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Books and Olive Oil: Why Antitrust Must Deal with Consolidated Corporate Power

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BOOKS AND OLIVE OIL: WHY ANTITRUST MUST DEAL WITH CONSOLIDATED CORPORATE POWER

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ABSTRACT†

Following an epic battle in the marketplace between Apple and major book publishers, on one side, and Amazon, on the other side, the United States Department of Justice and thirty-three states filed an antitrust lawsuit against Apple and the publishers, alleging that they had conspired to fix the prices of ebooks. Both the district court and a divided panel of the United States Court of Appeals for the Second Circuit decided the case in the government's favor. This Article argues that government regulators and the courts took the wrong side in the dispute and did so because of fundamental flaws in current antitrust policy. Adhering to the standard approach, regulators and the courts ignored unique aspects of the industry and treated books just as they would have treated cans of olive oil. Focusing exclusively on consumer welfare—that is, consumer prices and total industry output—regulators and the courts ignored critical social, cultural, and political ramifications of the dispute. Moreover, the widely accepted view that business firms are rational profit maximizers led regulators and the courts into making serious factual misjudgments. Although there are many calls for antitrust reform, most are limited to calls for more rigorous application of existing doctrine. This case study demonstrates why that is inadequate and a paradigm shift in antitrust policy is required.

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† This Article expands upon the author's earlier publication in the *Journal of Law Reform*. *See* Carl T. Bogus, *The New Road to Serfdom: The Curse of Bigness and the Failure of Antitrust*, 49 U. MICH. J.L. REFORM 1 (2015).

Introduction

In a scene in the movie *You've Got Mail,* Kathleen Kelly accuses Joe Fox of comparing books to cans of olive oil.[1] As those who have seen this wonderful romantic comedy will remember, Kelly, played by Meg Ryan, is the owner of an independent children's bookshop, and Fox, played by Tom Hanks, is an owner of a chain of book superstores that can afford to discount. When Fox opens a superstore near Kelly's small shop, he presents an existential threat to her business. Fighting for survival, Kelly gives an interview to a local television station. "I have to say, I have met Joe Fox, and I have heard him compare his store to a price club and the books in it to cans of olive oil," she tells the reporter.[2]

It was no accident that screenwriters Nora and Delia Ephron chose to make the struggle between Joe Fox and Kathleen Kelly about how books are presented and sold to the public. Books are special. They help elevate people from materialistic, self-centered beings into something more: creatures who create, preserve, and transmit knowledge; who are carried to imaginary lands by literature; and who ponder the meaning of existence. Books not only enrich individual lives but play a critical role in democracy for, as André Schiffrin put it, "[i]t is only in books that arguments and inquiries can be conducted at length and in depth."[3] It was not by chance that the screenwriters chose to make Kathleen Kelly's Shop Around the Corner a children's bookshop where Kelly regularly

1. YOU'VE GOT MAIL (Warner Brothers 1998).
2. *Id.*
3. ANDRÉ SCHIFFRIN, THE BUSINESS OF BOOKS: HOW INTERNATIONAL CONGLOMERATES TOOK OVER PUBLISHING AND CHANGED THE WAY WE READ 171 (2000). Schriffrin headed Pantheon Books for twenty-eight years before founding The New Press.

reads to enthralled children and knowledgeably recommends books that will stimulate their imagination and love of learning.

In comparing books to olive oil, Joe Fox was not, in fact, denying the special importance of books; he was merely suggesting that there is nothing unique about the economics of books.[4] Consumers benefit from lower prices for all products, and the laws of economics—such as economies of scale—apply just as much to selling books as to selling cans of olive oil. We may have nostalgic memories of the small bookstore we patronized long ago, but it makes no more sense to resist Fox Books in favor of the Shop Around the Corner than it did to resist the modern supermarket in favor of the mom-and-pop grocer.[5] Times change; the marketplace decides. That was Joe Fox's argument.

At first, the audience sympathizes with Kathleen Kelly, but by the end of the film the audience realizes the issue is complex. Fox Books provides many things that Kelly's small store could not: lower prices, greater selection, comfortable chairs in which to relax and look at books, and a coffee shop with cappuccinos. On the other hand, Kelly's shop was not merely a business; it was a labor of love. Kelly was a connoisseur of children's literature and knew her customers. She could recommend just the book for any child's current interest and stage of development.

In the twenty years since *You've Got Mail,* the one constant in book distribution has been continuous, unpredictable change. During the 1990s and early 2000s, about half of all independent bookstores went out of business as customers flocked to the Fox Books of the world.[6] At the moment, independent bookstores are making at least a minor comeback.[7] Now chain superstores may be

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4. Actually, Kathleen Kelly was mistaken. Joe Fox never compared his store to a price club or books to cans of olive oil. Rather, Fox had accused Kelly of assuming he sold books as if they were cans of olive oil. YOU'VE GOT MAIL (Warner Brothers 1998).

5. A century ago, there was just such a movement to hold back supermarkets and protect these small businesses. *See generally* MARC LEVINSON, THE GREAT A&P AND THE STRUGGLE FOR SMALL BUSINESS IN AMERICA (2011).

6. In 1991, there were 5,100 members of the American Booksellers Association (which may be the best metric of the number of independent booksellers because ABA membership does not include pharmacies, convenience stores, department stores, and other retailers that carry books within a much broader inventory). JOHN B. THOMPSON, MERCHANTS OF CULTURE: THE PUBLISHING BUSINESS IN THE TWENTY-FIRST CENTURY 31–32 (2d ed. 2012). By 2009, that number had fallen to 1,401. *See Number of Independent Bookstores in the United States from 2009 to 2017*, STATISTA (last visited Oct. 11, 2018), http://www.statista.com/statistics/282808/number-of-independent-bookstores-in-the-us/.

7. As of 2016, there are 1,775 companies operating independent bookstores. *Number of Independent Bookstores in the United States from 2009 to 2017*, STATISTA (last visited Oct. 11, 2018), http://www.statista.com/statistics/282808/number-of-independent-bookstores-in-the-us/. While the present number of independent booksellers is less than thirty-five per-

an endangered species. Borders, which had been the second largest superstore chain, went out of business in 2011.[8] Barnes & Noble remains, but it is closing stores and laying off employees, and industry analysts are debating whether it will survive.[9] The dominant bookseller in the United States is Amazon. Amazon accounts for more than forty percent of all of the books sold in the United States—hardback, paperback, and electronic—and two-thirds of all ebooks.[10] That is how things stand right now. No one can say what the market will look like in five years.

This Article deals with an epic battle that Apple and five book publishers waged against Amazon in late 2009 and early 2010. At that time, Amazon was selling ninety percent of all ebooks in America. It was, moreover, protecting its de facto monopoly by selling the most popular ebooks—new releases and bestsellers—below cost, thereby deterring potential rivals from entering the market. Apple wanted to open an ebook store for its new iPad customers, but it did not want to do so at a loss. Apple and the publishers agreed on a new pricing model that effectively ended below-cost pricing by all ebook retailers. Amazon complained to the Federal Trade Commission (FTC) that Apple and the publishers had conspired to fix prices and to force Amazon to raise its pricing to the prescribed level. In April 2012, the United States and thirty-three states filed a complaint in federal court, alleging that Apple and the book publishers had engaged in unreasonable restraints of trade, in violation of Section 1 of the Sherman Act.[11] The publishers settled and entered into consent decrees. The case proceeded to trial against Apple alone. Following a three-week bench trial, District Judge Denise Cote issued a seventy-page opinion in the

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cent of what it was in 1991, the number has risen modestly each year for the past seven years. *Id.*; THOMPSON, *supra* note 6, at 31–32.

8. Borders, which had eighty-five superstores in 1994, filed for bankruptcy and closed all of its stores in 2011. THOMPSON *supra* note 6, at 30. Meanwhile, the number of Barnes & Noble stores has declined each year from 2008 to 2015. *See Number of Barnes & Noble stores from fiscal year 2005 to fiscal year 2018*, STATISTA (last visited Oct. 11, 2018), http://www.statista.com/statistics/199012/number-of-barnes-noble-stores-by-type-and-year-since-2005/.

9. *See, e.g.*, Casey Quackenbush, *Barnes & Noble Is Laying Off Workers Amid Declining Sales*, FORTUNE (Feb. 13, 2018), http://fortune.com/2018/02/13/barnes-noble-layoff-workers-declining-sales; *How Can Barnes & Noble Avoid Borders' Fate?* KNOWLEDGE@WHARTON (Dec. 18, 2015), http://knowledge.wharton.upenn.edu/article/can-barnes-noble-avoid-borders-fate/.

10. Franklin Foer, *Amazon Must Be Stopped*, NEW REPUBLIC, Oct. 27, 2014, at 20.

11. United States v. Apple Inc., 952 F. Supp. 2d 638 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015), *cert. denied*, 136 S. Ct. 1376 (2016).

government's favor.[12] Apple appealed, a divided panel of the Second Circuit affirmed, and the Supreme Court denied certiorari.

As this Article will show, the government and the courts took the wrong side in this dispute. In siding with Amazon, they sided with a firm that had a monopoly and was preserving that position through predatory practices. Instead of addressing this monopoly, they punished the parties that sought to break it up. And it is even worse than that. Amazon was threatening to extend its monopoly in the retailing of ebooks into a monopoly in the retailing of *all* books. The economic consequences of that would be dire, but the political and cultural ramifications of having a single retailer of all books in the United States would be far worse. If that came to pass, one firm could decide which books to promote—through homepage displays, search engine results, recommendations, and otherwise—and which books to make inconspicuous.

All of this should have been obvious to the experienced attorneys in the Antitrust Division of the Department of Justice (DOJ) and the capable federal judges who handled this case. Yet, it was not. Why? This Article attempts to answer that question.

Although this Article uses books as a case study, it is about much more than books. The principal objective is not to show that regulators and courts reached the wrong result in this one case, as important as the case was. Rather, building on an argument I have previously advanced,[13] I use this case to illustrate why we need a paradigm shift in antitrust law. Under the current paradigm, antitrust is concerned exclusively with consumer welfare: What causes consumer prices to rise is bad, and what causes them to fall is good.[14] Everything else is largely ignored.[15] This blinkered view led regulators and judges astray in the Amazon case. Because they had

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12. The plaintiffs in the lawsuit were the federal government and thirty-three states, but the U.S. Department of Justice took the lead for all plaintiffs in the litigation. For simplicity's sake, therefore, when referring to the plaintiffs, this Article generally uses the singular term "government."

13. Carl T. Bogus, *The New Road to Serfdom: The Curse of Bigness and the Failure of Antitrust*, 49 U. MICH. J.L. REFORM 1 (2015) [hereinafter Bogus, *The New Road to Serfdom*]; *see also* Carl T. Bogus, *Trust-Busting: Labor's Forgotten Cause,* 26 NEW LAB. F. 46 (2017) (expanding on aspects of the central thesis involving worker freedom and wages).

14. In theory, total industry output is even more important than consumer prices, but prices and output are considered inextricably interlinked: When prices rise, output falls and vice versa. Thus, focusing on prices automatically embraces output. *See infra* note 383 and accompanying text.

15. While in theory consumer welfare includes product variety, quality, and innovation, these considerations are generally given little, if any, weight. *See, e.g.*, Rebecca Haw Allensworth, *The Commensurability Myth in Antitrust*, 69 VAND. L. REV. 1, 56 (2016); Robert H. Lande, *Consumer Choice as the Ultimate Goal of Antitrust*, 62 U. PITT. L. REV. 503, 525 (2001).

become accustomed to thinking of low prices as antitrust law's North Star, the Department of Justice and the courts overlooked the fact that Amazon's prices had been *too* low. Those prices had not been set through marketplace competition, nor did they reflect the cost of production. They were below-cost prices, artificially suppressed for predatory purposes. Additional fundamental problems with the existing paradigm complicated matters. This paradigm—heavily influenced by the Chicago School of law and economics—prefers logic to experience.[16] Its fundamental principles are assumptions, which it treats as axioms, and from which it deduces further principles and rules and even makes factual determinations about what parties intended. Its most basic principle is the assumption that people and businesses are rational maximizers.[17] That assumption subtly convinced the regulators and courts that the publishers must have been acting to increase short-term profits, and it made them incredulous that the publishers actually accepted lower profits to destroy Amazon's chokehold over ebooks.

The courts did just what Kathleen Kelly accused Joe Fox of doing—treating books just as they would have treated cans of olive oil or any other commodity. This approach flows naturally from a system that attempts to employ universal axioms. But, books are not olive oil. The current antitrust paradigm employs a cookbook approach to antitrust. As a result, the regulators and courts failed to consider not only unique aspects of books themselves, but special features of the business of book publishing and distribution. And most importantly, by focusing exclusively on consumer welfare, government regulators and the courts overlooked critically important social, cultural, and political issues, including what it would mean for American democracy if one firm can effectively determine which books are read.

Books, of course, are unique and have unique importance. This Article does not argue, however, that because books are unique, a different set of antitrust rules must be developed for them. This Article argues that—with respect to all products and industries—antitrust should not be concerned with consumer welfare alone. It should also be concerned with social and political consequences of consolidated corporate power, and to do that, it is necessary to understand the special features of the particular industry involved. All

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16. *See infra* notes 375–80 and accompanying text.
17. *See infra* notes 378–79 and accompanying text.

industries have their own special features. In this particular case, the industry was books, and it is necessary to learn a bit about the book business to understand the ramifications of consolidated power in that industry. Justice Louis D. Brandeis advocated for this approach and began every problem by intensively examining the facts.[18] He considered this so important, he believed that law schools should teach "that lawyers should not merely learn rules of law" but should also study the "facts, human, industrial, social, to which they are to be applied."[19] This approach is precisely *not* what the regulators and courts did in this case. The objective is not to condemn them, however; it is to show how currently-accepted antitrust thinking misled them and why a new antitrust paradigm must emerge.

Part I of this Article will, therefore, be about the business of book publishing and retailing. It is organized by describing, in turn, the parties in the three-way struggle between six book publishers, Amazon, and Apple. This organization allows a more or less chronological description of the book industry, the commercial and cultural context in which the Amazon dispute arose, and the underlying events. Part II will describe and critique the opinions by the district and circuit courts in the case. This Part will show how the courts could have reached the opposite result under existing doctrine. By doing so, I hope to demonstrate that even though we need a paradigm shift in antitrust doctrine, that does not mean that all antitrust doctrine, developed over more than a century, will suddenly be irrelevant. What matters most of all is a fundamental shift of worldview. Rather than having the single North Star of consumer welfare, antitrust must take into account other values. That shift will enable regulators and courts to apply many existing rules and principles more wisely. Part III will provide a more direct argument for why antitrust must be concerned first and foremost with consolidated corporate power and what that means. A brief Conclusion follows.

I. THE BOOK INDUSTRY

There were no Lilliputians in this dispute. This was a three-way contest involving the six largest book publishers, the largest book

18. MELVIN I. UROFSKY, LOUIS D. BRANDEIS: A LIFE 130, 157 (2009).
19. *Id.* at 209 (quoting Brandeis); *see also* JEFFREY ROSEN, LOUIS D. BRANDEIS, AMERICAN PROPHET 89–90 (2016).

retailer, and another large firm that wanted to enter the book retailing business. There were, nevertheless, significant disparities of power. One combatant, Amazon, had enormous market power in book retailing generally and a monopoly in one segment of that market, namely, ebooks. It protected that monopoly by selling below cost; and if the monopoly lasted long enough, it might become irreversible. All of this presented an existential threat to a second group of combatants, the book publishers. A battle ensued when another combatant, Apple, decided to enter the market—but only if it could demolish the existing system. Most importantly, the public had an enormous stake in the outcome of that battle.

A. *The Publishers*

At the time of the dispute, there were six major trade book publishers in the United States.[20] Together these six firms published roughly two-thirds of all books sold in the United States.[21] All six had been built through numerous mergers and acquisitions over a period of decades, and each published books under many different imprints. Random House, for example, published books under at least two dozen imprints, including Anchor, Alfred A. Knopf, Crown, Doubleday, Pantheon, and Vintage, all of which had once been the names of independent firms.[22] The other five major publishers were The Hachette Group,[23] HarperCollins,[24] MacMillan,[25] The Penguin Group,[26]and Simon & Schuster.[27] Random House and

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20. This Article generally focuses on trade book publishers, that is, firms that publish general interest books, fiction or nonfiction, for profit. Trade publishers can be distinguished from academic publishers, who are typically non-profit enterprises subsidized to some extent by universities or specialty publishers for religious, educational, or medical books. These distinctions are generally accurate even though there are not always clear lines between the categories. Academic publishers may be expected to be financially self-sufficient or even profitable, for example, and The Free Press may be classified as a trade publisher even though it is a non-profit company.

21. Boris Kachka, *Book Publishing's Big Gamble*, N.Y. TIMES, July 10, 2013, at A21.

22. THOMPSON, *supra* note 6, at 410; *Imprints of Knopf Doubleday Publishing Group*, http://knopfdoubleday.com/imprints/ (last visited Sept. 26, 2018).

23. Hachette published books in the United States under at least seventeen imprints, including Little, Brown & Company, Springboard Press, and Twelve. THOMPSON, *supra* note 6, at 412.

24. HarperCollins published books in the United States under at least twenty-three imprints, including Ecco, Harper, and William Morrow. *Id.* at 412–13.

25. McMillan's formal corporate name was Holzbrinck Publishers. It published books in the United States under at least nineteen imprints, including Farrar, Straus & Giroux, Henry Holt, Hill & Wang, and St. Martin's Press. *Id.* at 413.

26. The Penguin Group published books in the United States under at least thirty imprints, including G.P. Putnam's Sons, Grosset & Dunlap, Putnam, and Viking. *Id.* at 411.

Penguin have since merged, reducing the Big Six publishing houses to a Big Five.[28] A brief history of how these companies were assembled helps illuminate the unique features of book publishing.

In the first half of the twentieth century, book publishing was populated by dozens of relatively small, independent firms.[29] Some were family businesses. Many were owned entirely, or at least in significant part, by their top executives, who were a rather special, self-selected group.[30] These executives were, to be sure, businessmen interested in making a profit, but most had chosen book publishing—rather than, say, olive oil cannery—because they loved books and considered publishing something of a public-interest endeavor as well as a business.[31] The salaries of publishers were traditionally closer to those of university professors than executives in other industries.[32] Firms occasionally merged during this period. Most mergers occurred because executives of two firms had similar views about what they wanted to publish, had compatible title and author lists, and thought a combined firm would have greater prestige.[33]

Beginning in the early 1960s, things changed.

Along with other sectors of the economy, publishers began to pursue mergers aggressively.[34] Although the merger trend has continued unabated ever since, there have been distinctly different merger waves. The first wave occurred because media conglomer-

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27. Simon & Schuster published books in the United States under at least ten imprints, including Free Press, Pocket Books, Scribner, and Touchstone. *Id.* at 413.

28. *Id.* at 410–14; Julie Bosman, *Penguin and Random House Merge, Saying Change Will Come Slowly*, N.Y. TIMES (July 1, 2013), https://www.nytimes.com/2013/07/02/business/media/merger-of-penguin-and-random-house-is-completed.html.

29. THOMPSON, *supra* note 6, at 102.

30. *See id.*

31. André Schiffrin, for example, says that in the 1960s, he and his colleagues at Pantheon had "the conviction that we were participating in a common enterprise of shared cultural and political value." SCHIFFRIN, *supra* note 3, at 54. Bennett Cerf describes how, as a young man, he moved from a Wall Street brokerage firm to a small book publishing house, motivated by loving books and being star-struck by famous authors. BENNETT CERF, AT RANDOM: THE REMINISCENCES OF BENNETT CERF 25–28 (2d ed. 2002). Two years later, Cerf formed a partnership with a friend, Donald Klopfer, who also loved books. *Id.* at 54–55. Throughout their memoirs, both Schiffrin and Cerf recount with pride examples of books that they published, even though they knew that they would not be profitable, because they considered them to be socially important works.

32. SCHIFFRIN, *supra* note 3, at 120.

33. For example, see Bennett Cerf's description of Random House's first acquisition, namely, the firm of Smith and Haas in 1936. CERF, *supra* note 31, at 123.

34. THOMPSON, *supra* note 6, at 103–08. A catalyst for the first merger waves was that some of the larger publishers decided to go public. Both Random House and Penguin became public companies in 1961. *See* CERF, *supra* note 31, at 284; THOMPSON, *supra* note 6, at 119–20.

ates decided that book publishing offered synergies with their other corporate divisions. In 1965, Time-Life and Random House became interested in merging.[35] The principal rationale was that Time-Life, which published magazines for affluent subscribers, had a mail order list that could be used effectively to market Random House books. The companies abandoned the potential deal because informal discussions with the Department of Justice suggested that the government would oppose the merger on antitrust grounds. Very quickly thereafter, RCA acquired Random House. The deal was based on the rationale that Random House's textbook division could provide content for teaching machines to be developed by RCA.[36] During the same period, Viacom, which owned Paramount Pictures among other properties, acquired Simon & Shuster, and the Los Angeles Times Mirror Company acquired The New American Library.[37]

All of those corporate marriages ended in divorce. One of the principal reasons that these mergers failed is that the promised synergies never materialized.[38] That problem is not unique to books; throughout the corporate world the vision of merger synergies often turns out to be a mirage.[39] However, the mergers also failed for a more industry-specific reason. Book publishing is a low profit-margin industry. Traditionally, book publishers make a four to eight percent profit.[40] The conglomerates thought that, in addition to increasing profitability through synergies, they could increase profit margins by introducing more modern business practices to the stodgy world of book publishing.[41]

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35. For descriptions of both the discussions between Time-Life and Random House and RCA's subsequent acquisition of Random House, see THOMPSON, *supra* note 6, at 106–07; CERF, *supra* note 31, at 285–87.

36. SCHIFFRIN, *supra* note 3, at 74.

37. *See id.* at 47–48, 70. Similar dynamics were at play in Great Britain, too. In 1970, the British conglomerate Pearson PLC acquired Penguin Books. *Id.* at 47. That merger did last however.

38. John B. Thompson writes that the merging partners discovered that "'teaching machines' were a figment of the technological imagination at the dawn of the digital revolution," and that movie rights did not automatically follow publication rights but were retained for separate sale by writers' agents. THOMPSON, *supra* note 6, at 107.

39. *See, e.g.*, Edward A. Blackstone & Joseph P. Fuhr Jr., *Failed Hospital Mergers*, 36 J. HEALTH L. 301, 302–03 (2003); James A. Fanto, *Quasi-Rationality in Action: A Study of Psychological Factors in Merger Decision-Making*, 62 OHIO ST. L.J. 1333, 1334–35, 1368–72 (2001); James A. Fanto, *Breaking the Merger Momentum: Reforming Corporate Law Governing Mega-Mergers,* 49 BUFF. L. REV. 249, 255 (2001).

40. *See* SCHIFFRIN, *supra* note 3, at 118 (suggesting that the typical profit margin is around four percent); THOMPSON, *supra* note 6, at 149 (suggesting that six to eight percent is typical and three to four percent is not uncommon).

