new customers and to dissuade unhappy customers from leaving and switching to a rival MVPD. Other premium channels, like Starz or Showtime, are not adequate alternatives to HBO for MVPDs seeking to attract or retain customers with premium content. . . .

In addition, the merger would increase the likelihood and effect of oligopolistic coordination, particularly among certain vertically integrated MVPDs. AT&T itself has noted the high levels of concentration within the pay-TV industry and their stabilizing effect. In a presentation prepared for a meeting with Time Warner executives related to this merger, AT&T noted that, after the merger, the merged company and just three other companies would control a large portion of all three levels of the industry: television studio revenue, network revenue, and distribution revenue. AT&T went on to explain that—given these high levels of concentration—its "Core Belief #1" is that, notwithstanding the emergence of online video distributors, "[t]he economic incentives of major pay-TV players will encourage **stability** as the ecosystem evolves." (Emphasis added.) . . .

UNITED STATES OF AMERICA V. AT&T, INC., ET AL.,
(310 F. Supp. 3d 161 (D.D.C. 2018))

Judge Richard Leon delivered the opinion of the court

The Government claims, in essence, that permitting AT&T to acquire Time Warner is likely to substantially lessen competition in the video programming and distribution market nationwide by enabling AT&T to use Time Warner's "must have" television content to either raise its rivals' video programming costs or, by way of a "blackout," drive those same rivals' customers to its subsidiary, DirecTV. Thus, according to the Government, consumers nationwide will be harmed by increased prices for access to Turner networks, notwithstanding the Government's concession that this vertical merger would result in hundreds of millions of dollars in annual cost savings to AT&T's customers and notwithstanding the fact that (unlike in "horizontal" mergers) no competitor will be eliminated by the merger's proposed vertical integration.

. . . AT&T, Time Warner, and DirecTV, strongly disagree. Their vision couldn't be more different. The video programming and distribution market, they point out, has been, and is, in the middle of a revolution where high-speed internet access has facilitated a "veritable explosion" of new, innovative video content and advertising offerings over the past five years. Vertically integrated entities like Netflix, Hulu, and Amazon have achieved remarkable success in creating and providing affordable, on-demand video content directly to viewers over the internet. . . . Indeed, cost-conscious consumers increasingly choose to "cut" or "shave" the cord, abandoning their traditional cable- or satellite- TV packages for cheaper content alternatives available over the internet.

IV. Legal Standard

[T]o grant injunctive relief under the Clayton Act, the Court *must* conclude that the Government has introduced evidence sufficient to show that the challenged "transaction is likely to lessen competition substantially." *Baker Hughes,* 908 F.2d at 985. As part of satisfying that burden, Section 7 "demand[s] that a plaintiff demonstrate that the substantial lessening of competition will be 'sufficiently probable and imminent' to warrant relief." *Arch Coal,* 329 F. Supp. 2d at 115 (quoting *United States* v. *Marine Bancorporation,* 418 U.S. 602,623 n.22 (1974)). . . . [I]n the absence of a crystal ball, "allocation of the burdens of proof assumes particular importance." *Baker Hughes,* 908 F.2d at 991. To further assist courts in this prospective inquiry, our Circuit has set forth a burden shifting framework for use in determining whether a proposed transaction violates the Clayton Act. *See, e.g., id.* at 982-83.

Under that framework, the Government must first establish its prima facie case by 1) identifying the relevant product and geographic market and 2) showing that the proposed merger is likely to "substantially lessen competition" in that market. *Id.* at 982, 991; *see also Arch Coal,* 329 F. Supp. 2d at 117. If the Government satisfies its prima facie burden, the burden then shifts to defendants to "provide sufficient evidence that the prima facie case 'inaccurately predicts the relevant transaction's probable effect on future competition.'" *United States v. Anthem, Inc.,* 855 F.3d 345, 349 (D.C. Cir. 2017) (quoting *Baker Hughes,* 908 F.2d at 991). One way defendants may do so is to offer evidence that "post-merger efficiencies will outweigh the merger's anticompetitive effects." *Heinz,* 246 F.3d at 721. If the defendants put forward sufficient evidence to rebut plaintiff's prima facie case, "the burden of producing additional evidence of anticompetitive effect shifts to the [government], and merges with the ultimate burden of persuasion, which remains with the [government] at all times." *Anthem,* 855 F.3d at 350 (quoting *Baker Hughes,* 908 F.2d at 983).

C. Antitrust Analysis of Vertical Mergers

. . . The parties [] agree that in this case "there is no short-cut to establish anticompetitive effects, as there is with horizontal mergers." . . . With no presumption of harm in play, the

Government concedes that, to satisfy its burden here, it must make a "fact-specific" showing that the effect of the proposed merger "is likely to be anticompetitive." Such a showing is "necessarily both highly complex" and "institution specific." . . . Of particular relevance here, the Government states that a vertical merger may "act as a clog on competition" by giving the merged firm "control of a competitively significant supplier." (quoting *Brown Shoe,* 370 U.S. at 324). Such a situation would occur, the Government continues, if the merged firm were to withhold a source of supply from its rivals or otherwise foreclose access to the source "on competitive terms," such as by causing its rivals to "pay[] more to procure necessary inputs," which in turn could "harm[] competition and consumers." . . .

Further complicating the Government's challenge is the recognition among academics, courts, and antitrust enforcement authorities alike that "many vertical mergers create vertical integration efficiencies between purchasers and sellers." Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach,* 63 Antitrust L.J. 513, 519 (1995). The proposed merger reflects that principle . . . As the Government also notes, the "principal objective of antitrust policy is to maximize consumer welfare by encouraging firms to behave competitively." . . . As such, any proper assessment of a proposed merger, Professor Shapiro testified, must consider both the positive and negative "impact[s] on consumers" by "balancing" the proconsumer, "positive elements" of the merger against the asserted anticompetitive harms. . . . Given all of the competing considerations at play, "the analysis of vertical mergers" has been described as "much more complex than the analysis of horizontal mergers.'" Scheffman & Higgins, *Vertical Mergers,* 12 Geo. Mason L. Rev. at 967. Things are made more difficult still by the lack of modern judicial precedent involving vertical merger challenges - a dearth of authority that is unsurprising, considering that the Antitrust Division apparently has not tried a vertical merger case to decision in *four* decades!

. . . To sum up, the Court accepts that vertical mergers "are not invariably innocuous," but instead can generate competitive harm "[i]n certain circumstances." Non-Horizontal Merger Guidelines §§ 4, 4.2. The case at hand therefore turns on whether, notwithstanding the proposed merger's conceded procompetitive effects, the Government has met its burden of proof of establishing, through "case-specific evidence," that the merger of AT&T and Time Warner, at this time and in this remarkably dynamic industry, is likely to substantially lessen competition in the manner it predicts. Unfortunately for the Government, for the following reasons, it did not meet its burden.

ANALYSIS

II. Conceded Consumer Benefits of Proposed Merger

. . . Vertical mergers often generate efficiencies and other procompetitive effects. The proposed merger is no exception. Indeed, the Government concedes that this case implicates one "standard benefit" associated with vertical mergers: the elimination of double marginalization ("EDM"). . . . As relevant here (and at the risk of oversimplifying things), double marginalization refers to the situation in which two different firms in the same industry, but at different levels in the supply chain, each apply their own markups (reflecting their own margins) in pricing their products. Those "stacked" margins are both incorporated into the final price that consumers have to pay for the end product. By vertically integrating two such firms into one, the merged company is able to "shrink that total margin so there's one instead of two," leading to lower prices for consumers. EDM is, therefore, procompetitive. . . .

