LOS ANGELES & SAN FRANCISCO
Daily Journal
www.dailyjournal.com
TUESDAY, MAY 21, 2019

PERSPECTIVE

Hope for antitrust regulation?

By David W. Kesselman

In what some have characterized as a bit of a surprise ruling, the U.S. Supreme Court this month sided with consumers in holding that they have standing to pursue a proposed antitrust class action against Apple for monopolization. In *Apple Inc. v. Pepper, et al.*, 2019 DJDAR 3951 (May 13, 2019), the court ruled 5-4 that the consumer plaintiffs were not barred by the "indirect purchaser rule" that generally limits standing in federal antitrust cases to direct purchaser plaintiffs only.

Perhaps the biggest surprise was the author of the majority opinion: Justice Brett Kavanaugh, who joined with the four "liberal" members of the court to reject a series of arguments by Apple for why the lawsuit should be dismissed. Justice Kavanaugh not only held that the consumer plaintiffs have standing, but he suggested that the federal antitrust laws still have a vital role in our society — a proposition that has been under constant threat by the court's increasingly conservative jurisprudence over the past 30 years. Specifically, Justice Kavanaugh observed that: "The plaintiffs seek to hold retailers to account if the retailers engage in unlawful anticompetitive conduct that harms consumers who purchase from those retailers. That is why we have antitrust law." He further noted that the text of the key statute governing private antitrust enforcement (Clayton Act Section 4), "broadly affords injured parties a right to sue under the antitrust laws." Whether Justice Kavanaugh's break with the other conservative justices in this case is an unexpected shift in his view of antitrust law, or merely a blip that turns on the indirect purchaser standing issue presented in this case, remains to be seen.

The Indirect Purchaser Rule

The dispute in the Apple case arises from the Supreme Court's decision in *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), to limit standing in antitrust cases brought by private plaintiffs seeking damages. In *Illinois Brick*, the plaintiffs asserted that a group of defendant concrete manufacturers had fixed prices. The plaintiffs in that case had not directly purchased concrete from the defendants but rather were purchasers further down the distribution chain. The plaintiffs argued that they were still impacted by the price fixing scheme because the higher prices had been "passed on" to the plaintiffs by the direct purchasers. The Supreme Court ruled that, as a matter of policy, the plaintiffs in *Illinois Brick* could not bring suit because they had not purchased the concrete directly from the price-fixing defendants. The court held that only the direct purchasers, i.e. "the immediate buyers" had standing to sue. The court justified this limitation on standing as necessary to facilitate efficient enforcement of the antitrust laws, avoid complicated damages calculations, and eliminate the potential for duplicative recoveries against the same defendants.

There was a significant backlash to the *Illinois Brick* decision across the country. About half the states passed what are often referred to as Illinois-Brick "repealer" statutes. In these states, including California, the state antitrust laws have been amended to make clear that indirect purchasers do have standing to sue. As a result, it is now quite common for there to be multiple class actions consolidated against antitrust defendants: a direct purchaser class action under federal law, and also a series of indirect purchaser class actions filed under various state antitrust laws. Federal courts have become increasingly adept at managing and navigating the multiple class actions and so increasingly some have suggested that the original rationale for the *Illinois Brick* rule — administrative efficiency and the avoidance of complex damage calculations for multiple parties — no longer justifies the rule.

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The *Apple* Case

The facts underlying the *Apple* case are fairly straight forward. The consumer plaintiffs, owners of Apple iPhones, alleged that Apple has violated Section 2 of the Sherman Act by monopolizing the market for the sale of apps. The plaintiffs alleged that Apple, which requires that iPhone owners buy apps only through Apple's App Store, has used its monopoly power to charge higher prices than would otherwise exist in a competitive market.

Importantly, Apple does not create most of the apps in the App Store. Independent developers create most of the apps but then contract with Apple to sell the apps directly to iPhone owners. Apple sets certain pricing criteria (all app prices must end in $0.99) but the developers can set the prices within those parameters. However, Apple mandates that it will keep 30 percent of the sales price in all circumstances.

In 2011, plaintiffs sued Apple in the Northern District of California, and alleged that Apple's requirement that iPhone owners purchase apps only through Apple's App Store, and mandating a 30 percent markup on all apps, constitutes an unlawful exercise of monopoly power. Plaintiffs alleged that in a competitive market, free from these restrictions, they would be able to purchase apps elsewhere and there would be increased price competition.

Apple filed a motion to dismiss and asserted that the plaintiffs lacked standing to maintain the lawsuit under the Supreme Court's *Illinois Brick* decision. The district court agreed with Apple's argument that the plaintiffs should not be deemed direct purchasers because the independent developers set the final retail price, and therefore any claim for monopolization against Apple could only be filed by the independent app developers.

The 9th U.S. Circuit Court of Appeals reversed the district court's ruling. The 9th Circuit found that the consumer plaintiffs are direct purchasers because, regardless of who sets the price, the iPhone owners purchase the apps directly from Apple.

The Supreme Court granted Apple's petition for certiorari. Interestingly, while the consumer plaintiffs did not ask the court to reconsider the *Illinois Brick* decision, an amicus brief filed by 30 state attorneys general and the District of Columbia expressly asked the court to overturn *Illinois Brick*'s indirect purchaser rule. The state attorneys general argued that the rule was no

longer necessary in light of subsequent developments in economic modeling and the federal courts' experience handling both direct and indirect purchaser claims over the past four decades. When Justices Samuel Alito and Neil Gorsuch raised the possibility of revisiting *Illinois Brick* during oral argument, some observers began to ask whether the court might use the *Apple* case as an opportunity to reverse the indirect purchaser rule.

