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Antitrust ADVISORY ■

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U.S. Supreme Court Clarifies the Direct-Purchaser Rule, Allows App Purchasers to Proceed Against Apple

On May 13, 2019, the U.S. Supreme Court issued a 5–4 decision that will increase the likelihood that e-commerce giants will face antitrust consumer class actions on a variety of theories, even though the Court did not overrule—or, in its view, change—any prior precedent. In *Apple v. Pepper*, the Court held that consumers who bought apps from Apple's App Store were "direct purchasers" with standing to sue Apple over allegedly monopolistic practices, rejecting Apple's argument that the consumers' claims should be barred because independent app developers set the prices charged by Apple for their apps. The Court characterized its holding as applying rather than departing from "the straightforward rule of *Illinois Brick*" that restricts standing to bring a Sherman Act claim for monetary damages to direct purchasers. The opinion makes clear that the direct-purchaser rule will be applied in its most literal sense, and all direct purchasers from a party alleged to have engaged in anticompetitive conduct can sue under the Sherman Act.

Case Background

Apple's App Store is the exclusive authorized platform for the purchase and sale of apps developed for iPhones and other Apple devices. Generally speaking, Apple does not create the apps sold in the App Store. Rather, independent developers create the apps, and Apple's rules for the App Store allow the independent developers to set the price that consumers pay for their apps—provided that the price ends in 99 cents. When a consumer buys an app from the App Store, the consumer directly pays Apple the full price set by the developer, Apple keeps a 30% commission, and Apple pays the developer the remaining 70% of the purchase price.

In 2011, a putative class of consumers brought suit against Apple under Section 2 of the Sherman Act, alleging that Apple has monopolized the market for the sale of iPhone apps, that the 30% commission charged by Apple is higher than it would be in a competitive market, and that plaintiffs paid more for iPhone apps as a result. In 2013, Apple moved to dismiss the plaintiffs' case on the ground that the consumers were not direct purchasers under the Supreme Court's long-established *Illinois Brick* rule that limits federal antitrust standing to persons who purchased products or services directly from the party that committed the antitrust violation. The district court granted Apple's motion. The district court reasoned that, even though consumers paid Apple directly, the only proper plaintiff in a case would be app developers because the developers set the price, and Apple's 30% commission was taken out of the payment that would otherwise go to them. In the district court's view, the plaintiffs were relying on a "pass-on" theory similar to the theories rejected in *Illinois Brick* and other cases that articulated the direct-purchaser rule.

In 2017, the Ninth Circuit Court of Appeals reversed. The Ninth Circuit cast the case as a straightforward application of Supreme Court precedent. Apple was the company that allegedly committed anticompetitive conduct. Consumers purchased directly from Apple. Therefore, consumers were direct purchasers with standing to sue.

The Supreme Court's Ruling

The Supreme Court affirmed the Ninth Circuit, holding that the consumer plaintiffs were direct purchasers from Apple and therefore had standing to bring a Sherman Act claim. The Court characterized its ruling as a "straightforward" application of *Illinois Brick* and related precedent regarding the direct-purchaser rule: "The iPhone owners purchase apps directly from the retailer Apple, who is the alleged antitrust violator.… The absence of an intermediary is dispositive." The Court ruled that this conclusion was dictated by precedent, particularly read in the context of the text of the Sherman Act, which broadly provides that "any person" injured by prohibited anticompetitive conduct can bring a claim.

While the Court's holding was based on precedent applied in the context of the broad statutory text, the Court also addressed the economic and policy arguments raised by Apple and the four-Justice dissent. The Court rejected the notion that the *Illinois Brick* direct-purchaser rule was "based on an economic theory about who set the price," and the Court instead embraced the most literal meaning of the direct-purchaser rule, which the Court repeatedly characterized as a "bright-line rule."

The Court addressed the economics of the transaction by rejecting the argument that, because Apple took the 30% commission out of a payment that would otherwise go to app developers, the app developers were the only parties who could have been directly harmed. In doing so, the Court recognized that Apple's allegedly monopolistic conduct can cause analytically distinct and nonduplicative harm to consumer purchasers and app developer sellers. Specifically, the Court observed that consumers can recover an overcharge if they can prove that Apple's allegedly monopolistic practices caused the consumers to pay more for the products than they would have paid in a competitive market. App developers, in contrast, could bring monopsony claims against Apple and seek lost profits if they can prove that they earned less than they would have earned in a competitive market.

