18. Unilateral Refusals to Deal

Antitrust Law

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Unilateral Refusals to Deal

- Concept
  - Firm A, acting solely on its own, refuses to deal with Firm B
  - Examples
    - Firm A refuses to sell a product or service to Firm B
    - Firm A refuses to buy a product or service from Firm B
    - Firm A refuses to allow Firm B to interconnect to Firm A's network
    - Firm A refuses to provide Firm B with advance notice of Firm A's design changes, preventing Firm B from adapting its products and having them available for sale at the time of Firm A new design release
    - Firm A refuses to design its products so that Firm B's product will work with them

- Question
  - Under what circumstances, if any, is Firm A's refusal to deal a violation of the antitrust laws?

Unilateral Refusals to Deal

- Statutory coverage
  - Sherman Act § 1: Not applicable *provided that the refusal to deal stays unilateral*
  - Sherman Act § 2: Applies to unilateral action, but the refusal to deal must—
    - Be anticompetitively exclusionary, *and*
    - Be part of a scheme to obtain or maintain monopoly power in a relevant market (monopolization) or have a dangerous probability of achieving a monopoly (attempted monopolization)

> *Remember*: Footnote 4 of *Trinko* requires that every antitrust violation satisfy each and every element of the prima facie case for some statutory violation.[1]

[1] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 415 n.4 (2004).

Unilateral Refusals to Deal

- No general antitrust duty to deal
  - A simple unilateral refusal to deal is *not* an anticompetitive exclusionary act that can predicate a Section 2 violation in the absence of a violation of an *antitrust deal to deal*
  - There is no general duty to deal imposed by the antitrust laws[1]
    - This is known as the *Colgate* doctrine
  - Duties to deal imposed by other (regulatory) laws do not create a duty to deal under the antitrust laws unless Congress so specifies[2]

[1] United States v. Colgate & Co., 250 U.S. 300 (1919).
[2] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004).

Unilateral Refusals to Deal

- Policy rationale

> Firms may acquire monopoly power by establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill-suited. Moreover, compelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion. Thus, as a general matter, the Sherman Act "does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal." United States v. Colgate & Co., 250 U.S. 300, 307(1919).[1]

- Summary
  - Reduces incentives to greater better products or services in order to gain a competitive advantage
  - Problems setting, monitoring and enforcing terms of dealing
  - May facilitate collusion

[1] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407-08 (2004).

Unilateral Refusals to Deal

- Exceptions
  - *Aspen*[1]

> However, "[t]he high value that we have placed on the right to refuse to deal with other firms does not mean that the right is unqualified." Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 601 (1985). Under certain circumstances, a refusal to cooperate with rivals can constitute anticompetitive conduct and violate § 2. We have been very cautious in recognizing such exceptions, because of the uncertain virtue of forced sharing and the difficulty of identifying and remedying anticompetitive conduct by a single firm. The question before us today is whether the allegations of respondent's complaint fit within existing exceptions or provide a basis, under traditional antitrust principles, for recognizing a new one.[1]

    - Requirements
      - Prior voluntary (and presumably profitable) course of dealing
      - Termination of that prior course
      - Sacrifice of short-term profits because of the termination
      - Expectation that sacrifice of short-term profits from the termination will lead to higher profits in the long term resulting from anticompetitive changes in the market
    - Observation
      - Subsequent courts have often noted that the *Aspen* defendant refused to sell to the plaintiff even at full retail price that the defendant readily sold to other third parties.

[1] Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985) (discussed *infra*)
[2] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 408 (2004) (finding no exception in the circumstances of the case).

Unilateral Refusals to Deal

- Turning a unilateral conditional sales policy into concerted action[1]
  - Conditional sales policy
    - Scenario
      - "You are free to do anything you want, but please be aware that I will continue to deal with you only as long as you follow my sales policy"
      - When the downstream firm violates the seller's sales policy, the seller refuses to continue to sell to the downstream firm
    - *Rule*: Standing alone, announcing a conditional sales policy and refusing to sell to a firm that violates the policy is not an exclusionary act that can predicate a Section 2 violation
      - This is the classic example of the application of the *Colgate* doctrine
  - Agreement to abide by conditional sales policy
    - Scenario
      - "I know that I violated your sales policy. I promised not to do it again. Please continue selling to me." And the seller continues to sell.
    - Courts treat this as concerted action cover by Sherman Act § 1.
  - The key to unilateral action is that the downstream firm must not make any explicit or implicit promise to abide by the seller's sale policy

[1] United States v. Parke, Davis & Co., 362 U.S. 29 (1960).

