App Store Opinion Returns Antitrust Enforcement To Its Roots

By **Lauren Weinstein**

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Congress made clear when it enacted the Sherman Act in 1890 that the federal antitrust enforcement regime relies on private enforcement actions — civil lawsuits seeking damages — to punish and deter anti-competitive activity. But there are limits on those lawsuits and, particularly, on who may bring them.

The "direct purchaser" rule, announced in Illinois Brick Co. v. Illinois,[1] is among those limitations: It prevents parties who have not transacted directly with the defendant from suing for damages under the federal antitrust laws. Suits seeking "pass-through" damages — i.e., damages that a party further up the distribution chain incurred and passed down to the would-be plaintiff — are prohibited.

Over the years, some courts narrowed Illinois Brick's reach by recognizing exceptions to the direct purchaser rule. Other courts, however, expanded the doctrine, further limiting which parties may bring private antitrust suits. This term, in Apple v. Pepper[2] the U.S. Supreme Court reined in the decades-old direct purchaser rule and reinforced the importance of private antitrust enforcement in the process.

Thirty years after the court decided Illinois Brick, Apple began selling iPhones. Not long after, Apple opened the App Store, a digital marketplace through which Apple sells "apps" — software applications that are by and large developed by third parties and that allow iPhone users to do all manner of things with their devices, including stream TV shows, track fitness and read the news (maybe even read this article). Apple uses its proprietary technology and licensing to ensure that iPhone users may download apps only from the App Store.

In 2011, four iPhone users filed a putative class action under the federal antitrust laws seeking damages for Apple's alleged monopolization of the iPhone app market. Apple moved to dismiss the complaint, arguing that Illinois Brick barred the plaintiffs' suit. The consumer class, Apple argued, consisted of indirect purchasers because, although the iPhone users may have transacted directly with Apple through the App Store, they were really suing on a pass-through theory of damages.

The third-party app developers, Apple explained, were the ones who set the apps' prices. Apple simply kept 30% of the sales price. To the extent consumers had overpaid, Apple argued, it was because of the pricing decisions app developers had made and passed on to the iPhone users. The district court agreed with Apple and granted the motion to dismiss.

The U.S. Court of Appeals for the Ninth Circuit reversed, ruling that the suit should move forward. The key question, the Ninth Circuit explained, was whether Apple functioned as an app distributor that transacted directly with customers through the App Store. Apple had argued that it was not selling apps — and for that reason it was not an app distributor — but that it was selling software distribution services to app developers. Therefore, if anyone had standing to complain about Apple's monopolization of app distribution services, it was the app developers.

The Ninth Circuit rejected that explanation of Apple's role, holding that even if Apple sold distribution services to app developers, it also sold apps to customers through the App

Store. The court expressly did not rest its conclusion on the fact that the consumers paid the App Store directly because such a formalistic understanding of Illinois Brick would allow Apple to escape liability "simply by tinkering with the order in which digital banking data zips through cyberspace during a sales transaction."

The Supreme Court affirmed. Rather than focus on whether Apple was a distributor or manufacturer or producer, the Supreme Court focused on Illinois Brick's bright-line rule that those who purchase goods directly from an alleged monopolist may sue for damages under the federal antitrust laws. Because the consumers had bought apps directly from Apple through the App Store, they were direct purchasers and could bring a damages suit under the federal antitrust laws.

The Supreme Court, like the Ninth Circuit, rejected Apple's argument that because the app developers set the price for apps, consumers were indirect purchasers seeking pass-through damages. The court explained that — in addition to being contrary to the text of the Sherman and Clayton Acts and to Illinois Brick's holding — Apple's proposed "who sets the price" rule was contrary to the consumer protection rationale of the federal antitrust laws.

Looking at who sets the price for a transaction to determine whether a plaintiff may sue, the court explained, would "provide a road map" for alleged monopolists to evade liability. Instead of purchasing goods from a supplier and selling those goods to consumers at a markup, monopolistic retailers could instead acquire (without purchasing) goods from a supplier and sell them to consumers at a price set by the supplier, sharing a portion of that final purchase price with the supplier. The retailer would be insulated from a consumer antitrust suit because it did not set the price. And it likely would not face liability from the supplier because there would be no economic incentive for the supplier to risk its relationship with the monopolistic retailer, particularly where the retailer is sharing with the supplier a portion of the supracompetitive price paid by the consumers. The court refused to embrace a rule that would allow companies to escape liability through clever transaction structuring.

Of course, the court's ruling did not go as far as it could have. A group of 30 states and Washington, D.C., submitted an amicus brief in support of the plaintiff-respondents arguing that Illinois Brick should be overturned. Neither side had urged the court to revisit that precedent, and the court had not granted cert on the question. As a result, overruling Illinois Brick was an unlikely outcome. The court ultimately did not take the bait. In a footnote, the court explained that it had no occasion to consider the arguments for overruling the decision because of its ruling in favor of the plaintiffs. The court could consider overruling Illinois Brick in another case, but nothing in the majority opinion suggests that it is likely to do so.

Instead of tossing out a decades-old precedent, the court returned the decision to its roots. By emphasizing that extraneous factors like who sets the price in a transaction are irrelevant to whether a party is a direct purchaser under Illinois Brick, the court reined in a rule that had begun to expand beyond its doctrinal underpinnings and that threatened the ability of consumers to serve their critical role as private enforcers of the federal antitrust laws.

In its concluding paragraph, the court made clear that Illinois Brick should not serve as an obstacle to private enforcement of the antitrust laws. To the contrary, the court emphasized that its decision was guided by the consumer protection rationale that has been the bedrock of the federal antitrust laws for over a century.

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Disclosure: The author served as counsel of record for 18 antitrust scholars supporting respondents in Apple v. Pepper.

[1] Illinois Brick Co. v. Illinois, 431 U.S. 720 (1977)

[2] Apple v. Pepper (No. 17-204)