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New Toys For Old Games: eBooks – iTroubles

Jay L. Himes & Meegan Hollywood
Labaton Sucharow LLP

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I. INTRODUCTION

On April 11, 2012, media outlets exploded with the news that the Department of Justice had filed a civil antitrust case against Apple and five of the six largest publishing companies in the United States for illegally conspiring to fix eBook prices. The DOJ's complaint alleged that HarperCollins, Hachette, Macmillan, Penguin, and Simon & Schuster (the "Publishers"), along with Apple, conspired to raise prices by collectively adopting "agency" agreements to market eBooks. Under these new arrangements, the Publishers were able to set the price of their own eBooks and to eliminate pro-consumer discount pricing by Amazon, the then-leading eBook seller, at its Amazon.com website. Apple, the DOJ charged, participated in the conspiratorial activity when, in 2010, it entered agreements with the Publishers to distribute their eBooks through its newly created iBookstore for use with its iPad tablet computer.[2]

Almost immediately after filing suit, the DOJ came under intense criticism. Many wondered whether the DOJ "got it right," as Amazon, the retail monolith with an enormous hold on the eBooks market, stood to gain from the government's lawsuit.[3] Additionally, many assert that, by introducing the iPad, Apple sparked an explosion of innovation and competition in the eBook tech world. For instance, the advent of the iPad pushed the creative minds behind "eReaders" to develop devices with new and improved features such as color pictures, audio and video, and fixed display. These new features contrasted sharply with the black-and-white, "one-trick-pony" that Amazon's "Kindle" reader, introduced in 2007, represented. Shouldn't the government encourage this kind of ingenuity and product development, particularly in emerging markets? Perhaps it should—but certainly not if we have to sacrifice our antitrust laws as a result.

The DOJ, we believe, got it exactly right here. The government's 35-page complaint is rife with secret meetings at upscale New York eateries and communications between high-level Publisher executives. Writing to be "Twombly-compliant," the pleading, which reads like a pitch to a publishing house for a suspense novel, alleges serious anticompetitive misconduct. The DOJ details a price-fixing conspiracy that it could not responsibly ignore.

Thus, while the innovations of Apple and others over the past two years may reflect significant industry advances and offer considerable consumer benefits, still, the antitrust laws

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[1] The authors are, respectively, partner and associate at the law firm of Labaton Sucharow LLP, in New York City. Mr. Himes, who co-chairs the firm's Antitrust Practice Group, is the former Antitrust Bureau Chief, Office of the Attorney General of New York. Firm attorneys are counsel for plaintiffs in the civil class action eBooks litigation.

[2] Random House, also one of the six largest publishing companies in the United States, was not named as a defendant by the DOJ.

[3] *See, e.g.,* Letter from Scott Turow: Grim News (Mar. 9, 2012) (The Authors Guild President writing that the DOJ "may be on the verge of killing real competition in order to save the appearance of competition"), *available at* http://www.authorsguild.org/advocacy/articles/letter-from-scott-turow-grim.html ("Turow Letter").

cannot be jettisoned to accomplish such goals. That's cheating, and it's illegal. The changes here may be innovative. But the antitrust law is textbook.

II. THE ARRIVAL OF DIGITIZED CONTENT AND THE $9.99 "PROBLEM"

Before the coming of eReaders and multi-function tablets like Apple's iPad, major publishers and other industry members sold hardcover books and paperbacks to brick-and-mortar retailers using a distribution arrangement known as the "wholesale model." Under this model, publishers sold their titles to bookstores at wholesale prices, which typically represented a percentage discount off of a title's cover or list price. The retailers then decided, independently, their own retail price on sales to end-user consumers. The Publishers used this model for decades, and they continued to use it when online vendors, such as Amazon, began selling physical books on their websites.

When Amazon released the Kindle in late 2007, each of the Publishers decided to sell their digital content, "eBooks," to Amazon using the wholesale model. Amazon was, therefore, free to charge consumers whatever price it deemed fit for eBooks, and it opted for an aggressive discount pricing strategy. For many titles, especially new releases, Amazon charged only $9.99 or lower—far less than the price at brick-and-mortar retailers for the same physical book. In some instances, Amazon's eBook price was less than the wholesale price that Amazon paid to the publisher.

