

No. 16-1454

In the Supreme Court of the United States

STATE OF OHIO, *et al.*,

Petitioners,

v.

AMERICAN EXPRESS CO., *et al.*,

Respondents.

**On Writ Of Certiorari To The United States Court
Of Appeals For The Second Circuit**

**BRIEF OF WAL-MART STORES, INC., THE HOME
DEPOT, INC., TARGET CORPORATION, SEARS
HOLDING MANAGEMENT CORPORATION, JO-
ANN STORES, LLC, AND MERCHANT
TRADE ASSOCIATIONS AS *AMICI CURIAE*
IN SUPPORT OF PETITIONERS**

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INTEREST OF *AMICI CURIAE*¹

The merchant and trade association *amici* are or represent national and regional retailers. Retail contributed \$2.6 trillion to annual GDP, and is a daily barometer for the nation's economy. Retail is the nation's largest private sector employer, supporting one in four U.S. jobs—42 million working Americans.

Amici Wal-Mart Stores, Inc., The Home Depot, Inc., Target Corporation, Sears Holding Management Corporation, and Jo-Ann Stores, LLC represent a diverse assortment of the country's largest retailers, ranging from those offering a wide range of merchandise across all categories, to others that operate in a single large retail vertical, and still others that cater to specific consumer needs. All are dedicated to providing superior products and service to clients at affordable prices. *Amici*'s customers pay for goods and services using various payment methods, including credit cards, so *amici* pay millions of dollars in fees each year to Amex and the other major credit card networks.

The Retail Litigation Center, Inc. (RLC) engages in significant legal proceedings that have a national impact on the retail industry on behalf of its 23 members who are some of the country's largest and most innovative retailers that collectively employ

¹ No counsel for any party authored this brief in whole or in part, and no entity or person, other than *amici*, their members, and their counsel, made any monetary contribution toward the preparation or submission of this brief. All parties have filed blanket consents to the filing of *amicus* briefs.

millions of people throughout the United States, provide goods and services to tens of millions more, and account for tens of billions of dollars in annual sales. RLC's members include retailers across all retail verticals from Apple to Walmart, 7-Eleven to Whole Foods, Best Buy, PetSmart, AutoZone, REI, and many more.

The National Retail Federation (NRF) is the world's largest retail trade association, representing discount and department stores, home goods and specialty stores, Main Street merchants, grocers, wholesalers, chain restaurants, and Internet retailers from the United States and more than 45 countries.

The National Association of Convenience Stores (NACS) is an international trade association that represents both the convenience and fuel retailing industries, with more than 2,200 retail and 1,800 supplier company members. The United States convenience industry has more than 154,000 stores across the country and had nearly \$550 billion in sales in 2016.

The Food Marketing Institute (FMI) proudly advocates on behalf of the food retail industry, which employs nearly 5 million workers and represents a combined annual sales volume of almost \$800 billion. FMI membership includes the entire spectrum of food retail venues; single owner grocery stores, large multi-store supermarket chains, and online and mixed retail stores, with FMI member companies operating nearly 33,000 retail food stores and 12,000 pharmacies.

The National Grocers Association (NGA) is the national trade association representing the retail and wholesale grocers that comprise the independent sector of the food distribution industry. Independent retailers are privately owned or controlled food retail companies operating a variety of formats and this sector is responsible for generating \$131 billion in sales, 944,000 jobs, \$30 billion in wages, and \$27 billion in taxes.

The National Association of Shell Marketers, Inc. (NASM) is a national trade association representing approximately 140 wholesale distributors of Shell-branded petroleum products, together with 65 suppliers of goods and services to the petroleum industry. NASM's members, and the service station dealers supplied by them, engage in credit card transactions involving the sale of convenience store merchandise and Shell-branded motor fuels to consumers at thousands of retail locations throughout the United States.

The Retail Industry Leaders Association (RILA) is a public policy organization consisting of the country's largest retailers. Together RILA's members account for more than \$1.5 trillion in annual sales, provide millions of jobs and operate more than 100,000 stores, manufacturing facilities, and distribution centers.

INTRODUCTION

American Express ("Amex") prohibits merchants from truthfully telling their customers that Amex is a higher-fee credit card or giving their customers any incentive to pay with lower-fee cards. After a seven-week trial, the district court found that these

prohibitions—Amex’s so-called Non-Discrimination Provisions (NDPs)—actually restrain competition among card networks, cause merchants to pay them higher fees, and lead to increased prices for all consumers (whether they pay by card, cash, check, or using government benefits).

That state of affairs is possible only because merchants have no other choice. For all but some of the smallest merchants, accepting Amex cards is a requirement of doing business. Declining to accept Amex, experience has taught, is a customer-losing proposition. Consumers who hold Amex cards regularly insist on paying with them. The simple fact of life is that, if a merchant does not accept Amex, many consumers will shop elsewhere.

That reality gives Amex significant market power, which it uses to dictate the price and terms on which merchants (even the largest and most sophisticated merchants in the country) accept Amex. In particular, Amex asserts its market power to prevent accurate price information being provided to consumers—which enables Amex to charge supra-competitive merchant fees.

Assume, for example, that a customer at the cash register holds both an Amex card that would give Amex a 3% cut of the impending purchase, as well as Amex’s competitor’s card that would cost the merchant only half as much. Amex’s NDPs strictly prohibit the merchant from providing *truthful information* to that customer about the relative costs of the cards so that the customer can make an informed decision about which card to use. Nor can the merchant offer its customers discounts or other benefits for opting to use the lower-fee card. Amex’s

NDPs prohibit the merchant from giving its customers truthful information on the costs of payment choices and from giving customers incentives to use a lower cost option. Amex's NDPs also remove any incentive for competing card issuers to reduce their merchant fees, since they will receive no benefit from doing so.

