POST *U.S. V. APPLE*: HOW SHOULD MOST-FAVORED NATION CLAUSES BE TREATED NOW?[♦]

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INTRODUCTION

In *United States v. Apple Inc.*,[1] the Department of Justice ("DOJ"), along with thirty-three states and U.S. territories, alleged that Apple conspired with five of the six largest publishing companies in the

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[1] 952 F. Supp. 2d 638 (S.D.N.Y. 2013). There have been a total of four related actions brought before the S.D.N.Y against Apple and the Publisher Defendants. This case represents two actions, one brought by the U.S. Department of Justice and one brought by the thirty-three states and U.S. territories, alleging that Apple and the Publisher Defendants conspired to raise e-book prices. The third action is *Texas v. Hachette Book Grp., Inc.*, 12 Civ. 6625 (S.D.N.Y.), a settlement action brought by forty-nine states, the District of Columbia, and U.S. Territories against Hachette, HarperCollins, and Simon & Schuster. The fourth action is *In re: Elec. Books Antitrust Litig.,* 11 MD 2293 (S.D.N.Y.), a consolidated class action brought by private plaintiffs against Apple and the Publisher Defendants for damages.

United States ("Publisher Defendants")[2] to raise, fix, and stabilize retail prices for e-books.[3] Prior to the launch of the iPad in January 2010, Apple signed agency agreements with the Publisher Defendants to sell the Publisher Defendants' e-books in Apple's iBooks Store.[4] The agreements utilized a principal-agency model, price tiers, and a most favored nation clause ("MFN"),[5] which guaranteed Apple the lowest retail price that the Publisher Defendants offered to any of their e-tailers.[6] Through these agreements, prices in the e-book industry increased by 50% or more "virtually overnight."[7] On July 10, 2013, the United States District Court for the Southern District of New York found that Apple violated Section 1 of the Sherman Antitrust Act's prohibition of unreasonable restraints of trade[8] by participating in and facilitating a horizontal price-fixing conspiracy with the Publisher Defendants to raise e-book prices.[9] The court's Final Judgment has now prohibited Apple from enforcing any retail price MFN[10] or entering into any new or future agreement that contains a retail price MFN with an e-book publisher.[11]

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[2] The Publisher Defendants are Hachette Book Group, Inc., HarperCollins Publishers LLC, Holtzbrinck Publishers LLC d/b/a Macmillan, Penguin Group (USA), Inc., and Simon & Schuster, Inc., each of which have settled their claims with the DOJ and the states. The Publisher Defendants and Random House, known as the "Big Six," are the six largest publishing companies in the United States. U.S. v. Apple, Inc., 952 F. Supp. 2d. 638, 645–47 (S.D.N.Y. 2013).

[3] E-books are electronic books that are read on a variety of electronic devices, including dedicated e-readers, multipurpose tablets, smartphones, and personal computers. Complaint, U.S. v. Apple, Inc., 952 F. Supp. 2d 638 (No. 12 CV 2826), 2012 WL 1193205 (S.D.N.Y. Apr. 11, 2012) [hereinafter Complaint] at ¶ 1.

[4] *Apple*, 952 F. Supp. 2d. at 645.

[5] *Id.* at 648. An MFN is also known as an "anti-discrimination" clause or "most favored customer" clause. Jonathan B. Baker, *Vertical Restraints with Horizontal Consequences: Competitive Effects of "Most-Favored-Customer" Clauses*, 64 ANTITRUST L.J. 517, 519 (1996).

[6] *Apple*, 952 F. Supp. 2d at 648. An e-tailer is an individual who sells products, such as e-books, via the Internet.

[7] *Id.*

[8] 15 U.S.C. § 1 (2004) ("Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be unlawful.").

[9] *Apple*, 952 F. Supp. 2d at 694.

[10] The Final Judgment defines "Retail Price MFN" as:

> [A] term in an agreement between an E-book Publisher and an E-book Retailer under which the Retail Price at which an E-book Retailer, or under an Agency Agreement, an E-book Publisher sells one or more E-books to consumers depends in any way on the Retail Price, or discounts from the Retail Price, at which any other E-book Retailer or the E-book Publisher, under an Agency Agreement, through any other E-book Retailer sells the same E-book(s) to consumers.

Plaintiff United States' Final Judgment and Plaintiff States' Order Entering Permanent Injunction at 4, *Apple*, 952 F. Supp. 2d 638 (No. 12 CV 2826), 2013 WL 4774755 (S.D.N.Y. Sept. 5, 2013).

[11] *Id*. at 5. Apple is appealing the judgment. Appellant Apple Inc.'s Opening Brief, U.S. v. Apple Inc., No. 13-3741 (L) (2d Cir. Feb. 25, 2014). The U.S. Court of Appeals for the Second Circuit heard oral arguments on December 15, 2014. *NY Court Weighs Apple, Amazon e-Book Arguments*, N.Y. TIMES (Dec. 15, 2014), http://www.nytimes.com/aponline/2014/12/15/us/ap-us-electronic-books-antitrust-lawsuit.html.

Over the past thirty-five years, MFNs have been periodically challenged under federal and state antitrust laws due to their anticompetitive potential.[12] An MFN is a type of vertical arrangement between suppliers and buyers. In the most common example, a seller promises a buyer that if he lowers the price to another buyer, the first buyer's price will be lowered to match. MFNs vary in different respects: they can be negotiated bilaterally as an explicit contractual provision or as a policy adopted unilaterally by a firm applicable to all buyers; they can occur contemporaneously or retroactively; and they can be used in contracts at different levels of distribution by either retailers or intermediate good suppliers.[13]

The *Apple* case is significant because it was the first instance in which a court found that an MFN has anticompetitive effects through a trial, rather than just in pretrial proceedings.[14] Although the court did not find that the MFN itself was inherently illegal, it found that the MFN was the key component of a *per se* illegal conspiracy that effectively allowed Apple and the Publisher Defendants to eliminate retail price competition and raise e-book prices.[15] This tension raises the question whether MFNs should be analyzed under a heightened antitrust standard of review. Upon a closer look though, it is clear that the rule of reason remains the preferable standard of review, as it allows courts to consider all circumstances of a case in order to correctly determine whether an MFN resulted in a net anticompetitive effect.

Part I of this Note provides a critical analysis of the *Apple* case, specifically how the court's decision could be interpreted as holding that MFNs are *per se* illegal in effect. Part II argues that the rule of reason is the preferable standard of review due to the need to fully analyze the conditions of an MFN that result in either anticompetitive harm or pro-competitive benefits. Finally, Part III explores the potential of applying a heightened standard of review in an MFN analysis, but ultimately argues that the rule of reason remains the preferable standard.

I. U.S. v. APPLE

A. *Background*

In December 2009, when Apple began planning its entry into the e-book market, both Apple and the Publisher Defendants shared one common objective: to eliminate retail price competition in the e-book

[12] Anthony J. Dennis, *Most Favored Nation Contract Clauses Under the Antitrust Laws*, 20 U. DAYTON L. REV. 821, 823 (1995).

[13] Jonathan B. Baker & Judith A. Chevalier, *The Competitive Consequences of Most-Favored-Nation Provisions*, 27 ANTITRUST 20, 20 (2013).