Exceptions to the *Colgate* Rule

- Other exceptions to the *Colgate* rule
  - Secondary boycotts: "I will not deal with you if you deal with Firm X"[1]
  - Enlisting third parties to monitor compliance with a conditional sales policy[2]
  - (Perhaps) a discriminatory refusal to deal[3]
  - Discontinuing an historical, profitable course of dealing with a competitor with intent to destroy competition and harm a competitor, with the result that the seller gains or preserves monopoly power[4]
    - These are the facts in *Aspen Skiing*, which the *Trinko* Court described this as "at or near the outer boundary of § 2 liability."[5]

[1] Lorain Journal Co. v. United States, 342 U.S. 143 (1951).
[2] United States v. Parke, Davis & Co., 362 U.S. 29 (1960).
[3] Otter Tail Power Co. v. United States, 410 U.S. 366 (1973).
[4] Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985).
[5] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 409 (2004)

The "Essential Facilities" Doctrine

- The concept
  - The essential facilities doctrine imposes on the owner of a facility that cannot reasonably be duplicated and which is essential to competition in a given market a duty to make that facility available to its competitors on a reasonable nondiscriminatory basis
    - *Example*: A railroad owns a bridge over a river. If the bridge could not reasonably be duplicated, the railroad would have an antitrust duty to make the bridge available to its railroad-competitors on reasonable nondiscriminatory terms
      - This is *Terminal Railroad*, except that a single railroad rather than a railroad consortium owns the bridge
- Origins
  - The single-firm version has its source in *Otter Tail*,[1] where an electric utility was forced to allow a competitor to transmit power over its lines
- Judicial acceptance
  - At best, the doctrine gained only limited acceptance by the courts as an antitrust rule
  - The Supreme Court has never explicitly recognized the doctrine

[1] Otter Tail Power Co. v. United States, 410 U.S. 366 (1973).

The “Essential Facilities” Doctrine

- Requirements [1]
  - Courts that have accepted the doctrine usually require the following:
    - Control of the essential facility by a monopolist
    - A competitor's inability practically or reasonably to duplicate the essential facility
    - The denial of the use of the facility to a competitor
    - The feasibility of providing the facility

[1] *See* MCI Commc’ns Corp. v. AT&T Co.,, 708 F.2d 1081. 1132-33 (7th Cir.1982),

The "Essential Facilities" Doctrine

- Two interpretations
  - Where the requirements of the essential facility doctrine apply, the failure to provide reasonable nondiscriminatory access to competitors violates the antitrust laws
    - This was the usual interpretation
    - This interpretation surely has been rejected by *Trinko*, since the doctrine's four elements by themselves do not satisfy the requirements for a prima facie case of monopolization or attempted monopolization
  - A more nuanced interpretation is that the doctrine's four elements define when a refusal to provide reasonable nondiscriminatory access qualifies as an anticompetitively exclusionary act that could predicate a monopolization or attempted monopolization violation[1]
    - But this appears to be rejected by *Trinko* as well, since the facts of *Trinko* satisfied the four requirements (and in addition a regulatory duty to deal) and yet the Court reversed the lower court, which had used the essential facilities doctrine to find an antitrust violation
- Vitality today
  - Today, especially after *Trinko*, the doctrine as applied to single firms is essentially dead
    - The *Terminal Railroad* rule, which speaks to the duty of a horizontal combination to provide reasonable nondiscriminatory access to non-consortium competitors remains well-accepted law

[1] *See* MCI Commc'ns Corp. v. AT&T Co.,, 708 F.2d 1081 (7th Cir.1982).

