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Pleading a Monopolist's Supracompetitive Pricing and Antitrust Injury:

The Curious Case of **Somers v. Apple** *and Allegations of a Monopolist's Flat Pricing*

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Ten years ago, the Ninth Circuit issued a little-followed decision in the case of an Apple music purchaser in which the court assessed the sufficiency of the purchaser's Sherman Act Section 2 claim against Apple. *Somers v. Apple, Inc.*, 729 F.3d 953 (9th Cir. 2013). Some suggest the case stands for the proposition that, if an alleged monopolist's pricing stays constant or flat before, during and after the alleged period of monopoly, then there can be no antitrust injury since, as a matter of law, there was no overcharge or supracompetitive pricing.

With the frequency of Section 2 litigation seemingly on the upswing,[1] and more and more companies in and outside of tech facing Section 2 claims, the demise of Somers' pleading is gaining new attention. The question is, should it; is the Ninth Circuit's decision one of broad and important application serving as a get-of-out-of-court pass for alleged monopolists—or is the decision best considered pigeon-holed by its rather unusual facts? You decide.

To set the stage, the Ninth Circuit explained that "Somers alleges that she suffered injury in the form of inflated music prices. The premise of her overcharge theory is that Apple used software updates to thwart competitors . . . and gain a monopoly in the music download market, which permitted Apple to charge higher prices for its music than it could have in a competitive market." *Id*. at 964.

But, the Ninth Circuit held, Somers' "own allegations do not square with her overcharge theory" because she alleged Apple's "price for music downloads remained the same (99 cents) since it entered the market in 2003," "*after* it allegedly acquired monopoly in that market in 2004," and "even after Apple's alleged monopoly ended in the beginning of 2008." *Id*. The Ninth Circuit concluded that "the stability of Apple's pricing in the face of increased competition only undermines Somers' allegation that Apple's music prices were supracompetitive." *Id*. at 966.

I. *Somers v. Apple:* An Overview

The Ninth Circuit was evaluating the district court's dismissal of Somers' Second Amended Complaint, which included monopolization, attempted monopolization, and California UCL claims. The district court had previously rejected claims for a purported class of indirect purchasers of iPods who allegedly paid an inflated price for the iPod due to Apple's tying of

[1] *See* Sam Skolnok, *'Big Is Bad' Antitrust Explosion Propels Cadre of Top Law Firms*, BLOOMBERG LAW (July 19, 2021), https://news.bloomberglaw.com/business-and-practice/big-is-bad-antitrust-explosion-propels-cadre-of-top-law-firms.

iPods to iTunes music through technological interoperability. *See Somers v. Apple, Inc.*, No. C 07-06507 JW, 2011 U.S. Dist. LEXIS 77165, at *5-9 (N.D. Cal. June 27, 2011).

Somers replaced her tying theory of harm with a monopolization claim based on Apple's software updates to prevent compatibility with potential competitors. The court rejected these claims for damages based on "diminution of iPod value," rather than overcharges, as blocked by *Illinois Brick* and damages based on supracompetitive music pricing for failing to allege anticompetitive conduct (the adoption and use of digital rights management ("DRM") encryption) and resulting supracompetitive pricing. *See id*. at *10.

The Second Amended Complaint's claims were based on Apple's "software updates to thwart programs that removed the DRM encryption from songs purchased on [iTunes]," resulting in higher prices on the iTunes Music Store. *Id*. at *16. Somers sought to represent a class of purchasers of music from the iTunes Music Store.

According to the operative complaint, Apple launched the iTunes Music Store in 2003, selling downloadable digital music tracks. *Somers*, 729 F.3d at 957. The music files were encrypted with Apple's proprietary DRM, FairPlay, and could only be played on Apple's portable digital media player, the iPod. *Id*. at 956. The iPod, in turn, could play only music downloaded from iTunes Music Store. *Id.* at 957. As a result, consumers needed to purchase music on iTunes Music Store to play on their iPods, and needed iPods to play music purchased from the iTunes Music Store. *Id*. Somers alleged that Apple quickly achieved a monopoly in both the music downloads market and personal digital music player market. *Id*. at 958.