[14] Joe Palazzolo, *Apple Ruling Heaps Doubt on 'MFN' Clauses*, WALL ST. J. (July 14, 2013), http://online.wsj.com/article/SB10001424127887323664204578605880157245830.html.

[15] U.S. v. Apple Inc., 952 F. Supp. 2d 638, 699 (S.D.N.Y. 2013).

market and raise the price of e-books above the status quo $9.99 price point.[16] At this time, the publishing industry utilized a wholesale pricing model.[17] The publisher set the e-book's list price, also known as the suggested retail price, and then sold the book to a retailer for a wholesale price, which was roughly 50% of the hardcover list price.[18] The retailer then sold the book to consumers at whatever price it chose.[19] In 2009, Amazon was the dominant retailer of e-books, selling nearly 90% of all e-books in the United States.[20] Much of its success was due to its "loss leaders" strategy, under which Amazon sold its newly released and best-selling e-books at $9.99.[21] Amazon's $9.99 price point roughly matched the wholesale price of many of its e-books.[22]

The Publisher Defendants, as well as Random House, were extremely unhappy with Amazon's strategy. They feared that the $9.99 price point would have negative effects on their profits both in the short-term and long-term.[23] In the short-term, the Publishers believed that the low price point hurt the "sales of their profitable hardcover books, which were often priced at $30.00 or more," as well as "the viability of the brick-and-mortar stores" that sold the hardcover books.[24] In the long-term, they feared that the low price point would threaten the business model for the publishing industry, since customers would become accustomed to the lower prices, and as such, prices for all books would quickly erode.[25] The Publishers did not feel that the $9.99 price point reflected the true value of many of their books.[26] Additionally, they feared that Amazon, with its strong market power, would push for even lower wholesale prices for e-books or even compete directly with the Publishers by negotiating with authors and literary agents for rights, a process known as disintermediation.[27] As a result, the Publisher Defendants attempted various strategies to combat this perceived problem, including raising the wholesale prices for e-books and windowing.[28] These efforts, however, failed to change Amazon's pricing policies, and the Publisher Defendants became

[16] *Id.* at 647.
[17] *Id.* at 649.
[18] *Id.* at 649, 665.
[19] *Id.* at 649–50.
[20] *Id.* at 649.
[21] *Id.* at 649–50.
[22] *Id.* at 649.
[23] *Id.*
[24] *Id.*
[25] *Id.*
[26] *Id.*
[27] *Id.*
[28] *Id.* at 650–53. Windowing is the practice of delaying the release of the e-book version of new book releases in order to protect the sales of their hardcover versions. *Id.* at 651–52.

desperate for other ways to gain long-term control over their e-books.[29]

Like the Publisher Defendants, Apple also wanted a higher price point for newly released e-books. It did not want to engage in price wars with other e-tailers, especially Amazon.[30] Rather, Apple preferred to compete in the field of e-readers where it believed its iPad—a "revolutionary" e-reader that had a touch screen, audio and video capabilities, and the capacity to display text and photographs in color—would dominate.[31] Thus, Apple and the Publisher Defendants drafted agreements that reflected their common objective to raise the prices of e-books above $9.99.[32]

The agreements between Apple and each Publisher Defendant contained the same three components: the principal-agency model, price caps, and MFN.[33] The principal-agency model gave the Publisher Defendants control over retail pricing. Under this model, the publisher, as the principal, set the retail price of an e-book, and Apple, as the agent, sold the e-book in its iBooks Store for a 30% commission.[34] The price caps, however, limited the Publisher Defendants' control over pricing. Apple wanted to ensure that the iBooks Store prices remained realistic and that the Publisher Defendants would not embarrass Apple by setting their prices too high.[35] Thus, all bestselling and newly released titles bearing a hardcover list price between $25.01 and $35.00 had their e-book prices capped at $12.99, $14.99, or $16.99—the retail e-book price increasing in relation to the hardcover list price.[36] These caps were a "game-changer for the e-book industry," as they became the new standard industry-wide prices.[37]

The MFN was the key component of the agency agreements that effectively forced the entire e-book industry's shift to the agency model. Apple's MFN read as follows:

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[29] *Id.* at 653.
[30] *Id.* at 701 n.64.
[31] *Id.* at 663.
[32] *Id.* at 677–78.
[33] *Id.* at 648.
[34] *Id.* at 662.
[35] *Id.* at 692.
[36] Complaint, *supra* note 3, at ¶ 7. For new release titles listed between $25.01 and $27.50, the e-book prices would be no greater than $12.99; for new release titles listed between $27.51 and $30.00, the e-book prices would be no greater than $14.99. The e-book prices of books listed between $30.01–$35.00 and $35.01–$40.00 would be capped at either $16.99 or $19.99, respectively. The agency agreement also included special pricing tiers for e-book versions of books on the N.Y. TIMES fiction and non-fiction bestseller lists. The e-book prices of N.Y. TIMES bestsellers listed for $30.00 or less would be capped at $12.99, and the e-book prices of bestsellers listed above $30.00 and up to $35.00 would be capped at $14.99. U.S. v. Apple Inc., 952 F. Supp. 2d 638, 669 (S.D.N.Y. 2013).
[37] *Apple*, 952 F. Supp. 2d at 669.

> [I]f, for any particular New Release in hardcover format, the then-current Customer Price at any time is or becomes higher than a customer price offered by any other reseller ("Other Customer Price"), then Publisher shall designate a new, lower Customer Price to meet such lower Other Customer Price.[38]

The MFN essentially stated that if the retail price of an e-book offered in Apple's iBooks Store was higher than the retail price of the same e-book in another e-tailer's bookstore, the publisher had to designate the lower retail price to the e-book in the iBooks Store. For example, if a publisher moved all other e-tailers to the agency model, but allowed Amazon to remain on the wholesale model, and Amazon sold an e-book for $9.99, the publisher would be obligated under the MFN to allow Apple to sell the same e-book in its iBooks Store for $9.99. Under the wholesale model, the publisher received roughly 50% of an e-book's hardcover list price, whereas under the agency model, the publisher received 70% of the e-book's *retail* price.[39] This meant that for an e-book with a hardcover list price of $26.00, the publisher would receive $13.00 from Amazon under the wholesale model, but only $7.00 from Apple for the same e-book under the agency model, so long as Apple sold the e-book at the $9.99 price point.[40] However, if both Amazon and Apple operated under the agency model and the publisher was able to sell an e-book at the top of the model's pricing tier at $12.99, the publisher would receive $9.10 each from Amazon and Apple.[41] Thus, the Publisher Defendants suffered a "severe financial penalty" if they did not first move their other e-tailers to the agency model.[42] Otherwise, Apple would be able to sell its e-books at its competitors' lower prices, and the Publisher Defendants would receive a smaller commission from Apple than they would have if all e-tailers operated under the agency model.