Seminal Cases

United States v. Colgate & Co.[1]

- Indictment (1917): Resale price maintenance under *Dr. Miles*
  - Charged that Colgate had created and engaged in a combination in violation of Section 1 with its wholesale and retail dealers to fix the resale prices of Colgate's laundry soaps, toilet soaps and other toilet articles and so competition among its dealers
  - Factual allegations: Colgate
    - distributed lists of uniform resale prices,
    - urged dealers to conform to them
    - informed dealers that Colgate would refuse to sell to those that did not adhere to its price lists
    - requested dealers to inform Colgate of other dealers who sold at different prices
    - maintained lists of nonconforming dealers
    - Reinstated dealers on the "suspended list" if they gave assurances that they would adhere to the lists in the future

- District court: Sustained demurrer
  - No monopolization or attempted monopolization charged
  - No horizontal manufacturer conspiracy
  - No allegation that Colgate's prices were unfair
  - No allegation that Colgate restricted the buyers to whom its dealers could resell or required its dealers to impose resale restrictions on their customers
  - Colgate had no contracts with its dealers that require them to sell at Colgate's resale prices
  - Indictment was solely against Colgate

[1] 250 U.S. 300 (1919).

United States v. Colgate & Co.

- Supreme Court: Affirmed (9-0)
  - Procedure
    - Direct appeal under Criminal Appeals Act
    - Bound by district court's interpretation that there was no contract between Colgate and its dealers to maintain resale prices
  - Merits
    - *Key*: Unilateral sales policy

> [A Colgate dealer], after buying, could, if he chose, give away his purchase or sell it at any price he saw fit, or not sell it at all, his course in these respects being affected only by the fact that he might by his action incur the displeasure of the manufacturer who could refuse to make further sales to him, as he had the undoubted right to do.[1]

  - *Rule*: A seller may announce a sales policy as to the conditions under which it will sell and is free to refuse to continue to sell to buyers that do not abide by the rules
  - Footnotes
    - This is a very technically based opinion, yet one that announced a fundamental rule of antitrust law
    - Colgate's counsel: former Justice Charles Evans Hughes, the author of the Court's opinion in *Dr. Miles*

[1] *Colgate*, 250 U.S. at 306 (quoting 253 F. 522, 527 (E.D. Va. 1918)).

Lorain Journal Co. v. United States[1]

- Background
  - Since at least 1932, Lorain Journal was the only newspaper in Lorain, Ohio
  - In 1948, WEOL established in Elvira, Ohio, 8 miles south of Lorain
  - Lorain Journal refused to accept local advertisements from anyone:
    - Who advertised on WEOL, or
    - LJ believed was about to advertised on WEOL
- Complaint
  - Sherman Act § 1 conspiracy between Loran J. Co. & 4 of its officers/Sherman § 2 conspiracy to monopolize
  - Sherman § 2 attempt to monopolize
- District court: Found for plaintiff on attempt to monopolize
- Supreme Court: Affirmed
  - Relevant markets
    - Interstate news
    - National advertising
  - Conduct exclusionary—Secondary boycott
    - Advertising in LJ essential to local merchants → Local merchants would not advertise on WEOL
    - WEOL could not survive without local advertising
  - Dangerous probability of success (specific intent to monopolize not challenged)

[1] 342 U.S. 143 (1951).

United States v. Parke, Davis & Co.[1]

- Background
  - Parke, Davis
    - A major pharmaceutical manufacturer, producing some 600 products that it distributed through drug wholesalers and retailers
    - Had announced policy that it would not continue to sell to wholesalers and retailers that followed PD's suggested resale prices
      - PD intended its practices to fall within the *Colgate* doctrine
  - Violation of policy
    - In 1956, several retailers in the District of Columbia and Virginia advertised and sold PD vitamin products at prices substantially less than PD's suggested resale level
  - PD response
    - PD would not sell to wholesalers that sold PD products to any retailer that did not abide by PD's resale price policy
      - PD told each of the five area wholesalers that it was imposing the same policy on all wholesalers
      - All five area wholesalers indicated a willingness to follow the new policy
    - PD informed each of the area retailers of this new policy and of the fact that the policy would apply to all area retailers
      - Several retailers indicated their willingness to abide by PD's suggested resale prices
      - Other retailers continued to sell at discounted prices
    - PD provided the names of the discounting retailers to the area wholesalers
      - Thereafter, neither PD nor its wholesalers would sell PD products to the identified retailers
    - Once the retailers ceased selling below Parke, Davis' suggested retail resale prices, however, Parke, Davis resumed selling to them and authorized its wholesalers to do the same

[1] 362 U.S. 29 (1960).