Apple allegedly maintained and furthered its monopoly in these markets through software updates that were "intended to prevent competitors" from selling music downloads compatible with iPods. *Id*. By excluding competitors, it was able to maintain supracompetitive prices for music downloads. *Id*. Apple subsequently issued a series of software updates to block competing programs that would allow users to play iTunes Music Store-purchased music on non-Apple devices. *Id*. As competitors introduced workarounds to establish interoperability, Apple updated its software to block the workaround.

The Ninth Circuit affirmed the district court's dismissal because Somers did not plead sufficient facts to state a plausible antitrust injury from higher digital song prices. *Id*. at 956. It found that "her own allegations do not square with her overcharge theory" because she alleged Apple's music price (99 cents) remained the same when it first entered in 2003, after it acquired a monopoly in 2004, after its monopoly ended in 2008 with Amazon's entry into the music downloads market, and when it began selling DRM-free music in 2009. *Id*. at 964.

The Ninth Circuit further found that, "if Somers' overcharge theory were correct, then Apple's music prices from 2004 to 2008 were supracompetitive as a result of software updates that excluded competition, and the emergence of a large seller such as Amazon would have caused [iTunes Music Store] music prices to fall." *Id*. Not only did Somers not allege that prices fell after Amazon's entry, but she alleged that Apple's prices went up after removing DRM protections. *Id.* This pricing pattern contradicted the allegations that Apple "would have had to lower the price of its music to compete with its rivals" and plaintiff's admission that "under basic economic principles, increased competition . . . generally lowers prices." *Id*.

The court ruled that these inconsistent allegations failed to allege a credible injury caused by Apple's anticompetitive conduct. *Id*. at 964. The complaint therefore failed to plead a plausible antitrust injury. Additionally, Somers did not plead any other facts that could explain Apple's flat pricing, or how that could square with her overcharge theory. *Id*. at 965.

Though monopoly power "may be evaluated by other factors," if Apple was not charging inflated prices for its music, there was "no basis for damages" under Somers' overcharge theory. *Id*. And the Ninth Circuit found "other 'obvious alternative explanation[s]' for the music pricing." *Id*. (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 567 (2007)). These other explanations, such as keeping music prices low to incentivize customers to purchase an iPod, would also contradict the overcharge theory of injury and did not make the allegations of antitrust injury plausible. *Id*. The Ninth Circuit affirmed dismissal of the complaint.

II. How Broadly Should *Somers* be Read?

Somers presents an unusual series of factual allegations and pricing patterns. The complaint also suffered from changing theories of harm to address the district court's prior dismissals, leading to inconsistent allegations. That said, are those who assert that allegations of flat pricing cannot state a monopolization claim correct? Consider:

a. Defining Achievement of Monopoly

First, Somers identified a point when Apple achieved a monopoly in music downloads, and alleged the same pricing before and after this point of monopolization. Somers alleged "[s]pecifically" that shortly after the iTunes Music Store was released, "Apple achieved and maintained a market share of over 70 percent of the audio download market" and increased its market share of the personal digital music player market "from 11 to 99 percent." *Somers*, 729 F.3d at 958. Somers alleged that Apple had achieved a monopoly in both "markets by 2004, at the latest." *Id.*

Pinpointing the acquisition of monopoly power, with distinct before and after phases, is not a simple proposition. The ability to control prices or output does not appear definitively one day nor is it automatic upon reaching a certain market share threshold. Identifying market power will generally require detailed analysis of the market and changes in its structure, an analysis not usually feasible or undertaken at the pleadings stage. *See NCAA v. Alston*, 141 S. Ct. 2141, 2158 (2021) ("Whether an antitrust violation exists necessarily depends on a careful analysis of market realities. If those market realities change, so may the legal analysis.") (citations omitted).

But the analysis of a rapid change from new entry to monopoly may also be flawed given that the iTunes Music Store was helping develop the "audio downloads" market that Somers alleged. The market definition may have been too narrow by not including music recordings on physical media consumers may have considered substitutes in 2003, when the digital music market was still emerging and expanding.

