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Is It Bad To Be Big?

An Antitrust Update On Monopoly Law And Enforcement

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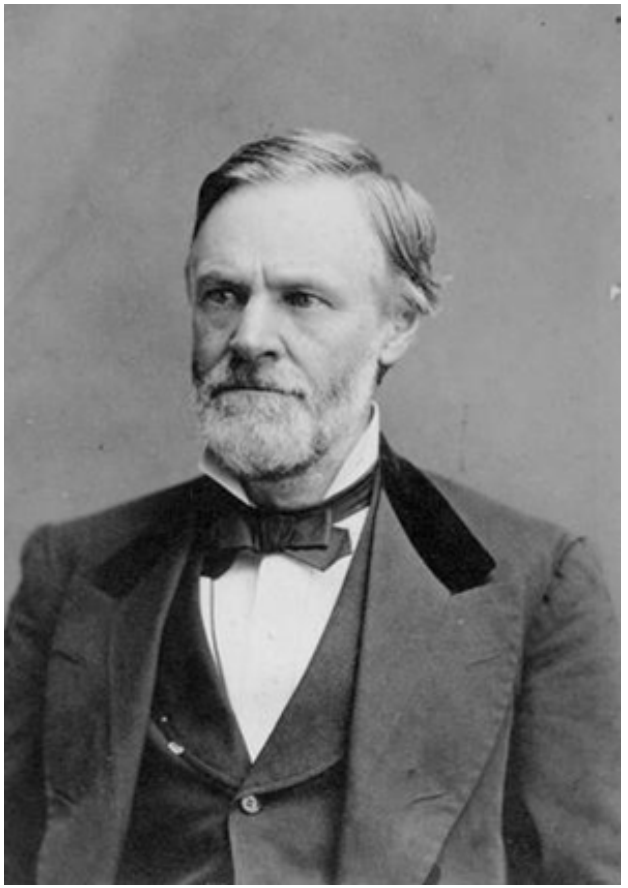
May 23, 2019

MCLE Certificate Information

- Most participants should anticipate receiving their certificate of attendance in four weeks following the webcast.
- Virginia Bar Association members should anticipate receiving their certificate of attendance in six weeks following the webcast.
- All questions regarding MCLE Information should be directed to Jeanine McKeown (National Training Administrator) at 213–229-7140 or jmckeown@gibsondunn.com.

Sherman Act Section 2

"Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony."
15 U.S.C. § 2.



"'M' for Monopolist is today's scarlet letter"

Break 'em up, say Dems: Why the 2020 field is taking aim at monopolies

REAL TIME ECONOMICS | ECONOMY

Monopolistic Power Is Growing Around the World, IMF Says

Tech Policy

Sen. Amy Klobuchar: 'We have a major monopoly problem'

APPLE \ POLICY \ TECH

Supreme Court says Apple will have to face App Store monopoly lawsuit

"Ever since Congress overwhelmingly passed and President Benjamin Harrison signed the Sherman Act in 1890, 'protecting consumers from monopoly prices' has been 'the central concern of antitrust.'"
— *Apple Inc. v. Pepper* (2019)

Elements of a Section 2 Violation

Monopolization

- Monopoly power in relevant market
- Anticompetitive conduct

Attempted Monopolization

- Dangerous probability of achieving monopoly power in relevant market
- Anticompetitive conduct
- Specific intent to monopolize

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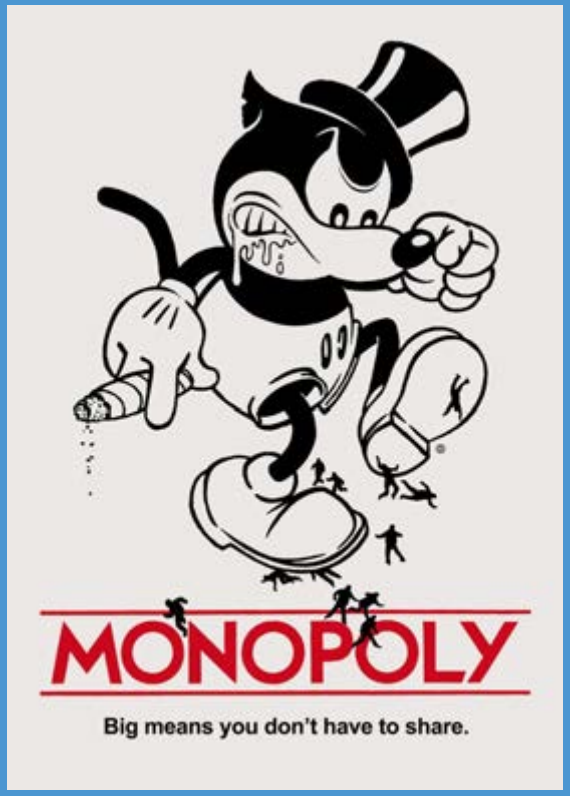