United States v. Parke, Davis & Co.[1]

- Complaint
  - Alleging that PD's actions in securing compliance to its suggested retail prices went beyond what *Colgate* permitted and so violated Section 1 of the Sherman Act
- District court: Dismissed complaint
  - After the government completed the presentation of its evidence at trial, and without hearing PD's evidence in its defense, the district court dismissed the complaint for the government's failure to prove its prima facie case
- Supreme Court : Reversed (6-3)
  - Brennan (for six members)
    - *Colgate* limited to announcement of policy and a simple refusal to deal with those that do not abide
    - Here, PD—
      - Engaged in a secondary boycott with wholesalers against discounting retailers and disseminated names of discounting retailers to wholesalers in furtherance of this boycott
      - Reached agreement with some retailers that they would cease discounting
        - Sometimes a simple agreement
        - Other times, particular retailers required PD to obtain agreement from other retailers that they each would cease discounting before the target discounter would agree to stop discounting (i.e., "I will agree to stop discounting only if you get my competitors A and B to stop discounting")
    - Remanded with instructions to enter judgment for the government
  - Harlan (dissenting, with two other members)
    - *Colgate* should apply on the facts found by the district court—Majority went beyond those facts

[1] 362 U.S. 29 (1960).

Official Airline Guides, Inc. v. FTC[1]

- Background
  - OAG
    - Published the monthly Official Airline Guide—the "bible" for flight information—which provided detailed flight information between city pairs (e.g., between New York and Indianapolis) for the following types of flights:
      - Direct flights of certificated carriers
      - Connecting flights of certificated carriers, that is, flights involving the use of one direct flight in conjunction with another to provide transportation between two cities
      - Direct flights of intrastate air carriers
      - Direct flights of commuter air carriers
    - OAG did not publish flight schedules for connecting flights of commuter air carriers
- FTC
  - OAG was a monopolist in flight information
  - Its refusal to list fight information for connecting flights of commuter air carriers significantly handicapped them in competing with certificated carriers in violation of FTC Act § 5
- Second Circuit: Reversed
  - Upheld FTC's findings of significant competition between certificated and commuter carriers, injury to that competition as a result of OAG's refusal to publish connecting commuter flight information, and that this refusal was arbitrary (unjustified)
  - But OAG was not a competitor in airline fights and neither Section 5 nor the antitrust laws impose a duty to deal on noncompetitors acting unilaterally even if arbitrarily

[1] 630 F.2d 920 (2d Cir. 1980).

Aspen Skiing Co. v. Aspen Highlands Skiing[1]

- Background
  - Between 1945-1967, three major facilities independently developed:
    - Aspen Mountain (Ajax) by Ski Co. in 1946
    - Aspen Highlands (Highlands) in 1957
    - Buttermilk, (1958) which was acquired by Ski Co. in 1964
    - Snowmass, developed by Ajax in 1967
  - Tickets
    - For a number of years, Ski Co. and Highlands cooperatively offered an “all-Aspen” ticket
    - In 1979, after repeatedly demanding an increased share of the proceeds, the defendant withdrew its participation in the all-Aspen ticket
  - Highlands response
    - Tried to recreate joint ticket, even offering to buy Ski co.’s tickets at retail
    - Without all-Aspen ticket, Highlands became a "day" ski resort
      - Share steadily declined from 20.5% (1976-77) to 11% in 1980-81 (making Ski Co. 89%)
      - Ancillary revenues from ski school, ski rentals, restaurants also declined

- Highlands complaint
  - Ski Co. monopolized market for downhill skiing at Aspen
  - Prayer: Treble damages and injunction to continue to deal

[1] 472 U.S. 585 (1985).

Aspen Skiing Co. v. Aspen Highlands Skiing

- Lower courts
  - District court
    - Jury: Found for plaintiff and awarded $2.5M actual damages ($7.5 million trebled)
    - Court: Injunction requiring Ski Co. to participate in a 4-area, 6-out-of-7 day pass for a period of 3 years
  - Tenth Circuit: Affirmed
- Supreme Court: Affirmed (8-0). Opinion by Justice Stevens
  - Relevant market: Not contested
  - Monopoly power: Not contested
  - Intent: General intent sufficient for monopolization
  - Exclusionary act
    - Δ: Refusal to deal not exclusionary
    - Stevens: Evidence was sufficient for jury to find that refusal to deal was anticompetitively exclusionary
      - All-Aspen ticket was profitable to Ski Co. as shown by its willingness to participate for years
      - Consumers strongly valued the all-Aspen ticket → consumers were materially harmed by the refusal
      - Refusal impaired Highlands' ability to compete and increased Ski Co.'s share
        - Highland's share dropped from 20% to 11% over four years since the all-Aspen pass discontinued
      - Ski Co. had no efficiency justification
      - Unwillingness to sell Highlands tickets even at retail price showed that Ski Co. wished to harm a competitor by reducing competition (i.e., the ability of its only competitor to compete)
  - Conclusion: Evidence sufficient to support jury finding
    - Jury could have concluded that Ski Co. "elected to forgo . . . short-run benefits because it was more interested in reducing competition in the Aspen market over the long run by harming its smaller competitor."