While some major record labels had attempted to launch their own online stores prior to iTunes, they were largely unsuccessful.[2] Peer-to-peer file sharing services had some popularity but faced legal scrutiny for copyright infringement and security concerns from users.[3] This market in technological transition makes it more difficult to identify Apple's achievement of monopoly power and subsequent loss of power and to draw conclusions about a plaintiff's antitrust injury from consistent pricing. *Cf. FTC v. Qualcomm Inc.*, 969 F.3d 974, 1003 (9th Cir. 2020) (comparing the case to *Ohio v. Am. Express Co.*, 138 S. Ct. 2274 (2018), as one "where a company's novel business practice at first appeared to be anticompetitive, but in fact was disruptive in a manner that was beneficial to consumers in the long run").

Alternatively, if digital "audio downloads" were a separate product from other ways to obtain song recordings, iTunes likely had market power upon entry as it actually created a new market.[4] The allegations would not lead to the Ninth Circuit's inference that iTunes Store entered the market in 2003 pricing all songs at 99 cents, obtained a monopoly less than a year later, and continued to price at 99 cents for years while maintaining its monopoly. *See Somers*, 729 F.3d at 958. Apple could have been pricing at a supracompetitive rate the entire time, making the constancy uninformative for purposes of pleading antitrust injury.

b. Insufficient Exclusionary Conduct

Second, the alleged anticompetitive conduct was unclear. Since the "mere possession of monopoly power, and the concomitant charging of monopoly prices," is not inherently unlawful, the lack of clear exclusionary conduct likely made the claim of flat yet supracompetitive pricing insufficiently plausible. *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 407 (2004). The district court held that the use of DRM was not anticompetitive, requiring Somers to shift the focus of her conduct allegations.

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[2] *See* Eric Harvey, *Station to Station: The Past, Present, and Future of Streaming Music*, PITCHFORK (April 2014), *available at* https://pitchfork.com/features/cover-story/reader/streaming/ ("RealNetworks launched MusicNet in early 2001 with the EMI, Warner, and BMG catalogs, while Sony and Universal started the very similar service Pressplay. For between $9.95 and $24.95 a month, subscribers could navigate woefully incomplete artist catalogs; ugly, ad-laden interfaces; and bizarre usage restrictions.").

[3] *See* Priti Trivedi, *Writing the Wrong: What the E-Book Industry Can Learn from Digital Music's Mistakes with DRM*, 18 J.L. & POL'Y 925, 939-42 (2010).

[4] As noted, while iTunes Music Store was not the first entrant, it was the first to offer a large catalog of audio downloads that provided the purchaser access to high-quality song files that the user could play an unlimited number of times. *See* Press Release, Apple Inc., *Apple Launches the iTunes Music Store* (Apr. 28, 2003), https://www.apple.com/newsroom/2003/04/28Apple-Launches-the-iTunes-Music-Store/ ("The iTunes Music Store offers groundbreaking personal use rights, including burning songs onto an unlimited number of CDs for personal use, listening to songs on an unlimited number of iPods, playing songs on up to three Macintosh® computers, and using songs in any application on the Mac®"; "The iTunes Music Store features over 200,000 songs from music companies including BMG, EMI, Sony Music Entertainment, Universal and Warner").

Somers initially alleged an illegal tie between iPods that played only iTunes-purchased music files and iTunes music files that could only be played on iPods (or other Apple products). *Somers*, 2011 U.S. Dist. LEXIS 77165, at *6. When the district court rejected this theory, Somers instead asserted a diminution in the value of the iPod because it could not be used to play other music files—without the Apple DRM—that competitors allegedly would have sold at lower prices. *Id*. at *10. But any claims based on iPod purchases were still blocked by *Illinois Brick* because Somers was an indirect purchaser. *Id.*

Somers then asserted she and the proposed class paid music prices that were too high because of the subsequent software updates to prevent cross-compatibility with non-Apple products and music purchased on other online stores. Both the district court and Ninth Circuit found this to be the same general "use of DRM" allegation that was previously rejected. Because Apple's decision to include DRM compatible with its own products was not anticompetitive at the outset, Apple's software updates to "maintain[] the status quo" could not become anticompetitive. *Somers*, 729 F.3d at 962.

c. Allegations that Competitors Offered Lower Prices

Third, the new entrants allegedly charged lower prices than Apple. Real Networks sold songs for as low as 49 cents on its online store, and its songs included a technology that made them compatible with iPods and other digital media players (until Apple's software update that prevented this compatibility). *Id.* at 958. Amazon sold half of its song catalog for 89 cents each, without DRM restrictions. *Id.* at 958-59. In 2009, having ceased use of FairPlay encryption, Apple offered top selling songs for $1.29; Amazon offered these same selections for 99 cents. *Id*. at 959.

