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Apple urges US Supreme Court to reject app antitrust claims

Should Apple be subject to antitrust claims by consumers for the terms and commissions it imposes on developers? During the next term of the US Supreme Court, the Court will hear the case of *Apple Inc. v. Pepper*¹, which could have broad implications for e-commerce platforms that offer goods and services for third parties. While the case focuses on Apple's iPhone application ('app') platform, the Supreme Court's decision in this case could affect numerous online marketplaces such as Amazon, Google, eBay, Stubhub, and Facebook's 'Marketplace,' by determining which parties have proper standing to bring antitrust claims when platforms offer others' goods and services. The case also calls into question the modern day application of Supreme Court precedent dating back to 1977, and whether the Ninth Circuit Court of Appeals' ('the Ninth Circuit') ruling in this case rejecting the 1977 Supreme Court doctrine should be overturned, as Michelle Cohen, Member at Ifrah Law PLLC and Member of the *Digital Business Lawyer* Editorial Board, explains.

Background

Robert Pepper and other plaintiffs bought Apple iPhones and apps and filed a purported class action lawsuit seeking to represent a class of similarly situated people in the US who purchased an iPhone app. The plaintiffs assert claims under federal antitrust laws. Specifically, plaintiffs brought suit under Section 2 of the Sherman Antitrust Act of 1890², which makes it unlawful for any person to 'monopolize or attempt to monopolize, or combine or conspire or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States[...].' Section 4 of the Clayton Act of 1914³, in turn, permits civil suits for treble damages for any person injured through acts forbidden under the antitrust laws. Section 4 also permits the recovery of attorney's fees. The plaintiffs claim that Apple monopolised the distribution of iPhone apps, and that the 30% commissions that Apple charges to app developers ultimately inflate the prices consumers pay for the apps.

The potential damages in this case, if allowed to proceed, could be enormous. The Apple App Store offers over 2 million apps. According to a recent article, for calendar year 2017, the App Store (just over ten years old), generated approximately \$11.4 billion in revenue, representing almost 5% of the company's projected \$237 billion in total revenue⁴. According to Apple, during 2017,

developers earned \$26.5 billion, a 30% increase over 2017 developer earnings⁵.

The key question before the Supreme Court is whether the plaintiff consumers can bring a suit under the antitrust law when Apple's practices are directed at the developers. Apple sets terms and conditions for developers' access to the iPhone platform. Apple establishes the commission structure it charges developers. However, Apple does not set the fees for the apps, the app developers set the fees (if any, many apps are free for initial download).

The Supreme Court's *Illinois Brick* case: only direct purchasers can bring antitrust claims

Under the seminal case of *Illinois Brick Co. v. Illinois*⁶ ('*Illinois Brick*'), the Supreme Court held in 1977 that the only parties who can recover damages for an antitrust violation are those who purchased the product or service directly from the alleged antitrust violator. Indirect purchasers, for instance, customers of the party who suffered the antitrust injury, are barred from recovery. There are several reasons for this limitation. Firstly, the Supreme Court sought to prevent multiple recoveries for the same actions. Secondly, the Supreme Court determined it would be difficult to ascertain which parties had proper standing to bring claims if one has to keep ascertaining the 'chain' of possible

affected parties. Thirdly, the Supreme Court reasoned it would be difficult to ascertain the amount of each party's 'flow down' damages. All of these uncertainties could actually defeat the purpose of the private claim of action and treble damages provision, since the uncertainty could discourage lawsuits seeking to challenge antitrust violations. As the Supreme Court concluded in *Illinois Brick*, "[a]dded to the uncertainty of how much of an overcharge could be established at trial would be the uncertainty of how that overcharge would be apportioned among the various plaintiffs. This additional uncertainty would further reduce the incentive to sue. The combination of increasing the costs and diffusing the benefits of bringing a treble damages action could seriously impair this important weapon of antitrust enforcement⁷."

The *Illinois Brick* case involved price-fixing claims associated with concrete manufacturers' sale of concrete brick to masonry contractors. The contractors would then use the brick to complete jobs for general contractors who hired the masonry contractors. The contractors used some of this brick to construct government buildings. The State of Illinois sued, claiming it was a victim of pricing-fixing since the contractors utilised the brick to construct state buildings. The Supreme Court rejected the State's claims, holding that it was

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only an indirect customer and that such indirect buyers could not seek antitrust remedies against the manufacturers. Thus, ‘downstream’ parties may not seek ‘pass-through’ damages. In other words, if the sugar manufacturer violated the antitrust law when it sold sugar to the distributor, who sold to the bakery, who sold the cupcakes to me, I cannot sue the manufacturer for my damages, nor can the bakery. Under *Illinois Brick*, only the distributor can sue the manufacturer.

The Ninth Circuit throws a brick at *Illinois Brick* and rejects the Eighth Circuit *Campos*⁹ case

One might ask, how does the *Illinois Brick* principle apply in an emerging field such as e-commerce marketplaces? In *Illinois Brick*, the manufacturer did not interact with the indirect purchaser/ plaintiff. However, many electronic marketplaces (including the App Store) do interact with purchasers. For instance, on eBay, purchasers search for products through the platform, can bid or purchase through the platform, and ultimately the platform facilitates the completion of the transaction. Similarly, Apple’s App Store allows users to search and download apps and delivers the apps to users. Online ticket brokers allow venues and other third parties to list available tickets where third parties can purchase tickets to sporting, music, and other cultural events. The online marketplaces sometimes also charge convenience or service fees to the purchasers.