As a result, Amex and its competitors are able consistently to increase their prices unencumbered by market pressure to keep prices down. The merchant's customer (assuming she is affluent enough to qualify for an Amex card), in turn, focuses solely on whatever "rewards" she might get for using an Amex card—unaware of the resulting cost to the merchant and, ultimately, to the customers themselves. Having thus prevented price signaling at the cash register, Amex then exploits the disconnect by bombarding the consumer with signals about the benefits of using its card. Armed with incomplete information, the consumer inaccurately perceives Amex's rewards to be a free lunch.

The record in this case amply demonstrates that merchants *want* to send accurate price signals to their customers by providing information about credit card costs or incentives for using lower-cost cards. By prohibiting merchants from doing so, Amex's restraint of trade suppresses price competition among credit card networks. As the district court correctly found, Amex "prevent[s] merchants from influencing their customers' payment choices." Pet. App. 202a. By tying merchants' hands in this manner, Amex's NDPs "effectively remove the incentive" for credit card networks "to compete with one another by offering

merchants a lower price.” *Id.* at 203a. That elimination of price competition not only protects Amex’s high-priced network, but also allows other credit card networks to raise their fees, as Discover did when it realized it could not gain market share with lower prices. Pet. App. 204a–06a. In other words, while Amex’s NDP’s are imposed by Amex unilaterally, their purpose and effect is to prevent fee competition among Amex, Visa, MasterCard, and Discover—the only four networks.

The undisputed result is that merchants pay higher fees than they would have to in a competitive environment. Indeed, as Kansas City Federal Reserve Bank researchers noted, the fees that U.S. merchants pay to credit card networks are among the highest in the world.² Merchants then pass those added expenses on to their customers through higher prices for goods and services. And *all* of a merchant’s customers bear that resulting burden—even if they pay by cash, check, or using government benefits such as “food stamps.” This is antithetical to all efficient markets, and particularly so in retail and other industries where businesses most aggressively wring out unnecessary costs to provide consumers the lowest-possible prices.

It is also a growing problem. The relentless march toward a cashless economy magnifies the

² Bradford & Hayashi, *Developments in Interchange Fees in the United States and Abroad*, Payment Sys. Research Briefing (Federal Reserve Bank of Kansas City), April 2008, at 1, <http://bit.ly/2jiwHMz>; see also Hayashi, *Credit and Debit Card Interchange Fees in Various Countries*, August 2016, <http://bit.ly/2BXgxgf>.

significance of non-cash transactions—and the economic drag from their inefficient and anti-competitive fees. A decreasing number of consumers pay for so little as a cup of coffee by cash or check—and fewer still shop online that way.

Amex nevertheless defends its restraint of interbrand competition among credit card networks as perfectly acceptable under the antitrust laws. It relies on the claimed two-sidedness of the credit card business, in which credit card networks compete for both merchants and cardholders. The merchant and cardholder sides of its business must be thought of as one market, Amex contends. Accordingly, it says, the district court’s unchallenged factual findings that Amex has eliminated price competition among credit card networks and caused merchants to pay “dramatically” higher prices prove nothing—not even a *prima facie* case requiring rebuttal. Pet. App. 71a.

The special “two-sidedness” rule that Amex seeks turns antitrust doctrine on its head. Markets, for antitrust purposes, are about substitutes; they comprise things that customers would substitute in response to a price increase. The record in this case amply demonstrates—and the district court correctly found—that merchants can substitute only among the major credit card networks in response to a price increase by any one of them (or all of them). That, accordingly, is the relevant market, and the effect of Amex’s elimination of price competition in that market, the district court found, is rising prices without meaningful opportunities for exit. See Pet. App. 150a.

Moreover, it is well-established that courts must evaluate trade restraints’ competitive effects on the

goods or services that sellers offer to buyers. Courts properly focus on whether a restraint enhances the competitive process. Claims that third parties to that exchange may benefit from anticompetitive restraints on it are routinely rejected, as are arguments that withholding information from consumers can be justified as pro-competitive. This Court has emphasized that the “Sherman Act reflects a legislative judgment that, ultimately, competition will produce not only lower prices but also better goods and services.” *Nat’l Soc’y of Prof’l Eng’rs v. United States*, 435 U.S. 679, 695 (1978). Nothing about the nature of Amex’s business “platform” requires upending that sound application of settled antitrust doctrine.

* * * * *

This brief details merchants’ uniquely relevant perspective on why that must be so in the credit card industry just as it is in every other industry. As explained below, the record here is full of compelling evidence—much of it developed through testimony from merchants about their actual experiences—of Amex’s market power and its use of that power to dictate the price and terms on which merchants must accept Amex cards. That evidence cannot be reconciled with the court of appeals’ conclusion that Amex’s actions may, by the magic of calling its business a two-sided platform, be procompetitive. Or that merchants are not subject to the market power they actually experience every time they deal with Amex. To the contrary, the record shows that even the largest merchants stand no realistic chance in the face of Amex’s market power, and that there is

no countervailing procompetitive byproduct to the way Amex exploits this coercive dynamic.

This brief also details how Amex's terms generate supra-competitive merchant fees that are in turn passed on to *all* customers. It explains how that harms even Amex cardholders, who are prevented from having the opportunity to make informed decisions about whether to accept discounts or other alternative "rewards" from merchants for their purchases. Tellingly, Amex wins big, as do the other major card networks (which also enjoy supra-competitive fees thanks to Amex).

Finally, this brief explains how the court of appeals' special rule for credit card network platforms ignores the market realities that merchants face, and demonstrates that traditional antitrust principles are more than up to the task of defining the relevant market and shifting the burden to Amex to demonstrate any procompetitive effects their conduct has elsewhere. Not only is there no reason to ramble through the wilds of economic theory to address a restraint of trade that increases prices, but doing so (as the court of appeals did) risks vesting already powerful companies like Amex (and those that will follow as our economy becomes increasingly electronic) with the power to throttle competition where it is most needed.

ARGUMENT

I. Amex Has Market Power Over Merchants, And Wields That Power To Stifle Competition And Harm Consumers

Some of the largest merchants in the country (including certain merchant *amici*) repeatedly testified at trial to their real-world experience as market participants, and the district court found that testimony to be credible evidence of market power and price distortion. Those factual findings were not challenged on appeal, nor did the court of appeals find them to be clearly erroneous.