The Publisher Defendants were hesitant about entering into the agency agreements.[43] Moving to the agency model was not in the Publisher Defendants' short-term financial interests, as they would lose "a stream of expected revenue from the sale of e-books on the wholesale model."[44] The Publisher Defendants also feared that Amazon, the largest e-book retailer, might retaliate against them for pressuring it to

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[38] Plaintiff's Exhibit PX-0002, *Apple*, 952 F. Supp. 2d 638 (S.D.N.Y. 2013) (No. 12 CV 2826). Customer Price was defined as "the price displayed to the [customer] on the [iBooks Store], as designated by [the] Publisher for each eBook by selecting from the prices set forth[.]" *Id.*
[39] *Apple*, 952 F. Supp. 2d at 665.
[40] *Id.*
[41] *Id.*
[42] *Id.* at 648.
[43] *Id.* at 674–78.
[44] *Id.* at 693.

raise its e-book prices, especially if they did not act collectively.[45] If only one or two of the Publisher Defendants moved to the agency model, Amazon would be unconvinced to change its pricing policy, and in the meantime, those Publisher Defendants would lose substantial revenue as the other Publisher Defendants continued to profit from remaining on the wholesale model.[46]

Apple, however, was able to facilitate collective action among the Publisher Defendants by assuring each one that the other Publisher Defendants were committing to the agency model under substantively identical terms.[47] Apple also kept the Publisher Defendants apprised of the status of the other agreements.[48] This is why "Apple's participation in the conspiracy proved [to be] essential."[49] By ensuring such cooperation, Apple enabled the Publisher Defendants to impose the agency model on all of their e-tailers. Amazon had no choice but to switch to the agency model "in light of the Publisher Defendants' overlapping threats to remove content from Amazon."[50]

As expected, Apple's price caps became the new retail prices for the Publisher Defendants' e-books,[51] raising their e-book prices "virtually overnight."[52] For some titles, e-book prices increased by 50% or more.[53] Within roughly two weeks of Amazon moving to the agency model, Amazon's "average per unit e-book retail price increase[ed by] 14.2% for their new releases, 42.7% for their *New York Times* bestsellers, and 18.6% across all of the Publisher Defendants' e-books."[54] Meanwhile, the average e-book prices of Random House, who had declined to move to the agency model, "hovered steadily around $8.00."[55] Consequently, millions of consumers suffered "clear and substantial harm,"[56] including having to "pay more for e-books . . . [buy] a cheaper e-book rather than the one they preferred to purchase . . . [or] deferring a purchase altogether rather than pay the

[45] *Id.* at 650, 674, 692.
[46] *Id.* at 692.
[47] *Id.* at 664, 692.
[48] *Id.* at 673–75.
[49] *Id.* at 692.
[50] *Id.* at 681.
[51] *Id.* at 682.
[52] *Id.* at 648.
[53] *Id.*
[54] *Id.* at 682. The Publisher Defendants also raised "the prices of some of their [n]ew [r]elease *hardcover* books [] in order to move the e-book version into a correspondingly higher price tier," and "raised the prices of their backlist e-book prices, which were not governed by the agreement's price tier regimen . . . . [T]he Publisher Defendants did this in order to make up for some of the revenue lost from the sales of their [n]ew [r]elease e-books" under the agency model. *Id.* at 683 (emphasis in the original).
[55] *Id.*
[56] Plaintiffs' Pretrial Memorandum of Law, U.S. v. Apple Inc., No. 12 CV 2826, 2013 WL 2101924 (S.D.N.Y. May 14, 2013) at 18.

higher price."[57]

B. Apple *Court's Treatment of the MFN*

The district court found that Apple committed a *per se* violation of the Sherman Antitrust Act by participating in and facilitating a horizontal price-fixing conspiracy with the Publisher Defendants.[58] The court explicitly stated that the specific terms of the agency agreements, including the MFN, were *not* illegal *per se*, "either alone or in combination."[59] However, this is in tension with the court's own finding that the MFN was the term that effectively forced the entire e-book industry to switch to the agency model.

Apple attempted to argue that the MFN was pro-competitive because the MFN lowered, not raised, retail prices.[60] If a publisher continued to allow some of its e-tailers to remain on the wholesale model and sell their e-books at prices below the price caps, then Apple would also be permitted to sell the same e-book at the discounted price in its iBooks Store per the MFN.[61] However, the mere presence of the MFN precluded any possibility of this situation. The Publisher Defendants already expected to lose revenue for every e-book sold under the agency model.[62] Allowing an e-tailer to remain on the wholesale model in the presence of an MFN would cause the Publisher Defendants to suffer additional losses, putting them "in significantly worse terms financially."[63] This is why it was imperative that the Publisher Defendants immediately move all of its e-tailers to the agency model.[64]

Given the central role that the court assigned to the MFN in its analysis, it is reasonable to conclude that in the absence of the MFN, Apple and the Publisher Defendants would not have been able to eliminate retail price competition and raise e-book prices as they did. It seems unusual, then, that the court found that the anticompetitive effect of the MFN was *per se* illegal, yet the MFN itself—the direct cause of the anticompetitive behavior—was not *per se* illegal. One plausible interpretation of the court's holding could be that MFNs are *per se* illegal in effect. If so, this raises the question of whether MFNs should be subject to a heightened standard of review.

[57] *Apple*, 952 F. Supp. 2d at 685.
[58] *Id.* at 694.
[59] *Id.* at 708.
[60] *Id.* at 701.
[61] *Id.*
[62] *Id.* at 692. For a typical e-book, instead of receiving $13.00 in commission under the wholesale model, the Publisher Defendants would receive $9.10 in commission under the agency model, contingent on the fact that they were able to sell the e-book at the top of the pricing tier at $12.99.
[63] *Id.*
[64] *Id.*

II. MFNS UNDER THE RULE OF REASON

MFNs have been traditionally been analyzed under the rule of reason.[65] Under the rule of reason, the fact finder must weigh all the circumstances of a case in order to correctly determine whether an alleged practice "should be prohibited as imposing an unreasonable restraint on competition."[66] This holistic approach is important to MFNs because an MFN's anticompetitive effects and pro-competitive effects are not mutually exclusive—they can occur simultaneously.[67] As such, determining whether an MFN creates a net anticompetitive harm or a net pro-competitive benefit requires a complete analysis of the circumstances of the case under the rule of reason.