III. The Government Has Failed to Meet Its Burden to Show That the Proposed Merger Is Likely to Substantially Lessen Competition by Increasing Turner's Bargaining Leverage in Affiliate Negotiations

The Government's primary theory of harm to competition focuses on the challenged merger's integration of Turner's important video content - content that includes, among other things, the networks CNN, TNT, and TBS - with AT&T's video distributors, U-verse and DirecTV. Specifically, the Government contends that, should the challenged merger proceed, Turner's relationship with AT&T will enable Turner to extract greater prices from AT&T's rival distributors for its "must-have" content than it could without the merger. The Government argues that distributors would then pass on those price increases to their subscribers, resulting in an increase of hundreds of millions of dollars in annual consumer payments. . . . Having heard and considered the evidence adduced at trial, I conclude that the Government has failed to clear the first hurdle of showing that the proposed merger is likely to increase Turner's bargaining leverage in affiliate negotiations . . .

A. Background of Increased-Leverage Theory of Harm

Given that blackouts [dropping programming because programmer and distributor could not reach agreement] are negative events for both programmers and distributors, however, deals between programmers and distributors are invariably struck in order to avoid long-term blackouts. . . . Indeed, when it comes to Turner, the record shows that there has *never* been a long-term blackout of the Turner networks. That fact is by no means lost on either side.

That background brings us to the Government's increased-leverage theory. Notably, under that theory, the Government does *not* allege that a post-merger Turner would be incentivized to start *actually* engaging in long-term blackouts with distributors. That is so, as Professor Shapiro concedes, because withholding Turner content would not be "profitable" to the merged entity given the attendant losses in significant advertising and affiliate fee revenues. In other words, and in contrast to a prevalent theory of vertical merger antitrust harm, Turner will not "foreclose" downstream distributors from accessing Turner content. . . . Instead, the Government's increased-leverage theory of harm posits that Turner's bargaining position in affiliate negotiations would improve after the merger due to its relationship with AT&T. That is so, the Government argues, because Turner and its distributor counterparties would recognize that, should Turner fail to strike a deal and engage in a long-term blackout with a distributor, Turner would no longer face the mere downside of losing affiliate fees and advertising revenues. Rather, some of those losses would be offset, according to the Government by new benefits to AT&T's video distribution companies via the following chain of events: 1) some of the rival distributor's customers would depart or fail to join the distributor due to the missing Turner content; 2) some portion of those lost customers would choose to sign up with AT&T's video distributors (which would have Turner); and 3) AT&T would profit from those gained subscribers. As a result, the Government predicts that Turner's downside position in the event of a blackout would improve as a result of the proposed merger. That improved downside position, according to the Government, would in turn enable Turner to demand higher prices for its content in post-merger affiliate fee negotiations with distributors - price increases that would ultimately be passed on to consumers. . . .

B. The Government's So-Called "Real-World Objective Evidence" Is Insufficient to Support Its Increased-Leverage Theory of Harm

To support its increased-leverage theory of harm, the Government first points to various pieces of the so-called "real-world objective evidence" it offered at trial. That evidence primarily consisted of defendants' ordinary course-of-business documents and excerpts of regulatory filings submitted by defendants in prior administrative proceedings, as well as the testimony of third-party witnesses from AT&T's rival distribution companies. Of particular importance here, the Government's so-called real-world evidence was directed at explaining and establishing two main concepts. First, the Government sought to establish the importance of Turner content to distributors and the resulting leverage Turner enjoys in affiliate fee negotiations. Second, the Government relied on this so-called "real-world objective evidence" to substantiate its prediction that Turner's leverage with distributors would *increase* as a result of Turner's post-merger relationship with AT&T.

1. *Evidence Regarding the Popularity of Turner Content Is of Limited Probative Value in Evaluating the Contention That Turner Will Gain Increased Leverage Due to the Proposed Merger*

. . . Based on the evidence, I agree with defendants that Turner's content is not *literally* "must have" in the sense that distributors cannot effectively compete without it. The evidence showed that distributors have successfully operated, and continue to operate, without the Turner networks or similar programming. . . . I therefore give little credit to blanket statements by third-party competitor witnesses indicating that the entire "viability of [their] video model" could depend on whether they offer Turner programming. [Citing several examples from the record] Such statements were largely unaccompanied by any sort of factual analyses or, worse, contradicted by real-world examples from the witnesses themselves. ("Q: And so today, you're not offering this Court any empirical data or any real-world evidence of subscriber losses if RCN didn't have Turner, right? A: No, not our company."). . . . Indeed, the evidence indicated that the term "must have" is a marketing phrase used by virtually every programmer to suggest that its content is popular with viewers. . . .

I do nonetheless accept the Government's contention that Turner has popular content - especially live sporting events and live news - and, as a result, enjoys bargaining leverage with distributors. Importantly, however, accepting that straightforward proposition - *i.e.,* that popular programmers such as Turner are able to demand more for their content than less popular programmers - does not prove that the challenged *merger* would harm competition pursuant to the Government's increased-leverage theory of harm. To prove its increased-leverage theory, in other words, it is not sufficient for the Government to put forward evidence that Turner has important content and thus bargaining leverage – that fact is true today, pre-merger. Rather, the Government's increased-leverage theory posits that Turner's pre-merger bargaining leverage would materially increase as a result of its post-merger relationship with AT&T and that, as a result, distributors would cede greater affiliate fees than they would absent the merger. . . .

2. Defendant's Own Statements and Documents Provide Little Support for the Contention That Turner Will Gain Increased Leverage Due to the Proposed Merger

Generic statements that vertical integration *"can"* allow the integrated entity to gain an "unfair advantage over its rivals," do not come close to answering the question before the Court in relation to the Government's increased-leverage theory: whether the Government has carried its Section 7 burden to show, through proof at trial, that Time Warner will gain increased bargaining leverage in affiliate negotiations on account of the proposed merger and, if so, whether that increased bargaining leverage would result in increased distributor or consumer costs that would constitute a substantial lessening of competition under Section 7.

. . . Given all that, defendants' specific predictions regarding the ability of a merged Comcast-NBCU to leverage price increases by threatening to withhold the particular programming at issue is not particularly probative of whether a merged AT&T-Time Warner could do the same with its programming in today's more competitive marketplace. . . . Moreover, as discussed in more detail below, defendants' expert Professor Carlton concluded in an econometric analysis of content pricing following the Comcast-NBCU merger that, contrary to the predictions offered by competitors in the regulatory filings, the merger did *not* cause content prices to increase. . . .

3. Third-Party Competitor Witness Testimony Provides Little Support for the Contention That Turner Will Gain Increased Leverage Due to the Proposed Merger

Much of the third-party competitor testimony I heard consisted of speculative concerns regarding how the witnesses thought Turner might act in negotiations after the merger. Some witnesses simply accepted key assumptions of the Government's increased-leverage theory without any supporting analysis or data. For example, testimony from the Government's lead-off witness, Cox negotiator Suzanne Fenwick, helps to illustrate both of those problems. When asked on direct examination about her views of the proposed merger, Fenwick stated that she is "very concerned" that, post-merger, Cox would be presented by Turner with "a horribly ugly deal and that when faced with that deal, we have to think about that if we do go dark, they have a benefit in picking up Cox customers" via DirecTV. Fenwick continued that, as a result of that "benefit that is created in this merger that isn't there today," the negotiating "leverage changes" and that AT&T "has a different incentive now than they had before" - namely, the incentive to "pick up customers" lost by Cox in a Turner blackout. Fenwick's speculation about how Turner might act relies on certain key assumptions for which she had no factual basis. Indeed, the amount of customers that distributors would lose as a result of a Turner blackout (not to mention the resulting "benefit" to AT&T), is one of the central disputes in this case. . . .