Instead, the court of appeals dispatched the evidence presented and the district court's factual findings as misplaced observations about just one facet of a larger platform. It contended, moreover, that the district court "ignore[d]" that *some* merchants *do not* accept Amex, see Pet. App. 46a, and minimized "cardholder insistence" on using Amex cards as being little more than a fancy name for "cardholder satisfaction," *id.* at 48a.

The court of appeals was wrong. Below, we highlight merchant testimony and other record evidence demonstrating (1) Amex's very real market power to dictate fees and other terms to even the largest merchants in the country, which have no practical choice but to accept Amex cards, and (2) the anticompetitive effects its exercise of that power has on all merchants and their customers. These real world facts illustrate the actual harm that Amex's conduct imposes on merchants and, by extension, consumers.

A. Even The Largest U.S. Merchants Have No Choice But To Accept Amex On The Terms That Amex Dictates

Virtually every major, multi-location retailer in America accepts Amex, even though Amex charges them higher fees than Amex’s competitors. The court of appeals tried to minimize that fact by pointing out that one-third of merchants who accept credit card payment do not accept Amex. Pet. App. 46a. That is true, but misses the point. By the end of 2016, Amex cards were accepted in locations accounting for *90 percent* of credit card spending in the United States. American Express Company, Form 10-K for year ending Dec. 31, 2016, at 3 (Feb. 17, 2017). The Amex holdouts are “very, very small,” in the words of Amex’s senior vice president for merchant relations. Pet. App. 224a n.48. Most of them “are ‘probably half the size’ of ‘your local florist.’” *Ibid.*³

As a result, customers expect all but a small minority of the smallest merchants to accept any and all cards from the major networks (Visa, MasterCard, and Amex). The district court found that to be true, specifically, for Amex cardholders. Some are required to use Amex cards for business expenses, and others want the airline miles, statement credits, or other benefits that come with card use. Pet. App.

³ Even among this group of small merchants, Amex acceptance may be increasing. The district court found that much of Amex’s coverage gap results from its historical choice not to *pursue* small merchants for its network. Pet. App. 186a–87a. But Amex recently has begun to seek out this additional merchant base. *Id.* at 187a–88a; see also *id.* at 89a (discussing Amex’s “Small Business Saturday” and other initiatives “to promote spending at small businesses”).

157a–58a. The resulting cardholder insistence has long safeguarded Amex’s position in the industry. Such cardholder insistence is becoming all the more a factor as commerce increasingly moves online. These days, a customer who encounters a merchant that does not accept Amex can choose to purchase the same goods from one that will, all without leaving the couch.

Not surprisingly, then, medium and large merchants have just about universally concluded that refusing to accept Amex is not a commercially viable option. In other antitrust cases, unsuccessful customer attempts to exit in response to exercises of market power must be hypothesized or assumed, but in this case there is concrete record evidence that Amex is able “to force [merchants] to do something that [they] would not do in a competitive market.” *Eastman Kodak Co. v. Image Tech. Servs., Inc.*, 504 U.S. 451, 464 (1992).

An overcharged merchant can dream, of course, but most quickly awaken to this market reality. At trial, witnesses from Ikea, Best Buy, Enterprise, and Sprint all testified that their respective companies conducted analyses, surveys, and “war game[s]” regarding the feasibility of declining Amex. Pet. App. 159a n.27. Each concluded that “the foregone profits associated with losing Amex-insistent customers”—customers who will shop elsewhere if they are unable to use Amex—“rendered dropping Amex commercially impractical.” *Id.* at 159a.

Hilton Hotels, for example, predicted that if it dropped Amex it would lose *two-thirds* of its Amex charge volume. Pet. App. 158a–59a n.26. Witnesses from Sears, Crate & Barrel, and The Home Depot

testified that their companies determined they did not need a detailed study to know that refusing to accept Amex was nonsensical. *Ibid.* As one merchant testified, dropping Amex would be “crazy.” *Ibid.*

Two major merchants put that wisdom to the test. As briefly explained below, their experience confirmed what their counterparts predicted: Amex acceptance is effectively mandatory for all but a small percentage of the smallest merchants. Before long, the “rogue” merchants were back in the Amex fold—and on Amex’s terms.

Walgreens stopped accepting Amex cards in 2004 after Amex raised its merchant fee by ten basis points (notwithstanding that the fee was already forty basis points higher than Visa’s or MasterCard’s). Pet. App. 163a. At the time, Walgreens was the ninth largest retailer in the United States. But that size could not carry the day against Amex. In the end, Walgreens “was forced to retreat” from its decision “in the face of public outcry from its customers.” *Ibid.* Walgreens ended up “capitulat[ing]” to Amex and accepting “pricing terms that were substantially similar to those [it] had previously deemed unacceptable.” *Ibid.*

Murphy Oil likewise stopped accepting Amex in 2008, at which point it operated roughly a thousand gas stations and convenience stores in Walmart parking lots across the country. Murphy Oil ended up losing *twice* the number of customers that even Amex had predicted it would. Pet. App. 162a. That substantial wave of customer attrition forced Murphy Oil to resume accepting Amex—yet again, on Amex’s terms. *Id.* at 163a. The head of Amex’s pricing unit wrote to colleagues that Amex “should

be able to make use” of the Murphy Oil example during “merchant negotiations.” *Ibid.*

The lack of realistic exit ramps for merchants, the district court concluded, has put Amex in the driver’s seat. The district court found, after extensive analysis (see, e.g., Pet. App. 166a–72a), that “American Express’s ability to impose significant price increases during its Value Recapture initiatives between 2005 and 2010 without any meaningful merchant attrition is *compelling evidence* of Defendants’ power in the network service market.” *Id.* at 150a (emphasis added). The NDPs ensured that competition from other credit cards did not constrain Amex’s ability to raise prices.