Relevant Markets and Monopoly Power

Relevant Markets

- Whether conduct has an anticompetitive effect is assessed in the context of a relevant market, or a defined area of commerce.
- Used to identify affected products, market players, and calculate measure of market concentration.
- Relevant market has two dimensions:
  - Product market
  - Geographic market

Relevant Markets

- Product Market: "The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962).

- Geographic Market: The geographic area within which competition in the relevant product market takes place.

Monopoly Power

- "Monopoly power is the power to control prices or exclude competition."
  United States v. E.I. du Pont Nemours & Co., 351 U.S. 377 (1956)

- "Price and competition are so intimately entwined that any discussion of theory must treat them as one. It is inconceivable that price could be controlled without power over competition or vice versa." *Id.*

- Monopoly power "under Section 2 requires . . . something greater than market power under Section 1."
  Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451 (1992)

Monopoly Power

- Direct Proof
- Circumstantial Proof
  - Market Share
  - Barriers to Entry/Expansion
  - Durability
  - Other Factors, such as:
    - Regulation of the industry
    - Size and sophistication of buyers
    - Pace of technological change

Market Share

- 90% "is enough to constitute a monopoly; it is doubtful whether 60 or 64 percent would be enough; and certainly 33 per cent is not"
  - *U.S. v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945) (Learned Hand, J.)
- 80% sufficient to survive summary judgment
  - *Eastman Kodak v. Image Tech.*, 504 US 451 (1992)
- < 50% generally held insufficient for monopolization claim

Market Share

- Lesser market share can suffice in attempted monopolization cases and Section 1 cases
  - >50%: Courts often find dangerous probability
  - ≤ 30%: Most courts find insufficient

- Declining market share alone may not rule out a finding of power

- **Note:** High market share does **not** result in inference of market or monopoly power absent significant barriers to entry

Pleading Relevant Market and Market Share

- Plaintiffs may attempt to plead narrow markets that produce high shares in order to survive motion to dismiss
  - Single-brand markets
  - Aftermarkets
  - Geographic or product sub-markets
  - Cluster markets

Monopsony Power

- A *buyer* may also possess power over price and entry: "[m]onopsony power is market power on the buy side of the market." *Weyerhaeuser Co. v. Ross-Simmons Hardware Lumber Co.*, 549 U.S. 312, 320 (2007)

- Recent surge of interest in supply-side concentration, particularly in labor markets.
  - "A firm that has market power when purchasing inputs or hiring workers – an employer with monopsony power – will face strong incentives to employ fewer workers, at lower wages, than they would in a competitive labor market." *Letter from Sen. Cory Booker to FTC and DOJ (Nov. 2017)*