41. THOMPSON, *supra* note 6, at 107.

Once book publishers found themselves part of corporate conglomerates, they found themselves subjected to pressure to acquire other publishing firms. Rapid growth and fat profit margins are highly desired by large corporations because investors are constantly looking for high-performance stocks. The easiest way to grow quickly is by buying other companies; it is much more difficult to grow by outperforming rivals. But mergers can be a short-term fix because investor focus immediately turns to the profit margin of the combined entity, and for reasons we will turn to shortly, the traditionally low profit-margins of book publishers turned out to be more durable than the acquirers imagined.

A second wave of mergers started in the late 1970s. For the most part, a different set of corporations purchased the book publishers. In 1987, Rupert Murdoch's News Limited, which also owned newspapers, purchased Harper & Row.[42] Two years later, the Newhouse family, which owned newspapers and magazines, purchased Random House from RCA.[43] Meanwhile, the French firm Hachette began purchasing book publishers.[44] The main objective in this wave was to achieve efficiencies through consolidations, and therefore the parent companies also purchased other book publishers.[45] Shortly after buying Random House, for example, the Newhouse family purchased Crown Books,[46] and Murdoch's firm purchased the British book publisher William Collins & Sons.[47] This second wave continues unabated to the present day. Imprints and entire publishing groups are bought and sold in what seems like a never-ending game of musical chairs—so much so that even people in the industry have a difficult time knowing who owns what at any given time. Meanwhile, the trend toward greater consolidation has been relentless.

But consolidation has not changed one basic fact about trade book publishing: It is an industry with relatively thin profit margins. Economies of scale may have increased profit margins to some extent. It appears that when firms were independent, profit

42. SCHIFFRIN, *supra* note 3, at 69; *Company Profile*, HARPERCOLLINS PUBLISHERS, http://corporate.harpercollins.com/about-us/company-profile (last visited Oct. 27, 2018).

43. *Id.* at 77–81.

44. THOMPSON, *supra* note 6, at 121–24.

45. *See id.* at 108–18, 379–83.

46. SCHIFFRIN, *supra* note 3, at 80.

47. *Company Profile*, *supra* note 42.

margins were traditionally in the four to five percent range.[48] By consolidating some functions, such as printing, warehousing, distribution, accounting, sales forces, and negotiations with major retailers, the now-larger publishing groups reduced overhead and increased profit margins to some extent.[49] Nevertheless, profit margins are most often in the six to eight percent range, and margins of three to four percent are still not uncommon.[50] Dreams of profit margins of twelve to fifteen percent have proved elusive.[51]

Why is it so difficult to achieve larger profit margins in trade book publishing? First, it is an industry with significant costs. Reputable trade presses invest considerable time and money on every book they publish. Each book goes through at least two separate edits, first for content and then for typographical and grammatical errors, syntax, and style. The publisher also designs the dustjacket and promotes the book with book review editors and retailers. Finally, publishers experience significant costs in returns, that is, unsold books that retailers return for credit.[52]

The publisher also pays the author an advance against royalties.[53] Authors generally receive royalties of fifteen percent on the retail price on hardcover books. Advances, however, are nonrefundable so that if an advance is not "earned out," that is, if the book does not sell well enough for the author to fully earn the advance, the author benefits at the publisher's expense. Agents for brand name authors negotiate large advances, making the profitability of even these books uncertain. One larger publisher estimated that as a result of all of these pressures, the actual split of net revenues is a ratio somewhere around 75/25 or 80/20 in favor of the author.

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48. *See* SCHIFFRIN, *supra* note 3, at 119 (stating that conglomerate profit margin targets were in the twelve to fifteen percent range, which was "three to four times what publishing houses have made in the past").

49. THOMPSON, *supra* note 6, at 148–52.

50. *Id.* at 149.

51. When it purchased Random House in 1998, the German firm Bertelsmann predicted that Random House (which already included Bantam, Doubleday, Dell, and other imprints) would achieve a fifteen percent profit margin, and corporate targets are generally for-profit margins in the twelve to fifteen percent range. SCHIFFRIN, *supra* note 3, at 115, 119. Nevertheless, profit margins have proved to be "stubbornly low," and profit margins of ten percent are exceptional. THOMPSON, *supra* note 6, at 107, 149.

52. Retailers tend to order more copies of a new book than they wind up selling, and if a title is not moving, retailers will pack up and return its unsold inventory within ninety days or so. The rate of return for new books by trade publishers generally runs around forty-five percent. THOMPSON, *supra* note 6, at 285.

53. This discussion of royalties and the effective split of net revenues between publisher and author is drawn from THOMPSON, *supra* note 6, at 216–17.

The revenue side of the ledger is equally difficult because no one has found a way to reliably predict which books will be profitable. There are some exceptions to this general rule. If an author, such as George R.R. Martin or David McCullough, has an established fan base, sales of that author's previous books can be a reasonable predictor of how the author's next book will do.[54] Beyond that, publishing executives—no matter how experienced and savvy—can only make uncertain guesses about what will sell.[55]

Working in an industry with small profit margins was acceptable to many people who traditionally went into book publishing because they knew that, while they were unlikely to become wealthy, they could eke out a reasonably comfortable living in an endeavor they loved and found gratifying. They hoped for the occasional bestseller, but their bread and butter were books that were moderate successes—books that would turn a profit by selling 10,000 copies and wind up selling 30,000 copies. Further, books that continued to sell a few hundred copies every year for ten or even thirty years on the publisher's backlist provided financial ballast.[56]

The consolidation of publishers has not changed the hard realities of the business. It has, nevertheless, changed attitudes. Consolidation created much larger firms, which in turn increased corporatization. The new owners—whether shareholders in a public company or private investors—see the enterprise more as a profit-making endeavor and less as a contribution to society. Profit margins of four to five percent are not sexy enough for investors.[57] This has made publishers search more intensively for breakout books, "black swans" that will become mega-sellers.[58] But as quintessential examples—such as *Harry Potter and the Sorcerer's Stone,* which was rejected by twelve publishers before it found a home,[59] and *Capital in*

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54. *Id.* at 190, 212–19.

55. Editors are reluctant to admit how great the level of uncertainty is. After all, the editor's job is to select potential winners out of a mountain of proffered manuscripts, just as the stockbroker's job is to select potential winners in the stock market. On the condition that he would not be identified, someone who spent his career in book publishing conceded: "Why is it that this book we're really hot on turns out to be an absolute bomb and then something we just didn't expect at all takes off? . . . We don't know, *we just don't know*." *Id.* at 191 (emphasis in original) (quoting the unnamed publishing executive).

56. *Id.* at 220–22.

57. *See* SCHIFFRIN, *supra* note 3, at 107 (quoting a knowledgeable source as stating that "mergers have increased the obsession with the bottom line," and also reporting that the "big companies impose sales quotas.").

58. This discussion of how publishers must rely on big books is drawn from THOMPSON, *supra* note 6, at 188–212.

59. Sam Marsden, *The Cuckoo's Calling: publishers' embarrassment at turning down JK Rowling detective novel*, THE TELEGRAPH (July 14, 2013, 6:59 PM), http://www.telegraph.co.uk/

the Twenty-First Century, a dense book with charts and mathematical formulae about income inequality in Western societies that astonished everyone by becoming a runaway, international bestseller[60]—demonstrate, no one can confidently predict which books will be blockbusters. Nevertheless, corporatization has forced publishers into relentlessly seeking bestsellers and super-bestsellers. That, in turn, has led them to publish and heavily promote books that seem comparable to recent bestsellers.[61]

Consolidation has not only created financial incentives for a business model based on a search for bestsellers and blockbusters, but it has also made that business model more feasible. Just as an investor is more likely to purchase a stock that skyrockets in value if she buys positions in, say, two hundred companies rather than twenty companies, a book publisher has a better chance of publishing bestsellers if, through its multiple divisions, it publishes two hundred titles a year rather than twenty titles. That does not mean the model works perfectly—or even very well. No matter how careful the selection process, unprofitable and barely profitable books are likely to outnumber very profitable books. And the competition for brand-name authors whose works can be reliably expected to become bestsellers results in publishers over-guaranteeing their royalties with large advances, thereby reducing profit margins even on bestsellers.[62] All of this explains why book publishing remains an industry with relatively small profit margins, even among the large, top-tier publishers.

Consolidation has not reduced the number of books being published. On the contrary, there has been a general upward trend in the number of different titles published annually in the United States.[63] Nor, by most accounts, has the quality of the work publish-

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culture/books/10178960/The-Cuckoos-Calling-publishers-embarrassment-at-turning-down-JK-Rowling-detective-novel.html.

60. Marc Tracy, *Picketty's 'Capital': A Hit That Was, Wasn't, Then Was Again*, NEW REPUBLIC (Apr. 24, 2014), https://newrepublic.com/article/117498/pikettys-capital-sold-out-harvard-press-scrambling; *see also* Sam Tanenhaus, *Hey, Big Thinker*, N.Y. TIMES (Apr. 27, 2014), http://www.nytimes.com/2014/04/27/fashion/Thomas-Piketty-the-Economist-Behind-Capital-in-the-Twenty-First-Century-sensation.html?_r=0.

61. THOMPSON, *supra* note 6, at 202–04.

62. *Id.* at 216.

63. Before 1980, traditional book publishers published less than 50,000 different book titles per year in the United States. *Id.* at 239. This climbed to 265,000 in 2000, and about 316,000 in 2010. *Id.* at 240. Since that time, the number of different titles seems to have plateaued or slightly decreased. In 2014, 309,957 different titles were published by traditional book publishers in the United States, a slight reduction from the prior year. *Traditional Print Book Production Dipped Slightly in 2013*, BOWKER (Aug. 5, 2014), http://www.bowker.com/news/2014/Traditional-Print-Book-Production-Dipped-Slightly-in-

ers do—particularly in editing—declined.[64] The question of whether consolidation has, on the whole, been good for authors is more difficult to answer. Famous writers, from Daniel Silva and Nora Roberts to Hillary Clinton and Bill O'Reilly, have surely benefitted from greater capital and fiercer competition for potential blockbusters. Meanwhile, less famous authors may be disadvantaged because some large publishing groups forbid their constituent imprints from bidding against each other for new titles.[65] An author who may have two or three publishers interested in her book in an unconsolidated industry may, in the current era, only have one interested publisher.

Perhaps the most worrisome result of consolidation is the homogenization of published content. As previously mentioned, the more-intense search for future bestsellers causes publishers to look for books similar to past bestsellers. Still, with more than 300,000 different titles published in the United States each year, there is a very rich diversity in books published. But there is less diversity in what publishers vigorously market and promote, and thus there is less diversity in what comes to readers' attention. Sociologist John B. Thompson, who has studied book publishing, explains:

> [T]he key issue in the field of trade publishing today is not so much diversity of output, it is diversity in the *marketplace*. In other words, the real source of concern is not the diversity or otherwise of the books that are *published,* but rather the diversity or otherwise of the books that are *noticed, purchased and read*. The field may be characterized by an ex-

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2013.html. Not all of these are trade books; a significant share are academic works. Nevertheless, about 50,000 fiction titles are published annually. THOMPSON, *supra* note 6, at 241.

64. *See* THOMPSON, *supra* note 6, at 145 (stating that "it is difficult to see any substance in the view that, as a general trend, editors in the large corporations do less editing today than editors did in the past"). *But see* SCHIFFRIN, *supra* note 3, at 152 (arguing that oligopoly and corporatization are turning books into "mere adjuncts to the world of the mass media, offering light entertainment and reassurances that all is for the best in this, the best of all possible worlds").

65. *See* SCHIFFRIN, *supra* note 3, at 81 (criticizing the practice of allowing constituent imprints to bid against each other because it leads to much higher advances for famous authors); THOMPSON, *supra* note 6, at 139 (stating that in some instances publishing companies allow their imprints to bid against each other while in other instances there is one house bid with the understanding that, if successful, the author and agent may select which of the company's imprints will publish the book); Kachka, *supra* note 21, at A23 (describing a "persistent gripe of writers and agents" that large publishing companies either forbid or restrict their constituent imprints from bidding against each other for manuscripts). Schiffrin also argues that consolidation has resulted in the CEOs of parent corporations personally directing that their book publishers pay excessive advances for books by powerful friends and politicians. SCHIFFRIN, *supra* note 3, at 80–81.

> tremely diverse output, but if only a very limited number and range of titles are picked out and noticed—that is, made visible in a crowded marketplace—then we have a different kind of problem about diversity.[66]

This is a very important point—one very much related to the problem of treating books like cans of olive oil[67]—and one discussed below. For now, it just bears highlighting that there may be just as much output in the industry as before, and just as much diversity in the total output—that is, just as many different titles published and in just as broad a spectrum of genres and topics—but far less diversity in which books are brought to readers' attention and, therefore, find an audience.

Perhaps surprisingly, consolidation has not reduced the total number of book publishers. In fact, there are more book publishers than ever before.[68] In 2004, there were an estimated 62,815 book publishers in the United States. That is an astounding number. However, only 6.5 percent of the publishers had annual revenues exceeding $1,000,000, and nearly three-quarters of them had annual revenues of no more than $50,000.[69] Why are there so many small—even tiny—publishers? The principal reason is that the costs of entry are quite low in this industry. Moreover, desktop publishing replacing physical typography has further lowered entry costs.[70] Someone who loves books and dreams about being a publisher can set up shop and try to succeed. Small publishers, however, are often undercapitalized and under constant financial stress.[71]

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66. THOMPSON, *supra* note 6, at 397. One is reminded of the words of poet Thomas Gray:

> Full many a gem of purest ray serene,
> The dark unfathom'd caves of ocean bear:
> Full many a flow'r is born to blush unseen,
> And waste its sweetness on the desert air.

ELEGY WRITTEN IN A COUNTRY CHURCHYARD 8 (5th ed. 1751).

67. Ironically, the corporatization of the industry as a whole, which included previously-independent publishers being absorbed into conglomerates and the growth of chain bookstores, resulted in books being increasingly treated like other commodities by the industry itself. Thompson observes that "the more books were treated like any other commodity and subjected to the same principles of retailing, the more the chains would be forced to focus on fast-selling titles by brand-name authors at the expense of those titles that would add depth and range to the store but that would have much slower stock turns." THOMPSON, *supra* note 6, at 35.

68. *Id.* at 153.

69. *Id.*

70. *Id.* at 155.

71. *Id.* at 162.

As already noted, success in this industry depends not merely in publishing a book but in getting a book noticed. Small publishers do not have the same contacts with book review editors at major newspapers and magazines or to producers at syndicated radio shows, not to mention the resources to pay retailers to feature their books at tables in the front of a bookstore or on their website homepages.[72] It has long been said that "every independent publisher is just one crisis away from bankruptcy," and that statement appears to be especially true today.[73]

On the whole, however, until recently book publishing was a relatively stable industry—at least for large and medium-sized firms. It may have been an industry with inherently small profit margins (despite the demands of new corporate chieftains) and its share of challenges, but it was, nevertheless, an industry that produced something of great value for which there will always be a reliable and durable demand. That, at least, was the traditional view. In 2004, however, dark clouds appeared on the horizon. The National Endowment for the Arts (NEA) released a report titled *Reading at Risk*.[74] The document began:

> *Reading at Risk* is not a report the National Endowment for the Arts is happy to issue. This comprehensive survey of American literary reading presents a detailed but bleak assessment of the decline of reading's role in the nation's culture. For the first time in modern history, less than half of the adult population now reads literature, and these trends reflect a larger decline in other sorts of reading.[75]

As social trends go, this one was moving quickly.[76] Most concerning of all, the rate of decline was greatest among young adults. For

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72. Publishers pay large retailers to display their books. *Id.* at 35.

73. *Id.* at 173.

74. NATIONAL ENDOWMENT FOR THE ARTS, READING AT RISK: A SURVEY OF READING IN AMERICA (2004), https://www.arts.gov/publications/reading-risk-survey-literary-reading-america-0.

75. *Id.* at vii.

76. In just the past twenty years, the portion of adult Americans reading literature had dropped 10.2%. *Id.* at ix. "Literature" was defined as novels, short stories, plays, and poetry. *Id.* at 1. The portion of Americans who said they had read any form of literature for leisure over the past twelve months declined from 56.9% in 1982 to 46.7% in 2002. *Id.* at ix. There was a parallel drop in reading nonfiction as well. *Id.* A second NEA study confirmed the drop in reading three years later. NATIONAL ENDOWMENT FOR THE ARTS, TO READ OR NOT TO READ: A QUESTION OF NATIONAL CONSEQUENCE (2007), https://www.arts.gov/sites/default/files/ToRead.pdf. Among other things, the second survey found that over a ten-year period the average spending on books by American households fell from an already paltry

example, the percentage of Americans reading literature in the eighteen to twenty-four years of age group dropped seventeen percent in the past two decades, a decline rate of twenty-eight percent.[77] While book publishing was not about to suddenly disappear, it now looked like an industry with a declining market.[78]

Meanwhile, something equally disturbing—and far more immediate—was going on.

B. *Amazon*

In 1994, Jeff Bezos left Manhattan and the hedge fund at which he worked, moved to Seattle, and founded Amazon.[79] Bezos' objective was to create a company that would sell commodities of all kinds over the internet. He began with books for three reasons. First, books are not fragile and are easy to ship. Second, selling books would allow Amazon to gather valuable data about its customers which could be used effectively to sell them other goods and services later.[80] Does a customer order books about financial investing, traveling, gourmet cooking, or new cars? That just scratches the surface. It is easy to see why librarians safeguard their patrons borrowing history.[81] Amazon would know if a customer ordered *The Cancer Fighting Kitchen,*[82] *How To Find a Good Psychothera-*

$35.00 to $27.00 per year. *Id.* at 49. By contrast, on average Americans watch television for two hours and twenty-one minutes per day on weekdays and more than three hours per day on weekends and holidays. *Id.* at 39 tbls. 3B & 3C.

77. *Id.* at xi, 26.

78. Surprisingly, a third NEA report, issued in 2009, showed a possible reversal of the trend. NATIONAL ENDOWMENT FOR THE ARTS, READING ON THE RISE: A NEW CHAPTER IN AMERICAN LITERACY (2009). According to the third report, the portion of adult Americans reading literature bottomed out at 46.7% in 2002 and rose to 50.2% in 2008. *Id.* at 3–4. However, that may have been partly due to the researchers expanding the definition of "literature" to include fiction, poetry, or drama read online. *Id.* at 8. Most significant for book publishers, the report showed that while the number of Americans reading books increased due to an increase in population, the percentage of Americans reading books continued to decline. *Id.* at 7.

79. George Packer, *Cheap Words: Amazon Is Good for Consumers. But Is It Good for Books?*, NEW YORKER, Feb. 17 & 24, 2004, at 66, 67.

80. *Id.* at 68.

81. Principle III of the Code of Ethics of the American Library Association states: "We protect each library user's right to privacy and confidentiality with respect to information sought or received and resources consulted, borrowed, acquired or transmitted." *Professional Ethics*, AM. LIBRARY ASS'N, http://www.ala.org/advocacy/proethics/codeofethics/codeethics.

82. REBECCA KATZ & MAT EDELSON THE CANCER-FIGHTING KITCHEN: NOURISHING, BIG-FLAVOR RECIPES FOR CANCER TREATMENT AND RECOVERY (2009).

pist,[83] *What To Do When You're Dating a Jew?,*[84] *Parenting a Child with Asperger's Syndrome,*[85] or *In Trump We Trust: E Pluribus Awesome!.*[86] Amazon would know a great deal indeed about someone after they ordered a dozen or more books. Third, customers who order books are, as a group, affluent, and information about them is especially commercially valuable.

At first, publishers were thrilled with Amazon.[87] It was a great new way to market and distribute books. Among other things, it helped sell books on publishers' backlists.[88] If a reader decided she wanted to read a biography of Abraham Lincoln, she could browse through the hundreds of available titles on Amazon's website, select one, even one published years ago and no longer carried by traditional bookstores, order it, and have it within a few days. And she could do all of this without leaving her house.

Amazon attracted customers by creating an appealing, user-friendly, and very informative website. It included customer ratings and comments, as well as editorial blurbs and reviews about books. Amazon even hired a staff to supplement what was available by writing their own reviews and creating lists of favorite books that their reviewers thought had special merit.[89] And Amazon came up with other useful features. For example, a reader who liked a particular book could see what other books readers of that book were purchasing. Amazon's website was a fabulous success. It did not take long before at least thirty million people visited the website per day.[90] Publishers had every reason to hope that Amazon might increase book reading and book sales.

In its early days, Amazon was, from the publishers' point of view, a traditional bookseller, though a national and increasingly successful one. Their financial arrangement with Amazon was essentially the same as with physical bookstores. Publishers set suggested retail prices for their books and then sold their books to retailers at some percentage of that price. For example, a publisher might set a suggested retail price for a new book at $24.99 and sell that book to retailers at a wholesale price of $14.99, forty percent below the

83. JUDITH CECERE STRIANO, HOW TO FIND A GOOD PSYCHOTHERAPIST (1988).

84. VIKKI WEIS & JENNIFER A. BLOCK, WHAT TO DO WHEN YOU'RE DATING A JEW: EVERYTHING YOU NEED TO KNOW FROM MAZOH BALLS TO MARRIAGE (2000).

85. BRENDA BOYD, PARENTING A CHILD WITH ASPERGER SYNDROME (2003).

86. ANN COULTER, IN TRUMP WE TRUST: E PLURIBUS AWESOME! (2016).

87. Packer, *supra* note 79, at 69.

88. *Id.* at 68–69.

89. *Id.* at 69.

90. *Id.*

suggested retail price.[91] The retailer was free to sell the book at any price it chose. If it wanted to stick to the suggested retail price, that was fine. If it wanted to discount New York Times bestsellers by selling them ten or twenty percent below suggested retail prices, that was fine, as well. Publishers received their wholesale price regardless. In theory, a retailer was free to sell books below their wholesale price. In practice, however, this seldom happened because, instead of taking a loss on a book that was not moving off its shelf, a retailer could simply return that book for a credit.[92] From its inception, Amazon more deeply discounted books than other retailers, but so what?[93] Publishers made the same amount. Besides, lower prices might mean more books sold. Publishers also liked Amazon because it paid faster and returned fewer books than most brick-and-mortar booksellers.[94]

However, as Amazon's market share grew, so did its leverage to extract better terms from publishers. In this regard, Amazon was like other companies that achieved a dominant position over the distribution of products in a particular field. Often, those who create products—physical or intellectual—are taken hostage by those who distribute their products. When Comcast, for example, became the dominant cable provider, it demanded increasingly rich tributes from the networks and cable channels that produced the shows that Comcast's customers wanted to watch. Walmart has similarly been able to hold hostage manufacturers who sell large shares of their total output through Walmart stores. In theory, the Robinson-Patman Act prohibits Amazon, Comcast, or Walmart from extracting better terms from suppliers than are available to their smaller rivals, but Robinson-Patman is notoriously weak legislation and there are many ways around it.[95]

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91. *See* THOMPSON, *supra* note 6, at 368–69 (describing the traditional model).

92. *Id.* at 285–91.

93. Amazon offered a thirty-five percent discount of both hardback and paperback bestsellers, and ten percent on hundreds of thousands of other titles. *See id.* at 42–43.

94. *See* Packer, *supra* note 79, at 68–69.