At trial, however, Amex tried to insist that it can’t be *that* powerful given that *some* merchants got out from under its standard NDPs. But its own evidence proved the opposite. It could find only 139 merchants—***out of the over 3 million in its network***—who had received even marginal variations on the NDPs in negotiations with Amex. Pet. App. 97a. And, as the district court found, those variations did not open a pathway to meaningful competition among card networks: “[T]he [non-standard] rules still restrict[ed] nearly all forms of point-of-sale steering, including merchants’ ability to express a preference for a particular card brand.” *Ibid.*

Such widespread merchant acquiescence in Amex’s standard anti-steering rules is not for want of pushback. “[M]any * * * larger merchants have requested that Amex remove its NDPs from their agreements entirely.” Pet. App. 97a. Representatives from merchants as ubiquitous as The Home Depot,

Hilton, and Sprint established at trial that they took their best shot at getting anti-steering rules removed from their respective Amex agreements. See *id.* at 97a–98a. None succeeded. See *ibid.* Amex’s ability to impose these restraints on unwilling merchant after unwilling merchant is a testament to what the district court correctly recognized as Amex’s “significant power” over merchants large and small. *Id.* at 159a.⁴

B. The Anti-Steering Rules Amex Imposes On Merchants Have Actual and Substantial Anticompetitive Effects

The rule of reason prohibits restraints of trade that have unjustified anticompetitive effects. *Chi. Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918); Pet. App. 108a–09a. To establish a *prima facie* case, a plaintiff may prove such effects directly. *Ibid.* When the anticompetitive effects are obvious,

⁴ Amex’s NDPs sustain the market power that allows Amex to impose them in the first place. Amex cardholders—shielded by the NDPs from truthful information about the cost to merchants of Amex card use—make the economically rational choice to insist on using Amex. The cardholder gets rewards and benefits from Amex for doing so, while paying the same retail price as everyone else. Amex’s vicious cycle of market-power maintenance—on the backs of merchants and their customers—has been extraordinarily successful. The court of appeals incorrectly concluded, however, that Amex’s investment in its rent-seeking activity—through the cardholder rewards that drive the customer insistence that gives it market power—somehow *disproves* that Amex has that market power. See Pet. App. 46a. Not so. Rather, this is the textbook behavior of a rent-seeking firm engaging in (and trying to safeguard) anticompetitive conduct. See, e.g., Baumol & Blinder, *Economics: Principles and Policy* 381 (13th ed. 2015).

or there is a “naked restraint” on price or output, the Rule of Reason can “be applied in the twinkling of an eye.” *NCAA v. Bd. of Regents*, 468 U.S. 85, 109–10 & n.39 (1984). Alternatively, if the plaintiff shows that a defendant has market power, it is enough to show that the restraint has potential anticompetitive effects. Pet. App. 108a–09a. Amex’s NDPs were shown to be anticompetitive under both methods.

1. Plaintiffs demonstrated the anticompetitive effects of Amex’s NDPs directly. Not surprisingly, the record showed (and the district court found) that everyone—except Amex and the other major payment card networks—loses from the market failure caused by Amex’s NDPs.

a. The district court found ample direct evidence of anticompetitive effects, and those findings are not challenged. Merchants are “[d]eprived of any meaningful ability to regulate their own consumption of network services in response to differences in network pricing.” Pet. App. 196a. The result—indeed, Amex’s *intended* result—is that merchants pay “dramatically” higher prices to all four card networks for services than they would but for the rules. *Id.* at 71a. Indeed, U.S. merchants pay among the highest fees to credit card networks in the world. See *supra* p. 6 & n.2.

The NDPs prohibit merchants that accept Amex from engaging in practices that would encourage competition among credit card networks over the price that merchants must pay for their services. Among other things, the anti-steering rules prevent merchants from:

- giving consumers truthful information about the relative costs of their cards;
- indicating or implying, directly or indirectly, that they prefer any other payment products over Amex;
- giving consumers any inducements, such as loyalty points or discounts, for using a different card;
- imposing any restrictions, conditions, disadvantages, or fees that are not imposed equally on all other payment products (except for electronic funds transfer, cash, or check);
- promoting any other payment product (except the merchant's own private-label card that it issues for use solely at the merchant's establishment) more actively than it promotes Amex.

See Pet. App. 95a–96a.

Those provisions constrain interbrand competition not only *with Amex*, but among *all* the card networks. Pet. App. 100a–01a. That is, a merchant that accepts Amex is barred from communicating a preference even between *non-Amex* credit cards. And that remains true notwithstanding that Visa and MasterCard each ceased enforcing *their own* prohibitions against discounting as a result of this litigation.

In the absence of Amex's NDPs, credit card networks would have an incentive to compete on price. Indeed, the district court found that the NDPs' genesis lay in putting an end to such competition. Starting in the late 1980s, for example, Visa

launched a “We Prefer Visa” campaign to encourage competition and consumer preference for its cards. Pet. App. 92a. During the late 1990s, moreover, Discover spotted an opportunity to gain market share from competing card networks amidst “merchant dissatisfaction” over those networks’ fee increases. Pet. App. 204a. Discover intended to “partner with merchants in helping them control payment costs and proposed that they steer customers to the lower-cost Discover cards.” *Ibid.* “Discover representatives * * * met with a number of larger merchants to offer discounts from the network’s already lower prices if they would steer customers to Discover.” *Ibid.*

But Amex would have none of it. It “tightened” its NDPs to nip such competition in the bud. Visa could no longer sustain a campaign built on merchant preference for its cards. And Discover’s efforts at price competition “failed to produce any significant movement in [market] share due to the anti-steering rules” that Amex and the other dominant networks (Visa and MasterCard) maintained at the time. Pet. App. 205a (internal quotation marks omitted). Discover was forced to abandon its low-cost strategy and, predictably, then raised its merchant fees. *Id.* at 206a. Discover’s CEO testified at trial that, as a result of the anti-steering rules, “offering a lower price was not going to give Discover any business benefits.” *Ibid.* (alteration marks omitted). Lowering prices in the absence of meaningful competition was just “leaving money on the table.” *Ibid.* The district court correctly found that “the failure of Discover’s low-price value proposition” to merchants “is emblematic of the harm

done to the competitive process by Amex's rules against merchant steering." *Ibid.*