The Majority Opinion

Ultimately, the Supreme Court affirmed the 9th Circuit's decision and held that the plaintiff consumers have standing to sue. As the majority explained, "It is undisputed that that the iPhone owners bought the apps directly from Apple. Therefore, under *Illinois Brick*, the iPhone owners were direct purchasers who may sue Apple for alleged monopolization."

The court explained that this holding was simply a "straightforward" application of the statutory text and the case law. The court noted that Section 4 of the Clayton Act provides that "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue." Further, the court explained that "unlike in *Illinois Brick*, the iPhone owners are not consumers at the bottom of a vertical distribution chain … there is no intermediary … iPhone owners purchase apps directly from the retailer Apple … [and] the absence of an intermediary is dispositive."

The majority rejected Apple's various arguments for finding that *Illinois Brick* should preclude standing in this case. Among other things, the court rejected Apple's contention that plaintiffs should only be allowed to sue "the party that sets the retail price, whether or not that party sells the good or service directly to the complaining party." The court found that "Apple's theory contradicts statutory text and precedent." The court reiterated that Section 4 of the Clayton Act "broadly affords injured parties a right to sue under the antitrust laws," and that *Illinois Brick*'s "bright-line rule … was not based on an economic theory about who set price." In a strong rebuke to Apple's legal and economic arguments, the court pragmatically noted that "Apple's line-drawing does not make a lot of sense other than as a way to gerrymander Apple out of this and similar lawsuits."

In finding in favor of the plaintiffs, the court asserted that its ruling was well within the policy rationales underlying the *Illinois Brick* decision. Thus, the court rejected the request of the 30 states and the District of Columbia to overturn the indirect purchaser rule. The court explained: "In light of our ruling in favor of plaintiffs in this case we have no occasion to consider [the] argument for overruling *Illinois Brick*."

However, several observations in a later portion of the majority opinion could give hope to those who want to at least narrow the scope of the *Illinois Brick* doctrine. For example, the court acknowledged Apple's contention that calculating damages in this circumstance might be complicated: "It is true that it may be hard to determine what the retailer would have charged in a competitive market. Expert testimony will often be necessary. But that is hardly unusual in antitrust cases. *Illinois Brick* is not a get-out-of-court free card for monopolistic retailers to play any time that a damage calculation is complicated."

Similarly, the court acknowledged that, in addition to the iPhone owners, "it could be that some upstream app developers will also sue Apple on a [purchasing or buyer side] monopsony theory." Yet, the majority was unpersuaded that this would create concerns about overlapping damage claims because even if there were two antitrust lawsuits (one from consumers and one from app developers), they would rely on "fundamentally different theories of harm."

The Dissent

The dissent, written by Justice Gorsuch, offered a stinging rebuke to the majority opinion. In Justice Gorsuch's view, *Illinois Brick* clearly barred the plaintiffs from suing *Apple* for monopolization. Indeed, in his expansive view of the *Illinois Brick* doctrine, Justice Gorsuch explained in a footnote that not only would he bar the consumer plaintiffs from bringing a damages claim under Section 4 of the Clayton Act, but he also believes that the indirect purchaser rule should be extended to deny plaintiffs standing even for injunctive relief claims under Section 16 of the Clayton Act. Such a limitation on standing for injunctive relief has never been adopted by the Supreme Court. Justice Gorsuch's observation suggests that he may have a narrow view of private antitrust enforcement — notwithstanding support from many plaintiff-side antitrust practitioners who, at the time of his nomination to the court, believed (perhaps incorrectly) that he would be a voice of reason on a court that has increasingly limited the scope of antitrust law in recent years.

On the merits, the dissent argued that the majority was effectively disregarding the underlying rationale for *Illinois Brick*. In the dissent's view, *Illinois Brick* was premised primarily on proximate causation concerns (taken from traditional tort law). In tracing the rationale for the *Illinois Brick* rule, Justice Gorsuch cited to the court's earlier decision in *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968). In *Hanover Shoe*, the court rejected the so-called "pass-on defense" in antitrust cases. That defense, which was expressly rejected by the court, is based on the idea that even if a defendant has unlawfully charged a plaintiff higher than competitive prices, the defendant's liability to the plaintiff should be limited if the plaintiff simply "passed-on" the overcharge to downstream customers. Justice Gorsuch explained that *Illinois Brick* was "just the other side of the coin": "With *Hanover Shoe* having held that an antitrust defendant could not rely on a pass-on theory to avoid damages, *Illinois Brick* addressed whether an antitrust plaintiff could rely on a pass-on theory to recover damages." The answer was no, and so, in the dissent's view, the same rationale should have applied in this case.

Interestingly, notwithstanding his comments during the oral argument, Justice Gorsuch rejected the states' suggestion that the court should consider overturning the *Illinois Brick* rule. While acknowledging that "[m] aybe there is something to these arguments; maybe not … there is plenty of reason to decline any invitation to take even a small step away from *Illinois Brick* today."

The Aftermath

The Supreme Court's decision, particularly Judge Kavanaugh's surprisingly strong language touting the importance of antitrust enforcement against monopolists, may give a glimmer of hope to those who want to see a reinvigoration of antitrust enforcement, particularly when it comes to Silicon Valley companies. Yet caution is in order. The court's string of decisions limiting the rights of consumers to maintain class action claims, and it's now decades-long antipathy toward, and narrowing of, antitrust enforcement, make it difficult to read too much into this one decision. But it would certainly be a surprise to many if Justice Kavanaugh were to carve out a position on antitrust enforcement that is not simply in lock step with the other conservative justices on the court. Time will tell.

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