Amazon's pricing strategy helped to fuel sales of its Kindle reader, which carried a much higher profit margin than did sales of eBooks. Amazon also could subsidize its pricing on new releases from sales of "backlist" or out-of-print titles, where it was the dominant supplier. The strategy worked. Amazon achieved great success with its Kindle, capturing upwards of 80 percent of U.S. eBook sales by 2010. Throughout this period, eBook sales catapulted to become the fastest-growing segment of the publishing industry. Indeed, by the second quarter of 2010, Amazon's sales of eBooks surpassed its sales of hardcover books for the first time. Consumers, of course, benefited from Amazon's lower prices for eBooks.

III. THE PUBLISHERS COME TO VIEW AMAZON AS A COMMON "ENEMY"

By the fall of 2008, the Publishers had concluded that Amazon's success represented a significant threat to their business model and to the publishing industry as a whole. The Publishers worried that readers would come to expect lower prices for books.[4] As it were, readers already believed that eBook prices ought to be less than those of physical books due to lower or non-existent costs associated with printing, distributing, and returning eBooks.[5] The Publishers feared that this belief would condition consumers to believe that a book was only "worth" $9.99, and that this consumer expectation would cause downward pressure on prices for eBooks and physical books alike. Ultimately, brick-and-mortar stores, the Publishers reasoned, would become obsolete. Thus, for them, Amazon's continued success foreshadowed an ominous industry upheaval.

[4] Complaint at ¶¶ 3, 37, *United States v. Apple, Inc., et al.*, 12-CV-2826 (S.D.N.Y. Apr. 11, 2012) ("DOJ Comp.").

[5] *Id.* at ¶ 30.

According to the DOJ's complaint, the Publishers believed that none alone could successfully pressure Amazon and other online retailers to increase their prices for eBooks. So the Publishers conspired to do so.[6] Beginning no later than September 2008, the Publishers' senior executives engaged in secret meetings, discrete telephone conversations, and other communications in which they jointly acknowledged the threat that they believed Amazon's pricing strategy posed and the need to work together to end that strategy.[7] Initially, various Publishers developed a strategy of delaying the release date of an eBook until well after that of the hardcover version, an industry practice called "windowing."[8] However, this approach proved unsuccessful in pressuring Amazon to raise its prices.[9]

IV. THE SCHEME EVOLVES: APPLE TO THE RESCUE

Apple's planned introduction of its iPad tablet in early 2010 provided the perfect storm of opportunity for the Publishers to implement a plan to eliminate the threat that Amazon presented.[10] In late 2009, as the iPad product launch approached, Apple considered how best to facilitate eBook sales through its existing online retail outlet, iTunes.[11] iTunes already offered media content such as music and movies, and had an enormous pre-existing customer base—with associated credit card information—in the millions. Thus, iTunes was primed to sell eBooks, and despite selling existing content via the agency model of distribution on iTunes, Apple initially contemplated selling eBooks through the established wholesale model of distribution.[12] However, the Publishers seized the opportunity before them and, together with Apple, settled on a strategy to replace the wholesale model with an agency model industry-wide.[13] In sum, Apple's entry into the sale of eBooks via iPad facilitated the Publishers' transforming the publishing industry to a new business model that, they believed, would sustain the industry to their own liking.

Recall that under the traditional wholesale model, the publisher sells to the retailer, who then sets its resale price to consumers. By contrast, with the agency model, the publisher itself sets the price for eBooks, which the publisher sells directly to consumers. The retailer acts as the publisher's agent by making the publisher's titles available for sale in the retailer's store or online website. In exchange for providing this marketing and distribution service, the retailer receives a percentage commission of the retail price for each eBook sold through its outlet.

In January 2010, Apple signed nearly identical contracts with each Publisher.[14] Each agency agreement included four major elements:

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[6] *Id*. at ¶¶ 3, 35, 37.

[7] *Id* at ¶¶ 37, 39-49.

[8] Opinion & Order at 9, *In re Electronic Books Antitrust Litigation*, 11-MD-2293 (S.D.N.Y May 15, 2012) ("Order Den. Mot. to Dismiss").

[9] *Id*.

[10] DOJ Comp. at ¶ 51.

[11] *Id*.

[12] *Id*.

[13] *Id*. at ¶¶ 52-64, 73.

[14] *Id*. at ¶ 74.