The district court also found that Amex's NDPs "are responsible for inhibiting the development of several proposed merchant-owned payment solutions." Pet. App. 213a. For example, an effort by forty large retailers to develop a new, lower-cost payment platform ran into hurdles established by the restrictions on merchant steering. *Ibid.* By thus "impeding development of novel payment solutions," the NDPs prevent the "diversification" of the network services industry, which would also "improve the quality of offerings therein." *Id.* at 214a.

b. Consumers who do not use Amex are directly harmed by Amex's supra-competitive fees. The "merchant discount fees" that card networks charge on every credit card transaction are a substantial business expense for almost all merchants. Merchants, like *amici*, testified that they each pay hundreds of millions of dollars each year in credit card fees. In 2013, the four major card networks handled nearly \$2.4 trillion in credit and charge card spending for merchants. Pet. App. 74a. And all indications are that the volume of credit card activity has been increasing ever since. See Nilson Report Issue 1103 (Feb. 2017), <http://bit.ly/2zUVF8V>. Those fees, like other costs of merchant operations, ultimately are imposed on consumers through higher prices, reduced service, or other measures.

All consumers, no matter their method of payment, end up paying the higher prices that result from anticompetitive credit card fees. The district court found that non-Amex cardholders are thus

forced to “subsidiz[e] * * * the cost of the premium rewards conferred by American Express.” Pet. App. 212a. That forced subsidy—from all of a merchant’s customers to a mere subset of them—is not only economically inefficient, but also “highly regressive.” *Ibid.* Amex has a “relatively small, affluent cardholder base.” *Ibid.* But *everyone* pays higher retail prices to fund Amex cardholders’ benefits.

c. Amex cardholders are harmed as well. The anti-steering rules deprive each Amex cardholder of the “chance to decide whether he or she wants to get the rewards for [a] given purchase from the card issuer or whether he or she would rather get some sort of reward from the merchant.” Pet. App. 220a (ellipses omitted). For example, some merchants testified that they would offer incentives, such as rewards points, to customers using less expensive cards. Consumers may very well prefer merchant rewards, but the NDPs deny Amex cardholders that choice (and make their “choice” to get Amex rewards or to get nothing). Such a “restraint that has the effect of reducing the importance of consumer preference in setting price and output is not consistent with th[e] fundamental goal of antitrust law.” *NCAA*, 468 U.S. at 107.

d. The big winner in all of this is, of course, Amex (along with the other credit card networks it has freed from the inconvenience of competition). The district court found that, by preventing any steering among card networks, Amex has “blocked an important safety valve that would have moderated its efforts to increase discount rates [*i.e.*, prices].” Pet. App. 208a. The anti-steering rules have thus “aided the network’s efforts to profitably raise its

discount rates on merchants.” *Ibid.* Merchants have been dissatisfied with these fee increases, but (like most victims of anticompetitive conduct) they have had no choice but to accept them. Tellingly, Amex did not lose a *single* large merchant, and only a tiny handful of medium ones, as a result of its dozen or so significant fee increases between 2005 and 2010. *Id.* at 165a–72a.

Amex has complained that its “current business model” would collapse if exposed to “interbrand competition.” Pet. App. 235a. The antitrust laws were enacted for “the protection of competition,” however, “not competitors” and their preferred business models. *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962). In any event, the district court found that Amex would adapt “to suit a market in which it is required to compete” for both merchants and cardholders. Pet. App. 244a. Amex’s unwillingness to do so is no defense.

It is no surprise, either. The merchant fee increases that the NDPs have made possible have been extraordinarily high and incredibly profitable. For example, Amex’s rate increases just between 2006 and 2010 “resulted in \$1.3 billion in incremental pre-tax income” for Amex. Pet. App. 170a. Those fee hikes, the district court found, were “not paired with offsetting adjustments on the cardholder side of the platform,” and, as a result, “are properly viewed as changes to the net price charged across Amex’s integrated platform.” *Id.* at 166a–67a; see also *id.* at 209a (finding that Amex’s price increases resulted in a “higher net price”). The district court approvingly credited the government’s economist’s observation “that American Express

spends *less than half* of the discount fees it collects from merchants on cardholder rewards.” *Id.* at 209a–10a (emphasis added). Those findings are not challenged on appeal or clearly erroneous. The Second Circuit likewise acknowledged that the “evidence on the record suggests—and Amex conceded at oral argument—that not all of Amex’s gains from increased merchant fees are passed along to cardholders in the form of rewards.” *Id.* at 51a. Much of the premium Amex charges merchants, in the candid words of its CFO, gets “drop[ped]” into profit on Amex’s “bottom line.” *Id.* at 209a.

2. Plaintiffs also established their *prima facie* case by the indirect method. Amex’s significant market power means that the price distortion caused by its NDPs is likely to have anticompetitive effects. Price distortions like those enforced by the NDPs cause market failures. When actors do not bear the full costs of an activity, they will engage in that activity more often than is socially desirable. See, e.g., Baumol & Blinder, *Economics: Principles and Policy* 305–06 (13th ed. 2015). Such distortions “impair[] the ability of the market to advance social welfare by ensuring the provision of desired goods and services to consumers at a price approximating the marginal cost of providing them.” *FTC v. Ind. Fed’n of Dentists*, 476 U.S. 447, 459 (1986). For that reason, “[a]bsent some countervailing procompetitive virtue,” restraints that distort prices “cannot be sustained under the Rule of Reason.” *Ibid.*; accord *NCAA*, 468 U.S. at 107.