4. Real-World Evidence Indicating That Prior Vertical Integration of Programmers and Distributors Has Not Affected Affiliate Fee Negotiations Undermines the Government's Increased-Leverage Theory of Harm

. . . That conclusion is further bolstered by evidence relating to three prior instances of vertical integration in the video programming and distribution industry: 1) News Corp., a programmer, acquiring part of DirecTV in 2003 and then spinning it off in 2008; 2) the 2009 split of Time Warner, a programmer, from Time Warner Cable, a MVPD; and 3) the 2011 combination of Comcast, a distributor, and NBCU, a programmer. . . .

a. Professor Carlton's Econometric Analyses of Prior Vertical Transactions Found No Statistically Significant Effects on Content Pricing

When it comes to evaluating the antitrust implications of proposed mergers, both Professor Shapiro and Professor Carlton recognize that empirical analysis of prior, similar transactions can be "convincing evidence." *cf* Horizontal Merger Guidelines § 2.1.2 ("The Agencies look for historical events, or 'natural experiments,' that are informative regarding the competitive effects of the merger. For example, the Agencies may examine the impact of recent mergers, entry, expansion, or exit in the relevant market."). In this case, however, neither the Government nor Professor Shapiro presented original analysis of any prior vertical transactions in this industry. . . .

Defendants, by contrast, did seek to analyze the available pricing data resulting from prior instances of vertical integration. . . . Defendants' lead economic expert, Professor Dennis Carlton, then analyzed that third-party pricing data, among other proprietary and public-source data in his possession. to test whether it is "true that content prices are higher on a network when it's sold by someone who's vertically integrated." Specifically, Professor Carlton performed a "regression analysis or an econometric analysis, which is a statistical attempt to answer the question precisely." In running his regressions, Professor Carlton used different "statistical techniques to analyze the problem in a variety of ways." All of that analysis, Professor Carlton testified, generated "completely consistent" results across all three examples he considered: "There's absolutely no statistical basis to support the government's claim that vertical integration in this industry leads to higher content prices." . . .

Professor Shapiro and the Government [] denounced Professor Carlton's analysis on the basis that the prior vertical transactions are not sufficiently similar to the challenged merger. They pointed out, for example, that two of the prior transactions involved regional cable distributors (Comcast and Time Warner Cable), whereas the challenged merger involves DirecTV, which operates nationally. Regional operation means, Professor Shapiro testified, that one would "not expect[] to see evidence of post-merger price increases beyond the overall industry increases" because "most of the MVPDs . . . don't compete with Comcast," for example. Professor Carlton explained, however, that the regional versus national distinction is "irrelevant" when it comes to his analysis of DirecTV and DISH prices; that is so, Professor Carlton stated, because those two satellite companies compete "everywhere" the regional cable companies operate and it is the "national share" that matters to Professor Shapiro's bargaining model. To the extent the Government is now arguing that one would not expect to see *any* increased-leverage harm due to Comcast's status as a regional distributor, I simply note that the Government argued to the contrary prior to this case. *See, generally, e.g.,* Compl., *Comcast Corp.,* 808 F. Supp. 2d 145 (No. 11-cv-106).

Finally, the Government and Professor Shapiro note that the prior vertical transactions all were "remediated" by regulatory or court-ordered conditions – conditions that will not apply to the challenged merger. Professor Carlton agrees that, in theory, his study's conclusions would be affected if the conditions associated with the prior transactions were not "sufficiently similar" to those at issue here. I will thus briefly address Turner's 2017 arbitration offer and its relation to the conditions on the Comcast-NBCU transaction.

The arbitration proceedings envisioned by Turner's offer are similar in many of "the fundamental ways" to those blessed by the FCC, DOJ, and this Court in the Comcast-NBCU merger. Most notably, both arbitration arrangements are "baseball-style": each party puts forward a final offer before knowing about its counterparty's offer, and the arbitrator chooses between those two. In addition, both sets of arbitration arrangements contain "standstill provisions," which prevent the blackout of content while the arbitration is pending. They also both set out "fair market value" as the standard, and have similar discovery procedures. As Professor Katz testified, "the objective is the same. The overall structure the same. So they are similar overall." Given all of these similarities, I conclude that Professor Carlton's econometric analysis of the pricing effects of the Comcast-NBCU combination can be afforded probative weight in predicting the potential pricing effects of the challenged merger. . . .

b. Executives from Vertically Integrated Programmers and Distributors Testified That Vertical Integration Does Not Affect Affiliate Fee Negotiations

. . . Consideration of potential Comcast gains during an NBCU blackout "doesn't factor at all" into his negotiations, Bond continued, nor has anyone from Comcast "ever asked" him "to think about that." Bond's statements were similar to testimony given by Comcast's chief negotiator, Greg Rigdon, who testified that he has never suggested, or seen a Comcast document suggesting, that NBC "should go dark on one of [Comcast's] competitors because then [Comcast] might pick up some subscribers" or that NBCU should "hold out for a little bit more in affiliate fees because that will harm" Comcast's competitors.

. . . Time Warner executives testified similarly about their time at the company when it was vertically integrated with Time Warner Cable. Recalling that period, Time Warner CEO Jeff Bewkes testified that he was not aware of any Time Warner negotiator "articulating this theory of added incentive or added ability to leverage a price increase" because Time Warner was "vertically integrated with Time Warner Cable." . . . [V]arious industry witnesses testified that the identity of a programmer's owner does not affect the negotiating dynamic.

The Court accepts Professor Shapiro's (and the Government's) argument that, generally, "a firm with multiple divisions will act to maximize profits across them." That profit-maximization premise is not inconsistent, however, with the witness testimony that the identity of a programmer's owner has not affected affiliate negotiations in real-world instances of vertical integration. Rather, as those witnesses indicated, 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. ("Q: And, in fact, what you were doing is trying to maximize the revenue of NBC as a programmer in those negotiations, correct? A: Yes, sir." (quoting testimony of M. Bond of NBCU)). In the case of programmers, that means pursuing deals "to be on all the platforms," rather than undertaking a "series of risks" to threaten a long-term blackout. So understood, the consistent and, in this Court's judgment, credible, trial testimony is not in fact in "serious tension" with "economic logic" . . ..

[The court examined several other aspects of the Government's economic analysis, ultimately rejecting the Government's bargaining model on grounds that certain key inputs to the model were based on data that were incomplete, were contradictory to real-world experience, or were derived from methods that the court did not find convincing.]

IV. The Government Has Failed to Meet Its Burden to Show That the Proposed Merger Is Likely to Substantially Lessen Competition on the Theory That AT&T Will Act to Harm Virtual MVPDS Through Its Ownership of Time Warner Content

. . . The Government's second theory of competitive harm relates to virtual MVPDs. Virtual MVPDs, like traditional MVPDs, offer consumers linear (or "live") television programming in exchange for a subscription fee. Unlike traditional MVPDs, however, virtual MVPDs transmit their video content over the internet. Compared to traditional MVPDs, virtual MVPDs generally offer lower-cost programming packages to consumers; those packages, known in the industry as "skinny bundles," contain fewer networks than do the larger bundles offered by MVPDs. Although virtual MVPDs are of recent vintage, they are quickly gaining market share in the video programming and distribution industry. . . .

According to the Government, the challenged merger would give AT&T the "ability to harm competition by slowing the growth of emerging, innovative online distributors" - that is, virtual MVPDs. AT&T could do so, the Government asserts, either acting on its own (under the "unilateral theory") or in coordination with Comcast-NBCU (under the "coordination theory"). Defendants counter that the evidence does not support the Government's virtual MVPD theories. Far from showing that AT&T is trying to marginalize virtual MVPDs, defendants claim that the trial demonstrated that AT&T is embracing those providers - even launching and supporting a successful virtual MVPD, DirecTV Now. With respect to the supposed incentive to coordinate with Comcast, defendants argue that the Government's theory ignores critical differences between the positions of AT&T and those of Comcast vis-a-vis virtual MVPDs as well as key limitations on the companies' abilities to coordinate successfully. For the following reasons, I agree with the defendants that the Government has failed to show a likelihood that the merger would substantially lessen competition by empowering the merged company to act, either unilaterally or in coordination with Comcast-NBCU, to harm virtual MVPDs.