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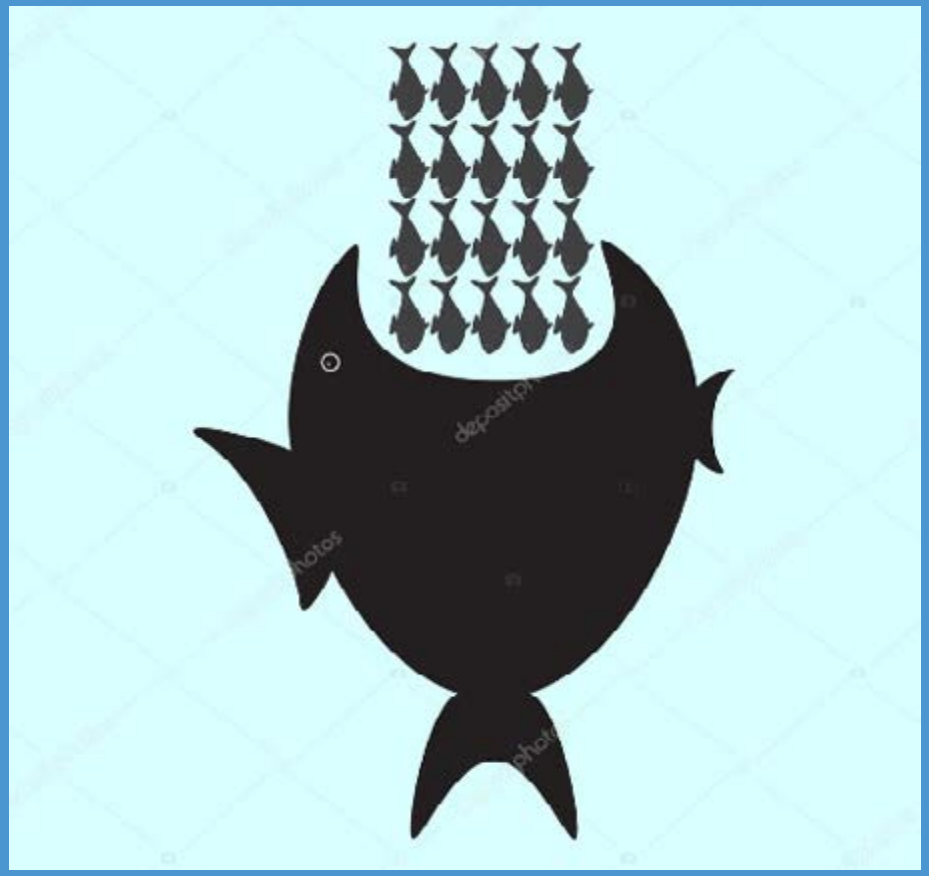


Anticompetitive Conduct

Anticompetitive Conduct

"[T]he possession of monopoly power will ***not*** be found unlawful ***unless it is accompanied by an element of anticompetitive conduct***."

"The ***mere … charging of monopoly prices***, is not only ***not unlawful***; it is an important element of the free-market system. [It] is what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth."

— *Verizon Communs. v. Trinko,* 540 U.S. 398 (2004)

Anticompetitive Conduct

"[T]he antitrust laws aren't designed to be a guide to good manners. ***Were intent to harm a competitor alone the marker of antitrust liability, the law would risk retarding consumer welfare by deterring vigorous competition***—and wind up punishing only the guileless who haven't figured out not to write such things down despite (no doubt) the instructions they received in countless 'antitrust compliance' seminars."

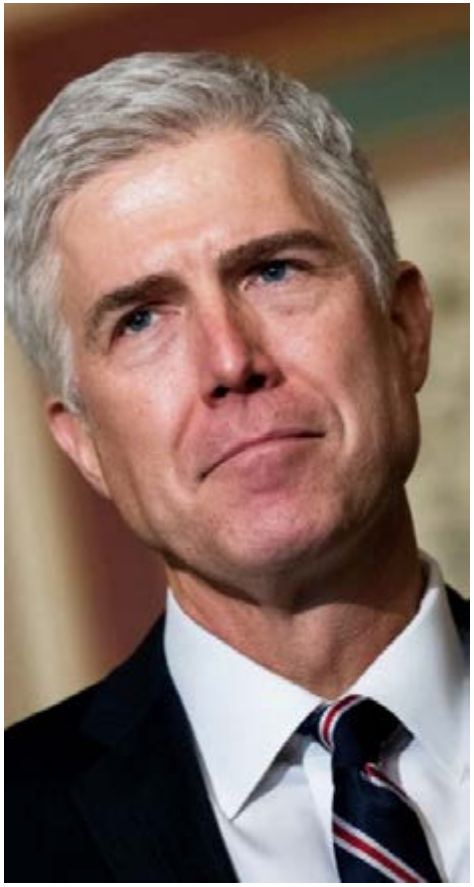
— *Novell v. Microsoft Corp.*, 731 F.3d 1064 (10th Cir. 2013)

Anticompetitive Conduct

"Whether any particular act of a monopolist is exclusionary, rather than merely a form of vigorous competition, can be difficult to discern… The challenge for an antitrust court lies in stating a general rule"

— *U.S. v. Microsoft*, 253 F.3d 34 (D.C. Cir. 2001)

"So What Exactly Qualifies As Anticompetitive Conduct Under §2?"



"[T]he question we often find ourselves asking is whether… the conduct at issue before us has little or no value beyond the capacity to protect the monopolist's market power—bearing in mind the risk of false positives (and negatives) …, and the limits on the administrative capacities of courts to police market terms and transactions."