1. Each agreement specified that with the launch of Apple's iPad and iBookstore on April 3, 2010, the Publisher would sell its eBooks in the iBookstore under the agency model. For each sale from the iBookstore, Apple was to receive a commission of 30 percent of the sales price.
2. Each agreement included a most-favored-nation clause.[15] The MFN stipulated that the sales price for eBooks on other platforms could not be lower than the price for that same title in the iBookstore.[16] This price-matching feature essentially precluded other eBook retailers from offering inducements to Publishers in exchange for lowering the retail price below that available at iBookstore. Thus, the MFN eliminated retail competition by arresting downward pricing pressure.[17]
3. Each agreement set the prices for eBooks according to a formula tied to the list price of physical books. Under this formula, the eBooks prices would range from $12.99 to $14.99 for most newly released general fiction and nonfiction titles.[18]
4. Each agreement required the Publishers to use the agency model when selling eBooks through other vendors of any meaningful size, beginning no later than the launch date of the iPad.[19]

V. IPAD LAUNCHES: THE FIX IS IN

Apple held its iPad launch event on January 27, 2010. Apple announced that it had signed agreements with each Publisher to sell eBooks under the agency model. Apple also revealed that the prices for eBooks on the iPad would be higher than the $9.99 price that Amazon had been offering. How, one might fairly ask, could this work? Right after the launch event ended, the *Wall Street Journal*'s Walter Mossberg asked Apple's then-CEO, Steve Jobs, that very question: "Why should [the customer] buy a book for $14.99 on your device when she can buy one at $9.99 at Amazon or from Barnes & Noble on the Nook?" Jobs responded with an assurance that, "[t]he prices will be the same." Jobs added, "[t]he Publishers are actually withholding their books from Amazon because they are not happy."[20]

The Mossberg/Jobs exchange was captured on (ironically) digital camera, and has since circulated around the internet. Moreover, the following day, Jobs told his biographer:

> Amazon screwed it up. It paid the wholesale price for some books, but started selling them below cost at $9.99. The publishers hated that. . . . So we told the publishers, "We'll go to the agency model, where you set the price, and we get our 30%, and *yes, the customer pays a little more, but that's what you want anyway*.". . .

[15] *Id*. at ¶ 63.
[16] *Id*. at ¶¶ 65, 77-78.
[17] *Id*. at ¶ 66.
[18] *Id*. at ¶¶ 68, 75.
[19] *Id*. at ¶ 76.
[20] Philip Elmer-DeWitt, *Steve Jobs on Camera: The Publishers are actually going to withhold their books from Amazon* (May 15, 2012) *available at* http://tech.fortune.cnn.com/2012/05/15/steve-jobs-on-camera-the-publishers-are-actually-going-to-withhold-their-books-from-amazon/?source=linkedin, and linked video, *available at* http://m.wsj.net/video/20100128/012810atdmossy/012810atdmossy_320k.mp4 (at approximately 1:58-2:28).

> Given the situation that existed, what was best for us was to do this aikido move and end up with the agency model. And we pulled it off.[21]

Notably, even though, as Jobs said, "the customer pays a little more" under the agency model, the Publishers actually stood to make **less** money per eBook under the agency model than they had been making under the wholesale model. This occurs because a publisher captures only 70 percent of the retail sales price of an eBook under the agency model, whereas under the wholesale model, it captured the entire wholesale price.

For example, if the typical wholesale price for a newly released eBook was $14 (roughly half the list price), the publisher would receive $14 under the wholesale model even if the retailer, such as Amazon, sold the eBook for $9.99. Under the agency model, however, with an eBook sales-price of $14 (essentially the mid-point in the range of eBook prices that Jobs mentioned), the publisher nets only $9.80—70 percent of $14—taking account of the 30 percent commission paid to the sales agent, here Apple. Indeed, for a publisher to net the same $14 under the agency model that it received under the wholesale model, the publisher would have to price its title to the consumer at $20.

So, while consumers paid higher prices for eBooks, the Publishers themselves made less money. Why, then, did the Publishers agree to this business model shift, especially when they themselves considered it a "financial pain"?[22]

VI. THE PUBLISHERS AND APPLE FORCE AN INDUSTRY SHIFT

The Publishers' end goal here was to end Amazon's discount pricing. Shortly after penning agency agreements with Apple, and just days before the iPad product launch, representatives from Hachette, HarperCollins, Simon & Schuster, and Macmillan each met separately with Amazon representatives to propose that Amazon also shift to the agency model.[23] Macmillan even offered to give Amazon the same 30 percent commission it was giving to Apple—while, at the same time, threatening to delay the release of its eBooks to Amazon until seven months after the launch of the hardcover edition if Amazon did not agree.[24] Amazon initially resisted, and briefly pulled all Macmillan titles off both the Kindle website and Amazon.com.[25] Macmillan refused to retreat from its ultimatum, however. Within days, Amazon, knowing full well that Macmillan was just the first publisher to threaten access to its titles, succumbed to the agency model.[26] By April 1, 2010, each of the Publishers had concluded negotiations with Amazon to sell eBooks under the agency model.[27]

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[21] Order Den. Mot. to Dismiss at 14 (emphasis in original).