Entering at a lower price may be a business strategy to recruit customers away from the monopolist, and the presence of lower-priced competitors can be evidence of supracompetitive pricing by a dominant firm. The Ninth Circuit dismissed evidence of Real Networks' introductory price of 49 cents, half of Apple's price, and Amazon's price of 89 cents, as insufficient to indicate that Apple's pricing was supracompetitive. *Id*. at 965-66. The court stated that "such variations in pricing exist even in competitive markets" and "the stability of Apple's pricing in the face of increased competition only undermines Somers' allegation that Apple's music prices were supracompetitive." *Id*.

This may be an incorrect inference in other situations though. An entrant's ability to gain market share with lower pricing than the alleged monopolist can indicate that the monopolist's price is too high, with consumers moving to the competitor to get a lower price. Following entry, the dominant firm will seek to maximize its profits by adjusting its price and quantity in response to the increased supply. It will drop its quantity to account for the new entrants' supply, and its profit-maximizing price will decrease. Areeda & Hovenkamp, *Antitrust Law* (5th ed. 2020) ¶ 391e1. Accordingly, the prevailing price in the market will be lower.

d. Pricing After Anticompetitive Conduct

Fourth, Somers alleged an *end* to the anticompetitive conduct (ceasing FairPlay encryption), and Apple's pricing after it ceased the DRM encryption. While the Ninth Circuit

noted that the pricing remained flat at 99 cents in the before, during, and after monopoly phases, it also explained that Apple later increased its prices to $1.29 for DRM-free music downloads. That is, after removing the alleged anticompetitive restraint and facing real competition, Apple increased its pricing.

The Ninth Circuit also assumed Apple's monopoly ended after Amazon's entry. *Somers*, 729 F.3d at 964 ("after Apple's alleged monopoly ended in the beginning of 2008—when Amazon began selling DRM-free music"). Entry does not necessarily terminate monopoly power, which is the relevant consideration rather than the total number of competitors. The Ninth Circuit recognizes market shares of approximately 65% as sufficient to allege monopoly power, when coupled with allegations of barriers to entry. *See Image Tech. Servs. v. Eastman Kodak Co.*, 125 F.3d 1195, 1206 (9th Cir. 1997) ("Courts generally require a 65% market share to establish a prima facie case of market power."); *see also Rebel Oil Co. v. Atl. Richfield Co.*, 51 F.3d 1421, 1438 (9th Cir. 1995) ("numerous cases hold that a market share of less than 50 percent is presumptively insufficient to establish market power").

But Somers alleged that Apple actually increased its prices after dropping the FairPlay encryption that limited interoperability with non-Apple products. In January 2009, Apple began selling DRM-free music for $1.29, or allowed customers to upgrade existing music files to DRM-free versions for 30 cents, making the net price $1.29. *Somers*, 2011 U.S. Dist. LEXIS 77165, at *3 (citing Second Amended Complaint). The Ninth Circuit found that this contradicted Somers' argument that Apple would have had to lower its pricing to compete if it had not used the software updates to thwart competition. *Somers*, 729 F.3d at 964.

III. Alleging Supracompetitive Pricing by a Monopolist

Flat pricing does not necessarily preclude stating a claim in other contexts, depending on the market structure and exclusionary conduct alleged by the plaintiff.

Antitrust damages are often calculated "by comparison of profits, prices and values as affected by the [violation], with what they would have been in its absence under freely competitive conditions." *Bigelow v. RKO Radio Pictures*, 327 U.S. 251, 265 (1946). It is not difficult to imagine a scenario where pricing was flat in the real world but would have dropped in the "but-for" world without the alleged anticompetitive conduct. Because the price would have been lower in the absence of the alleged violation, the pricing was still supracompetitive during the monopolization, even if the price did not change in absolute terms. *See* Areeda & Hovenkamp ¶¶ 391e1, 391e2 (explaining that damages are determined by comparing the actual economic condition to the conditions that would have prevailed "but for" the defendant's anticompetitive conduct).