95. *See, e.g.*, HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE 779 (5th ed. 2016) (stating "[t]he Robinson-Patman Act is a morass of technical requirements that often hide or subvert its basic purpose."); THOMPSON, supra note 6, at 301 ("[W]hile in principle the Robinson-Patman Act creates a level playing field among retailers in the US, in practice there are many ways in which this playing field can be turned into rough and uneven ground that gives large retailers certain advantages either because they are able to leverage their size and strategic importance to exact better terms and conditions or because the small independent booksellers are less efficient, less well-equipped in terms of their IT infrastructure or simply less well organized.").

One way Amazon extracted better terms was through cooperative advertising, or "co-op" programs.[96] These programs existed in the book industry long before Amazon came along. Co-op policies are designed, in theory, as a means by which publishers pay a share of a retailer's costs of marketing and promoting that publisher's books. The amount that a publisher provides to the retailer for these purposes, and the methods under which the money is provided, depends upon each individual publisher's co-op policy. Most typically, a publisher makes available a particular sum based on the amount of a retailer's net sales of the publisher's books in the prior year. Thus, if a publisher's co-op policy was three percent, and the retailer's net sales of that publisher's books in the previous year were $100,000, then the publisher would make available to that retailer $3,000 to spend promoting its books in the current year.[97] Co-op programs were traditionally a way to evade requirements of the Robinson-Patman Act, but following litigation between small, independent booksellers and the large chain stores in 1982, 1994, and 1998, publishers agreed to make their co-op programs more clear and transparent.[98]

Nevertheless, Amazon used its power to demand increasingly favorable terms, and its unique status as an internet seller gave it an argument that special treatment did not violate the Robinson-Patman Act. For example, publishers were used to paying retailers to display their books on tables in the front of their stores and on end caps with book covers rather than book spines facing out. Amazon took this to a new level. It demanded that publishers pay it $10,000 to feature a book on its homepage.[99] Amazon demanded larger co-op fees and adjusted its recommendation algorithms to disfavor books by recalcitrant publishers.[100] The customer searching for the best biography of Lincoln may not realize it, but when she types "Abraham Lincoln" or "Lincoln biographies" into Amazon's search engine, the books she sees, and the order in which

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96. *See generally* THOMPSON, *supra* note 6, at 261 (describing how cooperative advertising works in the book industry generally).

97. *Id.*

98. The American Booksellers Association, which is composed of small, independent booksellers, has twice filed lawsuits complaining that publishers give large retail chains better terms in price, credit, and return policies. *Id.* at 33–34, 299–302.

99. *See* Packer, *supra* note 79, at 70.

100. *Id.* at 71.

they are displayed, are in part determined by the promotional fees paid by the publishers.[101]

Moreover, Amazon played the hardest of hardball. Starting with the smallest and weakest publishers, Amazon demanded increasingly favorable terms, especially on promotional fees. Amazon CEO Jeff Bezos told his staff to approach "small publishers the way a cheetah would pursue a sickly gazelle."[102] In negotiations with a new publisher named Melville House in 2004, Amazon made demands that Dennis Johnson, Melville House's co-owner, considered extortionate.[103] He refused and reported the shakedown to *Publisher's Weekly*, which ran a story. The next day, Amazon removed the "buy" button from all Melville House books on its website. Eight percent of Melville House's total sales were through Amazon, and it could not afford to lose that much of its business. Melville House had no choice but to capitulate. That was well over a decade ago, and today, Amazon is far more powerful. It sells more than forty percent of all books in the United States, including hardback, paperback, and electronic.[104]

Amazon has, in large part, replaced "co-op fees" with "marketing development funds," but the essential features are the same: Publishers pay Amazon a percentage of their gross sales on its website from the previous year.[105] The percentage is renegotiated annually, and it has steadily increased. The fees used to be in the range of two to three percent of gross sales; they are now typically five to seven percent for large retailers and even higher for sickly gazelles.[106] This has pushed these fees to the point where, when a customer buys a book on its website, Amazon keeps more than half the sale price.[107] This, of course, in no way reflects the relative values added by the author, publisher, or Amazon. It simply reflects the relative market power of the parties.

From the publishers' standpoint, all of that was bad enough. But things became dramatically more threatening after Amazon

101. *Id.* Following a lengthy investigation, the FTC decided that similar practices by Google did not violate antitrust laws. Marina Lao, *Search, Essential Facilities, and the Antitrust Duty to Deal*, 11 NW. J. TECH. & INTELL. PROP. 275, 276 (2013).

102. Packer, *supra* note 79, at 71.

103. *See id.*

104. Foer, *supra* note 10, at 20. The author does not have information about Amazon's market share of audio books.

105. *Id.*

106. *Id.*

107. Packer reports that, as of 2014, Random House, the largest publishing company in the United States, paid Amazon an effective discount of fifty-three percent and small publishers paid up to sixty percent. *See* Packer, *supra* note 79, at 71–72.

launched its Kindle ebook reader in November 2007.[108] There was nothing inherently worrisome about electronic books *per se*; quite the contrary, electronic books do not have to be printed, bound, or shipped. Best of all, unsold copies are not returned. The problem was that Amazon announced that it was going to sell the ebook versions of new releases[109] and *New York Times* bestsellers for $9.99. That made publishers terribly unhappy.

Why should publishers care about Amazon's retail prices even though they did not affect how much Amazon paid publishers? The reason was simple: Selling books at $9.99 devalued them.[110] It created the impression in the public's mind that was what books were worth, even though publishers (not to mention authors) believed they were worth considerably more. Publishers feared that, if this went on long enough, consumers would not be willing to pay more than $9.99 for a book. The publishers were, in fact, aware of a precedent that frightened them: music. When Apple opened its iTunes store in April 2003, it made 200,000 individual songs available for ninety-nine cents each.[111] Within a very short time, the price established the value of a song in the public's mind. The music industry was generally pleased and cooperated with Apple on its iTunes store because songs were promiscuously pirated through Napster and similar websites. One of the principal benefits of iTunes was that it reversed the conventional wisdom, in the minds of teenagers especially, that songs were free. Nevertheless, the point remains: Ninety-nine cents became the accepted value of a song. Book publishers were worried that, in much the same way, Amazon was establishing $9.99 as the value of a book.

Publishers conceded that ebooks should be less expensive than physical books, and they priced their ebooks accordingly. The costs of printing, binding, warehousing, and shipping books represented about twenty percent of the total costs of producing a book. Eighty

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108. *See* THOMPSON, *supra* note 6, at 368–69.

109. New releases are books that have been released within the current month. *See* Trial Transcript at 331, United States v. Apple Inc., 952 F. Supp. 2d 638 (S.D.N.Y. Nov. 18, 2013) (No. 12 CV 2826) [hereinafter Trial Transcript, United States v. Apple Inc.]. The trial transcript is consecutively paginated and is scattered across ECF Nos. 388, 390, 392, 394, 396, 398, 400, 402, 404, 406, and 408.

110. *See generally* THOMPSON, *supra* note 6, at 369–70

111. *Cf.* WALTER ISAACSON, STEVE JOBS 394–402 (2013 ed.). Record companies received seventy percent of the sale price of their songs on iTunes. *Id.* at 396. When, six years later, record companies and artists prevailed upon Apple to raise the price of many songs to $1.29, there was concern that customers would revolt. Dawn C. Chmielewski, *Hottest tracks to cost $1.29 at ITunes starting April 7,* L.A. TIMES (Mar. 26, 2009), http://articles.latimes.com/2009/mar/26/business/fi-cotown-itunes26; *see also* THOMPSON, *supra* note 6, at 371.

percent of publishing costs go to author royalties, editor salaries, and marketing. As a general rule, therefore, some publishers thought ebooks should sell for about eighty percent of the hardback price.[112] Their goal was to make roughly the same net profit on physical books and ebooks so that they could be indifferent as to which version readers preferred.[113] Some publishers set suggested retail prices for ebooks at eighty percent of the list price for the hardback version and sold their ebooks to Amazon at a forty-eight percent discount from that price.[114] Thus, if the list price of the hardback version of a new release was $24.99, the wholesale ebook price was $10.40.[115] Amazon sold that ebook to its customers for $9.99, and lost forty-one cents on each sale. Some new releases had hardback list prices of $27.99 or $29.99; Amazon's losses on the ebook version of those titles were $1.65 and $2.48 respectively. Whether these losses were reduced to some extent by marketing development fees is not entirely clear. The trial court did not consider this of great importance in the Apple case and gave it little attention. It found that "Amazon's $9.99 price point roughly matched the wholesale price of many of its ebooks," and did not elaborate.[116] Even if Amazon broke even in terms of its gross margin, that fails to take into account Amazon's overhead costs. Moreover, Amazon's ebook prices were below its wholesale prices for eighty percent of all new releases.[117] Its losses on ebooks were, therefore, considerable.

Amazon claimed it was willing to sustain such losses because it was following a loss-leader strategy. That is, it was willing to sustain losses on the sales of ebooks in order to stimulate sales for its Kindle, which was selling for $399.00 when first introduced.[118] Whether Amazon was following a legitimate loss-leader strategy—as op-

112. This appears to have been a popular practice, though some publishers set one price for all of its ebooks, such as $16.99. *See* THOMPSON, *supra* note 6, at 337, 368.

113. *Id.* at 373; *see also* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 498–99, 515, 558, 600 (testimony of Carolyn Kroll Reidy, President and CEO of Simon & Shuster, explaining repeatedly that she considered the crucial question in ebook pricing to be the relationship between the ebook price and the price of the physical book).

114. *See* THOMPSON, *supra* note 6, at 369. *See generally* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 573 (testimony of Carolyn Kroll Reidy).

115. For a hardback with a list price of $24.99, the suggested ebook retail price was $19.99 (twenty percent off the hardback list price), and the wholesale ebook price was forty-eight percent off from that price. *See* THOMPSON, *supra* note 6, at 369.

116. *Apple Inc.*, 952 F. Supp. 2d at 649; *see also* United States v. Apple Inc., 791 F.3d 290, 299 (2nd Cir. 2015) (accepting the district court's finding).

117. Brief of Amici Curiae The Authors Guild, Inc. et al. at 12 n.8, Apple Inc. v. United States, No. 15-565 (U.S. Dec. 2, 2015), *cert. denied*, 136 S. Ct. 1376 (2016).

118. THOMPSON, *supra* note 6, at 369–70.

posed to an illegal predatory pricing strategy, designed to deter rivals from entering the market[119]—would depend, in part, on whether it was making a profit on its Kindle and ebook business taken as a whole. That is, Amazon might take losses on ebooks in order to make profits on the Kindle if it thought that was the best way to maximize net profits. Notwithstanding Amazon's claims, however, it was possible that Amazon was willing to sustain losses in its entire ereader/ebook business until its dominant position was irreversible.[120] Once enough readers had Kindles, it would be difficult, if not impossible, for rivals to successfully enter the market.[121] This was, moreover, consistent with Jeff Bezos's philosophy of favoring growing market share over short-term profitability.[122]

It was a successful strategy. Barnes & Noble introduced its ereader in November 2009, almost exactly two years after Amazon introduced its Kindle. Critics rated the Nook as better than the Kindle,[123] and the Nook turned out to be more successful than

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119. Predatory pricing is below-cost pricing designed either to drive rivals out of a market or deter rivals from entering a market. *See generally* HOVENKAMP, *supra* note 95, at 455–93; STEPHEN F. ROSS, PRINCIPLES OF ANTITRUST 55–72 (1993). A great deal of attention has been given to how cost should be defined, and specifically whether marginal cost, average variable cost, or average total cost should be used for this purpose. That question has little relevance when evaluating pricing by a retailer, such as Amazon, who is selling below the wholesale prices it paid. It is selling below cost under any definition.

120. This is a classic, real-world example of predatory pricing, which is most effective as a means of deterring potential rivals from entering the market. As Herbert Hovenkamp observes, "Predatory pricing and other pricing strategies are generally plausible only for firms that are *already* dominant in their markets." HOVENKAMP, *supra* note 95, at 469. Moreover, predatory pricing is commonly directed against prospective rivals who are contemplating entering the market. *Id.* at 461, 463.

121. John B. Thompson suggests that that was Amazon's objective. He writes that Amazon hoped to sell enough Kindles "to establish a dominant position in the market." THOMPSON, *supra* note 6, at 369–70. While it may be possible to read Nook books on a Kindle, it is difficult to do so. *See* Marziah Karch, *How to Read Nook and Kobo Apps on Your Kindle Fire*, Lifewire, http://google.about.com/od/kindlefire/ss/How-To-Install-Nook-And-Kobo-Apps-On-Your-Kindle-Fire.htm (last updated Oct. 22, 2018) (advising Kindle Fire users that they "may run into difficulty if [they] want to read Nook, Kobo, or Google eBooks"); Lina M. Khan, Comment, *Amazon's Antitrust Paradox*, 126 YALE L.J. 710, 760 (2017) (stating that Amazon and other ebook sellers "used a scheme known as 'digital rights management' [to limit] the types of devices that can read certain e-book formats.").

122. Bezos announced this philosophy in his first public letter to investors. BRAD STONE, THE EVERYTHING STORE: JEFF BEZOS AND THE AGE OF AMAZON 69 (2013). Amazon did not make a profit in its first nine years of operation. Saul Hansell, *Technology; Amazon Reports First Full-Year Profit*, N.Y. TIMES, Jan. 28, 2004, at C00003, https://www.nytimes.com/2004/01/28/business/technology-amazon-reports-first-full-year-profit.html; *see also* FRANKLIN FOER, WORLD WITHOUT MIND: THE EXISTENTIAL THREAT OF BIG TECH 224–25 (2017) (noting that Bezos convinced investors of the benefits of Amazon's growth-instead-of-profits strategy).

123. *See, e.g.*, CONSUMER REPORTS BUYING GUIDE 2014, at 61 (2014) (rating the two versions of the Nook ahead of four versions of the Kindle in the six- to seven-inch category of ebook readers, the only category in which Barnes & Noble competed). A third competitor, Kobo, has captured a very small market share, and Sony competed in the market for a time

even Barnes & Noble had anticipated.[124] Nevertheless, the Kindle enjoyed a significant advantage over the Nook: a two-year lead. Many customers who were interested in ereaders already owned Kindles. They were likely to buy ebooks exclusively from Amazon, and unlikely to buy a second ereader for a considerable period of time. Moreover, as the first popular ereader, the Kindle brand name had become nearly synonymous with the product category. People did not call ereaders "ereaders"; they called them "Kindles," just as people used to call refrigerators "Frigidaires," tissues "Kleenex," and cola drinks "Cokes," or today call a browser search "Googling."[125] Even with a superior product, Barnes & Noble would ultimately capture no more than twenty-five percent of the market.[126] Amazon's two-year lead gave it brand recognition and acceptance that were hard to challenge.

There may have been another reason why Amazon successfully maintained dominance. Amazon's strategy of selling bestselling ebooks at a loss put Barnes & Noble in something of a pickle. Barnes & Noble had entered the ebook business reluctantly. Unlike Amazon, its principal business was physical bookstores; it operated about seven hundred self-standing superstores and nearly one hundred smaller stores in malls.[127] It did not to want to encourage the growth of ebooks.

Nevertheless, Barnes & Noble really had no choice but to enter the ereader/ebook market; it could not afford to stay out of that market only to discover too late that ebooks had largely replaced physical books. So, it invested in developing its own ereader. In order to compete with Amazon, however, it was forced to sell the most popular ebooks at $9.99. That led Barnes & Noble to sustain losses, and the more books it sold, the more money it lost.[128] Barnes & Noble, therefore, faced a dilemma: It needed to promote its ebook business, yet at the same time it could not afford to be too successful. Nor could Barnes & Noble hope to beat Amazon at its

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but closed its ebook store in March 2014. *See Welcome Reader Store Customers*, KOBO, https://www.kobo.com/sony (last visited Nov. 30, 2018).

124. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2174–75.

125. *See* Herbert B. Dixon Jr., *The Courtroom of the Present: The Bare Essentials for a Technologically Competent Courtroom*, 48 JUDGES' J. 37, 37 (2009) (regarding brand names that became synonymous with product categories); *see also, e.g.*, Brian Heater, *E-Reader Innovation Has Stalled*, TECHCRUNCH (Oct. 12, 2017), https://techcrunch.com/2017/10/12/e-reader-innovation-has-stalled/ ("Kindle has become synonymous with e-reader for most mainstream users.").

126. THOMPSON, *supra* note 6, at 339.

127. *Id.* at 29.

128. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2173–76, 2179, 2441.

own game of winning and maintaining market share through loss-leader pricing. As a much larger and better-positioned company, Amazon could absorb greater losses, and do so over a longer period of time.[129] Indeed, Barnes & Noble represented to the court that it could not have continued to promote the Nook and its ebook business under the existing system.[130] Thus, while Amazon's strategy of below-cost pricing in ebooks did not succeed in keeping Barnes & Noble out of the ebook market entirely, it may have caused Barnes & Noble to pull its punches when deciding how aggressively to promote its Nook and ebook business. Moreover, if Amazon was able to continue its loss-leader pricing strategy, it may well have succeeded in driving Barnes & Noble out of the ebook business.

Amazon may have driven publishers out of the business as well. At the time of the dispute, physical books still accounted for ninety-five percent of publishers' sales, and publishers could still sell physical books at whatever prices the market would bear.[131] But this was cold comfort. For one thing, the public would come to believe that the *contents* of books were worth $9.99, and the rest of the price for hardbacks and paperbacks were related to the physical package. That is, in fact, not the case. Paper, printing, and distribution together constitute only a small fraction of the cost of a physical book.[132] The lion's share of the costs are in author royalties, editorial work, and marketing and promotion. If the price of a new hardback were $29.99 and the price of the Kindle versions were $9.99, how long would people be willing to purchase hardbacks? And, indeed, at the time of the dispute it was unclear whether physical books would survive. In 2006, the large trade publishers received, on average, about 0.1% of their revenue from ebook sales.[133] By 2010, that had risen to eight percent—and industry analysts were projecting that percentage could skyrocket to as

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129. In 2010, Amazon ranked forty-seventh in the Fortune 500 and had revenues of more than $61.1 billion while Barnes & Noble ranked number 360 and had revenues of $7.1 billion. *Largest U.S. Corporations*, FORTUNE, May 20, 2013, at F-3 and F-19. Both companies recorded losses in 2010, but Amazon's business strategy—well-understood and supported by its shareholders and investors—included a willingness to operate at a loss and build to shareholder value.

130. *See* Brief of Amici Curiae The Authors Guild, Inc. et al., *supra* note 117, at 20.

131. *See* United States v. Apple Inc., 952 F. Supp. 2d. 638, 652–53, *aff'd*, 791 F.3d 290 (2d Cir. 2015) (citing Mokoto Rich, *Publishers Delay E-Book Releases*, N.Y. TIMES: ARTSBEAT (Dec. 9, 2009, 4:12 PM), https://artsbeat.blogs.nytimes.com/2009/12/09/publishers-delay-e-book-releases/).

132. THOMPSON, *supra* note 6, at 337–38.

133. *Id.* at 321.

much as twenty-two percent in the very next year.[134] No one knew whether ebooks would largely supplant physical books.[135] In fact, one prominent analyst predicted that paper would be obsolete by 2015.[136] Publishers simply could not survive if they could only sell books at $9.99.

If that became the norm, would no one publish books? That probably would not come to pass. Publishers would disappear, but many authors would self-publish. Authors would either design their own covers or hire professional designers, forego professional editing or hire their own editors, promote their own books or hire specialists to assist them with that too. Some talented writers who did not want to be entrepreneurs might give up writing books entirely. Would more or less books ultimately be published? No one knows. But with the gatekeepers—as in the agents and publishers—gone, people who always wanted to write books but previously could not find agents or publishers interested in their work might suddenly feel empowered to write and publish books. It is entirely possible that more books might be written than is presently the case.

But regardless of whether more or less books were written, it is unlikely that this brave new world of book publishing would be good for readers. Presently, most terrible manuscripts simply are not published. And when traditional publishers believe they have an extraordinarily good book by a new author, they give that book special attention, promoting it with book review editors and bookstore buyers, advertising it, sending the author on a book tour, or nominating it for a literary prize. It may not be a perfect system, but at least someone other than the authors themselves are

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134. *Id.*

135. *See id.* at 324 (regarding industry uncertainty about whether printed books would survive); *see also* Daniel Victor, *The Internet Hasn't Won: Printed Books Still Prevail,* N.Y. TIMES, Sept. 5, 2006, at B5 (quoting Lee Rainie, the director of internet, science, and technology research for the Pew Foundation, who said that five to ten years ago "there were folks who thought the days of the printed book numbered."). In fact, the opposite has come to pass: the sales of physical books have increased while sales of ebooks have declined. *See* Alexandra Alter, *The Plot Twist: E-Book Sales Slip, and Print is Far From Dead* (Sept. 22, 2015), https://www.nytimes.com/2015/09/23/business/media/the-plot-twist-e-book-sales-slip-and-print-is-far-from-dead.html?_r=0; Jim Milliot, *As E-book Sales Decline, Digital Fatigue Grows* (Jun. 17, 2016), http://www.publishersweekly.com/pw/by-topic/digital/retailing/article/70696-as-e-book-sales-decline-digital-fatigue-grows.html; Sian Cain, *Ebook Sales Continue to Fall as Younger Generations Drive Appetite for Print* (Mar. 14, 2017 7:10 AM), https://www.theguardian.com/books/2017/mar/14/ebook-sales-continue-to-fall-nielsen-survey-uk-book-sales.

136. FOER, *supra* note 122, at 224–25.

vouching for the quality of books in the first instance.[137] In a world without gatekeepers, James Patterson fans would still find his next book but finding good books by unknown authors would be extremely difficult. It is no accident that self-published books are not eligible for nomination for major awards because, if they were, finding great books would be like looking for the proverbial needle in haystack.[138]

Amazon might welcome a brave new world without traditional publishers. It has become a leader in self-published books, selling services to authors who wish to publish in print, Kindle, or audio formats.[139] While Amazon has competition in that market, it enjoys the enormous advantage in being the world's largest book retailer. Authors want their books well-promoted on Amazon's website, and they may reasonably believe that their chances of that increases by self-publishing through Amazon itself.

Publishers understood that if they were going to successfully take on Amazon, they had to do so collectively.[140] Beginning in December of 2008, the Big Six publishing houses began to talk among themselves about finding a way "to create an alternative platform to Amazon for e-books."[141] The CEOs of the Big Six met approximately every three months to discuss Amazon and other

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137. Four trade magazines specialize in prepublication book reviews: Publishers Weekly, Library Journal, Kirkus, and Booklist. Bookstore buyers rely heavily on Publishers Weekly, library selectors rely heavily on Library Journal, and book review editors look at all four. Publishers Weekly reviews about 10,000 books per year, which is no more than seventeen percent of all books published annually in the United States. *See* Adelle Waldman, *Book Report: How Four Magazines You've Probably Never Read Help Determine What Books You Buy,* SLATE (Sept. 12, 2003, 3:28 PM), http://www.slate.com/articles/arts/culturebox/2003/09/book_report.htm; Nick Morgan, *Thinking of Self-Publishing Your Book in 2013? Here's What You Need to Know*, FORBES (Jan. 8, 2013), https://www.forbes.com/sites/nickmorgan/2013/01/08/thinking-of-self-publishing-your-book-in-2013-heres-what-you-need-to-know/ (stating that somewhere between 600,000 and 1,000,000 books are published annually in the United States). If publishers disappeared, how would these magazines decide which books to review? Kirkus will currently review a self-published author's book for a price ($425 to review a book within seven to nine weeks). Kirkus Indie, KIRKUS, https://www.kirkusreviews.com/indie-reviews/how-it-works (last visited Sept. 9, 2018).