[22] Second Amended Complaint for Injunctive Relief, Civil Penalties & as Parens Patriae on behalf of Consumers at ¶ 68, *The State of Texas, et al. v. Apple, Inc.*, *et al.*, 12-CV-03394, 11-md-02293 (S.D.N.Y. May 17, 2012) ("States SAC").

[23] Order Den. Mot. to Dismiss at 17.

[24] *Id.*; *see also* DOJ Comp. ¶ 80.

[25] Order Den. Mot. to Dismiss at 17; DOJ Comp. ¶ 80.

[26] DOJ Comp. ¶ 84.

[27] Order Den. Mot. to Dismiss at 17.

After the agency model was adopted, the price of new best-selling eBooks increased by 40 percent on average, even though there was no corresponding cost increase.[28] By mid-2010, eBook prices were identical across the four major eBook distributors, Amazon, Sony, Apple, and Barnes & Noble.[29] In some instances, the price of the eBook even exceeded the price of the counterpart physical book.[30]

VII. CLASS ACTIONS, GOVERNMENT ACTIONS, AND FOREIGN COMPETITION AUTHORITIES. . . . OH, MY!

The actions of the Publishers and Apple quickly attracted the attention of the private bar, as well as federal, state, and foreign competition authorities. First, in mid-2010, the Texas and Connecticut Attorneys General announced investigations into eBook pricing.[31] Then, on March 2, 2011, the European Commission confirmed unannounced raids in Europe the previous day on eBook publishers suspected of having violated EU competition laws.[32] Not long thereafter, the first private class action complaint against the Publishers and Apple was filed in the Northern District of California in August 2011.[33] Between August and December of 2011, 29 more class actions were begun in both the Northern District of California and the Southern District of New York. Then, in December of 2011, the European Commission announced a formal investigation into the Publishers and Apple for colluding to raise eBook prices.[34] Hot on the heels of the EC's announcement, the DOJ confirmed at a December congressional hearing that it too was investigating the eBook industry for price-fixing.[35]

On April 11, 2012, the DOJ and 16 states filed civil cases against the Publishers and Apple, alleging that the companies violated the antitrust laws by conspiring to fix eBook prices.[36] Since then, 15 additional states have joined the States' action.[37] The private class actions, the DOJ action, and the States' action have come to be venued in the Southern District of New York. On May 15, 2012, District Judge Denise Cote denied both the Publishers' and Apple's motions to dismiss the class action lawsuit.[38]

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[28] *Id.* at 18.

[29] *Id.*

[30] *Id.*

[31] Office of Attorney General State of Connecticut, Press Release, *Attorney General Investigates Potential Anticompetitive E-Book Deals with Amazon and Apple* (Aug. 2, 2010), *available at* http://www.ct.gov/ag/cwp/view.asp?Q=463892&A=386; Maya Reynolds, *Texas AG Probes Publishing Agency Model, One Writer's View of the World* (June 2, 2010), *available at* http://mayareynoldswriter.blogspot.com/2010/06/publishers-marketplace-had-interesting.html.

[32] Europa, *Antitrust Commission Confirms Unannounced Inspections in the e-Book Publishing Sector* (Mar. 2, 2011), *available at* http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/11/126.

[33] *See Petru v. Apple, Inc.*, No. 3:2011CV03892 (N.D. Cal. Aug. 9, 2011).

[34] Europa, *Antitrust Commission Opens Formal Proceedings to Investigate Sales of e-Books* (Dec. 6, 2011), *available at* http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/1509&format=HTML&aged=0&language=EN.

[35] Thomas Catan, *Justice Department Confirms E-Book Pricing Probe*, Wall Street Journal Online (Dec. 18, 2011), *available at* http://online.wsj.com/article/SB10001424052970203501304577084331269336926.html.

[36] *See* DOJ Comp.; Complaint for Injunctive Relief, Civil Penalties & as Parens Patriae on behalf of Consumers, *State of Texas, et al. v. Penguin Group USA Inc., et al.,* A12CV0324LY (W.D. Tex. Apr. 11, 2012).

[37] *See* States SAC, cited in full *supra* note 22.

[38] Order Den. Mot. to Dismiss at 55.