A. *Rule of Reason v.* Per Se *Rule*

The rule of reason is the accepted standard to determine whether a practice restrains trade in violation of Section 1 of the Sherman Antitrust Act.[68] In *Board of Trade v. United States*,[69] Justice Brandeis set forth appropriate factors for courts to consider in order to decide whether a practice imposes an unreasonable restraint on competition:

> [F]acts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable[;] [t]he history of the restraint; the evil believed to exist; the reason for adopting the particular remedy; and the purpose or end sought to be attained.[70]

Under this analysis, the plaintiff bears the initial burden of demonstrating that "the defendants' challenged behavior 'had an *actual* adverse effect on competition as a whole in the relevant market.'"[71] If proving actual detrimental effects is too difficult, the plaintiff must prove that the defendant had market power—that is, "the ability to raise prices above those that would prevail in a competitive market."[72] Once the plaintiff satisfies his initial burden, the burden shifts to the defendant who must then introduce sufficient evidence that his conduct

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[65] Baker, *supra* note 5, at 520.
[66] Cont'l T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 49 (1977).
[67] Baker & Chevalier, *supra* note 13, at 20. *See* Steven C. Salop & Fiona Scott Morton, *Developing an Administrable MFN Enforcement Policy*, 27-SPG ANTITRUST 15, 18–19 (Spring 2013).
[68] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 885 (2007).
[69] Bd. of Trade v. U.S., 246 U.S. 231 (1918).
[70] *Id.* at 238.
[71] Geneva Pharm. Tech. Corp. v. Barr Labs. Inc., 386 F.3d 485, 506–07 (2d. Cir. 2004) (quoting Capital Imaging Assocs., P.C. v. Mohawk Valley Med. Assocs., Inc., 996 F.2d 537, 543 (2d. Cir. 1993)).
[72] U.S. v. Brown Univ., 5 F.3d 658, 668 (3d Cir. 1993) (citing Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 27 n.46 (1984)).

promoted a legitimate objective.[73] The plaintiff may rebut the defendant's case by introducing evidence that the defendant's objective was illegitimate, the challenged behavior did not substantially serve the claimed legitimate objective, or the objective could have been achieved by a significantly less restrictive alternative.[74] If the plaintiff's rebuttal is successful, then he prevails.[75] If not, the court must weigh and balance the alleged harms against the alleged benefits.[76]

By contrast, the *per se* rule is reserved for practices that "would be invalidated in all or almost all instances under the rule of reason."[77] Examples of *per se* illegal practices include price fixing, division of markets, group boycotts, and tying arrangements.[78] Because such practices "always or almost always tend to restrict competition and decrease output,"[79] courts may conclusively presume them to be unreasonable, and therefore, illegal. Under the *per se* rule, there is no need to undertake a full-scale rule of reason analysis, which is often "complicated and expensive,"[80] thereby promoting "business certainty and litigation efficiency."[81] Since the *per se* rule is such a demanding standard, courts have often been reluctant to apply the rule to types of agreements with which they have had little experience, or which have ambiguous or pro-competitive economic effects.[82] The courts must be able to predict with confidence that the restraint is manifestly anticompetitive with absolutely no redeeming virtue before applying the *per se* rule.[83]

B. *Anticompetitive Effects of MFNs*

There are three common anticompetitive harms that may result from MFNs: (1) collusion, specifically facilitating anticompetitive coordination; (2) exclusion; and (3) increasing a seller's bargaining power.[84] The first potential anticompetitive effect of MFNs is that an

[73] 7 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW § 1507(c) (2d ed. 2003).
[74] *Id.*
[75] *Id.*
[76] *Id.*
[77] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 878 (2007).
[78] Capital Imaging Assocs., P.C. v. Mohawk Valley Med. Assocs., Inc., 996 F.2d 537, 542–43 (2d. Cir. 1993).
[79] *Leegin*, 551 U.S. at 886 (quoting Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 723 (1988)).
[80] N. Pac. Ry. Co. v. U.S., 356 U.S. 1, 5 (1958).
[81] Ariz. v. Maricopa Cnty. Med. Soc., 457 U.S. 332, 344 (1982).
[82] *Leegin*, 551 U.S. at 887.
[83] *Id.*
[84] Baker & Chevalier, *supra* note 13, at 24–25. Another collusive theory is that MFNs dampen competition "by making firms less aggressive in settings in which rivals respond by becoming less aggressive as well." Jonathan B. Baker, *supra* note 5, at 528–29 (1996). When a seller agrees to an MFN, it suffers a severe financial penalty if it lowers its prices to any buyers other than the beneficiary of an MFN. In some industries, the firm's commitment to an MFN will lead rivals to see that it is their best interest to allow industry prices to rise. *Id.* The effect is greater when most

MFN may make it less likely for a buyer and seller to deviate from a coordinated arrangement.[85] In a typical horizontal agreement, a buyer and seller will agree on a set price for a good to be sold. The MFN, however, discourages the seller from offering a discounted price to another buyer because any discount offered to one buyer must also be extended to the first buyer, who is protected by the MFN.[86] This raises the seller's costs of discounting, thereby facilitating anticompetitive coordination, as the original price agreed upon by the parties becomes the floor price of the good. This often leads to higher prices, especially when sellers are confident that their competitors will act similarly in face of the same disincentives.[87] Meanwhile, other buyers frequently agree to the floor price because they do not want to waste time negotiating prices with a seller who is not willing to discount.[88] Buyers have little incentive to drive a hard bargain, as their efforts will not result in a competitive advantage in this situation.[89]

The facilitating coordination theory was the theory behind the *Apple* case. Under the agency model, the Publisher Defendants were allowed to set their e-book prices according to the model's pre-set pricing tiers.[90] The MFN, however, discouraged the Publisher Defendants from providing their e-tailers a "discount"—that is, allowing an e-tailer to remain on the wholesale model and independently set the retail prices for the Publisher Defendant's e-books. As stipulated by the terms of Apple's MFN, if a Publisher Defendant kept an e-tailer, like Amazon, on the wholesale model, Apple would be able to sell the Publisher's e-books for the same price that Amazon did.[91] The Publisher Defendants were already expected to lose profits under the agency model and thus would only suffer more if they did not impose agency terms on their other e-tailers.[92] This is why Apple did not need to include an explicit term in the agency agreements that required a Publisher Defendant to move all of its e-tailers to the agency model; "[t]he MFN was sufficient to force the change in model."[93]

The second potential anticompetitive effect of MFNs is that an MFN may exclude potential entrants and constrain fringe rivals from fully entering the market.[94] When a seller enters into an agreement with

or all firms in an industry adopt these practices. *Id.*

85 Baker, *supra* note 5, at 520.

86 Baker & Chevalier, *supra* note 13, at 23.

87 *Id.*

88 *Id.*

89 *Id.*

90 U.S. v. Apple, Inc., 952 F. Supp. 2d 638, 669–70 (S.D.N.Y. 2013).

91 *Id.* at 665.

92 *Id.* at 692 .

93 *Id.*

94 Baker & Chevalier, *supra* note 13, at 24.

a dominant incumbent buyer, the presence of an MFN discourages the seller from bargaining with smaller entrants or rivals for a better price because the seller must also offer that better price to the incumbent buyer.[95] This insulates the incumbent buyer from competition and protects its higher prices.[96] The harm to competition is exacerbated when the MFN takes the form of an "MFN plus," which stipulates that the supplier must not only match the lowest price offered to another buyer, but also provide an even better price to the incumbent buyer.[97] An MFN plus buyer receives the lowest price of all prices offered.[98] For example, in *U.S. v. Blue Cross Blue Shield of Mich.*, the DOJ alleged that Blue Cross Blue Shield of Michigan ("Blue Cross") included MFN plus clauses, in addition to standard MFN clauses, in their contracts with participating hospitals.[99] The MFN plus clause required the hospitals "to charge some or all other commercial insurers more than the hospital charge[d] Blue Cross."[100] Some hospitals had to "charge Blue Cross' competitors as much as 40% more than they charg[ed] Blue Cross."[101] Therefore, through use of an MFN plus clause, an incumbent buyer can protect his market power against both existing and potential rivals.[102]