138. *See, e.g.*, *How the National Book Awards Work*, NATIONAL BOOK FOUNDATION (last visited Oct. 26, 2018), http://www.nationalbook.org/national-book-awards/how-works/ (stating that self-published books are not eligible for the National Book Award); *Approved Publisher List***,** MYSTERY WRITERS OF AMERICA, http://mysterywriters.org/how-to-become-a-member-of-mwa/approved-publisher-list (last updated Oct. 4, 2018) (stating that only approved publishers may nominate books for the Edgar Awards).

139. *Take Control with Self-Publishing*, AMAZON, http://www.amazon.com/gp/seller-account/mm-summary-page.html?topic=200260520 (last visited Oct. 26, 2018).

140. *See* United States v. Apple Inc., 952 F. Supp. 2d 638, 650 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015); *see also* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 468.

141. *Apple Inc.*, 952 F. Supp. 2d at 651.

challenges facing their industry. Meetings among competitors have always been highly suspect. In 1776, Adam Smith famously wrote: "People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices."[142] The standard advice that lawyers give to their clients is to have antitrust counsel present at all meetings with competitors, including trade association meetings, to ensure that no prohibited discussions take place.[143] However, the Big Six CEOs met alone in private dining rooms of New York City restaurants,[144] without lawyers or other assistants.[145] Perhaps, the executives did not know how ominous their private dinners would later look. In fact, if there is a term that rings alarms in the minds of lawyers and judges, it is "private dinner" for the simple reason that some of the most infamous agreements in antitrust history happened to occur at just such a venue.[146]

Among the topics discussed at these dinners was what to do about Amazon. "I hate [Amazon's] bullying behavior and will be happy to support a strategy that restricts their plans for world domination," Hachette's CEO wrote in an email to the CEO of Hachette's parent corporation before one of the dinners.[147] Some of the publishers had already tried eliminating the wholesale discount for ebooks; rather than setting the wholesale price of an ebook at eighty percent of the price of the physical book of the same title, they raised the wholesale price to match the price of the physical book.[148] Their objective was to make Amazon take a larger loss on ebooks, thereby pressuring Amazon to raise its prices. But that did not work. Amazon was willing to absorb larger losses.

The publishers also discussed among themselves "windowing" ebook versions of new releases, that is, delaying an ebook edition

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142. ERNEST GELLHORN ET AL., ANTITRUST LAW AND ECONOMICS IN A NUTSHELL 284 (Thomson West, 5th ed. 2004) (citing ADAM SMITH, THE WEALTH OF NATIONS 128 (Canaan ed. 1937)).

143. *See, e.g.*, PRACTICAL LAW ANTITRUST, INVITATIONS TO COLLUDE, PRACTICE NOTE 8-543-2405 (Thomson Reuters Practical Law 2018) ("Counsel should be notified before any meeting between competitors . . . . If the client permits, antitrust counsel should attend the meeting.").

144. *See Apple Inc.*, 952 F. Supp. 2d at 651.

145. *Id.*

146. *See, e.g.*, William H. Page, *The Gary Dinners and the Meaning of Concerted Action*, 62 SMU L. REV. 597 (2009).

147. *Apple Inc.*, 952 F. Supp. 2d at 651.

148. *Id.* at 650; *see also* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 465.

for a period of time after publication of the hardback edition.[149] Four of the Big Six announced that they would window some of their ebooks, though their individual policies differed. HarperCollins said it would window five to ten titles per month while Macmillan announced it would window most of its ebooks for a period of ninety days following publication in hardback.[150] But windowing ebooks was problematic. The publishers feared that it would alienate readers and encourage piracy. Penguin conducted a study that found that delaying the release of ebooks resulted in a loss of sales that was never recovered, and both Penguin and Random House decided against windowing ebooks. Even the four publishers who decided to window ebooks considered this only a short-term tactic, and one of them, Macmillan, wound up never implementing its announced policy.[151]

Here, then, are how things stood at the end of 2009: Amazon had the market power to extract discounts from book publishers, whether in the form of co-op fees, market development fees, or otherwise. Amazon already had an effective monopoly in ebooks, and by pricing ebooks below costs Amazon was working toward making its monopoly position so entrenched as to be irreversible. Amazon was also training the public to believe that ebooks were worth $9.99. In the short run, Amazon's price was an almost insurmountable barrier to entry to potential rivals. Beyond Barnes & Noble, which was exclusively in the book business and therefore had no choice, who would enter the ebook market only to lose money? If Amazon succeeded in making its monopoly unassailable and irreversible, and if ebooks supplanted print books, Amazon would effectively have a monopoly in retailing all books. It would be positioned to continue selling ebooks at $9.99 and demand price concessions from publishers that would make its ebook business profitable.[152] In this scenario, publishers might not be able to

149. *Apple Inc.*, 952 F. Supp. 2d at 651–54. The term "windowing" originally referred to delaying release of the paperback edition for a period of time, often one year, after publication of the hardback edition. *See id.* at 651 n.10; Edward Wyatt, *Rethinking the Paperback Timeline*, N.Y. TIMES: ARTSBEAT (June 2, 2008, 10:18 AM), https://artsbeat.blogs.nytimes.com/2008/06/02/rethinking-the-paperback-timeline/ ("[I]t is still common for publishers to wait nine months to a year after a book is released in hardcover to produce a less expensive paperback version.").

150. *See Apple Inc.*, 952 F. Supp. 2d at 653.

151. *Id.* at 653 n.1; *see also* United States v. Apple Inc., 791 F.3d 290, 301 (2d Cir. 2015) ("[T]he publishers viewed even this strategy to save their business model as self-destructive.").

152. The antitrust traditionalist will ask, "If Amazon were to have an unassailable monopoly, would it not raise prices?" I believe that while Amazon would like to capture monopolist profits, it is more likely—given Amazon's history and image, and its customers' ex-

stay in business by selling books to Amazon at the prices that Amazon would demand—which would suit Amazon just fine. It was already the leader in selling services to authors who wanted to self-publish their books, and it was uniquely positioned to become the dominant firm in that industry.

Publishers complained bitterly to Amazon about its $9.99 price point.[153] But if anything, their gnashing of teeth was music to Amazon's ears. Amazon appeared to be looking forward to the day when publishers would go belly up. They had tried acting collectively by eliminating the wholesale discount for ebooks and by windowing ebooks, but those efforts had proved ineffective. Amazon was simply too strong. What publishers—and the public—needed was a savior to demolish Amazon's dominant position. That probably seemed too much to hope for. Yet, at the end of 2009, a savior materialized.

C. *Apple*

That savior was Apple. Only a company as large and powerful as Apple could hope to successfully challenge Amazon's monopoly position. Apple was, at the time, number fifty-six on the Fortune 500 (Amazon was 100).[154] Apple was still led by its brilliant founder, Steve Jobs, but Jobs was ill. He had been diagnosed with pancreatic cancer six years earlier and was living on borrowed time.[155] Jobs had been the creative force behind iconic products such as the Macintosh, iPhone, and iPod. The iPad, Apple's computer tablet, was destined to be his last creation. The iPad was an intimate device on which one could access email, watch movies, listen to music, look at photos, and read newspapers and magazines.[156] The project had been under development for at least three years.[157] At nearly the last minute, Apple decided to try to add books. The public launch of the iPad was already scheduled for January 27, 2010, but, in November of 2009, Steve Jobs gave Eddy Cue the go-ahead

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pectation of $9.99 books—to achieve its objective by keeping the retail price stable and using its monopsony power to drive down the wholesale price it pays to publishers.

153. *See Apple Inc.*, 952 F. Supp. 2d at 650.

154. *Fortune 500 2010*, FORTUNE, http://fortune.com/fortune500/2010 (last visited Oct. 26, 2018).

155. *See* ISAACSON, *supra* note 111, at 456, 484, 489.

156. To demonstrate the iPad, Jobs did all of those things at the iPad launch on January 27, 2010. *Id.* at 493–94.

157. *See id.* at 491 (reporting that in 2007 Jobs decided to vigorously pursue developing an Apple tablet).

to develop an Apple ebookstore.[158] Cue, one of Jobs's closest associates, was in charge of internet content for Apple and had helped build the spectacularly successful iTunes Store six years earlier.[159] Cue had a personal as well as a professional reason to want to succeed: He wanted to make his friend's last new product as successful as possible.[160]

Cue and his team had already done their research on the book industry. They knew that the major publishers desperately wanted to break Amazon's stranglehold and end the practice of selling bestsellers and new releases for $9.99.[161] Cue and his team knew that the $9.99 price point meant operating at a loss, and Apple had decided that it would enter the ebook business only if it could turn a profit.[162] They had analyst reports that suggested that a price point of $12.99 could offer a reasonable profit margin.[163]

Beginning on December 8, 2009, Cue's team began calling each of the Big Six to ask them to meet to discuss an "extremely confidential" subject.[164] The publishers had little trouble guessing what Cue wanted to discuss. The press was reporting that Apple was on the verge of announcing a revolutionary new device, and what would the leading firm in personal electronic devices want to discuss with book publishers other than ebooks? The district court thought it highly significant that the Big Six CEOs immediately telephoned each other. There were twenty-one calls between those CEOs from Tuesday, December 8, through the end of that work week, compared to just one such call in the last four days of the previous work week.[165] We will discuss the possible significance of those calls in more detail later. For now, suffice it to say that the antitrust laws do not prohibit rivals from talking to each other or

158. *Apple Inc.*, 952 F. Supp. 2d at 654–55.

159. *See* ISAACSON, *supra* note 111, at 574 (regarding Cue's close relationship with Jobs); *id.* at 531 (regarding Cue supervising internet content for Apple); *id.* at 403 (regarding Cue building the iTunes Store).

160. *See Apple Inc.*, 952 F. Supp. 2d at 655.

161. As Cue himself bluntly put it, "all the content owners hate Amazon." *Id.* at 654.

162. *Id.* at 656.

163. The court wrote that the reports "indicated that a price of $12.00 could be a *more* profitable price point for e-books than Amazon's $9.99." *Id.* at 654 (emphasis added). This erroneously suggests—or, at a minimum, leaves open the possibility—that there was profit at selling ebooks at $9.99. The court seemed determined to avoid recognizing that Amazon was deliberately losing money on ebooks.

164. *Id.* at 655.

165. *Id.* at 709 app. A; *cf. id.* at 655 n.14, 674.

exchanging information as long as they do not do so as part of some agreement.[166]

Eddy Cue and two other Apple executives—Keith Moerer, a director of Apple's iTunes Store, and Kevin Saul, an Apple in-house attorney—traveled from Apple's headquarters in Cupertino, California, to New York City, where they had a series of individual meetings with each of the Big Six publishers on December 15 and 16, 2009.[167] The district court described the meetings as follows:

> Following a script, Apple conveyed in each of these meetings that it hoped to be able to begin selling e-books through an e-bookstore within the next 90 days as a feature on a new web-enabled machine. Apple expected that its entry into the market with an iBookstore on this device would help make books "cool" for the iTunes generation and quickly make Apple the vehicle through which a significant percentage of e-books were sold.
>
> Cue emphasized that Apple would only launch an e-bookstore if it got all of the major Publishers to sign on. As Cue intended, each of the Publishers understood that this was a reference to the Big Six.[168]

Cue told all of the publishers that Apple was opposed to windowing ebooks and wanted to be able to sell ebooks at lower prices than their physical counterparts.[169] All of the publishers told Cue that they were unhappy with Amazon's $9.99 price point. Some confided that they were searching for ways to gain more control over the retail pricing of ebooks and that they previously made some attempts to force a change but had been unsuccessful. Cue told the publishers that Apple was willing to sell ebooks for prices up to $14.99 for new releases and best sellers.[170] However, the publishers told Cue that their wholesale prices for most ebooks were in the $13.00 to $15.00 range, and that they wholesaled some ebooks for as much as $17.50. That presented a problem. Apple decided it would not open an ebook store if it was going to lose money, and

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166. *See generally* HOVENKAMP, *supra* note 95, at 281–87; GELLHORN ET AL., *supra* note 142, at 283–96.

167. *Apple Inc.*, 952 F. Supp. 2d at 656. According to the court of appeals, Apple said that it would only open an iBookstore if a critical mass of major publishers participated. United States v. Apple Inc., 791 F.3d 290, 302 (2d Cir. 2015).

168. *Apple Inc.*, 952 F. Supp. 2d at 656.

169. *Id.* at 657.

170. *Id.*

the difference between current wholesale prices and the prices at which Apple thought it could successfully sell ebooks left little or no profit. Nevertheless, all the parties were optimistic. The publishers had a powerful incentive to bring Apple into the market, and, thus, to help find a way to make that possible.

Ultimately, the solution presented itself during Apple's meeting with Hachette on December 15. Hachette suggested that Apple consider adopting an entirely different model of pricing ebooks. Under the then-existing wholesale model, publishers provided a suggested retail price (typically printed on the dustjacket or back cover of physical books), but retailers were free to sell the books at any price they desired. Hachette proposed that Apple instead employ an agency model. Under that system, publishers would set the retail price of the book and the retailer would receive a set percentage of that price as a commission. On the following day, HarperCollins made the same suggestion. That was not coincidence; during the prior week, Hachette and HarperCollins had discussed exploring an agency model with Apple.[171] Nor was switching to an agency model a new idea within the industry. Some publishers had previously told Amazon they wanted to switch to an agency model—to no avail. Moreover, Barnes & Noble wanted to stem its own losses in ebooks by switching to an agency model, although doing so while Amazon was still on the wholesale model and selling ebooks for $9.99 was not feasible.[172]

The agency model proposal surprised Cue, however, and he initially rejected it. Nevertheless, the agency model made sense for all parties for a number of reasons. First, it allowed publishers to set the retail price, which was something they cared very much about as a result of Amazon's practice. Second, it guaranteed a reasonable profit to the retailer, provided of course that the commissions were set at a suitable level. Third, it navigated around a potentially thorny legal problem. The law is far from clear as to when a supplier can dictate to a dealer the retail price of its product.[173] However, suppliers can traditionally set the retail price for products sold to retailers on consignment, that is, when suppliers retain title

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171. *Id.* at 657 n.16.
172. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2441.
173. *See infra* notes 325–35 and accompanying text.

to the goods and the retailers act as agents of the suppliers and are paid by commission upon sales to consumers.[174]

It is no surprise, therefore, that when Cue and his team returned to Cupertino and thought hard about what they had heard, they decided to embrace the agency model.[175] The Apple team developed a proposal based on the agency model. Cue, a skilled and experienced negotiator, decided to test his proposal with three selected publishers. He already knew that Hachette and HarperCol- HarperCollins liked an agency model, so he did not need to return to them yet. Cue pegged Penguin's CEO, David Shanks, as a "follower," and therefore felt that there was little point in talking to him first. Cue believed that Carolyn Reidy, Simon and Shuster's CEO, was an industry leader, so he wanted to test his proposal with her. In addition, Cue decided to test his proposal with Random House because it was the largest and most desirable publisher. And, in what would prove to be an especially savvy choice, Cue decided to test his proposal with Macmillan because, even though it was the smallest of the Big Six, it had cachet within the industry. Macmillan had a reputation for publishing quality books, and it was led by John Sargent, who came from a family with a distinguished history in book publishing.[176]

Over the following week, Cue talked individually to top executives from those three publishers. He proposed an agency model with a thirty percent commission to Apple. He also wanted a deal that included two other elements that ultimately became the largest legal problems. First, Cue wanted a mechanism ensuring "some level of reasonable pricing."[177] Apple thought it essential that publishers price ebooks significantly below their physical book counterparts. Readers expected to pay less for an ebook than for a physical book. They had become accustomed to that through Amazon's pricing, and they knew that ebooks saved publishers money in paper, printing, and transportation costs. Thus, Cue suggested capping the retail price for new releases at $12.99.

Second, Apple needed to find a way to ensure that Amazon could not continue its loss-leader strategy and dramatically undersell Apple. The simple solution would be to require the publishers

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174. HOVENKAMP, *supra* note 95, at 635–39. Although Supreme Court doctrine regarding resale price maintenance was substantially changed in 2007, federal court decisions in 2008 and 2009 held that the consignment exception remained viable. *Id.* at 639.

175. *Apple Inc.*, 952 F. Supp. 2d at 658.

176. Sargent's father led Doubleday from 1963 to 1978, expanding it into an industry giant. *Id.* at 660 n.18.

177. *Id.* at 660.

to agree that they would switch to the same agency model with Amazon, and the first draft of Apple's agreements with publishers required that the publishers employ an agency model for all ebook retailers.[178] However, Apple worried that that presented legal problems.[179] So, instead, Apple included a most favored nation (MFN) clause in the agreements. This permitted Apple to obtain ebooks from publishers at thirty percent less than the lowest retail price on the market. Thus, if Amazon was selling an ebook for $9.99, the publisher would have to make that ebook available to Apple for $6.99, thereby allowing Apple to match Amazon's price and receive its thirty percent commission. As a practical matter, that would compel publishers to move Amazon to an agency model—something that most of them wanted to do anyway.

Each of the publishers then engaged in vigorous, individual negotiations with Apple, with most of the focus on price caps. John Sargent of Macmillan, for example, suggested that Apple offer each publisher a choice between a thirty percent agency model without windowing or a wholesale model with windowing.[180] Sargent also wanted to be able to price most new releases within a range of $12.95 to $14.95 with the ability to price selected ebooks at $19.95. The other publishers also balked at the combination of a $12.99 price with a thirty percent cut for Apple. It left them with less than they wanted.[181] Ultimately, however, Apple and each of the publishers agreed to a thirty percent commission agency model without windowing and with tiered price caps. For example, if a hardcover bestseller were priced at $30 or less, the ebook price would be capped at $12.99; if a hardcover bestseller was priced above $30.00 and up to $35.00, the ebook price would be capped at $14.99.[182] There were similar, but not identical, tiers for other new releases and higher tiers of $16.99 and $19.99 for some new releases with higher hardback list prices. Some of the publishers remained less than happy with the price caps, but they concluded it was the best they could do. At Simon & Shuster's request, Apple agreed to revisit the price caps after a year.[183]

178. *Id.* at 662–63.

179. It is unclear whether Apple thought it would be unlawful to include such a clause in its agreement with publishers or that such a clause would be legally unenforceable. *Id.* at 663 n.23.

180. *Id.* at 660.

181. *See id.* at 661.

182. *See id.* at 669–70 (describing in more detail the price tiers proposed by Cue and stating that after further negotiations the publishers ultimately agreed to Cue's proposed tiers).

183. *See id.* at 670.

Although Apple negotiated individually with each publisher, it informed the publishers that it would ultimately offer them substantially identical deals.[184] There was, meanwhile, no shortage of conversations among individual publishers about their discussions with Apple.[185] By the end of January, five of the Big Six signed agreements with Apple. The single holdout was Random House, the largest publisher, and the one that Apple had considered to be essential at the beginning of the process.[186] Random House was reluctant to abandon the wholesale pricing model, which provided higher profits, at least for the present.[187] Apple informed the other publishers that Random House would not agree, and that it was willing launch its iBookstore as long as four of the Big Six signed on.[188] The other five publishers decided they were willing to give up short-term profits for a more secure long-term future.

D. *Confrontation*

The publishers now faced the unnerving task of switching Amazon to the agency model. This was, of course, something the publishers wanted to do, but it was an intimidating prospect nonetheless. Amazon was not only immensely powerful as the largest bookseller in the world, it was notorious for riding roughshod over those who stood in its way.[189] As the district court put it, the deal with Apple "stiffened the spines" of the publishers to finally take on Amazon.[190]

On January 27, 2010, Apple formally announced its iPad at a large event in San Francisco.[191] Walter Mossberg, a columnist covering technology at the *Wall Street Journal* asked how Apple expected to sell iBooks for $14.99 with Amazon selling them for $9.99. "Well," Jobs replied, "that won't be the case."[192] "You mean you won't be $14.99 or they won't be $9.99?," Mossberg asked. "The price will be the same," said Jobs. "Publishers are actually withhold-

184. *See id.* at 664.
185. The district judge observed, "The CEOs of the Publisher Defendants made over 100 telephone calls to one another in the short period of time between December 8, when Cue first contacted them, and January 26, when the Agreements were signed." *Id.* at 674.
186. *Id.* at 656, 660.
187. *See id.* at 673, 677; United States v. Apple Inc., 791 F.3d 290, 308 (2d Cir. 2015).
188. *Apple Inc.*, 952 F. Supp. 2d at 673.
189. *See generally* STONE, *supra* note 122.
190. *Apple Inc.*, 952 F. Supp. 2d at 665.
191. ISAACSON, *supra* note 111, at 493.
192. *Apple Inc.*, 952 F. Supp. 2d at 679; *see also* ISAACSON, *supra* note 111, at 493.

ing their books from Amazon because they are not happy."[193] It was a statement that the courts would later view as a smoking gun.[194]

The publishers had all been invited to the iPad launch. Macmillan's John Sargent did not go. He believed that he should tell Amazon in person that Macmillan needed to move it to the agency model. So instead of flying to San Francisco to attend the iPad event, Sargent flew to Seattle to, as he predicted to a friend, "get [my] ass kicked by Amazon."[195] On January 28, Sargent and a colleague met in a small conference room at Amazon headquarters with Russ Grandinetti, Amazon's senior vice president for Kindle content.[196] Sargent told Grandinetti that Amazon could either switch to an agency model or stay with a wholesale model, but under the wholesale model Macmillan would window ebooks for seven months (the period of time that books were designated as new releases and thus subject to price caps and the MFN clause under the Macmillan-Apple contract).[197] Within twenty minutes, an angry Grandinetti escorted the two Macmillan executives out of the building.[198] When Sargent arrived back in New York the next day he learned that "buy" buttons had been removed from all Macmillan books, both print and electronic, on Amazon.com.[199]

As sociologist John B. Thompson describes it, over the next few days "many in the publishing industry were riveted to their computer screens, watching in astonishment as one of the first great conflicts of the new digital age unfolded before them."[200] Were it alone, Macmillan would have been forced to capitulate, but Macmillan had reason to believe that other publishers would soon insist that Amazon switch to the agency model.[201] It had to survive in the meantime, however. John Sargent decided to take the dispute public. He took out a full-page ad in the trade publication *Publishers Lunch* to publish an open letter to Macmillan authors and the literary agent community.[202] Sargent recounted his meeting with

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193. *Apple Inc.*, 952 F. Supp. 2d at 679.
194. *See id.* at 679, 705; United States v. Apple Inc., 791 F.3d 348, 308, 317 (2d Cir. 2015).
195. Packer, *supra* note 79, at 72.
196. *Id.*; *Apple Inc.*, 952 F. Supp. 2d at 679.
197. *Apple Inc.*, 952 F. Supp. 2d at 679.
198. Packer, *supra* note 79, at 72.
199. *Apple Inc.*, 952 F. Supp. 2d at 679; Jay Yarow, *Macmillan CEO Takes Out a Full Page Ad to Explain His War With Amazon*, BUS. INSIDER (Jan. 31, 2010, 11:45 AM), http://www.businessinsider.com/macmillan-ceo-takes-out-a-full-page-ad-to-explain-his-war-with-amazon-2010-1.
200. THOMPSON, *supra* note 6, at 375.
201. "I had no doubt that others would eventually follow," Sargent wrote to a friend a few days later. *Apple Inc.*, 952 F. Supp. 2d at 680.
202. Yarow, *supra* note 199.