Somers alleged a foreclosure theory of harm, where Apple was able to maintain supracompetitive prices by foreclosing potential competitors, *i.e.*, other digital music stores. The measure of consumer injury for foreclosure cases is usually the overcharge paid—the difference between the actual price and the but-for price, times the quantity purchased at the inflated price. *See id.* ¶ 391e1.

One common way of measuring overcharge damages from supracompetitive pricing is a "before-and-after" model, wherein the plaintiff uses the price "it paid (or received) prior to and after the monopolization or price-fixing activity as a basis for inferring what the prices would have been during the damage period but for the unlawful overcharges." *Id.* ¶ 392e.

Somers presented the unusual scenario when the alleged prices before and after the monopoly would imply zero or negative overcharges during the alleged period of wrongful conduct, as the prices were the same before the alleged monopolization period and higher after. Nor were there allegations of Apple's costs falling and profits rising during the monopoly phase. In this case, there were no damages to causally attribute to the alleged anticompetitive conduct. *Cf. NorthBay HealthCare Grp. v. Kaiser Found. Health Plan, Inc.*, No. 17-cv-05005-LB, 2018 U.S. Dist. LEXIS 146475, at *23 (N.D. Cal. Aug. 28, 2018) (finding that plaintiff's alleged injury suffered "would be the same regardless of whether [defendant] were a monopoly or had a dozen competitors. An action that would have injured the plaintiff in the same way regardless of whether or not the defendant has a potential to monopolize does not give rise to an antitrust injury.")

In many scenarios, plaintiffs allege an ongoing antitrust violation, so defendants will not be able to point to a post-violation period that counterintuitively has higher prices. One can foresee an argument that this would preclude dismissal under the *Somers* analysis.

a. Flat Pricing Attributable to Other Market Factors

Even without a post-violation period, other courts have been unwilling to draw conclusions about whether a complaint adequately alleges antitrust injury through supracompetitive pricing based on allegations of flat pricing patterns. For example, a Northern District of California court recently rejected a comparison to *Somers* at the pleadings stage. *See In re Juul Labs, Inc.*, No. 20-cv-02345-WHO, 2021 U.S. Dist. LEXIS 157126 (N.D. Cal. Aug. 19, 2021).

In *Juul*, defendants Juul Labs and Altria argued that Juul's product price decreased after Altria withdrew its competing e-cigarette products from the market (part of the alleged anticompetitive agreement between the companies). The court found the potential decrease in absolute prices claimed by the defendants, even if factually true, did not defeat plaintiffs' "plausible allegation that Altria's departure led to supracompetitive process [sic], reduced output, and reduced innovation." *Id*. at *56.

The court distinguished the allegations from *Somers*, which it characterized as involving "no price change in the market nor increased competition from other digital music platforms, [so] there could have been no competition eliminated." *Id*. at *57. Plaintiffs alleged that in the short term after the alleged agreement, "economic metrics in the market were impacted by [Juul's] decisions to withdraw its fruit-flavored pods and take other steps in response to the regulatory and public pressure," and plaintiffs adequately pleaded that Juul was able to establish supracompetitive prices in the more concentrated market after Altria's departure. *Id.*

b. Flat Pricing with Locked-In Customers and/or Increasing Profits

Other decisions related to new and emerging technology have also taken a different approach as to what is sufficient to allege anticompetitive conduct, including when the alleged monopolist "locked in" customers to its new technology or standard. These courts have been more forgiving in allowing claims to move past a motion to dismiss with alleged injuries of higher royalties and decreased innovation after the alleged monopolist obtained market power in a relevant market due to its patented technology.

Although *Somers* did not involve standard essential patents or technology standards, the theory of harm relied on a concept of "lock-in" to Apple's closed ecosystem of Apple-compatible digital music, requiring customers to purchase audio downloads from iTunes Music Store if they wanted to listen on their iPods, or purchase an iPod if they wanted to listen to songs purchased from iTunes Music Store. Somers' allegations of harm relied on consumers' dual reliance on the two products and precluding consumers' use of competing online stores or personal digital media players.