Three Publishers, Hatchette, HarperCollins, and Simon & Schuster, have agreed to a proposed settlement with the DOJ, as well as with 29 states, the District of Columbia, and Puerto Rico.[39] The DOJ's settlement, which is subject to Tunney Act proceedings and court approval, will require the three publishers, among other things: (1) to terminate the anticompetitive MFN agreements with Apple and other eBook retailers, (2) to refrain from entering into such deals for at least two years, and (3) to abstain from retaliating against any retailer setting, altering. or reducing the retail price of any eBook.[40] The States' action, in addition, requested restitution to consumers, and early news reports placed recovery to the tune of $52 million in the States' settlement with the three Publishers, which apparently is still being ironed out.[41]

VIII. HORIZONTAL PRICE-FIXING: ILLEGAL *PER SE*

Section 1 of the Sherman Act makes illegal "[e]very contract, combination . . . , or conspiracy, in restraint of commerce among the several States."[42] To establish a conspiracy in violation of Section 1, proof of joint or concerted action is required.[43] Thus, the key is whether the challenged conduct stems from independent decision or from an agreement.[44]

Some agreements—those held to be illegal *per se*—"are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality."[45] Generally speaking, price-fixing agreements or agreements to divide markets that are horizontal in nature—meaning that the parties to the agreement are "competitors at the same level of the market structure—are *per se* unlawful."[46] Time and again, courts have made clear that competitors may not lawfully agree to adopt a pricing structure: "Any combination which tampers with price structures is engaged in an unlawful activity."[47] Put another way, "the machinery employed by a combination for price-fixing is immaterial," as a conspiracy "formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity . . . is illegal *per se*."[48]

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[39] Proposed Final Judgments as to Defendants Hachette, HarperCollins, and Simon & Schuster, *United States v. Apple, Inc., et al.,* 12-CV-2826 (S.D.N.Y. Apr. 11, 2012).

[40] *Id*.

[41] The State of Connecticut Attorney General, Press Release, Apple, Publishing Companies Charged With Illegal Price-Fixing Scheme in Marketing of eBooks (Apr. 11, 2012), available at http://www.ct.gov/ag/cwp/view.asp?Q=502294&A=2341; paidContent, All 50 States May Join E-Book Refund Settlement (Apr. 18, 2012), available at http://paidcontent.org/2012/04/18/All-50-States-May-Join-E-Book-Refund-Settlement. See also U.S. Sues to Lower Prices of e-Books, USA Today (Apr. 12, 2012), available at http://www.usatoday.com/USCP/PNI/Business/2012-04-12-PNI0412biz-electronic-books_ST_U.htm.

42 15 U.S.C. § 1.

[43] *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984).

[44] *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 553 (2007).

[45] *Texaco Inc. v. Dagher*, 547 U.S. 1, 5 (2006).

[46] *Anderson News v. Am. Media, Inc.*, 10-cv-4591, 2012 WL 1085948, at *16 (2d Cir. Apr. 3, 2012); *see also Starr v. Sony BMG Music Entertainment,* 592 F.3d 314, 326 n. 4 (2d Cir. 2010). By contrast, relationships between parties at different levels of the distribution system can also implicate antitrust violations. But "vertical cases" tend to be more difficult to prove because impact in the market and injury to purchasers or competitors typically need to be shown. *See Anderson News*, 2012 WL 1085948, at *16.

[47] *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 221 (1940).

[48] *Id. at* 223; *see also, e.g., Arizona v. Maricopa Cnty. Med. Soc'y*, 457 U.S. 332, 344-48 (1982); *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647 (1980); *United States v. Gen. Motors Corp.*, 384 U.S. 127, 147 (1966); *Federal*

The DOJ's central allegation is that the Publishers and Apple colluded in signing identical agency agreements in January 2010, and that there was a collective effort to force an industry-wide shift to the agency model, thereby taking control of retail pricing and hiking the price to consumers. The crux of the DOJ's complaint is that no individual publisher was prepared to try to act alone. Therefore, they decided to work in concert. Basically, although the Publishers would certainly share the benefits of an industry switch, including consumer perception of an increased value for books and a slowed industry transition from the brick-and-mortar retail model, there also were costs associated with any individual Publisher acting alone. Most prominently, that Publisher risked at least a short-term decrease in market share as its book title prices increased. Moreover, in order to compel Amazon to abandon the wholesale model, a critical mass of Publishers was needed. No single Publisher likely had the leverage to force Amazon to make the switch. For these reasons, no Publisher Defendant would likely have signed an agency agreement with Apple absent a firm understanding that its rivals would also do so.