Unilateral Theory. The Government first claims that AT&T has an incentive to harm innovative virtual MVPDs and could act unilaterally on that incentive by foreclosing or restricting virtual MVPDs' access to "must-have" Turner content. . . . [D]efendants put forward additional evidence that AT&T would have incentive to *license* Time Warner content to virtual MVPDs after the merger. For starters, given Turner's imperative of broad distribution, *see supra* pp. 10-11, Turner executives testified that it is important for Turner's content to be included on virtual MVPDs as they continue to grow in relevance. With consumers choosing to cut or shave the cord, Turner has "embrac[ed] virtual MVPDs," Turner CEO John Martin testified, "because, again, we need to be distributed to as full distribution as possible.". . .

The entire premise of the proposed merger - allowing AT&T to go mobile with video content - provides yet another reason to reject the Government's unilateral merger theory. . . . Within its wireless business, AT&T Chairman and CEO Randall Stephenson explained, "getting video delivered onto the mobile device" is one of AT&T's "big focus areas." Increased video consumption is lucrative for AT&T because viewers consume more data on the wireless network. This leads AT&T customers to "buy up" on data plans, get more devices, or connect more devices to the network - all "good for [AT&T's] business." Indeed, "over half of all of the traffic on [AT&T's] network today is video, delivering video." Industry trend-lines point toward increased video consumption in the future – and AT&T aims to ride these tailwinds. . . . [T]his gives the combined entity even more reason to distribute Time Warner content as broadly as possible in order to encourage the proliferation of virtual MVPDs. As Randall Stephenson put it, the proposed merger is a "vision deal" reflecting a belief "that distribution of [Time Warner] content to wireless will drive the value of the content up" and that "the ability to pair our data with [Time Warner's] advertising inventory" for digital ads delivered over the internet "will drive value."

Against that evidence, the Government cites a handful of AT&T documents and statements related to virtual MVPDs - documents the Government says show AT&T has the incentive to slow the rise of virtual MVPDs. For multiple reasons, however, I do not consider the fact that AT&T executives may have previously expressed displeasure with Turner's relationships with its competitor virtual MVPDs to be probative of AT&T's post-merger economic incentive to license Turner content to virtual MVPDs. First, these statements shed no light on the post-merger incentive AT&T would have to maximize distribution of Turner content. As the reader now knows, wide distribution is the *sine qua non* of the programming industry, driving both subscription and advertising revenue. Indeed, because of these "[gains] from trade" associated with licensing Turner content as broadly as possible, Professor Shapiro himself refused to countenance the Government's unilateral virtual MVPD theory. Second, these statements do not explain why AT&T would discard the profits associated with increased video consumption by its 100 million-plus wireless subscribers accessing virtual MVPD offerings. In short, the Government's evidence on its unilateral withholding theory is fatally anemic.

Second, from the other direction, the Government advances an alternative unilateral claim: that AT&T would have the ability to break the "skinny bundle" models of virtual MVPDs by forcing those distributors to take *too many* Turner networks. . . . The Government's skinny bundle point also overlooks the fact that Turner - like other programmers - already fights tooth and nail to get all of its networks into all of the packages of every distributor. Simply put, the Government has not produced sufficient evidence to show that the challenged merger is likely to make a meaningful difference to that dynamic. For all of the above reasons, I conclude that the Government has failed to meet its burden on its claims arising from AT &T's asserted potential to unilaterally harm virtual MVPDs through its post-merger control of Turner content.

Coordination Theory. The Government posits that the challenged merger would also create a likelihood that AT&T would coordinate with Comcast-NBCU to harm virtual MVPDs. . . . In order to assess whether a merger will lead to an unacceptable risk of competition-stifling coordination, courts evaluate various "market conditions, on the whole." *H & R Block,* 833 F. Supp. 2d at 77 (citation omitted). In short, that analysis involves consideration of whether would-be coordinators could wield anticompetitive power "by recognizing their shared economic interests and their interdependence with respect to price and output decisions." *Brooke Grp.,* 509 U.S. at 227. Not so here!

. . . Here, the Government assumes that, "[a]s the only two vertically integrated traditional MVPDs, Comcast and AT&T would share an incentive to slow the entry and growth of virtual MVPDs." To act on that incentive, the Government further asserts, the companies could "mutually forbear" from licensing their programming content "without any communication between them." Not only is that theory overly speculative, it ignores key differences between AT&T and Comcast that undermine the Government's argument.

First, the Government has failed to put forward sufficient evidence to show more than a theoretical "possibility" of coordination. *Cf Baker Hughes,* 908 F.2d at 984 ("Section 7 involves *probabilities,* not certainties or possibilities."). . . . When questioned at trial about the Government's coordinated effects theory, Professor Shapiro conceded that he had no "way of accessing [sic] the probability" of coordination and thus had not attempted to "quantif[y] any risk whatsoever" that the predicted coordination "could occur." Accordingly, Professor Shapiro confirmed that he was "not in a position to say" that coordination is "more likely to happen than not," and indeed was not even prepared to say that there's a "one percent chance that coordination will happen" []. . . .

Second, the Government's argument regarding the incentive of AT&T and Comcast to coordinate to harm virtual MVPDs ignores that both stand to lose large amounts of affiliate fee and advertising revenues by withholding their content from virtual MVPDs. . . . The Government has not explained why either company would be willing to forgo those affiliate fees and advertising revenues from virtual MVPDs. Nor has the Government proffered any expert analysis, for example, of how those economics could, or would, change assuming a coordinated blackout of both Turner and NBCU.

Third, and critically, the Government's argument also ignores key differences between the two companies - differences that AT&T executives believe give AT&T a competitive advantage over Comcast moving forward in this new era of rising virtual MVPD prevalence. . . . Under the Government's coordination theory, one party - AT&T or Comcast - would have to "jump first," giving up valuable programming rights on the hope that the other, in some years' time, would elect to do the same. Indeed, this barrier to coordination is so great as to put to rest the notion not only that AT&T and Comcast would have the *incentive* to coordinate, but that the post-merger marketplace would afford them the *ability* to do so. Whether by way of tacit coordination or an illegal agreement, putting such blind faith in one's chief competitor strikes this Court as exceedingly implausible!

V. The Government Has Failed to Meet Its Burden to Show That the Proposed Merger Is Likely to Substantially Lessen Competition on the Theory That AT&T Will Restrict Distributors' Use of HBO as a Promotional Tool

The Government's final theory centers on HBO. On this score, the Government alleges that the combined entity will have the "incentive and ability" to prevent rival distributors from using HBO as a promotional tool to attract and retain customers. . . . The Government has failed to meet its burden of proof on this theory for two independent reasons. *First,* the Government has failed to show that the merged entity would have *any* incentive to foreclose rivals' access to HBO-based promotions. This is because the Government's promotion-withholding theory conflicts with HBO's business model, which remains "heavily dependent" on promotion by distributors. HBO does not run ads, leaving subscription fees as its overwhelming source of revenue. . . .

Second, the Government fails to establish that HBO promotions are so valuable that withholding or restricting them will drive customers to AT&T. Put differently, the Government has failed to show that the marketplace substitutes for HBO are "inferior, inadequate, or more costly." . . . A Comcast executive confirmed that Netflix is a "substitute" for HBO that Comcast has incorporated into its set top box and includes in marketing. . . . [T]he Government's evidence is too thin a reed for this Court to find that AT&T has, in that well-worn turn-of-phrase, either the "incentive" or the "ability" to withhold HBO promotional rights in order to "lessen competition substantially."

