



U.S. v. Amex

*New York State Bar Association
Antitrust Section – Executive Committee*

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October 19, 2016

Case Timeline

- » Oct. 4, 2010: DOJ sues Amex, Visa, & MasterCard in EDNY
 - Case challenged nondiscrimination provisions (NDPs) that prohibit merchants from encouraging consumers to use lower-cost forms of payment
 - DOJ settled immediately with Visa and MasterCard, which agreed not to block merchant steering
- » July 7, 2014: Trial commences before Judge Garaufis
 - 7-week trial; over 30 fact witnesses; four experts; over 1,000 exhibits introduced into evidence
- » Feb. 19, 2015: Judge Garaufis releases decision for the DOJ
- » Apr. 30, 2015: Judge Garaufis enters injunction against Amex
 - June 16, 2015: Second Circuit denies stay of injunction
- » Dec. 17, 2015: Second Circuit hears oral argument
 - Dec. 18, 2015: Second Circuit stays injunction
- » Sept. 26, 2016: Second Circuit reverses Judge Garaufis' decision and remands case with instruction to enter judgment for Amex

Judge Garaufis' Decision

88 F. Supp. 3d 143 (E.D.N.Y. 2015)

- » Engaged in full rule-of-reason analysis to find that Amex's NDPs violated § 1 of the Sherman Act
 - Indirect path: market power plus
 - General purpose card network services market (as in *U.S. v. Visa*)
 - 26 percent share in market with high barriers to entry *plus* insistence *plus* Value Recapture evidence established market power
 - Direct path: actual adverse effect
 - NDPs harmed interbrand competition by eliminating any incentive for credit card networks to lower prices to attempt to increase transaction volume
- » Decision purported to account, at each stage of the analysis, for two-sided features of the market

Second Circuit Decision

» Market Definition

- Wrong for Judge Garaufis to pattern relevant market inquiry after *U.S. v. Visa*
 - Focusing on provision of network services to merchants misses platform-wide effects of Amex's NDPs
 - *Visa* addressed horizontal restraints; *Amex* considered vertical restraints
- Judge Garaufis improperly applied the Hypothetical Monopolist Test
 - He didn't apply the test to define the market; he only used it to determine whether debit card network services were part of the relevant market
 - Analysis failed to consider feedback effect on cardholder side of platform following any degree of merchant attrition

Second Circuit Decision

» Market Power

- Value Recapture not evidence of market power
 - Focus on the merchant side of the platform missed benefits to the cardholder side and the impact on output and value of the network
 - Error for Judge Garaufis to exclude evidence offered by Amex of two-sided prices that incorporated fully Amex's payments on the cardholder side
- Insistence cannot be a source of market power
 - Insistence reflects Amex's investments on the cardholder side of the platform, which bring value to merchants
 - "A firm that can attract customer loyalty only by *reducing* its prices does not have the power to *increase* prices unilaterally"
 - 3 million merchants do not accept Amex; belies suggestion that merchants cannot drop Amex
 - "No monopolistic purpose" in NDPs because they prevent a merchant from advertising Amex acceptance, attracting "high-end clientele," but then steering consumers to other cards

Second Circuit Decision

» Actual Adverse Effects on Competition

- Evidence of harm to merchants doesn't establish "adverse effect on competition as a *whole* in the relevant market"
 - DOJ could have shown (but failed to show) that there were fewer card transactions, that quality had diminished, or that Amex's pricing was supracompetitive
- Increase in credit card use (output) "indicative of a thriving market for credit-card services" and that Amex and its NDPs "*increased* rather than *decreased* competition overall within the credit card industry"

Second Circuit Decision

» Takeaways

- Antitrust immunity for vertical restraints in two-sided markets?
- Impact on challenges to other steering restrictions?
 - In June 2016, DOJ filed case challenging anti-steering provisions maintained by the Carolinas Healthcare System that block insurance companies from incentivizing patients to use other hospitals' less-expensive services
 - Defendant last week brought *Amex* decision to district court's attention
- Impact on willingness of DOJ to pursue major conduct investigations and litigation?

Second Circuit Decision

Two-sided Prices

- » Second Circuit: “The District Court erred in concluding that ‘increases in *merchant* pricing are properly viewed as changes to the net price charged across Amex’s integrated platform,’ *Am. Express Co.*, 88 F. Supp. 3d at 196 (emphasis added), because merchant pricing is only one half of the pertinent equation.”
- » Judge Garaufis: “**Because these Value Recapture initiatives were not paired with offsetting adjustments on the cardholder side of the platform**, the resulting increases in merchant pricing are properly viewed as changes to the net price charged across Amex’s integrated platform.”
 - Value Recapture price increases were profitable for Amex
 - No “reliable measure” of two-sided prices, but circumstantial and expert evidence of “higher net price”
- » Second Circuit: “Because Plaintiffs provided neither ‘a reliable measure of [Amex’s] per transaction margins,’ . . . nor ‘a reliable measure of [Amex’s] two-sided price that appropriately accounts for the value or cost of the rewards paid to cardholders,’ . . . they failed to meet their burden to show anticompetitive effects directly.”

Second Circuit Decision

Harm to the Competitive Process?

- » Can proving harm to the competitive process establish actual anticompetitive effects?
 - *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 461-62 (1986): Practice “likely enough to disrupt the proper functioning of the price-setting mechanism of the market” condemned “even absent proof that it resulted in higher prices”
- » Judge Garaufis found that Amex’s NDPs harmed the competitive process:
 - “[B]y disrupting the price-setting mechanism ordinarily present in competitive markets, the NDPs reduce [networks’ incentives] to offer merchants lower discount rates and, as a result, they impede a significant avenue of horizontal interbrand competition in the network services market.”
 - “[T]he NDPs represent a decision made by [Amex] on behalf of all participants in the network services market that networks will not compete . . . by lowering their merchant pricing; rather, by suppressing competition on the merchant side of the GPCC platform, Amex has effectively compelled its rival networks and their issuing partners to focus their competitive efforts on cardholders. . . . Yet not all networks necessarily prefer to compete primarily on the cardholder side of the platform. . . . [Amex’s NDPs] deny other firms the ability to differentiate themselves on the basis of their merchant pricing.”

Second Circuit Decision

Insistence

- » “The District Court’s finding that cardholder insistence ‘effectively prevents merchants from dropping American Express,’ . . . ignores the fact that roughly one-third of credit-card accepting merchants in the United States currently do not accept Amex. As explained by the economist *amici*, ‘[t]here is no meaningful economic difference between “dropping American Express” . . . and a decision not to accept American Express in the first place.’”
 - Implies reasonable interchangeability for many merchants between acceptance and non-acceptance (and lack of market power over merchants)
 - Judge Garaufis found that Amex’s acceptance gap “is largely a product of its own business decisions”