For its part, Apple had a strong incentive to encourage the Publishers to act collectively. If multiple Publishers had not worked together to force an industry-wide switch to the agency model, Apple would have had to compete with Amazon in establishing its iBookstore. And, Apple probably would have had to compete with Amazon on price by offering eBooks around $9.99. Or else, Apple would have had to sell eBooks at higher prices than Amazon and other platforms operating under the wholesale model, while relying on non-price competition or on bundling value to capture business. Either way, Apple would have faced a greater challenge in entering the eBooks market and gaining a significant market share.

On similar facts, in *Interstate Circuit v. United States*[49] the Supreme Court upheld an injunction entered against the defendants for violating Section 1 of the Sherman Act. Specifically, the defendants in *Interstate Circuit* consisted of a group of film distributors and a group of theaters, known as Interstate Circuit. Interstate had a monopoly on the showing of movies in several Texas cities. The company's general manager sent identical letters to eight branch managers of the film distributors, each of which included the names of all eight companies as addressees and proposed identical deal terms. The letters provided that in exchange for allowing the distributors to continue showing their firms in its theaters, Interstate would require the distributors to refuse to license a movie to any theater that charged below 25 cents for tickets to certain films, or that showed double-features under certain conditions. These restrictions were designed to limit the ability of Interstate's competitors, principally second-run theaters, to compete in those cities where Interstate did not have a monopoly.[50] All eight distributors agreed to the proposal.

Although all the distributors' trial witnesses denied any "agreement" with each other, the district court found a Sherman Act violation. Affirming, the Supreme Court held that direct evidence of agreement among the distributors was not essential. Rather:

Trade Commission v. Cement Institute, 333 U.S. 683, 693(1948); *United States v. Trenton Potteries Co.*, 273 U.S. 392, 397-98 (1927); *United States v. Trans-Missouri Freight Ass'n*, 166 U.S. 290, 313 (1897).

[49] 306 U.S. 208 (1939).

[50] *Id*. at 215-18.

> It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that the cooperation was essential to successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce, which, we will presently point out, was unreasonable within the meaning of the Sherman Act, and knowing it, all participated in the plan.[51]

More recently, in *Toys "R" Us, Inc. v. Federal Trade Commission*,[52] the Seventh Circuit affirmed the FTC's holding that Toys "R" Us had coordinated a horizontal agreement in restraint of trade by signing identical agreements with various major toy manufacturers from which it purchased. In the agreements, each manufacturer promised to restrict sales of its products to low-priced warehouse club stores—competitors of Toys "R" Us—on the condition that the other manufacturers would also do so.[53]

As alleged by the DOJ, the conduct of the Publishers and Apple closely resembles that of the defendants in *Interstate Circuit* and *Toys "R" Us*. Apple coordinated a series of identical agreements with the Publishers. Similarly, according to the DOJ, Apple made clear to each Publisher that it was offering the others a comparable deal. And, as in *Interstate Circuit* and *Toys "R" Us*, cooperation among the Publishers was essential to the success of the overall plan—to limit the price competition by Amazon, a soon-to-be Apple competitor, as well as by other eBook platforms. The Publishers were already trying to figure out a way to stop Amazon's discount pricing, and Apple's desire to begin selling eBooks as one of its intended iPad features afforded the Publishers the help they needed.

At its root, the DOJ alleges a horizontal conspiracy among the Publishers in which Apple participated. As with the movie distributors in *Interstate Circuit* and the toy manufacturers in *Toys "R" Us*, the "only condition on which" a Publisher would agree to Apple's terms "was if it could be sure its competitors were doing the same thing."[54] Apple thus aided "the suppliers to collude."[55]

To be sure, Apple's pre-iPad position in the eBooks industry was not like that of the theater circuit monopolist in *Interstate Circuit*, or that of the power buyer in *Toys "R" Us*. Also, here, the collusive impetus may well have originated at the supplier (Publisher) level, rather than with the customer as in the two earlier cases. But neither distinction should be material. What matters is that competitors—the Publishers—agreed to collectively impose an industry structure on eBook sellers and that a common customer—Apple—was enlisted to help accomplish the unlawful restriction on competition. The agreement among the Publishers and Apple "has nothing to do with enhancing efficiencies of distribution from the manufacturer's point of view."[56] Just the opposite, the idea here was to use a new distribution arrangement to increase the prices that consumers paid, and, as of the point that the DOJ sued, the conspiracy had

[51] *Id.* at 226-27.
[52] 221 F.3d 928 (7th Cir. 2000).
[53] *Id.* at 930.
[54] *Id.* at 936.
[55] *Id.*
[56] *Id.*

accomplished that anticompetitive goal. What we have here "is a horizontal agreement."[57] It is *per se* illegal.

