**Fifth Annual Supreme Court Webinar: Cases of Significance to Business**

**November 8, 2017**

***Ohio v. American Express Co.***

Case Summary by Timothy Taylor

**1. Case information.**

*Ohio v. American Express Co.*, No. 16-1454

* *cert. granted* Oct. 16, 2017
* *oral argument schedule:* TBD

Opinions below:

* *United States v. American Express Co.*, 838 F.3d 179 (2d Cir. 2016)
* *United States v. American Express Co.*, 88 F. Supp. 3d 143 (E.D.N.Y. 2015)

**2. Question presented.**

Credit-card networks compete in two markets simultaneously: the market for cardholders and the market for merchants. American Express (Amex) bars Amex-accepting merchants from encouraging customers to use other credit cards, which may charge the merchants lower fees. The government proved that Amex’s nondiscrimination agreements had anticompetitive effects in the merchant market. But under the rule of reason, was the government also required to prove as part of its prima facie case that those anticompetitive effects outweighed any benefits in the cardholder market?

**3. Background.**

The credit-card industry operates in a “two-sided market,” in which competing credit-card networks must both attract merchants to accept their cards and attract consumers to use their cards.[[1]](#footnote-1) This is a balancing act. If a credit-card network’s merchant prices are too high, then merchants will not accept the card and customers will not use it because the network is too small.[[2]](#footnote-2) But if a credit-card network’s merchant prices or fees to cardholders are too low, then the network cannot fund the points and perks customers expect.[[3]](#footnote-3)

Amex positions itself on this continuum as a prestige credit-card network.[[4]](#footnote-4) It generates most of its revenue from merchant fees rather than credit-card interest (the Visa and MasterCard model), but it attracts merchants all the same by delivering “marquee” cardholders who spend more—and who expect a more robust menu of benefits from Amex.[[5]](#footnote-5)

Visa and MasterCard took market-share from Amex in the 1990s by highlighting Amex’s limited merchant network.[[6]](#footnote-6) You may remember the catchy slogans, “Visa: It’s Everywhere You Want To Be” and “For Everything Else, There’s MasterCard.” Amex responded by strengthening the nondiscrimination provisions in its merchant contracts, which essentially forbid its merchants from indicating that they prefer any form of payment over MasterCard.[[7]](#footnote-7) These nondiscrimination provisions, and other networks’ similar restraints, “aim to increase cardholders’ certainty as to whether [a network’s] cards will be accepted and on what terms.”[[8]](#footnote-8) Without them, the card networks would have more difficulty balancing their two-sided net price—the amounts charged to cardholders versus merchants.

**4. Procedural history.**

In 2010 the United States and 17 states[[9]](#footnote-9) sued Amex, Visa, and MasterCard for unreasonably restraining trade in violation of § 1 of the Sherman Act. They alleged that the credit-card networks’ nondiscrimination provisions propped up card fees, blocked competition from other networks, and prevented merchants from encouraging use of cheaper or otherwise preferred cards.[[10]](#footnote-10) In 2011 Visa and MasterCard entered consent judgments and have since rescinded their nondiscrimination provisions.[[11]](#footnote-11) But Amex proceeded in 2014 to a seven-week bench trial. It lost. The district court made three key findings:

1. That card networks operate in two interrelated markets, for cardholders and for merchants, but the only relevant market for this case was the merchant market;
2. That Amex possesses sufficient market power in the merchant market to prevent merchants from dropping Amex when faced with price increases; and
3. That Amex’s nondiscrimination provisions are anticompetitive: they “short-circuit the ordinary price-setting mechanism … by removing the competitive ‘reward’ for [card] networks offering merchants a lower price ….”[[12]](#footnote-12) They also raise prices for merchants, who then pass on those higher costs to consumers.[[13]](#footnote-13)