Amazon in Seattle and how Amazon responded by removing Macmillan books from the Amazon.com and Kindle websites. Sargent continued:

> In the ink-and-paper world we sell books to retailers far and wide on a business model that provides a level playing field, and allows all retailers the possibility of selling books profitably. Looking to the future and to a growing digital business, we need to establish the same sort of business model, one that encourages new devices and new stores. One that encourages healthy competition. One that is rational and stable. It also needs to insure that intellectual property can be widely available digitally at a price that is both fair to the consumer and allows those who create it and publish it to be fairly compensated . . . .
>
> The agency model would allow Amazon to make more money selling our books, not less. We would make less money in our dealings with Amazon under the new model. Our disagreement is not about short-term profitability but rather about long-term viability and stability of the digital book market.[203]

The dispute got wide publicity, both in the trade and mainstream press. Even many Amazon customers were outraged at its brutality.[204] Amazon stock fell nine percent.[205] By Sunday night, Amazon announced it was throwing in the towel, though it did not restore buy buttons for Macmillan titles for several more days.[206] The five publishers all switched to agency models with Amazon by summer. Meanwhile, the publishers also switched to an agency model with Barnes & Noble, which was only too happy to make the switch.[207]

Random House remained a holdout. Amazon rewarded it by promoting its titles heavily. "When you go on the Kindle website, it could be the Random House homepage," remarked Penguin's CEO.[208] But in March of 2011, Random House also adopted an

203. *Id.*
204. *Cf. Apple Inc.*, 952 F. Supp. 2d at 680.
205. *Id.*
206. Motoko Rich & Brad Stone, *Macmillan Books Still Mostly Absent From Amazon.com*, N.Y. TIMES (Feb. 2, 2010, 2:19 PM), https://bits.blogs.nytimes.com/2010/02/02/macmillan-books-still-mostly-absent-from-amazoncom/.
207. *See* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2178–81.
208. *Id.* at 2160.

agency model with all three of the major ebooksellers.[209] Amazon tried to maintain wholesale contracts with smaller publishers, but that began to fall apart, as well.[210] Amazon complained to the FTC that it was the victim of a conspiracy among Apple and the five publishers.

II. *U.S. v. Apple*: The Court Decisions

On April 11, 2012, the federal government filed a civil action against Apple and the five publishers.[211] As the government saw it, Amazon was a boon to readers. "E-book sales have been increasing rapidly ever since Amazon released its first Kindle device in November of 2007," the complaint alleged.[212] "One of Amazon's most successful marketing strategies was to lower substantially the price of newly released and bestselling e-books to $9.99."[213] According to the government, Apple and the publishers had conspired to end that beneficial state of affairs and fix prices. "Defendants were determined to end the robust retail price competition in e-books that prevailed, to the benefit of consumers" and "raise the prices consumers pay for e-books through the adoption of identical pricing tiers."[214] The complaint noted that prices for ebooks published by the defendants had risen to $12.99 or $14.99.[215] The government

209. THOMPSON, *supra* note 6, at 375; *see also Apple Inc.*, 952 F. Supp. 2d at 685–86.

210. In March 2010, the Perseus Book Group signed an agency contract with Apple that presumably had the same MFN clause. Though much smaller than the Big Six, Perseus published books under a number of highly-regarded imprints, including Basic Books and Public Affairs. Even more importantly for Amazon, Perseus served as the distributor for more than three hundred smaller publishers. In 2016, Perseus was itself acquired by Hachette. Motoko Rich & Brad Stone, *Amazon Threatens Publishers as Apple Looms*, N.Y. TIMES, Mar. 17, 2010, at B1, http://www.nytimes.com/2010/03/18/technology/internet/18amazon.html; Motoko Rich & Brad Stone, *Perseus Signs an EBooks Deal for the iPad*, N.Y. TIMES: MEDIA DECODER (Mar. 22, 2010, 1:22 PM), https://mediadecoder.blogs.nytimes.com/2010/03/22/perseus-signs-an-ebooks-deal-for-the-ipad/?_r=0. *See generally* THOMPSON, *supra* note 6, at 179.

211. *Apple Inc.*, 952 F. Supp. 2d at 645. Forty-nine states, the District of Columbia, and six U.S. territories and possessions filed a *parens patriae* action, and representative private plaintiffs filed two class actions, against Apple and the publishers. All of the actions were consolidated in the U.S. District Court for the Southern District of New York. *Id.* at 645 n.1. For simplicity's sake, I shall call plaintiff "the government," referring to the federal government only.

212. Complaint ¶ 2, United States v. Apple Inc., 952 F. Supp. 2d 638 (S.D.N.Y. Apr. 11, 2012) (No. 12 CV 2826), ECF No. 1, 2012 WL 1193205.

213. *Id.*

214. *Id.* ¶ 5.

215. *Id.* ¶ 92.

asserted that Apple and the defendants had violated section 1 of the Sherman Act[216] by conspiring to fix prices for ebooks.[217]

"The Government sides with monopoly, rather than competition, in bringing this case," Apple declared in its answer. "The Government starts from the false premise that an eBooks 'market' was characterized by 'robust price competition" prior to Apple's entry." [218] In fact, there had been no real competition in the ebook market—only Amazon, which had been selling nearly ninety percent of all ebooks.[219] Apple argued that its entry into the market had benefitted consumers by bringing Amazon's monopoly to an end. Although Amazon still enjoyed a dominant share in the ebook market, it was "now forced to compete with Apple, Barnes & Noble, and others."[220]

All of the publishers settled, and the case proceeded to trial against Apple alone.

A. The District Court

Following a nearly three-week-long bench trial, Judge Denise Cote issued her opinion on July 10, 2013.[221] She found that

> Apple knowingly and intentionally participated and facilitated a horizontal conspiracy to eliminate retail price competition and to raise the retail prices of e-books. Apple made a conscious commitment to join a scheme with Publisher Defendants to raise the prices of ebooks.[222]

Judge Cote considered the MFN clause to be a critical tool of the conspiracy. She conceded that MFN agreements may be entirely lawful.[223] After all, MFNs generally lower prices. Apple had argued that lowering prices was, in fact, the sole purpose of the MFN clauses. If Apple discovered that another retailer was selling an ebook at a price lower than the retail price set for Apple by the

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216. 15 U.S.C. § 1 (2018).
217. Complaint, *supra* note 212, ¶¶ 94–95.
218. Apple Inc.'s Answer at 1, United States. v. Apple Inc., 952 F. Supp. 2d 638 (S.D.N.Y. May 22, 2012) (No. 12-CV-2826), ECF No. 54, 2012 WL 1862008.
219. *Id.* at 2.
220. *Id.* at 3.
221. United States v. Apple Inc., 952 F. Supp. 2d 638, 647 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015).
222. *Id.* at 697.
223. *Id.* at 698.

publisher, Apple had a right to match that price.[224] That would have been perfectly acceptable, Apple argued. It could happily make profits selling ebooks at $9.99 as long as it received a thirty percent commission.[225] Although Judge Cote agreed that one purpose of the MFN was to allow Apple to meet a lower price, she found that it also had a second purpose: to insure that the publishers would switch Amazon and other ebook distributors to an agency model.[226] This switch would raise prices,[227] which is what Apple and the publishers intended[228] and, in fact, occurred.[229] Judge Cote rejected Apple's argument that there was no violation as long as the MFN had one lawful purpose.[230] "The issue is not whether an entity executed an agency agreement or used an MFN, but whether it conspired to raise prices," she wrote.[231]

Judge Cote also found that the publishers expressly agreed among themselves to all move Amazon to an agency model and that they did so at Apple's insistence. The strongest evidence she described to support that finding involved the following sequence of events. On January 20, John Sargent, Macmillan's CEO, and Russell Grandinetti, an Amazon senior executive, had lunch.[232] (This was one week before the previously-described meeting between the two, when Sargent passed up the iPad launch and instead flew to Seattle to "get [my] ass kicked by Amazon."[233]) At that meeting, Sargent told Grandinetti that Macmillan would give Amazon the option of choosing between the agency or wholesale models. "But, Sargent was mistaken," Judge Cote wrote in her opinion.[234] "Neither Apple nor his fellow Publisher Defendants would allow Amazon the option of remaining on a wholesale model."[235] That evening, Sargent and Apple's Eddy Cue had dinner. Judge Cote believed that at dinner Sargent told Cue about his lunch with

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224. *See* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2483.
225. *Id.* at 2490–91, 2496–97, 2519.
226. *Apple Inc.*, 952 F. Supp. 2d at 692.
227. The essence of the conspiracy, Judge Cote wrote, was that Apple and publishers joined together "to eliminate Amazon's power to set retail prices and then to raise prices to the point that Apple would permit." *Id.* at 705.
228. Judge Cote wrote: "The evidence is overwhelming that Apple knew of the unlawful aims of the conspiracy and joined that conspiracy with the specific intent to help it succeed." *Id.* at 700.
229. *Id.* at 682–83.
230. *Id.* at 701 n.65.
231. *Id.* at 672.
232. *Id.* at 672.
233. *Id.* at 679; s*ee supra* note 195 and accompanying text.
234. *Apple Inc.*, 952 F. Supp. 2d at 672.
235. *Id.*

Grandinetti, and Cue explained to Sargent how the MFN clause effectively required Macmillan to move Amazon to the agency model.[236] The next morning Cue called Carol Reidy of Simon & Shuster and Brian Murray of HarperCollins, and following those calls, Reidy and Murray called Sargent. Cote believed that Cue "enlisted" Reidy and Murray to intercede with Sargent.[237] "The straight talk from Reidy, Murray, and Cue worked," Judge Cote concluded.[238] "Sargent called Grandinetti immediately after hanging up with Reidy, and told him that the Apple contract 'required' Macmillan to offer Amazon the agency model only."[239] Both Sargent and Cue denied that Cue had told Sargent that Macmillan was required to move Amazon to the agency model, but Judge Cote found that neither Sargent nor Cue was credible.[240]

A price fixing conspiracy is illegal *per se*, and thus, in Judge Cote's view, that was that.[241] She added, however, that if Apple's conduct was analyzed under the rule of reason, the result would be the same because Apple's agreements with the publishers had no procompetitive effects.[242]

This was a stunning finding. No procompetitive effects? What about the fact that before Apple's entry into the market, Amazon was a monopolist in ebook retailing market and, moreover, that it maintained that position through predatory pricing? Judge Cote acknowledged that Apple was a new competitor in ebook retailing, but she did not think its entry meaningfully increased competition. She wrote:

> Apple demanded, as a precondition of its entry into the market, that it would not have to compete with Amazon on price. Thus, from the consumer's perspective—a not unimportant perspective in the field of antitrust—the arrival

236. *See id.*
237. *Id.* at 673. Reidy denied having any conversations with any of the other Big Six publishers about moving Amazon to the agency contract. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 455–56. She admitted that Cue told her that Simon & Schuster had to get all other retailers to switch to the agency model. *Id.* at 500–01, 520. However, when asked whether the MFN clause in the Apple contract forced Simon & Shuster to move Amazon and other retailers to the agency contract, Reidy said that that was "the wrong conclusion." *Id.* at 533–34. "We wanted to do it. It had nothing to do with whether Apple made it a demand or not," she explained. *Id.* at 505.
238. *Apple Inc.*, 952 F. Supp. 2d at 673.
239. *Id.*
240. *Id.* at 672 n.38.
241. *Id.* at 694.
242. The government had shown "that the Agreements did not promote competition, but destroyed it," wrote Judge Cote. *Id.*

> of the iBookstore brought less price competition and higher prices.[243]

Besides, if Apple thought that Amazon was monopolizing the ebook market through predatory pricing, its remedy was to complain to law enforcement agencies or file its own civil lawsuit. Another company's illegal behavior does not excuse engaging in illegal activity oneself, reasoned Judge Cote, and thus whether Amazon had been violating the antitrust laws was not her problem.[244]

B. *The Second Circuit*

1. The Majority

On appeal, the Second Circuit's three-judge panel split. Judge Debra Ann Livingston wrote the majority opinion. As she saw it, Apple and the publishers acted collectively to achieve a common goal of raising ebook prices.[245] The court saw the conduct of Apple and the publishers in terms of a classic hub-and-spoke price-fixing conspiracy.[246] The hub was Apple and the spokes were the five publishers. The distinction between independent and concerted action is fundamental to antitrust analysis.[247] Apple was permitted to act independently to negotiate and sign agreements with individual publishers at whatever prices Apple and each individual publisher found acceptable. Apple was also permitted to ask publishers to sign identical agreements and to tell each publisher what it was doing, provided that Apple was acting independently and in its own interests. However, Apple could not lawfully be either a ringmaster or an agent of a conspiracy among competitors. The issue in hub-and-spoke cases is whether there were agreements around the rim of the wheel—among the publishers—to create agreements that fixed prices.[248]

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243. *Id.* at 708.
244. "This trial has not been the occasion to decide whether Amazon's choice to sell NYT Bestsellers or other New Releases as loss leaders was an unfair trade practice or in any other way a violation of law," Judge Cote wrote. *Id.*
245. United States v. Apple Inc., 791 F.3d 290, 317 (2d Cir. 2015).
246. *Id.* at 314.
247. *See, e.g.,* Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752, 760–61 (1984).
248. *See, e.g.*, Howard Hess Dental Labs., Inc. v. Dentsply Int'l, 602 F.3d 237, 255 (3d Cir. 2010).

The court concluded that "ample evidence identified by the district court established both that the Publisher Defendants' shifting to an agency model with Amazon was the result of express collusion among them and that Apple consciously played a key role in organizing that collusion."[249] Key evidence was the MFN, which was specifically designed to persuade the publishers to act collectively to switch Amazon to agency agreements. "Indeed," wrote the court, "the MFN's capacity for forcing collective action by the publishers was precisely what enabled Jobs to predict with confidence that 'the price will be the same' on the iBookstore and the Kindle when he announced the launch of the iPad."[250]

The court noted that "Apple never seriously argues that the Publisher Defendants were not acting in concert."[251] That was correct. Apple argued that the government had not met its burden of proving that the publishers had engaged in a conspiracy to raise prices, but that was as far as it went.[252] In his closing summation Apple's counsel said "we do not have an opinion one way or another," about whether the publishers had engaged in a horizontal price-fixing conspiracy among themselves.[253] We only know what we know, Apple essentially argued, and we don't know what the publishers were doing among themselves without telling us. That position was an interesting tactical choice because it comes dangerously close to conceding that the publishers had engaged in a horizontal price-fixing conspiracy. Indeed, that tactical decision may have been decisive in persuading the trial and appellate judges that there had been a conspiracy.[254]

But what was the evidence that the publishers conspired to fix prices? As with the district judge, the court of appeals made much of the many conversations among the publishers.[255] It was, however, not unlawful for publishers to talk among themselves as long as they did not agree to fix prices or collectively engage in other activity that unreasonably restrained trade.[256] Rather than identifying

249. *Apple Inc.*, 791 F.3d at 316.
250. *Id.* at 317.
251. *Id.* at 318.
252. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2525–28.
253. *Id.* at 2458.
254. "I think that the critical question is, in terms of Apple's liability, whether Apple was aware of such a horizontal conspiracy," Apple's counsel stated. "Oh, I agree with that, absolutely," Judge Cote responded. *Id.*
255. *See, e.g.*, *Apple Inc.*, 791 F.3d at 318 ("That the Publisher Defendants were in constant communication regarding their negotiations with both Apple and Amazon can hardly be disputed.").
256. *See infra* notes 273–74 and accompanying text.

anything unlawful or even problematic in those conversations, the court merely states, "Indeed, Apple never seriously argues that the Publisher Defendants were not acting in concert."[257]

As Judge Livingston saw it, the publishers' objective was principally, if not solely, to raise the price of ebooks. She wrote, "[f]aced with downward pressure on prices but unconvinced that withholding books from Amazon was a viable strategy, the Publisher Defendants—their coordination orchestrated by Apple—combined forces to grab control over price."[258] But Judge Livingston's opinion becomes murky about precisely who wanted to raise prices and who wanted the price caps. "This control over pricing facilitated *their* ultimate goal of raising ebook prices to the price caps," she wrote.[259] To whom does "their" refer? Since "their" is plural, it cannot refer to Apple alone. Yet the evidence was that Apple imposed the price caps against the wishes of the publishers.[260] Moreover, price caps were solely in Apple's interest. Publishers set the retail prices in the wholesale model, and price caps restricted their discretion.

Although she did not say so clearly, Judge Livingston seemed to accept Judge Cote's conclusion that the price caps were not truly ceilings imposed by Apple but rather a camouflaged price-fixing agreement among the publishers.[261] She wrote that the publishers "had grown accustomed to a business in which they rarely competed with one another on price," and that they wanted to regain control over pricing and use that control to facilitate "their ultimate goal of raising ebook prices to the price caps."[262] This rather obliquely suggests that the publishers established the caps and that they intended them to be not merely caps but the actual retail prices. Judge Livingston's thinking probably came from this statement by Judge Cote in her opinion below, "[a]s the Publisher Defendants' CEOs testified, the Publishers did not compete with each other on price; while they were serious competitors, their pre-

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257. *Apple Inc.*, 791 F.3d at 318.
258. *Id.* at 327.
259. *Id.* (emphasis added).
260. *See, e.g.,* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 396 (testimony from David Shanks, Chief Executive Officer, Penguin Group U.S.A., who stated, "We wanted no price caps."); *Apple Inc.id.* at 1803 (testimony from Eddy Cue, Senior Vice President of Internet Software and Services for Apple Inc., who stated that he proposed price caps).
261. *See supra* notes 258–59 and accompanying text.
262. *Apple Inc.*, 791 F.3d at 327.

ferred fields of competition were over authors and agents."[263] Judges Livingston and Cote seemed to believe that the publishers did not compete on price because of some kind of agreement among them, but the judges misunderstood what the publishers were saying.

Because of the unique nature of the book business, publishers do not really compete on price—or at least do not compete on price in the same way as producers of most other products.[264] Consider someone shopping for extra virgin olive oil in the supermarket. There are many brands on the shelf in front of him, and he does not have a strong brand preference.[265] Price may well be the determining factor.[266] The more fungible the product, the more price is likely to be controlling. Nothing is less fungible than books. Each book is unique. A Tana French fan wants to read French's latest mystery, *Trespasser,* not just any mystery. If she finds the hardback version too pricey at $19.12, she might decide to wait for the paperback, purchase the ebook version, or borrow *Trespasser* from the library. She is, however, unlikely to substitute Sue Grafton's most recent mystery because its hardback version is selling for $17.40.[267] When Tana French's publisher, Penguin, decided how to price *Trespasser,* it considered how to maximize total revenue from all of the versions of the book that it would ultimately release. It

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263. United States v. Apple Inc., 952 F. Supp. 2d 638, 651 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015).

264. *Cf.* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 383 (testimony from David Shanks, who stated, "Sometimes we would need to compete on price," but suggesting this is something of a rarity).

265. He may or may not be aware that the representations made on olive oil labels are notoriously unreliable. *See, e.g.,* Larry Olmstead, *It's Extra Virgin Olive Oil Day—Is Your EVOO Real or Fake?,* FORBES (Sep. 30, 2016, 9:24 AM), https://www.forbes.com/sites/larryolmsted/2016/09/30/its-extra-virgin-olive-oil-day-is-your-evoo-real-or-fake.

266. This does not necessarily mean the customer selects the least expensive brand. She may assume price is correlated with quality.

267. These are the actual prices offered by Barnes & Noble on the day I write this for *Trespasser* and Grafton's newest book, *Y is for Yesterday.* There are, of course, readers who will select one of those two books despite never having previously read French or Grafton, but price is unlikely to be determinative for those readers as well. Most will make the choice based on reviews, recommendations from friends, or plot descriptions and blurbs on the dust jackets. The $1.62 price differential will not drive the decision. On the other hand, price may affect a choice among similar books by a particular author. For example, based on a glowing review of *Glass House,* the latest novel by mystery writer Louise Penny, whom I had never previously read, I decided to try her. I often read mysteries on my Nook. Rather than spending $14.99 for the Nook version of *Glass House,* I instead purchased the Nook version of Penny's previous novel *A Trick of the Light* for $2.99. Why so cheap? *A Trick of the Light* received critical acclaim, and it may be one of Penny's best mysteries. My guess is that either Barnes & Noble or Penny's publisher wanted to encourage readers like me to try one of Penny's best books in the hope of making a new Penny fan who will wind up buying more of her fourteen novels.

asked itself whether pricing the hardback at a particular level would cause too many readers to forgo purchasing that version in favor of waiting for the paperback or visiting the library.[268] This consideration, more than the prices of other books, drives a publisher's pricing decision.

Judge Livingston saw the facts much as Judge Cote had below. "Apple consciously played a key role in organizing" a horizontal price-fixing conspiracy among the publishers," she wrote.[269] But, once again, what was the evidence that the publishers and Apple had conversations that could properly be characterized as price fixing? Judge Livingston, like Judge Cote below, seemed to assume that conversations among publishers were nefarious for the simple reason that they were rivals.[270] Judge Livingston observed, "[w]hen time ran short, Apple coordinated phone calls between publishers who had agreed to join and those who remained on the fence."[271] But was it unlawful for Apple, which had a legitimate self-interest in wanting a critical mass of publishers to participate in its iBookstore, to ask one publisher to help persuade other publishers to participate?

Apple, of course, understood that the publishers wanted to end Amazon's below-cost pricing of ebooks. It also understood that the publishers were afraid to take on Amazon over that issue alone. There is little doubt that Apple wanted to take advantage of that fear. Like Judge Cote, Judge Livingston believed that Apple deployed the MFN to force the publishers to act collectively to switch

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268. *See* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 336 (testimony from David Shanks, Chief Executive Officer, Penguin Group U.S.A, who explained this in general terms; the specific examples of *Trespasser* and *Y is for Yesterday* are mine).

269. United States v. Apple Inc., 791 F.3d 290, 318 (2d Cir. 2015).

270. Admittedly, that assumption received a bit of support from skillful cross-examination by the government. As previously discussed, there were a series of dinners among CEOs of the Big Six publishers. *See supra* note 146 and accompanying text. The CEO of the Penguin Group parent company attended those meetings. At trial, government's counsel asked that man's subordinate, CEO of the subsidiary Penguin U.S.A., "Do you find it odd that your boss from London would be in the United States, in New York, at meetings with the CEOs of your principal rivals and not telling you about it? Do you find that odd as you sit here today?" The witness answered: "I guess so, yes." Rather than asking why he might consider that odd, counsel reminded the witness (and the court) that the man who attended the dinners was the one who made the final decision to switch to agency contracts, and then quickly switched to another topic. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 358 (testimony from David Shanks). The careful reader will recognize, however, that the cross-examiner deftly deployed innuendo and nothing more.