Accordingly, even if (counterfactually) the district court had not found *actual* anticompetitive effects of Amex’s conduct, there could hardly be

clearer evidence of the *potential* for those effects than Amex’s elimination of any “incentive for [Amex] or its network competitors to compete with one another by offering merchants a lower price,” and suppression of a “critical form of horizontal, interbrand competition.” Pet. App. 203a. Price is “the central nervous system of the economy,” *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 224 n.59 (1940), and neither Amex nor the Second Circuit has cited any case in which a restraint with the purpose and effect of preventing firms from inducing horizontal price competition has passed muster, let alone failed to support a *prima facie* case of violation.

II. The Second Circuit’s Special Rule For Two-Sided Platforms Condones Anticompetitive Conduct In What Traditional Antitrust Principles Recognize As A Separate Market

After a seven-week trial, the district court found that Amex’s restraint of trade caused price distortions that prevented competition, “dramatically” raised prices for merchants and consumers, erected barriers to market entry, and stifled innovation. Pet. App. 71a, 203a, 210a–11a, 214a. As a result, the burden was properly on Amex to demonstrate that its conduct nevertheless has offsetting procompetitive effects that made it reasonable. See *Cal. Dental Ass’n v. FTC*, 526 U.S. 756, 775 n.12 (1999); *FTC v. Actavis, Inc.*, 133 S. Ct. 2223, 2236 (2013). The district court found that Amex failed to make such a showing; in fact, the court found that the evidence demonstrated that the asserted benefits to cardholders did not offset the anticompetitive effects on merchants and their customers.

The court of appeals, however, crafted a special rule for credit card platforms that ignores how the market actually operates for merchants. By focusing on the interdependency of prices charged on both sides of the platform, it abandoned the traditional approach to market definition grounded in the interchangeability of products and services. After thus expanding the relevant market to encompass the entirety of Amex’s “platform,” the court faulted plaintiffs for not *disproving* the possibility that Amex giveth to cardholders every penny it taketh away from merchants and their customers.

We detail below the absurdity of that special rule—an observation that is best isolated by looking at the market-definition question from the merchants’ vantage point. Prices in *all* markets depend to some degree on prices in other markets. The real question when setting out to determine the relevant market in which a firm may have power is whether other services are available to merchants to substitute for credit card acceptance if (as Amex does here) the card network charges supra-competitive fees. The district court correctly concluded that there is no substitute, thereby properly defining the appropriate market (and explaining why merchant fees have stayed so high for so long).

Analyzing the potential substitutes that merchants might have for credit card acceptance is how courts have defined and should define a market such as this, and nothing about two-sided platforms merits a new and different approach. If Amex’s restraint of competition among card networks for merchants’ sales has pro-competitive effects in some

other part of its business, then the burden was on Amex to prove it.

A. Economic Activity On Each Side Of A Two-Sided Platform Should Not Be Collapsed Into One “Market” For Antitrust Purposes

1. The Second Circuit erred in treating different markets connected by a platform as a single market for antitrust purposes. Ignoring the district court’s factual finding that merchants and cardholders are in different markets, the Second Circuit determined that, as a matter of law, the relevant market had to encompass both merchants *and* cardholders because they are “equally important and interdependent sets of consumers” and that the price charged each group affects “the optimal level” of price to charge the other. Pet. App. 50a. A common-sense application of the antitrust laws, and decades of settled doctrine, establish otherwise.

This Court has long held that a “market is composed of products that have reasonable interchangeability for the purposes for which they are produced.” *Int’l Boxing Club of N.Y., Inc. v. United States*, 358 U.S. 242, 250 (1959). The reason, other courts have explained, is that it is “the ability of consumers to turn to other suppliers [that] restrains a firm from raising prices above the competitive level.” *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 218 (D.C. Cir. 1986) (Bork, J.).

The question, then, is to what substitute can a merchant turn if Amex raises its price above a competitive level. There is no dispute that they could

turn to other credit card networks (Visa, MasterCard, and Discover). So those networks undoubtedly provide services to merchants in the same market as Amex.⁵

But how could the services that Amex provides to its cardholders be a substitute for the services it provides to merchants? A merchant facing a fee increase from Amex cannot swap out its acceptance of Amex cards for the services Amex provides to “Mary Johnson, cardholder since 1998.” Even if the *prices* that Amex charges users on each side of its platform are *interdependent*—and that has not been established—the *services* are not *interchangeable*.

That is the lesson of this Court’s holding in *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594 (1953). That decision recognized that newspapers are “dual trader[s] in separate though interdependent markets.” *Id.* at 610. They sell “the paper’s news and advertising content to its readers; in effect that readership is in turn sold to the buyers of advertising space.” *Ibid.* But this Court recognized that the case before it “concern[ed] solely one of these markets,” and had no qualms about analyzing defendants’ market position solely by reference to its “dominance in the advertising market, not in readership.” *Ibid.* The mere fact that prices in the two connected markets were “interdependent” did not collapse them into a single market. *Ibid.*

⁵ The district court evaluated whether debit cards could substitute for credit cards and thereby “temper an exercise of market power” by credit card networks, and found they could not. Pet. App. 124a.

The “indisputable proposition[.]” that substitutability is what tempers market power explains why courts, the Department of Justice, and the Federal Trade Commission have long employed the so-called “hypothetical monopolist test” to define markets. See 2B Areeda & Hovenkamp, *Antitrust Law* ¶ 536, at 302 (4th ed. 2014). Under that test, if a hypothetical monopolist could impose “a small, but significant non-transitory increase in price (‘SSNIP’)” in a proposed market “without losing so many sales to other products as to render the SSNIP unprofitable, then the proposed market is the relevant market.” Pet. App. 37a. Amex’s successful implementation of its Value Recapture campaign *demonstrates*—and not at all hypothetically—that it has and does profitably impose price increases on merchants without losing enough business to render the move unprofitable. The services that credit card networks provide cardholders did not constrain Amex’s ability to significantly raise prices on merchants, demonstrating that Amex’s different services are provided in different markets.

Also unavailing is Amex’s “one product, one market” argument. In Amex’s view, it produces “credit card transactions” paid for by both merchants and cardholders. Amex indisputably faces two different groups of consumers that ask it for different things, and pay different prices in different ways for those things. The fact that Amex’s business consists of pairing two distinct sets of customer groups does not require collapsing the distinct markets in which Amex operates.