The Second Circuit on review first described the legal framework. Restraints of trade are analyzed under the three-part “rule of reason” (except for purely collusive price-fixing or market division, which are per se illegal).[[14]](#footnote-14) “*First*, a plaintiff bears the initial burden of demonstrating that either (i) a defendant’s challenged behavior ‘had an *actual* adverse effect on competition as a whole in the relevant market’”[[15]](#footnote-15) or (ii) the defendant had market power “plus some other ground for believing that the challenged behavior could harm competition in the market.”[[16]](#footnote-16) *Second*, if the plaintiff satisfies its burden, “the burden shifts to the defendant to offer evidence of any competitive effects of the restraint at issue.”[[17]](#footnote-17) *Third*, if the defendant provides that proof, then “the burden shifts back to the plaintiff to prove that any legitimate competitive benefits offered by defendant could have been achieved through less restrictive means.”[[18]](#footnote-18)

The Second Circuit held that each of the district court’s three findings were in error. *First*, the district court erred by “excluding the market for cardholders from its relevant market definition.”[[19]](#footnote-19) This was error because the merchant and cardholder markets are interdependent.[[20]](#footnote-20)

*Second,* the district court erred by holding that Amex had “sufficient market power to affect competition adversely in the relevant market.”[[21]](#footnote-21) The district court focused on an Amex price-increase program in the 2000s, with little merchant attrition.[[22]](#footnote-22) But the district ignored the other half of the equation: a possible price decrease for cardholders, which would mean more cardholders coming to those merchants.[[23]](#footnote-23) And it is Amex cardholders’ loyalty (which is only as good as the benefits financed by the fees) that makes it worthwhile for merchants to pay Amex’s relatively high fees.[[24]](#footnote-24) (This aspect of the Second Circuit’s ruling has not been challenged.)

*Third*, the district court erred by holding that, even though “it had no ‘empirical evidence that [Amex’s] NDPs have resulted in a higher two-sided price,’” “[p]roof of anticompetitive harm to *merchants, the primary consumers* of [Amex’s] network services, is sufficient to discharge Plaintiffs’ burden in this case.”[[25]](#footnote-25) “Because the NDPs affect competition for cardholders as well as merchants, the Plaintiffs’ initial burden was to show that the NDPs made *all* Amex consumers on both sides of the platform—*i.e.*, both merchants and cardholders—worse off overall.”[[26]](#footnote-26) “Without evidence of the net price affecting consumers on both sides of the platform, the District Court could not have properly concluded that a reduction in the merchant-discount fee would benefit the two-sided platform overall.”[[27]](#footnote-27) Thus the plaintiffs failed to carry their initial burden of proving a § 1 violation, either directly or indirectly.[[28]](#footnote-28)

**5. Arguments.**

The parties have not yet filed their merits briefs, so the arguments below come from their certiorari-stage briefs.

**The petitioner States.** The petitioners, 11 of the states who lost below,[[29]](#footnote-29) argue that the Second Circuit’s decision conflicts with the “general antitrust guidance” of the Supreme Court.[[30]](#footnote-30) The petitioners first dispute the Second Circuit’s holding that the district court should have considered both sides of the credit-card network—merchants *and* cardholders. They maintain that a market is made up of goods or services that are “reasonably interchangeable,”[[31]](#footnote-31) but services to cardholders and merchants are not. They may be interdependent, but that does not make them part of the same market.[[32]](#footnote-32) For instance, a newspaper makes money from both advertisers and readers, but the Supreme Court has treated those customers as separate markets.[[33]](#footnote-33) And the government did not need to show how the NCAA’s restrictions on televising college football games affected live viewership—it was enough to show that the restrictions raised the price of broadcasting games.[[34]](#footnote-34)

The petitioners also argue that the Second Circuit misunderstood the government’s burden of proof. “With the market defined to include cardholders, the Second Circuit held, the Government bore the initial burden to prove that any anticompetitive effects caused on the prices for merchants (and their consumers) were not offset by any alleged countervailing benefits to Amex cardholders. This reasoning effectively collapsed the staggered rule-of-reason framework into a single, all-encompassing step.”[[35]](#footnote-35) The petitioners do not do much more to develop that argument, citing a few snippets of Supreme Court case law that simply rehearse the rule-of-reason framework. This is surprising, given the petitioners’ emphasis on this point in their version of the question presented.