271. *Apple Inc.*, 791 F.3d at 319. Although Apple disputed that it had encouraged communications among the publishers, the district court found that Apple had in fact done so. *Id.* at 319 n.18.

Amazon to an agency model.[272] As Judge Livingston herself recognized, a violation of section 1 of the Sherman Act requires "a conscious commitment to a common scheme *designed to achieve an unlawful objective*."[273] Collective action by the publishers, whether on their own initiative, at Apple's inducement, or a combination of the two, only matters if they collaborated to achieve an illegal objective. Judge Livingston believed that the unlawful objective was "the goal of raising ebook prices."[274] However, that brings us to the key question: Was it unlawful for the publishers to act collectively to end Amazon's practice of below-cost—and, arguably, predatory—pricing? That question was never clearly framed, let alone addressed, by either the district court or the Second Circuit.

"Horizontal price-fixing conspiracies traditionally have been, and remain, the 'archetypical example' of a *per se* unlawful restraint on trade," Judge Livingston wrote.[275] True enough. But if this was a price-fixing conspiracy at all, it most certainly was not an archetypical one.

The Second Circuit brought cookie-cutter analysis to a unique set of facts. For example, it inferred that a conspiracy existed from parallel action by the publishers demanding that Amazon switch to an agency model.[276] The court recognized, however, that parallel action by itself is not sufficient. When there is parallel action by rivals, there must also be a good reason to infer that they were acting in parallel as a result of an explicit or implicit agreement to do so and not merely because they were doing the same thing because they each concluded it was in their individual interest to do so.[277] Sometimes collaboration can be inferred from one member of the alleged conspiracy acting against its own self-interest. Take, for example, an alleged price-fixing conspiracy in which there are five manufacturers of widgets who all sell their widgets for $10.00 each. One company has an excessive inventory of widgets and a desperate need for cash. Widgets are moving slowly and are generally sold

272. The purpose of the MFN, she wrote, was to "entice a critical mass of publishers . . . collectively to shift Amazon to agency." *Id.* at 317.

273. *Id.* (quoting Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752, 764 (1984) (emphasis added)).

274. *Id.*

275. *Id.* at 321.

276. Although the court of appeals made much of the publishers' parallel action, it neglected to explicitly identify which parallel action it was focused on. Presumably, it was their parallel action in requesting that Amazon switch to the agency model.

277. The court itself recognized this. *See Apple Inc.*, 791 F.3d at 315 (noting that additional circumstances, or "plus factors," in addition to parallel action, can prove an antitrust conspiracy).

in lots of 500 or less. A customer offers to purchase 10,000 widgets for $95,000.00 ($9.50 each). The company would make a profit, and the sale would eliminate the need for it to borrow $95,000.00 at a high interest rate. It is in the company's interest to make the sale, yet it does not do so. It is possible to infer that the firm declined to make the sale because it was party to a price-fixing agreement.

Attempting to follow that logic, the court of appeals noted the following: "Under Apple's proposed agency model, the publishers stood to make *less* money per sale than under their wholesale agreements with Amazon, but the Publisher Defendants were willing to stomach this loss because the model allowed them to sell new releases and bestsellers for more than $9.99."[278] The court characterized the conduct of the publishers and Apple as a classic hub-and-spokes price-fixing conspiracy.[279] The court noted that such conspiracies are unlawful *per se* because they "always or almost always tend to restrict competition and decrease output."[280] But what kind of price-fixing conspiracy is it if the participants are plotting to *decrease* their profits?[281] It is certainly not a classic price-fixing conspiracy. One ought to wonder whether it is an unlawful price-fixing conspiracy at all.[282]

After concluding that Apple's conduct constituted a *per se* violation of the Sherman Act, Judge Livingston, writing for herself

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278. *Id.* at 316 (emphasis added).

279. *See, e.g.*, *id.* at 322 (analogizing the facts in the case at hand to those in United States v. General Motors, 384 U.S. 127 (1966), and mentioning that the Supreme Court characterized the latter as a "classic conspiracy"); *id.* at 326 (analogizing the facts in the case at hand to those in Catalano, Inc. v. Target Sales, Inc., 446 U.S. 643 (1980) and mentioning that the Supreme Court characterized the latter as an "'archetypal example' of a *per se* unlawful restraint of trade"); *id.* at 327 (stating "[t]he conspiracy among Apple and the Publisher Defendants comfortably qualifies as a horizontal price-fixing conspiracy" that deserves to be condemned as *per se* unlawful).

280. *Id.* at 322 (quoting Leegin Creative Leather Products, Inc. v. PSKS, Inc., 551 U.S. 877, 886 (2007)).

281. It has long been accepted that "[a]ny combination which tampers with price structures is engaged in an unlawful activity," regardless of whether the goal is to raise, lower, or maintain prices. United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 221 (1940). Regardless of how they may seek to manipulate prices, however, we expect that the goal of participants in a price-fixing conspiracy is to maximize profits.

282. This is sufficiently unusual that, even if the publishers agreed to try to raise prices, the courts should have evaluated their conduct under the rule of reason. *See, e.g.*, Broad. Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 9 (1979) ("[It] is only after considerable experience with certain business relationships that courts should classify them as *per se* violations.") (quoting United States v. Topco Assocs., 405 U.S. 596, 607–08 (1972)).

alone,[283] went on to decide that Apple's conduct also failed a "quick look" rule of reason analysis.[284] Courts use quick look when a defendant has employed a type of restraint that is considered unreasonable on its face—such as, in this case, price fixing—but has done so in an unusual way or in unusual market context.[285] Judge Livingston employed the quick look analysis by assuming that Apple's conduct had an actual adverse effect on competition but giving Apple the opportunity to prove that its conduct had procompetitive justifications.[286]

Apple's main procompetitive justification was that its contracts with publishers allowed it and other ebook retailers to enter a market previously dominated by a single firm. To Judge Livingston, this was tantamount to saying "that higher prices enable more competitors to enter a market."[287] Apple's complaints about Amazon's $9.99 price point were whining by a less efficient firm.[288] Judge Livingston was unmoved by the fact that Amazon had been pricing ebooks below cost, thereby creating a barrier to rivals entering the market.[289]

Echoing Judge Cote's opinion below, Judge Livingston wrote that if Apple or the publishers thought that Amazon's pricing violated the antitrust laws, they should have sued Amazon for monopolizing the ebook market.[290] There are, however, at least two serious problems with that analysis.

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283. *Apple Inc.*, 791 F.3d at 339–40 (Lohier, J., concurring). Judge Raymond J. Lohier, who joined the first part of Judge Livingston's opinion, believed that the case should be determined on a *per se* analysis and a rule of reason analysis should not be undertaken. *Id.*

284. Whether there is, in fact, a well-defined quick look analysis is debatable. *See* California Dental Ass'n v. FTC, 526 U.S. 756, 779 (1999) ("The truth is that our categories of analysis of anticompetitive effect are less fixed than terms like 'per se,' 'quick look,' and 'rule of reason' tend to make them appear."); *see also* HOVENKAMP, *supra* note 95, at 349 ("The Court has used the term [quick look] in only three decisions, and has rejected its application on all three.").

285. *See* HOVENKAMP, *supra* note 95, at 347–48.

286. *Apple Inc.*, 791 F.3d at 330. Judge Livingston emphasized that although she was relieving the government of the burden of showing, through a full market analysis, that Apple's conduct had an anticompetitive effect, she was nonetheless giving Apple's procompetitive justifications as much attention as she would under a full rule of reason analysis. *Id.* at 329–30.

287. *Id.* at 330.

288. *See id.* at 333 (asking, rhetorically, whether "it is desirable to require more efficient competitors to charge the same as their less efficient rivals solely so the latter will be spared the indignity of not charging the best price?")

289. *See id.* Judge Livingston contrasted Apple's unwillingness to enter a market in which Amazon was pricing below cost with Barnes & Noble, which had done exactly that, but she was insensitive to the business necessity that left Barnes & Noble little choice but to enter the ebook market, even if it would to lose money. *See supra* notes 127–30 and accompanying text.

290. *Id.* at 332.

First, it is unclear whether Apple or the publishers had standing to sue. Only parties injured in "their business or property" have standing to bring antitrust claims.[291] Arguably, the publishers were not injured because they made profits on their sales to Amazon. Their profits, moreover, were unaffected by Amazon's retail pricing. Publishers were gravely concerned that Amazon's pricing threatened book publishing in the long run, but courts would almost certainly consider those concerns too remote and contingent to constitute an injury for antitrust standing purposes.[292] If anything, Apple had an even more serious standing problem. Although courts liberally find that injured competitors have standing, Apple was not Amazon's competitor before it actually entered the market. It was not in the ebook business; it was merely contemplating entering that business. This is called the problem of the unestablished business.[293] It is one thing, for example, for a widget seller in New York to sue a rival for preventing it from expanding into New England by selling widgets there below cost, but it is quite another thing for a firm not in the widget business at all to make that complaint. Courts generally find that an unestablished business lacks standing unless, at a minimum, it made substantial expenditures in preparation to enter the market before the defendant frustrated its plans through allegedly unlawful conduct.[294] This does not mean that Apple and publishers indisputably lacked standing to sue, but at a minimum they would have faced serious standing issues at the outset of a monopolization case against Amazon, diminishing the feasibility of the litigation alternative.

Second, putting aside the question of whether a lawsuit was feasible, why should a party oppressed by another party's unlawful antitrust practices not challenge those practices in the marketplace if it has the ability to do so? Why require litigation rather than self-help?[295] Judges Cote and Livingston were too dismissive of the ar-

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291. *See* Clayton Act, ch. 323, § 4, 15 U.S.C. § 15 (2018).

292. *See, e.g.*, Blue Shield of Virginia v. McCready, 457 U.S. 465, 477 n.13 (1982) (suggesting that traditional proximate cause concepts apply, such as whether the connection between defendant's conduct and plaintiff's injury is remote or tenuous); Illinois Brick Co. v. Illinois, 431 U.S. 720, 748 n.2 (1977) ("There is, of course, a point beyond which antitrust defendants should not be held responsible for the remote consequences of their actions.")

293. *See, e.g.*, HOVENKAMP, *supra* note 95, at 825–26.

294. *See, e.g.*, *id.* at 825.

295. Judge Jacobs made a similar point in dissent when he observed that it would not have been feasible for Apple to challenge Amazon's predatory pricing through litigation and then added: "More fundamentally, litigation is not a *market* alternative . . . . A requirement that potential market entrants litigate instead of enter the market on restrictive (but legal and reasonable) terms, would license monopoly for the duration." *Apple Inc.*, 791 F.3d at 352 (Jacobs, J., dissenting) (emphasis in original).

gument that it was reasonable for Apple to fight fire with fire, that is, for Apple to engage in questionable conduct to destroy a monopoly protected by predatory pricing. "Another company's alleged violation of antitrust laws is not an excuse for engaging in your own violation of law," Judge Cote wrote.[296] That is, at best, too absolute a statement. The law often finds violations of law to be justified. Criminal law recognizes a lesser-evil or necessity defense, under which one may be forgiven for violating the law if adhering to it would have resulted in greater harm. Lesser-evil questions are very controversial. Lawyers, philosophers, and ethicists vigorously debate such questions as whether one may throw a switch to divert a train from one track on which it will kill ten people to another track on which it will kill one person, or whether it is permissible to torture a terrorist to force him to reveal the location of a ticking time bomb.[297] Nevertheless, the lesser-evil defense is widely recognized in the criminal law.[298] Other areas of the law have similar doctrines. Tort law, for example, recognizes that one may not be liable for conduct that is generally tortious when the available alternatives would have been worse for social welfare.[299] The balancing of harms is generally a principal focus of these doctrines.[300]

296. United States v. Apple Inc., 952 F. Supp. 2d 638, 708 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015). Although Judge Cote did not cite it, some believe *Fashion Originators' Guild of America v. FTC*, 312 U.S. 457 (1941), stands for the proposition that firms victimized by unlawful conduct cannot collectively engage in unlawful conduct themselves in an effort to protect themselves. However, *Fashion Originators'* is very different from *United States v. Apple*. In *Fashion Originators'*, the 136 manufacturers that comprised the defendant Guild occupied a "commanding position" in the industry. *Id.* at 462. Their market share in one segment of the industry exceeded sixty percent. *Id.* The Guild and its members were seeking to preserve their commanding position, whereas Apple and the publishers were challenging Amazon's commanding position and seeking to bring more competition to the market.

297. *See, e.g.,* TORTURE: A COLLECTION (Sanford Levinson rev. ed. 2006) (wherein various contributors address both hypotheticals). Reality struck far too close to the latter hypothetical when lawyers in President George W. Bush's administration wrote legal memoranda to justify torturing of prisoners. They accomplished their goal by defining torture as only those things that cause bodily injury that rises "to the level of death, organ failure, or the permanent impairment of a significant body function." *See* Padilla v. Yoo, 678 F.3d 748, 753 (9th Cir. 2011).

298. MODEL PENAL CODE § 302 (AM. LAW INST., Proposed Official Draft 1962). More than twenty states have lesser-evil defenses (also referred to as choice-of-evil and necessity defenses in their criminal codes); George Christie, *The Defense of Necessity Considered From the Legal and Moral Points of View*, 48 DUKE L.J. 975, 1025 (1999).

299. *See, e.g.*, Surocco v. Geary, 3 Cal. 69 (1853) (holding that defendant was not liable for destroying plaintiff's home to stop the progress of fire threatening an entire city); Zeni v. Anderson, 243 N.W.2d 270 (Mich. 1976) (holding that because of heavy snowfall defendant had an excuse for violating a statute that made it unlawful to walk in the road rather than on the sidewalk); Harrison v. Wisdom, 53 Tenn. 99 (1872) (holding that defendants were not liable for destroying all the liquor in town before the arrival of the Union army).

300. *See* John T. Parry, *The Virtue of Necessity: Reshaping Culpability and the Rule of Law,* 36 HOUS. L. REV. 397, 408 (1999); Adav Noti, Note, *The Uplifted Knife: Morality, Justification, and*

Antitrust law considers balancing of harms in an even more fundamental way: it is an integral part of evaluating whether a party's conduct should be deemed unlawful under a rule of reason analysis. Under a rule of reason analysis, conduct is not deemed unlawful when its benefits outweigh its harms.[301] Moreover, conduct that has significant virtues should always be evaluated under the rule of reason and never condemned as unlawful *per se*.[302] The Supreme Court's 2007 decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*[303] reinforced this concept. The Court decided that whether resale price maintenance is to be deemed lawful or unlawful depends upon whether, in a particular situation, its procompetitive benefits outweigh its anticompetitive deficits.

As Judges Cote and Livingston saw it, Apple's conduct had no social benefits, and a balancing of harms would have been beside the point. How did they reach that conclusion in light of the social benefits flowing from destroying Amazon's chokehold over ebooks? The answer, of course, is that they believed it was proper to consider only the single social benefit of consumer welfare, which to them meant prices, industry output, and little else. They were not alone in this view. Regrettably, for these purposes as well as for others, courts generally ignore everything other than price and output.[304]

Judge Livingston's analysis also suffered from an unwarranted factual assumption. "[A]mazon was taking a risk by engaging in loss-leader pricing, losing money on some sales in order to encourage readers to adopt the Kindle," she wrote.[305] Judge Livingston did

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the Choice-of-Evils Doctrine, 78 N.Y.U. L. REV. 1859, 1872–73 (2003) (regarding criminal law); RESTATEMENT (SECOND) OF TORTS § 263 cmt. d, § 288A(e) (AM. LAW INST. 1975) (regarding torts).

301. Richard S. Wirtz, *Purpose and Effect in Sherman Act Conspiracies,* 57 WASH. L. REV. 1, 12 (1981). Wirtz argues: "The question is whether in a given case there is a reasonable likelihood that [conduct that stifles competition in some fashion] will do equivalent good." *Id.*

302. *See, e.g.*, *id.* at 39.

303. 551 U.S. 877 (2007).

304. *Cf.* John B. Kirkwood, *Collusion to Control a Powerful Customer: Amazon, E-Books, and Antitrust Policy*, 69 U. MIAMI L. REV. 1, 20 (2014) (stating that contemporary antitrust "decisions have rejected attempts to justify collusion on the ground that it would promote social values, like public safety, or put an end to illegal behavior.").

305. United States v. Apple Inc., 791 F.3d 290, 332 (2d Cir. 2015). Judge Livingston also observed that "the district court did *not* find that Amazon used the $9.99 price point to 'assure[] its domination' in the ebook market, or that its pricing strategy acted as a 'barrier to entry' for other retailers." *Id.* at 299 (emphasis in original). That was literally true but misleading because it erroneously implied that the district court found that Amazon had not engaged in predatory pricing. Judge Livingston also suggested that Amazon's $9.99 price point caused it to lose only a small amount of money on only a small percentage of its total sales, which it used as loss leader to encourage customers to purchase the Kindle. *Id.* at 327.

not cite a factual finding by the district court for that proposition. In fact, the district court never made such a finding. Judge Cote had found that Amazon was selling many books "as loss leaders at $9.99."[306] That may have implied that Amazon made up those losses elsewhere—on its Kindle or on ebooks—but it was nothing more than an unsupported implication. In fact, Judge Cote had expressly chosen not to consider whether Amazon had engaged in legitimate loss leading or predatory pricing.[307]

The courts should have determined whether Amazon's $9.99 price point constituted predatory pricing.[308] That should have been an integral part of their rule of reason analysis. After all, Apple's conduct would have an important procompetitive effect if it eliminated an unlawful predatory pricing scheme. Moreover, the Department of Justice should have considered whether Amazon was engaging in predatory pricing before bringing its action against Apple and the publishers in the first place. As DOJ saw it, Apple and the publishers engaged in conduct that violated the antitrust laws. However, even assuming that DOJ was correct, should DOJ have exercised its discretion to intervene in this marketplace battle if the purpose and effect of Apple and the publishers' conduct was to extinguish a predatory pricing scheme that Amazon used to protect a monopoly?

In his dissent, Judge Jacobs said those statements were apparently based on a filing by Amazon that the district court never accepted. Moreover, it ignored the fact that the books that Amazon sold for $9.99—bestsellers and new releases—accounted for a disproportionately high fraction of its total ebook sales. *Id.* at 344 (Jacobs, J., dissenting).

Judge Livingston may also have been influenced by something else, as well. Based on Chicago School doctrine, which held that for the most part predatory pricing schemes would be irrational, courts became skeptical about predatory pricing claims in general. The Supreme Court famously declared: "[T]here is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful." Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 572, 589 (1986) (citing Chicago School adherents Robert Bork and Frank Easterbrook, among others). This mindset could easily prompt one to leap to the conclusion that Amazon must have been engaging in loss leading rather than predatory pricing. Chicago School theory notwithstanding, real-world experience shows that predatory pricing schemes do exist and are often successful. *See* Bogus, *The New Road to Serfdom, supra* note 13, at 25; Khan, *supra* note 121, at 730 (2017) (stating that "a host of research shows that predatory pricing can be 'an attractive anticompetitive strategy' and has been used by dominant forms across sectors to squash and deter competition."); and sources cited in both articles.

306. United States v. Apple Inc., 952 F. Supp. 2d 643, 650 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015).

307. *Id.* at 708.

308. *Cf.* Kirkwood, *supra* note 304, at 34 (arguing that "it is likely that Amazon was engaged in loss leading rather than predatory pricing" because, in Kirkwood's view, Amazon was not trying to drive rival ebook retailers out of the market).

That raises the question of whether Amazon was engaged in loss leading.[309] Loss leading is using below-cost pricing on one product or service as a magnet to draw customers in the hope of making a profit from other transactions. Grocery stores, for example, often use milk as a loss leader. Consumers are particularly conscious of milk prices.[310] The stores heavily advertise milk prices, and they place milk at the furthest point from the entrance. Their strategy is to attract customers to the store to buy milk, entice them to pick up other products while they are there, and make a profit on the total purchase at checkout. Loss leading is a venerable and often-accepted practice. Predatory pricing, by contrast, is pricing below cost—and absorbing losses—for the purpose of driving rivals out of a market or deterring rivals from entering a market.[311] It is unlawful because it is attempting to monopolize a line of commerce.[312] The key distinction between loss leading and predatory pricing is the seller's intent. Related to that, of course, is whether the seller possessed the market power to sustain below-cost pricing long enough to succeed in driving rivals out of the market or persuading them to abandon plans to enter a market.

There were good reasons to suspect that Amazon engaged in predatory pricing. Amazon has long been notorious for both employing predatory practices and for being willing to sustain losses for long periods of time in order to build its business.[313] In addition, using ebooks as loss leaders to sell ereaders is, on its face, a dubious strategy. Customers who invest in a Kindle plan on purchasing scores—if not hundreds—of ebooks over the life of their

309. Although scholars have vigorously debated the appropriate accounting method to determine whether a seller is selling below cost, they have given remarkably little attention to differentiating loss leading from predatory pricing.

310. *See What Are Loss Leaders in Grocery Stores?*, CULINARYLORE (Aug. 9, 2016) https://culinarylore.com/food-culture:what-are-loss-leaders-in-grocery-stores; *see also* Chris Fleisher, *Loss-leaders: predatory or practical?*, AM. ECON. ASS'N (Mar. 24, 2017), https://www.aeaweb.org/research/loss-leading-bans-retail-competition (noting that loss leading is unlawful in some states).

311. HOVENKAMP, *supra* note 95, at 455; *see also* Shaun D. Ledgerwood & Wesley J. Heath, *Rummaging Through the Bottom of Pandora's Box: Funding Predatory Pricing Through Contemporaneous Recoupment,* 6 VA. L. & BUS. REV. 509, 566 (2012) (discussing when loss leading becomes predatory pricing). For another example of loss leading, *see supra* note 268, which describes pricing one of Louise Penny's mystery books at an extremely low price in the hope of creating new Penny fans who will buy more of her fourteen books.

312. HOVENKAMP, *supra* note 95, at 455–56.

313. *See, e.g.*, Bogus, *The New Road to Serfdom, supra* note 13, at 25 n.127 (regarding Amazon's history of predatory pricing); STONE, *supra* note 122, at 69, 96–97 (regarding Amazon's history of sustaining losses for long periods of time).

devices.[314] Could Amazon's profit margin on the Kindle have been fat enough to compensate for a very long chain of small losses? When first released in 2007, Amazon sold the Kindle for nearly $400.00, but that did not last long. The Kindle sold for $150.00 by July 2010 and for less than $100.00 the following year. Market analysts believed that at least by 2011Amazon was selling the Kindle, as well as ebooks, below cost.[315] It appears that the old joke applies: Amazon was selling everything below cost but making it up on volume.[316]

2. The Dissent

"I have no quarrel with the district court's conscientious findings of fact; I affirmatively rely on them and cite them throughout," wrote Judge Dennis Jacobs as he began his dissent.[317] As he saw it, however, the district court failed to understand the significance of those facts or properly relate them to the applicable legal standards.

