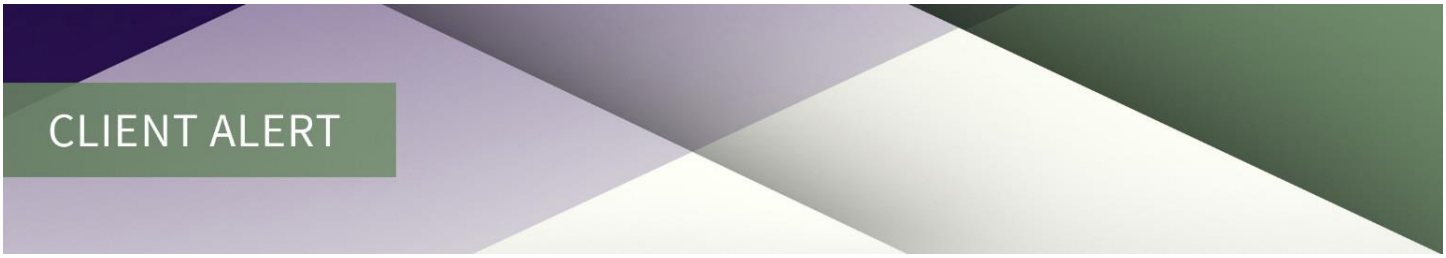


# Apple Antitrust: Contractual Privity Trumps Proximate Cause Under *Illinois Brick*, But Maybe Not Under *Associated General Contractors*?

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In *Apple Inc. v. Pepper*, a 5-4 Supreme Court affirmed the right of app purchasers under the indirect-purchaser rule of *Illinois Brick Co. v. Illinois* to sue Apple, Inc., for monopolizing the retail market for iPhone apps based upon an alleged overcharge levied upon app developers. The discrepancy between the identity of plaintiffs—the app users—and the direct payers of the alleged monopoly overcharge—the app developers—caused much controversy within the antitrust bar as to the application of the *Illinois Brick* indirect-purchaser rule.

Justice Brett Kavanaugh, writing for the majority, resolved that controversy in favor of plaintiffs by interpreting *Illinois Brick* as a rule of contractual privity. Justice Neil Gorsuch, writing for the dissent, argued that *Illinois Brick* rests on principles of proximate cause—that a plaintiff must allege that the defendant proximately caused the plaintiff's antitrust injury. The Kavanaugh-Gorsuch dispute will be assessed by antitrust students for years to come as a classic debate over the proper reading of a dispositive case.

The debate between the *Apple* majority and dissent is also ironic: Although Justice Kavanaugh's privity criterion will govern the application of *Illinois Brick*, Justice Gorsuch's discussion of proximate cause may be cognizable under the Supreme Court's case in *Associated General Contractors of California, Inc. v. California State Council of Carpenters* ("*AGC*"), 459 U.S. 519 (1983), which followed *Illinois Brick* by six years. *AGC* requires courts to consider multiple factors in a standing analysis, including the causal connection between the antitrust violation (in *Apple*, the alleged monopolistic commission charged by Apple to app developers) and the plaintiff's injury (the payment by app users of a

supracompetitive app price due to the overcharge to developers). *Id.* at 540-41. A plaintiff in privity with the defendant thus could have standing under *Illinois Brick* but lose standing under *AGC* due to remote causation.

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Plaintiff-consumers brought their action in the U.S. District Court for the Northern District of California alleging that Apple requires app developers to pay Apple a 30% share of sale proceeds (a commission) to sell their apps as approved for Apple devices through Apple's app store. *In re Apple iPhone Antitrust Litig.*, No.: 11–cv–06714–YGR, 2013 WL 6253147, at *2 (N.D. Cal. 2013). The district court, quoting the Second Amended Complaint, described Apple's 30% commission as "'a *share of* the third party's sales proceeds.'" *Id.* (emphasis in district court opinion). Apple collects the entire payment from the customer and "sells the Apps (or, more recently, licenses for the apps) directly to the customer." *In re Apple iPhone Antitrust Litig.*, 2013 WL 6253147, at *2.

Plaintiffs alleged that the 30% commission charged by Apple was an "obvious monopoly price." *Id.* The district court found that plaintiffs were "indirect purchasers" and thus lacked standing, as the complaint "is fairly read to complain about a fee created by agreement and borne *by the developers* to pay Apple 30% from their own proceeds—an amount which is passed-on to the consumers as part of the purchase price." *Id.* at *6 (emphasis in original).

The Ninth Circuit reversed and remanded, finding that Apple was a "distributor of the iPhone apps, selling them directly to purchasers through its app store." As a contractual matter, the app purchasers entered into a sales or license agreement with Apple, not the developers. *In re Apple iPhone Antitrust Litig.*, 846 F.3d 313, 317 (9th Cir. 2017). The Ninth Circuit thus found that plaintiffs were not indirect purchasers and had standing to sue. *Id.*

The Supreme Court affirmed the Ninth Circuit. Justice Kavanaugh articulated the "bright-line rule" of *Illinois Brick* as prohibiting "indirect purchasers who are two or more steps removed from the antitrust violator in a distribution chain" from suing the violator and permitting only "the immediate buyers from the alleged antitrust violators" to sue. *Apple Inc. v. Pepper*, 139 S.Ct. 1514, 1521 (2019) [hereinafter, "Majority Op."].