2. The developing economics literature on two-sided and multi-sided “markets” does not displace

this Court’s approach to market definition and the principles underlying it. Indeed, some of that literature is careful to acknowledge that it uses “[t]he term ‘market’ * * * loosely” and not “how that term is often used in antitrust.” Evans & Schmalensee, *Markets With Two-Sided Platforms*, 1 *Issues in Competition L. & Pol’y* 667, 668 (2008). Nothing about a platform’s “two-sidedness” undermines why this Court has looked to the interchangeability of goods and services to define antitrust markets. It is the ability to substitute that tempers any monopolist’s attempt to exercise market power. See *Int’l Boxing Club*, 358 U.S. at 250; *Rothery Storage*, 792 F.2d at 218.

What is more, economists do not agree on what two-sidedness actually entails. See Hagiu & Wright, *Multi-Sided Platforms*, 43 *Int’l J. Indus. Org.* 162, 163 (2015) (“[T]here is disagreement among those in the literature about what constitutes an appropriate definition.”). Definitions of a two-sided platform advanced by authorities in the field include:

- An intermediary that “can affect the volume of transactions by charging more to one side of the [platform] and reducing the price paid by the other side by an equal amount.” Rochet & Tirole, *Two-Sided Markets: A Progress Report*, 37 *RAND J. Econ.* 645, 664–65 (2006).
- An intermediary that serves “two or more groups of customers”; “who need each other”; “who cannot capture the value from their mutual attraction”; and “rely on [a] catalyst to facilitate value-creating interactions.” Evans & Schmalensee, *The Antitrust Analysis of Multisided Platform Businesses*, in 1 *The Oxford*

Handbook of International Antitrust Economics 404, 409 (Blair & Sokol eds., 2014).

- A platform that, in addition to “other requirements,” “enable[s] direct interactions” between two sides that must be “affiliated with the platform.” Hagiú & Wright, *supra*, at 163.

A recent article “document[ing] serious conceptual divergences” in the literature on two-sided markets includes an appendix comparing how different prominent definitions of the concept affect which industries count as two-sided—with markedly divergent results. See Auer & Petit, *Two-Sided Markets and the Challenge of Turning Economic Theory into Antitrust Policy*, 60 *Antitrust Bul.* 426, 427, 458–61 (2015).

Indeed, under a sufficiently broad concept of “two-sidedness” a court could find it to “exist in practically all markets.” Rysman, *The Economics of Two-Sided Markets*, 23 *J. Econ. Perspectives* 125, 127 (2009). For example, “the market for autos could be viewed as two-sided because manufacturers must attract both consumers and mechanic expertise.” *Ibid.*

Or take retailers: it could even be said that “a conventional retailer” operates a two-sided platform under broad-enough definitions of the term. Carlton & Winter, *Vertical MFN’s and the Credit Card No-surcharge Rule*, at 39 (June 6, 2017), <http://bit.ly/2mcYNKa>. After all, retailers facilitate interaction between manufacturers and end consumers. Neither manufacturers nor end consumers would transact with retailers if the other group did not do so. Manufacturers, moreover, can be

said to pay a “negative price” to the retail “platform” for the service of bringing customers to their wares, while customers pay the bulk of the “net price.” And yet few people would say that retailers sell “transactions in goods” at a “net price” to manufacturers and end users. Rather, retailers effectively provide shelf space to manufacturers and sell goods to customers in two separate but interdependent markets.

The same thought experiment can be run on just about *any* market that involves pairing inputs from two or more distinct groups. Sorting out which industries must be treated as multi-sided platforms meriting a special rule and which are subject to traditional antitrust principles would be as complicated as it is unwarranted. The parties do not agree, for example, on whether newspapers or the NCAA constitute multi-sided platforms. Compare *Pet. 21–23*, with *Amex Opp. 18–19*.

Courts should not be required to resolve such esoteric questions to resolve otherwise straightforward antitrust cases. Judges faced, as here, with clear evidence of anticompetitive conduct and effect need not “ramble through the wilds of economic theory” to decide whether plaintiffs have made out a *prima facie* case. *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 609 n.10 (1972).

B. Amex Did Not Carry Its Burden To Demonstrate Any Procompetitive Effects Of Its NDPs

1. In whatever way the market is defined here, once plaintiffs demonstrated the anticompetitive effects of Amex’s NDPs—higher merchant fees,

higher prices for goods and services, etc.—the burden shifted to Amex to demonstrate that its restraint of trade had offsetting procompetitive effects. The district court correctly found that Amex could not carry that burden.⁶

That is how burden-shifting works under the traditional rule-of-reason analysis. “Once the plaintiff satisfies its initial burden to prove anticompetitive effects, the burden shifts to the defendant to offer evidence of any procompetitive effects of the restraint at issue.” Pet. App. 28a. The courts of appeals all apply a version of this framework,⁷ and this Court has found no cause to disturb it. See, e.g., *Cal. Dental Ass’n.*, 526 U.S. at 775 n.12; *Actavis*, 133 S. Ct. at 2236. Here, Amex proposed two procompetitive justifications for its conduct, but the district court found that neither “offset * * * the more widespread and injurious

⁶ More than that, the district court found that the evidence pointed *in the opposite direction*. Amex’s unsuccessful attempt to provide a procompetitive justification for restricting interbrand competition only “highlight[ed]” that “Amex’s current business model could not survive if exposed to the full spectrum of interbrand competition.” Pet. App. 235a. That is, Amex’s model depends on the anticompetitive effects it has baked into the market via its NDPs.