IX. THE DOJ GOT IT RIGHT

Despite the criticism, the DOJ was right to bring suit. Digital eBooks, and the promotion of eReaders—the iPad, the Kindle, the Nook and others—are surely innovative. But the antitrust implications of the conduct by the Publishers and Apple here is not. Criticism of the DOJ for filing suit bespeaks a fundamental misunderstanding of the antitrust laws.

The goal of antitrust law is to protect the competitive process, not the fortunes of individual competitors. Businesses, large and small, are expected to achieve their success by offering lower prices, improved efficiencies, better service, and cooler gadgets. When a company does so in a legal manner, other companies facing pressure from such a successful rival simply cannot band together to protect themselves. It is no defense to conspiracy to assert that the group collectively sought to jump-start the efforts of a new entrant to compete with an established industry leader—even a dominant one.

Indeed, first by offering sales of physical books online, and later by selling eBooks for use with its Kindle eReader, Amazon exercised the very sort of skill, foresight, and business acumen that the antitrust laws are supposed to encourage. Amazon's eBooks pricing strategy was beneficial to consumers, the intended beneficiaries of the antitrust laws. The Publishers may well have found themselves challenged by Amazon's pricing as they tried to predict its long-term impact on the industry. But when businesses face challenges such as this, each is expected to examine its business model, to decide for itself whether that model is antiquated or salvageable, and to adapt accordingly—and individually. That is competition on the merits.

The antitrust laws, however, do not entitle businesses to respond to industry challenges by collectively adopting a distribution model that they prefer. The very fact here that eBook prices paid by consumers increased, while eBook revenues received by the Publishers decreased, are telltale signs that whatever was going on here, it was *not* competition on the merits.

X. THE $64,000 QUESTION

Perhaps the most interesting question here is not why the DOJ filed suit, but rather why it filed a civil case instead of a criminal one. The DOJ's complaint is chock full of the sort of high-level executive meetings and other communications that regularly result in criminal antitrust charges. So, why didn't the DOJ empanel a grand jury with a view to securing indictments?

Some have suggested that the DOJ's primary goal is judicial relief that not only ends the conspiratorial restraints, but also operates to restore eBook competition, in turn lowering prices to consumers. A civil litigation leading to an injunctive decree may, therefore, be the most appropriate form of enforcement action. But that explanation seems inadequate. For one thing, the DOJ typically opts for civil enforcement where the challenged anticompetitive conduct is sufficiently ambiguous to make criminal prosecution unwarranted. The collusion here looks pretty clear, however. Moreover, nothing prevents the DOJ from bringing not only a criminal case, but also a civil one to secure the equitable relief needed to remedy the anticompetitive

[57] *Id*. at 940.

restraints. The DOJ used to file simultaneous criminal and civil cases, although it has not done so in recent years.[58] Further, even in a criminal case, the DOJ probably could secure what amounts to equitable relief in a negotiated plea agreement (assuming of course that the criminal defendants would cop a plea instead of going to trial), or perhaps as a condition of dispensing with the company's probation.[59]

Accordingly, a more likely explanation seems to lie in the risks that a criminal trial itself might have presented for the DOJ. The case would almost surely have to be tried to a jury, which would have to reach a unanimous verdict under the proof-beyond-a-reasonable-doubt standard in order to convict. No trial to a judge where a preponderance of the evidence suffices to prove the violation. Now, in prosecuting the Publishers, these increased risks for the DOJ could well be tolerable. But Apple is another matter.