Judge Jacobs argued that the district court made three fundamental errors. First, the district court erred in finding that Apple's conduct constituted a *per se* violation of the antitrust laws. "A vertical arrangement that facilitates a horizontal price fixing conspiracy does not amount to a *per se* violation," he wrote. Second, Judge Jacobs believed that "the district court assessed impacts on competition without recognizing that Apple's role as a vertical player differentiated it from the publishers."[318] Apple was a direct rival of Amazon; both were ebook retailers (as was Barnes & Noble). All the talk of conspiracy and collusion was misplaced. This was not a situation where, for example, competitors colluded against their customers. "All Apple's energy—and all it did that has been condemned in this case—was directed to weakening its competitive rival, and pushing it aside to make room for Apple's entry," Judge

314. I suspect my own experience is typical. The Nook books I tend to purchase are new releases, the very category Amazon sold below cost. If a paperback edition is available, I generally prefer that format to the ebook edition.

315. *See* Khan, *supra* note 121, at 757 (stating that analysts estimated that Amazon was selling the Kindle below its manufacturing cost).

316. *Cf.* Richard J. Gilbert, *E-books: A Tale of Digital Disruption,* 29 J. ECON. PERSP. 165, 172 (2015) (stating that the evidence is consistent with Amazon's strategy to use its entire book business, including both physical and ebooks, as loss leaders to draw customers to its website in order to sell them "the plethora of other items that Amazon sells.").

317. United States v. Apple Inc., 791 F.3d 290, 340 (2d Cir. 2015) (Jacobs, J., dissenting).

318. *Id.* at 341.

Jacobs wrote.[319] Apple did, of course, enter into vertical arrangements with publishers, but such arrangements are customary and necessary and "do not represent the same presumptive threat to competition."[320] Moreover, every term that Apple included in its contracts with publishers—the agency model, the MFN clause, and price caps—were lawful.[321] Third and most importantly, Apple increased competition. It entered a market dominated by a firm with a ninety percent market share. How could the district court have thought that ending a monopoly was somehow anticompetitive? It reached that result by mistakenly assuming that Amazon's $9.99 price was good for consumers because it was so low—lower even than cost—and prices rose after the switch to the agency model.[322] However, the goal of antitrust is competition, not low prices. "[I]t can be safely assumed that if competition sharpens, prices will take care of themselves," Judge Jacobs noted.[323] When properly assessed under the rule of reason, it became clear that Apple's conduct "was unambiguously and overwhelmingly pro-competitive."[324]

Judge Jacobs relied heavily on *Leegin*,[325] in which the Supreme Court reversed a century of precedent regarding resale price maintenance. Prior to *Leegin*, a manufacturer could set and require retailers to adhere to a retail price if it acted entirely unilaterally. If, however, the manufacturer's policy resulted from an agreement with distributors or retailers, the agreement was deemed a *per se* violation of section 1 of the Sherman Act. In *Leegin*, the Supreme Court recognized that there were procompetitive justifications for resale price maintenance. Leegin designed and manufactured leather belts and other women's fashion accessories. It sold its products under the brand name "Brighton," and it sought to create a certain image and reputation for that brand. In furtherance of that strategy, Leegin sold its products through boutiques and specialty stores that provided customers with better service and more attractive settings than they would receive in large, impersonal stores. Those stores had higher overheads than large stores. Leegin, therefore, set suggested retail prices that would provide retailers with a generous margin and adopted a policy of not selling

319. *Id.* at 347–48.
320. *Id.* at 348.
321. *Id.* at 350.
322. *Id.* at 343–44.
323. *Id.* at 350.
324. *Id.* at 341.
325. *See* Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007).

to retailers that sold Brighton products below Leegin's suggested retail price.

Leegin cut off a retailer for discounting Brighton goods, and the retailer sued. If plaintiff could show that Leegin's resale price maintenance policy resulted from agreements with or at the request by other retailers, Leegin's conduct would have constituted a *per se* violation under prior doctrine. In *Leegin,* the Supreme Court overturned that rule. The Court began by noting that the *per se* rule is appropriate for restraints that have manifestly anticompetitive effects and lack any redeeming virtues.[326] Courts originally thought that resale price maintenance benefitted only distributors by eliminating price competition among them. But modern economics recognized that such policies can benefit manufacturers and promote inter-brand competition. Resale price maintenance helped to "give consumers more options so that they can choose among low-price, low-service brands; high-price, high-service brands; and brands that fall in between," the Court explained in *Leegin.*[327]

Leegin rounded out a series of cases that draw sharp distinctions between horizontally imposed and vertically imposed restraints. Taken together, the cases hold that courts must evaluate all vertical restraints under the rule of reason. The Court had previously held that courts should not apply the *per se* rule to vertical nonprice restraints[328] or to vertical arrangements that set maximum prices.[329] In *Leegin*, the Court made clear that courts must evaluate *all* vertical price restraints under the rule of reason, including specifically those fixing minimum prices.[330] "Our recent cases formulate antitrust principles in accordance with the appreciated differences in economic effect between vertical and horizontal agreements," the Court explained.[331] The Court noted that most vertical restraints promote interbrand competition, and that interbrand competition is more important than intrabrand competition because it facilitates market entry for new firms and new products, promotes innovation, provides consumers with a greater diversity of products, and

326. *Id.* at 886.
327. *Id.* at 890.
328. *See id.* at 901 (citing Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977)).
329. *See id.* at 902 (citing State Oil Co. v. Khan, 522 U.S. 3 (1997)).
330. *See id.* at 907 (declaring that "[v]ertical price restraints are to be judged by the rule of reason.").
331. *Id.* at 888.

promotes a dynamic economy.[332] Thus, courts must evaluate any restraints imposed vertically by Apple under the rule of reason.

It is necessary, therefore, to decide whether the contract terms at issue in *United States v. Apple*—the agency model, price caps, and an MFN clause—should be classified as vertical or horizontal restraints. They would be vertical restraints if Apple included them in its contracts with the publishers on its own initiative and for its own interests. To track language from a seminal Supreme Court case, the courts should have asked themselves: Did Apple "rely on individual self-interest to bring about general voluntary acquiescence" by the publishers?[333] Conversely, did each publisher make an "individual free choice prompted alone by the desirability" of the Apple contract?[334] If the answers to those questions are yes, then the contractual devices are vertical. On the other hand, if Apple pressured the publishers into "substantial unanimity" and deliberately induced them to take "concerted action" to switch Amazon to the agency model, it became "the organizer of a [horizontal price-fixing] combination or conspiracy" among the publishers.[335] Deciding which scenario occurred required the courts to make a judgment not only about what Apple and publishers did, but on the subjective motivations for their actions. That is a difficult and uncertain endeavor. It is, therefore, not surprising that the judges divided on the vertical versus horizontal question. As Judges Cote, Livingston, and Lohier saw it, the publishers engaged in horizontal price-fixing conspiracy, which Apple either joined or instigated. Judge Jacobs did not challenge the district court's finding that the publishers had engaged in a horizontal conspiracy, but he believed that even if that were the case, Apple's relevant conduct was vertical. "On the only horizontal plane that matters to Apple's ebook business, Apple was in competition and never in collusion," he wrote.[336]

How sensible is this inquiry? Briefly reconsider the key facts: Even before Apple showed up, the publishers were talking among

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332. *See id.* at 890, 895 (stating that the laws are designed primarily to protect interbrand competition); *id.* 889–92 (describing the benefits of inter-brand competition); *cf.* HOVENKAMP, *supra* note 95, at 651 (expressing skepticism about balancing intrabrand and inter-brand competition).

333. *See* United States v. Parke, Davis & Co., 362 U.S. 29, 46–47 (1960) (suggesting that pursuit of individual self-interest by a manufacturer legitimizes retail price maintenance).

334. *Id.*

335. *Id.* at 47.

336. United States v. Apple Inc., 952 F. Supp. 2d 638 (S.D.N.Y. 2013), *aff'd*, 791 F.3d 290 (2d Cir. 2015).

themselves about the danger that Amazon's $9.99 price point posed for their industry. They feared that selling ebooks below cost devalued their product—books, in all formats—in the public's mind, and, thus, they wanted ebook retail prices for new releases and bestsellers to rise. In one fashion or another, they communicated all of that to Apple. A couple of publishers discussed between themselves whether the agency model would be desirable, and perhaps whether they ought to suggest it to Apple. Later they did, in fact, suggest the agency model to Apple. Did those publishers agree that they would both urge Apple to adopt the agency model? Or after jointly brainstorming the question did each publisher individually decide to suggest the agency model to Apple? My guess is that if we asked the publishers which scenario occurred, they themselves honestly might not know the answer.

Meanwhile, from Apple's perspective, the publishers' desires were fortuitous. Apple wanted to enter the ebook retailing business provided it could make a profit. It could not do so under the wholesale model as long as Amazon sold ebooks below cost. After talking with the publishers, Apple realized that their interests were compatible with its own. It devised a contract that gave the publishers control over the retail price of their ebooks—which it knew was something the publishers wanted—but Apple limited their control with price caps. Apple included an MFN clause, which gave publishers an incentive to switch Amazon to the agency model and protected Apple in the event they did not do so. Apple told the publishers it was offering all of them the same basic contract, and there would have been nothing wrong with their confirming that with each other. The publishers believed they could not take on Amazon individually, and Apple knew that was what the publishers believed. Ultimately, five of the Big Six demanded that Amazon shift to the agency model.

The key legal question is whether the publishers acted collectively or in unison. Collective action is the product of agreement. While agreements can be made expressly or impliedly, collective action requires active agreement by some method. Acting in unison, in contrast, means taking the same action simultaneously without agreement. A school of fish changes direction because the fish act in unison. Each fish independently changes direction because it senses what the other fish are doing, and it feels safest staying in the school. There is no "unity of purpose," "common design and understanding," or "meeting of minds" among the fish, which are the hallmarks of collective action under antitrust law.[337] It is entirely possible the publishers acted in unison rather than collectively. Each publisher knew that the Apple contract gave the other publishers strong incentives to switch Amazon to the agency model. Each publisher was able to predict that many, if not all, of the other publishers would move to switch Amazon to the agency model.[338] Moreover, each publisher knew that its acting to switch Amazon to an agency contract would increase the chances of other publishers following suit. That is quite different from agreeing to act in concert with other publishers.

* * *

Regulators and the courts could have, and should have, reached the opposite result under existing doctrine. The Department of Justice should not have brought this lawsuit in the first place. When it did, the courts should have decided the case in Apple's favor. There are at least three reasons why the courts should have reached a different result. First, Judge Cote should not have concluded that the publishers conspired to fix prices. This shall be explained further in the next Section of this Article. Second, regulators and courts should have evaluated the contract terms at issue—price caps and the MFN clause—under the rule of reason and concluded that they were justified by procompetitive effects. Third, as part of their rule of reason analysis, regulators and courts should also have excused any technical violation under lesser-evil or necessity-type theories.

Although it has been necessary to discuss the courts' analyses, the primary objective of this Article is not to demonstrate how the case could have come out differently by applying this or that rule differently. Rather, it to show *why* the regulators and judges reached such a wrongheaded result. What misled them was not discrete rules of antitrust law but the big things—the basic assumptions and overarching worldview into which they had been acculturated and took for granted. It was as if they tried to make their

337. *See* Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752, 764 (1984) (quoting American Tobacco v. United States, 328 U.S. 781, 810 (1946)).

338. There was evidence to support this interpretation of events. *E.g.,* Trial Transcript, United States v. Apple Inc., *supra* note 109, at 469–70 (testimony from Carolyn Kroll Reidy, who stated that, based not on private conversations but on public comments reported in newspapers, she felt "fairly confident" that if her firm changed its business model with Amazon, Hachette and HarperCollins would follow suit); *id.* at 612–14 (describing how, based on knowing her counterparts so well, together with tidbits of information she was able to pick up, she was able to predict what other publishers were likely to do).

way through a legal thicket with a map that was more or less accurate, but they kept misreading the map because their compass constantly pointed in a wildly wrong direction. They were fixated on lower prices when they should have been worrying about consolidated corporate power.

III. WHY ANTITRUST MUST DEAL WITH CONSOLIDATED CORPORATE POWER

This should have been a simple case. With a ninety percent market share, Amazon enjoyed a de facto monopoly in ebook retailing.[339] As the court of appeals itself noted, a market share exceeding eighty percent is deemed to constitute a monopoly under antitrust law.[340] Although Barnes & Noble had just entered the market, Amazon enjoyed significant advantages over its single major competitor.[341] One advantage was Amazon's relative financial strength. As the 372nd largest corporation in America, Barnes & Noble was no bit player; nevertheless, Amazon, which ranked 100th on the Fortune 500, dwarfed its competitor.[342] In addition, Amazon was willing to use financial strength to protect its monopoly with predatory pricing. Its pricing scheme not only deterred putative competitors from entering the market but also drained resources from Barnes & Noble. In a marathon price war between these two firms, Amazon would likely win, notwithstanding critics rating the Nook as the superior ereader.

Even more importantly, there was a real risk of Amazon parlaying its monopoly in ebook retailing into a monopoly in *all* book retailing.[343] In 2010, no one knew whether ebooks would replace physical books. Some knowledgeable observers thought they

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339. With the exception of legally sanctioned monopolies such as public utilities and patented products, there are few absolute monopolies. It is generally accepted that firms with a sixty-five or seventy percent market share may possess monopoly power—that is, the ability to reduce total industry output and increase prices—and firms with a ninety percent market share do possess market power. *See* Steven F. Ross, *Principles of Antitrust* 38–39 (1993) (citing the seventy and ninety percent thresholds); GELLHORN ET AL., *supra* note 142, at 118 (citing sixty-five percent as the "minimum monopolization threshold . . . ."). Market share alone may be a misleading indicator of monopoly power where there is high product differentiation or easy entry into the market. *Id.* at 115–16. Neither of those situations are present here.

340. *Apple Inc.*, 791 F.3d at 342.

341. *Apple Inc.*, 952 F. Supp. 2d at 650.

342. *Fortune 500 2010*, *supra* note 154.

343. *See supra* notes 128–35 and accompanying text.

would, and the shift would come quickly.[344] That is why Barnes & Noble had no choice but to enter the ebook market, even though it had to compete with a financially stronger company selling ebooks below cost. It was damned if it did and damned if it didn't; what else could it do but take the plunge and try to swim in rough water? A potential Amazon monopoly in book retailing had consequences not just for Barnes & Noble and independent booksellers but for the nation. Books are of profound importance to American culture and its political discourse. Having a single firm decide which books are sold in America, and how books offered for sale are displayed—which are conspicuously promoted, which are hard to find—would be an Orwellian nightmare.

Apple's entry into the market accomplished two things: It added a financially capable and technologically sophisticated competitor to the market, and it knocked down the barriers to entry protecting Amazon's de facto monopoly. In view of these simple realities, Apple should have been welcomed as a rescuer on a white horse. Instead, antitrust regulators and the courts viewed Apple as a villain. Why?

Let's start with Judge Cote's most critical finding of fact. "[T]his Court has found," she wrote, "that Apple knowingly and intentionally participated in and facilitated a horizontal conspiracy to eliminate retail price competition and raise the retail prices of ebooks."[345] But, there was no direct evidence to support that finding.[346] Eddy Cue, Apple's chief negotiator, and CEOs of the publishing companies all denied that they had conspired to fix prices. That, of course, did not settle things. It is not unheard of for participants in unlawful enterprises to deny wrongdoing. This, however, was far from the typical case. The publishers freely admitted they wanted to raise ebook prices.[347] This case is also unusual in

344. *See supra* notes 133–36 and accompanying text.

345. *Apple Inc.*, 952 F. Supp. 2d at 697.

346. Judge Cote claimed that her finding was supported by both direct and circumstantial evidence. *Id.* However, I would characterize all the evidence she cited as circumstantial. Direct evidence does not require the fact finder to make an inference or deduction to reach the desired conclusion while circumstantial evidence requires reasoning in order to reach the desired conclusion. Someone who testifies that he saw the defendant shoot the victim has given direct evidence. Someone who testifies that he heard a gunshot sound and then immediately saw the defendant, holding a smoking gun, run from a room in which only the defendant and victim had been present, has given circumstantial evidence. Neither form of proof is inherently superior to the other. *See, e.g.*, KENNETH S. BROUN (ed.), MCCORMICK ON EVIDENCE 308 (6th ed. 2006); CHRISTOPHER B. MUELLER & LAIRD C. KIRKPATRICK, EVIDENCE 155–56 (4th ed. 2009).

347. *See, e.g.*, Trial Transcript, United States v. Apple Inc., *supra* note 109, at 484 (testimony from Carolyn Kroll Reidy).

that the publishers did not want to raise prices to increase their profits. They made less money selling under the agency model with price caps than they had previously under the wholesale model with Amazon. Moreover, price caps are, at least on the surface, not fixed prices. So how did the Judge Cote find that the publishers and Apple conspired to fix prices?

She based her determination largely on the following evidence. After Apple opened its iBookstore, the five defendant publishers priced nearly all ebooks at or very close to the price caps.[348] Judge Cote noted that not only did the publishers increase their ebook prices, but they also increased prices for hardback editions of some new releases. Because ebook price caps were related to hardback list prices, Judge Cote believed the publishers increased hardback prices in those circumstances "in order to move the e-book version into a correspondingly higher price tier."[349] The price increases were "sudden and immediate" for all five of the publishers that signed agency agreements with Apple.[350] Meanwhile, the average ebook prices for Random House, the one major publisher that did not sign Apple's contract, remained unchanged.[351] Judge Cote also noted that, in their negotiations with Apple the publishers "fought hardest over the price caps."[352] From this evidence, Judge Cote reasoned that, when they negotiated the contracts, the publishers and Apple intended the price caps to be the actual, fixed prices for ebooks. Calling them "caps" was camouflage.

Despite its surface appeal, Judge Cote's conclusion falls far short of the preponderance of the evidence standard. That is, it is not reasonable to conclude from the evidence that it is more likely than not that Apple and the publishers agreed, either expressly or tacitly, that the price caps were to be the actual prices of ebooks. There are at least two other explanations as to why all five publishers raised their ebook prices to the level of the price caps while Random House did not.

The first possibility is that the caps were too low, meaning, lower than ebook prices would be in a competitive market with no

348. Judge Cote wrote: "In the five months [following Apple opening its iBookstore], the Publisher Defendants collectively priced 85.7% of their New Release titles sold through Amazon and 92.1% of their New Release titles sold through Apple within 1.00% of the price caps. This was also true for 99.4% of the NYT Bestseller titles on Apple's iBookstore, and 96.8% of NYT Bestsellers sold through Amazon." *Apple Inc.*, 952 F. Supp. at 682.

349. *Id.* at 683.

350. *Id.*

351. *Id.* at 682–83.

352. *Id.* at 667.

agreement on pricing. Bear in mind that the $9.99 pricing was too low. It was below the wholesale price of ebooks and, if ebooks were to carry their fair share of costs, below production costs. Apple was willing to allow the publishers to set the retail prices of their books—but only up to a point. It wanted to limit how far prices could rise. Price caps are synthetic: They do not allow prices to be entirely determined by the free market. If the caps were, in fact, too low or, at least, the publishers perceived them as being too low, it is entirely understandable that they would be the subject of intense negotiations. Apple had an interest in controlling ebooks costs—a quite particular interest because, unlike Amazon and Barnes & Noble, it sold only ebooks and not physical books. The publishers' interest was to have as much freedom as possible in setting retail prices for their ebooks—ideally, complete, unrestricted freedom. The evidence was that Apple wanted the price caps and imposed them against the wishes of the publishers.[353] All of this explains why the parties vigorously negotiated the caps, and why all of the publishers raised their ebook prices to the caps as soon as they could. Meanwhile, there was no corresponding change in Random House ebook pricing at Amazon (which is what the court measured) because Random House had not changed its arrangement with Amazon. Moreover, Amazon was rewarding Random House by giving its books special prominence on its website. Random House was, therefore, hardly the valid "control group."[354]

There is another possible explanation for the five publishers' decision to all raise their prices to the caps. When a limit is established, common forces often propel independent actors to cluster near the limit. At my law school, for example, instructors must distribute grades in required courses so that the mean grade falls within a prescribed range. As it turns out, most instructors award grades just below the upper limit of the range. That does not happen because the faculty members agreed to grade near the limit; nor did the faculty intend that outcome when it established the curve. I suspect that faculty tend to grade at or near the top of the grade curve because they feel generous towards their students, want to be liked by their students, want students to register for

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353. *See supra* note 260 and accompanying text.

354. An expert witness for the government testified that the publisher defendants' ebook sales declined by 14.5% relative to the control group, Random House. Apple argued that this was due to Amazon aggressively promoting Random House on its website. Judge Cote found this unpersuasive but did not explain why other than saying Apple had failed to persuade her. *Apple Inc.*, 952 F. Supp. 2d 684, 684 n.56.

their elective courses, or some combination thereof. At the risk of dating myself, let me offer a second example. When I was a college freshman, there was a 2:00 AM weekend curfew for women students. A very high portion of dates ended just before curfew. That certainly did not result from any agreement. It happened because ending a date earlier was tantamount to announcing to each other and all friends that the date had been a failure. When women's curfews were abandoned a year or two later there was, immediately, no longer any particularly popular time for ending dates.

Just suggesting a price—whether in the form of a cap or otherwise—will almost certainly affect pricing. This is because of a phenomenon that psychologists call the anchoring effect. Anchoring is a heuristic or cognitive shortcut "in which decisions are made based on an initial 'anchor.'"[355] The first experiments involved suggesting a particular value before asking subjects to guess, estimate, or predict a value. Daniel Kahneman gives the following example: "If you consider how much you should pay for a house, you will be influenced by the asking price. The same house will appear more valuable if its listing price is high than if it is low, even if you are determined to resist the influence of this number."[356] Retailers specializing in expensive designer goods often employ the anchoring heuristic as a sales device. A Prada T-shirt may be priced at $500.00, for example, not as much to sell that T-shirt but to sell another one priced at $275.00.[357]

Research on the anchoring effect has upset long-held beliefs. It used to be conventional wisdom that a negotiator should let the other side make the first offer. Behavioral economists now tell us that the party making the first offer generally has an advantage because it gets the benefit of the anchoring effect.[358] Anchoring affects everyone, even professionals making judgments in their areas of expertise.[359] It works for at least two reasons. One is the subtle power of suggestion.[360] The other is that an anchor prompts people

355. *Anchoring (and Adjustment)*, BEHAVIOURALFINANCE.NET, http://heuristics.behaviouralfinance.net/anchoring (last visited Oct. 28, 2018); *see also* DANIEL KAHNEMAN, THINKING, FAST AND SLOW 117–28, 427–30 (2013).

356. KAHNEMAN, *supra* note 355, at 120.

357. Blair Enns, *Always Be Anchoring*, WIN WITHOUT PITCHING, https://www.winwithoutpitching.com/always-be-anchoring (April 1, 2015).

358. *Id.*; *see also* KAHNEMAN, *supra* note 355, at 126–27; Jenny Roberts & Ronald F. Wright, *Training for Bargaining*, 57 WM. & MARY L. REV. 1445, 1483–87 (2016).