— *Novell v. Microsoft*, 731 F.3d 1064 (10th Cir. 2013)

Anticompetitive Conduct

Exclusionary or predatory conduct is "[the] willful acquisition or maintenance of [monopoly] power as distinguished from growth or development as a consequence of a ***superior product, business acumen, or historic accident***."

— *U.S. v. Grinnell Corp.*, 384 U.S. 563 (1966)

Anticompetitive Conduct

"If a firm has been 'attempting to exclude rivals ***on some basis other than efficiency***,' it is fair to characterize its behavior as predatory."

— *Aspen Skiing v. Aspen Highlands Skiing*, 472 U.S. 585 (1985)

What Is A Procompetitive Justification?

- A valid justification relates directly or indirectly to the enhancement of consumer welfare, such as:
  - Expanding output
  - Improving quality or promoting innovation
  - Reducing cost
  - Preventing "free riding" by competitor
  - Increasing efficiency in other ways

- "A plaintiff may rebut an asserted business justification by demonstrating … that the justification is pretextual." *Image Tech. v. Eastman Kodak*, 125 F.3d 1195 (9th Cir. 1997).

Types of Anticompetitive Conduct

- **Pricing**
  - Below-cost
  - Package discounts
  - Loyalty discounts
  - MFNs
- **Sales/Distribution**
  - Exclusivity
  - Tying
  - "Unfair competition"
- **Product Design**
  - Lockout/incompatibility
- **Noncooperation with Rivals**
  - Refusal to deal
  - Dealing on discriminatory terms
  - Price squeeze
  - Denial of essential facility
- **Intellectual property**
  - Refusal to license IP
  - "Sham" litigation
  - Standard setting abuse

Aspen Skiing v. Aspen Highland Skiing, 472 U.S. 585 (1985)

- Monopoly owner of 3 Aspen ski areas entered into and then terminated a joint marketing arrangement with a 4th ski area. Court focused on various factors:
  - Voluntary prior history of dealing
  - No business justification offered
  - Monopolist unwilling to deal even if plaintiff paid retail prices

- *Held*: Defendant breached duty to deal. Terminating voluntary (presumably profitable) course of dealing suggested willingness to forsake short-term profits to achieve anticompetitive end in violation of § 2

When Does a Duty to Cooperate Arise?

- "[T]here must be a preexisting voluntary and presumably profitable course of dealing between the monopolist and rival." — *Novell*

- "[W]e require proof not just that the monopolist decided to forsake short-term profits," but that "the monopolist's conduct [is] irrational but for its anticompetitive effect." — *Novell*

- "[A] defendant with no antitrust duty to deal with its rivals has no duty to deal under the terms and conditions preferred by those rivals." — *LinkLine*

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Prospects for Congressional Action

Big = Bad?

- Sen. Klobuchar: block mergers involving large acquirer or significant increase in concentration

- Sen. Warren: require large “platform utilities” to divest participants; undo major tech mergers

Branded Pharmaceutical Companies

- Reverse-payment settlements: Compensation from patent holders barred except in narrow circumstances
- Facilitating generic competition: judicial remedy against branded cos. that refuse to sell samples to potential generic competitors
- Passed House May 16
- Senate action likely

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Antitrust and the Supreme Court

Prospects for Supreme Court Guidance

- Declining caseload
  - 70 merits cases per Term
  - Half the level of three decades ago

- Little Interest in Antitrust?
  - 15 antitrust cases in 20 years
  - 3 substantive Section 2 cases - 0 exclusive dealing
  - Contrast: 38 patent cases

- Potential for Growth
  - Justices Gorsuch & Kavanaugh

Apple v. Pepper

- Issue: Does *Illinois Brick* direct-purchaser rule bar suit by iPhone app purchasers challenging Apple's 30% commission to developers?

- Holding: No. Application of *Illinois Brick* rule depends on formal presence or absence of intermediaries, not economic substance

- Implications
  - Impact on electronic marketplaces?
  - Survival of *Illinois Brick* rule?
  - Extension to injunctive claims?
  - Populist tone – signaling or rhetorical flourish?

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Agency Overview

DOJ Leaders' Comments on Single-Firm Conduct

"I don't think big is necessarily bad, but I think a lot of people wonder how such huge behemoths that now exist in Silicon Valley have taken shape under the nose of the antitrust enforcers. You can win that place in the marketplace without violating the antitrust laws, but I want to find out more about that dynamic."

