



## Antitrust/Financial Services & Products ADVISORY ■

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### U.S. Supreme Court Creates Framework for Analyzing Antitrust Claims for Two-Sided Markets

On June 25, 2018, the U.S. Supreme Court held that credit card services provider American Express's ("AmEx") rules that prohibit merchants from "steering" cardholders to use other credit cards do not violate federal antitrust laws. The decision in *Ohio v. American Express Co.*, No. 16-1454, is notable because it outlines a new approach to analyzing potential antitrust issues in "two-sided" markets (here, credit card services provided to merchants who accepted cards and to consumers who held them). This decision may have broader implications beyond the payment industry and will likely impact antitrust litigation and government enforcement in other industries where intermediaries connect groups of buyers and sellers, including social networking, search engines, and ridesharing.

#### **Background**

In 2010, the U.S. Department of Justice (DOJ) and attorneys general from 18 states brought an antitrust lawsuit against AmEx in the Eastern District of New York to prevent the credit card provider from enforcing "antisteering" rules in its merchant agreements. These rules prevent merchants from using pricing discounts or other incentives to persuade customers to use other credit cards that charge merchants lower transaction fees than those charged by AmEx. The DOJ and the states challenged the rules as being anticompetitive and harmful to merchants because the rules allegedly distort competition and insulate AmEx from price competition from Visa, Mastercard, and Discover.<sup>1</sup>

After a seven-week bench trial, the district court found that AmEx's antisteering rules violated federal antitrust law. The lower court found that the relevant product market was network services for general-purpose credit cards provided to merchants and held that the services provided to cardholders was a separate and distinguishable market. When evaluating whether the government had met its initial burden to show an anticompetitive effect from the antisteering rules, the district court focused solely on the merchant side of the market and found that the rules result in higher fees paid by merchants.

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<sup>1</sup> Similar lawsuits challenging antisteering provisions were filed in 2010 against Visa and Mastercard. Those companies settled with the plaintiffs shortly after those challenges were filed, agreeing to remove the antisteering provisions from their merchant agreements.

AmEx appealed to the Second Circuit, which reversed the lower court's decision, holding that it was an error to analyze anticompetitive effects by evaluating only one-half of a two-sided market. The Second Circuit found that AmEx's business model, which involves more generous benefits to cardholders, increases rather than decreases competition in the credit card industry and provides value to consumers that was not recognized by the district court. Following the loss in the Second Circuit, the state attorneys general successfully petitioned the U.S. Supreme Court to grant certiorari.<sup>2</sup>

## The Supreme Court's Opinion

The Supreme Court's 5–4 decision split along traditional ideological lines, with Justice Clarence Thomas authoring the majority opinion. The decision discussed the nature of two-sided platforms and how "indirect network effects" can make them less susceptible to anticompetitive effects. The majority held that in two-sided transaction platforms—like credit card networks—a network service provider cannot raise prices on one side of the platform (i.e., by increasing transaction fees on merchants) without risking a feedback loop of declining demand across both sides of the platform. Because each credit card transaction requires one merchant and one consumer, the majority held that the interconnected pricing and demand for credit card transactions creates a check on supracompetitive pricing by the network provider and promotes competition across credit card network providers.

The Court held that in the context of this two-sided market, the DOJ and the state AGs had failed to meet their initial burden under the fact-intensive "rule of reason" to prove anticompetitive effects from AmEx's antisteering rules. The Court found that proof of increased merchant fees charged by AmEx was insufficient to establish an antitrust violation without also weighing the effect the steering provisions had on cardholders.

The Court's decision provided new guidance for courts weighing how to apply the "rule of reason" test to two-sided platforms. The rule of reason is the standard commonly used to evaluate antitrust claims other than per se violations such as price fixing. The majority held that markets should be defined by the "commercial realities" of the relevant industry—combining markets for different products or services into a single market if that reflects the reality in which businesses and consumers operate. While the Court was clear that credit card networks are two-sided markets, the majority was careful to limit its analysis to those markets where indirect network effects across both sides of a platform are "major," rather than "minor." In doing so, the Court distinguished a prior decision that looked only at the impact of a newspaper's policies on the market for newspaper advertising, despite newspapers operating as two-sided platforms that require both readers and advertisers to thrive.

The dissent, written by Justice Stephen Breyer, argued that the majority's decision was inconsistent with long-standing antitrust precedent and ignored detailed factual findings from the trial court. The dissent contended that the majority falsely conflated two separate markets and argued that the introduction of "two-sided markets" into traditional rule of reason analysis will produce absurd results as courts grapple with where to draw the line when an increasing number of antitrust defendants contend that their businesses operate as two-sided platforms.

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<sup>2</sup> After the Trump Administration took office in 2017, the DOJ declined to petition for certiorari (reasoning that the law regarding two-sided platforms was too underdeveloped for Supreme Court review) but ultimately argued against AmEx before the Supreme Court in briefing and oral argument.

## Takeaways

The Court's *American Express* decision may have long-lasting effects on the analysis of two-sided platforms under the rule of reason, which is the primary test that courts use to assess alleged antitrust violations under Section 1 of the federal Sherman Act. While the Court provided some guidance on when markets are sufficiently interconnected to constitute a single, two-sided market, that guidance will be thoroughly tested and challenged. Inevitably, antitrust defendants will argue that the commercial realities of their industries dictate that the relevant markets be defined as two-sided, with plaintiffs arguing the opposite and distinguishing *American Express* based on the specific facts at issue in that case. That battle is most likely to be fought in future antitrust litigation regarding Internet services, social networking sites, health care, travel, media, and rideshare platforms. The majority's opinion leaves open the possibility that modern Internet businesses selling advertisements to merchants and providing Internet services to consumers may not be subject to the same analysis as credit card providers. The Court acknowledges that "nontransaction" platforms, like newspapers, compete with different types of platforms (e.g., television networks) for advertisers but not necessarily for consumers.

It remains to be seen whether this same logic could be used to differentiate social media platforms and Internet search providers that operate as two-sided transactional platforms. In fact, the head of the Justice Department's Antitrust Division—who only two weeks earlier was handed a defeat by a district court judge in the division's challenge to the AT&T and Time Warner merger that involved issues involving vertical consolidation and technology—[has already said](#) the decision will not necessarily prevent enforcement challenges to the conduct of leading technology platforms. And the Federal Trade Commission recently [announced an in-depth series of hearings](#) beginning this fall examining antitrust and consumer protection issues on topics that include platform businesses and the technology industry. Regardless, the Court's decision creates a significant new obstacle for antitrust plaintiffs seeking to challenge vertical restraints in industries that arguably operate as two-sided platforms. Litigants should expect additional discovery and scrutiny into market definition in vertical restraint cases as defendants seek to shield themselves with the two-sided platform approach outlined by the Court.

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