NOTES AND QUESTIONS

1. Why was the DOJ willing to accept behavioral remedies in the Comcast/NBCU merger but not in AT&T/Time Warner? Does the complaint allege different harms? Or, was the decision to go to trial motivated more by a changed view on the effectiveness of behavioral remedies? At around the same time the Government filed suit against AT&T/Time Warner, the Assistant Attorney General for Antitrust, Makan Delrahim, gave a speech to the ABA in which he stated:

> In recent years, antitrust enforcers have struggled more and more with the challenges of crafting and enforcing effective behavioral relief. . . . Without getting into specifics, I can say that behavioral remedies have proven challenging to enforce today. In recent years, the Division has investigated a number of behavioral decree violations, but has found it onerous to collect information or satisfy the exacting standards of proving contempt and seeking relief for violations. We have a limited window into the day-to-day operations of business, and it is difficult to monitor and enforce granular commitments like non-discrimination and information firewalls. Behavioral remedies presume that the Justice Department should serve as a roving ombudsman of the affairs of business; even if we wanted to do that, we often don't have the skills or the tools to do so effectively.
>
> Another problem with behavioral remedies is determining their expiration. A short-term remedy is a band-aid, not a fix, and as FTC Commissioner McSweeny said last year, "the relief at best only delays the merged firm's exercise of market power." On the other hand, if we make behavioral commitments indefinite, then we really are becoming full-time regulators instead of law enforcers.

> That is not to say we would never accept behavioral remedies. In certain instances where an unlawful vertical transaction generates significant efficiencies that cannot be achieved without the merger or through a structural remedy, then there's a place for considering a behavioral remedy if it will completely cure the anticompetitive harms. It's a high standard to meet.

See, https://www.justice.gov/opa/speech/assistant-attorney-general-makan-delrahim-delivers-keynote-address-american-bar

2. Why does Judge Leon reject the Government's bargaining theory? Does he not accept the theory? Or does he believe the theory is not borne out by the evidence? If the latter, consider what evidence the court did or did not find persuasive. What would the Government need to have shown in order to prevail?

3. Does the court give any indication in its decision of why it thinks AT&T wanted to merge with Time-Warner? What, if any, efficiencies does the court identify? Do you find those arguments persuasive?

4. The government relied on a bargaining model that presumed that the merging firms were profit maximizers and would remain so subsequent to the merger. The district court, however, noted and apparently credited testimony from the defendants' employees that they would continue to maximize Time-Warner's profits separately, even after it was a wholly owned subsidiary. The difference could be significant. As an unintegrated firm Time-Warner would very likely have an incentive to make every sale that it could. Once it was vertically integrated into AT&T, however, it might earn more by selectively denying licenses to non-AT&T customers or else charging them more. Should the government be able to rely on a presumption that firms maximize overall profits? The Agencies do it all the time in the bargaining models that they employ to evaluate horizontal mergers. Cf. Copperweld Corp. v Independence Tube Corp., 467 U.S. 752 (1984) (a firm, including its separately incorporated subsidiaries, should be treated as a single entity for antitrust (Sherman Act) purposes).

Chapter 9 ANTITRUST, OTHER FORMS OF REGULATION, AND EXEMPTIONS

…

III PROBLEMS OF FEDERALISM: PREEMPTION AND THE "STATE ACTION" DOCTRINE

[B] The "State Action" Doctrine

[2] The "Active Supervision" Requirement

p. 1101, insert at end of chapter:

NORTH CAROLINA STATE BOARD OF DENTAL EXAMINERS V. FTC

135 S.Ct. 1101 (2015)

Opinion

Justice KENNEDY delivered the opinion of the Court.

This case arises from an antitrust challenge to the actions of a state regulatory board. A majority of the board's members are engaged in the active practice of the profession it regulates. The question is whether the board's actions are protected from Sherman Act regulation under the doctrine of state-action antitrust immunity, as defined and applied in this Court's decisions beginning with *Parker v. Brown,* 317 U.S. 341 (1943).

In its Dental Practice Act (Act), North Carolina has declared the practice of dentistry to be a matter of public concern requiring regulation. N.C. Gen.Stat. Ann. § 90–22(a) (2013). Under the Act, the North Carolina State Board of Dental Examiners (Board) is "the agency of the State for the regulation of the practice of dentistry."

The Board's principal duty is to create, administer, and enforce a licensing system for dentists. See §§ 90–29 to 90–41. To perform that function it has broad authority over licensees. The Board's authority with respect to unlicensed persons, however, is more restricted: like "any resident citizen," the Board may file suit to "perpetually enjoin any person from ... unlawfully practicing dentistry."

The Act provides that six of the Board's eight members must be licensed dentists engaged in the active practice of dentistry. They are elected by other licensed dentists in North Carolina, who cast their ballots in elections conducted by the Board. The seventh member must be a licensed and practicing dental hygienist, and he or she is elected by other licensed hygienists. The final member is referred to by the Act as a "consumer" and is appointed by the Governor…..

The Board may promulgate rules and regulations governing the practice of dentistry within the State, provided those mandates are not inconsistent with the Act and are approved by the North Carolina Rules Review Commission, whose members are appointed by the state legislature.

In the 1990's, dentists in North Carolina started whitening teeth. Many of those who did so, including 8 of the Board's 10 members during the period at issue in this case, earned substantial fees for that service. By 2003, nondentists arrived on the scene. They charged lower prices for their services than the dentists did. Dentists soon began to complain to the Board about their new competitors. Few complaints warned of possible harm to consumers. Most expressed a principal concern with the low prices charged by nondentists.

Responding to these filings, the Board opened an investigation into nondentist teeth whitening. A dentist member was placed in charge of the inquiry. Neither the Board's hygienist member nor its consumer member participated in this undertaking. The Board's chief operations officer remarked that the Board was "going forth to do battle" with nondentists…..

Starting in 2006, the Board issued at least 47 cease-and-desist letters on its official letterhead to nondentist teeth whitening service providers and product manufacturers. Many of those letters directed the recipient to cease "all activity constituting the practice of dentistry"; warned that the unlicensed practice of dentistry is a crime; and strongly implied (or expressly stated) that teeth whitening constitutes "the practice of dentistry."…

These actions had the intended result. Nondentists ceased offering teeth whitening services in North Carolina.

In 2010, the Federal Trade Commission (FTC) filed an administrative complaint charging the Board with violating § 5 of the Federal Trade Commission Act, 38 Stat. 719, as amended, 15 U.S.C. § 45. The FTC alleged that the Board's concerted action to exclude nondentists from the market for teeth whitening services in North Carolina constituted an anticompetitive and unfair method of competition. The Board moved to dismiss, alleging state-action immunity. An Administrative Law Judge (ALJ) denied the motion. On appeal, the FTC sustained the ALJ's ruling. It reasoned that, even assuming the Board had acted pursuant to a clearly articulated state policy to displace competition, the Board is a "public/private hybrid" that must be actively supervised by the State to claim immunity. The FTC further concluded the Board could not make that showing….

[T]he Court of Appeals for the Fourth Circuit affirmed the FTC in all respects…. This Court granted certiorari.

Federal antitrust law is a central safeguard for the Nation's free market structures. In this regard it is "as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms." *United States v. Topco Associates, Inc.,* 405 U.S. 596, 610 (1972). The antitrust laws declare a considered and decisive prohibition by the Federal Government of cartels, price fixing, and other combinations or practices that undermine the free market.

… The States, however, when acting in their respective realm, need not adhere in all contexts to a model of unfettered competition. While "the States regulate their economies in many ways not inconsistent with the antitrust laws," in some spheres they impose restrictions on occupations, confer exclusive or shared rights to dominate a market, or otherwise limit competition to achieve public objectives. If every duly enacted state law or policy were required to conform to the mandates of the Sherman Act, thus promoting competition at the expense of other values a State may deem fundamental, federal antitrust law would impose an impermissible burden on the States' power to regulate. See *Exxon Corp. v. Governor of Maryland,* 437 U.S. 117, 133, 98 S.Ct. 2207, 57 L.Ed.2d 91 (1978); see also Easterbrook, Antitrust and the Economics of Federalism, 26 J. Law & Econ. 23, 24 (1983).

For these reasons, the Court in *Parker v. Brown* interpreted the antitrust laws to confer immunity on anticompetitive conduct by the States when acting in their sovereign capacity…. That ruling recognized Congress' purpose to respect the federal balance and to "embody in the Sherman Act the federalism principle that the States possess a significant measure of sovereignty under our Constitution." *Community Communications Co. v. Boulder,* 455 U.S. 40, 53 (1982).