The anticompetitive exclusion theory has been the basis of recent challenges to the use of MFNs in various health insurance provider agreements.[103] For example, the DOJ relied on the anticompetitive exclusion theory in its complaint against Delta Dental of Rhode Island ("Delta"), alleging that the anticompetitive effects of Delta's MFN in its contracts with participating dentists outweighed any of its potential competitive benefits.[104] In its complaint, the DOJ alleged that Delta

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95 *Id.*
96 *Id.*
97 *Id.*
98 *Id.*
99 U.S. v. Blue Cross Blue Shield of Mich., 809 F. Supp. 2d 665, 669 (E.D. Mich. 2011) (where the court rejected defendant's motion to dismiss, finding that the DOJ's complaint plausibly alleged sufficient facts that the MFNs produced anticompetitive effects, including excluding other health insurers from entering the relevant product and geographic markets). In light of the dismissal, the state of Michigan enacted legislation that prohibits health insurers, including Blue Cross Blue Shield of Michigan, from including or using MFNs in any contracts with health care providers. Press Release, U.S. Department of Justice, Justice Department Files Motion to Dismiss Antitrust Lawsuit Against Blue Cross Blue Shield of Michigan After Michigan Passes Law to Prohibit Health Insurers from Using Most Favored Nation Clauses in Provider Contracts (Mar. 25, 2013), http://www.justice.gov/opa/pr/2013/March/13-at-345.html (noting the MFN ban took effect on Jan. 1, 2014).
100 *Blue Cross Blue Shield*, 809 F. Supp. 2d at 669.
101 *Id.*
102 Baker & Chevalier, *supra* note 13, at 24.
103 Joseph Kattan & Scott A. Stempel, *Antitrust Enforcement and Most Favored Nations Clauses*, 10-SUM ANTITRUST 20, 23 (Summer 1996).
104 U.S. v. Delta Dental of R.I., 943 F. Supp. 172, 189 (D.R.I. 1996). The MFN in Delta's Participating Dentist's Agreement was stated as follows: "Delta Dental reserves the right to limit reimbursements to dentists to such levels as such dentists have agreed to accept from other non-

selectively enforced its MFN "whenever the fees that a participating dentist accept[ed] from another non-governmental third-party payer [were] demonstrably significantly lower than (Delta's)."[105] The DOJ contended that Delta had significant market share, "[a]s the state's largest dental insurer, insur[ing] or administer[ing] plans for 35–45% of persons covered by any type of dental insurance in Rhode Island . . . . 90% of the dentists actively practicing in Rhode Island accept[ed] Delta."[106] Delta's MFN, therefore, caused "participating dentists [to] either withdraw[] from—or refuse[] to join—lower-cost dental plans, or insist[] as a condition of their participation that payments be increased to Delta's price levels."[107] Potential competitors who offered new low-cost dental plans were also excluded from the dental insurance market, and existing competitors were prevented from expanding their insurance programs into lower price options "for fear of detection by Delta and the inevitable application of its MFN clause."[108] As a result, the costs of dental insurance and services to Rhode Island consumers substantially increased.[109] Furthermore, there were no perceivable pro-competitive effects of this scheme, as suggested by the fact that Delta's selective use of the MFN did not result in any discernible cost savings.[110] The court concluded that "[t]he net effect [of Delta's MFN] was an alleged detrimental impact on the dental market without any *discernible* competitive benefits."[111] The DOJ and Delta have since settled the case; the final judgment prohibited Delta Dental from including any MFN in any of its contracts with participating dentists for ten years.[112]

The third potential anticompetitive effect of an MFN is the increase in a seller's bargaining power, particularly a monopolist of durable goods.[113] In the absence of an MFN, a buyer holds significant bargaining power. Instead of buying the good at the seller's monopoly price right away, he can delay his purchase and wait for the monopolist to discount or negotiate a competitive price.[114] This strategy may be worthwhile even if the seller offers a price only slightly above the

governmental dental benefit reimbursement programs." *Id.* at 183.
[105] *Id.* at 183.
[106] *Id.*
[107] *Id.* at 179.
[108] *Id.* at 179, 184, 192.
[109] *Id.* at 177, 192.
[110] *Id. But cf.* Ocean State Physicians Health Plan Inc. v. Blue Cross & Blue Shield of R.I., 883 F.2d 1101 (1st Cir. 1989) (holding that the MFN was not anticompetitive because the defendant saved $1,900,000 through the MFN, resulting in lower prices of its overall health insurance product, despite the anticompetitive exclusionary effects of defendant's MFN).
[111] *Delta Dental*, 943 F. Supp. at 192.
[112] Final Judgment at 3, 9, *Delta Dental*, 943 F. Supp. 172 (No. 96-113P) (D.R.I. July 2, 1997), http://www.justice.gov/atr/cases/f1100/1183.pdf.
[113] Baker & Chevalier, *supra* note 13, at 24. A durable good is a product that will last many years; for example, a factory machine. *Id.*
[114] *Id.*

competitive price.[115] If multiple buyers take this approach, the monopolist will have difficult making a profit as long as he insists on maintaining non-competitive pricing.[116] However, the introduction of an MFN allows the seller to commit buyers to the monopoly price by signaling to them that he will not discount in the future, since the presence of the MFN substantially increases the seller's cost of discounting.[117] This dramatically increases the seller's bargaining power, and as a result, the seller is able to obtain a much more favorable outcome.[118]

C. *Pro-competitive Effects of MFNs*

There are three common potential efficiency rationales that may result from MFNs: (1) eliminating the "hold up" problem; (2) preventing delays in transacting; and (3) reducing transaction and negotiation costs.[119] The first potential efficiency rationale is that an MFN may allow parties to contract more efficiently by eliminating the "hold up" problem.[120] The "hold up" problem occurs when a supplier tries to take advantage of a buyer after the buyer has already made costly investments in their business relationship.[121] For example, a buyer may invest by training his employees to handle the particular good sold by the supplier, or improve his infrastructure to accommodate the specifications of the good. After the buyer has made such investments, the supplier may exploit the buyer by making a better deal with a competing buyer or terminating the agreement altogether.[122] The MFN helps relieve this problem by tying the hands of both parties to their original agreement. Although the terms of the MFN do not mean that a supplier will not enter into an agreement with a competing buyer, at the very least, the supplier agrees not to give a competing buyer better terms.[123] The MFN then "operates similarly as a weaker version of an exclusive territory or non-encroachment contract."[124] An MFN may also relieve the "hold up" problem for parties who enter into long-term contracts knowing that supply and demand conditions might change unpredictably.[125] For example, well owners must enter into long-term price-fixed contracts with pipeline buyers without knowing

[115] *Id.*
[116] *Id.*
[117] *Id.*
[118] *Id.*
[119] *Id.* at 21–22.
[120] *Id.* at 21.
[121] *Id.*
[122] *Id.*
[123] *Id.*
[124] *Id.*
[125] Baker, *supra* note 5, at 533.