The petitioners also offer some policy reasons for favoring their position. They state that credit-card network’s nondiscrimination provisions prevent merchants from responding to merchant-fee increases, except by dropping a card network altogether.[[36]](#footnote-36) This means that the credit-card networks can charge higher fees than they would otherwise be able to do.[[37]](#footnote-37) And those higher fees are passed on to *all* consumers—which means that a high-fee/high-reward model like Amex’s free-rides on the expenditures of others.[[38]](#footnote-38)

**Respondent Amex.** Amex argues, of course, that the Second Circuit was correct. Amex first argues that the Second Circuit defined the market correctly. The credit-card networks ultimately compete not for merchants or cardholders but transactions: “A merchant and a cardholder cannot complete a transaction unless they use the same card network. Only the combination of Amex’s services to merchants and cardholders together competes with Visa’s similar offering.”[[39]](#footnote-39) That makes the credit-card market truly two-sided, unlike the newspaper business—where readers buy newspapers for the news, not the ads—or football broadcasts—which is just a classic vertical distribution from college to television network to viewer.[[40]](#footnote-40)

Amex also argues that the Second Circuit correctly held that the government failed to meet its initial burden of proof. “[B]oth courts below agreed that the record could not support a finding that Amex’s prices were supracompetitive, when accounting for both sides.”[[41]](#footnote-41) Which makes Amex’s argument on this issue a branch of its first argument: “The service that Amex competes to provide is completing payment transactions between a cardholder and a merchant—a service for which neither has any use unless the other does. Thus, Petitioners’ argument that a court need not account for cardholders is an invitation to misdefine the competition at issue.”[[42]](#footnote-42)

Amex also briefly addresses the petitioners’ policy arguments. Amex states that even if a vertical restraint, like a nondiscrimination provision, affects the prices set by the market, that is not necessarily a problem. All vertical restraints *restrain* competition; the question is whether they *harm* competition, a question whose answer is too unclear in this case to be the basis of any surefooted judicial decision-making.[[43]](#footnote-43)

**The United States.** The United States opposed granting certiorari because, in its view, the case did not conflict with a decision of the Supreme Court or another court of appeals, the scope of the Second Circuit’s ruling was unclear, and the types of nondiscrimination agreements involved in the case have been the subject of little case-law development thus far.[[44]](#footnote-44)

With that said, the United States agrees with the petitioner States that the Second Circuit’s decision was wrong. Like the States, the United States argues that the district court properly defined the market, because a market is made up of goods or services that can be substituted for one another, but cardholder services are no substitute for merchant services.[[45]](#footnote-45) And that merchant market is not functioning efficiently: card networks can raise merchant fees just to the point where the merchants would reject the use of cards altogether; but this raises prices for all consumers, meaning cash-using consumers effectively subsidize cardholders, and Amex cardholders most of all.[[46]](#footnote-46) The Second Circuit thus erred in holding that the United States was required to prove initially that Amex’s nondiscrimination provisions raised prices for Amex cardholders as well: proof of increased prices on the merchant side was sufficient.[[47]](#footnote-47)