In this case the Board argues its members were invested by North Carolina with the power of the State and that, as a result, the Board's actions are cloaked with *Parker* immunity. This argument fails, however. A nonsovereign actor controlled by active market participants—such as the Board—enjoys *Parker* immunity only if it satisfies two requirements: "first that 'the challenged restraint ... be one clearly articulated and affirmatively expressed as state policy,' and second that 'the policy ... be actively supervised by the State.' " *FTC v. Phoebe Putney Health System, Inc.,* 133 S.Ct. 1003, 1010 (2013) (quoting *California Retail Liquor Dealers Assn.* v. *Midcal Aluminum, Inc.,* 445 U.S. 97, 105 (1980)). The parties have assumed that the clear articulation requirement is satisfied, and we do the same. While North Carolina prohibits the unauthorized practice of dentistry, however, its Act is silent on whether that broad prohibition covers teeth whitening. Here, the Board did not receive active supervision by the State when it interpreted the Act as addressing teeth whitening and when it enforced that policy by issuing cease-and-desist letters to nondentist teeth whiteners.

Although state-action immunity exists to avoid conflicts between state sovereignty and the Nation's commitment to a policy of robust competition, *Parker* immunity is not unbounded. "[G]iven the fundamental national values of free enterprise and economic competition that are embodied in the federal antitrust laws, 'state action immunity is disfavored, much as are repeals by implication.' " *Phoebe Putney*, 133 S.Ct., at 1010

An entity may not invoke *Parker* immunity unless the actions in question are an exercise of the State's sovereign power. See *Columbia v. Omni Outdoor Advertising, Inc.,* 499 U.S. 365, 374 (1991).

… But while the Sherman Act confers immunity on the States' own anticompetitive policies out of respect for federalism, it does not always confer immunity where, as here, a State delegates control over a market to a non-sovereign actor…. For purposes of *Parker,* a nonsovereign actor is one whose conduct does not automatically qualify as that of the sovereign State itself…. State agencies are not simply by their governmental character sovereign actors for purposes of state-action immunity. See *Goldfarb v. Virginia State Bar,* 421 U.S. 773, 791, 95

S.Ct. 2004, 44 L.Ed.2d 572 (1975) ("The fact that the State Bar is a state agency for some limited purposes does not create an antitrust shield that allows it to foster anticompetitive practices for the benefit of its members"). Immunity for state agencies, therefore, requires more than a mere facade of state involvement, for it is necessary in light of *Parker*'s rationale to ensure the States accept political accountability for anticompetitive conduct they permit and control.

… Limits on state-action immunity are most essential when the State seeks to delegate its regulatory power to active market participants, for established ethical standards may blend with private anticompetitive motives in a way difficult even for market participants to discern. Dual allegiances are not always apparent to an actor. In consequence, active market participants cannot be allowed to regulate their own markets free from antitrust accountability….

Parker immunity requires that the anticompetitive conduct of nonsovereign actors, especially those authorized by the State to regulate their own profession, result from procedures that suffice to make it the State's own. See *Goldfarb, supra,* at 790, 95 S.Ct. 2004; see also 1A P. Areeda & H. Hovenkamp, Antitrust Law ¶ 226, p. 180 (4th ed. 2013) The question is not whether the challenged conduct is efficient, well-functioning, or wise. Rather, it is "whether anticompetitive conduct engaged in by [nonsovereign actors] should be deemed state action and thus shielded from the antitrust laws." *Patrick v. Burget,* 486 U.S. 94, 100 (1988).

To answer this question, the Court applies the two-part test set forth in *California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc.,* 445 U.S. 97, a case arising from California's delegation of price-fixing authority to wine merchants. Under *Midcal,* "[a] state law or regulatory scheme cannot be the basis for antitrust immunity unless, first, the State has articulated a clear policy to allow the anticompetitive conduct, and second, the State provides active supervision of [the] anticompetitive conduct."…

The two requirements set forth in *Midcal* provide a proper analytical framework to resolve the ultimate question whether an anticompetitive policy is indeed the policy of a State. The first requirement—clear articulation—rarely will achieve that goal by itself, for a policy may satisfy this test yet still be defined at so high a level of generality as to leave open critical questions about how and to what extent the market should be regulated…. Entities purporting to act under state authority might diverge from the State's considered definition of the public good. The resulting asymmetry between a state policy and its implementation can invite private self-dealing. The second *Midcal* requirement—active supervision—seeks to avoid this harm by requiring the State to review and approve interstitial policies made by the entity claiming immunity.

Midcal's supervision rule "stems from the recognition that '[w]here a private party is engaging in anticompetitive activity, there is a real danger that he is acting to further his own interests, rather than the governmental interests of the State.' " Concern about the private incentives of active market participants animates *Midcal*'s supervision mandate, which demands "realistic assurance that a private party's anticompetitive conduct promotes state policy, rather than merely the party's individual interests." *Patrick,* 108 S.Ct. 1658.

… In *Hallie v. Eau Claire,* 471 U.S. 34, 45 (1985), the Court held municipalities are subject exclusively to *Midcal*'s " 'clear articulation' " requirement. That rule, the Court observed, is consistent with the objective of ensuring that the policy at issue be one enacted by the State itself. *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." *Hallie* further observed that municipalities are electorally accountable and lack the kind of private incentives characteristic of active participants in the market. Critically, the municipality in *Hallie* exercised a wide range of governmental powers across different economic spheres, substantially reducing the risk that it would pursue private interests while regulating any single field. That *Hallie* excused municipalities from *Midcal*'s supervision rule for these reasons all but confirms the rule's applicability to actors controlled by active market participants, who ordinarily have none of the features justifying the narrow exception *Hallie* identified....

In [FTC v.] Ticor [Title Ins. Co., 504 U.S. 621 (1992)] the Court affirmed that *Midcal*'s limits on delegation must ensure that "[a]ctual state involvement, not deference to private price-fixing arrangements under the general auspices of state law, is the precondition for immunity from federal law." And in *Phoebe Putney* the Court observed that *Midcal*'s active supervision requirement, in particular, is an essential condition of state-action immunity when a nonsovereign actor has "an incentive to pursue [its] own self-interest under the guise of implementing state policies." … The lesson is clear: *Midcal*'s active supervision test is an essential prerequisite of *Parker* immunity for any nonsovereign entity—public or private—controlled by active market participants.

The Board argues entities designated by the States as agencies are exempt from *Midcal*'s second requirement. That premise, however, cannot be reconciled with the Court's repeated conclusion that the need for supervision turns not on the formal designation given by States to regulators but on the risk that active market participants will pursue private interests in restraining trade. State agencies controlled by active market participants, who possess singularly strong private interests, pose the very risk of self-dealing *Midcal*'s supervision requirement was created to address. See Areeda & Hovenkamp ¶ 227, at 226. This conclusion does not question the good faith of state officers but rather is an assessment of the structural risk of market participants' confusing their own interests with the State's policy goals….

While *Hallie* stated "it is likely that active state supervision would also not be required" for agencies, 471 U.S., at 46, n. 10, the entity there, as was later the case in *Omni,* was an electorally accountable municipality with general regulatory powers and no private price-fixing agenda. In that and other respects the municipality was more like prototypical state agencies, not specialized boards dominated by active market participants. In important regards, agencies controlled by market participants are more similar to private trade associations vested by States with regulatory authority than to the agencies *Hallie* considered. And as the Court observed three years after *Hallie,* "[t]here is no doubt that the members of such associations often have economic incentives to restrain competition and that the product standards set by such associations have a serious potential for anticompetitive harm." *Allied Tube [v. Indian Head, Inc.],* 486 U.S. [492] at 500 (1988). For that reason, those associations must satisfy *Midcal*'s active supervision standard.

