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Report from Washington

Supreme Court Holds that iPhone Owners Have Federal Antitrust Standing to Sue Apple for Monopolization of the iPhone App Market under the *Illinois Brick* Doctrine

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Introduction

On May 13, 2019, the Supreme Court in *Apple v. Pepper*, No. 17-204, held that iPhone app purchasers have standing to sue Apple for allegedly monopolizing the market for iPhone apps. A 5-4 justice majority affirmed the Ninth Circuit's decision that iPhone owners can sue Apple for violations of federal antitrust laws, notwithstanding *Illinois Brick Co. v. Illinois*' ban on indirect purchaser suits.[1] Apple had argued that iPhone users should be considered indirect purchasers because the prices the consumers pay are set by the app manufactures, not Apple, from whom they make the purchase.[2] In allowing the claims against Apple to move past the pleading stage, the Court disclaimed overturning any part of the *Illinois Brick* doctrine, as it concluded that the factual circumstances of *Apple v. Pepper* fell squarely within the bright-line rule issued by the *Illinois Brick* Court. This decision has the potential to significantly affect private antitrust enforcement in e-commerce and other markets with nontraditional sales channels by allowing the manufacturers of electronic platforms to be subject to antitrust suits even when they have not set the prices of the products sold in their markets. The impact of the decision on more traditional distribution channels remains an open question, and it will be interesting to see whether district courts show any more flexibility in allowing "indirect" suits in a more traditional supply-chain context.

*"*Illinois Brick*, as we read the opinion, was not based on an economic theory about who set the price. Rather,* Illinois Brick *sought to ensure an effective and efficient litigation scheme in antitrust cases."*

— Justice Kavanaugh

[1] 431 U.S. 720 (1977)

[2] Although third-party app developers were the ones who set the price for such apps, the Court observed that Apple did not merely facilitate transactions between the iPhone owners and the app developers. Rather, it was "undisputed that the iPhone owners bought the apps directly from Apple." *Apple*, No. 17-204, at 4.

Background

In 2011, iPhone owners filed a putative class action suit against Apple in the Northern District of California under § 2 of the Sherman Act, alleging that Apple monopolized the market for iPhone apps by charging an above-market commission to app developers and limiting the purchase and sale of iPhone apps to the Apple App Store. Apple moved to dismiss that suit on the ground that the iPhone owners are not "direct purchasers" for purposes of *Illinois Brick*, the Supreme Court's 1977 decision that bars indirect purchasers from bringing private damages suits under § 4 of the Clayton Act. Specifically, Apple argued that Plaintiffs purchase apps from app developers, who independently set the price for such apps and sell them on the App Store in exchange for a 30% commission. Accordingly, Apple argued that Plaintiffs are indirect purchasers in relation to Apple and do not have standing to sue Apple under federal antitrust law.

"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."

— Justice Kavanaugh

The District Court granted Apple's motion to dismiss for lack of antitrust standing, affirming Apple's view that Plaintiffs are indirect purchasers and thus lack standing under *Illinois Brick*. The court reasoned that because app developers set the ultimate price for apps, Plaintiffs' argument rested on a "pass on" theory of harm. The Ninth Circuit reversed, holding that iPhone owners are direct purchasers within the meaning of *Illinois Brick* because they purchase apps directly from Apple on the App Store, and Apple subsequently remits the proceeds from that purchase minus its commission to the app developers.

The Supreme Court granted *certiorari* to resolve a resulting split with the Eighth Circuit, which had previously held that ticket purchasers were indirect purchasers in relation to Ticketmaster despite buying tickets directly from the company on its electronic platform because Ticketmaster's compensation was derived from its contracts with concert venues.[3]

Summary of the Court's Opinion

In an opinion delivered by Justice Kavanaugh and joined by Justices Ginsberg, Breyer, Sotomayor, and Kagan, the Court held that the plain meaning of Clayton Act § 4 and Supreme Court precedent interpreting that provision confer standing on iPhone owners to sue Apple for the monopolization of iPhone apps. The Court boiled the case down to one simple issue: "whether the consumers were 'direct purchasers' from Apple." Because the Court found that they were, it declined to reach the issue of whether the *Illinois Brick* doctrine should be reexamined.

[3] *Campos v. Ticketmaster Corp.*, 140 F. 3d 1166 (8th Cir. 1998).

The Court rejected Apple's position for three reasons. First, the Court wrote that the plain meaning of Clayton Act § 4 and Supreme Court precedent interpreting that decision conflict with Apple's theory of *Illinois Brick*. Writing for the majority, Justice Kavanaugh stated that the *Illinois Brick* doctrine "sought to ensure an effective and efficient litigation scheme in antitrust cases." He wrote that the Court achieved this objective by creating a "bright line" rule that distinguished direct from indirect purchasers and conferred antitrust standing on the former. Because there is no "intermediary" party between Apple and iPhone owners when they purchase iPhone apps, the Court held that Plaintiffs constitute direct purchasers. The Court then engaged in a plain meaning interpretation of Clayton Act § 4, noting that the broad text of that provision showed that "direct purchasers from monopolistic retailers are proper plaintiffs to sue those retailers."