359. KAHNEMAN, *supra* note 355, at 124–27.

360. Psychologists call this a priming effect. *Id.* at 130–31. Regarding the power of suggestion, see generally Robert B. Michael et al., *Suggestion, Cognition, and Behavior,* 21 CURRENT DIRECTIONS IN PSYCHOL. SCI. 151 (2012).

to start their process of evaluation at the anchor and then assess whether that is too high or too low.[361] Regardless of whether the decision-making process is fully conscious, publishing executives will decide to price the ebook edition of a particular title at the cap unless they convince themselves there is a good reason not to do so. What would convince them otherwise? Bear in mind that their goal is not to maximize the sales of the ebook edition but to maximize total sales of *all* editions of a book. Pricing the ebook edition of a new release or bestseller too low would be unwise. The publishers do not want to skew consumer choices away from the hardback and toward the ebook edition, especially if they would make a smaller net profit on the ebook.

The evidence, therefore, does not warrant concluding that because the five publishers priced most of their ebooks at or very close to the caps they must have conspired to do so. Why did Judge Cote reach that conclusion? Her evaluation of witness credibility was not a deciding factor.[362] Even before she heard any of the witnesses testify before her, Judge Cote informed counsel that her "tentative view" was that Apple "knowingly participated in and facilitated a conspiracy to raise prices of e-books."[363] Nor did Judge Cote go astray because of any lack of skill, experience, or diligence. She is a highly regarded jurist.[364] And, of course, Judge Cote was hardly alone in going astray. Lawyers in the Antitrust Division of the U.S. Department of Justice and two of the three judges on the Second Circuit panel saw the case the same way she did. How could they all have been so wrong?

The answer is that they were steeped in Chicago School doctrine. As elaborated in more detail elsewhere, nearly everyone accepts the Chicago School worldview in antitrust law.[365] Although there are a few dissenters, the Chicago School is the consensus vision. It has so saturated antitrust law that many judges and lawyers

361. KAHNEMAN, *supra* note 355, at 122–23.

362. Regarding Judge Cote's evaluation of witness credibility, s*ee supra* note 240 and accompanying text.

363. See David Margolick, *The Judge that Apple Hates*, VANITY FAIR (June 2014), https://www.vanityfair.com/news/business/2014/06/judge-denise-cote-apple-sanctions-e-book-price-fixing.

364. Lawyers consider her exceptionally smart, knowledgeable, diligent, and fair. I base this both on the opinions of lawyers I know who have appeared before her and lawyer comments in the Almanac of the Federal Judiciary. *See Denise L. Cote*, 2 ALMANAC OF THE FEDERAL JUDICIARY, 2018 WL 3220091 (2018).

365. *See* Bogus, *The New Road to Serfdom*, *supra* note 13, at 15–26 (describing Chicago School doctrine), 26–37 (regarding the enormous influence of the Chicago School in antitrust doctrine).

have absorbed the basic doctrine without necessarily realizing that they are seeing antitrust through a very particular lens. In fact, the more knowledgeable a judge or lawyer is about antitrust law, the more likely he or she is to take the Chicago School worldview for granted.

What we call today the Chicago School of law-and-economics originated with an economist named Aaron Director, who, although he had no legal training, was appointed to the faculty of the University of Chicago Law School in 1946.[366] That appointment had been arranged by several people, including the famed Austrian economist Friedrich A. Hayek, who wanted to create an institute devoted to promoting libertarian visions of free market capitalism and to house it—not within the economics department, as might have been expected—within the law school.[367] The Volker Fund financed the project, and Director, who was personally close to Hayek and also happened to be Milton Friedman's brother-in-law, was selected to head the institute.

Director co-taught antitrust law, which was then a required course at the law school. Director was charismatic, and on the days he commanded the classroom, he argued that the traditional antitrust doctrine that his co-instructor had described in prior sessions was nonsense in terms of economic analysis.[368] One of Director's students, Robert Bork, described the experience as undergoing "what can only be called a religious conversion. It changed our view of the entire world."[369] Many of Director's other students and faculty colleagues also became devoted followers, including Richard Posner, Frank Easterbrook, and Douglas Ginsburg. Director also established the *Journal of Law & Economics,* which helped attract the future Nobel Laureate Ronald H. Coase to Chicago. "When I came to the University of Chicago, I regarded my role as that of Saint Paul to Aaron Director's Christ," said Coase.[370]

While Director never wrote much himself, his disciples did. Posner wrote many influential articles promoting the law-and-economics gospel, as well as the textbook *Economic Analysis of the*

366. *Aaron Director, Founder of the Field of Law and Economics*, U. CHI. NEWS OFFICE (Sept. 13, 2004), http://www-news.uchicago.edu/releases/04/040913.director.shtml.

367. STEVEN M. TELES, THE RISE OF THE CONSERVATIVE LEGAL MOVEMENT: THE BATTLE FOR CONTROL OF THE LAW 91–95 (2008)

368. Director's co-instructor was Edward Levi, who, during the course of his career, became dean of the Law School, president of the University, and Attorney General of the United States. *Id.* at 94.

369. TELES, *supra n*ote 367, at 94.

370. *Id.* at 96.

Law.[371] Bork wrote *The Antitrust Paradox: A Policy at War with Itself.*[372] It is almost impossible to overstate the impact of Bork's book on antitrust law. For forty years, it has been read by everyone who specializes in antitrust law. It has been cited in thousands of law review articles and in hundreds of decisions by courts and administrative agencies, including eighteen United States Supreme Court decisions.[373] No book in the history of American jurisprudence may have had a greater effect on a field of law than has Bork's.

At the time of his brother-in-law's death, Milton Friedman said that Director's great achievement had been "to apply economic analysis to the kind of issues that had been treated on the basis of supposed common sense before."[374] Friedman's statement suggests that Director and his disciples were merely using objective economic principles to inform legal doctrine—and therein lies the power of law-and-economics. Its adherents characterize it as neutral and quasi-scientific, and many have accepted it as such. In reality, however, Chicago School law-and-economics is an ideological movement with a libertarian worldview.[375] Its success can hardly be overstated. As Steven M. Teles has written, "[s]imply measured in terms of the penetration of its adherents in the legal academy, law and economics is the most successful intellectual movement in the law in the past thirty years, having rapidly moved from insurgency to hegemony."[376]

A full explanation of the Chicago School doctrine is both beyond the scope of this Article and unnecessary for its purposes. This Article does not argue that the government regulators and judges who handled the *Apple Inc.* case were dedicated members of

371. RICHARD A. POSNER, ECONOMIC ANALYSIS OF THE LAW (4th ed. 1992) (1973).

372. ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF (rev. ed. 1993) (1978).

373. WESTLAW, https://1.next.westlaw.com (search "'Bork' /2 'Antitrust Paradox'") (yielding 188 cases, 2645 secondary sources, and 3375 total results in search run on November 6, 2018).

374. Douglas Martin, *Aaron Director, Economist, Dies at 102*, N.Y. TIMES (Sept. 16, 2004), http://www.nytimes.com/2004/09/16/us/aaron-director-economist-dies-at-102.html.

375. *See, e.g.*, Thomas M. Melsheimera, *Economics and Ideology: Antitrust in the 1980s,* 42 STAN. L. REV. 1319, 1321 (1990) (stating "[t]he Chicago School of antitrust uses economic principles to buttress an ideology about antitrust that, in its most basic terms, is hostile to the idea of interference with the operation of the free market."); *see also* Bogus, *The New Road to Serfdom, supra* note 13, at 15–37; *cf.* Spencer Weber Waller, *The Law and Economics Virus,* 31 CARDOZO L. REV. 367, 367, 387 (2009) (stating that law-and-economics is "a leading example of a highly successful legal ideology," and that libertarians subscribe to a particularly strong form of Chicago School ideology); ANTHONY T. KRONMAN, THE LOST LAWYER 232 (1993) (advocating a similar view).

376. TELES, *supra* note 367, at 216. Teles describes how law-and-economics moved from a fringe "off the wall" movement to the mainstream of the legal academy. *Id.* at 216–19.

the Chicago School or knowledgeable about the intricacies of its philosophy. Yet, it is likely they had absorbed its basic premises, even without recognizing that they were applying doctrinal principles of the law-and-economics movement rather than uncontroversial principles of the disciplines of law and economics. These premises have become so widely accepted among judges and lawyers who specialize in antitrust that even Apple's lawyers did not question them or suggest that the ebooks litigation ought to be viewed through a different lens.[377]

I believe that government regulators and the courts were led astray by the interplay among four of the Chicago School's most basic premises, namely: (1) human beings and business organizations as rational maximizers;[378] (2) as rational maximizers, they make decisions "in accord with the tenets of simple pricing theory;"[379] (3) sound antitrust rules can all be logically deduced from the first two principles, and so can the motivations and likely conduct of business organizations;[380] and (4) antitrust should be exclusively about consumer welfare, which is defined as consumer prices and total industry output.

When one looks at the behavior of the publishers in this case through the Chicago School lens, one sees publishers who wanted to raise ebook prices to increase their profits. That, quite simply, is what rational maximizers do. To raise prices, it is necessary to depress total industry output. That is what the law of supply and demand requires. As the regulators and judges saw it, the market was ebooks, and that meant the publishers' goal was to raise the prices of ebooks and reduce the total industry output of ebooks.

The regulators and judges went in search of evidence to confirm what they were convinced must have happened—that is, that ebooks prices went up and total industry production of ebooks went down—and, not surprisingly, they found it, even if they had

377. This may have been because Apple's lawyers themselves accepted law-and-economics doctrine as neutral principles of law and economics or because they believed it tactically unwise to attempt to question such widely accepted premises.

378. Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U. PA. L. REV. 925, 928, 932 (1979); *see also* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 5 (1992) (stating that the "task of economics . . . is to explore the implications of assuming that man is a rational maximizer of his ends in life, his satisfactions—what we shall call his 'self-interest.'"). Posner is a leading advocate of the Chicago School. *See also* Bogus, *The New Road to Serfdom*, *supra* note 13, at 21–26 (criticizing the rational maximizer assumption).

379. POSNER, *supra* note 378, at 928.

380. *Id.* Although Posner only says explicitly that antitrust policy is deducible from the rational maximizer premise, the thrust of his comments suggest that business conduct is also deducible from that premise.

to trip over themselves to do so. In its complaint, the government alleged that "the e-book market has exploded, registering triple-digit sales growth each year" since 2007.[381] That was a faux pas. Apple was quick to pounce. "As a result [of the new state of affairs in ebooks]—as even the Government is compelled to admit—output has exploded," it noted its answer.[382] The parties considered this important because what matters most under Chicago School antitrust theory is total industry output: what increases total industry output is good; what decreases it is bad.[383] Antitrust law is also concerned with consumer prices, but because prices and output are deemed to be inversely related by an ironclad law—when prices rise, demand falls, and vice versa—it is, grand theory aside, not important which one is more important than the other. The government realized its error and changed its tune. By trial, it argued that total production—that is, ebook sales—fell after the shift to the agency model caused prices to rise.[384] Apple continued to argue that ebook sales increased.[385] Moreover, according to figures from impartial industry sources, ebook sales dramatically increased in 2010, even at Amazon.[386] Because the popularity of ebooks increased and more people acquired ereaders, it was entirely possible that ebook prices and the total number of ebooks sold both increased. Nevertheless, the government had little trouble persuading Judge Cote that ebook sales had dropped. "Not surprisingly," she wrote, "the law of supply and demand were not suspended for e-books. When the Publisher Defendants increased the prices of their e-books, they sold fewer books."[387]

By applying the Chicago School cookie-cutter approach, government regulators, and the courts ignored critical features of the industry. They ignored that, from the publishers' point of view, the

381. Complaint, *supra* note 212, ¶ 27.

382. Apple Inc.'s Answer, *supra* note 218, at 2.

383. Bogus, *The New Road to Serfdom*, *supra* note 13, at 15–21.

384. Trial Transcript, United States v. Apple Inc., *supra* note 109, at 2587.

385. *Id.* at 2511–12; Apple Inc.'s Answer, *supra* note 218, at 1. Apple Inc. Apple also argued that prices did not rise. Apple argued that during the relevant time frame the average ebook price fell from $7.97 to $7.34. *Throwing the Book at Apple*, WALL STREET J. (June 12, 2013, 7:08 PM), https://www.wsj.com/articles/SB10001424127887324063304578525454146561648.

386. Claire Cain Miller, *E-Books Tops Hardcovers at Amazon*, N.Y. TIMES (July 19, 2010) http://www.nytimes.com/2010/07/20/technology/20kindle.html; *see also Industry Sales Rose 3.1% in 2010; Trade E-book Sales the Big Winner*, PUBLISHERS WKLY. (Aug. 9, 2011), https://www.publishersweekly.com/pw/by-topic/industry-news/financial-reporting/article/48280-industry-sales-rose-3-1-in-2010-trade-e-book-sales-the-big-winner.html (providing revenue figures rather than number of units sold however).

387. *Apple Inc.*, 952 F. Supp. 2d at 684.

market was not ebooks but books. Publishers wanted to sell as many copies as possible of a particular title, and they wanted to be able to be indifferent about whether readers were choosing physical or ebook editions. They ignored the fact that if the publishers conspired, they conspired to make less rather than more money on ebooks. They ignored that books are not olive oil: Each book is unique, and books do not compete with one another the way fungible products do. They ignored that publishers have little incentive to fix prices because publishers compete with one another on authors and content and not so much with prices. They ignored that publishers do not produce ebooks quite the way manufactures produce physical products. Placing an ebook for sale online makes an unlimited quantity available; publishers do not decide to reduce production in order to increase price.

Focusing single-mindedly on the North Star of industry output and consumer prices was powerfully misleading in this case. Government regulators and the courts saw parties that wanted to raise the consumer price of ebooks. They also believed the parties collaborated toward that end. Certainly, the publishers did discuss among themselves their desires to raise the retail prices of ebooks, and five of them signed contracts with Apple that were designed to raise those prices. Since the regulators and judges viewed consumer prices as all-important, they unquestioningly assumed that low prices are good and any collaborative effort to raise them was an unlawful price-fixing conspiracy. However, the $9.99 price point was not merely a low price—it was a *too-low* price. It was not a price set through free market competition. It was not low because a seller realized new efficiencies. It did not reflect the cost of production; it was below the cost of production. The price was synthetically low because a party with enormous market power was seeking to concretize a retail monopoly in ebooks, and perhaps parlay that into a retail monopoly in all books (not to mention even in publishing books). Under the particular circumstances of this case, there was nothing nefarious, evil, or against the social welfare for publishers and Apple to collaborate, as they did, to raise ebook prices. Apple and the publishers acted in—not against—the public interest.[388]

The result in this case would have horrified Louis Brandeis, who believed it essential to understand the industry in question.

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388. As Judge Cote saw it, consumers suffered in three ways: having to pay more for ebooks, making do with less expensive books they did not desire as much, or foregoing purchases. *Id.* at 685.

Brandeis almost certainly would have found for Apple.[389] And a school of thought that teaches that everything that matters can be logically deduced from a few basic premises would have appalled Oliver Wendell Holmes, who famously wrote: "The life of the law has not been logic; it has been experience."[390]

Surely many economists would also be horrified at the Chicago School's highly reductionist and simplistic antitrust economics. As the old adage teaches, a little knowledge is dangerous. Economist James Kwak warns against "economism," which he defines as "the belief that a few isolated Economics 101 lessons accurately describe the world."[391] He explains:

> The key insights of the competitive market model . . . are deeply seductive to many people who share its secrets. This elegant framework promises to explain virtually all social phenomena with a handful of diagrams . . . . [But it's] a lot easier to make a case in the abstract world of supply and demand curves than it is in the real world of people and institutions. That's a major reason why economism is so widespread and powerful. But it's the real world that we live in, not a textbook.

Because they were trained in a doctrine with such a narrow vision, government regulators and the courts were blind to the elephant in the room: They saw the case as about the evils of higher prices and reduced industry output when they should have seen it as about the economic, social, and political consequences of consolidated corporate power.

"First do no harm," Hippocrates taught. Government regulators and the courts should have heeded that advice in this case, but they did not. In *United States v. Apple* and related class action litigation, the court ordered Amazon to pay $450 million to consumers

389. Brandeis' biographer, Jeffrey Rosen, speculates that Brandeis may have wanted to check Amazon's power and been sympathetic to publishers' efforts to stop Amazon from using its monopoly power to sell ebooks below the price it paid for them. ROSEN, *supra* note 19, at 205. "For Brandeis," writes Rosen, "book pricing should offer reasonable rewards for the individual creative author, not the giant distributor." *Id.* at 206.

390. Holmes continued that the law must take account "[of] moral and political theories, intuitions of public policy" and much else, and "cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics." OLIVER WENDELL HOLMES, THE COMMON LAW 5 (Mark DeWolfe Howe ed., Harvard Univ. Press 1963) (1881).

391. JAMES KWAK, ECONOMISM: BAD ECONOMICS AND THE RISE OF INEQUALITY 8–9 n.* (2017).

who, the court believed, had been overcharged for ebooks.[392] More significantly, the court ordered publishers to terminate their contracts with Apple and enjoined them from entering into new contracts with an ebook retailer that contained MFN clauses or restricted the retailer's right to discount ebooks (as long as a retailer was not, in the aggregate, taking a loss on all of a publisher's ebooks).[393] This largely restored things to the status quo ante bellum. Today Amazon controls sixty-five percent of the retail ebook market and seventy-four percent of the ereader market.[394] Sony, though in the market briefly, has stopped selling ereaders in the United States.[395] Barnes & Noble has slashed funding on the Nook and laid off workers in its physical stores. Analysts are speculating about whether Barnes & Noble will go out of business or be sold. Based on the Department of Justice and the courts' actions, the publishers are surely not going to band together to try to resist the Amazon juggernaut.

CONCLUSION

There is renewed interest in antitrust law. It has become a popular subject of political speeches,[396] newspaper columns,[397] and a prominent plank in a new Democratic Party platform.[398] While in-

392. A total of $450 million was paid to both consumers and their attorneys. *See* Plaintiffs' Consumer Distribution Plan at 3, *In re* Elect. Books Antitrust Litig., No. 12-CV-03394 (S.D.N.Y. Nov. 14, 2014), ECF No. 676-10. The court approved this plan shortly after its filing. Final Judgment at 5, *In re* Elect. Books Antitrust Litig., No. 12-CV-03394 (S.D.N.Y. Nov. 21, 2014), 2014 WL 11125070, at *3.

393. *See, e.g.*, Settlement Agreement, No. 11-MD-02293 (S.D.N.Y. June 21, 2013), 2013 WL 10620148 (providing simplified highlights of complicated provisions); Final Judgment as to Defendants Hachette, HarperCollins, and Simon Schuster at 8, 10–14, United States v. Apple Inc., 952 F. Supp. 2d 638 (S.D.N.Y. Sept. 6, 2012) (No. 12 CV 2826), ECF No. 119. The description in the main body provides simplified highlights of complicated provisions.

394. Khan, *supra* note 121, at 761–62.

395. *Id.*

396. *See, e.g.*, Senator Elizabeth Warren, Reigniting Competition in the American Economy, Keynote Remarks at New America's Open Markets Program Event (June 29, 2016), https://www.warren.senate.gov/files/documents/2016-6-29_Warren_Antitrust_Speech.pdf.

397. *See, e.g.*, Jared Bernstein, *Democrats say they want to go after monopoly power. Here's why that's a great idea,* WASH. POST (July 27, 2017), https://www.washingtonpost.com/news/posteverything/wp/2017/07/27/democrats-say-they-want-to-go-after-monopoly-power-heres-why-thats-a-great-idea.

398. *See Crack Down on Corporate Monopolies & the Abuse of Economic and Political Power*, DEMOCRATIC LEADER: A BETTER DEAL, http://www.democraticleader.gov/wp-content/uploads/2017/07/A-Better-Deal-on-Competition-and-Costs.pdf (last visited Oct. 28, 2018); *see also* Chuck Schumer, *A Better Deal for American Workers,* N.Y. TIMES (July 24, 2017), https://www.nytimes.com/2017/07/24/opinion/chuck-schumer-employment-democrats.html.

terest is especially intense in progressive circles, the revived interest in antitrust spans the ideological spectrum. In the main, calls for reform advocate for more aggressively enforcing existing antitrust doctrine. This Article argues for something different: a paradigm shift in antitrust. Rather than being concerned exclusively with consumer welfare, antitrust law must also be concerned with the social and political—as well as economic—consequences of consolidated corporate power.

Adherents of the current consensus will object that I am advocating for a return to what they call "the bad old days." By that they mean a time before the Chicago School brought supposed economic objectivity and rigor to antitrust analysis—a time when, according to Robert Bork, antitrust was "nothing more or less than judicial subjectivism." Antitrust, they believe, is administrable with the single objective of enhancing consumer welfare, so long as "consumer welfare" is defined exclusively in terms of lower prices and increased output. But antitrust would not be sensibly administrable, according to the current consensus, if courts are asked to consider other economic matters, not to mention social and political values, too. Regulators and courts will operate without a map and become lost. Court decisions will be driven by the personal views of judges rather than by neutral legal principles. That is what many fear.

The fears are not entirely without merit, but we need a new antitrust paradigm anyway. We have given up far too much for supposed objectivity. The things we have given up are precious and fundamental. It is a bedrock principle of American democracy that too much power must never be consolidated in one place. We rely on constitutional law—which includes a rich jurisprudence on separation of powers, among other relevant areas—to guard against the dangers of consolidated governmental power. In the modern world, however, governments are not the only entities possessing great power. Corporations possess enormous power, as well. Antitrust needs to play a parallel role in guarding against the dangers of consolidated corporate power. Adherents of the current consensus recoil at that suggestion. Protecting America against consolidated corporate power is a worthy objective, they believe, but other fields of law should do that. To which one should ask: What other fields of law? As I have demonstrated with considerable evidence elsewhere, antitrust was designed to be the principal legal instrument for protecting America against consolidated corporate power. Its abdication of that responsibility is damaging America in many ways.

It is no more possible for one person to develop a simple formula for how antitrust must shoulder that responsibility than it is for one person to attempt a similar feat for constitutional law. The framers of our most important antitrust statutes—the Sherman Act, the Clayton Act, and Celler-Kefauver Act—understood that. They wrote broad principles, and they expected the courts, through common law adjudication, to develop doctrines in accordance with those principles and over time modify doctrine as necessary. That is how courts proceed in matters of constitutional law. There are, of course, great debates about constitutional law. Those debates take place everywhere: in law reviews and newspapers; in high school classes, on college campuses, in in law schools; on political soapboxes and in congressional committees; on television, radio, and throughout the Internet. On some level, all of that debate influences common law decision making. It affects how judges decide cases, as well as who becomes judges. It is a messy and uncertain process. That is how a democracy operates. Moreover, that is how a democracy should operate because fundamental societal values can never be the exclusive province of specialists.

Does accepting the premise that antitrust must consider consolidated corporate power make *United States v. Apple* a difficult case? This Article submits that it does not. The potential danger of having one firm ultimately decide which books will be published or visibly promoted in America is unacceptable. That danger far outweighs the benefits of low consumer prices—prices which, in fact, were not the product of free market competition but held at a synthetically low level by a firm with a firm with a de facto monopoly.

United States v. Apple is one stark example of the fundamental values that are at stake.