Aspen Skiing Co. v. Aspen Highlands Skiing

- Supreme Court (con't)
  - Remember the procedural posture of the case (challenge to the sufficiency of the evidence):

> Perhaps most significant, however, is the evidence relating to Ski Co. itself, for Ski Co. did not persuade the jury that its conduct was justified by any normal business purpose. Ski Co. was apparently willing to forgo daily ticket sales both to skiers who sought to exchange the coupons contained in Highlands' Adventure Pack, and to those who would have purchased Ski Co. daily lift tickets from Highlands if Highlands had been permitted to purchase them in bulk. The jury may well have concluded that Ski Co. elected to forgo these short-run benefits because it was more interested in reducing competition in the Aspen market over the long run by harming its smaller competitor.[1]

- *Trinko* take on *Aspen*

> Aspen Skiing is at or near the outer boundary of § 2 liability. The Court there found significance in the defendant's decision to cease participation in a cooperative venture. The unilateral termination of a voluntary (and thus presumably profitable) course of dealing suggested a willingness to forsake short-term profits to achieve an anticompetitive end. Similarly, the defendant's unwillingness to renew the ticket even if compensated at retail price revealed a distinctly anticompetitive bent.[2]

- Footnote: In 2001, Ski Co. acquired Highlands

[1] *Aspen Skiing*, 472 U.S. at 608.
[2] *Trinko*, 540 U.S. at 409.

Verizon Commc'ns Inc. v. Trinko[1]

- Background
  - To facilitate entry into local telephone service, the Telecommunications Act of 1996 requires Incumbent Local Exchange Carriers (ILECs)—the original Baby Bell companies—to provide new, so-called Competitive Local Exchange Companies (CLECs) with access to the ILEC's local telephone network, including access to individual network elements on an "unbundled" basis
  - Verizon, the ILEC in New York State, signed interconnection agreements with a number of CLECs, including AT&T (the long-distance carrier, which wanted to also provide local telephone service)
  - When CLECs complained to the FCC that Verizon was failing to deal with them as required by the Telecommunications Act, the FCC opened an investigation, which resulted in a consent decree that imposed financial penalties and remediation measures on Verizon
- Complaint
  - Trinko, a local telephone service customer of AT&T, filed a class action against Verizon alleging that Verizon had dealt with CLECs in violation of its statutory duty to deal to discourage customers from becoming customers of CLECs and maintain its local telephone service monopoly in violation of Section 2 of the Sherman Act.
- District court: Dismissed complaint on the pleadings
  - Failure to allege an exclusionary act within the meaning of Section 2
    - The Telecommunication Act imposes a regulatory duty to deal enforceable by the FCC, but not an antirust duty to deal

[1] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004).

Verizon Comm'c'ns Inc. v. Trinko

- Second Circuit: Reversed and reinstated antitrust claim
  - Trinko sufficiently alleged anticompetitively exclusionary conduct under two distinct theories
  - Essential facilities
    - Independently of the requirements of the Telecommunications Act, a monopolist has a duty to make its essential facilities available to competitors on reasonable terms
      - Citing Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 601 (1985)
    - Here, the complaint alleged that—
      - Verizon's network is an "essential facility" to which a communication must have access in order to compete, and
      - Verizon failed to grant reasonable access to its competitor AT&T to the Verizon network
  - Monopoly leveraging
    - Second Circuit recognizes monopoly leveraging as a Section 2 violation when the defendant—
      1. possesses monopoly power in one market;
      2. uses that power to gain a competitive advantage in another distinct market; and
      - causes injury by such anticompetitive conduct
    - Here, the complaint alleged that—
      - Verizon has monopoly power over a wholesale market in which it sells access to the local loop to telecommunications carriers
      - Verizon used that power to gain a competitive advantage in a retail market in which telecommunications carriers sell local phone service to consumers
      - Trinko, as a local telephone service customers, was injured by the anticompetitive conduct