**6. Highlights from the amici.**

* A group of grocery-store and drug-store chains—including Albertsons, CVS, Kroger, Meijer, Safeway, and Walgreens—who assert that credit-card fees “are among [their] largest and fastest-growing expenses,”[[48]](#footnote-48) highlight the fact that Professor Herbert Hovenkamp, an antitrust scholar liberally cited in the briefs and opinions in this case, believes the Second Circuit was incorrect. “[T]he court failed to see … that under antitrust policy competition should choose the optimal mix of revenue as between the two sides, an issue obfuscated by the incorrect finding that these two elements of revenue were within the same antitrust market.”[[49]](#footnote-49)
* A retailer association raises the interesting point that the Supreme Court held earlier this year (2017) that a state law barring merchants from charging higher prices to card-using customers implicates the First Amendment, yet Amex’s nondiscrimination provisions prevent merchants from stating anything to consumers about card fees.[[50]](#footnote-50)
* All of the eight amicus briefs support the petitioner States’ positions. (Time will tell whether the weight of amici will shift at the merits stage.)
* Many of the amicus briefs emphasize the economic importance of the case. Credit-card transactions now amount to more than $3 trillion per year and are growing rapidly as consumers spend more online and less in store and use phone apps like Apple Pay. They are one of the single largest items of cost for many merchants, even though the costs to the credit-card networks of providing services has dropped.

**7. Implications.**

The *Amex* case will provide new guidance to actors in two-sided markets—markets which are rapidly growing because of information-technology’s ability to bring actors together at a low cost. Ride-share services like Uber and Lyft; dating services like OkCupid and Tinder; buy-sell platforms like Amazon, eBay, and StubHub; and any other platform that matches users could be affected.

The *Amex* case will also affect the credit-card industry, and thereby nearly all of us. An amicus brief authored by the credit-card network Discover suggested that allowing merchants to discriminate among cards would allow Wal-Mart to have a quicker Discover-only checkout line or offer a discount on prescriptions if paid by Discover card. It is just as easy to picture an Internet checkout screen where the price changes slightly in response to your credit-card information.

Finally, the *Amex* case may provide additional guidance on the rule-of-reason’s burden-shifting framework. The briefs devoted less attention to this question, but the Supreme Court could further develop its doctrine on what an antitrust plaintiff must prove as part of its initial burden.