While the Court acknowledged that both of these categories of damages could come out of Apple's 30% commission, the Court observed that "[t]his is not a case where multiple parties at different levels of a distribution chain are trying to recover the same passed-through overcharge initially levied by the manufacturer at the top of the chain." Rather, potential plaintiffs at different distribution levels (i.e., app developer "manufacturers" and consumer purchasers) can each suffer direct harm from a monopolistic retailer. To use a simple example to illustrate the Court's reasoning, if app developers could sell directly to consumers and the price for an app in a fully competitive market would be $0.89—rather than $0.99 in the App Store—then the consumer's direct damages would be the $0.10 overcharge, and the app developer's direct damages would be the $0.20 difference in profits between the competitive sales price and the current $0.99 price with Apple's allegedly anticompetitive 30% commission taken out (i.e., the developer would currently earn approximately $0.69 per sale post-commission rather than the full $0.89 in this illustration).

Finally, the Court rejected Apple's "who set the price" argument as one that would elevate form over substance by distinguishing between economically identical sales based on the manner Apple structures its relationship with its upstream suppliers (the app developers). Specifically, Apple's theory would acknowledge liability to consumers if a retailer like Apple purchased a product from an upstream supplier outright and then resold it at a monopolistic markup, but Apple's theory would avoid liability if the same retailer made the same sale on an agency or commission basis—even if the markup by the retailer and the price paid by the consumer were exactly the same. The Court

concluded that, "if accepted, Apple's theory would provide a roadmap for monopolistic retailers to structure transactions with manufacturers or suppliers so as to evade antitrust claims by consumers and thereby thwart effective antitrust enforcement."

Conclusions and Implications

1. For all the press that this case has received, the Court employed an approach consistent with the common understanding that a direct purchaser is one who pays to buy a product from another—even in cases where the economics of the market or transaction might be complex. By rejecting arguments that try to look under the hood of a transaction to determine whether a plaintiff's theory depends on "pass-on" or other similar economic arguments, the Court's ruling embraces what appears to be a simple and straightforward rule that should be easy to apply. That said, the clarity and directness of the decision (not to mention its language supportive of antitrust enforcement) will encourage additional antitrust suits against e-commerce giants who sell directly to the public, regardless of how the sellers structure their relationships with upstream suppliers. Consumer claims in this space—including the claims against Apple in this case—can still fail on the merits for a variety of reasons, but *Illinois Brick* has been essentially removed as a potential bar at the pleadings stage.

2. While the Supreme Court did not offer an opinion on this issue, it appears that the *Illinois Brick* direct-purchaser rule will not be abolished any time soon. Many states have passed "*Illinois Brick* repealer" statutes that allow indirect purchasers to sue alleged antitrust violators under state antitrust laws. In this case, various amici, including 30 states and the District of Columbia, asked the Court to likewise overrule the Court-created *Illinois Brick* rule and allow indirect purchasers to sue under the Sherman Act. The Court declined that invitation, in part because neither of the parties requested or litigated that issue in this case. Notably, the Court referred to the direct-purchaser rule as a "bright-line" rule seven times in the 14-page opinion, but some of the commentary in the dissent about the need to focus on proximate causation and the substance of transactions could become fodder for another challenge to the judicial doctrine in *Illinois Brick*.

3. The Court expressly recognized the possibility that plaintiffs at different levels of a supply chain can bring valid claims against an alleged monopolist (or cartelist) based on the same conduct. If an alleged antitrust violator is not at the very top of the supply chain, it may become increasingly common to see both purchasers and suppliers simultaneously bring claims that are based on the same conduct but assert different theories of direct harm.

4. The manner the Court split in this case could signal a certain amount of future unpredictability in the area of antitrust enforcement, which has seen a number of pro-defendant rulings in the Roberts era. Justice Kavanaugh wrote for the Court and was joined by Justices Ginsburg, Breyer, Sotomayor, and Kagan. The Court's other newest member, Justice Gorsuch, authored a dissent joined by Chief Justice Roberts and Justices Alito and Thomas. This split continues what may be an emerging trend in which Justices Kavanaugh and Gorsuch have ended up on opposite sides of issues, with one or the other of them joining the same four Justices who joined Justice Kavanaugh's majority decision in this case.

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