In *Wi-LAN Inc. v. LG Elecs., Inc.*, 382 F. Supp. 3d 1012 (S.D. Cal. 2019), for example, the court found LG's allegations in its Section 2 counterclaim sufficient to state a claim. LG adequately alleged Wi-LAN possessed market power in "various markets for technologies that—before the IEEE 802.16 standard and the 3GPP LTE standard were implemented—were competing to perform each of the various functions covered by each of Wi-LAN's purported essential patents for the" two standards. *Id*. at 1021. The "poststandardization lock-in effect" meant other technologies were no longer viable substitutes and Wi-LAN could assert the patents to extract royalties or other licensing terms in excess of what it would have obtained prior to implementation of the two standards. *Id*.

LG's allegations of antitrust injury were also determined to be sufficient, unlike Somers' alleged injury, because LG alleged exclusion from, and increased royalties and other costs associated with, "the manufacture and sale of downstream wireless communications devices that implement" the two standards, and chilled competition to develop and sell new standards-compliant products, "resulting in increased prices and decreased quality and innovation in downstream product markets and complementary innovation markets." *Id.* at 1024. LG sufficiently alleged that Wi-LAN was able to extract supracompetitive pricing.

Similarly, in *Apple Inc. v. Samsung Electronics Co.*, No. 11-CV-01846, 2012 U.S. Dist. LEXIS 67102 (N.D. Cal. May 14, 2012), Apple alleged (in a counterclaim) that Samsung possessed market power in markets for "technologies that — before the standard was implemented — were competing to perform each of the various functions covered by each of Samsung's purported" standard essential patents. *Id*. at *20. Apple alleged it was "locked-in to the technology standard" and "could not switch to alternative technology absent undue cost." *Id*. at *23-24.

The district court found its allegations that the standard setting organization would have adopted different technology but-for the alleged anticompetitive conduct to be sufficient and to adequately support Apple's alleged injury from Samsung's ability to raise prices and exclude competition in the technology markets. *Id*. at *23, 29-30.

Another way to determine supracompetitive pricing, though perhaps harder to do without fact discovery, is through marginal cost information. *See In re Se. Milk Antitrust Litig.*, 739 F.3d 262, 277 (6th Cir. 2014) ("Market power is defined as the ability to charge a supracompetitive price — a price above a firm's marginal cost."). For example, in *US Airways, Inc. v. Sabre Holdings Corp.*, 938 F.3d 43 (2d Cir. 2019), "US Airways presented evidence at trial of supracompetitive net pricing through the testimony of two expert witnesses." *Id*. at 61. One, an accounting expert, "testified that Sabre was consistently more profitable than comparable companies." *Id*. The other, an economic expert, testified that the relevant market was "highly noncompetitive" and "the returns are considerably in excess of normal market returns." *Id*. at 62.

A plaintiff may be able to allege that an alleged monopolist's marginal costs have decreased significantly, even while it has maintained consistent pricing. Such allegations could be sufficient to allege supracompetitive pricing, with the company achieving returns "considerably in excess of normal market returns," thus allowing the complaint to survive a motion to dismiss. This might be particularly true in an industry with significant upfront costs but then high efficiencies of scale, leading to low ongoing costs after market power has been achieved.

IV. **Conclusion**

Somers presents an extreme and idiosyncratic scenario where, among other pleading anomalies, pricing was alleged to be flat before, during, and after the period of alleged monopoly. Other cases may involve flat pricing for only some of those time periods. Differing circumstances can be endless. For instance, another alleged monopolist may hold its pricing flat while enjoying outsized and/or quickly increasing profits during the monopoly phase.

If profits are quickly increasing during the alleged monopoly phase (perhaps due to rapidly declining costs of, say, digital distribution), then does *Somers'* heavy focus on Apple's flat music pricing offer much precedential value for cases *not* involving consistent prices during all three phases -- before, during *and* after the monopoly phase – and/or cases that allege rapidly increasing profits during the monopoly phase despite the monopolist's flat pricing? These are questions for another court assessing Section 2 allegations of flat pricing to decide. Where do you come out?