In *Apple v. Pepper*, the district court dismissed the antitrust action under the *Illinois Brick* precedent. The district court held that the consumer plaintiffs sought pass-through damages since they based their monopolisation claims on the services Apple offers and the charges it imposes on developers. On appeal, the Ninth Circuit took an unusual turn. It reversed the district court. The Ninth Circuit held that the consumers

qualify as direct purchasers of iPhone apps from Apple under *Illinois Brick* and therefore had standing to sue. The Ninth Circuit concluded (without much analysis) that “Apple is a distributor of the iPhone apps, selling them directly to purchasers through its App Store. Because Apple is a distributor, Plaintiffs have standing under *Illinois Brick* to sue Apple for allegedly monopolizing and attempting to monopolize the sale of iPhone apps⁸.” The Ninth Circuit rejected Apple’s arguments that Apple does not set the prices of the apps and that Apple does not own the apps but, rather only makes them available through the App Store.

The Ninth Circuit’s decision represents a significant shift in an appellate court’s treatment of *Illinois Brick*. In fact, it contravenes an analogous case in the Eighth Circuit Court of Appeals (the ‘Eighth Circuit’) involving Ticketmaster.

In *Campos v. Ticketmaster Corp.* (*‘Campos’*), the Eighth Circuit held that concert ticket purchasers could not bring a claim against Ticketmaster alleging that Ticketmaster was a “monopoly supplier of ticket distribution or ticket delivery service to large-scale popular music shows¹⁰.” The plaintiffs in *Campos* based their claims on the fees set in contracts between Ticketmaster and the venues. Ticketmaster (like Apple) acted as a distributor to the public of the venues’ tickets. Ticketmaster interacted directly with the consumer plaintiffs. Consumers paid the ticket prices and added fees to Ticketmaster. The Ticketmaster fees were actually identified as fees imposed by Ticketmaster. The Eighth Circuit applied *Illinois Brick* and rejected the claims, because the antitrust claim was based on a pass-through theory: i.e., that the venues passed Ticketmaster’s fees in setting ticket prices on to consumers. In *Campos* the Eighth Circuit concluded that determining how much of Ticketmaster’s alleged illegal fees would require a court

to conduct a pass-through determination that *Illinois Brick* specifically forbade¹¹.

In the *Apple v. Pepper* case, the Supreme Court requested the views of the US’ Solicitor General (on behalf of the US). In an *amicus curiae* brief, the Solicitor General urged the Supreme Court to grant *certiorari* due to the circuit conflict created by the Ninth Circuit’s interpretation of *Illinois Brick* and its rejection of the *Campos* precedent. The Solicitor General explained that the consumers’ claims should be barred because they sought recovery on a ‘pass through’ theory: when, in fact, the prices for apps are set by third party developers, not Apple¹².

Next steps

The Supreme Court will hear arguments in the *Apple v. Pepper* case during the next term, which begins in October 2018. Unless the Supreme Court is ready to reject *Illinois Brick* or limit it as applied to electronic marketplaces, I would expect that Apple prevails. The Ninth Circuit essentially created its own law in allowing consumers’ claims to proceed, particularly with the *Campos* precedent. Ticketmaster even added on fees it charged consumers, which Apple does not. There is a distinction between an electronic marketplace that offers goods and services and facilitates transactions versus others that offer their own products and set the terms for those goods and services (e.g., Amazon selling third party goods versus Amazon selling ‘Amazon basic’ products such as batteries). Going forward, courts will need to review how the products are offered, and who sets the prices and the terms and conditions. Here, Apple’s practices may be subject to challenge by the app developers, but *Illinois Brick*, *Campos*, and their progeny lead to the conclusion that the Supreme Court should reject the consumers’ claims and reverse the Ninth Circuit decision.

1. 17-204 (cert. granted 18 June 2018).

2. 15 U.S.C. § 2.

3. 15 U.S.C. § 15(a).

4. Chuck Jones, Apple’s App Store Generated Over \$11 Billion in Revenue For The Company Last Year, FORBES, 6 January 2018, <https://www.forbes.com/sites/chuckjones/2018/01/06/apples-app-store-generated-over-11-billion-in-revenue->

[for-the-company-last-year/#6030ab0b6613](https://www.forbes.com/sites/chuckjones/2018/01/06/apples-app-store-generated-over-11-billion-in-revenue-for-the-company-last-year/#6030ab0b6613).

5. Press release, Apple, Inc., App Store kicks off 2018 with record-breaking holiday season (4 January 2018), <https://www.apple.com/newsroom/2018/01/app-store-kicks-off-2018-with-record-breaking-holiday-season/>.

6. 431 U.S. 720 (1977).

7. 431 U.S. at 745.

8. 846 F.3d 313, 324 (9th Cir. 2017)

9. 140 F.3d 1166 (8th Cir. 1998), cert. denied, 525 U.S. 1102 (1999).

10. 140 F.3d at 1168.

11. 140 F.3d at 1171-72.

12. Brief for the United States as *amicus curiae* at 13, *Apple Inc. v. Pepper*, et al., 8 May 2018 (No. 17-204)