*"*Illinois Brick *is not a get-out-of-court-free card for monopolistic retailers to play any time that a damages calculation might be complicated."*

— Justice Kavanaugh

Second, the Court held that Apple's interpretation of the *Illinois Brick* doctrine "is not persuasive economically or legally" because it would yield illogical results where consumers can sue retailers who derive their compensation from mark-ups but cannot file suit against retailers who derive their compensation through commissions. Indeed, the Court reiterated the Ninth Circuit's ruling that "the distinction between a markup and a commission is immaterial" and wrote that "[i]f a retailer has engaged in unlawful monopolistic conduct that has caused consumers to pay higher-than-competitive prices, it does not matter how the retailer structured its relationship with an upstream manufacturer."

Third, the Court held that Apple's theory of *Illinois Brick* would enable monopolists to circumvent antitrust liability by structuring their contractual relationships with manufacturers so that the manufacturer sets and receives the proceeds of the sale to the consumer even if the retailer collects those proceeds. For instance, the Court noted that under Apple's interpretation of the case, a retailer may simply switch to a commission-based compensation scheme in order to avoid any antitrust liability, even if it charges supra-competitive prices to consumers.

Finally, the Court rejected Apple's arguments that the *Illinois Brick* rationale supports barring suits by the iPhone owners. The *Illinois Brick* Court was motivated in part by its belief that indirect-purchaser suits would: (1) undermine private enforcement of federal antitrust laws; (2) require complex damages calculations; and (3) result in duplicative liability. None of those policy rationales applied to Apple, however. The Court wrote that Apple's argument that downstream app consumers cannot sue because upstream app developers also have the ability to sue Apple contradicts the "goal of private enforcement and consumer protection in antitrust cases." Further, the Court stated that even though apportioning damages may be difficult in this case, "*Illinois Brick* is not a get-out-of-court-

free card for monopolistic retailers to play any time that a damages calculation might be complicated." The Court concluded that while both app consumers and developers could sue Apple under the Sherman Act, these suits would rest on separate theories of harm and thus should both be allowed to proceed.

Written by Justice Gorsuch and joined by Chief Justice Roberts and Justices Thomas and Alito, the dissenting opinion firmly rejected the majority's application of the *Illinois Brick* doctrine to this case, noting that it fundamentally misinterpreted the purpose of the doctrine. The dissent argued that the *Illinois Brick* doctrine rests on traditional principles of proximate cause. According to the dissent, the app developers, not consumers, are direct purchasers as they are contractually obligated to pay Apple a 30% commission for each sale of their apps. As such, the dissent wrote that Plaintiffs' argument relied on the notion that the app developers passed Apple's commission onto consumers by raising prices, so Plaintiffs' theory of harm was too speculative, and Plaintiffs should therefore be classified as indirect purchasers under the spirit of the *Illinois Brick* doctrine. By contrast, Justice Gorsuch wrote that the majority replaced that longstanding interpretation of *Illinois Brick* with a contractual privity test, which triggers all three concerns the *Illinois Brick* Court sought to avoid in rendering its initial decision. The dissent concluded by implying that the majority seemed to disagree with the holding of *Illinois Brick* and should have considered overturning it altogether rather than "whittling it away to a bare formalism."

"Maybe the Court proceeds as it does today because it just disagrees with Illinois Brick. *After all, the Court not only displaces a sensible rule in favor of a senseless one; it also proceeds to question each of* Illinois Brick*'s rationales."*

— Justice Gorsuch

Implications

This decision will likely have a substantial effect on how the lower courts apply the Illinois Brick doctrine in the context of certain e-commerce marketplaces and other nontraditional sales channels. While the Court declined to confront the doctrine's continued viability directly and claimed its ruling derived from a straightforward application of *Illinois Brick* to the facts at hand, courts may now feel compelled to better understand the economic underpinnings of an e-commerce marketplace before dismissing consumer suits for lack of antitrust standing.

The decision potentially opens the door to antitrust suits against similarly situated technology companies that operate platforms on which third parties can market and sell their products. A trade organization that represents such companies filed an *amicus* brief in support of Apple's position while the case was pending before the Supreme Court, and

expressed disappointment with the Court's decision because it feared that it would expose their businesses to a range of new costly antitrust litigation and potentially harm app developers themselves. [4]

[4] Tony Romm & Robert Barnes, *Supreme Court Rules against Apple, Allowing Lawsuit Targeting App Store to Proceed*, WASH. POST (May 13, 2019), https://www.washingtonpost.com/technology/2019/05/13/supreme-court-rules-against-apple-allowing-lawsuit-targeting-app-store-proceed/?utm_term=.9369ee5fa752.

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