It is easy enough, as a commentator, to speak assuredly of Apple's "participation" in this anticompetitive conspiracy. However, proving it under the demands of a criminal proceeding is not so simply accomplished. Unlike the Publishers, Apple has a tenable theme to play out, which focuses on the challenges that it faced entering a new field of endeavor, the sale of eBooks, where it would have to compete against a well-heeled player like Amazon. Add to that Apple's caché as a persistent innovator and driving force in the technology world. Indeed, Apple's defense in the DOJ civil case probably mirrors what would have been a predictable theme if it had needed to defend criminally:

> Apple's entry has benefited consumers. Apple's entry brought competition where none existed . . . . Apple introduced a number of innovative features, such as color pictures audio and video, the read and listen feature, and fixed display . . . . As a result—as even the Government is compelled to admit—output has exploded. Customers enjoy vastly increased choice. Amazon has to compete and innovate beyond its small black and white reader, enriching the experience for consumers across all platforms.[60]

Moreover, Apple seemingly would have significant allies in battling the DOJ. The Authors Guild, for example, has endorsed the agency model as "loosening Amazon's chokehold

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[58] *See Standard Sanitary Mfg. Co. v. United States*, 226 U.S. 20, 52 (1912) ("The Sherman Act provides for a criminal proceeding to punish violations and suits in equity to restrain such violations, and the suits may be brought simultaneously or successively."); UNITED STATES ATTORNEYS MANUAL at 9-27.250 (instructing DOJ attorneys to "familiarize themselves with these alternatives"—such as civil actions under the antitrust laws—and to "consider pursuing them if they are available to a particular case. Although on some occasions they should be pursued in addition to the criminal law procedures."), *available at* http://www.justice.gov/usao/eousa/foia_reading_room/usam/title9/27mcrm.htm#9-27.250.

[59] *See* United States Sentencing Commission, 2011 FEDERAL SENTENCING GUIDELINES MANUAL, ch. 8 (Sentencing of Organizations) at 542, § 8D1.1(a)(6) ("The court shall order a term of probation: . . . (6) if such a sentence is necessary to ensure that changes are made within the organization to reduce the likelihood of future criminal conduct"), *available at* http://www.ussc.gov/Guidelines/2011_guidelines/Manual_PDF/Chapter_8.pdf; *United States v. A-Abras, Inc.*, 185 F.3d 26, 30 (2d Cir. 1999) ("trial courts traditionally have enjoyed broad discretion to tailor the conditions of probation to the particular circumstances of each case, provided that such conditions are reasonably related to the dual goals of rehabilitating the offender and protecting the public.").

[60] Apple Inc.'s Answer at 2, *United States v. Apple, Inc., et al.*, 12-CV-2826 (S.D.N.Y. May 22, 2012).

on the e-book market" and as "giv[ing] bookstores a fighting chance."[61] Barnes & Noble, too, has credited the Publishers' agency model with increasing competition and driving down Amazon's share of eBook sales from 90 percent to 60.[62]

Imagine, in addition, the jury box. After all the peremptories and challenges for cause are exercised, do you suppose that, maybe, there might be one or two jurors who loved and cherished their (take your pick) iMac, iPhone, iPod, or iPad, as well as the music, TV shows, and movies downloaded from iTunes—not to mention the eBooks themselves from iBookstore?

The risks inherent in a criminal trial against Apple, therefore, should not be minimized and the embarrassment potential for DOJ was correspondingly high. Apple today is Reach-Out-and-Touch-Someone 2.0. Sometimes, discretion is the better part of valor. Thus, we have a civil case instead. The Publishers and their high-level executives should all thank their lucky stars. Put in terms familiar to antitrust lawyers, they are likely free-riders. The Antitrust 101 crash-course that they so badly need compares favorably to what they could have faced.

XI. CONCLUSION

In sum, the eBooks antitrust litigation is about new technology against the backdrop of time-honored law. Like those who have gone before them, the Publishers and Apple got together in a scheme to hurt not only rivals, but also consumers—the antitrust laws' beneficiaries. And, regardless of what critics may say, neither the ingenuity that Apple has brought time and again with its glam products, nor Amazon's dominance in the sale of eBooks, allows for special treatment in the eyes of the law. The DOJ got it right—as did the States and, by the way, the private plaintiffs who sued even earlier.

[61] The Authors Guild, *The Justice Department's E-Book Proposal Needlessly Imperils Bookstores: How to Weigh In* (June 4, 2012), *available at* http://www.authorsguild.org/advocacy/articles/the-justice-departments-e-book-proposal-needlessly.html. Throughout, The Authors Guild President has supported the Publishers' adoption of the agency model, at least insofar as they did not collude. *See, e.g.,* Turow Letter, *supra* note 3 ("any rational publisher would have leapt at Apple's offer and clung to it like a life raft").

[62] Comments of Barnes & Noble, Inc. on the Proposed Final Judgment at 3, *United States v. Apple, Inc., et al.*, 12-CV-2826 (S.D.N.Y. June 7, 2012), *available at* http://gigaompaidcontent.files.wordpress.com/2012/06/barnes-noble-complaint.pdf.