The similarities between agencies controlled by active market participants and private trade associations are not eliminated simply because the former are given a formal designation by the State, vested with a measure of government power, and required to follow some procedural rules. See *Hallie, supra,* at 39 (rejecting "purely formalistic" analysis). *Parker* immunity does not derive from nomenclature alone. When a State empowers a group of active market participants to decide who can participate in its market, and on what terms, the need for supervision is manifest. See Areeda & Hovenkamp ¶ 227, at 226. The Court holds today that a state board on which a controlling number of decisionmakers are active market participants in the occupation the board regulates must satisfy *Midcal*'s active supervision requirement in order to invoke state-action antitrust immunity.

The State argues that allowing this FTC order to stand will discourage dedicated citizens from serving on state agencies that regulate their own occupation…. There is … a long tradition of citizens esteemed by their professional colleagues devoting time, energy, and talent to enhancing the dignity of their calling….

Today's holding is not inconsistent with that idea. The Board argues, however, that the potential for money damages will discourage members of regulated occupations from participating in state government…. But this case, which does not present a claim for money damages, does not offer occasion to address the question whether agency officials, including board members, may, under some circumstances, enjoy immunity from damages liability. And, of course, the States may provide for the defense and indemnification of agency members in the event of litigation.

States, furthermore, can ensure *Parker* immunity is available to agencies by adopting clear policies to displace competition; and, if agencies controlled by active market participants interpret or enforce those policies, the States may provide active supervision…. The reasoning of *Patrick v. Burget, supra,* applies to this case with full force, particularly in light of the risks licensing boards dominated by market participants may pose to the free market. See generally Edlin & Haw, Cartels by Another Name: Should Licensed Occupations Face Antitrust Scrutiny? 162 U. Pa. L.Rev. 1093 (2014)….

The Board does not claim that the State exercised active, or indeed any, supervision over its conduct regarding nondentist teeth whiteners; and, as a result, no specific supervisory systems can be reviewed here. It suffices to note that the inquiry regarding active supervision is flexible and context-dependent. Active supervision need not entail day-to-day involvement in an agency's operations or micromanagement of its every decision. Rather, the question is whether the State's review mechanisms provide "realistic assurance" that a nonsovereign actor's anticompetitive conduct "promotes state policy, rather than merely the party's individual interests." *Patrick, supra.*…

The Court has identified only a few constant requirements of active supervision: The supervisor must review the substance of the anticompetitive decision, not merely the procedures followed to produce it, see *Patrick,* 486 U.S., at 102–103; the supervisor must have the power to veto or modify particular decisions to ensure they accord with state policy, see *ibid.*; and the "mere potential for state supervision is not an adequate substitute for a decision by the State," *Ticor, supra,* at 638, 112 S.Ct. 2169. Further, the state supervisor may not itself be an active market participant. In general, however, the adequacy of supervision otherwise will depend on all the circumstances of a case.

* * *

The Sherman Act protects competition while also respecting federalism. It does not authorize the States to abandon markets to the unsupervised control of active market participants, whether trade associations or hybrid agencies. If a State wants to rely on active market participants as regulators, it must provide active supervision if state-action immunity under *Parker* is to be invoked.

The judgment of the Court of Appeals for the Fourth Circuit is affirmed.

It is so ordered.

Justice ALITO, with whom Justice SCALIA and Justice THOMAS join, dissenting.

The Court's decision in this case is based on a serious misunderstanding of the doctrine of state-action antitrust immunity that this Court recognized more than 60 years ago in *Parker v. Brown,* 317 U.S. 341 (1943). In *Parker,* the Court held that the Sherman Act does not prevent the States from continuing their age-old practice of enacting measures, such as licensing requirements, that are designed to protect the public health and welfare….

Today, however, the Court takes the unprecedented step of holding that *Parker* does not apply to the North Carolina Board because the Board is not structured in a way that merits a good-government seal of approval; that is, it is made up of practicing dentists who have a financial incentive to use the licensing laws to further the financial interests of the State's dentists. There is nothing new about the structure of the North Carolina Board. When the States first created medical and dental boards, well before the Sherman Act was enacted, they began to staff them in this way. Nor is there anything new about the suspicion that the North Carolina Board—in attempting to prevent persons other than dentists from performing teeth-whitening procedures—was serving the interests of dentists and not the public. Professional and occupational licensing requirements have often been used in such a way. But that is not what *Parker* immunity is about. Indeed, the very state program involved in that case was unquestionably designed to benefit the regulated entities, California raisin growers.

The question before us is not whether such programs serve the public interest. The question, instead, is whether this case is controlled by *Parker,* and the answer to that question is clear. Under *Parker,* the Sherman Act (and the Federal Trade Commission Act) do not apply to state agencies; the North Carolina Board of Dental Examiners is a state agency; and that is the end of the matter. By straying from this simple path, the Court has not only distorted *Parker*; it has headed into a morass. Determining whether a state agency is structured in a way that militates against regulatory capture is no easy task, and there is reason to fear that today's decision will spawn confusion. The Court has veered off course, and therefore I cannot go along….

In order to understand the nature of *Parker* state-action immunity, it is helpful to recall the constitutional landscape in 1890 when the Sherman Act was enacted. At that time, this Court and Congress had an understanding of the scope of federal and state power that is very different from our understanding today. The States were understood to possess the exclusive authority to regulate "their purely internal affairs." Leisy v. Hardin, 135 U.S. 100, 122 (1890). In exercising their police power in this area, the States had long enacted measures, such as price controls and licensing requirements, that had the effect of restraining trade.

The Sherman Act was enacted pursuant to Congress' power to regulate interstate commerce, [b]ut in 1890, the understanding of the commerce power was far more limited than it is today. …As a result, the Act did not pose a threat to traditional state regulatory activity.

By 1943, when *Parker* was decided, however, the situation had changed dramatically. This Court had held that the commerce power permitted Congress to regulate even local activity if it "exerts a substantial economic effect on interstate commerce." *Wickard v. Filburn,* 317 U.S. 111, 125 (1942). This meant that Congress could regulate many of the matters that had once been thought to fall exclusively within the jurisdiction of the States. The new interpretation of the commerce power brought about an expansion of the reach of the Sherman Act…. And the expanded reach of the Sherman Act raised an important question. The Sherman Act does not expressly exempt States from its scope. Does that mean that the Act applies to the States and that it potentially outlaws many traditional state regulatory measures? The Court confronted that question in *Parker*….

The Court's holding in *Parker* was not based on either the language of the Sherman Act or anything in the legislative history affirmatively showing that the Act was not meant to apply to the States. Instead, the Court reasoned that "[i]n a dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress."… For the Congress that enacted the Sherman Act in 1890, it would have been a truly radical and almost certainly futile step to attempt to prevent the States from exercising their traditional regulatory authority, and the *Parker* Court refused to assume that the Act was meant to have such an effect.

When the basis for the *Parker* state-action doctrine is understood, the Court's error in this case is plain. In 1890, the regulation of the practice of medicine and dentistry was regarded as falling squarely within the States' sovereign police power. By that time, many States had established medical and dental boards, often staffed by doctors or dentists, and had given those boards the authority to confer and revoke licenses….

The Board is not a private or "nonsovereign" entity that the State of North Carolina has attempted to immunize from federal antitrust scrutiny. *Parker* made it clear that a State may not " 'give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful.'" Nothing similar is involved here. North Carolina did not authorize a private entity to enter into an anticompetitive arrangement; rather, North Carolina *created a state agency* and gave that agency the power to regulate a particular subject affecting public health and safety….

[T]he Court not only disregards the North Carolina Board's status as a full-fledged state agency; it treats the Board less favorably than a municipality. This is puzzling. States are sovereign, and California's sovereignty provided the foundation for the decision in *Parker, supra,* at 352, 63 S.Ct. 307. Municipalities are not sovereign.

The Court recognizes that municipalities, although not sovereign, nevertheless benefit from a more lenient standard for state-action immunity than private entities. Yet under the Court's approach, the North Carolina Board of Dental Examiners, a full-fledged state agency, is treated like a private actor and must demonstrate that the State actively supervises its actions.