the future demand for gas.[126] This causes production to respond inefficiently to changes in demand.[127] The alternative solution, however, places well owners in a "difficult bargaining position": if a well owner had to renegotiate the price with a pipeline buyer every year, he would be subject to the buyer's exploitation, since he had already made a substantial investment in the relationship by drilling.[128] An MFN relieves this problem by allowing the parties to sign a long-term contract that contemplates annual price changes, while also constraining the buyer's ability to exploit the supplier.[129] The presence of the MFN obligates the buyer to offer the supplier the same price that he has already offered to his other suppliers.[130] In this way, the MFN pins the transaction price in the long-term contract to the market price.[131]

The second potential efficiency rationale is that an MFN may prevent delays in transacting, specifically where a buyer's project is contingent on the agreement of multiple sellers.[132] For example, a land developer may have a project that is contingent on a number of small parcel holders selling their property.[133] However, the land developer may have trouble securing each parcel because each seller wants to be the last one to make the deal.[134] If a seller holds the last parcel of property necessary for the land developer's project, the developer may be more likely to offer a price greater than market value in order to move the project forward.[135] An MFN solves this problem by promising all sellers that the buyer will pay them the difference between the price that they originally received and the price that the last seller received.[136] As a result, the MFN creates efficiency, eliminating the sellers' incentive to delay.[137]

The MFN can also reduce transaction delays in markets where buyers may expect the price of a good to eventually decrease or the supplier to discount unsold inventory.[138] Buyers will simply wait until they can receive the best deal. An MFN, however, can encourage early transactions by promising the buyer that the supplier will offer a partial refund if the supplier later sells the good to another buyer at a

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[126] *Id.*
[127] *Id.* ("A long-term fixed-price contract is unattractive because it would not lead production to respond efficiently to changes in demand.").
[128] *Id.*
[129] *Id.*
[130] *See* Palazzolo, *supra* note 13 & accompanying text.
[131] *See id.*
[132] Baker & Chevalier, *supra* note 13, at 21.
[133] *Id.*
[134] *Id.*
[135] *Id.*
[136] *Id.*
[137] *Id.*
[138] *Id.*

discounted price.[139] Buyers, therefore, have no reason to delay the transaction.

The third potential efficiency rationale is that an MFN may reduce transaction and negotiation costs.[140] The MFN guarantees that a buyer will receive another buyer's best price without having to engage in costly negotiations or undertake an extensive search on his own for the best available price.[141] The MFN can also reduce renegotiation costs by guaranteeing a buyer that he will not be disadvantaged if a future competitor receives a better deal the following year.[142] Because of the MFN, the buyer will receive the same price as his competitor without having to bear the costs of renegotiation.

However, there are at least two limitations that diminish the efficiency gained from reducing transaction and negotiation costs.[143] First, an MFN can create an additional cost to the buyer by requiring him to monitor whether the seller is adhering to the terms of the MFN.[144] If a buyer has no way of monitoring the prices that a supplier offers to the buyer's competitors, then the supplier may offer the buyer's competitors discounted prices in violation of the MFN.[145] Even if a buyer has the right to audit the supplier's records, the buyer will want to look at, in addition to price, other terms of his competitor's contracts in order to determine whether the competitors have received better overall terms from the supplier, "a costly and difficult task."[146] An MFN is only as effective as a buyer's ability to enforce it.

Additionally, the MFN may provide little incentive for both suppliers and buyers to push for discounts,[147] as discussed above, as a result of the facilitating coordination theory. In the presence of an MFN, a seller has little incentive to offer a discounted price to a buyer, since any discount offered to one buyer must be extended to all buyers protected by MFNs. The seller's costs of discounting thus increase.[148] Meanwhile, buyers are less likely to push for discounts because any discount received from the seller will also extend to their competitors who have MFNs.[149] Therefore, there is no "cost advantage by negotiating a discount from a seller."[150]

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139 *Id.*
140 *Id.* at 22.
141 *Id.*
142 Kattan & Stempel, *supra* note 104, at 20.
143 Baker & Chevalier, *supra* note 13, at 22.
144 *Id.*
145 *See id.*
146 *Id.*
147 *Id.*
148 *Id.*
149 *Id.*
150 *Id.*

D. *Analyzing MFNs in Context*

As discussed, an MFN may result in anticompetitive harm or pro-competitive benefits. However, whether an MFN creates a *net* anticompetitive harm or pro-competitive benefit depends upon the circumstances of the case. For example, evidence of certain conditions such as: reduced or deterred innovation, increased or decreased input costs, increased or decreased output costs, the market power of the sellers and buyers, and the relevant product market, may be useful to a fact-finder.[151] In *Apple*, at least two additional conditions suggested that Apple's MFN resulted in anticompetitive harm: the use of the MFN in a horizontal price-fixing agreement and increased prices.[152]

The presence of a horizontal price-fixing agreement may be evidence of an MFN's anticompetitive harm because such agreements are generally *per se* unlawful.[153] In *Apple*, the court found that the agreement among the Publisher Defendants to raise e-book prices constituted a horizontal price-fixing conspiracy.[154] The court also found that Apple's agency agreements with the Publisher Defendants, despite being vertical arrangements, were "at root, [] horizontal price restraint[s]."[155] Horizontal price-fixing agreements knowingly entered into and facilitated by a vertical actor, which cause anticompetitive harm to the vertical actor's horizontal competitors, may also be *per se* unlawful.[156] In *Apple*, the technology giant coordinated and facilitated the Publisher Defendants' horizontal price-fixing conspiracy by signing vertical agreements with substantively identical terms, including the MFN, with the Publisher Defendants.[157] This coordination allowed the MFN to have the effect it did: "change the business model for the distribution of e-books, impose that new model on Amazon against its will, and effect a significant increase in the retail prices of e-books."[158] Without Publisher Defendant's collective action, facilitated by Apple, the MFN likely would not have raised anticompetitive concerns because of the smaller impact the MFN would have made in the e-books market.

The presence of increased prices also suggests that an MFN has caused anticompetitive harm to consumers, especially when the prices

[151] Salop & Morton, *supra* note 67, at 17.
[152] *See id.*
[153] U.S. v. Apple, Inc., 952 F. Supp. 2d 638, 688 (S.D.N.Y. 2013) (citing Starr v. Sony BMB Music Entm't, 592 F.3d 314, 326 n.4 (2d Cir. 2010) & Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 886 (2007)).
[154] *Apple*, 952 F. Supp. 2d at 691.
[155] *Id.* at 707 (quoting *In re* Elec. Books Antitrust Litig., 859 F. Supp. 2d 671, 685 (S.D.N.Y. 2012)).
[156] *Apple*, 952 F. Supp. 2d at 690. *See* Interstate Cir. v. U.S., 306 U.S. 208, 230–32 (1939); Toys "R" Us, Inc. v. FTC, 221 F.3d 928, 930 (7th Cir. 2000).
[157] *Apple*, 952 F. Supp. 2d at 692.
[158] *Id.* at 697.

are not offset by increases in quality or innovation.[159] In *Apple*, the increased e-book prices were not the result of either of those factors. Phenomena such as "[Apple's] launch of the iBooks Store, the technical novelties of the iPad [and] the evolution of digital publishing more generally . . . [were] independent of the [agency a]greements."[160] Instead, the increased prices were the direct product of Apple and the Publisher Defendants' efforts to control retail e-book pricing and raise e-book prices, with the MFN being the key component of the agency agreements that allowed them to do so.[161] As a result, consumers were harmed in more ways than one.[162]