The dissent, however, argued that *Illinois Brick* rested on proximate cause: "[A]n antitrust plaintiff [in *Apple*, the app purchasers] can't sue a defendant for overcharging *someone else* [the app developers] who might (or might not) have passed on all (or some) of the overcharge to him." *Apple Inc. v. Pepper*, 139 S.Ct. 1514, 1525 (2019) (Gorsuch, J., dissenting) (emphasis in original) [hereinafter, "Dissent"].

In *Illinois Brick*, the State of Illinois sued Illinois Brick Company. 431 U.S. 720 (1977). The State alleged that Illinois Brick had "engaged in a combination and conspiracy to fix the price of concrete blocks" and that "the amounts paid by [the State] … were more than $3 million higher by reason of this price-fixing conspiracy." *Id*. at 726-27. The Illinois Brick Company, however, did not sell the blocks directly to the State but rather to "masonry contractors," who sold to "general contractors for the masonry portions of construction projects," who then sold their services to "the State of Illinois." *Id.* at

726. The State argued that it paid higher prices than it otherwise would have because of the alleged antitrust violations committed at the top of the distribution chain. *Id.* at 726-27. The Supreme Court rejected that theory of antitrust standing and found that only the direct purchasers from the alleged violators could sue the violators.

According to Justice Kavanaugh, *Illinois Brick* should be read as holding that "[t]he proper plaintiff to bring that claim against Illinois Brick . . . would be an entity that had purchased directly from Illinois Brick." Majority Op. at 1521. Justice Kavanaugh observed that plaintiff-consumers "purchase[d] apps directly from the retailer Apple" and concluded that, as such, they could not be indirect purchasers—the "absence of an intermediary is dispositive." *Id.*

According to Justice Gorsuch, *Illinois Brick* prohibited plaintiffs from asserting injuries grounded in the pass-on of an overcharge. Dissent at 1526-27. The dissent argued that *Illinois Brick* rejected the State of Illinois' claim not because the State lacked privity with Illinois Brick but because the State's pass-on theory "would require determining how much of the manufacturer's monopoly rent was absorbed by intermediary building contractors and how much they were able and chose to pass on to their customers like the State." *Id*. at 1527. To avoid those issues, according to Justice Gorsuch, *Illinois Brick* decided "to adhere to traditional rules of proximate causation and allow only the first affected customers—the building contractors—to sue for the monopoly rents they had directly paid."[1] *Id.*

Turning to the *Apple* case, the dissent observed that "the 30% commission falls initially on the developers," *id.* at 1528, and that plaintiffs were injured "*only* if the developers are able and choose to pass on the overcharge to them in the form of higher app prices that the developers alone control." *Id.* (emphasis in original). Such a claim would "necessitate a complex inquiry into how Apple's conduct affected third-party pricing decisions." *Id*.

Moreover, the parties would have to account for how Apple's requirement that all app prices end in $0.99 affected prices, as "Apple's 99-cent rule creates a strong disincentive for developers to raise their prices [and thus] makes plaintiffs' pass-on theory of injury even harder to prove." *Id*. Finally, the rule announced by the majority would require apportioning of recovery among all the potential plaintiffs affected by the alleged overcharge, including both app purchasers *and* developers. *Id.* at 1529. (On June 4, 2019, an alleged class of app developers filed suit in the Northern District of California seeking monetary damages and injunctive relief from Apple for antitrust and unfair competition claims arising from, among other things, the 30% commission and Apple's mandate that all app prices greater than $0 end in $.99. Complaint, *Cameron et al. v. Apple, Inc.*, No. 5:19-cv-03074-DMR (N.D.Cal. Jun. 4, 2019).)

[1] The dissent also stated that, given its proximate-cause reading of the *Illinois Brick* indirect-purchaser rule, the rule should apply to claims for injunctive relief as well as damages, as a "plaintiff who's not proximately harmed by a defendant's unlawful conduct has no cause of action to sue the defendant for any type of relief." Dissent at 1527 n.1.

The debate between the majority and dissent on the proper reading of *Illinois Brick* may not resolve all standing concerns in the *Apple* litigation. Supreme Court in *AGC* identified multiple factors for assessing whether the plaintiff is a proper party to assert its antitrust claim. Those factors have been summarized as "(1) ***the causal connection between the antitrust violation and the harm to plaintiff***, and whether the harm was intended; (2) the nature of the injury, including whether the plaintiff is a consumer or competitor in the relevant market; (3) ***the directness of the injury***, and whether the damages are too speculative; (4) ***the potential for duplicative recovery, and whether apportionment of damages would be too complex***; and (5) the existence of more direct victims." American Bar Association, Section of Antitrust Law, Antitrust Law Developments 743-44 (8th ed. 2017) (emphasis added).

Although plaintiffs prevailed under *Illinois Brick* due to their contractual privity with Apple, might Apple renew its motion against plaintiffs' standing under *AGC* on the causation, remoteness, and apportionment grounds that were presented by the dissent?

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

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