William Barr, Senate Confirmation Hearing

"In the United States, we believe that antitrust authorities should be cautious about challenging [unilateral] conduct.... The challenge is that, with respect to unilateral conduct, it is extremely difficult to distinguish between aggressive competition and anticompetitive conduct. As a result, over-zealous enforcers and courts run a significant risk of deterring hard—yet legitimate—competition...."

Makan Delrahim, *Antitrust Enforcement Priorities and Efforts Towards International Cooperation* (November 2004)

DOJ's Stance on §2 Enforcement

- No major monopolization case since enforcement action against United Regional Health Care System (2011)

- Section 2 enforcement does not appear to be enforcement priority
  - Principal DAAG Andrew Finch's speech on platforms and industry consolidation listed five enforcement priorities
    1. Vigilant merger review
    2. Structural remedies, not behavioral decrees
    3. Eliminate regulatory barriers to entry
    4. Anticompetitive conduct, such as information sharing
    5. Common ownership and interlocking directorates

FTC Leaders' Comments on Single-Firm Conduct

"I believe that big is not necessarily bad. I also believe that big is not necessarily good . . .Companies that are already big and influential can sometimes use inappropriate means, anticompetitive means to get big or to stay big. If that's the case, then we should be ... vigorously enforcing the antitrust laws and attacking that conduct and prohibiting it."

Joseph Simons, Senate Confirmation Hearing

"[W]e have a legal framework that requires that we be able to show that competition—not just competitors—has been harmed by the challenged conduct, and, in most cases, that the firm engaging in the conduct is a monopolist or is likely to become one. [This legal constraint] wisely keeps us focused on avoiding making an unwarranted inference of competitive harm from mere tough competition.

Bruce Hoffman, Speech on Tech Industry (2018)

FTC on §2 Enforcement

- Has been more active than DOJ – e.g., *Qualcomm*, *Surescripts*

- *FTC v. Surescripts, LLC* (complaint filed April 2019)
  - FTC: Monopolization in "e-prescription" markets
    - (1) routing (provider sends Rx to pharmacy)
    - (2) eligibility (PBM sends to provider)
  - Two-sided transactional platform markets
    - Bruce Hoffman: "Great deal of similarity" to *AmEx* case
  - Exclusive agreements, loyalty programs, and threats
    - Maintained 95+% share

FTC v. Qualcomm Inc.

- Complaint filed in January 2017
  - Alleged monopolization of baseband processors
- Court: Qualcomm violated both § 1 and § 2
  - Monopoly power in (1) CDMA and (2) premium LTE modem chip markets
  - Qualcomm has "strangled competition in the CDMA and premium LTE modem chip markets for years, and harmed rivals, OEMs, and end consumers …"
- Injunctive relief
  - No more "no license, no chips" policy
  - Must license standard-essential patents to other suppliers on FRAND terms
  - Cannot sign exclusive supply agreements with OEMs

Potential FTC Activity in §2: Technology Task Force

- Announced in February 2019
- Dedicated to monitoring, investigating, and taking enforcement actions in U.S. technology markets
- Characteristics
  - **Strong leadership**: Patricia Galvan, Krisha Cerilli and 15 attorneys
  - **Enforcement-oriented**, rather than focused on policy
  - **Modeled on the hospital merger task force** launched in 2002 by then-Bureau Director Joe Simons
  - May include **review of consummated mergers**
- Will try to create new enforcement paradigm for analyzing platforms

Section 2 in Politics and Public Discourse

- Sen. Elizabeth Warren (Mar. 2019)
  - Big Tech has too much power over economy, society, democracy
  - Regulate platforms as utilities
  - Break up Amazon, Facebook, Google by unwinding mergers

- Nobel laureate Joseph Stiglitz (Apr. 2019)
  - *People, Power, and Profits*
  - Updated antitrust rules needed to tackle income inequality, concentration of market power, and data privacy

- Prof. Jonathan Baker (May 2019)
  - *The Antitrust Paradigm*
  - Chicago School has fallen behind modern economy
  - Antitrust law should be updated for IT economy

Where is it all going?