As evidenced by the *Apple* case, it is necessary to look at all of the circumstances of a case in order to determine whether an MFN generated a net anticompetitive or pro-competitive effect. This is why the rule of reason is necessary to an MFN analysis—the rule's holistic approach allows the court to balance various factors, including the conditions under which the MFN was adopted and the effects resulting from the implementation of the MFN.[163] Some critics argue that the rule of reason's holistic approach is too burdensome for plaintiffs, as plaintiffs are never sure as to the exact quality or quantity of proof necessary for a court to determine whether an alleged practice is unreasonable.[164] Subsequently, the application of the rule is unpredictable, and as a result, parties may waste time and resources developing and presenting aspects of their case that do not end up factoring into the court's decision.[165] Despite its vagueness, the rule of reason provides a court great flexibility in the quality and quantity of evidence that it may consider. This is crucial to an MFN analysis where so many factors may be relevant in determining whether an MFN generated a net anticompetitive or pro-competitive effect.

III. Should MFNs Be Subject to a Heightened Antitrust Standard of Review?

Although the rule of reason is the preferable standard under which to analyze MFNs, the court's treatment of the MFN in *Apple* raises the question of whether MFNs should be subject to a heightened standard of review. By holding that the anticompetitive effect of the MFN was *per*

[159] Salop & Morton, *supra* note 67, at 17.
[160] *Apple*, 952 F. Supp. 2d at 694.
[161] *See supra* Part I.a.
[162] *See supra* note 57 & accompanying text.
[163] *See* Salop & Morton, *supra* note 67, at 17–19.
[164] *See* Jesse W. Markham, Jr., *Sailing a Sea of Doubt: A Critique of the Rule of Reason in U.S. Antitrust Law*, 17 FORDHAM J. CORP. & FIN. L. 591, 597–98 (2012); Jay P. Yancey, *Is the Quick Look Too Quick?: Potential Problems with the Quick Look Analysis of Antitrust Litigation*, 44 U. KAN. L. REV. 671, 676 (1996).
[165] *See* Markham, *supra* note 164.

se illegal, but the MFN itself—the direct cause of the anticompetitive effect—was not, the court could plausibly be interpreted as holding that MFNs are *per se* illegal *in effect*. If so, courts would benefit from applying a heightened standard of review, such as the quick look approach, under which there would be a rebuttable presumption of illegality against MFNs. This would save the court both time and resources. However, application of the quick look approach may actually inhibit a court's ability to conduct a proper MFN analysis. Therefore, the rule of reason remains the preferable standard of review.

A. *Quick Look Approach*

The quick look approach is an "intermediate standard" that falls somewhere between the *per se* rule and the rule of reason.[166] Under the quick look approach, there is a rebuttable presumption of illegality against the challenged behavior.[167] In order to rebut that presumption, a defendant must provide pro-competitive justifications for its conduct.[168] If no legitimate justifications are provided, the presumption prevails and the "court condemns the practice without ado."[169] However, if a defendant's justifications are sound and capable of proof, the court proceeds with a "full-scale rule of reason analysis."[170]

The quick look approach is applied in cases where application of the *per se* rule is inappropriate, but the challenged behavior is sufficiently anticompetitive on its face to presume that there is anticompetitive harm[171] With respect to MFNs, the clauses' substantial anticompetitive harm, as seen in *Apple*, would seemingly justify use of the quick look approach when analyzing MFNs. Under the quick look approach, MFNs would be presumptively illegal, thereby eliminating the need to conduct a full-scale rule of reason analysis in order to determine whether the challenged MFN is anticompetitive.[172] A full-scale rule of reason analysis would only become necessary if a defendant was able to provide pro-competitive justifications for using the MFN, such as one of MFN's efficiency rationales discussed above.

One of the most useful aspects of the quick look approach is that it allows a plaintiff to avoid engaging in the troublesome undertaking of proving a defendant's market power, an often-necessary task under the rule of reason. Proving market power is one of two ways in which a plaintiff may meet their initial burden of showing that the challenged behavior produced anticompetitive effects within the relevant product

[166] U.S. v. Brown Univ., 5 F.3d 658, 669 (3d Cir. 1993).
[167] *Id.*
[168] *Id.*
[169] *Id.*
[170] *Id.*
[171] *See id.*
[172] *Id.*

and geographic markets under the rule of reason.[173] The alternative, proving the existence of actual anticompetitive effects, is often impossible "due to the difficulty of isolating the market effects of the alleged restraint."[174] Thus, courts will frequently allow a plaintiff to prove that a defendant had market power.[175]

A proof of market power analysis, however, is often considered to be the single most complex and expensive aspect of an antitrust case.[176] It involves multiple elements, including:

> [D]etailed analysis of the proper definition of the relevant product and geographic markets; the defendant's market share; the identities and market share of other existing market participants; entry conditions and trends; the identity, proximity and relative strength of potential entrants; consumer substitution and cross-elasticities of demand; supply-side substitution; as well as inferences from subjective sources such as from the internal documents of market participants and opinions of expert observers.[177]

Because these elements are fact-intensive, proving market power quickly becomes a battle of the experts.[178] It is also time-consuming and difficult to establish. However, under the quick look approach, a plaintiff does not have to prove market power, since the anticompetitive nature of the practice, alone, satisfies a plaintiff's initial burden of proof. Therefore, this approach allows for greater efficiency and cost-savings for the plaintiffs, as the burden immediately shifts to defendants to establish the challenged behavior's pro-competitive justifications.

B. *The Rule of Reason is Preferable to the Quick Look Approach*

1. Proof of Market Power Analysis is Absent Under the Quick Look Approach

Avoiding a proof of market power analysis is one of the greatest benefits of the quick look approach. However, proof of market power is often a key indicator in determining whether an MFN has caused anticompetitive harm. For example, in *Delta Dental,* Delta had significant market power as Rhode Island's largest dental insurer, covering 90% of the dentists practicing in the state.[179] This evidence

[173] *Id.* at 668.
[174] *Id.*
[175] *Id.*
[176] Markham, *supra* note 164, at 638.
[177] *Id.*, at 639.
[178] *Id.*
[179] U.S. v. Delta Dental of R.I., 943 F. Supp. 172, 183 (D.R.I. 1996); *see also* U.S. v. Blue Cross Blue Shield of Mich., 809 F. Supp. 2d 665 (E.D. Mich. 2011) (finding that it was plausible that the MFNs entered into between Blue Cross Blue Shield of Michigan and various hospitals

largely contributed to the court's finding that Delta's MFN had serious anticompetitive effects for Rhode Island consumers, as Delta's market power undoubtedly helped Delta prevent competitors from entering into the dental insurance market, and, in turn, substantially increased the price of dental insurance services.[180] In an MFN analysis, however, neither party would save time or resources by avoiding a market power analysis. A defendant with little market power would be expected to introduce evidence of said lack of market power in order to rebut the presumption of illegality against MFNs. Meanwhile, plaintiffs would need to conduct their own proof of market power analysis as a rebuttal to the defense.