The Court's analysis seems to be predicated on an assessment of the varying degrees to which a municipality and a state agency like the North Carolina Board are likely to be captured by private interests. But until today, *Parker* immunity was never conditioned on the proper use of state regulatory authority. On the contrary, in *Columbia v. Omni Outdoor Advertising, Inc.,* 499 U.S. 365 (1991), we refused to recognize an exception to *Parker* for cases in which it was shown that the defendants had engaged in a conspiracy or corruption or had acted in a way that was not in the public interest. The Sherman Act, we said, is not an anticorruption or good-government statute. We were unwilling in *Omni* to rewrite *Parker* in order to reach the allegedly abusive behavior of city officials. 499 U.S., at 374–379, 111 S.Ct. 1344. But that is essentially what the Court has done here….

As a result of today's decision, States may find it necessary to change the composition of medical, dental, and other boards, but it is not clear what sort of changes are needed to satisfy the test that the Court now adopts. The Court faults the structure of the North Carolina Board because "active market participants" constitute "a controlling number of [the] decisionmakers," but this test raises many questions.

What is a "controlling number"? Is it a majority? And if so, why does the Court eschew that term? Or does the Court mean to leave open the possibility that something less than a majority might suffice in particular circumstances? Suppose that active market participants constitute a voting bloc that is generally able to get its way? How about an obstructionist minority or an agency chair empowered to set the agenda or veto regulations?

Who is an "active market participant"? If Board members withdraw from practice during a short term of service but typically return to practice when their terms end, does that mean that they are not active market participants during their period of service?

What is the scope of the market in which a member may not participate while serving on the board? Must the market be relevant to the particular regulation being challenged or merely to the jurisdiction of the entire agency? Would the result in the present case be different if a majority of the Board members, though practicing dentists, did not provide teeth whitening services? What if they were orthodontists, periodontists, and the like? And how much participation makes a person "active" in the market? The answers to these questions are not obvious, but the States must predict the answers in order to make informed choices about how to constitute their agencies….

The Court has created a new standard for distinguishing between private and state actors for purposes of federal antitrust immunity. This new standard is not true to the *Parker* doctrine; it diminishes our traditional respect for federalism and state sovereignty; and it will be difficult to apply. I therefore respectfully dissent.

NOTES AND QUESTIONS

1. Does *North Carolina Dental* effectively overrule *Parker*? Or does it simply add further refinement? Neither the authorization ("clear articulation") nor "active supervision" requirements of the modern state action doctrine were developed until more than three decades after *Parker*.

The distinction between "private" conduct and the conduct of a sovereign state is critical to understanding modern "state action" antitrust doctrine. If a state is regulating within its territory *and* it is actually the state that is doing the regulating, then the highly general language of the antitrust laws generally requires federal antitrust tribunals to stand aside. Federal antitrust has no power to police bad state regulation as such. It cannot require that state regulations pass a cost-benefit test that might weed out some instances of badly designed regulation. But it can properly insist on a showing that the conduct in question be that of the state, and not of a private entrepreneur.

The antitrust "state action" doctrine addresses this problem by trying to identify the line between sovereign state conduct, which is largely immune from federal antitrust oversight, and private conduct, which is not. After nearly forty years of litigation the Supreme Court adopted the modern two-prong test in Cal. Retail Liquor Dealers Ass'n, v. Midcal Aluminum, 445 U.S. 97 (1980), which after subsequent elaboration, states:

a. "Sovereign" conduct performed by the "state itself" is immune; by contrast,

b. "Private" conduct must be both (a) authorized by the state, and (b) any anticompetitive consequences must be "actively supervised" by a government official.

These prongs have been further refined:

c. In between the extremes defined by (a) and (b) is conduct by state-created entities or subdivisions that are not "sovereign" under the United States Constitution (although they may be under state law); for these, the challenged activity must be "authorized" but it need not be "supervised;" and

d. The issue whether conduct is "private" or that of a state-created subdivision presents a federal question; that is, a state legislature's designation of a private group as an "agency" of the state does not necessarily make it so.

2. Under the dissent's interpretation in *North Carolina Dental* can a state authorize any cartel it wishes -- such as price fixing by gasoline retailers -- simply by passing a statute calling the cartel an "agency," and giving it carte blanche over prices? Should that concern us? Both the traditional state action doctrine as interpreted by the majority and the dissent's view place a high value on federalism, but the latter is more extreme. Under the majority's view the state can authorize a gasoline retailers' cartel if it wants, but the cartel would have to be managed by an independent state official. The official might even be instructed that his or her only duty is to maximize the retailers' profits --

that is, the official would manage the cartel in the same way that a private manager would do. The important difference, of course, is that the statute would bring the cartel out into the open political process rather than the secrecy that attends most private cartels. This fact also serves to explain why the active supervision requirement does not generally apply to the actions of municipalities, provided that they are properly authorized. As the Court points out, municipalities have their own political processes that create transparency. For example, if a city council captured by gasoline interests should permit a cartel of gasoline retailers they would have to answer to angry voters in the next election.

3. In Parker v. Brown, 317 U.S. 341 (1943), raisin growers in California shipped more than 90% of their product outside the state. As a result, the state's own economy was an enormous beneficiary of the raisin cartel, while the harm was imposed mainly outside. In *North Carolina Dental*, by contrast, nearly everyone who purchased teeth whitening services from North Carolina dentists lived inside the state. Indeed, to the extent the cartel forced any interstate movement one can surmise that it might lead some patients to obtain teeth whitening services elsewhere. As a result North Carolina was shooting itself in the foot, so to speak, by permitting the state's dentists to pass a rule that injured the state's own economy. For purposes of federalism should that fact be important? Should the national competition policy articulated for the Sherman Act be any weaker when the injuries caused by state-authorized anticompetitive activity burden mainly the state's own residents?
4. The "state action" antitrust doctrine is judge made. By contrast the antitrust immunity for the insurance industry, which was created at the same time, is statutory. The McCarran-Ferguson Act, passed in 1945, expressly exempts the insurance industry from the antitrust laws, but only if the industry is "regulated by state law." 15 U.S.C. §§ 1101–1102. Does that help in understanding how Congress at the time envisioned the division of state and federal authority? Under subsequent interpretation the states can pretty much regulate the industry as they wish, including even approving price fixing among insurers. But if they wish to retain the immunity they do not have the option of not regulating at all. *see* 1A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶219 (4th ed. 2013).
5. The dissent makes a point of the fact that in 1890 when the Sherman Act was passed the statute would not have reached into purely intrastate activities under the then existing interpretation of the federal Commerce Clause. Only after Wickard v. Filburn, 317 U.S. 111 (1942) did federal authority reach anticompetitive practices that "affected" interstate commerce. The *North Carolina Dental* case was brought under Section 5 of the Federal Trade Commission Act, however, which reached only activities "in commerce" in 1914, when it was originally passed. However, in 1975 Congress amended Section 5 of the FTC Act so as to reach restraints "in or affecting" commerce. 15 U.S.C. §45(a)(2). Since then the FTC Act has been applied to anticompetitive conduct involving medicine, dentistry and other learned professions many times. See Herbert Hovenkamp, *Rediscovering Capture: Antitrust Federalism and the North Carolina Dental Case*, CPI Antitrust Chronicle (April 2015).
6. In *United Nat. Maintenance, Inc. v. San Diego Convention Center, Inc.,* 766 F.3d 1002 (9th Cir. 2014), cert. denied, 135 S.Ct. 980 (2015), the Ninth Circuit held that the state action immunity applied to a city convention center's decision to use its own cleaning

staff rather than hire outsiders such as the plaintiff. The statute in question granted the municipality the authority to create a Commission to run the Center. Query: how could it be an antitrust violation to clean your own building yourself, rather than hiring someone else to do it, even assuming the building dominated a relevant market? Should a court jump to the "state action" exemption analysis if there is clearly no antitrust violation to begin with?