1. *See United States v. Am. Express Co.*, 838 F.3d 179, 185–86 (2016). [↑](#footnote-ref-1)
2. *See id.* at 186. [↑](#footnote-ref-2)
3. *See id.* [↑](#footnote-ref-3)
4. *See id.* at 189. [↑](#footnote-ref-4)
5. *Id.* [↑](#footnote-ref-5)
6. *Id.* at 190. Amex describes this move as “campaigns to sow doubts in the minds of cardholders” designed to “‘break[]’ the premium ‘success cycle.” Amex’s Opp’n to Pet’n for Writ of Cert. at 6, *Ohio v. Am. Express Co.*, No. 16-1454 (August 2017). [↑](#footnote-ref-6)
7. *See id.* at 191. [↑](#footnote-ref-7)
8. *Id.* at 191–92. [↑](#footnote-ref-8)
9. Arizona, Connecticut, Idaho, Illinois, Iowa, Maryland, Michigan, Missouri, Montana, Nebraska, New Hampshire, Ohio, Rhode Island, Tennessee, Texas, Utah, and Vermont. Hawaii also sued but dropped its claims without prejudice before trial. *See id.* at 192 & n.40. [↑](#footnote-ref-9)
10. *See id.* at 192. [↑](#footnote-ref-10)
11. *See id.* [↑](#footnote-ref-11)
12. *Id.* (quoting *United States v. Am. Express Co.*, 88 F. Supp. 3d 143, 150 (E.D.N.Y. 2015)). [↑](#footnote-ref-12)
13. *See Am. Express*, 88 F. Supp. 3d at 216–17. [↑](#footnote-ref-13)
14. *See Am. Express*, 838 F.3dat 193–94. [↑](#footnote-ref-14)
15. *Id.* at 194 (emphasis added) (quoted source omitted). [↑](#footnote-ref-15)
16. *Id.* at 195 (quoted source omitted); *see id.* at 200 (“Market power is the power to force a purchaser to do something that he would not do in a competitive market.” (quoted source omitted)). [↑](#footnote-ref-16)
17. *Id.* [↑](#footnote-ref-17)
18. *Id.* (brackets and quoted source omitted). [↑](#footnote-ref-18)
19. *Id.* at 197. [↑](#footnote-ref-19)
20. *See id.* at 200. [↑](#footnote-ref-20)
21. *Id.* (citation omitted). [↑](#footnote-ref-21)
22. *See id.* at 201–02. [↑](#footnote-ref-22)
23. *See id.* at 202. [↑](#footnote-ref-23)
24. *See id.* at 203. [↑](#footnote-ref-24)
25. *Id.* at 204 (quoting *American Express*, 88 F. Supp. 3d at 208, 215 (emphasis added)). [↑](#footnote-ref-25)
26. *Id.* at 205. [↑](#footnote-ref-26)
27. *Id.* at 206. [↑](#footnote-ref-27)
28. *See id.* at 207. [↑](#footnote-ref-28)
29. Connecticut, Idaho, Illinois, Iowa, Maryland, Michigan, Montana, Ohio, Rhode Island, Utah, and Vermont. *See* Pet’n for Writ of Cert., *Ohio v. Am. Express Co.*, No. 16-1454 (June 2017). Ohio took the lead on the brief. Some states did not join appeal to the Supreme Court: Arizona, Missouri, Nebraska, New Hampshire, Tennessee, and Texas. [↑](#footnote-ref-29)
30. *Id.* at 18. [↑](#footnote-ref-30)
31. *Id.* at 19 (quoting *United States v. Grinnell Corp.*, 384 U.S. 563, 571 (1966)). [↑](#footnote-ref-31)
32. *See id.* at 20–21. [↑](#footnote-ref-32)
33. *See id.* at 21–22 (discussing *Times-Picayune Publ’g Co. v. United States*, 345 U.S. 594, 610 (1953)). [↑](#footnote-ref-33)
34. *See id.* at 22–23 (discussing *NCAA v. Bd. of Regents of the Univ. of Okla.*, 468 U.S. 85 (1984)). [↑](#footnote-ref-34)
35. *Id.* at 24 (citations omitted). [↑](#footnote-ref-35)
36. *See id.* at 32–33. [↑](#footnote-ref-36)
37. *See id.* at 33. [↑](#footnote-ref-37)
38. *See id.* at 35 (“At day’s end, it cannot be called an ‘efficiency’ justification for a Visa holder to pay higher prices at the gas station in order to subsidize an Amex holder’s frequent flyer miles.”). [↑](#footnote-ref-38)
39. Amex’s Opp’n at 16. [↑](#footnote-ref-39)
40. *See id.* at 17–19. [↑](#footnote-ref-40)
41. *Id.* at 23. [↑](#footnote-ref-41)
42. *Id.* at 24. [↑](#footnote-ref-42)
43. *See id.* at 28–29. Interestingly, Amex did not argue in its opposition that its vertical restraints enhance competition by preventing other card networks from freeriding: the offer of Amex at a merchant attracts Amex’s high-end clientele, but then at the point of sale that clientele is persuaded to switch to a lower-price card. [↑](#footnote-ref-43)
44. *See* Br. for the U.S. in Opp’n at 19–21, *Ohio v. Am. Express Co.*, No. 16-1454 (Aug. 2017). [↑](#footnote-ref-44)
45. *See id.* at 10–13. [↑](#footnote-ref-45)
46. *See id.* at 13–15. [↑](#footnote-ref-46)
47. *See id.* at 16–19. [↑](#footnote-ref-47)
48. Br. for *Amici Curiae* Ahold U.S.A., Inc. et al. in Supp. of Pet’rs at 1, *Ohio v. Am. Express Co.*, No. 16-1454 (July 2017). [↑](#footnote-ref-48)
49. *Id.* at 3 (ellipsis in original) (quoting P. Areeda & H. Hovenkamp, *Antitrust Law* § 562e (Supp. 2017)). [↑](#footnote-ref-49)
50. Br. for *Amici Curiae* Retail Litig. Ctr., Inc. in Supp. of Pet’rs at 6, *Ohio v. Am. Express Co.*, No. 16-1454 (July 2017). [↑](#footnote-ref-50)