The *Apple* decision demonstrates the importance of proving market power in an MFN analysis. In *Apple*, the court avoided engaging in a full-scale proof of market power analysis; rather it only defined the relevant product market, an integral aspect of proving market power, since practices that harm consumers in a narrow market may have an insignificant impact or no impact at all in a broader market.[181] The court accepted the DOJ's characterization of the relevant product market: trade e-books[182] because, as expressed in the Complaint, "the anticompetitive acts at issue [] directly affect[ed] the sale of trade e-books to consumers."[183] There are no "reasonable substitutes" for e-books, including print books, since "[e]-books can be stored and read on electronic devices" and "located, purchased, and downloaded anywhere a customer has an Internet connection, while print books cannot."[184]

One issue with providing such a narrow definition of the relevant product market is that it fails to consider the possibility that the relevant product market may also include print books. The DOJ alleged, and the *Apple* court agreed, that the Publisher Defendants' fears about the adverse impact of Amazon's e-book discounting on print books was the

established anticompetitive effects as to other health insurers and the cost of health services in those areas. Blue Cross is the largest provider of commercial health insurance in Michigan, insuring more than nine times as many Michigan residents as its next largest commercial health insurance competitor).

[180] *Delta Dental*, 943 F. Supp. at 179, 183.

[181] Yancey, *supra* note 164, at 694–95; *see also* Jonathan B. Baker, *Market Definition: An Analytical Overview*, 74 ANTITRUST L.J. 129, 129 (2007) (defining the market is often the most critical step in evaluating market power; the outcomes of cases have turned more on market definition than on any other substantive issue). *See, e.g.*, U.S. v. Microsoft Corp., 253 F.3d 34, 53–54 (D.C. Cir. 2001) (largely focusing on resolving the issue of defining the relevant market).

[182] U.S. v. Apple, Inc., 952 F. Supp. 2d 638, 694 n.60 (S.D.N.Y. 2013). Trade e-books include general interest fiction and non-fiction e-books, where as "non-trade e-books include electronic versions of children's picture books and academic textbooks, reference materials, and other specialized texts that typically are published by separate imprints from trade books, often are sold through separate channels, and are not reasonably substitutable for trade e-books." Complaint, *supra* note 3, at ¶ 27.

[183] Complaint, *supra* note 3, at ¶ 99.

[184] *Id.*

impetus behind the collusive activity between Apple and the Publisher Defendants.[185] Perhaps, this is evidence that many consumers do in fact consider e-books as substitutes for print books, and print books are a competitive threat to e-books.[186] If so, the relevant product market should have also included print books, and the court may not have found Apple's MFN to be anticompetitive due to the smaller impact it would have had on the overall book—both e-book and print—market.[187]

Regardless of the plausibility of such a definition of the relevant product market, the court failed to even consider this possibility by avoiding engaging in a market power analysis. Instead, they merely accepted the DOJ's characterization of the relevant product market because "Apple did not dispute [the DOJ's] characterization."[188] This is why the quick look approach has been criticized to be little more than "an elegant substitute for *per se* labeling"[189]—it presumes an alleged practice to be illegal before fully weighing all the circumstances of the case. The rule of reason, however, requires proof of market power in order to determine whether there was actual anticompetitive harm.

2. Lack of Judicial Experience with MFNs

The quick look approach is also inappropriate for an MFN analysis because courts lack experience with analyzing MFNs. Courts should apply presumptive rules, such as the quick look approach, instead of the rule of reason *only* when "'an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets.'"[190] Antitrust scholars and practitioners have not reached this level of understanding with MFNs; "[the] analysis of MFNs is still in an embryonic stage."[191] It was only recently that the courts began to recognize the superficiality of earlier presumptions that MFNs automatically lead to lower prices.[192] The *Apple* court was also the first court to find, through a trial, that an MFN had anticompetitive effects.

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[185] Evan D. Brewer, *The E-books Price Fixing Litigation: Curious Outlier or Harbinger of Change in Antitrust Enforcement Policy?*, 6 HASTINGS SCI. & TECH. L.J. 43, 65 (2014).
[186] *Id.*
[187] *Id.*
[188] U.S. v. Apple, Inc., 952 F. Supp. 2d 638, 694 n.60 (S.D.N.Y. 2013) ("Plaintiffs have defined the relevant market as trade e-books in the United States; Apple does not dispute that characterization.").
[189] Edward Brunet, *Antitrust Summary Judgment and the Quick Look Approach*, 62 SMU L. REV. 493, 500 (2009).
[190] FTC v. Actavis, Inc., 133 S.Ct. 2223, 2237 (2013) (citing Cal. Dental Ass'n v. FTC, 526 U.S. 756 (1999)).
[191] Jay L. Levine, Moving Forward—How Has Thinking About MFNs Evolved and Where Might It Go?, *in* PANEL SUMMARIES FROM DOJ AND FTC WORKSHOP ON MOST-FAVORED-NATION (MFN) CLAUSES AND ANTITRUST ENFORCEMENT AND POLICY (Sept. 2012), http://cdn.winston.com/images/content/1/2/v2/1282/AHLA-MFN-Conference-Article.pdf.
[192] Salop & Morton, *supra* note 67, at 16.

There are many conditions that suggest that MFNs are less likely to raise antitrust concerns: MFNs received only by smaller buyers, MFNs offered by smaller sellers that lack market power, MFNs in unconcentrated markets, inputs subject to MFNs with close substitutes, inputs subject to MFNs that have uncertain value, MFNs as part of a long-term contract with locked-in or sunk assets, MFNs in exchange for significant investment, and MFNs as part of a settlement in a series of lawsuits brought against the providers.[193] With so many conditions, any of which would significantly impact a rule of reason analysis, courts should not apply the quick look approach. Until courts can say with confidence that MFNs have likely anticompetitive effects, the rule of reason analysis remains the preferable standard of review.

CONCLUSION

Based on the *Apple* court's treatment of the MFN, the court could be interpreted as holding that MFNs are *per se* illegal in effect. However, this does not change the fact that the rule of reason remains the preferable standard under which to analyze MFNs. Determining whether an MFN creates a net anticompetitive harm or pro-competitive benefit requires a full analysis of the circumstances of the case, including the conditions under which the MFN was adopted and the effects resulting from the implementation of the MFN. Neither the *per se* rule nor the quick look approach allow for such an analysis. The *per se* rule would be inappropriate because it fails to acknowledge that an MFN may have pro-competitive potential. The quick look would also be inappropriate, as it ignores a proof of market analysis, which is integral to an MFN analysis. Courts do not have enough experience with MFNs to justify a presumption of illegality against these clauses.

Perhaps, the quick look approach will be appropriate to use in an MFN analysis in the future. However, we should only abandon the rule of reason in favor of a presumption of illegality after antitrust enforcement agencies and courts are fully confident that MFNs consistently lead to anticompetitive behavior. Until then, MFNs should continue to be analyzed under the rule of reason, thereby providing both plaintiffs and defendants a fair opportunity to present their cases.

*Jennifer D. Lee**

[193] *Id.* at 18.

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