Verizon Commc'ns Inc. v. Trinko

- Supreme Court: Reversed (9-0)
  - Scalia (for nine members)
    - *Rule*: A refusal to deal is an exclusionary act for the purpose of Section 2 only if the refusal violates an antitrust duty to deal
    - The Telecommunications Act does not create an *antitrust* duty to deal
      - Congress can create an antitrust duty to deal
      - But it did not do so in the Telecommunications Act
        - The creation of any such duty should be clear in the statute
        - The Telecommunications Act contained the following savings clause, which is inconsistent with the Act creating an antitrust duty to deal:

> [N]othing in this Act or the amendments made by this Act shall be construed to modify, impair, or supersede the applicability of any of the antitrust laws.

    - There is no "essential facility" duty to deal in this case
      - "*Aspen Skiing* is at or near the outer boundary of § 2 liability."[1]
      - Distinguishable here
        - *Aspen* involved the unilateral termination of a voluntary and profitable course of dealing and Ski Co.'s "unwillingness to renew the ticket even if compensated at the retail price revealed a distinctly anticompetitive bent"[2]
        - The complaint here does not allege that Verizon voluntarily engaged in a course of dealing with its rivals or would ever have done so absent statutory compulsion
      - The Telecommunications Act's extensive provisions for access and FCC enforcement makes judicial enforcement under the antitrust laws unnecessary and inappropriate

[1] *Trinko*, 540 U.S. at 409. [2] *Id*.

Verizon Commc’ns Inc. v. Trinko

- Supreme Court: Reversed (9-0)
  - Scalia (for nine members)
    - The Second Circuit’s monopoly leveraging theory fails as a matter of law:

> The Court of Appeals also thought that respondent's complaint might state a claim under a “monopoly leveraging” theory (a theory barely discussed by respondent, see Brief for Respondent 24, n.10). We disagree. To the extent the Court of Appeals dispensed with a requirement that there be a “dangerous probability of success” in monopolizing a second market, it erred, Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993). In any event, leveraging presupposes anticompetitive conduct, which in this case could only be the refusal-to-deal claim we have rejected.[1]

[1] *Trinko*, 540 U.S. at 415 n.4.

Apple iPod Antitrust Litigation

- Background
  - 2003: Apples launches iTunes music store—Designed as a semi-closed system
    - Record labels required Apple to have strict DRM (“FairPlay”) to guard against piracy
  - July 2004: RealNetworks announced Harmony technology
    - Allows RN music to be played on iPod
  - October 2004: Apple releases iTunes 4.7, which employed a new encryption method and ended the operability of RN music on iPods
  - September 2006: Apple releases iTunes 7.0
    - Prevented 3P applications (like RN’s Jukebox”) from placing music (“syncing”) on the iPod
    - Ostensibly to prevent corruption of iPod database
  - January 2009: Apple announces that it has reached agreement with labels to eliminate DRM (presumably accomplished by March 2009)
- Class action complaint filed in January 2005

Apple iPod Antitrust Litigation

- District court: May 19, 2001 SJ decision
  - iTunes 4.7 was a genuine product improvement required by the labels → design change is not an exclusionary act even if it excluded RN music from the iPod
  - Apple had no duty to license FairPlay to RN → refusal to license was not exclusionary
  - Denied summary judgment relating to claims on the introduction of iTunes 7.0 (September 2006)
    - Genuine issue of whether iTunes was actually designed to prevent corruption as opposed to simply preventing 3P applications from loading music onto an iPod
- District court: September 26, 2014 decision
  - Denied Apple's combined motion for summary judgment and Daubert motion
  - Plaintiff's theory on impact—overcharge on iPods
    - iTunes 7.0 made demand for iPods less elastic and so enable Apple to raise prices
      - Customers buy more from iTunes store
      - Cannot play iTunes music on alternative players (increased switching costs)
      - Makes them less likely to switch
      - ALSO: Reduced demand for 3P music, which reduced demand for 3P players
    - Key on Daubert: Noll damages number get presented to jury
      - Raised iPod prices to consumers by 7.45%, or $16.32 ($195 million for class)
      - Raised iPod prices to resellers by 2.38% ($149 million to reseller class members)
- Jury
  - Verdict for Apple—found that iTunes 7.0 was a genuine product improvement
    - Ended litigation, since the Ninth Circuit does not balance product improvements against competitive harms