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Section 2:
A Platform View

The Evolving Role of Platforms

- The growing importance of dominant platforms in modern economic and social life has created a policy challenge for competition agencies
  - Key questions: Are platform markets more prone to monopolizing conduct; is market power of platform firms more durable? Do we need new antitrust economics to deal with platforms?
- Some economics suggests that markets with Multisided Platforms (MSPs) may be more prone towards concentration and successful monopolization
- Vertical integration of platforms into complementary lines of business can be a source of "unfair" competitive advantage, create incentives for discriminatory treatment of rivals who use the platform, and facilitate monopolization of adjacent markets
- Some policy makers and scholars suggest that regulation and divestitures may be required to control the growth and conduct of platform monopolies.
- I disagree! Existing tools of antitrust policy, modified when needed and properly applied, can deal with many of the competitive issues engendered by MSPs' practices

What We Need to Know About MSPs

- Key features of an MSP:
  - (i) Serves at least two distinct groups of customers; (ii) at least one group (side) confers a *positive benefit (externality)* on customers on the other side (e.g., an increase in the number/quality of customers on one side benefits customers on the other side); and (iii) participation and the volume of transactions intermediated by the platform depends on *levels* of fees charged to each side and also on their *structure*
  - Example: price to group 1 is $2/transaction and to group 2 is $3 for the total of $5 resulting in 100 transactions/day. If prices are "swapped", holding the sum at $5 per transaction, the number of transactions can go up or down!
- Section 2 analysis of MSP markets and conduct must fully account for features (ii) and (iii), above
- Without understanding these features and their business role, the analysis of market power and monopolization as these pertain to MSPs can go awry

Is Extraordinary Vigilance Required?

- Is monopolizing conduct in platform markets more likely?
  - Are there more strategic options?
  - Greater opportunity to recoup?
- Are the risks of price predation that are unique?
- Are the risks of successful exclusionary conduct through rising rivals' costs and other strategies elevated by the multi-sided nature of platform businesses?
- Or are we over-reacting because of the lack of deep familiarity with and understanding of MSPs pro-competitive business practices?

Predation or Just Competition?

- Pricing by a platform operator must induce, maintain, and encourage participation on all sides of the platform
- Prices reflect not only the demand elasticities on the two sides but, crucially, the consequences of price changes on one side for the demand on the other side
- As a result, innocent profit maximization can lead to one side "subsidizing" the other side and thus appear monopolizing or predatory
  - Credit card platforms charge merchants a positive per transaction fee and a negative fee per transaction (rewards) to card users. Exchanges often charge positive transaction fees to liquidity takers and negative fees to liquidity makers.
  - Such asymmetric pricing need not be "predatory" or evidence exercise of market power. A test: compare the sum of prices
  - Regulations that force prices to some measures of allocated costs can weaken the platforms and harm consumers

Special Case: Free Services

- On subsidy-based platforms, like the social media platforms, pricing imbalance can be extreme
- For example, on a platform like Facebook or Spotify users don't pay. "Subsidizers" defray the full cost.
  - This is not predatory monopolization but reflects the fact that subsidizers covet access to the platform users
  - Charging users would inefficiently discourage their participation
- Still, this type of platform pricing raises some interesting policy questions:
  - Since usage of the platform generates valuable information, who owns the rights to this information?
  - Is "FREE" the right price for loss of privacy?
  - What is the impact of such pricing on non-platform rivals?
  - Can the platform owner use big data to foster its competitive services?
  - If excessive price is a sign of monopoly power, can a firm that charges "zero" ever exhibit market power?

Exclusivity and Exclusionary Conduct

- Markets with MSPs create opportunities for exclusionary conduct
  - However, not clear whether MSPs are especially prone to such conduct and monopolization is not necessarily more likely or plausible
- A dominant MSP may limit or impede the ability of its users to participate on rival MSPs.
  - When users participate on more than one MSP, they *multi-home;* if they participate on a single platform, they *single-home*
- Multi-homing fosters inter-platform competition: makes it easier for rivals to build membership and take advantage of scale economies
- Single-homing makes it more costly for a rival to divert demand from incumbent but creates incentives to build a high quality platform
- Exclusionary practice may harm one side and benefit the other side of a platform: how should the regulator weigh the costs and benefits of the practice to different sides?
- Perhaps we shall learn more from the case filed by the FTC against *Surescript* which focuses on *sophisticated* pricing strategies by a firm with a very *large market share* operating in *two-sided markets*: an economist's dream case!

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Our next Antitrust & Competition Law webinar is scheduled for **June 20th, 2019.**

Please join us for a discussion of "**Dealing with online markets and digital services**" in which our panel will give an overview of recent developments and future trends in emerging antitrust issues arising from online players.

Registration details will be available later this month. We encourage you to join us.