⁷ See, e.g., *Suture Express, Inc. v. Owens & Minor Distribution, Inc.*, 851 F.3d 1029, 1038 (10th Cir. 2017); *O’Bannon v. NCAA*, 802 F.3d 1049, 1070 (9th Cir. 2015); *King Drug Co. of Florence v. Smithkline Beecham Corp.*, 791 F.3d 388, 412 (3d Cir. 2015); *Schering-Plough Corp. v. FTC*, 402 F.3d 1056, 1065 (11th Cir. 2005); *Craftsmen Limousine, Inc. v. Ford Motor Co.*, 491 F.3d 380, 389 (8th Cir. 2007); *Nat’l Hockey League Players’ Ass’n v. Plymouth Whalers Hockey Club*, 325 F.3d 712, 718 (6th Cir. 2003).

effects of the NDPs on interbrand competition in the relevant market.” Pet. App. 229a.

The court of appeals did not dispute the district court’s factual findings on the NDPs’ various anticompetitive effects on merchants and consumers. But instead of leaving the burden to Amex (where it belongs), the court concluded that *plaintiffs* needed to *disprove* that any procompetitive effects on the cardholder side of Amex’s business outweighed the anticompetitive effects on the merchant side.

That is wrong. For starters, the court of appeals’ rationale runs counter to the basic precept that competition “cannot be foreclosed with respect to one sector of the economy because * * * such foreclosure might promote greater competition in a more important sector of the economy.” *Topco Assocs.*, 405 U.S. at 610. But even if it *could* be welfare-maximizing to restrain competition in one market for the benefit of competition in another, “courts are ill-equipped and ill-situated for such decisionmaking.” *Id.* at 611; see also *United States v. Phila. Nat’l Bank*, 374 U.S. 321, 370 (1963) (rejecting that “anticompetitive effects in one market could be justified by procompetitive consequences in another”). How is a court supposed to determine the number of airline miles awarded to cardholders that justify higher fees to merchants (and higher prices to all their customers)? Such an apples-to-oranges comparison across different “sides” of a business “platform” is “beyond the ordinary limits of judicial competence.” *Id.* at 371. Even Amex could not articulate a way to calculate a net price across both sides of the platform. Pet. App. 182a–86a, 209a.

So while Amex may prefer to restrict competition on the merchant side of its platform in order to manufacture resources with which to compete for cardholders, that is not a choice it gets to make. “[U]nder antitrust policy *competition* should choose the optimal mix of revenue as between the two sides.” Areeda & Hovenkamp ¶ 562e, at 101 (Supp. 2017); see also *Nat’l Soc’y of Prof’l Eng’rs*, 435 U.S. at 695 (“The Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services.”).

Even if Amex could conceivably justify the anticompetitive effects of its conduct on merchants and consumers by pointing to the rewards and other benefits it offers cardholders, there is every reason to put the onus on Amex to do so. Burdens are “traditionally * * * placed on the party having the readier access to knowledge about the fact in question.” James et al., *Civil Procedure* 421 (5th ed. 2001). Such information-forcing rules improve decisionmaking by “provid[ing] an incentive for the party with the best access to private information to disclose it.” Reinert, *Pleading as Information-Forcing*, 75 L. & Contemp. Prob. 1, 29 (2012).

Amex has designed and operates a business with two distinct groups of customers, and with complicated pricing structures on each side. “The defendant, being the author of the restraints, is in a better position to explain why they are profitable and in consumers’ best interests.” Areeda & Hovenkamp ¶ 1507, at 171 (Supp. 2017). By enacting a special rule for two-sided platforms, the decision below

unwisely departs from that long-settled, common-sense approach.

III. Reversal Will Encourage Competition And Enhance Consumer Welfare

The decision below should be reversed. Amex did not challenge the district court's findings of fact, but rather asserted that those findings were legally insufficient to sustain Plaintiffs' *prima facie* Section 1 case. See Amex C.A. Br. 37–83. But they are enough, and that should end the matter. Merchants and their customers eagerly await their long-incoming relief from Amex's anticompetitive conduct.

Reversing the decision below will, in addition to respecting settled antitrust principles, yield significant pro-competitive results for consumers nationwide. Amex's conduct fundamentally distorts the competitive process. On the merchant side, Amex has prevented other card networks from competing on price. On the cardholder side, Amex prohibits consumers from receiving truthful information and the price signals that they would ordinarily receive in a competitive market. The inefficient result is that an economically rational cardholder *should* prefer Amex and free-ride off the resulting higher prices for goods and services paid by all consumers.

The Sherman Act, as “the Magna Carta of free enterprise,” outlaws such anticompetitive and distortionary conduct. *Topco Assocs.*, 405 U.S. at 610. Retailers and consumers should benefit from the “unrestrained interaction of competitive forces” in the market for credit card services, which “will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest

material progress.” *N. Pac. Ry. Co. v. United States*, 356 U.S. 1, 4 (1958).

The district court found that enjoining Amex’s NDPs would “inure to the benefit of both merchants and customers alike.” Pet. App. 214a. Accordingly, “merchants actually are likely to steer customers between various forms of payment,” for example, by offering free shipping, discounts, or a faster check-out line for using a cheaper payment card. *Id.* at 221a. And even if not all merchants exercise that new-found freedom, “[p]roviding merchants the freedom to participate in their customers’ payment decisions will * * * restore downward pressure on [credit card networks] merchant prices.” *Id.* at 216a.

Merchants, in turn, “will pass along some amount of the savings associated with declining swipe fees to their customers in the form of lower retail prices.” Pet. App. 220a. And whatever merchants do not pass on in cost decreases, they would pass on in quality improvements. Indeed, merchants would have to do so because they, unlike the credit card networks, operate in a highly competitive market and, in such a market, “all elements of a bargain—quality, service, safety, and durability—and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers.” *Nat’l Soc’y of Prof’l Eng’rs*, 435 U.S. at 695.

Finally, given the extended reach of the credit card industry, any such improvements have far-reaching potential. Credit cards today are ubiquitous in modern life, and one need only ask someone under the age of 25 to pay with cash or (dare we say) a personal check, to see that trend-line rising. And as

we move ever closer to a purely electronic economy the opportunities and incentives for those with market power to throttle competition will be manifold. This Court should not invite such abuses.

CONCLUSION

The decision below should be reversed.

Respectfully submitted.

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